

Governance and operation of the Northern Australia Infrastructure Facility (NAIF)

Submission to the Senate Economic References Committee

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1. Background to the Implementation of the NAIF – Themes from: *It's Our North, Our Future: White Paper on Developing Northern Australia*

Northern Australia is generally defined as the land above the tropic of Capricorn. It includes all of the Northern Territory and significant parts of Queensland and Western Australia. Northern Australia makes up approximately 40 per cent of Australia's land mass which is in excess of 3 million square kilometres. Northern Australia receives in excess of 60 per cent of the annual national rainfall. In June 2015, the *Its Our North, Our Future: White Paper on Developing Northern Australia* was released. The paper sought to outline the regional economic opportunities presented to Northern Australia and to consider a plan for furthering the economic development and advancing population growth in Northern Australia. This was seen as being particularly strategic given its proximity to Asia and the emergency of a strong middle class in China and Asia where it is estimated that by 2030, Asia combined will represent approximately two-thirds of the global middle class population and will therefore represent two-thirds of global consumption.

Within this broader region, there is increasing demand for higher quality food products. For example, forecasts by the Australian Bureau of Agricultural and Resource Economics and Sciences calculate that between 2009 and 2050, the real value of beef consumption in China is projected to rise 236 per cent, dairy consumption 74 per cent, sheep and goat meat consumption by 72 per cent and sugar consumption by 330 per cent (in 2009 US dollars). This makes the prospect of development North Australia and responding to its core concerns, a potential economic imperative.

Within Northern Australia there is approximately 17 million hectares of irrigable land. However, only one tenth of the water in storage has the current capacity to be utilized to meet this potential. The region is sparsely populated with just over 1.3 million people. In 2016, population growth was occurring at the rate of 0.3 per cent per annum in the Northern Territory compared with the national average of 1.7 per cent.

In order to realise economic potential, some significant hurdles the white paper acknowledged that significant infrastructure needed to be developed. In particular, attention needed to be given to the lack of water capture and storage, limited telecommunications, a small population, lack of transport and intermodal infrastructure, biodiversity and biosecurity threats and, more fundamentally, cultural concerns relevant to native title claims and the capacity of native title holders to develop the economic potential of these entitlements through investment and secured lending.

2. Outline of the Northern Australia Infrastructure Facility

One of the most significant initiatives, following the release of the White Paper, was the creation of the Northern Australia Infrastructure Facility (NAIF). The NAIF is a A\$5 billion five year fully capitalised fund. It has been established as a fast track for economic growth and stimulation in Northern Australia. The idea is to provide concessional debt funding in conjunction with private sector debt for the development of economic infrastructure in Northern Australia. The fund was established pursuant to the *Northern Australian Infrastructure Fund Act 2016* (Cth).

Pursuant to section 3 of that Act, the object was for the Commonwealth to provide grants to states and territories for the construction of Northern Australian economic infrastructure that (a) provides the basis for economic growth and (b) stimulates population growth.

The NAIF was established by the act pursuant to section 6 which sets out that that the Northern Australia Infrastructure is a body corporate, must have a seal, may acquire and dispose of real property and may sue and be sued. In performing its functions, the NAIF must, pursuant to section 9, give regard to the investment mandate issued by the Minister. The investment mandate is effectively the directions set out by the Minister regarding the performance of the facility's functions.

3. Adequacy and Transparency of NAIF Governance Framework: Project Assessment and Approval Processes

(i) Risk management Framework for NAIF as a Commonwealth Entity

The first concern with the current framework for NAIF is that the establishing legislation does not explicitly incorporate a system of risk oversight and management. The NAIF is essentially controlled by a very broad discretionary Ministerial investment mandate. The investment mandate is comprised of a set of ministerial directions, issued by the relevant Commonwealth Minister. There are no explicit requirements for inclusion within this investment mandate as mandated by the relevant act. As such, the investment mandate is highly discretionary.

Section 10 of the legislation sets out that the following “may” be included but these are not mandatory:

- (a) objectives the Facility is to pursue in providing financial assistance;
- (b) strategies and policies to be followed for the effective performance of the Facility's functions;
- (c) loan characteristics for circumstances in which financial assistance is used to provide or support loans;
- (d) providing financial assistance for purposes other than to provide or support loans;

- (e) eligibility criteria for financial assistance;
- (f) risk and return in relation to providing financial assistance;
- (g) any other matters the Minister thinks appropriate.

None of these matters “must” be included. The only explicit requirement for the investment mandate is that it may not direct or have the effect of directing the facility to provide funds for a particular infrastructure or for a particular person. In effect, the investment mandate need only be a broad directional mandate. The framework prevents the Minister, via the investment mandate, from directly compelling the NAIF to use the money for a particular purpose.

Further, the NAIF need only make ‘reasonable efforts’ to comply with the investment mandate. Hence, if compliance with the investment mandate is deemed unreasonable by the board, given their discretion, the board has the capacity to ignore any directions included within this mandate.

Finally, any decision regarding the issuing of concessional loans by the NAIF must be subject to the consideration of the Minister. The *North Australian Infrastructure Fund Act 2013* (Cth) sets out that the NAIF must not give approval to a concessional loan until the Minister’s ‘consideration period’ is satisfied. The consultation period is 21 days following the proposal. During this period, the Minister may ‘reject’ the proposal where it is inconsistent with the objectives and policies of the Commonwealth government, has adverse implications for Australia’s national or domestic security or has an adverse impact on Australia’s international reputation or foreign relations.

The overall effect of these provisions means that it is possible that the NAIF board could make determinations regarding concessional loans over public resources for infrastructure in North Australia in circumstances where the eligibility of the applicant is unclear. The need to fully determine the need for financial assistance may not be included within the investment mandate. The need for the NAIF board to evaluate the suitability of the proposal, in comparison with other proposals that cohere with the core requirements for North Australia (as enunciated in the White Paper above) may not be a mandated criterion within the investment mandate. Furthermore, it is possible that NAIF board could, under the current legislative framework, make determinations regarding concessional loans for infrastructure in North Australia where

the risk and return in relation to the provision of that finance is not evaluated, where no strategic policy has been developed for risk management and where no public reporting requirements are imposed. This would seem to represent a clear violation of the purpose and objectives of the provisions of the PGPA with respect to the management and administration of public resources by Commonwealth entities.

(ii) *Outline of Requirements of the Public Governance and Accountability Act 2013 (Cth)*

Significantly, the *Public Governance and Accountability Act 2013 (Cth)* (PGPA) applies to the NAIF as the NAIF is regarded as a Commonwealth entity managing public resources. The focus of the PGPA is upon the reporting, use and management of public resources by Commonwealth entities. The provisions of the PGPA introduce a single definition of 'public resources' and they subject 'public resources' as well as 'relevant money', 'relevant property' and 'appropriations' held by Commonwealth entities to an aligned set of uniform obligations.

Sections 16-19 of the PGPA impose a duty on the part of NAIF to establish and maintain systems relating to risk and control. A duty to encourage cooperation with others. They also impose a duty to keep the responsible Minister and Finance Minister informed. Similarly, in sections 25-29, NAIF officials are subject to a duty of care and diligence; a duty to act honestly, in good faith and for a proper purpose with respect to their position and the use of information and a duty to disclose interests.

The PGPA requires that public resources be used properly. In the context of Commonwealth entities vested with the management of public resources this means efficiently, effectively and economically. The PGPA focuses upon resource management and, in particular, the adoption of resource management practices which reflect the cycle of planning, measuring, evaluating and reporting on the result of performance to Parliament, relevant Ministers and the public. The PGPA also seeks to facilitate collaboration. Hence, there is a clear duty on accountable authorities to facilitate collaboration amongst Commonwealth entities, and with their partners (including States and Territories, private sectors and not-for-profit sectors) and a duty to consider the effect of imposing compliance burdens on them.

(iii) *Scope and Operation of the Minister's Power of Veto*

The governance framework does not make it clear whether the Minister could ‘reject’ a proposal that does not conform with the risk or resource management protocols of the PGPA. Whilst the Minister has the capacity to reject a proposal which is inconsistent with the objectives and policies of the Commonwealth government, it is unclear whether this would include the objectives specifically set out under the PGPA or any other Commonwealth Act. The objectives of the PGPA include: the establishment of a coherent set of governance and accountability responsibilities within Commonwealth entities, the proper use and management of public resources (and this includes use that is consistent with public benefit) and the provision of meaningful information to the Parliament and the public.

The discretionary capacity of the Minister to reject a proposal where it is regarded as inconsistent amounts to a power of veto although the provisions guiding the exercise of this power are very broad and unstructured. In this regard, the power is insufficiently framed within the current governance framework. It is unclear whether a proposal which is ‘inconsistent with the objectives and policies of the Commonwealth government’ would include a proposal which goes against the PGPA purposes or whether the ‘inconsistency’ provision is a concept that the relevant Minister has a broad discretion to determine. If the latter, it is possible that the Minister would not reject a proposal that is non-compliant with the risk and resource management provisions in the PGPA.

(iv) Discretionary Functions of the NAIF Board

Providing the NAIF board with the discretion to make decisions regarding the use of funds that amount to ‘public resources’ in the absence of proper risk and resource management processes constitutes a breach of the existing PGPA provisions. The PGPA makes it clear, in section 16(a) that Commonwealth entities, such as the NAIF, must incorporate a system of risk management and oversight into their decision-making process regarding the management and distribution of public resources. Furthermore, the PGPA makes it clear that resource management practices need to accurately reflect a strategy that is underpinned by financial planning, measurement, evaluation and reporting of performance to Parliament and the public.

The best way to comply with s16(a) of the PGPA is to establish and maintain an appropriate system of oversight and management systems that accords with the Commonwealth Risk Management Policy. In accordance with this policy, these systems must be included in the corporate plan and they will:

- (i) Endorse the NAIF's risk management policy
- (ii) Endorse the NAIF's risk management framework
- (iii) Define responsibility for managing risk in the NAIF
- (iv) Define who is responsible for determining the NAIF's appetite and tolerance for risk
- (v) Allocate responsibility for implementing the risk management framework and
- (vi) Define roles and responsibilities in managing individual risks.

The *Northern Australian Infrastructure Fund Act 2016* (Cth) does not set up a framework that ensures these risk management protocols will be complied with because:

- i) There are no provisions in the *Northern Australian Infrastructure Fund Act 2016* (Cth) which explicitly require the board of the NAIF to set up risk and resource management, oversight or strategies that cohere with PGPA compliance requirements. The Act notes that the PGPA applies but goes no further.
- ii) The investment mandate that is issued by the Minister is essentially discretionary in nature. The Minister may include a provision requiring the board to establish risk and resource management processes however this is not compulsory and the discretionary nature of this investment mandate may be non-compliant with the requirements of the PGPA.
- iii) Even where a PGPA compliant investment mandate is issued by the Minister, which does include appropriate risk and resource management processes, the board of the NAIF need only make 'reasonable efforts' to comply with it.
- iv) The strategies and policies that the board of NAIF establishes must be within the scope of the investment mandate (as set out in section 14(1)(a)). As such, where an investment mandate does not incorporate appropriate risk and resource management strategies, the board of NAIF must, in accordance with section 14(1)(a), act within the scope of that mandate.

- v) The capacity of the Minister to reject a proposal for funding during the ‘consideration period’ is unclear. This is any such rejection would need to be based on the fact that the proposal is inconsistent with the objectives and policies of the Commonwealth government. This broad capacity is not refined by further provisions outlining how and why a funding proposal might be inconsistent and indeed, what the objectives and policies of the Commonwealth are within this context.

4.The adequacy of the NAIF’s Investment Mandate and the Public interest test in guiding decisions of the NAIF Board

The current investment mandate that has been issued pursuant to the *North Australian Investment Facility Act 2016* (Cth), and which the NAIF board must adhere to, incorporates mandatory and non-mandatory criteria.

The Mandatory Eligibility Criteria are as follows:

1. The project involves the construction or enhancement of economic infrastructure
2. The project will be of public benefit
3. The project is unlikely to proceed, or only at a much later date, or with limited scope, without NAIF financial assistance
4. The project is located in, or will have a significant benefit for northern Australia
5. NAIF’s loan is not the majority source of debt funding
6. The loan will be able to be repaid or refinanced

7. Indigenous engagement strategy

The Non-Mandatory Eligibility Criteria are as follows:

1. The project is seeking finance from NAIF for an amount of at least \$50 million
2. There is an identified need for the project

Projects need to demonstrate public benefit and there is a need for NAIF investment to involve construction or enhancement of economic infrastructure, have an Indigenous engagement strategy and effectively demonstrate that the loan will be able to be repaid. NAIF investment must not exceed 50 per cent of the total debt of the project. Projects do not need to be entirely within the boundaries of Northern Australia if they produce significant benefits for the north. For example, a project that enhances north-south connectivity may be eligible.

Other Considerations:

The Board must be satisfied that NAIF's return on the facilities it advances will cover at least the Commonwealth's cost of funding and NAIF's administrative costs. The Board will also have regard to the potential effect of the project on other infrastructure and of the NAIF's financing on the Australian infrastructure financing market and on the necessity of the NAIF investment to encourage private sector participation in financing the project.

(i) Inadequacy of Mandatory Eligibility Criteria for Risk Management

The mandatory eligibility criteria that has been set out within the investment mandate does not include adequate risk and resource management strategies to comply with the PGPA requirements. Other than the need for the loan to be repaid or refinanced, there is no explicit criteria that articulates clear and specific individual eligibility requirements for a concessional loan proposal from the NAIF (other than public benefit, enhancement of infrastructure, benefit to North Australia, that the loan not be the majority source of funding.)

There is no indication or guidance within the mandatory criteria setting out how the loan is to be assessed and in particular, how it is to be assessed by comparison with other urgent projects. Neither is there any mandatory criteria setting out what the maximum amount of any single loan should be for an individual applicant, how the economic enhancement of any

infrastructure is to be assessed (i.e. should short term or longer term economic perspective be adopted). Neither is there any mandatory criteria setting out how the NAIF is to determine whether the specific loan proposal coheres (if at all) with the broader themes relevant to the development of North Australia, as articulated within the white paper discussed above, and which explicitly include water capture and preservation, urban growth, biodiversity, native title and cultural engagement and improvement.

The existing mandatory eligibility requirements focus exclusively upon factors relevant to the infrastructure project itself and fail to balance this assessment with factors directly relevant to the individual applicants who are seeking the concessional loan (credit history, capacity to repay should the project prove financially unsuccessful, eligibility compared with other applicants; proportion of NAIF funding compared with other funding obtained by the applicant etc.). This generates strong risk management concerns which are not adequately offset by the bare inclusion of a criteria that requires the NAIF to take account of the ‘need’ for the loan to be repaid or refinanced nor the requirement that NAIF’s return on the facilities it advances cover at least the Commonwealth’s cost of funding and NAIF’s administrative costs.

The absence of this focused criteria is concerning, particularly given the fact that the fund is comprised of public resources and that the NAIF board is a Commonwealth entity which is statutorily obliged to ensure these funds are ‘properly’ managed for the benefit of the public. In this context, there is a substantial risk that public resources will be given over for individual proposals where the evidence of the capacity for repayment is either inadequate or unclear. The existence of vague and weak criteria within the investment mandate means that the NAIF lacks appropriate guidance with respect to this important risk management outcome.

There existing framework includes no mandatory transparency requirements. The absence of such requirements is directly inconsistent with the PGPA, which seeks to ensure that the NAIF and any Commonwealth entity managing public resources is compelled to comply with public reporting obligations. The mandatory criteria don’t require the applicant seeking funding to report on the status of the project and nor does it require the NAIF board itself to provide a public report detailing the reasons for their exercise of discretion or how this discretion coheres with the broader imperatives of North Australia as delineated within the White paper. This is a significant and concerning omission for a fund that has been established to administer public resources.

Failure to Define “Public Benefit” Means it is Equated with Enhanced Economic Infrastructure

The mandatory eligibility criteria don't define public benefit and it does not explain how public benefit must be assessed in the context of the management and distribution of significant amounts of public resources by a Commonwealth entity. Public benefit should not be presumptively equated with enhanced economic infrastructure, particularly within a public resource framework such as that which exists in Australia. The mandatory criteria set out in the existing investment mandate needs clearly defined to ensure that considerations relevant to public benefit are taken into account by the NAIF board.

Public benefit, particularly in the context of the development of onshore resource projects, incorporates a multifarious range of social, environmental, economic and communitarian perspectives. The public resource framework in Australia generates strong communitarian responsibilities and its public benefit mandate must be exercised in a manner that is consistent with broader social welfare objectives. A failure to do so means that the State is acting beyond its mandate.¹ The ownership and management of public resources by the State are formally justified on the ground that governments have a superior capacity to ensure that the economic and social gains associated with the exploitation of public resources are fairly distributed with relevant the community.² On this basis, public resources are managed by the state, but only for the interest of the public as a whole. Public benefit assessment in this context must not be a nominal criterion, capable of being upheld wherever economic enhancement (which is an ambiguous concept in itself) might be apparent. Public benefit assessment constitutes core legitimizing criteria that is integral to any administrative framework associated with the management and facilitation of public resources.

The state, as de jure owner of public resources, must ensure that in managing and lending public resources, it acts in a manner that maximises current broader conceptions of public

1. See generally Joseph William Singer, *The Reliance Interest in Property*, 40 STAN. L. REV. 611 (1988) (noting that resource ownership attracts variable).

2. This market based efficiency response to natural resource management has been rejected by environmental ethicists; see, e.g., Mark Sagoff, *On Preserving the Natural Environment*, 84 YALE L.J. 205, 225 (1974) (noting that realistically there is no economic or even utilitarian rationale available for preserving the natural environment).

interest.³ This is an onerous responsibility, particularly given the dramatic changes occurring within the onshore resource landscape.

The increased connectivity between ownership norms, ecological imperatives and market forces has fundamentally shifted public interest beyond economic imperatives.⁴ The Australian community has become more attuned to the obligation of the state to manage public resources in accordance with progressive social and communitarian welfare. These new perspectives include: the promotion of broad environmental values (sustainability, prevention of environmental degradation, security over food and water with the advent of climate change and broader habitat imperatives associated with the period of the Anthropocene), social harmony, public health imperatives and the promotion and adherence of global and domestic commitments.

Determining which communities are affected by a decision to issue public resources and furthermore, how those communities feel about the prospect of such development, is a crucial element within all public interest responsibilities. The state cannot make decisions regarding the distribution of public resources, that purport to maximize social good, if it does not fully understand or appreciate the nature and texture of the community where those decisions have the biggest effect, what the priorities of the community might be and the potential impact of a decision regarding the broader distribution of public resources. Neither can it conform with public benefit imperatives in the absence of adequate risk management processes.⁵

The deep-rooted notion that the public has no legitimate societal interest in decisions made by the state with respect to public resources managed by Commonwealth entities is a misnomer. Public interest can and must be defined by public engagement and public involvement. This is particularly true given the potent issues that underpin environmental management, ecological

3. See Omorogbe & Oniemola, at 118; see also Ostrom, at 335-37 (differentiating between open access resource ownership and common resource ownership and noting that *de jure* government property regimes often lack resources to monitor effective usage, particularly in developing countries).

4. See Lynda L. Butler, *The Pathology of Property Norms: Living Within Nature's Boundaries*, 73 S. CAL. L. REV. 927, 938 (2000) (outlining the connectivity between economics and individualism in ownership norms).

5. Cf. Alexander, *supra* note 23 (presenting theories of property where ownership comes with obligations of support towards the community); John O'Neill, *Property, Care and Environment*, 19 ENV'T & PLAN. C: GOV'T & POL'Y 695, 696 (2001) (noting that "[c]are for particular places which embody the life of a community [. . .] is often expressed through resistance to liberal property rights").

sustainability and bio-diversity.⁶ Non-engagement with communitarian values and perspectives disconnects public resource management from their social and ecological context.

5.NAIF and The Adani Loan Proposal: Risk Management and Transparency Concerns

In December, 2016, it was announced that the NAIF board had provided preliminary approval (subject to final detailed board approval and ministerial approval) for approximately A\$1 billion concessional loan to Adani Mining Pty Ltd for the development of a 310 kilometre rail link from the Adani Carmichael coal mine to the Port of Abbot Point in Queensland. The proposed rail line is expected to provide capacity of 100 million tonnes of coal per year, increasing access to the Galilee Basin.

The proposal suggests that the rail link is to be used by multiple users, contributing an expected A\$368 million annually to the Queensland economy once in operation. This concessional loan is, however, problematic because the structure of the legislation and the investment mandate, mean that it is unclear what the eligibility criteria was for the approval of this loan and, in particular, whether the eligibility criteria satisfied PGPA requirements and broader conceptions of public benefit. The board is yet to provide final approval to this loan. Adani has indicated that it has a \$3.3 billion funding shortfall for the \$6.7 billion first stage of the project.

The Adani proposal highlights a number of risk and resource management concerns with the NAIF framework. These may be summarized as follows:

- The concessional loan being sought for the rail link is essentially a consequence of the failure by Adani to obtain funding from other lending sources. Whilst the mandatory criteria indicate that NAIF should take into account the fact that the project is unlikely to proceed in the absence of NAIF funding, the Adani situation does not appear to clearly satisfy broader risk management processes. The circumstances of the Adani project indicate that even though NAIF is not the major source of funding for the overall project, the rail-link was unlikely to be developed without NAIF funding because a

⁶Joseph L. Sax, *Ownership, Property, and Sustainability*, 31 UTAH ENVTL. L. REV. 1, 10 (2011) (noting that “understanding the nature of sustenance and biodiversity calls for a rethinking of our assumptions about landownership”).

majority of lending institutions refused to fund it. These institutions refused because their internal processes incorporated a more rigorous risk-management assessment process. A majority of lending institutions concluded, in accordance with this rigorous risk management assessment, that such a large amount of money to fund a rail-link for a coal-mine was not economically viable in the context of a global decarbonized economy and given the fact that coal is increasingly perceived as a legacy technology. It was estimated, given the global deceleration of coal projects, that the rail-link would rapidly become a stranded asset and, in the event of this occurring, it was unlikely that loaned funds would be adequately recovered. The NAIF framework does not provide a framework that suitably ensures a rigorous assessment of this potential outcome. There is no clearly delineated strategy for the recovery of public resources funding in the event, as foreseen by the majority of other lending institutions, that the project does not succeed.

- The NAIF is a Commonwealth entity that is charged with the proper management and facilitation of public resources. If the loan is eventually authorized by the NAIF board, it is likely that the weak risk management processes that the state has adopted with respect to the administration of those public resources will non-compliant with PGPA and non-compliant with broader public interest imperatives. The reasons for this anticipated non-compliance is summarized below:
 - (ii) Public benefit is not properly defined by the NAIF framework and as such, it appears to be grounded purely in short term economic perspectives that are inconsistent with long term perspectives and broader global trends;
 - (iii) The proposal fails take account of the social, environmental and communitarian perspectives that underpin all public benefit assessment processes within the modern state.
 - (iv) The proposal fails to incorporate rigorous risk and resource management protocols that are necessary and imperative when a Commonwealth entity is dealing with public resources as is apparent from the detailed provisions of the PGPA.

- The funding being sought by Adani is manifestly excessive when compared with the overall amount of funding available in the fund. There are no mandatory criteria compelling the board of NAIF to consider maximum amounts – only minimum amounts. If the Adani proposal is approved, one fifth of the entire fund will be distributed to an international investor, in a coal plant in circumstances where coal production goes against global decarbonization trends. The approval of such a large amount of funding proposal would also be contrary to PGPA and public benefit risk management requirements. There is, for example, no parity between the provision of \$1billion of public resources to fund a rail link for a large coal plant and the provision of only \$200 million for the National Water Infrastructure Development Fund, the latter which seeks to implement augmented water infrastructure in Norther Australia. The funding available for the National Water Infrastructure is manifestly inadequate when compared with the funding proposed for the Adani rail link despite the fact that the Water Infrastructure would appear cohere far more directly with the imperatives for North Australia expressly articulated within the white paper where the need for irrigable land and the absence of water storage is noted as a significant deficiency for North Australia. This disparity in the management and facilitation of public resources indicates a failure to ensure that the NAIF adopts a considered, comprehensive and proportionate approach to the assessment of public interest imperatives in the management and distribution of public resources within this region.