CHAPTER 1

Introduction

1.1 On 6 March 2014, Senator Nick Xenophon, also on behalf of Senator John Madigan, introduced into the Senate the Flags Amendment Bill 2014 (Bill).[1]

1.2 On 20 March 2014, on the recommendation of the Senate Selection of Bills Committee, the Senate referred the Bill to the Senate Finance and Public Administration Legislation Committee (committee) for inquiry and report by 16 June 2014.[2]

1.3 The Bill amends the *Flags Act 1953* to require that all Australian flags flown, used or supplied by the Commonwealth are only manufactured in Australia from Australian materials.

Conduct of inquiry

1.4 Details of the committee's inquiry, including links to the Bill and associated documents, were placed on the committee's website at www.aph.gov.au/senate_fpa.

1.5 The committee directly contacted a number of relevant organisations to notify them of the inquiry and invite submissions by 17 April 2014. Six submissions were received by the committee and are listed at Appendix 1.

1.6 While the committee decided to prepare its report on the basis of submissions received and other available information, it was able to draw on relevant published information received by the Senate Finance and Public Administration References Committee (references committee) for its current inquiry into Commonwealth procurement procedures. In particular, the references committee, at its hearing on 28 April 2014, took evidence from two witnesses representing flag manufacturing organisations and also examined other witnesses with specific reference to this Bill.[3]

1.7 It is suggested that readers refer to the references committee report, to be tabled on 30 June 2014, for a broader examination of the issues around the Commonwealth procurement framework.

1.8 The committee thanks those who assisted by providing submissions to the inquiry and provided evidence to the references committee in its inquiry into Commonwealth procurement procedures.

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1 *Journals of the Senate*, No. 18, 6 March 2014, p. 583.

2 *Journals of the Senate*, No. 22, 20 March 2014, pp 663-664.

3 See http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Finance_and_Public_Administration/Commonwealth_procurement_procedures/Public_Hearings

Overview of Bill

Provisions of the Bill

1.9 Item 3 of Schedule 1 of the Bill amends section 7 of the *Flags Act 1953* to insert new subsection 7(2) to require that the Commonwealth must only fly, use or supply a designated flag if the flag was manufactured in Australia from materials manufactured in Australia. This item also inserts new subsection 7(3) to define a 'designated flag' as referring to a flag or ensign referred to or appointed in the *Flags Act 1953*.

Statement of compatibility with human rights

1.10 The Statement of Compatibility with Human Rights contained in the Explanatory Memorandum to the Bill states that the Bill does not engage any of the applicable rights or freedoms and is therefore compatible with human rights as it does not raise any human rights issues.[4]

Background

1.11 In his second reading speech, Senator Xenophon referred to evidence provided to the committee during the Additional Estimates 2013-14 hearings by the Department of Parliamentary Services (DPS) concerning the manufacture of the flags which fly in rotation above Parliament House. The Secretary of DPS confirmed that there is no requirement for any tender process undertaken by DPS to specify country of origin, including the flag above Parliament House:

> All our tenders, regardless of what they are for, comply with Commonwealth tender processes and legislation, which under free trade means that we can specify quality, we can specify design, we can specify value for money and other criteria; we cannot specify place of origin.
>
> …
>
> We have a philosophy that wherever possible we should strive to have Australian products, but we cannot breach Commonwealth guidelines in doing our procurement.[5]

1.12 Although it was confirmed in evidence to the committee that the current rotation of Australian flags which fly above Parliament House are Australian made,[6] Senator Xenophon noted in the Senate that under the current Commonwealth procurement regime these flags are not required to be Australian made.[7]

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4 *Explanatory Memorandum*, p. 3.

5 Ms Carol Mills, Secretary, Department of Parliamentary Service, *Estimates Hansard*, 24 February 2014, p. 40.

6 Answer to Question on Notice no. 138, Additional Estimates 2013-14, Department of Parliamentary Services.

7 Senator Nick Xenophon, *Senate Hansard*, 6 March 2014, p. 1018.

1.13 In addition to raising the possibility of foreign made flags flying above Parliament House (or other Commonwealth buildings), concern for Australia's manufacturing sector was also put forward as a reason for introducing the Bill:

> We need to do more to ensure the Parliament and the Commonwealth can support the Australian economy and our manufacturing sector, despite free trade agreements. Most Australians would agree that the flags flying from our Commonwealth buildings are an excellent place to start.[8]

Commonwealth Procurement Rules

1.14 The Commonwealth Procurement Rules (CPRs), issued under Regulation 7 of the *Financial Management and Accountability Regulations 1997*, are at the core of the Commonwealth's procurement framework.[9] The CPRs set out the policies and procedures which agencies must comply with when undertaking procurement processes.

1.15 The committee notes that the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) which will replace the *Financial Management and Accountability Act 1997* (FMA Act) and the *Commonwealth Authorities and Companies Act 1997* (CAC Act), comes into effect on 1 July 2014. It will be supported by rules setting out financial management requirements. The CPRs will form part of the PGPA rules and are being revised to include references to the PGPA Act.[10]

1.16 Division 1 of the CPRs sets out the rules that are applicable to all procurements, regardless of their value or whether an exemption from Division 2 applies to them, and are grouped according to the following areas:

- value for money;
- encouraging competition;
- efficient, effective, economical and ethical procurement;
- accountability and transparency;
- risk management; and
- procurement method.

1.17 Division 2 of the CPRs provides additional rules for procurements at or above the relevant procurement threshold, which is currently $80,000 for FMA Act agencies, other than for procurements of construction services; and $400,000 for relevant CAC Act bodies, other than for procurements of construction services.[11] Appendix A

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8 Senator Nick Xenophon, *Senate Hansard*, 6 March 2014, p. 1018.

9 The Commonwealth procurement framework is also supported by web based guidance issued by the Department of Finance, Finance Circulars and Chief Executive Instructions. See CPRs, 1 July 2012, paragraph 2.4.

10 References committee inquiry, Department of Finance, *Submission 12*, p. 2.

11 Section 3.3, CPRs, dated 1 July 2012, p. 12.

of the CPRs provides a list of procurements which are exempt from Division 2 rules but are still required to be undertaken in accordance with value for money and the rules contained in Division 1 of the CPRs.

Non-discrimination

1.18 Value for money is a key element of the CPRs and involves encouraging competition and the requirement for non-discrimination in procurement processes. Paragraph 5.3 of the CPRs states:

> The Australian Government's procurement framework is non-discriminatory. All potential suppliers to government must, subject to these CPRs, be treated equitably based on their commercial, legal, technical and financial abilities and not be discriminated against due to their size, degree of foreign affiliation or ownership, location, or the origin of their goods and services.[12]

Procurement of Australian goods and services under the CPRs

1.19 The ability for agencies to preference Australian goods and services in procurement processes is constrained under the CPRs on the basis that it incorporates Australian government commitments agreed to under free trade agreements (FTAs). Parties entering into the FTAs have entered into commitments to liberalise access to each other's market for goods and services, including government procurement. According to the Department of Finance:

> These commitments provide access for Australian suppliers to the government procurement markets of other countries, whilst also placing obligations on the Commonwealth Government to open up access to our procurement market. These commitments limit the extent to which the Commonwealth Government can preference local suppliers.[13]

1.20 Dr Nick Seddon in his evidence to the references committee inquiry into Commonwealth procurement procedures emphasised that 'one of the main reasons for entering into free trade agreements is to eliminate local preference and allow competition to operate.'[14]

Small and Medium Enterprises

1.21 Despite the emphasis on value for money and non-discrimination in the CPRs, the Department of Finance notes in its submission that the government procurement elements of Australia's international agreements allow for policies that benefit Small and Medium Enterprises (SMEs).[15] The CPRs state that the Australian Government is committed to FMA Act agencies sourcing at least 10 per cent of procurement by value

12 Paragraph 5.3, CPRs, 1 July 2012, p.17.

13 References committee inquiry, Department of Finance, *Submission 12*, p. 3.

14 *References committee Hansard*, 28 April 2014, p. 1.

15 An SME is defined in the CPRs as an Australian or New Zealand firm with fewer than 200 full-time equivalent employees, see CPRs, 1 July 2012, Appendix C: Definitions, p. 42.

from SMEs.[16] To ensure that SMEs can engage in fair competition for Australian Government business, paragraph 5.4 of the CPRs provides that:

> …officials should apply procurement practices that do not unfairly discriminate against SMEs and provide appropriate opportunities for SMEs to compete. Officials should consider, in the context of value for money:
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> a. the benefits of doing business with competitive SMEs when specifying requirements and evaluating value for money;
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> b. barriers to entry, such as costly preparation of submissions, that may prevent SMEs from competing;
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> c. SMEs' capabilities and their commitment to local or regional markets; and
>
> d. the potential benefits of having a larger, more competitive supplier base.

1.22 Dr Nick Seddon, in his evidence to the references committee, suggested paragraph 5.4 of the CPRs as currently drafted lacks clarity in how it is to be applied. He suggested that while it is clear that government agencies must not discriminate against SMEs when making purchasing decisions, it does not provide guidance on whether agencies can discriminate in favour of SMEs.[17]

1.23 To support his analysis, Dr Seddon posed the scenario of a procurement process, where the tenderers included an SME that was slightly more expensive or did not provide as good value for money, and asked whether the contract could still be awarded to that tenderer on the basis that it is an SME. In this case, he proposed using the Australia-United States Free Trade Agreement (AUSFTA) as an aid to interpret the intention of the CPRs:

> The CPRs are not clear on that, but, if you go back to the Australia-United States Free Trade Agreement, it is pretty clear that deciding whether to grant a contract to an SME is exempt from the basic principle that you should not give local preference.
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> …
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> I made the point that the Australia-United States Free Trade Agreement is not law in Australia. It is international law, but it is not domestic law and, strictly, one should just look at the CPRs. But on this question—can a government agency discriminate in favour of an SME?—I think the answer is probably yes because of the background, namely the free trade agreement on which the CPRs were based and chapter 15 of the Australia-United States Free Trade Agreement in particular.[18]

16 Paragraph 5.5, CPRs, 1 July 2012.

17 *References Committee Hansard*, 28 April 2014, p. 1.

18 *References Committee Hansard*, 28 April 2014, pp 1-2.