

Joint Committee of Public Accounts and Audit
Parliament House
Canberra, ACT 2600

29 June 2017

Re: Inquiry into the 2015-16 Defence Major Projects.

I hope with this fourth instalment to my submission, I will be able to show and point to some systemic failures in Defence that are causing many millions of dollars of unwarranted expenditure to the tax-payer.

In this, one can get lucky when I am able to quote from the retiring Secretary of Defence, Mr Dennis Richardson AO, when he said at his valedictory speech at the National Press Club on the 12th May 2017.

"The question of transparency, I think if you look at Senate Estimates today, you look at the fact that- the thing I find interesting is how much is in Senate Estimates and how little people take notice of it." Refer to Annex A for full quote in context.

A lot of my research has come from FADT Senate Estimates, but this submission comes from:

[Senate FADT Inquiry into Department of Defence's management of credit and other transaction cards](#)
[Public Hearing, Thursday 6 April 2017](#)

From listening to this public hearing and referring to the Hansard, I was to first learn about a senior Committee of Defence called the DARC (Defence Audit Risk Committee).

Senate Foreign Affairs, Defence and Trade References Committee
Department of Defence's management of credit and other transaction cards

Public Hearing, Thursday 6 April 2017

1.1 Refer Annex B for fragment of transcript

CHAIR: Okay. Can you place on the public record the audit process for Defence?
For a taxpayer out there who has read the Australian National Audit Office report, what is your normal audit process?
Is it internal or external?

Is it independent or is it employed by Defence?

External and Independent auditor is the ANAO

Dr. Clarke when asked about the internal audit said:

"I am independent of line management. I report to the Defence Audit and Risk Committee, which is chaired by an external member and has a majority of external members, and then that reports directly to the secretary."

My first question on hearing this, what or who are the Defence Audit and Risk Committee?

On reading the DARC Charter (Annex C) has Dr. Clarke misled the FADT Committee by stating that he reports only through the DARC?

BUT para 21 states

'The advisers for the DARC are the Chief Financial Officer and the First Assistant Secretary Audit and Fraud Control' raising the question of what is this independence and only reporting to the DARC as given in evidence, when the DARC Charter says they are advisers.

1.2 Refer Attachment 1 for the Defence Audit Risk Committee charter.

Refer Attachment 2 for Defence FOI response to questions relating to the DARC .

If the DARC (or its predecessors) had been doing their job, why have I (and others) been chasing the 'holy grail' of financial integrity in Defence.

Refer Attachment 3 - [Chief of Army Directive 21/13](#)

[Army Values and the Standard of Behaviour required of Army Personnel](#)

Refer Attachment 4 - DI(G) PERS 25-6 Conflict of Interest and Declarations of Interest

Please note this document refers to ADF and APS personnel.

Effective 29 March 2011

It is here where you examine the Charter of the Defence Audit Risk Committee.

This Charter contains 58 sections. (Annotations in Annex C)

As a private citizen and a past member of the Australian Defence Force, I have no right of access or interrogation of the D.A.R.C.

I am hoping this Joint Committee Public Accounts and Audit may fill the void.

It is here that I refer to ['Performance Audit Report No. 25 \(2012-13\) Defence's Implementation of Audit Recommendations'](#)

2.15 The Auditor-General also drew attention to the fact that the monitoring of audit recommendations was not one of the DARC's stated priorities, although it is a required under its Charter.⁶ ANAO also found that while DARC has the ability to call upon Group Heads and responsible officers to explain why recommendations are overdue, this has not occurred in recent years as the committee has turned its focus to other areas of risk in Defence. Further, the DARC made a verbal but not a written report to the Secretary, despite this being required by its Charter and recommended in the ANAO Better Practice Guide to Audit Committee.⁷

The Defence Audit Risk Committee is apparently a significant Committee, but with all the questions being raised over the last decade involving Major Projects I find it credulous that the Committee's working has not had much exposure.

I hope the Committee's report into the 2015-16 Defence Major Projects, will highlight the current, historical and future work of the Defence Audit Risk Committee.

For my ongoing question, is the Defence Audit Risk Committee functioning to its Charter?

If not, why not?

Michael Wunderlich

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Annexes

Attachments

Annex A: Quote from speech by Mr Dennis Richardson, AO

With thanks to the National Press Club for providing assistance.

QUESTION: Thanks, Chris. Mark Kenny from Sydney Morning Herald and The Age. Not so long ago, during the early days of one of our recent dysfunctional prime ministerships – and I won't say which one in deference to your public service position which exists at least for the remainder of today. But I suggested to a mutual friend of ours that perhaps they needed someone sensible and fearless and experienced in their office who could actually maybe bring some sanity to the operation. The intermediary got that message to you and a message came back to me, ask Mark has he lost his mind? So I thought that pretty much summed up the state of play there. But I wonder...

DENNIS RICHARDSON: [Interrupts] I am well past that sort of gig.

QUESTION: You don't appear to recall that incident. But I wonder if I could ask you about openness, whether there is enough openness in Australian public administration, in politics, and particularly in your area of defence. Many of my colleagues here who specialise in defence and security matters are well experienced in getting information, sometimes from foreign services, from the defence forces of other countries more easily than from ours, and certainly there is a very strict management of information these days in politics generally. As you depart the scene, can I invite you to comment on that, whether we could do with a great deal more openness in our official information dissemination?

DENNIS RICHARDSON: Well, given that I'm walking out the door, I just think there is just not enough transparency, just dreadful.

[Laughter]

Seriously, I think Defence is a difficult customer when it comes to the media. We have a lot of moving parts in the organisation and getting ourselves coordinated across that takes time. That causes real frustration to the media, and I understand that, and it certainly has not improved in my time there. The question of transparency, I think if you look at Senate Estimates today, you look at the fact that the thing I find interesting is how much is in Senate Estimates and how little people take notice of it. Departments can now be recalled to Senate Estimates at any time during the year, and that does happen. In terms of the media, I think, as said, the natural condition of public servants is to be cautious. I have often had differences in organisations I have worked in where people refuse to answer a simple question with a yes or no. Now, sometimes you can't, but to get yourself so acculturated whereby you can never say a yes or no, I think, is not good and I think that is the position where a lot of us are in with our organisations, and I have certainly not made inroads into that. And the views I have expressed to you are the views that I have expressed within Defence and elsewhere.

Annex B: Extract from Hansard - 06 April 2017

[Extract from Hansard - 06 April 2017 - Department of Defence's management of credit and other transaction cards.](#)

CHAIR: My first question is where is the CFO?

Ms Diamond : He is actually on leave.

CHAIR: His leave took precedence over this inquiry? How long is he on leave for?

Ms Diamond : He has been on leave for almost four weeks.

CHAIR: I am sure he was at estimates.

Ms Diamond : Yes, he was.

Mr Spouse : I think that was the last week before his leave.

Ms Diamond : He went on leave on 10 March.

CHAIR: Okay. Can you place on the public record the audit process for Defence? For a taxpayer out there who has read the Australian National Audit Office report, what is your normal audit process? Is it internal or external? Is it independent or is it employed by Defence?

Dr Clarke : It is both. We have an internal audit function and capability, which I manage, and we are also subject to external audit scrutiny through the ANAO.

CHAIR: Are you saying that the independent audit of your function is by the ANAO?

Dr Clarke : Our external audit is independent, by definition.

CHAIR: And internally?

Dr Clarke : I am independent of line management. I report to the Defence Audit and Risk Committee, which is chaired by an external member and has a majority of external members, and then that reports directly to the secretary.

CHAIR: What I am trying to get to the bottom of is that in 2009 you agreed to implement some controls and in 2015 or 2016, when the ANAO did its audit, it found that you had not acted on it. Can you please explain that?

Dr Clarke : I will defer to the CFO on the implementations of controls. They rest in the CFO group.

CHAIR: You are in charge of audit and there was an agreement in 2009 to implement some controls.

Dr Clarke : Indeed.

CHAIR: And you are now deferring to the chief financial officer for the answer of why it was not done.

Dr Clarke : The audit function is to review and provide assurance about the implementation of controls and the effectiveness of those controls. We do not implement the controls themselves. They rest with line management.

CHAIR: Thank you. Ms Diamond, are you going to tell us why you did not act on the 2009 report?

Ms Diamond : In terms of the levels of controls, Defence acknowledges that there were some weaknesses, which was part of the audit report that identified the three recommendations which we have implemented. Since that 2015 audit report which we are talking about, we have turned around and improved our controls framework.

CHAIR: Sorry, but you are not answering my question. In 2009 you gave assurances that you would put in place some controls. A subsequent audit, many years later, found that you had not acted on that 2009 report. Please tell me why.

Ms Diamond : We did actually have a controls framework back in 2009. Whether it was sufficiently addressing all the concerns has obviously been a part of the subsequent audit. There has been continuous improvement to our controls framework and we continue to look at those controls even today. I appreciate what you are saying, but it is an evolving and improving framework. If we look at the controls that we have today, they are looking more at analytics and doing far more forensic analysis than what we have done previously. That is part of improving our controls.

CHAIR: No. My question is very, very specific and it is contained in the independent audit of your activity. It says:

The suite of preventative controls used by Defence to control spending on credit cards is not complete and has limited effectiveness: it has not used blocking in any substantial way; access to cash advances for purchasing was not properly authorised until after this audit commenced; a 2009 plan to lower default limits on available credit was not implemented until January 2016; and Defence has issued thousands of credit cards that have never been used.

My question to either of you is: if a risk was identified in 2009, and the plan was not implemented in 2016, who is going to take ownership of that period?

Mr Spouse : As you say, and paragraph 9 of the audit report talks about the 2009 plan, the plan to implement lower thresholds was not implemented. As we became aware of that in 2015, we immediately implemented controls to review all credit card limits and lowered them where that was appropriate. But that was the action we took as a result of this report; in the earlier period, I am not aware why the measures from that earlier report were not implemented.

CHAIR: Do we just erase seven years from the memory? Who was responsible for that?

Mr Spouse : I am not aware. I was not involved, and Ms Diamond was not involved in the administration of credit cards at that time. What we have done is this: we reacted during the development of the audit report to strengthen the controls, to review the limits and to put in place the sorts of measures we now have—we have annual reviews, and the limit for every single card has been reviewed. That is the action we have taken.

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FOREIGN AFFAIRS, DEFENCE AND TRADE REFERENCES COMMITTEE

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CHAIR: I would accept your evidence that in 2016 you were taking proactive—

Mr Spouse: Absolutely.

CHAIR: I accept that evidence, but my concern is this: in regards to blocking mechanisms, Defence had no categories blocked on its purchasing card. On travel cards, only merchant category 7997 was blocked. That category is:

Clubs, Country Clubs, Membership (Athletic, Recreation, Sports), Private Golf Courses, Entertainment. However, 24 travel cards in the last three years still managed to spend \$15,000 within that category. So, you did not use your blocking mechanisms for about seven years.

Annex C: Questions of Interest - Defence Audit and Risk Committee Charter

DEFENCE AUDIT AND RISK COMMITTEE CHARTER

1. The purpose of this Charter is to set out the responsibilities of the Defence Audit and Risk Committee (DARC) and how it will operate. It is cognisant of the ANAO Better Practice Guide *Public Sector Audit Committees* March 2015 and will be reviewed annually.

[Public Sector Audit Committees - Independent Assurance and Advice for Accountable Authorities](#)

- a) Who within the DARC is on a sub-committee looking at 'risk'? (PDF Page 11 of 116)
- b) Who within the DARC is on a sub-committee looking at 'fraud'?
- c) Who within the DARC is on a sub-committee looking at 'security'?

[Public Sector Audit Committees - Companion to the Better Practice Guide](#)

2. The Defence Audit and Risk Committee (DARC) is a central element of governance in the Department of Defence (Defence). It has been established by the Secretary and Chief of the Defence Force (CDF) in compliance with section 45 of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), PGPA Rule section 17 Audit Committees for Commonwealth Entities and in accordance with the joint responsibilities of the Secretary and CDF under section 9A of the Defence Act 1903.

[s45 Public Governance, Performance and Accountability Act 2013 \(PGPA Act\)](#)

[PGPA Rule s17 Audit Committees for Commonwealth Entities](#)

Functions of the audit committee

- (2) The functions must include reviewing the appropriateness of the accountable authority's:

- (a) financial reporting; and
- (b) performance reporting; and
- (c) system of risk oversight and management; and
- (d) system of internal control;

for the entity.

[s9A Defence Act 1903](#)

3. The Secretary and CDF authorise the DARC, within the scope of its role and responsibilities to:
- 3.1. obtain any information it needs from any official and/or external party (subject to their legal obligation to protect information);

Please itemise by way of a list, all information received by way of any official and /or external party for the financial year 2015-16.
If not, why not?

Please itemise by way of a list, all Major Projects information received by way of any official and /or external party for the financial year 2016-17.
If not, why not?

- 3.2. discuss any matters with the Australian National Audit Office (ANAO), or other external parties (subject to confidentiality considerations);

Please list the items that were discussed with the ANAO for the financial year 2015-16.
If not, why not?

Please list which Major Projects were discussed with the ANAO for the financial year 2016-17.

- 3.3. request audits or reviews of specific areas or systems;

Please list the audits or reviews of specific areas or systems were requested for the financial year 2015-16.
If not, Why, not?

Please list which Major Projects audits or reviews of specific areas or systems were requested for the financial year 2016-17.

- 3.4. request the attendance of any official, including the Secretary and CDF, at committee meetings; and

Please list the

- a) dates of regular committee meetings for both 2015-16 and 2016-17,
- b) members of the committee that attended,
- c) those who attended as 'observers',
- d) those who attended as 'required attendees',
- e) dates that the Secretary of Defence attended,
- f) dates that the Chief of the Defence Force attended.

3.5. obtain legal or other professional advice, as the DARC considers necessary, to fulfil its role, at Defence's expense, subject to approval by the Secretary and/or CDF, or delegate.

- a) How many legal folio's were opened in each of 2015-16 and 2016-17?
- b) What was Defence's financial cost for this legal advice in each of 2015-16 and 2016-17?
- c) Did the Committee solely use Defence Legal, or were civilian firms involved?
- d) If civilian legal practices were used, what was the percentage attributed to both groups.
- e) Please list the civilian legal firms used for this advice?
- f) How many professional advice / consultant files were opened?
- g) Please list the companies and individuals that provided advice to the Committee.

FUNCTIONS

4. The DARC's role is to provide independent assurance and advice to the Secretary and CDF on Defence's financial and performance reporting responsibilities, risk oversight and management and system of internal control. This will be achieved through a rolling three year forward work plan to be updated annually.

Please explain in a succinct paragraph how the Committee is providing assurance and advice to the Secretary and CDF on the DMO/CASG's ongoing problem with 'slippage' in its Major Projects list. Please refer to the latest ANAO publication and JCPAA inquiry.

5. The DARC is not responsible for the executive management of functions it reviews. The DARC will engage with management in a constructive and professional manner in discharging its advisory responsibilities and formulating its advice to the Secretary and CDF.

In early 2014, the Secretary and the CDF approved the final report of the [Re-Thinking Systems of Inquiry, Investigation, Review and Audit](#)

The audit phase was completed on the 19th February 2014.

It identified the following categories of concern.

- 1. Gaps/delays in briefing senior decision makers and Ministers
- 2. Leadership failure at a senior level
- 3. Failure to appreciate complex interdependencies
- 4. Underestimated project complexity and cost
- 5. Changes to project scope and objectives

6. Project management deficiencies
7. Insufficient skilled personnel
8. Project record-keeping deficiencies
9. Controls not effective
10. Failure in project accounting

How has the DARC engaged with management in a constructive and professional manner in discharging its advisory responsibilities and formulating its advice to the Secretary and CDF to reconcile these ten audit concerns?

Reference is made here to point 2 of the Charter:

[PGPA Rule s17 Audit Committees for Commonwealth Entities](#)

Functions of the audit committee

- (2) The functions must include reviewing the appropriateness of the accountable authority's:

- (a) financial reporting; and
- (b) performance reporting; and
- (c) system of risk oversight and management; and
- (d) system of internal control;

for the entity.

Refer here to [Public Sector Audit Committees - Independent Assurance and Advice for Accountable Authorities](#) item 2.2.4 System of internal control PDF Pages 12-15.

6. The Chair is to report to the Secretary and CDF on matters of concern. Following each meeting, the Chair is to advise the Secretary and CDF on key issues arising from the DARC's meeting and activities.
7. The DARC, or any individual member, does not have a duty to initiate audits or activities, to seek out specific activities not compliant with policies and procedures, although there is a duty to act if any such activities come to their attention, and to assess compliance in general.

Is Charter Item 7, an excuse clause to be used when 'reputational risk' becomes an issue?

8. In relation to **Financial Reporting**, the DARC will review the annual financial statements and provide advice to the Secretary (including whether appropriate action has been taken in response to audit recommendations and adjustments) and recommend their signing by the Secretary.

This is a questionable proposal given the 'mandatory fields' mentioned in [Q170](#) Senate Estimates 2014 - PM&C Portfolio

In particular, the DARC will assure:

8.1. Defence's compliance with accounting standards

Refer [F147](#) Senate Budget Estimates 2014 - Finance Portfolio

Agencies reported 12,798 instances of non-compliance with the financial management framework in 2011-12 and 14,027 instances in 2012-13. This aggregate number includes serious issues such as fraud, financial errors and minor technical breaches. The nature of the information collected does not enable an overall figure for fraud to be determined. Further information is contained in the 2012-13 Certificate of Compliance Report to the Parliament.

8.2. the appropriateness of accounting policies and disclosures and any significant changes to accounting policies and practices

Refer 5(10) Failure in project accounting

Refer to the Senate FADT Inquiry

[Department of Defence's management of credit and other transaction cards](#)

[Refer to Parview for the 6th April 2017 for this Inquiry](#)

8.3. areas of significant judgement and financial statement balances that require estimation

Foreign currency application (No Win No Loss)

8.4. significant or unusual transactions

Refer Credit Card Inquiry

8.5. sign-off by Defence management in relation to the quality of the financial statements, internal controls and compliance, and

Refer 22 November 2004 when Auditor would sign off because \$8bn of assets and liabilities could not be accounted for.

8.6. whether appropriate management action has been taken in response to any issues raised by the ANAO, including financial statement adjustments or revised disclosures.

Review of Auditor-General's Reports 2000-01: Second and Third Quarter

[Chapter 3:](#)

[Audit Report No. 22, 2000-01: Fraud Control in Defence \(PDF Format 59KB\)](#)

3.9 The audit found that Defence lacked a suitable fraud intelligence capability. The ANAO maintained that having a sound fraud intelligence capacity would help in assessing whether Defence had under-estimated the extent of fraud in or against Defence.¹¹

¹¹ ANAO, Report No. 22. 2000-2001, pp 13

Can DARC give its understanding to what a 'fraud intelligence capability' is?

Does DARC consider that the Department of Defence has an effective capability in 2017?

On what basis do you give your understanding?

9. The DARC will review the processes in place designed to ensure that financial information included in the Defence Annual Report are consistent with the signed financial statements;

This is a questionable review given Q170 in Senate Budget Estimates 2014 - PM&C Portfolio

When has the DARC ever given a dissenting view?

10. The DARC will discuss with the ANAO the auditor's judgements about the adequacy of Defence's accounting policies and the quality of Defence's processes for the preparation of the financial statements.

Can the DARC give three recent examples?

11. In relation to **Performance Reporting**, the DARC will review Defence's systems and procedures for assessing and reporting the achievement of the Defence's performance. In particular, the committee will satisfy itself that:

- 11.1. Defence's Portfolio Budget Statements and corporate plan include details of how Defence's performance will be measured and assessed
- 11.2. Defence's approach to measuring its performance throughout the financial year against the performance measures included in its Portfolio Budget Statements and Corporate Plan is sound, and has taken into account guidance issued by the Department of Finance
- 11.3. Defence has sound processes in place for the preparation of its annual Performance Statement and the inclusion of the Statement in its annual report, and
- 11.4. Defence's proposed Performance Statement is consistent with Defence's financial information, including its financial statements, that it proposes to include in its annual report.

12. In relation to **Systems of Risk Oversight and Management**, the DARC will:

- 12.1. review the risk profile, risk appetite statement and enterprise risk assessment of Defence;
- 12.2. review whether management has in place a current and comprehensive enterprise risk management framework which includes internal controls for effective identification and management of Defence's strategic-level business and financial risks;

- 12.3. satisfy itself that a sound and effective approach has been followed in managing Defence's major risks and, as appropriate, those associated with individual projects, program implementation, and activities;
- 12.4. review Defence's fraud control plan and satisfy itself that Defence has appropriate processes and systems in place to detect, capture and effectively investigate fraud related information and that these processes facilitate and comply with Commonwealth policies;
- 12.5. review reports on fraud from the First Assistant Secretary Audit and Fraud Control that outline any significant or systemic allegations of fraud, the status of any ongoing investigations and any changes to identified fraud risk in Defence; and

Refer:

into [Evidence given to Senate FADT Committee on 6th April 2017](#) at the inquiry
[Department of Defence's management of credit and other transaction cards](#)

Historical note:

1/

In c2000 the ANAO made a recommendation for a fraud intelligence capacity in Defence, as reported in
[Chapter 3: Audit Report No. 22, 2000-01: Fraud Control in Defence \(PDF Format 59KB\)](#)

3.12 extract

"Furthermore, none of the military police, who investigate approximately 85 per cent of fraud cases, had obtained a *Certificate IV, Fraud Control (investigations)*. The certificate is considered the minimum industry qualification.¹⁵

3.13 extract

Defence stated that the cost of establishing an intelligence capacity would ... not seem to represent good value-for-money'.¹⁶

In the context of Defence's 2001 reply, please refer to the Australian Federal Police 2016 FOI Log, that highlights their final [report on Operation Majorca](#) from the late '90's.

From the [Defence Annual Report 2000-01](#) PDF Page 62 of 356 on \$12.319bn

"The determined fraud loss for completed cases was some \$1.06m, of which \$340,000 was recovered. Over the last seven financial years, detected fraud has averaged an estimated \$2.1m per year within a range of \$1.1m to \$3.1m per annum."

From [The Australian, January 30, 2008 - 'Billion dollar blowouts'](#)

"The delays, cost blowouts and failure to deliver we've experienced in defence procurement in recent years cannot be allowed to continue."

Yet beneath this glossy surface there lies a raft of multi-billion-dollar problems which Fitzgibbon has inherited and which he knows - with the passage of time - he will be blamed for unless they are fixed.

From the [Defence Annual Report 2010-11](#) PDF Page 200 of 498 on \$24.403bn

The determined fraud loss for completed cases in 2010-11 was \$0.9 million, while monies recovered amounted to \$0.4 million. As Table 6.1 shows, over the past five financial years detected fraud has averaged approximately \$1.1 million per year, within a range of \$0.7 million to \$2.3 million.

Table 6.1 Determined Fraud Loss and Recoveries 2006-07 to 2010-11^[1]

	2006-07 (\$)	2007-08 (\$)	2008-09 (\$)	2009-10 (\$)	2010-11 (\$)
Loss	707,230	2,302,281	690,452	1,039,721	916,419
Recovery ^{[2][3]}	112,320	189,494	300,796	359,393	422,691

From the [Defence Annual Report 2015-16](#) PDF Page 81 of 172 on \$31.989bn

In 2015-16, the determined fraud loss for completed investigations was \$535,766, while monies recovered amounted to \$202,879. Table 5.1 shows detected fraud over the past five financial years, averaging approximately \$870,000 per year within a range of \$480,937 to \$1.4 million.

Table 5.1: Determined fraud losses and recoveries, 2011-12 to 2015-16

	2011-12 (\$)	2012-13 (\$)	2013-14 (\$)	2014-15 (\$)	2015-16 (\$)
Loss	1,102,979	835,685	1,400,422 ¹	480,937	535,766
Recovery	493,210	393,902	133,457	161,693	202,879

Note

1. The determined fraud loss for 2013-14 has been adjusted since the last annual report to take into account a case where \$370,000 was incorrectly reported as a fraud loss.

The Defence Budget has literally tripled in the last 16 years but the Determined Fraud has halved.

In 2001, the only qualified fraud investigators (from memory, eleven) within Defence were held within the Inspector General - Defence (now ASFC since 2015).

However from [Senate Budget Estimates 28 May 2012 Q7 - Fraud Detection](#)

Defence admitted:

"There are currently 590 personnel in Defence who are either qualified or meet the prerequisites to be qualified in accordance with the Australian Government Investigations Standards to conduct fraud investigations."

I would hope that there is an equivalent if not more number in 2017.

It is more than disappointing to see that given the qualified personnel available in 2012, that the Determined Fraud Loss in 2016 (\$535,766) is half that of 2001 (\$1.06m).

When was the Defence Audit Risk Committee advised of this developing and now on-going situation?

If not, why not, given the assurances to the Minister and the Parliament in the Letter of Transmittal signed by the Secretary and the CDF over this 16 year period? Assurances supposedly emanating from this Committee.

Now a question here is whether the Senate Estimates process was misled in 2012 because in November 2011, 'The Report of the Five Year Audit of the Australian Defence Force Investigative Service' was released.

Refer:

AGIS Requirements

28. It was identified by the audit team that the ADFIC no longer complies as a qualification under Australian Government Investigation Standards (AGIS). However, the Defence Investigative Standards (DIS) sets a requirement for compliance with the AGIS.
29. However, previous amendments to the TMP have decoupled the AGIS requirements from the ADFIC. Currently the ADFIC only complies with AGIS methodologies, not with the qualification requirement (Certificate IV in Government, Fraud Control Investigation and Diploma of Government Fraud Control Investigation). It appears that the AGIS is considered a generic guide in the conduct of the ADFIC with regard to the evidence matrix and resource spread sheet.
- 12.6. review Defence's Workplace Health and Safety (WHS) Management and satisfy itself that Defence has the appropriate governance arrangements, plans, processes and controls to achieve a sound WHS Management Framework and supportive culture. This shall include consideration of the effectiveness of the management oversight committees, such as the Defence Work Health and Safety Committee.

13. In relation to Defence's **System of Internal Control**, the DARC will consider a broad range of factors:

13.1. Internal control framework:

Refer to the Canberra Times articles

- a) [Consultants and contractors now outnumber public servants in Defence Department - February 20, 2017](#)
- b) [Is Defence Department secretary Richardson for real about cutting back on consultants? - February 21, 2017](#)
- c) [Dennis Richardson calls time on Defence Department consultants' bonanza - March 11, 2017](#)

Refer to JCPAA [Inquiry into the 2015-16 Defence Major Projects Report Submission No. 1.2](#) by Michael Wunderlich

Was the growth in Service Providers, Contractors and Consultants, as reported in the Canberra Times, part of the package of briefings given to the Secretary of Defence?

If not, why not?

- 13.1.1. review whether management's approach to maintaining an effective internal control framework, including over external parties such as contractors and advisers, is sound and effective;
- 13.1.2. review whether management has in place relevant policies and procedures, including Accountable Authority Instructions or their equivalent and the delegations framework, and that these are periodically reviewed and updated;
- 13.1.3. satisfy itself that appropriate processes are in place to periodically (but not less than once per year) assess whether key policies and procedures are complied with;
- 13.1.4. consider how management identifies any required changes to the design or implementation of key internal controls; and
- 13.1.5. satisfy itself that management periodically assesses the adequacy of Defence's information security infrastructure.

13.2. Legislative and Policy Compliance:

- 13.2.1. review the effectiveness of the system for managing and monitoring Defence's compliance with relevant laws, regulations and associated government policies with which

Defence must comply, including the effectiveness of key governance processes;

- 13.2.2. review, where relevant, Defence's compliance with International Conventions, particularly the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions;
- 13.2.3. determine whether management has considered legal and compliance risks as part of Defence's enterprise risk management plan; and
- 13.2.4. provide advice to the Secretary regarding the issue of Defence's annual Compliance Report.

Refer [F147](#) Senate Estimates 2014 - Finance Portfolio

Agencies reported 12,798 instances of non-compliance with the financial management framework in 2011-12 and 14,027 instances in 2012-13. This aggregate number includes serious issues such as fraud, financial errors and minor technical breaches. The nature of the information collected does not enable an overall figure for fraud to be determined. Further information is contained in the 2012-13 Certificate of Compliance Report to the Parliament.

From memory, from a news article at the time, Defence was the worst culprit with a significant number of instances of non-compliance with the financial management framework in 2011-12 and 2012-13.

13.3. Internal Audit:

- 13.3.1. review the internal audit coverage and Audit Work Program, and ensure that the program has been drawn from Defence's enterprise risk management framework;
- 13.3.2. review all audit report summaries and, where appropriate, associated internal audit reports and provide advice to the Secretary and CDF on significant issues identified in the reports and action taken on issues raised, including identification and dissemination of good practice;
- 13.3.3. endorse the Audit Work Program, as well as any proposed changes, that may from time to time, be requested by the First Assistant Secretary Audit and Fraud Control before final approval by the Secretary and CDF;
- 13.3.4. advise the Secretary on the adequacy of the internal audit resources to carry out its responsibilities including completion of the approved internal Audit Work Program;
- 13.3.5. review the coordination of audit programs conducted by internal and external audit and other review functions;

- 13.3.6. monitor management's implementation of internal audit recommendations;
 - 13.3.7. periodically review the internal audit charter to ensure the appropriate organisational structure, authority, access and reporting arrangements are in place;
 - 13.3.8. periodically review the performance of internal audit, and raise any matters with the Secretary and CDF;
 - 13.3.9. provide advice to the Secretary and CDF on the appointment of the First Assistant Secretary Audit and Fraud Control for the in-house internal audit function, and review the evaluation processes for selecting an appropriate outsourced and/or co-sourced internal auditor; and
 - 13.3.10. meet privately with the First Assistant Secretary Audit and Fraud Control.
14. **Delegations:** review whether appropriate policies and supporting procedures are in place for the management and exercise of delegations.
15. **Business Continuity Management:** satisfy itself that a sound and effective approach has been followed in establishing Defence's business continuity planning arrangements, including whether business continuity and disaster recovery plans have been periodically updated and tested.
16. **Ethical and Lawful Behaviour:** assess whether management has taken steps to embed and maintain a culture that promotes the proper use of Commonwealth resources and is committed to ethical and lawful behaviour.
- Refer ABC News article dated 19 May 2017
[Defence Department accused of dudding Australian businesses](#)
- Accusation of dubious contract tendering processes and whether Australian local jobs are actually being prioritised.
17. **Governance Arrangements:** as determined by the Secretary, periodically review Defence's governance arrangements or elements of the arrangements as determined by the Secretary and CDF and suggest improvements, where appropriate, to the Secretary and CDF.

ENGAGEMENT WITH THE ANAO

Refer 2003 letter re ANAO acceptance BUT NOT Defence (personal experience with Defence)

Refer Senate FADT Reference Committee - Thursday 6 April 2017

- CHAIR: Okay. Can you place on the public record the audit process for Defence?
For a taxpayer out there who has read the Australian National Audit Office report, what is your normal audit process? Is it internal or external?
Is it independent or is it employed by Defence?
- Dr Clarke: It is both. We have an internal audit function and capability, which I manage, and we are also subject to external audit scrutiny through the ANAO.
- CHAIR: Are you saying that the independent audit of your function is by the ANAO?
- Dr Clarke: Our external audit is independent, by definition.
- CHAIR: And internally?
- Dr Clarke: I am independent of line management. I report to the Defence Audit and Risk Committee, which is chaired by an external member and has a majority of external members, and then that reports directly to the secretary.
- CHAIR: What I am trying to get to the bottom of is that in 2009 you agreed to implement some controls and in 2015 or 2016, when the ANAO did its audit, it found that you had not acted on it. Can you please explain that?
- Dr Clarke: I will defer to the CFO on the implementations of controls. They rest in the CFO group.

20. The advisers for the DARC are the Chief Financial Officer and the First Assistant Secretary Audit and Fraud Control

When did either the office of the Chief Financial Officer or the office of the First Assistant Secretary Audit and Fraud Control advise the Defence Audit and Risk Committee that the controls recommended by the ANAO in 2009 had not been implemented.

If not, why not?

What action has been taken to identify the breakdown and rectify the procedure?

What financial cost has been attributed to this negligence?

- CHAIR: You are in charge of audit and there was an agreement in 2009 to implement some controls.
- Dr Clarke: Indeed.
- CHAIR: And you are now deferring to the chief financial officer for the answer of why it was not done.
- Dr Clarke: The audit function is to review and provide assurance about the implementation of controls and the effectiveness of those controls. We do not implement the controls themselves. They rest with line management.
- CHAIR: Thank you. Ms Diamond, are you going to tell us why you did not act on the 2009 report?
- Ms Diamond: In terms of the levels of controls, Defence acknowledges that there were some weaknesses, which was part of the audit report that identified the three recommendations which we have implemented. Since that 2015 audit report which we are talking about, we have turned around and improved our controls framework.
- CHAIR: Sorry, but you are not answering my question. In 2009 you gave assurances that you would put in place some controls. A subsequent audit, many years later, found that you had not acted on that 2009 report. Please tell me why.
- Ms Diamond: We did actually have a controls framework back in 2009. Whether it was sufficiently addressing all the concerns has obviously been a part of the subsequent audit. There has been continuous improvement to our controls framework and we continue to look at those controls even today. I appreciate what you are saying, but it is an evolving and improving framework. If we look at the controls that we have today, they are looking more at analytics and doing far more forensic analysis than what we have done previously. That is part of improving our controls.

- CHAIR: No. My question is very, very specific and it is contained in the independent audit of your activity. It says: The suite of preventative controls used by Defence to control spending on credit cards is not complete and has limited effectiveness: it has not used blocking in any substantial way; access to cash advances for purchasing was not properly authorised until after this audit commenced; a 2009 plan to lower default limits on available credit was not implemented until January 2016; and Defence has issued thousands of credit cards that have never been used.
- Mr Spouse: My question to either of you is: if a risk was identified in 2009, and the plan was not implemented in 2016, who is going to take ownership of that period?
- CHAIR: As you say, and paragraph 9 of the audit report talks about the 2009 plan, the plan to implement lower thresholds was not implemented. As we became aware of that in 2015, we immediately implemented controls to review all credit card limits and lowered them where that was appropriate. But that was the action we took as a result of this report; in the earlier period, I am not aware why the measures from that earlier report were not implemented.
- CHAIR: Do we just erase seven years from the memory? Who was responsible for that?
- Mr Spouse: I am not aware. I was not involved, and Ms Diamond was not involved in the administration of credit cards at that time. What we have done is this: we reacted during the development of the audit report to strengthen the controls, to review the limits and to put in place the sorts of measures we now have — we have annual reviews, and the limit for every single card has been reviewed. That is the action we have taken.
- CHAIR: I would accept your evidence that in 2016 you were taking proactive —
- Mr Spouse: Absolutely.
- CHAIR: I accept that evidence, but my concern is this: in regards to blocking mechanisms, Defence had no categories blocked on its purchasing card. On travel cards, only merchant category 7997 was blocked. That category is: Clubs, Country Clubs, Membership (Athletic, Recreation, Sports), Private Golf Courses, Entertainment. However, 24 travel cards in the last three years still managed to spend \$15,000 within that category. So, you did not use your blocking mechanisms for about seven years.
- Mr Spouse: Which category?
- CHAIR: It is 7997. This is all part of the audit report—I do not suppose it is news to you?
- Mr Spouse: No, I just wanted to get the exact reference.
- CHAIR: So someone managed to spend \$15,000 in a category that was blocked. And if we go on to the purchasing card category 7997, that was not blocked, and over the same period \$3.3 million was spent. These are pretty serious —
- Mr Spouse: In the case of the category that relates to clubs and those sorts of things, what our work has shown us is that the merchant categories, whilst they are a description, can be a fairly loose description of the activities that are covered under those categories. For instance, where it talks about golf clubs, one of the things that we discovered is that using the facilities at golf clubs to run training courses and the like is actually far more cost - effective than using the facilities at maybe hotels and other venues. So, what can appear to be perhaps some sort of recreational activity quite often relates to training and development and those sorts of transactions. We have put a lot of work into the forensics of examining those categories and the expenditure within those categories.
- CHAIR: Okay. So 7997 is: Clubs, Country Clubs, Membership (Athletic, Recreation, Sports), Private Golf Courses, Entertainment.
- Mr Spouse: Yes.
- CHAIR: That was blocked on travel cards, but you still managed to spend \$15,000 in it, and you are saying that it was a training course. I am a golfer; I would prefer to do my training on a golf course as well, but is it an appropriate use of public money? I do not know.
- Mr Spouse: With the expenditure on purchasing cards in that sort of category — and I point out that the merchant category has actually come from the card providers and the banks; they are not categories set by Defence, so we need to work within their framework — we have not found anything that you would put into the fraudulent or suspected category. Where we do, on a monthly basis, refer those to Mr Clarke's team to have a look at.
- CHAIR: My point is that you made an agreement, or at least a risk was identified in 2009. Is your evidence here today is that you did not actually act on that until 2016?
- Mr Spouse: My evidence is that since I have been involved, and the CFO to my knowledge, my involvement has been in taking action to implement the findings of the 2016 ANAO report.
- CHAIR: So there is evidence there that blocking was not effectively managed?
- Mr Spouse: There are comments in the ANAO report, as you referred to in paragraph 2.9, 2.10 and in some of the footnotes. When we have looked at those transactions, there is a range of expenditure, the vast majority of which — and I would not say 100 per cent because I have not checked every transaction — is perfectly within the guidelines for expenditure on whatever that particular activity was be it a training course, be it some sort of activity. It might be on occasion an approved interservice sport activity.

- The ADF is involved in a whole range of activities that I would probably describe as a bit unusual for either corporate entities or other government departments.
- CHAIR: I am not satisfied with your assurance. I would like to see some evidence of that. Firstly, could you please take on notice how it was possible that \$15,000 was spent when the travel cards did have a blocking code. Secondly, how is it possible that on purchasing cards, which were not locked, you spent \$3.3 million.
- Mr Spouse: We will take that on notice.
- CHAIR: The ANAO report shows that analysis of credit card expenditure has revealed payment of traffic fines. I think everybody sitting at this table here gets a government provided car but I certainly know that when I infringe — and I do not do that — I pay it. How is it possible that Defence is refusing to nominate drivers and is paying fines on a credit card? How is it possible?
- Major Gen. Mulhall: As part of my role, I am head of the Defence fuel supply chain. The issue of traffic infringement notices came up through the ANAO audit with respect to fuel cards. Certainly the fact that a number of drivers could not be identified at the time of the audit was unacceptable. Chief of Defence Force took direct action on that. I am pleased to report we have substantially reduced the incidence of that. I accept and we agreed with the ANAO the fact that Defence was unable to identify drivers at a particular point in time was not good enough. We have taken very firm measures to ensure that we reduce the number of times by which corporate rate is paid in lieu of an individual bearing their responsibilities. I have personally, as part of my role with state and territory consultations, raised this matter directly with state and territory jurisdictions and they have assisted us in this.
- CHAIR: We believe that some \$75,138 was paid on purchasing cards for 119 infringements from 1 July 2012 to 9 November 2015. Have they all been investigated?
- Major Gen. Mulhall: Yes. We have taken it to the extent that we can. In some cases, we have been unable to find who was liable for the bill and therefore the department has paid that liability. However, in the last 12 months, in fact as of today, we are down to 15 outstanding traffic infringement notices — the oldest one is 27 February of this year — and we are actively managing those.
- CHAIR: Perhaps on notice if you could give us an assessment of what has happened with respect to the expenditure of taxpayer funds of \$75,138 on 119 infringements. I would appreciate that.
- Major Gen. Mulhall: Yes, we will take that on notice.
- CHAIR: I appreciate that.
- Senator MOORE: Major General Mulhall, I heard you say that have 15 — I was listening very closely — that are still without an outcome in terms of examination, but the latest one of those was earlier this year. So that has all happened since the audit. Is that right?
- Major Gen. Mulhall: You might appreciate that there is, if you like, a rolling nature of infringements. We have closed all of those leading up until 27 February.
- Senator MOORE: Does that means closed, as in no further action, or closed, as in having found out who did it?
- Major Gen. Mulhall: We have taken it to the extent that we can. I cannot give you 100 per cent assurance that we found every person and every occasion, but, in essence, yes, we have closed —
- Senator MOORE: You have closed action on that. My point is that you have 15 — which is a very small number; I am not even going to begin to think about all the data you have given us on how many you have in the whole service — that have occurred since the audit happened and since the information sharing across the whole service about how important this issue is. That worries me a bit.
- Major Gen. Mulhall: So 15 is the gross number of traffic infringements, and we are in the process of resolving them; 15 is not necessarily our inability to detect. These are simply under management action right now.
- Senator MOORE: Listening to your evidence, I thought that there were 15 since early this year that have not been reconciled.
- Major Gen. Mulhall: My apologies —
- Senator MOORE: I am sorry; I must have misunderstood. Just on that point, the other thing that we talked about previously was that, since the audit, there has been widespread information put out through the whole of the service about the importance, integrity and usage, hasn't there?
- Major Gen. Mulhall: Yes, there has been. The Chief of the Defence Force personally wrote to the service chiefs and drew their attention to this, and there has been concerted effort through each of the services and the other groups to get on top of this.
- Senator MOORE: Thank you. Sorry for my misunderstanding.
- CHAIR: Moving on to the withdrawal of cash, the Australian National Audit Office found that there was no obvious approval or acquittal for amounts ranging from \$6,132 to \$42,384. Given that that \$42,384 would be an outlier, I would imagine, does anybody have an explanation as to how that actually happened? Did someone simply go to a Travelex and withdraw \$42,000 in cash for some travel?

Mr Spouse: Could I get the reference there?
CHAIR: This is in relation to large cash withdrawals, and the amounts ranging from \$6,132 to an amount of \$42,384.
Mr Spouse: There are a couple of points I would make there in relation to cash. Post and during the conduct of the audit, we have, in fact, withdrawn the ability of people to make cash withdrawals on the Defence Purchasing Card. So that, literally, cannot happen anymore. Some of the references to cash actually refer to electronic funds transfers, which, in terms of the banks and the card providers, are treated the same way as cash. There is now a system —
CHAIR: Actually, they are treated differently, because they incur a charge.
Mr Spouse: They do incur a charge —
CHAIR: There was a charge there of some \$18,000 to do a transaction. So please expand.
Mr Spouse: The example that you talk about there is, I think, the example that relates to Exercise Talisman Saber, from memory, where an officer of —
CHAIR: He said he was buying rations and such.

18. In undertaking its role, the DARC will engage with the ANAO, as the external auditor, in relation to the ANAO's financial statement and performance audit coverage. In particular, the DARC will:

- 18.1. review the financial statements and performance audit coverage proposed by the ANAO and provide feedback on the audit services provided;
- 18.2. monitor management's responses to all ANAO financial statement management letters and performance audit reports, including implications to Defence of audit recommendations and guidance arising from cross-portfolio audits and better practice guides, and monitor management's implementation of audit recommendations;
- 18.3. provide advice to the Secretary and CDF on action to be taken on significant issues raised in relevant ANAO reports and better practice guides; and
- 18.4. meet privately with the ANAO at least once per year and as necessary, provide feedback on its cooperation with Defence.

COMPOSITION

19. The DARC membership is:

- Mr Paul Rizzo (Chair – Private Member)
- Mr Alan Beckett (Deputy Chair – Private Member)
- Ms Jennifer Clark (Private Member)
- Associate Secretary (Internal Member) Mr Brendan Sergeant
- Vice Chief of the Defence Force (Internal Member) RearAdm Griggs

20. The advisers for the DARC are the Chief Financial Officer and the First Assistant Secretary Audit and Fraud Control

21. Observers for the DARC are the Australian National Audit Office representatives

Secretariat

31. The Director of Defence Senior Committees will be the DARC Secretary, supported by the Secretariat.