

Chapter 3

Analysis of the bills

3.1 This chapter discuss the key issues raised in submissions and by witnesses in relation to:

- contributions to the nation-building funds;
- specific investment and payment provisions;
- role and independence of the advisory bodies;
- transparency; and
- reporting and accountability.

3.2 In general, there was broad support for the initial principle of the bills, and for the subsequent 'fast-tracking' of the expenditure.¹

Contributions to the nation-building funds

3.3 One of the earliest issues to arise was the extent of contributions to the nation-building funds. In the 2008-09 Budget, the government was expecting substantial ongoing budget surpluses, of the order of \$20 billion. The advent of the global financial crisis, and the concomitant decline in commodity prices and hence company tax and other revenues, has cut these projections to around \$5 billion (Table 1).

Table 1 – Budget surpluses: 2006-07 to 2011-12 (\$ billion)

	Actual	Estimates		Projections		
	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12
2008-09 Budget	17.2	16.8	21.7	19.7	19.0	18.9
Mid Year Economic & Fiscal Outlook			5.4	3.6	2.6	6.7

Sources: *2008-09 Budget*: Budget Overview: Appendix A; and *Mid Year Fiscal and Economic Outlook 2008-09*: Overview.

3.4 Obviously, the smaller projected budget surpluses reduce the scope for future contributions to the proposed nation-building funds. It will mean it would take longer

1 For example, see Universities Australia, *Submission 4*, p. 1.

for the funds to be built up to the levels aspired for in the 2008-09 Budget: namely, \$20 billion in the BAF; \$11 billion in the EIF; and \$10 billion in the HHF.² Given the deterioration in the global economic outlook since the MYEFO forecasts were compiled, the projected surpluses – and the expected returns on the assets in the funds – may now be lower. On the other hand, more decisive responses by overseas countries to their economic difficulties may see the longer term projected surpluses improve.

3.5 This uncertainty about the potential for further contributions to the funds concerned some submitters. Without guaranteed funding, the Association of Australian Medical Research Institutes, representing 37 independent medical research institutes, queried the long-term viability of the HHF.³ Infrastructure Partnerships Australia, a peak national body, similarly commented:

We hope that [the nation-building funds] prove to be long-term investment vehicles, not ones which will fall away after the initial endowment from the 2007-08 Budget surplus. While a fund's investment operations must be responsive and relevant to the prevailing conditions, they must also provide certainty to the infrastructure development market and be ongoing and properly funded into the future.⁴

3.6 ABN Amro strongly supported the expansion of 'public private partnerships' (PPPs), which may be a way of achieving more investment from a smaller government contribution.⁵ A 2007 report undertaken by the University of Melbourne and the Allen Consulting Group claimed these collaborative ventures have a number of benefits for Australia taxpayers, such as:

- demonstrated superior cost efficiency;
- economically and statistically significant cost advantage;
- less time over-run on a value-weighted basis;
- timeliness of completion not adversely by project size; and
- greater transparency due to availability of public data.⁶

3.7 However, to achieve these potential benefits it is necessary to ensure that PPPs are properly structured and overseen. To this end, Infrastructure Australia published a report on *National PPP Guidelines* in October 2008.⁷

2 *Budget Paper No. 2*, Budget Measures 2008-09, Part 2: Expense Measures, pp 184-5.

3 Association of Australian Medical Research Institutes, *Submission 5*, p. 3.

4 Infrastructure Partnerships Australia, *Submission 3*, p. 6.

5 ABN Amro, *Submission 1*, p. 1.

6 Allen Consulting Group and University of Melbourne, 'Performance of PPPs and Traditional Procurement in Australia', 30 November 2007, p. 32.

7 It is available at http://www.infrastructureaustralia.gov.au/files/Overview_3_10_1008.pdf.

3.8 Some commentators have suggested that even the \$41 billion originally envisaged in the Budget as the combined assets of the funds would have little overall impact on Australia's infrastructure needs. There are estimates that around ten times this amount will be needed for public infrastructure over the next decade.⁸ However, there was never any suggestion that the funds should be the *only* source of spending on infrastructure. The intention was to supplement current spending plans, not to replace all spending by the state governments.

3.9 Universities Australia welcomed the additional funding, but submitted that the initial EIF contribution of \$9 billion will cover only urgent infrastructure needs, and that a doubling of the endowment by June 2014 would be a more appropriate funding benchmark.⁹ They also wanted to ensure the funding from the EIF would be truly *additional*:

An explicit mechanism to ensure absence of reduced effort by states and territories as a condition of any EIF funding to TAFE is needed, and could be embedded in the legislation by way of amendment.¹⁰

Specific investment and payment provisions

3.10 As discussed in Chapter 2, the Future Fund Board of Guardians is responsible for investment of the financial assets of the nation-building funds, subject to certain limitations. The Australian National Audit Office told the committee that the definition of 'financial asset' was broad,¹¹ giving rise to considerations not addressed in the Nation-Building Funds Bill 2008.

3.11 A comparison was drawn with the Communications Fund, whose similarly broad definition of 'financial asset' was found to be too significant a departure from the categories of conservative investments authorised by the *Financial Management and Accountability Act 1997*. The *Telecommunications (Consumer Protection and Service Standards) Act 1999* was subsequently amended to return the Communications Fund to investments in low-risk, highly liquid, fixed interest asset portfolios:

This approach closely aligns with the approach adopted for entities investing under the FMA Act and is also more consistent with the policy that that Fund be perpetual in nature.¹²

8 Annabel Hepworth and Emma Connors, 'Push to reform infrastructure rules', *Australian Financial Review*, 13 August 2008. A useful list of the nation's big infrastructure objectives, including their projected costs and completion dates can be found in David Uren, Matthew Franklin et al, 'Surplus faces \$10bn threat', *The Australian*, 2 October 2008.

9 Universities Australia, *Submission 4*, p. 2.

10 Universities Australia, *Submission 4*, p. 2.

11 The definition is detailed in the submission from Australian National Audit Office: *Submission 2*, pp 2-3.

12 Australian National Audit Office, *Submission 2*, p. 2.

3.12 While the Nation-Building Funds Bill 2008 proposes a broad definition of 'financial asset', it also proposes a conservative approach to the use of financial derivatives. Unlike the Communications Fund, the bill prohibits the acquisition of financial derivatives for the purposes of speculation or leverage.¹³ The Australian National Audit Office supported this approach, suggesting that it balances the risk posed by the breadth of 'financial assets'.

3.13 'Financial assets' acquired by the Commonwealth from payments other than grants of assistance are not assets of a nation-building fund. Therefore the provisions of the Nation-Building Funds Bill 2008 and the *Financial Management and Accountability Act 1997* do not apply. In particular, section 39 of that Act which requires the Finance Minister to invest public money in only a limited range of investments. This raises similar risk issues to those described in preceding paragraphs.

3.14 The Australian National Audit Office identified a further issue with such 'financial assets': the relevant portfolio minister will manage the Commonwealth's ownership obligations as well as issues of exposure and risk. However, individual portfolio departments sometimes have difficulty managing risk without 'adequate central agency coordination and a way of sharing knowledge and expertise.'¹⁴ It was suggested that the Nation-Building Funds Bill 2008 should further address applicable governance and investment-management parameters.

3.15 The Australian National Audit Office also noted that the breadth of 'financial assets' permissible under the Nation-Building Funds Bill 2008 places 'added emphasis on the Investment Mandate'. A broader range of instruments adds more risk than the conservative investments allowed under the *Financial Management and Accountability Act 1997*, while allowing for the possibility of higher returns:

There is a balance to be struck there...It is important to know that the expectations of that are set out very clearly in the investment mandate because, if the desire is for a very capital-secure highly liquid investment, that is where the investment managers should take you and, consequently, you might have a lower return. But the investment mandate that is developed for each of these funds will be a critically important document.¹⁵

3.16 The Australian National Audit Office supported the complex legislative framework, including for the making of payments from the nation-building funds. An officer of the department told the committee that this framework:

...involves ensuring that there [are] appropriate governance arrangements around the decision making and the recommendation from expenditure from the funds, as well as allowing a level of transparency through the financial statements of the various portfolio agencies of the expenditure that

13 Subclauses 42(1), 161(1) and 236(1) of the Nation-Building Funds Bill 2008

14 Australian National Audit Office, *Submission 2*, p. 7.

15 Mr Brian Boyd and Mr Warren Cochrane, ANAO, *Proof Committee Hansard*, Canberra, 25 November 2008, p. 5.

goes through each of those funds and into each of the areas of expenditure. The structure was developed to ensure that there was that level of accountability, governance and transparency and that is why it is a structure with many elements.¹⁶

3.17 The Australian National Audit Office agreed that there were potential benefits in terms of 'separately identifying the amounts being disbursed for different portfolio responsibilities, and the balance of remaining funds.' However, the Office expressed concerns regarding payments from the 12 Special Accounts, including:

- the lack of clarity regarding the criteria to be applied in determining the appropriate Special Account from which particular payments should be drawn; and
- the need for careful management to ensure:
 - each Special Account is administered in accordance with the legislation;
 - transactions made through each Special Account are accurately recorded; and
 - a consistent approach is adopted in making payments of a similar nature.¹⁷

3.18 As of March 2007, there is greater disclosure of the existence of Special Accounts, for example, through a list of accounts in the Budget Papers together with each account, its opening and closing balances, and receipts and payments being reported in the Consolidated Financial Statements.¹⁸

3.19 Some submissions queried whether specific terms are adequately defined. Universities Australia questioned whether 'development' in relation to the EIF encompasses restoration or refurbishment.¹⁹ The Association of Australian Medical Research Institutes similarly asked whether 'research institution' in relation to the EIF includes independent medical research institutes.²⁰

3.20 In the past, the Future Fund and the Higher Education Endowment Fund may have been seen as convenient places to 'park' budget surpluses.²¹ Some observers

16 Ms Katherine Campbell, Department of Finance and Deregulation, *Proof Committee Hansard*, 25 November 2008, p. 16.

17 Australian National Audit Office, *Submission 2*, p. 4.

18 Australian National Audit Office, *Submission 2*, p. 4. Also, see Senate Standing Committee on Finance and Public Administration, *Transparency and accountability of Commonwealth public funding and expenditure*, March 2007

19 Universities Australia, *Submission 4*, p. 2.

20 Association of Australian Medical Research Institutes, *Submission 5*, p. 2.

21 Richard Webb, Coral Dow and Rebecca de Boer, 'Nation-building Funds Bill 2008, *Bills Digest*, No. 67, 28 November 2008, p. 24.

might suggest that the nation-building funds and the COAG Reform Fund will be used for similar purposes. The provisions of the bills suggest that this is not the case, and the transparency of the Special Accounts enable scrutiny of the manner in which funds are credited to and debited from each nation-building fund.

3.21 In relation to the COAG Reform Fund, Treasury explained that it will be used for short-term purposes only:

We certainly do not...anticipate that the COAG Reform Fund would have large ongoing balances or monies to be invested, et cetera, for long periods of time. We anticipate a process where the funding will come into the COAG Reform Fund from the BAF, et cetera, or indeed direct from the budget, and then would flow.²²

Role and independence of the advisory bodies

3.22 The roles of the independent advisory bodies, the EIF Advisory Board, the HHF Advisory Board, and Infrastructure Australia, are described in Chapter 2. Submissions did not comment on how the relevant ministers treat the independent advice, nor did they reflect on the relevant ministers' discretion as to whether a particular proposal is recommended. One submission advocated an expanded role for the independent advisory bodies, wanting them to be more pro-active in 'providing responsible strategic advice toward identifying, anticipating, planning and providing for future infrastructure needs.'²³

3.23 There was more focus on the independence of the advisory bodies, including the development and application of the evaluation criteria. It was noted that the proposed legislation allows for ministers to formulate the BAF, EIF and HHF evaluation criteria.

3.24 As noted in the Bills Digest:

Much will depend on the criteria the bodies use to assess projects, how the bodies interpret the criteria, and how well placed the bodies are to make assessments.²⁴

3.25 The Association of Australian Medical Research Institutes indicated that there are potential applicants who could apply for funding from more than one nation-building fund. It cited the example of independent medical research institutes, which are involved in both education and health research. The Institute suggested that the evaluation criteria should recognise this possibility.²⁵

22 Mr Michael Willcock, Treasury, *Proof Committee Hansard*, 25 November 2008, pp 12-13.

23 Infrastructure Partnerships Australia, *Submission 3*, p. 4.

24 Richard Webb, Coral Dow and Rebecca de Boer, 'Nation-building Funds Bill 2008, *Bills Digest*, No. 67, 28 November 2008, p. 24.

25 Association of Australian Medical Research Institutes, *Submission 5*, p. 2.

3.26 The Association of Australian Medical Research Institutes suggested also that the evaluation criteria should be transparent, and clearly articulated. In relation to the HHF, the Institute described its ideal requirements for the criteria by way of example:

- reference/relevance to Australia's national health priorities;
- potential for impact on health care delivery;
- contribution to improvement of Australians' health and consequent increase in workplace productivity; and
- significance and novelty.²⁶

3.27 The committee asked the Department of Finance and Deregulation whether the proposed framework effectively allows for independence in project evaluation and selection. A representative responded:

...the disallowable nature of the instrument that will detail the evaluation criteria does provide a level of transparency to the parliament on how the projects will be assessed, and the independent bodies who will provide advice, and ministers having regard to that advice, is quite a strong governance model within the current legislation.²⁷

3.28 Infrastructure Partnerships Australia supported this view, unequivocally stating:

...The BAF/Infrastructure Australia, EIF and HHF advisory boards will bring independence and rigour to the project funding and analysis and evaluation by providing arms-length advice and direction to the responsible Minister.²⁸

3.29 However, there were some reservations in relation to Infrastructure Australia, whose task is:

...to have others perform an appraisal role, and obviously in some cases it might be project proponents performing their own appraisal. In that case, Infrastructure Australia's role is more to provide some scrutiny over such an appraisal and to put that through a prioritisation process. From our perspective, that is somewhat different from an independent body appraising individual project proposals from the beginning. We think that raises some challenges.²⁹

26 Association of Australian Medical Research Institutes, *Submission 5*, p. 2.

27 Ms Katherine Campbell, DFR, *Proof Committee Hansard*, 25 November 2008, p. 20.

28 Infrastructure Partnerships Australia, *Submission 3*, p. 4.

29 Mr Brian Boyd, ANAO, *Proof Committee Hansard*, 25 November 2008, p. 6.

Transparency

3.30 One the most important issues raised in submissions and evidence was the level of transparency provided in the Nation-Building Funds Bill, with commentary ranging from specific provisions to general issues.

3.31 The Australian National Audit Office, for example, cited the definition of 'financial assets', which they submitted was not as clearly stated in the bill as in some other legislation. This may make it more difficult for Parliament to determine whether the nation-building funds' assets have been invested in authorised investments.³⁰

3.32 Other submissions focussed on the publication of the evaluation criteria, the requirement for ministerial consideration of the independent advisory boards' advice,³¹ and most especially, the method by which projects are evaluated and selected for funding.

3.33 Infrastructure Partnerships Australia submitted that the nation-building funds must have the greatest transparency possible, subject to commercial-in-confidence, privacy, and intellectual property considerations:

It is of fundamental importance that the investment decisions and priorities of the respective Funds are transparent. If the nation-building funds were to be allocated and invested for reasons outside policy, we believe that support and appetite for much-needed Federal infrastructure investment and policy leadership would be imperilled.³²

3.34 Likewise, the Association of Australian Medical Research Institutes agreed that the 'funding distribution mechanisms' should be transparent, competitive and support the best proposals'. It advocated the creation and implementation of a contestable application process open to all stakeholders, with external expert panels reviewing applications.³³

3.35 In relation to the COAG Reform Fund Bill 2008, Infrastructure Partnerships Australia hoped that the National Partnership agreements would provide 'more scrutable processes than current arrangements', adding:

Rigorous monitoring of the use of NPP grants will be required to ensure that the funding levels and reform incentive payments are properly applied to achieve national policy objectives. Further detail will be required to ensure that the States can approach the determination of reward payment levels and allocations with certainty.³⁴

30 Australian National Audit Office, *Submission 2*, p. 2.

31 For example, Universities Australia, *Submission 4*, p. 1.

32 Infrastructure Partnerships Australia, *Submission 3*, p. 7.

33 Association of Australian Medical Research Institutes, *Submission 5*, p. 2.

34 Infrastructure Partnerships Australia, *Submission 3*, p. 6.

3.36 At the public hearing, the committee explored certain matters not detailed in the COAG Reform Fund Bill 2008, including determination of the National Partnership payments.

3.37 Treasury advised that the quantum of the National Performance payments would be determined by the government, having regard to government priorities and budget circumstances. The Commonwealth would then discuss the project at hand with the state or territory concerned and reach agreement on the nature of the reform and the performance benchmarks to be achieved to qualify for a National Partnership reward payment. The COAG Reform Council will then act as an independent arbiter, reporting to COAG on the satisfaction of each state and territory's performance benchmarks:

The actual payment...is still something that...is to be determined or decided by Commonwealth ministers, but it is with the advice of this independent assessor which obviously is a way of ensuring that the Commonwealth acts with input from an independent agent that is able to provide them with advice on compliance.³⁵

3.38 Treasury added that it would be in the Commonwealth, states and territories' best interests to publish the National Partnership agreements, and there is nothing to suggest that these will be kept secret.

Reporting and accountability

3.39 The legislative framework proposed by the Nation-Building Funds Bill 2008 and the COAG Reform Fund Bill 2008 emphasises transparency and accountability. However, as indicated in preceding paragraphs, there are areas in which the operations of the nation-building funds might be made more transparent, assisting Parliament to determine compliance with the legislative processes, standards, and responsibilities.

3.40 In particular, it is arguable that there is insufficient provision in the bills for directly informing Parliament of some important matters:

- there is no requirement for ministers to report to Parliament which projects have been approved, to supply reasons for decisions, or to report movements in the funds; and
- some legislative instruments are exempt from disallowance (such as authorisations of payments, including for acquisitions of financial assets).

3.41 However, it is not unusual for reasons for decisions to not be published, the Minister's payment authorisations are primarily administrative, and a range of accountability mechanisms do exist outside of the bills.

35 Mr Michael Willcock, Treasury, *Proof Committee Hansard*, 25 November 2008, p. 10.

3.42 The *Future Fund Act 2006* requires the Future Fund Board of Guardians to report annually on its operations, and the performance of the investments under the Board's management. The Nation-Building Funds (Consequential Amendments) Bill 2008 extends this annual reporting requirement to the nation-building funds.

3.43 Under the *Financial Management and Accountability Act 1997*, the Australian National Audit Office can examine the annual accounts of the nation-building funds: an audit is planned in the near future. The ANAO reminded the committee that under the *Auditor-General Act 1997* it also has performance audit powers, enabling it to examine how the nation-building funds are spent and the grants made from each fund.³⁶

The Audit Office operates in a world that is largely post the event but, through reporting to parliament on the results of the audit, we give accountability and transparency to those decisions...during the financial [audit] process, we make sure that all the funds that are going out are being duly authorised and duly accounted for and, from a performance audit process, we tend to look at whether those funds have gone out against the predetermined objectives and criteria that have been set up for each of the programmes or, in this case, the funds.³⁷

3.44 The committee queried whether there was potential for the Australian National Audit Office to be involved earlier in the process. A representative agreed that the Parliament could legislatively provide for such a role, but this would not be in accordance with the practice of most western nations.³⁸

3.45 The annual Budget process is a further example of existing accountability mechanisms where the declaration of annual drawing rights and fiscal appropriations enables the Parliament to scrutinise expenditure from the nation-building funds.

3.46 Infrastructure Partnerships Australia would welcome further detail in regulations:

...on what practical mechanisms, processes and checks and balances are required to be applied for each Fund to ensure responsible, consistent and transparent decision-making and funding allocation to the most critical, needed and worthwhile projects across transport, communications, energy, water, education and health sectors.³⁹

3.47 The committee prefers such important reporting and accountability mechanisms to be incorporated within the bills, but appreciates that the nation-building agenda is an ongoing construct and that not all its details have yet

36 Mr Warren Cochrane, ANAO, *Proof Committee Hansard*, 25 November 2008, p. 3.

37 Mr Warren Cochrane, ANAO, *Proof Committee Hansard*, 25 November 2008, p. 3.

38 Mr Warren Cochrane, ANAO, *Proof Committee Hansard*, 25 November 2008, p. 4.

39 Infrastructure Partnerships Australia, *Submission 3*, p. 7.

been formulated. The evaluation criteria, for example, are not contained within the Nation-Building Funds Bill 2008 because:

...they are being developed over time in consultation with the boards that are being established to provide advice on them.⁴⁰

40 Ms Katherine Campbell, Department of Finance and Deregulation, *Proof Committee Hansard*, 25 November 2008, p. 19.

