

The Parliament of the Commonwealth of Australia

**THE SALE OF
ADI LIMITED**

**REPORT OF THE SENATE FOREIGN AFFAIRS,
DEFENCE AND TRADE
REFERENCES COMMITTEE**

FEBRUARY 2000

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TERMS OF REFERENCE

1. Whether the proposed sale of Australian Defence Industries Limited (ADI) to Transfield Thomson-CSF has been conducted with prudence, discretion, integrity, skill and propriety necessary to:
 - (a) protect the value of ADI and its assets;
 - (b) realise the maximum price for ADI and its assets; and
 - (c) protect Australia's national interest, national security and defence relationships from compromise.

2. That, in considering these terms of reference, the Committee examine and report on the following issues:
 - (a) whether the actions of the Office of Asset Sales and IT Outsourcing, and those of all other parties in the sale process, best served the interest of Australian taxpayers and the broader national interest; and
 - (b) any other issues or questions, reasonably relevant to the terms of reference but not referred to above, which have arisen in the course of the inquiry.

TABLE OF CONTENTS

<i>Membership of the Committee</i>	<i>iii</i>
<i>Terms of Reference</i>	<i>v</i>
<i>Table of Contents</i>	<i>vii</i>
CHAPTER 1	1
Introduction	1
Establishment of Inquiry	1
Conduct of the Inquiry	2
Acknowledgements	2
CHAPTER 2	3
The Sale Process	3
Introduction	3
Background	3
Preparation for Sale of ADI Limited	5
Sale Process	6
The integrity of the sale process	14
The length of the sale process	17
The price & the value	20
ADI staff	23
Superannuation	24
CHAPTER 3	27
The Australian Submarine Corporation and the Sale of ADI	27
Exclusion of the Australian Submarine Corporation (ASC)	27
SECA's interest in the ASC	29
Alleged interest by Electric Boat in the ASC	32

CHAPTER 4	35
Industry issues arising from the ADI Sale	35
Regionalism	35
Foreign Investment in ADI	37
Safeguarding intellectual property	43
Access to global markets	46
Access to technology and research and development	47
CHAPTER 5	51
Structure of the Australian Defence Industry	51
Introduction	51
Industry comments	51
APPENDIX 1	
APPENDIX 2	
APPENDIX 3	

CHAPTER 1

INTRODUCTION

Establishment of Inquiry

1.1 On 25 August 1999, the Senate referred the following matter to the Committee for inquiry and report by 2 December 1999:

1. Whether the proposed sale of Australian Defence Industries Limited (ADI) to Transfield Thomson–CSF has been conducted with prudence, discretion, integrity, skill and propriety necessary to:

- (a) protect the value of ADI and its assets;
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2. That, in considering these terms of reference, the Committee examine and report on the following issues:

- (a) whether the actions of the Office of Asset Sales and IT Outsourcing, and those of all other parties in the sale process, best served the interest of Australian taxpayers and the broader national interest; and
- (b) any other issues or questions, reasonably relevant to the terms of reference but not referred to above, which have arisen in the course of the inquiry.

1.2 The Senate subsequently extended the reporting date to 17 February 2000.

1.3 The purpose of the inquiry was to review the sale process and not to interfere with that process or prevent the finalisation of the sale. In fact, the Committee delayed the start of the hearings until a time it thought the sale would have been concluded. As it turned out, the last stage of the sale took longer than expected and was only finalised as the Committee’s last hearing was taking place.

1.4 The Committee noted that some submissions opposed the privatisation of ADI. As this was going beyond the terms of reference, the Committee could not pursue such an option. However, the Committee did address some of the issues underpinning calls for the retention of government ownership of ADI.

1.5 The Committee makes no comment on the selection of Transfield Thomson–CSF as the new owner of ADI nor on the bid of its rival Tenix. The Committee does, of course, discuss such matters as foreign investment in ADI and Transfield Thomson–

CSF's plans for ADI, particularly for its assets in regional areas, technology transfers and capital investment.

Conduct of the Inquiry

1.6 The Committee advertised the inquiry in the *Australian* calling for written submissions to be lodged with the Committee. It also approached directly key players interested in the sale. A total of 17 written submissions was received. Details of the submissions are listed in Appendix 1.

1.7 After considering the written submissions, the Committee conducted hearings in Sydney on 25 October, in Melbourne on 19 November and in Canberra on 26 October and 29 November 1999. Details of these hearings are contained in Appendix 2.

1.8 The Hansard transcripts of evidence taken at the hearings are located on the Internet at www.aph.gov.au/hansard

Acknowledgements

1.9 The Committee wishes to thank the people and organisations who made written submissions, gave evidence at hearings or contributed in some other way to the inquiry.

CHAPTER 2

THE SALE PROCESS

Introduction

2.1 In this chapter, the Committee provides background information and then outlines the sale process. It also considers some issues relating to that process which arose during the inquiry.

Background

2.2 The Department of Defence's production facilities had evolved to meet defence needs during two world wars and later conflicts in Korea and Vietnam. This left Australia with a fragmented munitions industry comprising seven facilities at seven different sites and a vastly overdeveloped capacity for production.¹

2.3 The process of rationalisation began with the closure of the unprofitable Department of Defence Support in 1984. Since then, a continuing process of restructuring, rationalisation and commercialisation had overseen the closure of two government-owned Defence factories and the sale of the Williamstown Naval Dockyard in Victoria and of the Aircraft Work Shop in South Australia. Two former government-owned aircraft factories at Fisherman's Bend and Avalon were converted into the government-owned enterprise Aerospace Technologies of Australia, which was later privatised.

2.4 On 3 May 1989, Australian Defence Industries Pty Ltd (ADI) was created to take over the former Office of Defence Industries. The change put the Office's assets in the hands of a separate, limited liability company to be run as a commercial venture.² The overall objective was to revitalise the Australian defence industry and make it globally competitive.³

2.5 The corporatisation process, which began before corporatisation occurred in 1989, involved a major rationalisation of government-owned dockyards and factories. The rationalisation of munitions manufacturing capability involved the closure of two munitions factories, Albion Explosives Factory (1986) and the Explosives Factory at Maribyrnong (1993). The capabilities of these factories were moved to the Mulwala Explosives Factory. Associated costs of the closures were in the decontamination,

1 Max T. Hawkins, 'ADI moves to World Competitive Ammunition Manufacture', *Defence Industry and Aerospace Report*, vol. 9, no. 24, December 1990, p. 10.

2 *ADI Annual Report 1991*, p. 1.

3 *Defence Report 1989-90*, Program 2: Defence Development, p. 71.

demolition and preparation of those sites to meet regulatory requirements, preparatory to their redevelopment.⁴

2.6 Within its first year of operation, ADI Managing Director, Mr Ken Harris, announced that ADI would undergo a major restructuring program under which ADI would consolidate the currently fragmented industry by opening a new state-of-the-art ammunition facility at a 'greenfield' site, to be selected according to economic and strategic considerations. Other facilities at Maribyrnong, St Mary's and Footscray would be progressively closed and their sites sold for redevelopment for residential, light industrial or recreational purposes. These sales would in part fund ADI's new plant and the upgrading of the Bendigo factory, which was to become the centre of ADI's heavy engineering work. The Mulwala and Lithgow sites would continue production of explosives and small arms respectively as part of ADI's newly integrated business.⁵ In addition, ADI's profitable naval engineering and clothing divisions, through fulfilling a number of long-term Government contracts, would contribute to ADI's bid for sustainability.

2.7 In late 1992, ADI was given permission to build the new munitions factory at Benalla, Victoria.⁶ ADI considered that the introduction of modern technology and an 80 per cent cut in the labour force would give Australia one of the most efficient plants in the world.⁷ The new factory was opened on 6 August 1996.

2.8 In the mid 1990s, ADI focussed on enhancing its profile and participation in the international defence trade. In response to an increased international interest in ADI's products, the company had opened offices in Kuala Lumpur, Abu Dhabi, and Berlin.⁸

2.9 By 1997, the new munitions business in Benalla, now in full production, was a major contributor to the record profit.⁹ The Minehunter project was another strong contributor, also fuelling local confidence and expertise, with high Australian design and manufactured content.¹⁰

4 *Defence Report 1989–90*, Program 4: Defence Production, p. 85.

5 Hawkins, 'ADI moves to World Competitive Ammunition Manufacture', pp. 10–11.

6 *Australian Defence Report*, 24 June 1999, p. 6.

7 *ADI Annual Report 1991*, p. 6.

8 'ADI Reaches Mid-point in New Corporate Form', p. 5.

9 Company profits were also bolstered by the completion of major contracts for small arms completed at Lithgow and the sale of redeveloped properties at Footscray and Maribyrnong. A side effect of the latter was that ADI withdrew from its environmental decontamination business in Europe, with local work in this area largely completed.

10 80 per cent design and 70 per cent material, 'Year in Review', *ADI Annual Report 1997*, p. 3.

Preparation for Sale of ADI Limited

2.10 The possible sale of ADI, in its entirety or in parts, was considered in 1992 but no proposition acceptable to the Government was reached.¹¹ The matter was on the agenda again in 1995, when the then Minister for Defence announced that, after careful consideration of the question of privatising ADI, the Government had decided that it ‘was not appropriate to do so in the foreseeable future’.¹² Mr Harris told the Committee that whenever the Board of ADI was asked for advice before late 1996, the board replied that the company was not yet ready for sale.¹³ In February 1996, the then Leader of the Opposition, Mr John Howard, gave undertakings that they would not privatise ADI if they won government.¹⁴

2.11 The change of name to ADI Limited in January 1996 was designed to emphasise ADI’s private sector credentials. Mr Harris told the *Business Review Weekly*: ‘We operate as a normal private company under the Companies Act, and the Government happens to be a single share holder’.

2.12 In December 1996, ADI’s Board of Directors told the Government that ADI was ready for privatisation.¹⁵ Having proven that ADI could be viable as a corporate entity, the Board saw privatisation as the means to gain funding for further growth. Mr Harris later explained to ADI employees:

At the core of any debate that might take place about privatisation of the company, is the issue of the shareholder’s willingness to provide the company with capital to fund our future growth. Australian and overseas experience would lead to the conclusion that governments have some difficulty in funding the development of their companies.¹⁶

2.13 The new Government’s conviction was that governments are not appropriate partners for business enterprises.¹⁷ Mr Harris was confident that the commercial success ADI had achieved after corporatisation would attract the necessary investment for growth from the private sector.¹⁸

11 *Australian Defence Report*, 24 June 1999, p. 6.

12 Press Release, Minister of Defence, Senator Robert Ray, 27 June 1995.

13 *Committee Hansard* 19 November 1999, p. 113.

14 *Bendigo Advertiser*, Thursday, 15 February 1996.

15 See Ken Harris, *Committee Hansard* 19 November 1999, p. 113.

16 In the employee newsletter *Pursuit*, March 1997. Quoted in ‘Background to ADI’s Privatisation’, Privatisation News, *ADI Homepage* (21 September 1999).

17 For Harris see ‘ADI Welcomes Announcement’, 17 August 1999, ADI News Releases, *ADI Homepage* (16 September 1999) and for Liberal perspectives the Member for Mcpherson (QLD Liberal Party), Mr Peter White, in response to the Defence Minister’s statement launching ADI, *House Hansard*, 10 May 1989, p. 2348, [in particular, 1; 4–5].

18 ‘Background to ADI’s Privatisation’, Privatisation News, *ADI Homepage* (21 September 1999).

2.14 In the Budget of May 1997, the Government foreshadowed its intention to look into the optimal timing for the sale of ADI, the means of sale and related issues during 1997-98. On 1 July 1997, the Minister for Finance announced that the Government had appointed the firms Baring Brothers Burrows and Co. Limited and Blake Dawson Waldron as business and legal advisers (respectively) to the Office of Asset Sales & IT Outsourcing (OASITO) for the sale.¹⁹

2.15 The sale of ADI was complicated not only by the nature and structure of the company but also by its extensive relationship with the Commonwealth, which included:

- (a) the Commonwealth's role as sole shareholder of ADI;
- (b) the role of the Commonwealth, through ... Defence, as ADI's major customer;
- (c) various contractual arrangements between the Commonwealth and ADI, many of which related to the time of ADI's formation; and
- (d) the Commonwealth's responsibility for defence policy, defence industry policy and matters of national security.²⁰

2.16 OASITO submitted that it gave highest priority to protecting the interests of the Commonwealth at all times.²¹

Sale Process

2.17 The sale process began in July 1997. OASITO described the process as consisting of three phases:

- the scoping study;
- sale preparation; and
- the sale.²²

2.18 OASITO stated that the sale process was designed to take into account the nature of ADI and its relationship to the Commonwealth. Careful work was required to establish an appropriate structure for the sale and to identify areas for restructuring prior to it to reduce risk and to make ADI more attractive for prospective buyers.

19 'ADI Limited—Appointment of Advisers', Media Release, Minister for Finance and Administration the Hon John Fahey, MP, 1 July 1997 35/97. *Defence Acquisition Organisation* Internet site: http://www.dao.defence.gov.au/media/9-12-97_ADI_future.htm (16 September 1999).

20 OASITO submission, p. 8

21 OASITO submission, p. 8.

22 OASITO submission, p. 1.

Strict evaluation criteria were adopted to guide decision-making processes and to ensure the integrity of the sale process.²³

Scoping study phase

2.19 In the scoping study phase, the groundwork was done to establish the terms of the sale. It involved:

- a business analysis;
- vendor due diligence;
- an analysis of Defence policy; and
- a market testing exercise.

Business analysis

2.20 The business analysis involved consultation and site visits to each of ADI's facilities, presentations by ADI management, a review of ADI's financial performance as well as industry reviews and meetings with Defence representatives to gain a full understanding of ADI's business and the environment in which it operated.

Vendor due diligence

2.21 The vendor due diligence enabled the Commonwealth to make decisions about the sale structure, process and possible terms of sale. During this process and the sale phase, over 18,000 documents, which were identified and obtained from ADI and other Commonwealth agencies, were collated and tracked to form the Commonwealth Library. From these documents, a confidential four-volume Information Memorandum was compiled and provided to prospective buyers undertaking their own due diligence. They also had access to the Commonwealth Library through a CD ROM information dissemination system.²⁴

Analysis of Defence policy

2.22 The Government Sales Team analysed and reviewed Defence arrangements with ADI and consulted officers within Defence and other departments 'to identify key strategic and procurement policy issues and priorities'. Key issues and implications for Defence in the sale process were identified, including:

- (i) competition issues potentially arising in various defence industries, in particular the naval shipbuilding and repair sector. Defence agreed that the ACCC was the appropriate body to assess competition implications;

23 OASITO submission, p. 25.

24 OASITO submission, pp. 9–10.

- (ii) ADI's involvement in activities considered to be important to Australia's military strategic interests;
- (iii) ADI's operation or ownership of significant defence-related facilities such as Garden Island, Benalla and Mulwala (to which Defence may require access in emergency circumstances);
- (iv) possible foreign ownership in ADI;
- (v) the protection of classified information including that provided by other countries;
- (vi) security requirements for fulfilling Defence contracts;
- (vii) the need to remove Defence Required Support Capability (DRSC) arrangements at Garden Island, St Mary's and Mulwala;
- (viii) the need to remove a number of arrangements which were no longer appropriate for transmission to the private sector (eg foreign warship indemnity);
- (ix) the need to ensure any capabilities considered essential to Defence's strategic interests were recognised; and
- (x) potential issues for Defence's policy of achieving 'value for money' in all areas of procurement, in particular through arrangements maintaining open and effective competition.²⁵

Market testing exercise

2.23 The Government sales team conducted a market testing survey among defence industry participants in Australia and overseas, and among engineering/construction participants, investors and brokers. The survey revealed a strong preference for removal of defence property interests from the sale. OASITO reported that a number also saw no commercial rationale or market incentive for acquiring a merged ADI/Australian Submarine Corporation.²⁶ However, Dr White of SECA did express a strong interest in SECA buying the ASC in conjunction with ADI. He said that:

We believed that ADI was not in great shape in its current form. It really needed a great deal of work to it to turn it into a great company that we envisaged. We believed that ADI was really too small, as a stand-alone company, to compete in the international arena. Since our consortium of Australian companies was not backed in an equity sense by big overseas players, we believed we needed to bring ADI together with ASC, the Australian Submarine Corporation, in order to have a decent sized

25 OASITO submission, pp. 11–12.

26 OASITO submission, p. 12.

Australian company as the springboard for the internationally sustainable, majority Australian owned company we were envisaging in the long term.²⁷

2.24 The scoping phase was completed by December 1997.

2.25 On 9 December 1997, the Minister for Finance and the Minister for Defence issued a joint media release announcing that ADI Limited would be sold through an open tender trade sale. Expressions of interest were expected to be invited in the first quarter of 1998. The Government stated:

The sale of ADI Limited will represent the final stage of reform of the government-owned elements of the defence industry and is expected to facilitate growth in the defence industry through private capital investment and technology transfer.²⁸

The sale preparation phase

2.26 In this phase, OASITO addressed a wide range of matters identified during the scoping phase where action had to be taken to prepare ADI Limited for a smooth transition from government to private ownership. These were:

- restructuring of the long-term agreement between the ADF and ADI for the supply of munitions from ADI's Benalla facility to become the Strategic Agreement for Munitions Supply (SAMS), to meet Defence's long-term needs and keep an Australian munitions capacity.
- restructuring of the terms of supply of high explosive and propellants from Mulwala, a Commonwealth facility leased to ADI;
- identification and clarification of ADI's intellectual property and establishment of an intellectual property register;
- protection of the Commonwealth's commercial interests in the frigate upgrade and Bushmaster tenders, and separation of the two tenders from the ADI sale process;
- removal of ADI property interests from the sale;
- restructuring and renegotiation of the Garden Island lease;
- environmental assessment of ADI sites;
- development of strategies to identify and resolve as much as possible litigious or potentially litigious matters to which ADI was a party;

27 *Committee Hansard*, 19 November 1999, p. 135.

28 'The Future for ADI Limited and Australian Submarine Corporation Pty Limited', Joint Media Release, Minister for Finance and Administration the Hon John Fahey, MP and Minister for Defence, the Hon Ian McLachlan, AO, MP, 9 December 1997, 83/97, *Defence Acquisition Organisation* Internet site (16 September 1999).

- establishment of a contracts register;
- review of taxation issues;
- restructuring of debt facilities and guarantees;
- removal of indemnity arrangements and substitution of insurance suitable for private ownership;
- development of an occupation, health and safety strategy at ADI sites;
- clarification and amendment of ADI constitutional documents to remove references of Commonwealth ownership;
- identification and monitoring of human resources and industrial relations issues during the sale process;
- identification of competition issues and development of strategies in anticipation of possible contingencies, such as possible action by the ACCC under section 50 of the Trade Practices Act;
- seeking of third party consents to provision of sale information to Commonwealth and prospective buyers;
- analysis of risks arising from vendor due diligence covering terms of sale, warranties, indemnities, insurance, litigation and other arrangements; and
- foreign ownership in relation to structural approvals under the Government foreign investment policy.

The sale phase

2.27 The sale phase was conducted in four stages:

- the establishment of a sale strategy;
- calling for expressions of interest and requests for proposal;
- buyer due diligence; and
- evaluation of proposals received.

Sale strategy

2.28 The sale strategy was established in June 1998 to set a timetable for the process, and to assign roles and responsibilities. It set out the following sale objectives, against which the bids of tenderers would be evaluated:

- (i) to optimise sale proceeds within the context of the Government's other sale objectives;
- (ii) to minimise the Commonwealth's exposure to residual risks and liabilities;

- (iii) to ensure the new owner has the necessary financial capability to complete the sale and meet ADI's current and likely contractual arrangements;
- (iv) to ensure the new owner has the appropriate contract management expertise, capability and commitment to the fulfilment of ADI's current and likely contractual obligations with the Commonwealth;
- (v) to ensure the new owner has the necessary management expertise, defence and/or relevant general industry experience and a long term commitment to operate as a credible and effective participant in the Australian defence industry;
- (vi) to achieve a sale outcome which avoids the retention of any of ADI's businesses by the Commonwealth post sale;
- (vii) to ensure fair and equitable treatment of ADI staff in the Sale Process; and,
- (viii) to achieve a sale outcome which contributed to a competitive, sustainable and efficient Australian defence industry, as well as to regional industry development.²⁹

Expressions of interest

2.29 The calling of expressions of interest did not eventuate as predicted in the first quarter of 1998. On 22 April 1998, the Minister for Finance and Administration announced that expressions of interests would not now be called until June 1998. Defence was in the process of negotiating a new seventeen-year ammunition supply agreement with ADI which would lock any potential buyer into a continuing commitment to local munitions capability. The Government, therefore, wished to delay the sale process until this important agreement was settled.³⁰

2.30 It was also widely speculated that the new munitions contract would increase the estimated value of ADI (unofficially at \$400 million) to potential buyers. Mr Harris fuelled this speculation, saying that the new defence agreement was more 'commercially robust' than the previous one and that he was: 'sure that this outcome will be recognised by those companies currently preparing bids.'³¹

2.31 The expressions of interest and request for proposal phase was aimed at informing prospective buyers about how their offers would be assessed and was

29 OASITO submission, p. 18.

30 'Sale of ADI', Minister for Finance and Administration, the Hon John Fahey, MP, 22 April 1998, 37/97, *ADI Homepage* (21 September 1999).

31 Reported Andrew White, 'Plant Upgrade Lifts ADI Sale Outlook', *Weekend Australian*, 11 July 1998, p. 54.

conducted according to a pre-defined methodology, with the roles and responsibilities of each party being fully defined.³²

2.32 The invitation to register expressions of interest in ADI Limited was advertised in the media on 10 June 1998.³³ Expressions of interest were to be lodged by midday on 9 July 1998.³⁴ One hundred invitations to register an expression of interest were issued.³⁵ On 10 July 1998, the Government announced that the munitions contract had been finalised. It also stated that it had received expressions of interest for ADI which were being assessed, concluding that the 'signing of the ammunition agreement will assist short-listed parties to formulate their formal bids'.³⁶ On 31 July 1998, a press release announced that five consortia had been short-listed. Mr Hutchinson told the Committee that the identities of the five consortia were never disclosed.³⁷

2.33 In August 1998, a request for proposal was issued to the five short-listed prospective buyers. These provided an overview of the sale process, listed requirements for buyers and outlined the evaluation criteria by which offers would be assessed.

2.34 In September 1998, ADI was one of two contenders short-listed for Defence's billion-dollar guided missile frigate upgrade contract which was to be awarded later in the year. The Government was explicit about its expectations: 'Should ADI be selected as the preferred tenderer for the FFG Upgrade Project, the value placed by bidders on the company could be expected to be significantly enhanced.' A further variation to the original sale specifications were that ADI properties at St Mary's, Footscray and Maribyrnong, which were undergoing site redevelopment in a joint venture with Lend Lease, would not be included in the sale.³⁸

2.35 A phased date for receipt of offers was devised to accommodate the letting of the frigate upgrade contract. If ADI was not the preferred tenderer, offers for ADI were to be lodged by 25 February 1999. If it was the preferred tenderer, the closing

32 OASITO submission, p. 19.

33 OASITO submission, p. 19.

34 'Sale of ADI Limited', Joint Media Release, Minister for Finance and Administration the Hon John Fahey, MP and Minister for Defence, the Hon Ian McLachlan, AO, MP, 12 June 1998 55/98 *Defence Acquisition Organisation* Internet site (16 September 1999)

35 OASITO submission, p. 4.

36 'Defence and ADI Sign Ammunition Supply Agreements', Joint Media Release, Minister for Finance and Administration the Hon. John Fahey, MP and Minister for Defence, the Hon Ian McLachlan, AO, MP, 10 July 1998, Canberra, 65/97

37 *Committee Hansard*, 26 October 1999, p. 93.

38 'Sale of ADI Limited', Joint Media Release, Minister for Finance and Administration the Hon John Fahey, MP and Minister for Defence, the Hon Ian McLachlan, AO, MP, 31 July 1998, 72/98 *Defence Acquisition Organisation* Internet site (16 September 1999)

date for offers was deferred to 9 June 1999.³⁹ As it turned out, ADI secured the contract.

Buyer due diligence

2.36 Buyer due diligence began in September 1998.⁴⁰ This involved the supply of information to prospective buyers to ensure that the Commonwealth complied with its obligations of full disclosure prior to the sale. It was a two-way process during which site inspection and access to the Commonwealth Library led to formal question and answer engagements. Draft sale documents were issued to potential buyers in October and November 1998 and their comments on SAMS sought. Mid-term review meetings were held with representatives of the potential buyers in April 1999 to seek their opinions of the Commonwealth's approaches on a number of issues. During the period a number of consortia sought and were granted permission to make changes to their composition.⁴¹

2.37 With each new contract won by ADI, the consortia tendering for the purchase of ADI were required to undertake a fresh round of due diligence processes and site inspections in order to take into account the new contract in their bids. Responding to the rising uncertainty, on 3 May 1999, the Minister for Finance and Administration announced that it was the Government's intention that bids for ADI should be lodged by the end of June 1999 and that the sale should be completed by late Spring.⁴²

Evaluation of bids

2.38 After receipt of bids, they were evaluated against sale objectives. On 17 August 1999, Transfield Thomson-CSF was selected as preferred buyer of the Commonwealths shares in ADI Limited.

Preferred buyer due diligence phase

2.39 In the final part of the sale process, the preferred buyer was given the opportunity to undertake further due diligence and to inspect material withheld during previous due diligence phases. The Commonwealth also negotiated with Transfield Thomson-CSF Investments Pty Ltd to 'resolve all issues outstanding with its Offer'. As a result of these negotiations, agreement was reached between the Commonwealth and the preferred buyer on all major issues. 'This agreement has clarified the areas of uncertainty in the Offer of 30 June 1999 and has removed or revised a significant number of terms and conditions that were considered unacceptable to the

39 OASITO submission, p. 19 and supplementary submission, p. 3.

40 OASITO submission, pp. 21–4.

41 OASITO, supplementary submission, p. 23.

42 Jason Clout, 'ADI Bids to be in Place by June: Fahey', *Australian Financial Review*, 8 May 1999, p. 52.

Commonwealth'.⁴³ For commercial-in-confidence reasons, the terms and conditions in contention were not provided to the Committee.

2.40 At the same time, ADI's property interests were transferred to a new Commonwealth-owned company group, ComLand Limited. Sales documentation was finalised with provision of documents that had previously been available only in draft form. These comprised:

ADI Share Sale Agreement;

1999 Deed of Indemnity;

Intellectual Property and Material Transfer Deed;

Wrap UP Deed;

Record Transfer Deed; and

Environment Deed.⁴⁴

2.41 The ADI Share Sale Agreement was executed on 8 October 1999 subject to a number of conditions. These conditions were satisfied on 1 November 1999.⁴⁵ Details of these conditions were not made available to the Committee for commercial-in-confidence reasons. Final settlement of the transaction occurred on 29 November 1999, at which time Transfield Thomson-CSF Pty Ltd assumed ownership and full operational control of ADI Limited.

The integrity of the sale process

2.42 The terms of reference of the inquiry required the Committee to consider whether the sale of ADI had been conducted with the 'prudence, discretion, integrity, skill and propriety' necessary to:

- a) protect the value of ADI and its assets;
- b) realise the maximum price for ADI and its assets; and
- c) protect Australia's national interest, national security and defence relationships from compromise.

2.43 The terms also required the Committee to examine whether OASITO, its advisers and others engaged in the sale process had best served the interests of Australian taxpayers and the broader national interest.

43 OASITO, supplementary submission, p. 3.

44 OASITO, submission, p.5.

45 OASITO, supplementary submission, p. 5.

2.44 Mr Michael Hutchinson, Chief Executive of OASITO, told the Committee:

We have a high degree of confidence in the probity arrangements we have in place for the sale. We have every reason to believe they have worked as intended and no reason to believe there have been any flaws or failings in the probity process.⁴⁶

2.45 In its submission, OASITO documented the sale process, drawing out relevant details at issue in every sequence.⁴⁷ This approach, while somewhat repetitive, aimed to support OASITO's claim that the sale of ADI Limited was conducted 'with prudence, discretion, integrity, skill and propriety', sufficient to satisfy the terms of reference of this inquiry.

2.46 During the hearings, most witnesses expressed overall satisfaction with the process. In his opening statement, Mr Tony Shepherd, Chief Executive Officer, Project Development, Transfield, said: 'We consider the sale of ADI has been conducted with the utmost prudence, discretion, integrity, skill and propriety'.⁴⁸ Mr Ian Sharp, Managing Director of GEC-Marconi Systems Pty Limited agreed that 'with respect to probity, the process was fine'.⁴⁹ Group Manager-Commercial of Tenix Pty Limited, Mr John Favalaro, told the Committee:

I do not think that we have any objections to the way in which the process was conducted. I would agree that probity was paramount in the government's mind and I think they kept the process very clean. The confidentiality agreements, which they drove over the top of all this, were in our view extreme. They were very demanding. They were, in our view, probably more than was required. But, if nothing else, they drove home the point that probity was absolute.⁵⁰

2.47 The nature and complexity of ADI's business arrangements, its relationship to Government, and the fact that ADI was tendering for major Defence contracts during the sale period made probity and the integrity of the sale process a challenge for OASITO. Conjecture that the Government was seeking to appreciate the value of ADI by awarding it the billion-dollar frigate upgrade and Bushmaster contracts made OASITO's task even more difficult.⁵¹ Mr Hutchinson stated: 'In terms of the sale process, I have to say that it would have been an awful lot easier had those tenders not been in the marketplace during the sale process.'⁵²

46 *Committee Hansard* 26 October 1999, p. 89.

47 OASITO, submission.

48 *Committee Hansard* 25 October 1999, p. 27.

49 Mr Sharp, *Committee Hansard*, 25 October 1999, pp. 9–10.

50 *Committee Hansard* 25 October 1999, p. 60.

51 See 'Five to Contest ADI Sale', Headlines, *Australian Defence Business Review*, 31 July 1998, p. 5.

52 *Committee Hansard* 26 October 1999, p. 101.

2.48 Mr Hutchinson judged that the frigate upgrade was ‘one of the top three complexity factors’ in the sale process, with the other two being management of intellectual property and environment matters.⁵³ While the last two required sensitive handling, for strategic and economic reasons respectively, the need to guarantee separation of the tendering processes for ADI and the frigate upgrade, in particular, drove OASITO to adopt measures in pursuit of probity which were to have wider effects on the process.⁵⁴

2.49 Two steps were taken: the appointment of a special probity monitor and the phasing of the ADI sale process. The probity monitor was engaged to provide a degree of confidence to all parties that there would be no correspondence of information between individuals conducting the ADI sale process and Defence staff evaluating the contract tenders.⁵⁵ In relation to the phasing of the sale process, Mr Hutchinson told the Committee that this would:

allow the Commonwealth’s interest in those tenders to be settled before the Commonwealth’s interest in the sale process was settled, on the grounds that these tenders were far larger in scale than the Commonwealth’s financial interest in the ownership of ADI. Therefore, the Commonwealth’s overall interest was to be maximised by buying the right defence equipment and then selling the contractor rather than selling the contractor on the basis that we had awarded a tender to it or that we might award a tender to it ...⁵⁶

2.50 The Committee heard that OASITO’s concern for probity in the separation of tenders had other consequences for the sale process. ADI’s former Managing Director, Mr Ken Harris, noted that: ‘everybody in the government decision-making team was so nervous about the political consequences of those sort of allegations that they redoubled their efforts to be cautious’.⁵⁷ One effect was the lengthening of the time frame of the sale.

2.51 The Committee received no information that cast any doubt on the integrity of the sale process. It appeared that OASITO and its advisers went to considerable lengths to ensure the integrity and propriety of the sale even though this lengthened the process. These measures included OASITO’s requirement that participants adhere to extensive confidentiality provisions. As far as the Committee could determine, the confidentiality provisions were not breached. It notes, however, comments from some participants that the confidentiality provisions were too onerous.

53 *Committee Hansard* 26 October 1999, pp. 101-02. See also discussion of intellectual property in Chapter 4.

54 *Committee Hansard* 26 October 1999, pp. 100–01.

55 *Committee Hansard* 26 October 1999, p. 100.

56 *Committee Hansard* 26 October 1999, p. 100.

57 *Committee Hansard*, 19 November 1999, p. 121.

The length of the sale process

2.52 While OASITO was commended for its overall handling of the sale, the length of the sale process received comment and expressions of concern from some witnesses. Mr Harris (ADI) commented:

I have got admiration for the Office of Assets Sales...They have handled some large complex privatisation and they have done well. With this one, the time seemed to get out of hand and that really was the issue. The time was, I think, unduly long for a commercial sale such as this.⁵⁸

2.53 Apart from the deliberate phasing of the sale to protect the integrity of the tendering process, the complexity of ADI's businesses was an acknowledged cause of much of this delay. As Mr Shepherd (Transfield) said: 'ADI is a complex business, with 3,000 staff, many contracts and a diverse range of assets and facilities. This complexity contributed to the lengthy sales process'.⁵⁹

2.54 The complexity of the businesses meant that the vendor due diligence process was a long and difficult task. Mr Sharp (GEC-Marconi) said that his organisation had received literally 'boxes and boxes of wonderful data' during the sale process. He took this as being indicative of the Government sale team's determination to inform fully prospective bidders, given that Defence projects entail considerable risk and require extensive due diligence.⁶⁰

2.55 Even so, Mr Sharp did judge the sale process to be inordinately long. He noted that 12 months from concept to reality was normal for a merger or acquisition process, with a data room being set up within months, open for a number of weeks and an offer made within the following two weeks.⁶¹ He thought that part of the reason was that the cumulation and provision of information was not conducted as pragmatically as had been done in other merger processes in which his firm had been engaged.⁶²

2.56 Mr Sharp was not uncritical of the content of the information provided and, in particular, the timing of its provision. He noted that a lot of the information was of an historical nature. Information on ADI's present business position and future prospects was not provided until late in the process.⁶³ Mr Favaloro (Tenix) confirmed that the late release of this important financial information had meant that Tenix had lodged three bids and yet there were 'still hundreds of unanswered questions' about ADI. He

58 *Committee Hansard*, 19 November 1999, p. 118.

59 *Committee Hansard* 25 October 1999, p. 27.

60 *Committee Hansard*, 25 October 1999, pp. 9-10.

61 *Committee Hansard*, 19 November 1999, pp. 7-8.

62 For example, between Marconi Electronic Systems with British Aerospace, or Marconi Sonar with Thomson.

63 *Committee Hansard*, 19 November 1999, p. 2.

thought that the withholding of this information had been the ‘main sticking point’ for all bidders in the process.⁶⁴

2.57 Further, the late provision of this information made the process more expensive for prospective purchasers. Mr Sharp explained that GEC-Marconi had to pay its advisers a retainer fee on fixed rates for the whole sale process, with most of the valuation work having to be done in the last two months. This made the bidding process very expensive, a point reiterated by representatives from SECA, Tenix and Transfield.⁶⁵

2.58 However, Mr Hutchinson (OASITO) replied:

All the bidders received the information in line with the information disclosure plan that we had in place for the sale. It is always the case in a sale process that a bidder will want information that you are not yet prepared to release or that you do not yet have ready before you are ready to give it to them. I would be very surprised if any bidder told you that they got everything they wanted precisely when they wanted it, but we are confident that the information disclosure regime we put in place was appropriate, given our need to not only meet the needs of the bidders but also protect the value of the business from inappropriate disclosure and the post-sale interests of the Commonwealth by ensuring that the information that was disclosed was appropriately verified and appropriately reviewed before release.⁶⁶

2.59 The cost and complexities involved in bidding were similarly dismissed as ‘just a fact of life’. Mr Hutchinson explained that ADI’s business arrangements meant dealing with complexity and volume, and that, therefore, time and money would be spent in reaching the goal.⁶⁷ Overall, the contenders, while expressing some dissatisfaction, agreed with that view.

2.60 For ADI itself, the length of the process caused other problems. Mr Harris said that ADI’s management team was often distracted from running the company’s commercial interests by having to spend a lot of time providing information for due diligence upgrades and inspections with prospective buyers. The morale of ADI’s staff during the period also required continual support.⁶⁸

2.61 Dr White expressed similar sentiments:

64 *Committee Hansard* 25 October 1999, p. 58.

65 SECA’s former Managing Director, Dr John White, put the cost at around \$10 to \$12 million, see *Committee Hansard*, 19 November 1999, p. 142; Mr John Favoloro of Tenix put overall costs of bidding at in excess of \$2.5 million dollars, see *Committee Hansard*, 25 October 1999, p. 57; and see Mr Shepherd of Transfield at *Committee Hansard*, 25 October 1999, p. 37.

66 *Committee Hansard*, 26 October 1999, p. 89.

67 *Committee Hansard*, 26 October 1999, p. 90.

68 *Committee Hansard*, 19 November 1999, p. 117.

I think the process was too long. It made it very expensive and very changeable. ADI continued to deteriorate in its commercial viability. I think the process was started without any real statement of strategically desired outcomes in terms of Australian ownership industry capability.

...

I think any business which is up for sale suffers morale problems and problems in the market because potential customers, suppliers or partners are dealing with a situation of total uncertainty as to whom the future owner will be, what business they will be in, how they will be in it and who is employed.⁶⁹

2.62 Mr Harris also said that the extended sale process meant that necessary restructuring that would have given ADI Limited a stronger combat systems focus had not taken place. He had identified the need for the restructuring in 1997, but it had not been carried out because the sale, at that time, was thought to be imminent.⁷⁰ Even so, he concluded that the proposed restructuring would not have appreciated ADI's market value had it gone through. He explained that companies interested in ADI would have conducted their own evaluation and arrived at their own game plan for the company.⁷¹

2.63 Mr Hutchinson agreed with this view, noting that three serious bidders - SECA, Transfield Thomson-CSF and Tenix - all had very different structures in mind for ADI Limited. He discounted the suggestion, however, that OASITO had in any way discouraged Mr Harris from restructuring ADI at that time.⁷² Mr Hutchinson also partly attributed the length of the sale process to ADI's unpreparedness for sale when the process was started, despite contrary advice from ADI.⁷³

2.64 He explained that issues arising out of ADI's structure and method of operation, legacies of its days under Commonwealth ownership, were 'fairly lengthy and intractable' in resolution. He singled out three areas of particular concern:

Firstly, there was the need to resolve the occupational health and safety and environmental considerations at Mulwala, the explosives operation. Secondly, there was the need to completely redraft and reshape the strategic ammunitions supply contract with the Department of Defence, the cornerstone of the cash flows in the business. Thirdly, there was the need to resolve the indemnity structure that had been put in place on the foundation

69 *Committee Hansard*, 19 November 1999, p. 142.

70 *Committee Hansard*, 19 November 1999, p. 115.

71 *Committee Hansard*, 19 November 1999, p. 115.

72 *Committee Hansard*, 29 November 1999, p. 172.

73 *Committee Hansard*, 29 November 1999, p. 171.

of ADI that needed to be unwound, and unwound through the various Commonwealth contracts.⁷⁴

2.65 In addition to the need to address these matters and the deliberate phasing of the sale to accommodate the letting of tenders for defence contracts, Mr Hutchinson listed one other important factor which lengthened the sale process. This was the need to transfer and document intellectual property, and to allocate intellectual property between ADI and the Commonwealth. This had been a commitment made at the time of the foundation of ADI but which had never been finalised. Mr Hutchinson concluded that these were simply facts of the process, and not the fault of any party.⁷⁵

2.66 In answer to a question whether OASITO kept ADI informed of developments in the sale process, Mr Harris said;

It was an extremely difficult period but it was difficult for them as well. It was a difficult thing for everybody involved in the sale process. They told us as best they could what was happening, but I just do not think they were fully in control of all the events either, because you had another layer involved in it, namely the Department of Defence, and they had a program. they had activities which were influencing the outcome as well. So I think, in some respects, the Office of Asset Sales were caught in a project that turned out to be perhaps a bit larger and more complicated than people expected. Where they did not tell us of deadlines and dates, I think it was because they were not really in a position to be firmly clear about them.⁷⁶

2.67 The Committee acknowledges that it was undoubtedly a very long sale process, which was due to a number of factors. ADI's structure and the complexity of its business operations and OASITO's cautious and thorough approach to the task to ensure the integrity of the process and the protection of the Commonwealth's interests were never conducive to a quick sale. ADI's involvement in two major tenders also contributed to the length of the sale process.

2.68 The length of the sale process made the exercise more expensive for prospective buyers and made it difficult for management of ADI to keep its businesses going and maintain morale of staff. It also increased the Commonwealth's costs by having to keep the Government sale team together throughout the process. However, no-one suggested ways by which this particular sale process might have been shortened to any significant extent.

The price & the value

2.69 Throughout the sale process there was conjecture about the value of ADI and the price likely to be realised from its sale.

74 *Committee Hansard*, 29 November 1999, p. 171–72.

75 *Committee Hansard*, 29 November 1999, p. 172.

76 *Committee Hansard*, 19 November 1999, pp. 116-17.

2.70 The Government sale team determined that it would receive a better price for ADI if it were sold as a whole rather than broken up into several entities. However, ADI's property development interests were excluded from the sale when market testing suggested they lacked coherence with its core engineering businesses.⁷⁷ The sale team also agreed that complications in the ownership of the Australian Submarine Corporation (ASC) would cause problems if it was sold with ADI. The Government therefore decided that the sale of the ASC should be considered at a later time.⁷⁸

2.71 As the Government was unwilling to release official estimates of the value of ADI for fear of jeopardising the sale process, the value and likely sale price were subject to widespread speculation. Media estimates of the possible price for ADI ranged from \$225 million to twice that amount.⁷⁹ It should be noted that when the Office of Defence Production became ADI, it had assets of \$426 million, including the three properties excised from the ADI sale.⁸⁰

2.72 Dr John White told the Committee that SECA had made an unsolicited bid for ADI at book value of \$320 million in 1997, provided that SECA 'could also buy the Australian government's shares in ASC for some sort of book value or agreed value'.⁸¹

2.73 On 2 November 1999, the Ministers for Finance and Administration and Defence announced that the final price for ADI was \$346.78 million.⁸² The final price did not include ADI's development property assets, included in the early valuation, and which Mr Harris estimated to be valued at about \$160 million.⁸³

2.74 However, the value of ADI was not static over the period of the sale process. Mr Hutchinson told the Committee:

The factors that affected the evolving picture of the value of the company as the sale process advanced were principally its trading record, its success in winning new contracts, the resolution of outstanding commercial issues such as litigation within the business and the evolving expectation of future work

77 Mr Michael Hutchinson, *Committee Hansard*, 26 October 1999, p. 90.

78 Announced Joint Media Release, 'The Future Sale of ADI Limited and the Australian Submarine Co-operation Pty Limited', 9 December 1997 83/97.

79 See Mr Michael Hutchinson, OASITO, *Committee Hansard*, 29 November 1999, p. 170.

80 Gary Brown, *Australia's Security: Issues for the New Century*, Australian Defence Studies Centre, March 1994.

81 The bid was based on the proviso that SECA could also purchase the Government's shares in the ASC. Dr John White, *Committee Hansard*, 19 November 1999, p. 140.

82 See 'Sale of ADI Limited', Joint Media Release, 2 November 1999 71/99 and Stephen Spencer, FED: 'ADI Sold for \$346.7 Million', 2 November 1999, Australian General News, Parliamentary News Service.

83 *Committee Hansard*, 19 November 1999, p. 119; Board of Director's estimate of \$162.4 book value quoted in Trevor J. Thomas, 'Thomson Pays Twice for ADI', Advance Copy of *Australian Defence Business Review* Article, vol. 18, no. 17, 26 November 1999.

flow and therefore future cash flows. They are the sorts of factors that, as they changed, the expected value of the company would change.⁸⁴

2.75 Information received by the Committee late in the inquiry reported that, after a year of achievement in 1997, ADI experienced a year of marginal growth in 1998-99.⁸⁵ According to company accounts lodged with the Australian Securities and Investments Commission on 29 October 1999, ADI posted a \$190.6 million loss on a consolidated turnover of \$571.9 million after abnormals and tax were taken into account. ADI's operational profit pre tax in the year ending June 1999 had fallen sharply to \$12.2 million, down from \$37.5 million the previous year. To balance these losses, the Commonwealth had agreed to forgive ADI debts to the extent of \$45.5 million. This meant that ADI now had an asset value of \$163.7 million, less than half Transfield Thomson-CSF's final price.⁸⁶

2.76 Mr Hutchinson confirmed that ADI had been sold for approximately twice net asset value.

2.77 Mr Harris dismissed the idea that ADI's value could be ascertained from its fluctuating balance sheets. He argued that ADI was saleable because of its strong position in the market place, earned by the intellectual and technical skills of its staff, and not because of its material assets.⁸⁷

2.78 These two factors were clearly criteria rated highly by Transfield Thomson-CSF. The Joint Venture stated explicitly in its submission that ownership of ADI Limited constituted a 'major strategic investment opportunity', because it will bridge their aspirations to growth globally and in the region.⁸⁸ Mr Shepherd (Transfield) stated that the Joint Venture saw that the 'real asset value' of the company lay in ADI's staff.⁸⁹

2.79 The combination of the price paid for ADI by Transfield Thomson-CSF and Mr Harris' estimate of the value of ADI's development properties not included in the sale amounted to approximately \$500 million, which was towards the upper end of the speculated value of ADI during the sale process. The Committee received no evidence to suggest that the Commonwealth did not receive due value from the sale of ADI. There was also no criticism during the inquiry to suggest that the sale process used by OASITO and its advisers resulted in a lower price than might otherwise have been achieved. The integrity of the sale process was also not questioned by witnesses.

84 OASITO, *Committee Hansard*, 29 November 1999, p. 171.

85 Trevor J. Thomas, 'Thomson Pays Twice for ADI', *Advance Copy of Australian Defence Business Review* Article, vol. 18, no. 17, 26 November 1999.

86 Thomas, 'Thomson Pays Twice for ADI'.

87 *Committee Hansard*, 19 November 1999, p. 115.

88 Media Release, Transfield Thomson-CSF, Non-ADI News Releases, *ADI Homepage* (16 September 1999)

89 See *Committee Hansard* 25 October 1999, p. 47.

It is not possible for the Committee to establish whether the Commonwealth achieved the best price it could for ADI. However, the Committee does accept that OASITO did the best it could to achieve this goal.

2.80 It should, of course, be noted that price was not the only factor used in the evaluation of bids for ADI. The bids were evaluated against a number of criteria. The Committee was not privy to whether the price offered by Transfield Thomson-CSF was the highest price. The Government accepted the package offered by Transfield Thomson-CSF, which was subject to refinement before finalisation of the sale on 29 November 1999.

ADI staff

2.81 The Committee considered the position of ADI employees during and after the sale of ADI.

Staff Morale

2.82 Mr Shepherd and Mr Harris both commented on the negative effects of the long sale process on the morale of ADI's staff.⁹⁰ However, Mr Hutchinson told the Committee that:

it was explicitly an obligation on ADI management to keep its staff informed of both the development of the sale process - within the bounds of what was able to be said to them - and in respect of its own position. That is something that ADI management undertook to do, and did, during the sale process. It did not need, require or want any help from us in dealing with its own employees.⁹¹

2.83 Mr Harris told the Committee that on his extensive tours of ADI sites during the sale, it was not privatisation itself but the outcomes of privatisation that were of concern to employees. Employees asked, 'who is going to buy the company? What are they going to do? What does it mean for me? What does it mean for my local area?'⁹²

Post-sale conditions of service

2.84 Sale objective VII provided 'to ensure fair and equitable treatment of ADI staff in the sale process'.⁹³ While issues relating to industrial and human relations, such as redundancy, workers compensation and superannuation were reviewed in the scoping study, they did not raise matters that needed 'to be addressed in the sale

90 See Shepherd, *Committee Hansard* 25 October 1999, p. 47; and Harris, *Committee Hansard*, 19 November 1999, p. 118.

91 *Committee Hansard*, 26 October 1999, p. 95.

92 *Committee Hansard*, 19 November 1999, p. 118.

93 OASITO, submission, p. 18.

process - that is, matters that the sale process needs to intervene in as between employees and the company'.⁹⁴

2.85 Mr Hutchinson told the Committee that the Government had determined during the scoping phase that these issues were between ADI's management and its staff. They were not the responsibility of the Commonwealth during or after the sale process.⁹⁵ Asked whether 'there was nothing in the bidding process where you stipulated to the bidders that there was to be no loss of entitlements to the employees as a result of the sale of ADI', Mr Hutchinson said:

No, because the employees remain in a continuing employment relationship with ADI and therefore their future employment prospects are wholly governed by general community applicable industrial relations practices and laws. There is no change of employer and, therefore, there is no call to intervene between the employer and the employee. The employer, ADI Ltd, remains the same body.⁹⁶

Superannuation

2.86 In his submission, Mr Mervyn Smith urged the Committee to investigate any possible disadvantage to ADI's staff holding membership of the Commonwealth superannuation under the process of transferral to private ownership.⁹⁷

2.87 When ADI was corporatised, several hundred employees out of 4,000, who were at lower pay levels, were assessed as being disadvantaged by the move to private superannuation. As ADI was an approved authority under the *Superannuation Act 1976*, these disadvantaged employees were allowed to remain within the Commonwealth Superannuation Scheme (CSS). In mid 1999, ADI engaged consultants, Parker Financial Services, to analyse the effect of the forced change in their superannuation arrangements for the 337 employees still contributing to the CSS. The consultants found that there were 147 CSS members (44%) potentially detrimentally affected by the mandatory termination of their CSS contributory membership as at ADI's sale date (taken as 30 June 1999). They divided the employees into three age groups and calculated their positions at retiring ages of 55, 60 and 65.⁹⁸

2.88 The 36 employees aged 55 or more who had entered the CSS after 1 July 1976, were likely to be in detriment and would not be able to buy their way out. This means they would not have accumulated sufficient CSS and new ADI cash benefits as would have applied had they retired as a member of the CSS at their selected

94 *Committee Hansard*, 26 October 1999, p. 94.

95 *Committee Hansard*, 26 October 1999, pp. 94, 95.

96 *Committee Hansard*, 29 November 1999, p. 176.

97 Mr Mervyn Smith, submission.

98 Letter dated 18 May 1999 from Group General Manager Business Development, ADI, to OASITO, p. 4, attached to submission of Mr Mervyn Smith.

retirement age. ‘Of the remaining 111 potentially affected members, 65 are likely to be worse off at age 55, 48 are likely to be worse off at 60, and only 23 likely to be worse off at 65’.⁹⁹

2.89 ADI sought the approval of OASITO and the Government to allow the remaining 36 employees to stay with the CSS. The Government, however, rejected the proposal. In its reply to ADI of 1 June 1999, OASITO explained:

The policy departments are unable to support ADI’s proposal to establish a ‘virtual CSS’ arrangement and consider that such an arrangement has the potential to compromise the Government’s principles that guide privatisation initiatives from a human resource management policy viewpoint. These are:

- maximising return to the Commonwealth;
- minimising the transfer of Commonwealth employment conditions and any associated higher employment costs to the private operators; and
- maximising the future commercial viability of, and employment flexibilities available to, new operators.¹⁰⁰

2.90 Mr Hutchinson emphasised that ‘there was nothing unique’ in the process adopted by the Commonwealth in regard to ADI.¹⁰¹ It was the same as that followed for every other fully privatised government business enterprise. He explained that after a government entity passes to private ownership, employees are no longer eligible, by law, to be members of the Commonwealth or Public Sector Superannuation Schemes. Their employers are required to put in place alternative superannuation arrangements.¹⁰²

2.91 Mr Hutchinson stated that Commonwealth superannuation arrangements for ADI staff offered ‘no financial disadvantage’ as, although no future benefits would accrue, the accumulated entitlements of employees would be met.¹⁰³

2.92 Mr Hutchinson also told the Committee:

In terms of their future, their position is governed by their relationship with ADI and the relationship that ADI as the new owners establish for their

99 Letter dated 18 May 1999 from Group General Manager Business Development, ADI, to OASITO, p. 4, attached to submission of Mr Mervyn Smith.

100 Letter dated 1 June 1999 from Senior Director, OASITO, to Group General Manager Business Development, ADI, attached to submission of Mr Mervyn Smith.

101 *Committee Hansard*, 26 October 1999, p. 94.

102 *Committee Hansard*, 26 October 1999, p. 94. Later, Mr Hutchinson explained that these conditions apply once Commonwealth equity falls below 50 per cent. See *Committee Hansard*, 29 November 1999, p. 175.

103 *Committee Hansard*, 26 October 1999, pp. 94–95.

industrial relations and staff management arrangements. If ADI were to offer these employees an Australian workplace agreement, then that arrangement would have to pass the no disadvantage test.

As I understand it, the employer would advocate it. That no disadvantage test would then look at the arrangements that are on now and the arrangements that are offered to them and say, 'As a whole, do these arrangements pass the no disadvantage test?' It would not just be line by line, nor is the superannuation, the leave, and the pay the same, but as a whole the new deal is no disadvantage. That is what we had expected and expect to see happen because of the application of industrial relations law and practices generally.¹⁰⁴

2.93 On 4 January 2000, OASITO provided further written advice to the Committee on options available to ADI's CSS members. This information is contained in Appendix 3.

2.94 It is clear that ADI's CSS members were required to leave the CSS when ADI was sold to Transfield Thomson-CSF. It is also clear that the Government will not make any special arrangements for those CSS members disadvantaged by the forced change in their superannuation arrangements. The former Managing Director of ADI, Mr Harris, best summed up the position when he said, 'I do believe in any situation like this that if individuals are disadvantaged then it is the responsibility of the people running it to redress that disadvantage. I have always felt that.'¹⁰⁵

2.95 The Committee believes that there is an issue of equity to be addressed in this matter. As pointed out in evidence, if employees of ADI were to be offered workplace agreements, the no disadvantage rule would apply to their overall terms and conditions of service. In light of the evidence given by Mr Hutchinson and Mr Harris, referred to above, the matter now rests in the hands of the new ADI management to ensure that those former CSS members are not disadvantaged overall, even if their superannuation arrangements are less beneficial than they were before the sale of ADI.

104 *Committee Hansard*, 29 November 1999, p. 176.

105 *Committee Hansard*, 19 November 1999, p. 130.

CHAPTER 3

THE AUSTRALIAN SUBMARINE CORPORATION AND THE SALE OF ADI

Exclusion of the Australian Submarine Corporation (ASC)

3.1 The decision not to offer the ASC for sale with ADI Limited was raised in the inquiry. As noted above, OASITO had determined early in the sale process that it would not be advantageous to sell ASC with ADI. Accordingly, when the proposed sale of ADI was announced on 12 December 1997, the Government stated that it would defer, until the second half of 1998, consideration of the Commonwealth's shareholding in the ASC.¹ The decision was based on a number of factors.

3.2 The ASC had been established to develop and construct, as a prime contractor, six Collins class submarines for the Australian Navy. Kockums Pacific (a subsidiary of the Swedish Celsius group) held 49 per cent interest in the company while the Commonwealth, through the Australian Industry Development Corporation (AIDC), owned 48.45 per cent. The remaining 2.55 per cent was held by RCI (a subsidiary of James Hardie Industries Limited).² The shareholder arrangements were an important consideration in the Commonwealth's belief that inclusion of the ASC in the ADI sale would both lengthen the sale process and detract from ADI's saleability.

3.3 OASITO submitted that market research on the preferred model for sale of ADI and the ASC conducted during the scoping phase had revealed that: 'There was no commercial rationale or market interest in acquiring a merged ADI/Australian Submarine Corporation'.³ Mr Harris said that ADI had assessed the feasibility of acquiring the Government's equity in the ASC, and had judged that most of the profit in the company had already been taken up by investors, leaving 'a huge amount of risk'.⁴

3.4 Even before the ADI sale process began, the Collins class submarine was experiencing serious problems. The submarine project was eventually subject to an inquiry, the report of which (June 1999) confirmed serious design flaws requiring costly rectification.⁵ Debate about the submarine project had shadowed the sale

1 Joint Media Release, 'The Future Sale of ADI Limited and the Australian Submarine Co-operation Pty Limited', 9 December 1997, 83/97.

2 'The Future for ADI Limited and Australian Submarine Corporation Pty Limited', Joint Media Release, December 1997 83/97, *Defence Acquisition Organisation* Internet site (16 September 1999).

3 OASITO, submission, p. 12.

4 *Committee Hansard*, 19 November 1999, pp. 120.

5 See Report to the Minister for Defence on the Collins Class Submarine and Related Matters: Summary and Recommendations, attachment Media Statement, the Hon. John Moore, MP, Minister for Defence, 'Reform of the Defence Acquisition', 1 July 1999.

process, contributing to the Commonwealth's decision not to complicate the sale of ADI by including ASC.⁶

3.5 The Committee sought information about any approaches made to OASITO to include the ASC in the tender. Mr Hutchinson told the Committee that no unsolicited bids had been made for the ASC. This was in contradiction to newspaper reports suggesting that major tenderers Tenix Pty Limited and Transfield Thomson-CSF had both done so. Mr Hutchinson told the Committee that interested consortia did consider possible options for the ASC in their bids but none suggested that they would improve their bids for a joint sale, and nothing so formal as an 'unsolicited bid' had been received.⁷

3.6 The Committee noted Mr Hutchinson's reply that no bids had been received for the ASC. It then sought to establish whether there had been any unsolicited expressions of interest in the ASC. Mr Hutchinson said that an unsolicited expression of interest had been received during the expressions of interest phase, but the Government judged that the party was not sufficiently informed about the risks entailed in their bid at that point. The bid from that party was, therefore, not taken forward.⁸ Mr Ian King, Director of Baring Brothers Burrows, clarified this, saying: 'during the expression of interest phase you cannot stop unsolicited requests to buy all sorts of assets. We had quite strange requests to buy ADI from all sources and that includes ASC...our role was to assess whether there was any serious interest in it, and I think the answer was no'.⁹

3.7 Tenix confirmed that it did not make an unsolicited bid for the ASC.¹⁰

3.8 Transfield Thomson-CSF told the Committee that it had included an unpriced offer for the ASC in their proposal to buy ADI, but this was subject to certain conditions. These related to the need to sort out the current contractual issues surrounding the Collins project and to clarify the pre-emptive rights that the Swedish shareholder Kockums has over the Commonwealth's shareholding. The final proviso was that Transfield Thomson-CSF would only be interested in the ASC if it could obtain fifty per cent ownership.¹¹ Mr Shepherd regarded the Commonwealth's minority ownership in ASC as a problem. He said that ASC's inclusion in the ADI sale would have lengthened the process and made it more complicated.¹²

6 See for example, President Mr Lars Joseffson of Celsius, owner of ASC shareholder Kockums defence of the Collins submarine on 20 November 1998.

7 *Committee Hansard*, 26 October 1999, p. 96–97.

8 *Committee Hansard*, 26 October 1999, pp. 91–92.

9 *Committee Hansard*, 26 October 1999, pp. 103–04.

10 *Committee Hansard*, 25 October 1999, p. 66

11 *Committee Hansard*, 25 October 1999, p. 47.

12 *Committee Hansard*, 25 October 1999, p. 47.

SECA's interest in the ASC

3.9 The Committee was told that Systems Engineering Consortium of Australia (SECA) expressed an interest in acquiring the ASC along with ADI, although it did not ultimately make a bid for ADI. The Chairman of SECA, Dr John White, had previously put together Australian Marine Engineering Consortium, which purchased the Williamstown naval dockyards in 1987. The dockyards were subsequently bought by Transfield, which restructured them into a profitable enterprise.¹³

3.10 SECA's vision for ADI, based on the Williamstown model, was for it to become 'a premier technology company', supported by a strong Australian SME network.¹⁴ SECA had recruited Celsius, the Swedish parent company to Kockums and co-owner of the ASC, into the consortium with the intention of integrating shipbuilding interests into ADI, so creating a consolidated and predominantly Australian-owned defence industry.¹⁵

3.11 Dr White elaborated on his vision for a combined ADI and ASC, saying that the Australian defence industry needed consolidation so as to compete in the international arena. SECA had secured the support of Pratt's Visy industry group (30 per cent equity stake), the Australian National Bank (20 per cent equity) and incorporated Celsius on the clear understanding that they would ultimately consolidate their 49 per cent share in the ASC with ADI in majority Australian ownership.¹⁶

3.12 Mr Hutchinson acknowledged that the partnership with Celsius singled out SECA among other contenders in its desire to acquire the ASC:

Whereas the other bidding parties had expressed general interest in being involved or consulted or accommodated in whatever the Commonwealth in the future decided to do in respect of the ASC shareholding, of those who were on the list after the expressions of interest stage SECA was the most aggressive in pursuing and indicating a linkage to its interests in ASC.¹⁷

3.13 In early November 1997, Dr White had expressed his hopes that ADI and the ASC would be offered for sale together saying:

The Federal Government's sale of ADI and its shares in the ASC is a unique opportunity to create a strategically important 'smart' Australian company that can work across defence and civilian markets.¹⁸

13 *Committee Hansard*, 19 November 1999, p. 134.

14 Philip Hopkins, 'Transfield Project Seen as Model', *Age*, 17 August 1998, p. B4.

15 *Committee Hansard*, 19 November 1999, p. 136.

16 This totalled 80 per cent. The remaining 20 per cent would be filled by the 'most appropriate Australian company' with the Clough Group of Perth keenly interested. See *Committee Hansard*, 19 November 1999, p. 136.

17 *Committee Hansard*, 29 November 1999, p. 158.

18 Reported in Michael Gordon, 'When the Boat Doesn't Come In', *Age*, 26 June 1999, p. 4.

3.14 Dr White told the Committee that, in 1997, prior to ADI coming on the market, SECA had offered an unsolicited bid for ADI, at a book value of \$320 million, on the condition that it could purchase the Government's shares for the ASC at book value in return.¹⁹ Dr White stated that, after the Government announced its intention to sell ASC and ADI separately, SECA made a commercial decision to approach Celsius.²⁰

3.15 The viability of the SECA bid therefore hinged on the continued commitment on the part of the Celsius group. The basis of the agreement was that, having secured ADI, the consortium would work to consolidate the ASC into it.²¹ However, evidence revealed that the arrangement between the two was predicated on agreements being made with the Commonwealth that Dr White had hoped to secure prior to bidding.

3.16 The Committee sought to clarify these agreements. Mr Hutchinson explained that there were two aspects to SECA's request, made on 30 March 1999. The first was a standard request to vary the membership of the consortium from that declared at the expression of interest phase on 30 July 1998.²² The Committee was told that the first request was never finalised because the related second request, which involved the guaranteeing of certain consents and waivers, was not granted.²³

3.17 SECA proposed that the Commonwealth would guarantee that SECA could become fifty-fifty shareholders in the ASC with the Celsius vehicle, KPAC-Kockums Pacific Australia, building on its 49 percent holding and SECA claiming the AIDC's shares.²⁴ The ultimate aim of the request was that the Commonwealth would support this amalgamation as a new company called the Australian Naval Corporation Pty Ltd. Meanwhile, SECA would be collectively owned by a number of parties, including 30 per cent by Celsius.²⁵

3.18 As OASITO explained, acceptance of this rested on the second aspect which would have required the Commonwealth to agree not to exercise its pre-emptive rights under the Collins class submarine contract and also that the AIDC would agree not to exercise its pre-emptive rights in connection with equity in ASC. On this basis, and despite the fact the agreement would only be activated if SECA were selected as the preferred purchaser, Blake Dawson Waldron advised the Commonwealth not to give consent. Mr Hutchinson told the Committee:

19 *Committee Hansard*, 19 November 1999, p. 140.

20 *Committee Hansard*, 19 November 1999, p. 136.

21 *Committee Hansard*, 19 November 1999, p. 136.

22 *Committee Hansard*, 29 November 1999, pp. 148–49.

23 *Committee Hansard*, 29 November 1999, p. 150.

24 Presumably, the 2 per cent held by another firm would also be obtained by the consortium. *Committee Hansard*, 19 November 1999, p. 138.

25 Mr Michael Hutchinson, OASITO, *Committee Hansard*, 29 November 1999, p. 146.

SECA's application was rejected mainly on legal grounds. It would have been inappropriate to agree in advance of bid receipt and assessment to unsolicited proposals and conditions put to the Commonwealth in the context of the sale. The Commonwealth legal advisers warned that accommodating such an approach at that stage could have threatened the legal basis and integrity of the sale process.²⁶

3.19 He further explained that this was because any decision drawn on the matter would have called into consideration elements of the evaluation criteria set for the sale. These related to industry development and future industry structure. It was considered inappropriate to make judgement on these outside, and especially, in advance of the sale process. In essence, it would mean that the Commonwealth 'would be making bid related decisions for one party on matters that the other parties had not been given the opportunity to have considered'.²⁷ Mr William Conley, Managing Partner of Blake Dawson Waldron, confirmed Mr Hutchinson's summation noting, in particular, that:

there were industry issues which went to the heart of the application by way of the proposal of the SECA consortium which were the very issues, by way of evaluation criteria, all bidders were being asked to address in their bids, which were due on 30 June, and here we were in April, being asked to consider those very issues on behalf of one party.²⁸

3.20 Dr White had expressed concern that OASITO had engineered the rejection of SECA's proposal, independent of prior approvals gained from Defence.²⁹ Mr Hutchinson emphasised that the decision made against the proposal and correspondence about it was issued as a collective Commonwealth response, and not just that of OASITO, despite the latter's obvious responsibility as manager of the sale process.³⁰ OASITO also emphasised that SECA had been told that the decision had been made 'without prejudice' to SECA's proposal being subject to 'proper and constructive assessment' at the appropriate time, that is, at the time of bid assessment.³¹

3.21 Mr Hutchinson told the Committee that it was OASITO's perception at the time of the request for the ex ante arrangements that they were being sought in order to keep the SECA consortium together. On the basis of Dr White's evidence, OASITO drew the conclusion that: 'Celsius had been able to use the absence of the ex ante approvals to exercise an option to leave the consortium prior to bidding'.³² It is

26 *Committee Hansard*, 29 November 1999, p. 146.

27 *Committee Hansard*, 29 November 1999, p. 151.

28 *Committee Hansard*, 29 November 1999, p. 162.

29 *Committee Hansard*, 19 November 1999, p. 137.

30 *Committee Hansard*, 29 November 1999, p. 146.

31 *Committee Hansard*, 29 November 1999, p. 147.

32 *Committee Hansard*, 29 November 1999, p. 147.

reasonable to assume that the failure to gain advance security for future development plans was a catalyst to Celsius' withdrawal from SECA.

3.22 The *Australian Financial Review* of 14 May 1999 reported that, earlier in that month, Celsius had shocked the Swedish stock market by recording losses of \$1.6 million. These resulted from severe cutbacks in defence spending by governments globally, also leading to mergers in the industry. Celsius was said to be keen to consolidate its place in the Europe by the teaming up with other European firms. At the same time, however, Celsius President Lars Joseffson, commenting on the break-up with SECA, said that this was because of 'very different commercial judgements on a very central issue'.³³

3.23 The Committee was satisfied with the explanations received from OASITO and its advisers on SECA's request of 30 March 1999. It was, nevertheless, disappointing that SECA withdrew from the sale process, thereby reducing the number of bidders for ADI and weakening the process. It would have been a more commercially robust process if more of the original short-listed consortia had remained in the sale process and lodged bids for ADI.

Alleged interest by Electric Boat in the ASC

3.24 The Committee sought to establish whether Electric Boat, an American submarine company, had made any approaches to OASITO about the ASC and whether it was being advised by Baring Brother Burrows (or any related company).

3.25 The Committee asked OASITO:

if ING made any representations to OASITO in the early part of the sale, when there were expressions of interest, or later, on behalf of the Electric Boat company, the [American] submarine company.³⁴

3.26 Mr Hutchinson replied:

We know that they did not make any representations to OASITO at all. I cannot recall having heard from ING other than through their Baring Burrows subsidiary here in Australia.³⁵

3.27 The Committee asked 'did any company act on behalf of Electric Boat in making representations or unsolicited bids in respect of the Submarine Corporation?' Mr Hutchinson replied that he had 'no recollection of an unsolicited bid at all'. When prompted about 'any expressions of interest', he replied 'The unsolicited expression of

33 'ADI Battleground for Families at War', *Australian Financial Review*, 14 May 1999, pp. 48, 80.

34 *Committee Hansard*, 29 November 1999, p. 169.

35 *Committee Hansard*, 29 November 1999, p. 169.

interest that arose during the pre expressions of interest stage was not to my knowledge traceable to Electric Boat, to Barings or to ING'.³⁶

3.28 Mr King confirmed that Baring Brothers Burrows is 50 per cent owned by ING, and that the two are effectively the same business entity.³⁷ Asked whether the ING had represented Electric Boat at all, Mr King stated that he 'had no knowledge of that'. Mr Hutchinson also confirmed that the ING had not made any representations to OASITO on behalf of Electric Boat.³⁸

3.29 In subsequent written answers to questions taken on notice at the hearing on 29 November 1999, OASITO advised that 'Electric Boat has never been a client of Baring Brothers Burrows' and 'Preliminary inquiries have been undertaken of the global client data base of ING Barings, which indicate that Electric Boat is also not a client of the group'.³⁹

3.30 On the basis of the explanations received from OASITO and its advisers, the Committee is satisfied that Electric Boat had not approached OASITO directly or indirectly about any interest it might have in the Australian Submarine Corporation. On the same basis, the Committee is satisfied that Electric Boat was not a client of Baring Brothers Burrows or any related entity. Baring Brothers Burrows could not, therefore, have had a conflict of interest by advising both Electric Boat and OASITO.

36 *Committee Hansard*, 29 November 1999, pp. 169–70.

37 *Committee Hansard*, 29 November 1999, p. 169.

38 *Committee Hansard*, 29 November 1999, p. 169.

39 OASITO, letter to Committee dated 4 January 2000.

CHAPTER 4

INDUSTRY ISSUES ARISING FROM THE ADI SALE

Regionalism

4.1 One of the features of ADI is that its factories are widely dispersed, with many located in regional areas. These factories have been important employers in those regions. The prospect of ADI's privatisation, with its inevitable uncertainties about the continuation of ADI's regional facilities, has been a matter of concern for regional authorities.

4.2 The Committee received a number of submissions which focussed on the importance of continuing to operate ADI factories in regional areas, especially in Bendigo and Lithgow. Among these were submissions from the City of Greater Bendigo and the Council of the City of Lithgow. His Worship the Mayor of Bendigo, Councillor Daryl McClure, also gave evidence at a public hearing:

The council's concern in relation to the sale of ADI is particularly in regard to the Bendigo plant, which is the heavy engineering plant – formerly the Bendigo ordnance factory – and which employs a large number of people in Bendigo and has done for a very long period of time.

The council is concerned because it believes that the operation of that facility should continue beyond the time of the sale and, if possible, be improved, upgraded and offer even further employment opportunities within the city – either directly as part of its operations or indirectly through outsourcing various of its requirements within the city.¹

4.3 Councillor McClure drew attention to the recent history of the plant and its effects on Bendigo:

We all have an acute interest in the welfare of this particular plant but I suppose as a community we have been saddened since the mid-1980s as the workload at the plant has declined and the work force has declined. It has dropped towards 50 per cent of where it was. That is a substantial income loss to our economy.²

4.4 Councillor McClure went on to say that although Bendigo's population growth rate is 1.7 per cent per annum, the highest in regional Victoria, it would have been higher if the workforce of the ADI Bendigo plant had not declined. The higher population growth would have allowed better facilities for the people of the area.

1 *Committee Hansard*, 25 October 1999, p. 19.

2 *Committee Hansard*, 25 October 1999, p. 25.

4.5 The General Manager of the Council of the City of Lithgow, in his written submission, said that:

Obviously the Lithgow community looks to the new owners to commit to the development of the manufacturing capacity of the Lithgow facility, and the Council has offered to assist the new owners in a site-rationalisation process.³

4.6 The Committee noted that one of the objectives set out in OASITO's sale strategy was:

(viii) to achieve a sale outcome which contributed to a competitive, sustainable and efficient Australian defence industry, as well as to regional industry development.⁴

4.7 Mr Eaton (OASITO) told the Committee that retention of existing ADI regional facilities 'was not a specific requirement but it was part of the evaluation process. In other words, the bidders' plans for the regional activities of ADI were assessed as part of the evaluation process.' He went on to say:

We had a sale objective which was to achieve a sale outcome that would contribute to a competitive, sustainable and efficient Australian defence industry as well as to regional industry development. So the government wanted to measure the bids against those criteria, but it did not specify in advance that the existing regional structure had to be maintained – and it was prepared to look at restructuring if that was what the bidders proposed.⁵

Under the sale contract, Transfield Thomson-CSF is required to seek the permission of the Australian Government to dispose of ADI assets within 18 months of the date of sale⁶. After that time, Transfield Thomson-CSF may dispose of assets in line with its commercial judgement.

4.8 Transfield Thomson-CSF submitted that it:

plans to retain and develop ADI's regional operations at Bendigo, Benalla, Mulwala, Lithgow, Albury and Newcastle. Both Transfield and Thomson-CSF have demonstrated a strong commitment to regional industry development. With regard to ADI, Transfield has already provided precision engineering work to ADI Bendigo, e.g. telecommunications shelters. Through an extension of this relationship, Transfield can investigate providing additional civil workload to ADI operations in

3 Council of the City of Lithgow, submission.

4 OASITO, submission, p. 18.

5 *Committee Hansard*, 29 November 1999, p. 174.

6 Mr Tony Shepherd, Chief Executive – Project Development of Transfield Pty Ltd, inadvertently referred to this period as three years rather than 18 month when he gave evidence to the Committee on 25 October 1999 (p. 38). He corrected this error in a letter dated 18 November 1999.

regional facilities such as Bendigo and Lithgow, transfer of Transfield's Process Equipment business to Lithgow. Thomson-CSF is an international company and is well aware of their impact on local economies and communities and is actively contributing to job creation programs in areas affected by industry restructuring.

... the Joint Venture intends that the Engineering and Vehicle businesses at Bendigo should continue as going concerns and that work opportunities be found for those opportunities to grow employment for the direct and wider community. Increased investment at Bendigo to accommodate the Bushranger, GE and other contract development opportunities will ensure that ADI Bendigo continues its strong support of the local economy.

The Joint Venture's redevelopment proposal for Mulwala, when implemented, will immediately boost employment during the construction phase and ensure current jobs are secure in the future.

Lithgow will remain operational and ADI Albury's prospects will benefit from access to Thomson-CSF's world leadership in simulation and established presence in prospective international markets.⁷

4.9 Mr Shepherd told the Committee that:

We are going to work hard to endure the viability, as we do with all of the assets of ADI. As with all companies, we are cast adrift on a windy sea, and who knows what is going to happen in three, four or 10 years time? Who knows what is going to happen to Transfield? I cannot make a prediction 10 years out, but our intention as we sit here now is to grow the business and to make it viable and strong, and that is what we will do. We are not in the business of carving up businesses that we have paid a lot of money to acquire. We are driven to make them work.⁸

4.10 As detailed above, the successful tenderer, Transfield Thomson-CSF, has made written commitments to develop ADI's regional facilities. The Committee looks forward to the realisation of those commitments and to the benefits that should flow from them to the regional communities in which they are located. The maintenance and enhancement of employment opportunities and services in regional Australia are matters of concern for the whole Australian community. It is pleasing that a business is seeking to help develop existing facilities in regional areas. The Committee is aware that the future of these facilities is dependent on their commercial viability and that at least Transfield Thomson-CSF is seeking to secure that viability.

Foreign Investment in ADI

4.11 On 17 August 1999, when announcing the preferred buyer of ADI, the Minister for Finance and Administration and the Minister for Defence stated that:

7 Transfield Thomson-CSF, submission, p. 19.

8 *Committee Hansard*, 25 October 1999, p. 38.

The Joint Venture brings together two corporations with complementary skills and experience with the dual benefits of significant Australian involvement and access to world class defence technology.⁹

4.12 They emphasised that Thomson-CSF's bridge to international markets was anchored in three decades of involvement in local subsidiaries and joint venture partnerships in the Australian defence industry.¹⁰

4.13 Despite the Government's support for foreign investment in ADI, concerns over whether foreign ownership of ADI Limited would compromise Australia's national and strategic interests were raised during the sale process.¹¹ Defence sources immediately dismissed these concerns, with reports suggesting that privatisation had now gone too far for any alternative course to be taken.¹²

4.14 The Committee received several submissions expressing concern that the Government should contemplate selling Australia's defence industry and, in particular, into foreign ownership.¹³ These submitters questioned whether a foreign-owned firm could guarantee Australia's national interests would take precedence over the commercial interests of its parent company, or over the foreign policy objectives of its parent country. More pointedly, they asked whether sale to foreign owners would affect Australia's ability to defend itself or to engage in military or peace-making operations where and when the Australian Government judged it necessary.

4.15 In addition, the question was raised whether Thomson-CSF would use its position to lock Australia into purchasing products from overseas which may not be the best for Australian defence purposes. Mr Robert Downey observed that: 'It would seem unlikely that Thomson-CSF will regenerate manufacturing industry in Australia but [will] rely on the concept of purchasing from the cheapest source'.¹⁴ Mr Leonard Fallon also questioned the wisdom of facilitating domination of Australia's defence industry by such an aggressive and efficient partnership which, as a private entity, is not obliged to place its operations and financial performance on the public record.¹⁵

4.16 The Committee sought clarification of the status of French Government ownership and, in particular, to establish what influence the ownership would have on

9 Joint Media Release, 'Sale of ADI Limited—Selection of Preferred Purchaser', 17 August 1999, 42/99, p.1.

10 Joint Media Release, 'Sale of ADI Limited—Selection of Preferred Purchaser', 17 August 1999, 42/99, pp. 1–2.

11 See for example: *Canberra Times*, 18 August 1999; *Australian Financial Review*, 5 August 1999, pp. 1, 10; *Age*, 26 June 1999, p. 4 and *Australian Financial Review*, 25 June 1999, p. 21.

12 FED: 'No Worries about French Interest in ADI', *Australian General News*, 5 August 1999.

13 See for example submissions from: Mr Robert Downey; Ms Pauline Mitchell, Secretary, Campaign for International Cooperation and Disarmament; Mr Bob Cameron MP, State Member for Bendigo West; Dr Mary Maxwell and Ms Karen Kyle, Secretary, Bendigo Trades Hall Council.

14 Mr Robert Downey, submission, p. 1.

15 Mr Leonard Russell Fallon, AFAIM, CPI, FIPEA, submission, p. 7.

dealings of ADI Limited internationally. Mr Anthony Shepherd (Transfield) told the Committee:

The bottom line is that Thomson is a private company. It is run for the benefit of its shareholders, and it is still only a fifty-fifty partner in ADI, so we would not expect any political problems to impact on the continuing operation of ADI. We do not see it as an issue going forward. It is a privately owned company; that's it. What we do is what we do. It is not a functionary of the French Government or an outlet of the French Government in any way, shape or form.¹⁶

4.17 Mr Shepherd also observed that the French Government was in the process of reducing its current ownership from 40 per cent to 34 per cent.¹⁷

4.18 Commenting on previous tensions with France, Mr Gilbert Dangleterre, CEO of Thomson-CSF, said:

Just to add one point, the previous crisis never impacted on the business of Thomson-Marconi Sonar delivering sonar systems for the ANZAC and for the Minehunter. So I believe that we have proven that we have the capability to maintain full production for the Australian market through our activity in Australia. To respond to the political element, France has signed the agreement on non-testing of nuclear weapons, so I do not want to enter into this.¹⁸

4.19 Dispelling concerns that Transfield Thomson–CSF intended to use ADI as a shopfront for its own products, and that Australia's potential to tap into cutting edge United States' technologies would be damaged by ADI's French connections, Mr Shepherd explained:

It is our intention to source the most appropriate technology for Australia's needs from whatever source. To this end we have confirmed with the major US and other corporations already working with ADI that the current relationships with ADI will continue. In addition, we intend to develop a closer relationship between ADI and significant US companies, such as Raytheon, Computer Sciences Corporation and SAIC. It is interesting to note that our partners, Thomson-CSF, are already working with Raytheon to supply NATO the LOC 1 command and control system for air defence.¹⁹

4.20 A related concern investigated by the Committee was whether the sale of ADI to the French-Australian joint venture would affect United States' access to the Captain Cook Dry Dock at Garden Island, Sydney.²⁰ Questioned about ownership of

16 *Committee Hansard*, 25 October 1999, p. 31.

17 *Committee Hansard*, 25 October 1999, p. 31.

18 *Committee Hansard*, 25 October 1999, p. 31.

19 *Committee Hansard*, 25 October 1999, p. 28.

20 See Leonard Fallon, submission, pp. 6–7.

the dock after the sale, OASITO and Defence representatives stated that Defence regarded the dock as a strategic asset and would lease, but not sell, it to ADI's new owners.²¹

4.21 The Committee considered whether Transfield Thomson-CSF had a long-term commitment to maintain a balance between French and Australian ownership. In his opening statement to the Committee, Mr Shepherd emphasised that Thomson-CSF was building on already established connections in the local industry and the region:

Thomson-CSF has maintained a strong presence in Australia and the Asia-Pacific region for some 30 years. For example, Mr Malcor has been managing director of Thomson–Marconi Sonar in Australia, which has been very successful in supplying Australia's defence needs as well as growing a civil export capability.²²

4.22 In response to questioning by the Committee, Mr Shepherd said that any suggestion that Transfield would withdraw from the joint venture was 'a mischievous allegation'. He emphasised:

It is a genuine fifty-fifty arrangement. Transfield has put an enormous effort into the bid and is investing a significant amount of money into ADI and we are transferring some of our top executives into ADI. We are making a very big commitment. Relatively, given the size of the two companies, this is a far bigger commitment from Transfield than it is from Thomson. Our intention is to stay there as a full fifty–fifty partner forever. We have no intention of stepping back, walking away or anything. It would be a huge failure on our part to do so.²³

4.23 However, in terms of official requirements or guarantees made under the sale process, the preferred purchaser was not under obligation to retain ownership, or present ownership arrangements, in the long term. Mr Eaton (OASITO) said that:

The purchaser cannot dispose of or divest of any businesses for a period of 18 months post sale...without the Commonwealth consent. Beyond that the TTJV [Transfield Thomson Joint Venture] has given us, in its business plan, a general picture that it intends to maintain for the long term the current regional activities of ADI, subject, obviously, to commercial pressures that might arise in the future.²⁴

4.24 Mr Shepherd confirmed that, outside of the specified period, the buyers were in fact 'unfettered' in their business decisions about ADI.²⁵ On this note, Mr Malcor

21 *Committee Hansard*, 29 November 1999, p. 165.

22 *Committee Hansard*, 25 October 1999, p. 27.

23 *Committee Hansard*, 25 October 1999, p. 45.

24 *Committee Hansard*, 29 November 1999, p. 174.

25 *Committee Hansard*, 25 October 1999, p. 38.

sought to reassure the Committee that Transfield Thomson-CSF would not sacrifice 'core capability' defence production to commercial interests. He acknowledged the need to maintain capability in areas of production less profitable in peace time and banked on making profit from product diversification:

You need a core that you can expand quickly if you have to multiply your output by three or four. Having paid for this facility, there is a lot of what we call marginal business to be done around it, where you can be fairly competitive in the marketplace. That is what we are looking for.²⁶

4.25 Mr Harris told the Committee that the defence industry, like all other business, was subject to the 'global trend towards opening markets'. He judged that this meant that Australian ownership was not an important issue. Instead, commercial viability in the global market place was important. This, he thought, was why Transfield Thomson-CSF had been selected. They had offered Government the 'best proposition': 'international market access - capital and technology'.²⁷

4.26 From their side, Mr Dangleterre explained the comparative attraction of ADI to foreign industry participants:

The attraction for Thomson-CSF of the Australian defence market is its stability, clarity and predictability. It is true now that, like all the other markets, Australia is embarking on new, imaginative ways to develop the relationship between industry and defence for the long term, through the incentive scheme we call PFI and through long-term partnerships which are certainly necessary and which are on the verge of being implemented in Australia. So there is a parallel to be made between what we are encountering in Europe and in Australia. Australia is ranked as a significant, valuable market for any foreign country, I would say.²⁸

4.27 Transfield Thomson-CSF thus saw that Australia's defence industry had a viable future trading products back to the world.²⁹ Mr Harris explained the global dynamic conditioning this engagement, and what sort of obligations it places on defence industry participants:

what is interesting about this industry - and it is a global thing - is that companies are often competing against each other for some project and collaborating on others. So it is an industry that is strangely characterised by a high level of competition but also a high level of collaboration. We found ourselves - and other companies did - working with company X on one project and competing against one another on another project. That requires

26 *Committee Hansard*, 25 October 1999, p. 40.

27 *Committee Hansard*, 19 November 1999, p. 121-22.

28 *Committee Hansard*, 25 October 1999, p. 41.

29 *Committee Hansard*, 25 October 1999, p. 41.

a high degree of sophistication in managing those commercial relationships...³⁰

4.28 In its submission Transfield Thomson-CSF cites evidence of its expertise in managing its own commercial interests coupled with the strategic interests of its clients. In a section entitled ‘Protecting Australia’s Defence Relationships and National Security’, the submission states:

The Joint Venture will continue the current ADI strategy of teaming with the appropriate partners and suppliers, which have the products and expertise that best meet the needs of ADI’s clients. Consistent with this approach the Joint Venture will maintain procedures to deal with the transfer of technology from overseas companies, including those developing and owning US technologies.³¹

4.29 The submission goes on to state that: ‘Interoperability with the defence systems of Australia’s allies is a task addressed almost daily by Thomson-CSF when working on contracts in the US, Canada, the UK and other NATO countries’. It lists Thomson-CSF’s extensive commercial relationships with European and US firms, including GEC-Marconi and Raytheon, before elaborating its record on meeting Australia’s national security requirements.³² In particular, the submission states:

ADI will meet all of the requirements of the Defence Industrial Security Program (DISP) as set out in the SECMAN 2 and the Agreement between Australia and France, in particular those requirements relating to the protection of Australian and foreign sourced classified material and official information.³³

4.30 At hearings, it became clear that Joint Venture obligations to safeguard Australian interests through ADI Limited fit into Thomson–CSF’s necessary compliance with the international security requirements governing global armament trading. ADI Limited, as an international trader, must seek an ‘end user certificate’ for any export done, so as to safeguard national and international security, and non proliferation requirements. Mr Malcor explained that the process was ‘very thorough and deep’ and required extreme vigilance on the part of participants.³⁴

4.31 Mr Dangleterre (Thomson-CSF) drew attention to Thomson-CSF’s record to show that it can and will meet Australia’s national and security requirements:

I think the track record of Thomson-CSF in Europe has proven that we respect the national rules of each and every country we are established in.

30 *Committee Hansard*, 19 November 1999, p. 124.

31 Transfield Thomson–CSF, submission p. 25.

32 Transfield Thomson–CSF, submission pp. 25–6.

33 Transfield Thomson–CSF, submission pp. 27.

34 *Committee Hansard*, 25 October 1999, p.36.

We have more than 5,000 employees in the UK. We are a defence supplier in the UK, and we apply all of the rules which are incumbent on any UK company to whom we export. In a similar way we do it in Germany, in Spain and in the United States, where we have 1,000 employees. So we follow the national rules to the letter, in full.³⁵

4.32 Although concerns have been voiced about a French company with part French Government ownership investing in 50 per cent of ADI, the company has a long and successful history of working in the Australian defence industry. As a major international contractor, Thomson-CSF is in a position to provide ADI with finance, technology and access to markets overseas. By having only a 50 per cent interest in ADI, it does not have a controlling interest. The Committee has no reason to doubt that the new owners of ADI will proceed in accordance with the plans submitted to OASITO on which their bid was evaluated and won the tender.

Safeguarding intellectual property

4.33 Mr Chris Rodwell of the Australian Industry Group's Defence Council told the Committee that the protection of national security interests, particularly in Western countries, would be subject to increasing stress as a result of mergers amongst major European and US defence companies.³⁶ He also identified problems Australia's Department of Defence has in determining the best capability plans for future development, given that competing private companies advising them are reluctant to volunteer answers in advisory fora for fear of exposing their intellectual property, with subsequent loss of competitive advantage.³⁷

4.34 The underlying issue here, in both these cases, is the availability of intellectual property and the relative security of its exchange in an increasingly global and private sector dominated defence industry. Whether ADI's intellectual property can remain secure under these circumstances was examined by the Committee.

4.35 During the sale process, an emerging concern was that French ownership of ADI would compromise important defence ties with the United States. The issue crystallised after ADI won the frigate upgrade contract. The United States was reported to have reservations about potential intellectual property flow to France via the upgrade project if Transfield Thomson-CSF were selected as preferred buyers of ADI.³⁸ Mr Fallon submitted that:

anecdotal evidence that the US is screening and filtering data and information available to Australia based upon US concern that this data and

35 *Committee Hansard*, 25 October 1999, p. 36.

36 *Committee Hansard*, 26 October 1999, p. 85.

37 *Committee Hansard*, 26 October 1999, p. 85.

38 *Australian Financial Review*, 25 June 1999, p. 21.

information may become available to the French during defence project and contract work as a result of the sale of ADI limited.³⁹

4.36 OASITO representatives judged the management of intellectual property matters as one of the ‘three top complexity factors’ in the sale.⁴⁰ Mr Hutchinson said:

I think it is fair to say that the role of intellectual property in the ADI business and the importance of intellectual property to the ADI business are far greater than in any other Commonwealth business that we have dealt with, particularly third-party intellectual property that is licensed to ADI or licensed for use by ADI. It is integral to their business in a way that intellectual property is not really integral to the operations of many other Commonwealth businesses.⁴¹

4.37 OASITO submitted that intellectual property ownership and related rights was regarded as an important component of the value of ADI. In the scoping study, OASITO identified the need to form an intellectual property register to protect the Commonwealth’s interests and to enhance the commercial attractiveness of ADI to prospective buyers. OASITO listed the following measures which were taken in relation to intellectual property:

- (i) the identification and collation as far as possible of all documented and non-documented IP owned or used by ADI and the establishment of an IP register;
- (ii) the identification and clarification of IP issues arising under the original Deed of Transfer of IP from the Commonwealth to ADI in 1989 (including IP owned by third parties);
- (iii) the identification of IP which the Commonwealth required either revert to it or otherwise be confirmed as the subject of Commonwealth ownership;
- (iv) a review of the adequacy of various IP licences and, where necessary, the development of strategies for the negotiation of amendments to some licences; and
- (v) the development of strategies to address the likely concerns of Prospective Purchasers with various IP issues facing ADI.⁴²

4.38 Mr Hutchinson explained that the need to transfer and document intellectual property, and to allocate intellectual property between ADI and the Commonwealth, was a commitment made at the time of the foundation of ADI but had never been

39 Mr Leonard Russell Fallon, AFAIM, CPI, FIPEA, submission, p. 7.

40 *Committee Hansard*, 26 October 1999, p. 101.

41 *Committee Hansard*, 26 October 1999, p. 98.

42 OASITO, submission, p. 13.

finalised.⁴³ Mr Lewis (OASITO) confirmed that ADI's intellectual property register was more extensive compared with those prepared for other sales handled by OASITO. He stated:

We see it as a very important requirement to get these things absolutely of a high quality in order to protect the Commonwealth's interests post-sale, because any warranties we offer are in relation to those registers. ADI probably had a more extensive IP register than would be usual for a Commonwealth asset sale, but there have been IP registers in other asset sales.⁴⁴

4.39 Transfield Thomson-CSF sought to show that ADI's intellectual property was secure under its stewardship. Thomson-CSF had existing strong ties with the United States in this area and a good record of handling these matters efficiently and with integrity in the international arena.⁴⁵ Mr Shepherd emphasised that consideration of Australia's security interests here was a priority in Transfield Thomson-CSF's bid for ADI, and that measures were devised to ensure ongoing confidence:

We will put in place tried and proven processes which have been approved by the Department of Defence. These processes will ensure the integrity of any Australian classified material. We understand also that our closest ally, the United States, has approved these processes. The board of ADI will have a preponderance of Australian citizens, including myself, who will be suitably cleared from a security viewpoint.⁴⁶

4.40 On 5 August 1999, the *Australian Financial Review* reported that United States Government sources had denied that the sale of ADI to Thomson-CSF might raise technology transfer problems for Washington.⁴⁷ On the announcement of the sale, the Government was reported to be comfortable that Transfield Thomson-CSF had strong joint venture arrangements with the United States, dismissing fears that conflict over intellectual property matters might arise.⁴⁸

4.41 The Committee received no evidence that the sale of ADI to Transfield Thomson-CSF was likely to cause concern in the United States to the detriment of the close co-operation existing between Australia and the United States in relation to transfer of technology or related matters. Thomson-CSF is a respected international prime contractor with existing contracts with American firms. The Committee is satisfied that Thomson-CSF's investment in ADI is not likely to disadvantage Australia.

43 *Committee Hansard*, 29 November 1999, p. 172.

44 *Committee Hansard*, 26 October 1999 p. 98.

45 Transfield Thomson-CSF, submission pp. 27–8.

46 *Committee Hansard*, 25 October 1999, p. 27.

47 Geoffrey Barker, 'French Bid in ADI Sale Exposes Raw Nerves', *Australian Financial Review*, 5 August 1999, p. 10.

48 Lincoln Wright, 'PM Approves ADI Sale', *Canberra Times*, 18 August 1999.

Access to global markets

4.42 One of the main motivations of Government in securing the sale of ADI was to build Australia's defence export industry and to gain greater access to overseas markets. Questioned on 19 November 1999 about ADI's competitiveness prior to sale, former Managing Director Ken Harris stated that ADI had been very competitive in the domestic market, however:

The world marketplace is a different thing altogether. To be competitive in the world marketplace for a company the size of ADI you need stronger global links. I do not really believe a company coming out of Australia with the sort of technology we have here could ever be highly competitive in a global market, dominated as it is by customers who want to buy very complicated systems. Systems are the key to it. The key to ADI's future or any Australian company's future as an international competitor is to tie up with a company that can provide it with the technology it needs to compete internationally.⁴⁹

4.43 The interlinking between access to the global market place, enhanced IP and technical development and more capital investment were integral to the free market model of engagement driving the sale of ADI Limited. Mr Harris judged that Transfield Thomson-CSF had seemed to offer the strongest vehicle for success.⁵⁰ At hearings, Mr Malcor (Thomson-CSF) told the Committee that a strong network is needed to access international markets, given the difficult of doing this from Australia.⁵¹ He explained the joint venture's vision for ADI:

From our point of view, ADI is a company with real growth potential. I have been given the task to grow ADI. Growth is particularly dependent upon three factors: access to technologies; access to international markets; and access to capital. This is what Transfield and Thomson-CSF are providing. While operating as an independent company, ADI will be able to draw on the worldwide resources of the two shareholders. Our vision is to strengthen and revitalise ADI as Australia's premier defence company and to further expand in international and commercial markets.⁵²

4.44 Other industry witnesses in their evidence to the Committee confirmed that Australia's defence industry needs foreign participation to give it the necessary stimulation and contacts to remain viable and to grow.⁵³ Mr Sharp (GEC-Marconi) remarked that the size of the Australian market, and the cyclic nature of contract

49 *Committee Hansard*, 19 November 1999, p. 108.

50 Australian Defence Magazine, October 1999,, pp 68-70.

51 *Committee Hansard*, 25 October 1999, p. 33.

52 *Committee Hansard*, 25 October 1999, p. 28.

53 Dr John White, *Committee Hansard*, 19 November 1999, p.134; Mr John Favaloro, *Committee Hansard*, 25 October 1999, p. 54; Mr Chris Rodwell, *Committee Hansard*, 26 October 1999, p. 72.

letting, meant that there must be outside project work coming in.⁵⁴ He judged that having the right partner was most important. He thought that Thomson-CSF would provide access to markets in Europe, the United States and the Asian region.⁵⁵

4.45 Nevertheless, there was also scepticism about Transfield Thomson-CSF. Some submitters thought the Joint Venture aimed to dominate the Australian industry without any real commitment to generating local engagement. Mr Favalaro, (Tenix Pty Ltd) said that the joint venture was an ‘Australian facade for an overseas contractor who seeks to appear as a local’.⁵⁶ He explained that there is a need to gain ‘critical mass’ in the Australian industry so as to elevate Australian players into a level of significance within the international scene.

4.46 Mr Favalaro said that Tenix Pty Ltd combined with ADI Limited would have elevated the company to a level 30 or 40 on the world scale. This would have created a substantially Australian-owned industry of sufficient mass to attract international technology partners, and to develop skilled teams for platform construction and for systems integration and support.⁵⁷ However, as Mr Harris observed, ‘critical mass’ is what the joint venture already had. As a plus, it also offered established international connections:

It comes back to the point I made before that a country of Australia’s size - and it is critical mass thing - is always going to find it difficult to have its technology sold in a big way against suppliers of the big global systems. What I hope will come out of this sale is that Thomson will do some serious technology transfer into ADI and make ADI a centre of excellence for some of their high technology products and, if so, that will result in an awful lot of R&D being done in Australia in developing products for a global market.⁵⁸

Access to technology and research and development

4.47 Technology transfer underpins the vision for ADI’s future as a successful competitor in the global defence industry, and is understood to be the key to building a vital competitive local industry. Mr Harris explained the importance of technology transfer in the defence industry. He said that Defence budgets now concentrate on systems building and integration rather than on conventional military products - ammunition, weapons and engineered products. ADI had been restructured accordingly but gaining access to high technology remained ‘the biggest hurdle’ for ADI.⁵⁹

54 *Committee Hansard*, 25 October 1999, pp. 4, 7.

55 *Committee Hansard*, 25 October 1999, p. 8.

56 *Committee Hansard*, 25 October 1999, p. 55.

57 Annual listing of world defence contractors as published in the *US Defence News*. See *Committee Hansard*, 25 October 1999, p. 55.

58 *Committee Hansard*, 19 November 1999, p. 123.

59 *Committee Hansard*, 19 November 1999, p. 110.

4.48 Transfield Thomson-CSF supported this judgement. Mr Shepherd said:

The problem with ADI at the moment is that it is endeavouring to move into higher technology, but without access on a permanent basis to sources of this technology and know-how - that is not in question of product, just in question of how to deal with this technology - it is not going to go anywhere. So it was vital to form that international link with somebody or a company that had that expertise. Without that, ADI would have just drifted further and further into lower technology work and would not have had the capacity to participate as a prime contractor in the bigger programs.⁶⁰

4.49 Mr Shepherd further observed that the speed of development globally meant strong international links were essential.⁶¹ Thomson-CSF's credentials as one of the world's most advanced electronic systems suppliers and one of top five defence contractors in world guaranteed that:

The sale to our joint venture will result in the retention and revitalisation of ADI as a competitive, growing, high technology company in both defence and civil business. In this regard, ADI will enter a detailed technical cooperation agreement with Thomson-CSF whereby Thomson guarantees the transfer of valuable technology and know-how. We are committed also to the retention of ADI's regional facilities and have detailed plans to achieve this.⁶²

4.50 Transfield Thomson-CSF has pledged, as a priority, to invest \$40 million in ADI Limited, and in research and development within ADI, over the next five years⁶³ This money will fund an expanded technology base, and bringing 'a base of people' to ADI's facilities. Mr Malcor confirmed that Transfield Thomson-CSF has the necessary capital to inject sufficient research and development money 'to anticipate the extent of the market and to develop new products'.⁶⁴

4.51 Mr Shepherd emphasised that the above financial commitments are set down in Transfield Thomson-CSF's business plan for ADI, which is a part of the sale contract.⁶⁵

4.52 Vice Admiral Walls (Retired), a Director of Thomson-Marconi Sonar, also gave testament to the research and development orientation of Thomson. He said that about 60 per cent of 'Thomson-Marconi Sonar business today in Australia is export

60 *Committee Hansard*, 25 October 1999, p. 32.

61 *Committee Hansard*, 25 October 1999, p. 32.

62 *Committee Hansard*, 25 October 1999, pp. 27-28.

63 *Committee Hansard*, 25 October 1999, p. 34.

64 *Committee Hansard*, 25 October 1999, p. 33.

65 *Committee Hansard*, 25 October 1999, p. 34.

oriented and is directly related to R&D work that has been done in Australia with the Defence Science and Technology Organisation'.⁶⁶

4.53 Mr Harris emphasised the importance of research and development for the future growth and development of ADI:

Buying off the shelf is happening, it always has happened and always will happen, and that is important. But a lot of the products that Australia requires do need to be adapted for Australia's particular strategic and even environmental circumstances. A lot of R&D is directed towards that issue.

The R&D that would be of most interest to me, though, would be the contribution of R&D to the development of new business opportunities overseas. It comes back to the point I made before that a country of Australia's size - and it is critical mass thing - is always going to find it difficult to have its technology sold in a big way against suppliers of the big global systems. What I hope will come out of this sale is that Thomson will do some serious technology transfer into ADI and make ADI a centre of excellence for some of their high technology products and, if so, that will result in an awful lot of R&D being done in Australia in developing products for a global market.⁶⁷

4.54 The Committee raised broader issues relating to increasing research and development in the defence industry during the inquiry. Mr Rodwell (Defence Council) told the Committee:

There is a number of ways you can look at increasing your level of R&D. One is through the tax concession. Following the reduction in the company tax rate to 34 per cent and then to 30 per cent, that 125 per cent is effectively being diluted a little. There is actually a further reduction there. So you can look at increasing the R&D tax concession as a means of increasing research and development. You can look at the CRCs, the cooperative research centres, and defence research and development in that area. A number of CRCs are currently with Defence, and industry interests are being progressed there. So there is the ability there to increase the levels of R&D, and there is the ability, through DSTO, to once again increase the level of R&D.

It is not just a government issue but also an industry issue. The decisions of the defence industry are informed by the organisation. They have to look at the capability it needs over the next 10 years. It is not viable to put in an enormous amount of R&D in an area where there is no interest for Defence, so there is an onus on Defence in the broadest terms to inform the industry

66 *Committee Hansard*, 25 October 1999, p. 34.

67 *Committee Hansard*, 19 November 1999, p. 123.

about its capability decision making. They are the main ways that Defence can look at changing its R&D.⁶⁸

4.55 Mr Shepherd (Transfield) said that taxation concessions for investment in research and development in the defence industry are very important and would affect investment decisions. He also suggested that Defence should encourage the development of specific technologies through direct funding of technology demonstrator programs, which in effect become joint ventures between the private and public sectors, for mutual benefit.⁶⁹

4.56 Mr Favaloro (Tenix) told the Committee that research and development in the Australian defence industry is usually very focussed and is done at the behest of government or as a collaboration between industry and government. He said that taxation concessions for research and development in the defence industry are really government investment in a specific program from which it will ultimately benefit. In that way, they are different from general business research and development taxation concessions, which are provided to help in the development of Australian business.

68 *Committee Hansard*, 26 October 1999, pp. 84-85.

69 *Committee Hansard*, 25 October 1999, p. 34.

CHAPTER 5

STRUCTURE OF THE AUSTRALIAN DEFENCE INDUSTRY

Introduction

5.1 One of the threads that ran through the inquiry was the future structure of the Australian defence industry, including rationalisation of prime contractors and the role of government in shaping the evolving structure. It was a matter that arose out of the inquiry rather than one that was specifically referred to in the terms of reference¹. As a result, comments on this matter were restricted to companies and individuals who had some association with the sale of ADI and who took part in the inquiry. However, the Defence Council of the Australian Industry Group, the relevant industry association, took advantage of the inquiry to speak on this matter for the wider industry.

5.2 The Committee was not in a position to undertake a detailed inquiry into this area. This would have required specific terms of reference and an opportunity given to many more players within the Australian defence industry to participate in the inquiry. Nevertheless, the Committee believes that it should draw to the attention of the Government comments made on this matter during the inquiry. It is in the national interest for the Government to take all appropriate measures to ensure that, through the ongoing rationalisation of the defence industry, Australia continues to have a defence industry that meets our national needs.

5.3 The Australian defence industry now comprises a small number of privately owned prime contractors², small to medium-sized enterprises and small companies providing boutique or specialised services. Much of their defence work is supplied to the ADF or the Department of Defence. According to Mr Sharp (GEC-Marconi), not much is exported given the difficulties of breaking into overseas defence markets in competition with large foreign prime contractors.³

Industry comments

5.4 The Defence Council submitted that:

If the Government and/or the Defence Organisation have a vision for the future structure of the industry it is not being clearly articulated. This causes the industry significant uncertainty in positioning itself for the future. Such a vision could be expected to include:

1 These matters were considered under term of reference 2(b).

2 Although most witnesses said there were about five prime contractors, the Defence Council said there were 27 companies that had submitted bids for prime contracts.

3 *Committee Hansard*, 25 October 1999, p. 1.

- An appraisal of the current trends in industry restructuring around the globe, particularly among major defence powers;
- An assessment on how these trends will affect the Defence portfolio, including a forecast on how major capability decisions and the acquisition process will be affected, and the consequent ramifications for the domestic industry across all major tiers; and
- A broad action plan for detailing the Government's position on how the domestic industry can prosper in the new environment.⁴

5.5 In his evidence to the Committee, Defence Council Policy Adviser, Mr Christopher Rodwell, explained that the Department of Defence has strong links with the defence industry through the publication of the Pink Book (Defence New Major Capital Equipment Proposals 1998-2003) and the Yellow Book (Defence Forward Procurement Plans for Minor Capital Equipment 1999-2004) and 'through various forums, such as the Capability Development Advisory Forum'. However, he went on to say that:

I suppose this is a broader issue than any one forum. The 1998 defence industry strategic policy statement was, in a sense, an outlook for the defence and industry relationship. For the Industry Group Defence Council, the logical step then is to put together a vision for the future structure of the industry. We have looked at the defence-industry relationship; now it is time to move forward and look at what the future industry will look like, because it does affect Defence. The fact is that, if the industry does not rationalise, there is little doubt that we will be seeing more defence spending flowing overseas. Really, it is Defence's interests – and, more broadly, in the government's interests - to see that this vision is put forward to help industry set itself up for the future.⁵

5.6 In June 1998, the Government released its Defence and Industry Strategic Policy Statement. The foreword to the Statement reads:

This strategic defence industry policy will put into place the appropriate framework, in partnership with industry, to ensure the ADF acquires the capabilities we identify as vital, in a nationally efficient way.

5.7 As to whether the Department of Defence took into account the future shape of Australia's defence industry and national security when assessing the bids for ADI, the Head of Industry Procurement Infrastructure, Mr Graham Kearns, told the Committee:

Given that ADI is one of the largest players in the Australian defence industry, clearly what happens in the sales process is going to have some

4 Defence Council of the Australian Industry Group, submission.

5 *Committee Hansard*, 26 October 1999, pp. 74-75.

effect one way or the other on the shape of that industry and on whether that shape would better serve our interests or not. That was one issue that we certainly focused on, and that meant that we looked at the two bids in terms of what that shape of industry would be and to what extent we would prefer either bid from that point of view.⁶

5.8 Mr Ian Sharp, Managing Director of GEC-Marconi Systems Pty Ltd, expressed sentiments similar to those of Mr Rodwell in his evidence to the Committee:

First, Defence needs to sit down and understand what are its long-term strategic demands of industry, then within maybe an industry portfolio understand the benefits that a strong defence industry sector does bring to the Australian economy. Once those are understood, they should work with industry to achieve the outcomes they are looking for. Having worked in the defence industry now for 20 or 25 years, I say that to date such discussions and such a model have not been developed.⁷

5.9 Asked whether he thought there was not enough collaboration between the defence industry and the Department of Defence, Mr Sharp replied:

That is correct. Before you have that collaboration, and maybe it happens in parallel as well, a government of any persuasion needs to understand those benefits which we have just been talking about, develop an industry model and then work with industry for that outcome. Definitely from both the government and the opposition at the moment I have seen a change through the privatisation process, where these things have been thought about maybe for the first time, and I think that needs to continue.⁸

5.10 Mr Bathgate (Tenix) said that the initiatives being taken as a result of the 1998 policy statement will assist planning within the defence industry. He went on to say that Defence is talking to industry about the capabilities they have in mind in the future and seeking input from industry about achieving those capabilities, rather than about talking about particular contracts. He added that 'it is early days as yet; that might be the best and simplest way of putting it'.⁹

5.11 In his opening statement to the Committee, Mr Tony Shepherd, Chief Executive Officer, Project Development, Transfield Thomson-CSF Pacific Holdings, drew attention to the rationalisation already taking place within the Australian defence industry – the BAe acquisition of Siemens Plessey and the upcoming merger with GEC-Marconi, and the Lockheed Martin Tenix joint venture, apart from the Transfield Thomson CSF purchase of ADI. He went on to say that:

6 *Committee Hansard*, 26 October 1999, p. 103.

7 *Committee Hansard*, 25 October 1999, p. 15.

8 *Committee Hansard*, 25 October 1999, p. 15.

9 *Committee Hansard*, 25 October 1999, p. 64.

In examining the Australian defence industry, it is important not to get too carried away by the number of competitors; rather, one should focus on which companies are capable of being prime contractor on major procurements and have access to the appropriate technology. An examination of the industry on this basis shows that we have two, and at best three, competitors in each of the major defence segments of naval, aerospace, land and sea for ISR. A reinvigorated and independent ADI is vital to the retention of a strong local capability and competition, particularly given the small number of companies that are truly prime contractor capable.¹⁰

5.12 The rationalisation that is taking place within the Australian defence industry reflects global rationalisation trends but its evolving structure also reflects Australian Government acquisition policies and practices.

5.13 Mr Favaloro told the Committee:

The government is in an extremely powerful position to influence the shape and the structure of the Australian defence industry by the way that it implements its purchasing decisions. At the present moment, we find it difficult to understand how the procurement policy is being applied. It leaves us with the impression that the policy is being implemented as if there was a policy of competition at any cost. If that is the case, the Williamstown dockyard, which we own and control and use to build naval ships, in the scenario you have described would be ill-placed to cope, because in a \$5 billion program you can build another shipyard - perhaps it would cost you \$100 million or \$150 million - and you would add it to your price. It might not make a big difference in a \$5 billion program.¹¹

Having said that, there are ways that have been developed in other countries of having a defence procurement policy which would enable you to have a prime contractor with a single facility, such as our yard, contract that for a specific project in a specific fashion and have the suppliers and subcontractors and the technical solutions that would be wanted by the government run on a competitive basis underneath that yard. In other words, the yard is the prime contractor that is engaged for a specific project on specific terms, but the sourcing of and access to supplies, be they from the US or elsewhere, and the implementation and integration of those supplies into whatever the vessel is can also be done in a competitive spirit, because you are now running these things in a collaborative sense with your prime contractor sourcing best of breed from overseas. In addition, you can use the process to develop a local R&D which may not otherwise be there.¹²

10 *Committee Hansard*, 25 October 1999, p. 28.

11 *Committee Hansard*, 25 October 1999, pp. 56-57.

12 *Committee Hansard*, 25 October 1999, p. 57.

5.14 Mr Sharp also drew attention to Tenix's dockyard dilemma and then discussed a similar problem facing his company:

We suffer exactly same problem in electronics systems and software projects. We run a major project today which is coming to a conclusion. What do I do with 200 software engineers as I wait for the next contract to come through? We put a lot of investment into the processes, training of our people and the like, and, unless I can have a long-term plan, what do I do? As I go through the cycles of demand in the defence requirement area, I could possibly open and shut businesses of a totally different nature every five years to meet that demand to be competitive, but it does not make sense.¹³

5.15 When taken back to the dockyard example, Mr Sharp elaborated on the views he was putting to the Committee:

I think that in the planning and the concept of running a shipbuilding cycle from frigates to landing craft to whatever it happened to be there is a continuum which can be planned better than it is today. It is challenging, given different demands on the defence requirement, changes in priorities, Timor - it is a dynamic world. If it is communicated well with industry then I think we can live with it. I would suggest that in some areas competition as we have seen it today could change. You commented that you would not necessarily give it to that company. I would suggest that there are models which say you could give it to that company as long as you had an infrastructure in place that showed you are getting value for money.¹⁴

5.16 Asked whether the Government would still go out to tender, Mr Sharp replied:

Not necessarily. If you look at some of the models in the US and Europe, those governments definitely support certain prime contractors that are major employers where there is not necessarily the level of competition that we suffer today at a prime contract level. They have an open book policy where things are audited and you have got competition at various levels within the food chain. But I think you will find there are very few companies here today that have the deep pockets and the resources to prime contract and manage the risk successfully. That in itself is a challenge.¹⁵

5.17 Although Mr Favaloro had suggested views similar to those of Mr Sharp, Tenix had obviously taken note of the winds of change in relation to future naval ship building in Australia. He told the Committee:

The Williamstown dockyard was established for the purposes of naval ships. We have been building naval ships there since the middle of the 1980s - well, actually much longer. The Anzac ships were started there in the late

13 *Committee Hansard*, 25 October 1999, p. 16.

14 *Committee Hansard*, 25 October 1999, p. 16.

15 *Committee Hansard*, 25 October 1999, pp. 16-17..

1980s - 1988 or 1987, I think it was. That program runs out in 2004. Two years ago we realised that the Department of Defence's requirements were shifting and they were not going to be looking for more ships. So we have expanded and changed the shape of our business to be ready to be able to address the department's requirements when they eventually emerge in the future.

That is the reason why, for example, we now have a business that addresses the requirements of army, the land business. We have an aerospace business that is attempting to address the interests and requirements of the Air Force. Also, we have created a systems business, because you cannot run a modern Defence project unless you have the ability to take the various electronic components supplied from wherever, mostly overseas, and integrate them into a whole solution here in Australia. So we have created a business unit that is capable of doing that as well. We recognise that there is a need for us also to evolve and change to keep up with the government's and the department's requirements.¹⁶

5.18 It is evident to the Committee that there is concern within the Australian defence industry about the extent of consultation and co-operation between Defence and the industry about acquisition policies and practices and their effect on the evolving structure of the industry. The Committee does not wish to be prescriptive on the future of the Australian defence industry in this report because it would need a broader range of evidence under more specific terms of reference. Nevertheless, Committee believes that it is important to flag this concern to ensure that it is placed on the agenda and is discussed in appropriate consultative fora in the national interest. The ability of the defence industry to meet Australia's defence needs in the future is not something that should be taken for granted.

Senator John Hogg
Chairman

LIST OF SUBMISSIONS

Mr Robert Downey

Council of the City of Lithgow

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City of Greater Bendigo

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Mr Bob Cameron
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Mr F C Crook

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Office of Asset Sales and IT Outsourcing

Tenix Pty Limited

Australian Industry Group, Defence Council

Mr Mervyn Smith

GEC-Marconi Systems Pty Limited

Mr Leonard Fallon

**LIST OF WITNESSES WHO APPEARED BEFORE THE
COMMITTEE AT PUBLIC HEARINGS**

Monday, 25 October 1999 – Sydney

Mr Liam Bathgate, Manager, Group Communications, Tenix Pty Ltd
Mr Gilbert Dangleterre, Chief Executive Officer, Transfield Thomson-CSF Pacific Holdings
Mr John Favalaro, Group General Manager, Commercial, Tenix Pty Ltd
Mr Jean-Georges Malcor, Director, Transfield Thomson-CSF Pacific Holdings
Councillor Daryl McClure, Mayor, City of Greater Bendigo
Mr Ian Sharp, Managing Director, GEC-Marconi Systems Pty Ltd
Mr Anthony Shepherd, Chief Executive Officer, Project Development, Transfield Thomson-CSF Pacific Holdings and Director Elect, Australian Defence Industries
Vice Admiral Robert Walls, Director, Transfield Thomson-CSF Pacific Holdings and Director, Thomson-Marconi Sonar

Tuesday, 26 October 1999 - Canberra

Mr William Conley, Managing Partner, Blake Dawson Waldron
Mr Anthony Eaton, Senior Director, Office of Asset Sales and IT Outsourcing
Mr Michael Hutchinson, Chief Executive, Office of Asset Sales and IT Outsourcing
Dr Graham Kearns, Head, Industry and Procurement Infrastructure, Department of Defence
Mr Ian King, Director, Baring Brothers Burrows and Co Pty Ltd
Mr Simon Lewis, Executive Director, Office of Asset Sales and IT Outsourcing
Mr Ronald Richards, Director-General, Acquisition Management Projects, Department of Defence
Mr Christopher Rodwell, Policy Adviser, Australian Industry Group Defence Council

Friday, 19 November 1999 – Melbourne

Mr Kenneth Harris
Dr John White

Monday, 29 November 1999 – Canberra

Mr William Conley, Managing Partner, Blake Dawson Waldron
Mr Anthony Eaton, Senior Director, Office of Asset Sales and IT Outsourcing
Mr Alan Evans, First Assistant Secretary, Action Agenda Task Force, Department of Industry, Science and Resources
Mr Michael Hutchinson, Chief Executive, Office of Asset Sales and IT Outsourcing
Mr Ian King, Director, Baring Brothers Burrows and Co Pty Ltd
Mr Simon Lewis, Executive Director, Office of Asset Sales and IT Outsourcing
Mr Ronald Richards, Director-General, Acquisition Management Projects, Department of Defence

APPENDIX 3

INFORMATION ON SUPERANNUATION WHICH WAS PROVIDED TO OASITO BY THE COMMONWEALTH SUPERANNUATION GROUP, DEPARTMENT OF FINANCE AND ADMINISTRATION

Senate Foreign Affairs, Defence and Trade References Committee
Answers to questions on notice - Supplementary Hearing - 29 November 1999
Office of Asset Sales & IT Outsourcing

Senator Hogg asked (Hansard 29 November 99 page FAD&T 180):

Can you make available advice provided by the superannuation people in the Department of Finance and Administration in respect of superannuation?

Answer:

The following information was provided to OASITO by the Commonwealth Superannuation Group, Department of Finance and Administration.

CSS/PSS benefits on separation for employees affected by a sale, transfer or outsourcing.

The following comments are intended to provide a broad outline of the benefit options that apply to employees affected by a sale, transfer or outsourcing of an agency.

Before CSS/PSS members affected by a sale, transfer or outsourcing of an agency take any action or make any election in respect of superannuation, members are strongly advised to seek specific information based on their own individual circumstances. Employees could seek counselling from ComSuper with regards to any special circumstances that may apply in individual cases and they should also look at the ComSuper publications *CSS Your Super Scheme* and *PSS The Super Book*. Reference should also be made to the appropriate superannuation rules and legislation. This paper is not a substitute for the CSS and PSS rules and legislation.

Post 1 July 2000

From 1 July 2000 the CSS/PSS arrangements will require that members preserve at least the employer financed component of all lumpsum benefits before minimum retirement age.

Permanent, Temporary or Fixed -Term Contract Employees?

The provisions set out below apply equally to all types of employees, including employees on a fixed term contract who have not completed their contract at the time of the sale, transfer or outsourcing event. The rules for the PSS and CSS provide that where the contract of employment differs from 'normal' superannuation arrangements, the provisions in the contract will normally apply.

Superannuation Industry (Supervision) Act 1993 (SIS Act)

The SIS Act prescribes prudential and operating standards for superannuation funds and these standards can affect the benefit options available to an individual involved in a sale, transfer or outsourcing process. For example, SIS does not allow a cash in

hand payment of superannuation benefits (eg. lump sum, pension, etc.) when there is a change of owner and not a change of employer, as occurs when there is a sale of shares. The SIS Act also sets out the minimum preservation requirements. Prior to 1 July 1999 the minimum amount of CSS and PSS benefits which had to be preserved under SIS was equivalent to the Superannuation Guarantee (SG) minimum benefit. However, changes to the SIS preservation rules and scheme specific rules (eg CSS/PSS rules) may mean that more than that required under SIS will be required to be preserved.

Options available on sale, transfer or outsourcing when there is a change of owner but no change in employer

Where the employee continues in employment when there is no change of employer, (eg. when the Commonwealth sells shares in an organisation), the member has the following options:

Table Sale, Transfer or Outsourcing Options

CSS	PSS
<p>Rollover option* Employees who are: required to cease CSS membership in circumstances connected with a sale, transfer or outsourcing; and are under 55 may rollover an amount equal to the total involuntary retirement (redundancy) lump sum benefit</p>	<p>Rollover option* Employees who are: required to cease PSS membership in Circumstances connected with a sale, transfer or outsourcing; and are under 55 May rollover an amount equal to the total involuntary retirement (redundancy) lump sum benefit.</p>
<p>Preserve the total benefit Benefit entitlement can be preserved in the scheme until at least minimum retiring age (or earlier, in cases of invalidity retirement or death). In a sale, transfer or outsourcing two preservation options are available:</p> <p>Standard preservation - (Available if under minimum retiring age) CPI indexed pension based on 2.5 times members basic contributions plus interest earned until commencing pension. Plus payment of accrued member and productivity benefit, which may be received as a non-indexed pension.</p>	<p>Preserve the total benefit Total benefit entitlement is preserved in the scheme until at least age 55 and leaving the workforce (or earlier, in cases of invalidity retirement or death). Member and productivity component continue to earn interest. Remaining employer financed component increased in line with CPI.</p>

<p>Delayed Updated Pension (DUP) - (available irrespective of age) provides a CPI indexed pension on retirement from the work force after age 55 based on salary and length of scheme membership as at the sale, transfer or outsourcing day. The age at retirement from the workforce is used to assess the pension factor and the member's final salary is updated by CPI from sale, transfer or outsourcing day to retirement. Plus payment of accrued member and productivity component, which may be received as a non-indexed pension.</p>	
<p>Postpone the benefit Available if minimum retiring age or greater, but under age 65. (If over age 65 benefit must be taken immediately.)</p> <p>Postpone CPI indexed pension and own contributions plus interest and productivity contributions and interest until retirement from the work force.</p>	<p>Postpone the benefit Not available</p>

OASITO suggests that the Committee may be assisted by the attached ComSuper advice dated 11 June 1999 confirming the options available to ADI CSS members.



97/2923
Commonwealth Superannuation Administration
PO Box 22 Belconnen ACT 2616
Unit 1, Cameron Offices, Chandler Street
Belconnen ACT 2617

Reference:
Contact: Robert Fowler

Telephone: 02 6252-7528
E-mail: <http://www.robert.fowler@comsuper.gov.au/>

11 June 1999

Mr N Rokvic
Director
Office of Asset Sales and IT Outsourcing
Level 2, Burns Centre
28 National Circuit
FORREST ACT 2603

Dear Mr Rokvic,

I refer to your facsimile enquiry, addressed to John McCullagh, in which you ask for confirmation of the benefit options available to ADI employees who are currently members of the Commonwealth Superannuation Scheme (CSS), when ADI is sold.

The superannuation options available to members who are under 55 years of age, who cease CSS membership on change of owner, are:

- **Preserve all benefits in the CSS.** This option entitles the member to an employer-funded Deferred Pension, which is calculated as a percentage of accumulated basic contributions in the Fund at the date of claim, plus *either* a lump sum of accumulated contributions, *or* a non-indexed pension purchased with the accumulated contributions. This benefit may be claimed at any time after 55, providing the member has not re-entered eligible Commonwealth service.
- **Delayed Updated Pension.** This option entitles the member to an employer-funded indexed pension, which is calculated on the member's salary at the date of sale, updated by movements in the Consumer Price Index to date of claim, contributory service in years and days at the date of sale, and age in complete years when the benefit is claimed. The member is also entitled to *either* a lump sum of accumulated contributions, *or* a non-indexed pension purchased with the accumulated contributions. This benefit may be claimed after minimum preservation age, currently 55, and retirement from the Australian work force.
- **Rollover CSS equity to another Fund or Retirement Savings Account.** This option allows a rollover of 3.5 times accumulated basic contribution, plus accumulated supplementary contributions to a fund of the member's choice. There are no further benefits due or payable from the CSS. The employer component of this benefit may be claimed after minimum preservation age, currently 55, and retirement from the Australian work force. The member contributions remain a restricted non-preserved benefit until SIS requirements for release are satisfied.

The superannuation options available to members 55 years of age and over, who cease CSS membership on change of owner, are:

- **Delayed Update Pension.** See above.
- **Rollover CSS equity to another Fund or Retirement Savings Account.** See above.
- **Postpone Standard Pension and claim an immediate lump sum of accumulated contributions.** This option entitles the member to an employer-funded indexed pension, which is calculated on the member's salary at the date of sale updated by movements in the Average Weekly Ordinary Time Earnings to date of claim, contributory service in years and days at the date of sale, and age incomplete years when the benefit is claimed. The employer portion of the benefit may be claimed after retirement from the Australian work force.
- **Postpone all benefits.** This option entitles the member to an employer-funded indexed pension (outlined above) and *either* a lump sum of the accumulated contributions *or* a non-indexed pension purchased with the accumulated contributions. This benefit may be claimed after retirement from the Australian work force.

I trust that this information is of assistance to you. Should you require any further information, please contact my assistant manager, Heather Gill on 6252 6886.

Yours sincerely



Robert Fowler
Manager, Client Information Services

Senate Foreign Affairs, Defence and Trade References Committee
Answers to questions on notice - Supplementary Hearing - 29 November 1999
Office of Asset Sales & IT Outsourcing

Senator Hogg asked (Hansard 29 November 99 page FAD&T 180):

Provide criteria established for the standard application of established superannuation law and rules.

Answer:

Former Commonwealth employees who transferred to ADI on its establishment were able to remain members of the Commonwealth Superannuation Scheme (CSS) because ADI was an approved authority under the *Superannuation Act 1976* (the Act). ADI ceased to be an approved authority under the Act on sale date (29 November 1999). An extract of the Act, defining an 'approved authority' is set out below.

Part I Preliminary

Section 3

Superannuation Act 1976

approved authority means:

(a) an authority or other body that is declared by the Minister to be an approved authority for the purposes of this Act and is:

- (i) a body corporate incorporated, whether before or after the commencement of this Act, for a public purpose by an Act, regulations made under an Act or a law of a Territory; or
- (ii) an authority or body, not being a body corporate, established, whether before or after the commencement of this Act, for a public purpose by, or in accordance with the provisions of, an Act, regulations made under an Act or a law of a Territory; or
- (iii) a company or other body corporate incorporated, whether before or after the commencement of this Act, under a law of the Commonwealth or of a State or Territory, being a body corporate in which the Commonwealth has a controlling interest; or
- (iv) an authority or body established, whether before or after the commencement of this Act, and whether by or in accordance with the provisions of an Act, regulations made under an Act or a law of a Territory or otherwise, and whether a body corporate or not, being an authority or body which is financed in whole or in substantial part, either directly or indirectly, by moneys provided by the Commonwealth; or
- (v) a company or other body corporate incorporated, whether before or after the commencement of this subparagraph, under an Act or a law of a State or Territory, being a company or body corporate in which:

- (A) an authority or body referred to in subparagraph (i), (ii), (iii) or (iv), or that is an approved authority because of paragraph (b), has; or
- (B) the Commonwealth and one, or more than one, such authority or together have; or
- (C) 2 or more such authorities or bodies together have;

a controlling interest; or

(b) an authority or body that, immediately before the commencement of this Act, was an approved authority for the purposes of the superseded Act other than such an authority or body in relation to which a declaration under subsection (2A) is in force.