

CHAPTER 3

RATIONALISATION OF DEFENCE PROPERTIES

The property rationalisation policy

3.1 Although there are many reasons for Defence to declare a property surplus and commence disposal action, property rationalisation within Defence has resulted from two main initiatives:

- a) an ongoing whole of government policy to reduce its property holdings throughout Australia; and
- b) evolving Defence policy that has seen substantial changes in the state and deployment of the Australian Defence Force.

Government property rationalisation

3.2 The rationalisation of the Commonwealth estate has been proceeding for some time. The broad philosophical basis for the ongoing rationalisation was outlined by DoFA officers during their appearance before the Committee:

But the point is that the Commonwealth is not a property company and this is an opportunity cost of capital and the Commonwealth has determined that there are better things for it to do than be a property holding company.

[Private sector companies] believe that their capital should be focussed on their core business rather than owning property. The government has a similar view—that the ownership of property is not their core business.¹

Defence driven property rationalisation

3.3 The Defence policy on estate management has seen considerable change during the previous decade, driven by a number of changes in the wider Defence environment.² The Defence Efficiency Review noted in 1997:

While the current disposition [of the Defence estate] is largely historically based, major facilities decisions in recent times have been driven primarily by strategic considerations.³

3.4 In its submission, Defence also noted the considerations of Defence's basing policy:

1 Ms Kathryn Campbell, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, pp. 489–90

2 Much of the following is drawn from Department of Defence, submission no. 37, p. 258

3 Future Directions for the Management of Australia's Defence, addendum, p. 213

Defence basing policy is predicated on the development and maintenance of Australian Defence Force (ADF) capability to meet operational and strategic requirements. This further influenced by factors that are fundamental to the delivery of capability including support, personnel and training requirements.⁴

3.5 The operational and strategic requirements that have led to changes in the disposition of Defence units include:

- a) the move of the 1st Brigade to Darwin as part of the ‘Army Presence in the North’ policy;
- b) the development of a fleet base at *HMAS Stirling* in Western Australia under the Two Ocean Basing policy;
- c) the development of a chain of bare air bases in northern Australia;
- d) a drive to maximise tri-service functions has also led to the amalgamation of many of the logistics, training and administrative facilities of the individual services; and
- e) the Commercial Support Program (CSP) has seen the outsourcing of many Defence support services to private contractors.

3.6 Each of these has resulted in changing property requirements across the Defence Estate, with new facilities being created while older, often single service facilities, became surplus to requirements.

3.7 Defence studies also demonstrated that the costs of facilities and accommodation could be minimised by ensuring that bases are kept beyond a certain minimum size. As the Defence Efficiency Review explained:

Smaller bases do not provide economies of scale and available data indicates that per capita operating costs increase significantly for bases with less than 1000 personnel.⁵

3.8 In general, Defence also pointed out that, as there is a direct relationship between the Defence estate asset value and operating costs, it will always be important to minimise the overall size of the Defence estate, within the constraints of fulfilling the Defence task.⁶

3.9 Defence’s changing strategic and operational posture gives the opportunity to rationalise further property holdings in the capital cities and move from high-value metropolitan sites to lower-value regional sites that fit with Defence’s requirements.

4 Department of Defence, submission no. 37, pp. 258–9

5 Future Directions for the Management of Australia’s Defence, addendum, p. 228

6 Department of Defence, submission no. 37, p. 259

Defence said it will continue to pursue such opportunities. During the last few years, for example, Army elements have moved to Puckapunyal and Townsville from Sydney Harbour foreshore sites, the Hydrographic Office has moved from North Sydney to Wollongong, and the major Defence office at 350 St Kilda Rd Melbourne has been sold and significant elements relocated to Laverton.⁷

3.10 In the light of these considerations, a number of Defence studies examined the facilities requirements for the ADF, including the:

- Naval Infrastructure Strategy 2010;
- ADF Airfields Study;
- Review of Army's Long Term Facilities and Training Area Requirements;
- Facilities Rationalisation Study 1992;
- Force Structure Review 1991; and
- Defence Efficiency Review 1997.

3.11 These factors led to the sale of about 170 properties or parts of properties since 1991 with gross receipts of around \$450 million. Defence is continuing its rationalisation and consolidation of the Defence estate and proposes to reduce its property portfolio by a further 25 per cent over the next five or six years.⁸ In financial year 2000–01, Defence expects to return approximately \$97 million to its budget from property disposal, with this figure rising to \$173 million in 2001–02.⁹ Defence explained that:

This gives the opportunity to rationalise property holdings further in the capital cities and move from high value metropolitan sites to lower value regional sites that fit with Defence's strategic requirements and Defence will continue to pursue such opportunities. During the last few years, for example, Army elements have moved to Puckapunyal and Townsville from Sydney Harbour foreshore sites, the Hydrographic Office has moved from North Sydney to Wollongong, and the major Defence office at 350 St Kilda Road Melbourne has been sold and significant elements relocated to Laverton.¹⁰

7 Department of Defence, submission no. 37, p. 259 [see also 169]

8 Department of Defence, submission no. 37, p. 259

9 Mr Rod Corey, Head, Defence Estate, Department of Defence, *Committee Hansard*, 2 April 2001, p. 667

10 Department of Defence, submission no. 37, p. 259 [see also 169]

Current policy guidance

3.12 Defence is guided in the ownership and disposal of properties by both government-wide and Defence-specific policies.

Commonwealth property principles and the Commonwealth property disposals policy

The Commonwealth property principles

3.13 In summary, the Commonwealth property principles set out the circumstances in which the Commonwealth Government should own property. Embedded in the principles is the presumption that, in general, property should not be Commonwealth-owned unless the rates of return exceed a predetermined level. The aim of the property principles is to provide guidance on when the Commonwealth should own property:

The Commonwealth property principles generally apply to land that Commonwealth is still using and [they guide] whether or not it should remain in [Commonwealth] ownership.¹¹

3.14 Mr Stephen Bartos, General Manager, Budget Group, DoFA, told the Committee that a rate of return of 14 to 15 per cent is currently applied throughout the Commonwealth property principles.¹² Ms Kathryn Campbell, First Assistant Secretary, Property Group, DoFA, added:

The internal rate of return calculations generally look at the property over a ten to fifteen year period and take into consideration the costs that are likely to be invested in the property over that period, as well as the likely income from the property and determine the rate on that aspect.¹³

3.15 In addition, a property may remain in Commonwealth ownership if there are public interest considerations that outweigh economic considerations. Examples listed include symbolic significance, environmental, heritage or security requirements.¹⁴ Importantly, the onus is on each government agency to justify retaining a property in public ownership.¹⁵ The practical operation of these principles is examined in greater detail below.

3.16 The Commonwealth property principles detail a number of measures required to encourage efficient, effective and transparent decision-making and accountability.

11 Ms Kathryn Campbell, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, p. 477

12 Mr Stephen Bartos, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, p. 474

13 Ms Kathryn Campbell, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, p. 475

14 Commonwealth Property Principles, paragraph 2

15 Commonwealth Property Principles, paragraph 3

However, Mr Stephen Bartos, when questioned about the calculations that determined the sale and lease back of a number of Defence properties, stated:

In terms of whether or not these properties met the hurdle rate as applied in the property principles, yes that was done. The calculations were done prior to decision by cabinet. ... If these form part of a cabinet submission, they are not going to be made available.¹⁶

3.17 Although the Committee respects Cabinet confidentiality, the withholding of figures in this way is contrary to the policy of transparency and accountability laid down in the Commonwealth property principles. The inclusion of facts and figures in a Cabinet submission does not, of itself, render those facts and figures confidential. Cabinet submissions often contain information, which neither the Government nor anyone else would consider to be confidential. Unless those facts and figures have some inherent reason to be confidential (eg their release would be contrary to our national security interests), they should not be withheld from public release solely on the grounds of having been used in a Cabinet submission. The withholding of such information is not only contrary to principles of public accountability but also fosters the perception that such information would not stand up to scrutiny if released and that the withholding of that information is intended to prevent such scrutiny.

The Commonwealth property disposal policy

3.18 Once a Commonwealth property has been listed as surplus to requirements, the Commonwealth property disposal policy provides the requirements for property disposal. Foremost in this policy is the general principle that ‘Commonwealth property to be sold is to be sold on the open market at full market value.’ However, exceptions to the rule are provided for in the case of ‘priority sales’ and ‘concessional sales’.

3.19 Priority sales are those made to the purchaser without offering the property on the open market, and may be made in limited circumstances to former owners of the property, Commonwealth-funded organisations, or where the sale to a State or Territory Government would advance Commonwealth policy interest. The sale should still be at full market value. DoFA officers stated that ‘priority sales, indeed, are not encouraged’.¹⁷

3.20 Concessional sales are a type of priority sale where the price is below market value. They also require the permission of the Minister for Finance and Administration to proceed. While specific comment was not made, it can be assumed that these sales are discouraged more than priority sales.

16 Mr Stephen Bartos, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, pp. 474–5

17 Mr Paul Ferrari, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, p. 483

Defence policy

3.21 The plan for disposing of Defence properties across the short, medium and long term is articulated within the Defence Estate strategic plan. This plan is designed as a portfolio-level document to provide the longer-term planning framework for the rationalisation and consolidation of the Defence estate over the next 20 to 30 years. According to DEO:

The [strategic plan] is to be supported by detailed business case studies and facilitate the executive decision making process. The progressive implementation of the [strategic plan] will be instrumental in meeting DRP targets for property disposals and efficiency savings.¹⁸

3.22 The Committee sought a copy of the strategic plan from Defence to assist in its inquiry. However, the Minister for Defence declined to release it, owing to the latest revision not having been considered by government.

3.23 The unavailability of the strategic plan makes it difficult for the Committee to address in any meaningful way the first part of term of reference 5 regarding how the ADO decides whether property is surplus to requirements.

3.24 However, during another inquiry into recruitment and retention of ADF personnel, the Committee received evidence that the rationalisation and consolidation of bases in operational areas has had ramifications for recruitment and retention, especially the latter. As the majority of ADF members are recruited in the southern States, which is where most of their families and friends live, the closure of many bases in the southern State capital cities has had the effect of giving fewer serving members, particularly in Army, the opportunity to serve near family and friends and to live in cities, which have good facilities and amenities and better employment opportunities for spouses than in most other areas where there are large bases. As further rationalisation occurs, this will become increasingly a recruitment and retention issue.

Defence Estate Divestment Plan

3.25 In a DEO document entitled *Property Disposals Policy Framework*, there is reference to the Estate Divestment Plan. It states:

The Estate Divestment Plan (EDP) is the endorsed five-year property disposal program. It is made up of the list of potentially surplus Defence properties, its primary source being the SPDE [Strategic Plan Defence Estate]. It includes estimates of the revenues expected from each disposal and of the costs involved in achieving them. The EDP is reviewed and endorsed annually by the DEE, and plays an important part in development of the DEO's component of the FYDP.

18 *Defence Estate Organisation—The Way Ahead*, available on <http://www.defence.gov.au/deo/documents/deob.pdf>

The EDP is over programmed by 10 per cent as a mechanism for ensuring Defence Estate can meet FYDP guidance for receipts. To achieve the higher revenue target, additional disposal projects are positioned in the FYDP until the cumulative revenue estimate for any year of the FYDP is 10 per cent greater than the guidance figure of that year.

Endorsement of a disposal project as part of the EDP authorises disposal officers to raise purchase orders and expend funds to determine the extent of site constraints and opportunities and how they can best be dealt with. The EDP is reviewed and revised twice each year to reflect the latest revenue and expenditure projections, as information is gathered about the costs of preparing sites for sale, and about changes to valuations.

After analysis of the property constraints and opportunities and before funds can be expended on planning actions, remediation or marketing, a Disposal Strategy must be prepared presenting a business case on the disposal strategy to the appropriate delegate for approval.

The EDP is closely linked to the Green Book. Appreciation of this linkage is particularly important where the timing of a disposal at one location is dependent on the completion of a Green Book project at another. Development and review of the two programs in the same timeframe is an important factor in the coordination and planning of related projects.¹⁹

The legal environment

3.26 In examining the disposal of Defence properties, it is also important to consider the wider legal context in which these disposals occur. The *Land Acquisition Act 1989* (LAA), which is under the responsibility of the Minister for Finance and Administration, provides the legal framework within which Commonwealth property is administered. Any disposal of Commonwealth property requires authorisation under the LAA.²⁰

3.27 As the owner of land, Defence is bound by Commonwealth legislation in relation to issues such as heritage conservation²¹ and environmental protection.²² However, as a Commonwealth agency, it is not bound by State or Territory legislation. In the context of Defence disposals, this is significant in that Defence is not obliged to comply with local planning, environment or heritage laws. Nevertheless, once Defence sells the property, the new owner is bound by these laws, so, in practice, Defence has to take them into account prior to sale.

19 The DEO document was supplied to the Committee under cover of a letter from Mr Ross Bain, Assistant Secretary, Property Management, dated 30 April 2001

20 Department of Finance and Administration, submission no. 47, p. 94

21 *Australian Heritage Commission Act (Cth) 1976*

22 *Environment Protection & Biodiversity Conservation Act (Cth) 1999*

Sale and lease-back

3.28 Sale and lease-back arrangements apply when a property continues to be required by Defence but the financial benefit of keeping the property does not meet the 'hurdle rate'. When this occurs, the property is sold at market value and then leased back to Defence as part of the sale contract. Under most circumstances, Defence would enter into long-term lease arrangements with options for lease extension to gain security of tenancy.

3.29 During the inquiry, the Committee examined the sale and lease-back of Defence properties in the Melbourne and Sydney CBD and the Defence Headquarters complex at Russell in Canberra. The use of sale and lease-back will be discussed later in the report.

Selling or retaining: the options

The application of the property principles and disposal policy

3.30 The operation of the Commonwealth Property Principles and the Commonwealth Property Disposal Policy leave little room for ambiguity. If the property is declared surplus through lack of requirement or does not meet the 'hurdle rate' for retention under the Property Principles, the property then falls under the Disposal Policy. As previously stated, the disposal policy has the underlying principle of sale at market value. However, according to the policy, when certain other considerations are present, the property may also be disposed of as a priority sale, again at market value, or a concessional sale, at less than market value.

3.31 Evidence given by officials of both the Departments of Defence and Finance and Administration has made it clear that priority and concessional sales are both discouraged. Evidence given to the Committee by Mr Paul Ferrari, Acting Branch Manager, Competitive Tendering and Grants Branch, DoFA, supported this view:

Priority sales, indeed, are not encouraged. Quite clearly the policy on disposal of surplus property is to sell the property on the open market at full market value. There are some circumstances where priority sales are possible, but they are fairly limited circumstances. Within the Commonwealth they are fairly tightly controlled in the sense that it is the Minister for Finance and Administration who has ultimate responsibility to approve such priority sales, and he would normally do so on the basis of a recommendation from another minister. The case for such consideration would need to be developed and put to the Minister for Finance and Administration by that other Minister.²³

23 Mr Paul Ferrari, Department of Finance and Administration, *Committee Hansard*, 26 February 2001, p. 483