

Chapter 10

Governance arrangements—conflicts of interest and confidentiality

10.1 The committee's second major concern about the governance arrangements for the 2010 tender process centred on the early identification and management of potential or perceived conflicts of interest—especially those arising from the outside employment of ADF personnel. The circumstances surrounding Major Charlton's employment in JMCO in Brisbane and his activities as a civilian in the air charter business especially his association with a likely tenderer highlighted three issues of policy, practice and procedure. They are:

- Defence policies on the disclosure and management of conflicts of interest;
- the contractual management of conflicts of interest; and
- adherence to risk management measures documented in the TEP.

Defence policies on the disclosure and management of conflicts of interest

10.2 The 2010 tender process appears to have revealed a gap in Defence policy on the disclosure and management of perceived conflicts of interest in respect of Reservists who:

- are not engaged in continuous full-time service; and
- are not directly involved in the relevant procurement being conducted within their group.

10.3 The evidence before the committee is that Major Charlton re-engaged with the ADF on a part-time basis.¹ As noted in the Deloitte Review, it appears that he was not, at any material time during the 2010 tender process, subject to the mandatory procedures in the relevant Defence Instructions on secondary employment² and the disclosure and management of conflicts of interest.³

1 See for example, Deloitte Review p. 19.

2 Deloitte Review, p. 19. Defence Instruction (General) PERS 25-2—Employment and voluntary activities of Australian Defence Force Members in off-duty hours.

3 Defence Instruction (General) PERS 25-3—Disclosure of interests of members of the Australian Defence Force. It is, however, acknowledged that Major Charlton was subject to legal and ethical requirements of general application—for example, the *Crimes Act 1914* (Cth) s 70(2) (the offence of the unauthorised disclosure of information by a Commonwealth officer); the *Criminal Code Act 1995* (Cth) s 135 (the offence of dishonestly obtaining a gain or financial advantage from the Commonwealth); *Defence Force Discipline Act 1982* (Cth) s 58 (the offence of the unauthorised disclosure of information likely to be prejudicial to national security or defence); and DI(G) PERS 25-6—conflicts of interest and acceptance of offers of gifts and hospitality, p. 3 (general duty to disclose actual or perceived conflicts of interest).

10.4 These Instructions do not apply to ADF Reservists who are not employed on continuous full-time duty. They are expressed as applying to 'members' of the ADF. The term 'member' is defined narrowly to mean a permanent ADF member or a Reservist engaged in continuous full-time service.⁴ The Instructions do not provide reasons for their limited application, nor do they cross-reference any specific policies or procedures applicable to Reservists who are engaged on a part-time basis.

10.5 In contrast, the Defence Instruction on post-separation employment applies to Reservists who are on duty or rendering continuous full-time service.⁵ The Instruction also makes reference to the risk that conflicts of interest may arise from Reservists' civilian employment.⁶ However, it does not appear to regulate conflicts of interest arising upon a member's re-engagement with the ADF following a period of separation.

10.6 The Defence Instruction on conflicts of interest and acceptance of offers of gifts and hospitality contains a general duty to disclose conflicts of interest.⁷ As it is expressed as applying to 'all ADF members' without defining the term 'member', it appears to extend to Reservists employed in part-time service. However, the Instruction refers back to the procedures set out in the Instruction on the disclosure of interests (DI (G) PERS 25-3) for the notification of such conflicts. As noted above, the latter Instruction does not apply to ADF Reservists engaged in part-time service.

10.7 Cumulatively, these Instructions evince Defence's appreciation of the substantial risk in procurement processes that the outside employment or other private interests of Defence members—including Reservists—may create actual or perceived conflicts of interest. However, the limited definition of 'ADF member' in the Instructions on secondary employment and conflicts of interest means that this in-principle awareness is not reflected comprehensively at a procedural level.

10.8 While the committee welcomes the reforms announced by Defence, it notes that the measures identified in the Department's submission were limited expressly to Reservists who are engaged in continuous full-time service.⁸ Accordingly, the

4 DI (G) PERS 25-2, paragraph 3(c); DI (G) PERS 25-3, paragraph 3. See further, Deloitte Review p. 19.

5 Defence Instruction (General) PERS 25-4—Notification of post-separation employment, annex a.

6 DI (G) PERS 25-4, annex b, paragraph 3.

7 High-level statements on the disclosure and management of conflicts of interest also appear in various other Defence policy documents and industry publications. See for example, Department of Defence, *Guidance on Conflict of Interest Issues for Defence Personnel*, Circular Memorandum No 53/98, [1]; Department of Defence, *Defence and Industry—an Ethical Relationship* (1998), pp. 2–4; Department of Defence, *Ethics Matters in Defence Resource Management* (2002), pp. 10–12.

8 Department of Defence, *Submission 5*, p. 35.

committee is concerned that neither the current Instructions nor the proposed reforms appear to apply to Reservists who are engaged on a part-time basis.

Recommendation 2

10.9 The committee recommends that Defence reviews all Defence Instructions and related documents in respect of Reservists, full or part time, to ensure that real and potential conflicts of interest that might arise as a result of past, current or post separation employment are identified, reported and managed appropriately. In particular:

- (a) Defence considers whether Defence Instructions DI(G) PERS 25-2 (Employment and voluntary activities of ADF members in off-duty hours) and DI(G) PERS 25-3 (Disclosure of interests of members of the ADF) should be extended to Reservists who are not engaged in continuous full-time service; or**
- (b) if there is no intention to extend the application of DI(G) PERS 25-2 and DI(G) PERS 25-3 to Reservists who are not engaged in continuous full-time service, Defence develops specific policies covering the civilian employment of, and the disclosure of conflicts of interests by, these personnel.**

The contractual management of conflicts of interest

10.10 The Defence Instruction on post-separation employment referred to above makes reference to the contractual management of conflicts of interest. It notes the inclusion in Defence contracts of standard provisions governing contractors' engagement of former Defence personnel. These provisions generally require contractors to disclose the proposed use of former Defence personnel, and in certain circumstances seek written approval from Defence before engaging such personnel.⁹

10.11 As mentioned in chapter 3, a provision of this nature was included in the Deed of Standing Offer. Under Clause 22, Adagold was required to:

- ensure that any of its employees who were former Defence employees complied with the requirements of the Defence Instruction on post-separation employment; and
- seek the prior written consent of Defence before permitting a person to contribute to the performance of services provided under the deed, where that person was a Defence employee in the previous 12 months.

10.12 The clause required Defence, in assessing a contractor's application, to consider:

- the character and duration of the person's engagement with Defence and the contractor; and

9 DI(G) PERS 25-4, paragraph 28.

- the potential for real or perceived conflicts of interest; and
- the effects of withholding permission on the person's employment opportunities or the performance of the deed.

10.13 As mentioned in Chapter 6, the AGS Review found that Adagold did not comply with this clause before seeking the assistance of Major Charlton, through AIS, in the preparation of its tender response. However, as the clause was not expressed as a mandatory condition of participation, AGS concluded that it was open to Defence to accept Adagold's tender response despite its non-compliance. This finding may well be valid but it then raises the question about what is the point in having such a clause if it can be ignored with impunity.

10.14 Even so, the committee is concerned by the conclusion reached by AGS that it was unlikely Defence would have withheld approval had Adagold complied with clause 22 and sought permission to obtain Major Charlton's assistance in the preparation of its response. The basis for this conclusion was that Major Charlton's engagement in JMCO Brisbane was unrelated to the procurement and, consequently, 'the potential for real or perceived conflicts of interest or probity objections would have been assessed as low'.¹⁰

10.15 While it may be that Defence would have assessed the potential for conflicts of interest as low, it does not follow that such an assessment would have been reasonable in the circumstances of the procurement. Defence should have been sensitive to the heightened potential for probity objections and perceived conflicts of interest and the adverse impact they may have on procurement outcomes. Defence had received Strategic's preliminary concerns about the involvement of Major Charlton in Adagold's tender response. Notwithstanding these complaints, and the receipt of Major Charlton's declaration of a potential conflict of interest, Adagold's compliance (or the failure thereof) with clause 22 does not appear to have been considered at any stage in the procurement process.

10.16 The committee considers that compliance with contractual clauses on conflicts of interest should be given closer attention in future procurements. It is also encouraged by Defence's proposed review of its standard contractual provisions on the use of former Defence personnel and post-separation employment, to clarify and strengthen probity arrangements.¹¹ It requests that Defence keep it informed of progress in this regard.

Adherence to risk management measures documented in the tender evaluation plan

10.17 The committee is concerned that the 2010 tender process has highlighted multiple failures to adhere to documented risk management processes, namely:

10 AGS Review, p. 7.

11 Department of Defence, *Submission 5*, p. 35.

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- security measures to confidential tender files were not applied in a timely way;
 - conflict of interest declarations by tender evaluation team members were not signed before the evaluation process began and were deficient in their coverage; and
 - specific probity briefings to tender evaluation team members were not provided prior to the commencement of the evaluation process.

10.18 In light of the probity concerns outlined above, the committee considers that compliance with probity measures should be prioritised in future procurements of air sustainment services to the MEAO. In this respect, the committee welcomes Defence's proposed reforms to the use of conflict of interest declarations. The committee understands that all Reservists on full-time or part-time service employed in procurement or contract management activity will be required to sign a conflict of interest declaration prior to their engagement for that duty. In addition, the committee understands that commanding officers or supervisors will be required to make a risk-based assessment as to which other Reserve personnel under their supervision must complete a declaration, and must document their decisions.¹²

10.19 Irrespective of Defence's broader reform timeframes, it is essential that these measures are implemented, as a matter of priority, in any future tenders of the MEAO contract. Further, in assessing the need for Reserve personnel to sign declarations, the committee emphasises the importance of identifying and considering Reservists' civilian employment or other financial interests in the commercial air charter industry—as well as their professional and social relationships with persons holding such interests.

10.20 The committee also supports the findings of the Deloitte Review in respect of the scope of conflict of interest declarations.¹³ It considers that all future conflict of interest declarations should routinely address the matters identified in that review — 'declarations should include possible conflicts arising from employment, prior employment other financial interests in potential suppliers or relationships with persons who have interests in these organisations'. In line with the observations made in the AGS' review, the committee also notes the importance of all personnel, including people involved in the preparation of request documents, signing conflict of interest declarations before embarking on their respective tender work.

Recommendation 3

10.21 The committee recommends that, prior to the re-tendering of any future contracts for the provision of air sustainment services to the MEAO, Defence ensures that:

12 Department of Defence, *Secretary's Opening Remarks* (tabled 29 March 2011), pp. 20–21.

13 See chapter 6.

- (a) all Reserve personnel involved in the procurement complete a conflict of interest declaration; and**
- (b) commanding officers or supervisors in 1JMOVGP:**
 - (i) make a risk-based assessment as to which other Reserve personnel must complete a conflict of interest declaration and which personnel do not;**
 - (ii) in making a risk-based assessment, give consideration to identifying and obtaining conflict of interest declarations from Reservists who have associations with the commercial air charter industry. Such associations may include:**
 - present or previous civilian employment with air transport providers;**
 - financial interests in these companies or related companies; or**
 - professional or social relationships with members or employees of these companies; and**
 - (iii) document their decisions whether or not to require these Reservists to complete a conflict of interest declaration.**

Recommendation 4

10.22 The committee recommends Defence ensures that, in all future procurements of air sustainment services to the MEAO:

- All members of tender evaluation boards and working groups, and all persons involved in the development of requests, sign conflict of interest declarations. Such declarations:**
 - (a) should be signed prior to the commencement of the tender evaluation process or the development of the request (as applicable); and**
 - (b) include declarations about possible conflicts of interest arising from their employment, prior employment, financial interests in potential suppliers or relationships with persons who have interests in potential suppliers.**
- All members of tender evaluation boards and working groups receive specific briefings on conflicts of interest and other probity matters, prior to the commencement of tender evaluations.**

Conclusion

10.23 In considering its terms of reference with respect to governance arrangements, the committee finds that:

- there was insufficient evidence to determine whether the decision to award the contract to Adagold was influenced by any vested interests, outside influences or any other perceived or actual conflicts of interest;
- while departmental personnel in the tender process may not have breached Commonwealth procurement policy or procedure they certainly failed to heed strong advice and guidance provided in these documents on managing probity risk; and
- the governance arrangements were inadequate and did not protect the process from perceived conflicts of interest. There was, however, no convincing evidence that those with a potential conflict acted improperly.

10.24 The committee has made a number of recommendations designed to improve the way in which risk management and probity concerns are managed in future tenders. The most important is the appointment of a probity adviser for such complex tender processes and the implementation of a more robust system governing conflicts of interest protocols especially as they relate to reservists. When it comes to probity matters, the committee believes that Defence needs to strive for best practice rather than mere compliance with the wording of Commonwealth procurement policy documents.

