COMMONWEALTH OF AUSTRALIA

Official Committee Hansard

SENATE

FINANCE AND PUBLIC ADMINISTRATION REFERENCES COMMITTEE

Reference: The government's information technology outsourcing initiative

THURSDAY, 17 MAY 2001

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SENATE

FINANCE AND PUBLIC ADMINISTRATION REFERENCES COMMITTEE

Thursday, 17 May 2001

Members: Senator George Campbell *(Chair)*, Senator Watson *(Deputy Chair)*, Senators Buckland, Lightfoot, Lundy and Ridgeway

Substitute member: Senator Eggleston for Senator Watson

Participating members: Senators Abetz, Allison, Brown, Calvert, Carr, Chapman, Conroy, Coonan, Crane, Eggleston, Faulkner, Ferguson, Ferris, Gibson, Harradine, Harris, Knowles, Mason, McGauran, Murphy, Murray, Payne, Tchen, Tierney and Watson

Senators in attendance: Senators George Campbell, Eggleston and Lundy

Terms of reference for the inquiry:

For inquiry into and report on:

The Government's information technology (IT) outsourcing initiative in the light of recommendations made in the committee's report, *Contracting out of government services—First Report: Information technology*, tabled in November 1997, and the Auditor-General's report No. 9 of 2000-2001, and the means of ensuring that any future IT outsourcing is an efficient, effective and ethical use of Commonwealth resources, with particular reference to:

(a) the need for:

(i) strategic oversight and evaluation across Commonwealth agencies,

(ii) accountable management of IT contracts, including improved transparency and accountability of tender processes, and

(iii) adequate safeguards for privacy protection and security;

(b) the potential impact on the capacity of agencies to conduct their business;

(c) savings expected and achieved from IT initiatives; and

(d) the means by which opportunities for the domestic IT industry, including in regional areas, can be maximised.

WITNESSES

Committee met at 9.05 a.m.

BROOME, Mr John Harold (Private capacity)

CHAIR—I wish to advise for the record that the witness appearing before the committee this morning is protected by parliamentary privilege with respect to evidence provided. The committee has agreed to Mr Broome's request to hear his evidence in camera. However, he is advised that it may subsequently be made public by order of the Senate. I also take this opportunity to remind the witness that the giving of false or misleading evidence may constitute a contempt of the parliament. Mr Broome, do you have any comments to make on the capacity in which you appear?

Mr Broome—I am appearing as a private citizen, although I am a former agency head of the National Crime Authority.

CHAIR—Do you wish to make an opening statement?

Mr Broome—I will make some very brief observations. In relation to the fact that these proceedings are in camera, I asked that that be done for one simple reason; that is, I did not want the discussion of the particular facts and circumstances surrounding the NCA's involvement in cluster 3 to be seen by anybody as an attempt by me to involve the political process in those issues. I think the work this committee is doing is important, and it ought to be aware of some of the circumstances that agencies faced. Equally, I think it is much more important that we focus on how we get these things right in the future. I thought it might have been a little easier if this were done in camera. Having said that, I am happy to appear before the committee in a public session if it wants me to do so. I thought it would be useful to outline the reason for that request at this stage.

I suspect that most of the issues I want to touch on will be raised in the questions you may put to me. I will make a couple of general observations to start with. My concern about our involvement in the process was that—and bear in mind that we were effectively the first cluster to be established—the surrounding rules seemed to be ill-defined at that time. I cannot comment on what happened subsequently. They were changed in the course of the process, which I thought was unsatisfactory. There were disclosures of information to parties which I thought were surprising. For example, agencies were required to provide to OASITO the details of their present costing, which I understood—and I do not know this for a fact but I was told this was the purpose—would be made available to tenderers. That seemed to me to be an unsatisfactory process. Throughout the actual negotiation of the contract there were a number of very unsatisfactory elements from our perspective. Our concerns were not adequately taken into account. They were dismissed almost peremptorily. There were agreements reached with ministers which were simply not honoured. I felt that the whole process was quite unsatisfactory. I am still left bemused as to why an agency which provided about three per cent of both the value and volume of the contract was seen to be such a critical linchpin to it that we were not under any circumstances to be allowed out of the deal, as it were.

No-one has ever explained to me why three per cent was critical, bearing in mind that not long before the composition of the cluster was settled such a minor agency as the then ASC, now ASIC, was removed from the cluster. They were an organisation of 4½ thousand or 5,000

people around Australia—clearly a much more significant component. That did not seem to cause the cluster any great difficulties, but our involvement was seen to be critical, for reasons, as I say, that I never understood.

As I said, there were a whole range of issues in relation to the contract itself, which I have outlined in the submission that I sent to Mr Humphry. I believe that, while the process may have improved subsequently—and I do not have any personal knowledge of that—certainly the first exercise was very unsatisfactory from the point of view of agencies. It cost us a great deal of time, effort and grief to be part of it. We then had subsequent difficulties which I have outlined in the submission in relation to adequate security control of the data, cost increases and so on, all of which I think demonstrated that the original contract was not satisfactory. If there are lessons to be learned from this, it is that while governments have every right to expect that contracts will be entered into quickly and effectively and that there should be no unreasonable delays in giving effect to government policy, nonetheless there are questions about the adequacy and effectiveness of the contractual arrangements which ought not to be lost sight of. Some predetermined date for a press conference is not a reason to sign an unsatisfactory contract. More importantly, if agency heads are to be personally responsible for what happens that affects their agency—as they are expected to be these days—they ought to be given some control over the decisions that are made which can affect those outcomes.

I was facing the situation where a contract which I believed was unsatisfactory, which did not adequately protect information that I believed should be adequately protected, was entered into on our behalf, irrespective of our agreement. Yet you all know that if there had been a leak of information through that material being held on the outsourced mainframe, it would not have been the executives of the company fronting a Senate or parliamentary committee and the press; it would have been me. As you all know, I have been there and done that in other circumstances. I have had to live with other people's mistakes. That is the role we undertake, and I accept it. But it is not good enough in those circumstances, in my view, for agency heads to have their genuine and real concerns totally ignored. You cannot have it both ways. You cannot have a risk management approach that says the agency heads have to make those judgments and live with the consequences and then have somebody in another agency with no responsibility take over those decision making functions but never take over the risk.

Peter Boxall was never going to have to cover for some mistake that was made in the contract; I was. That, I think, is part of the fundamental shift that we have to recognise if we want agency heads to accept the level of responsibility which is now being imposed upon them. With that risk should go the capacity to make the decisions. You cannot be held accountable for something that you do not have any control over. This was a classic example of a whole exercise where departmental secretaries and agency heads did not have control over it, yet they were to carry the can for it, including the budgetary consequences in the second, third and fourth years of the contract, long after the announcements about savings had been made, and long after the trumpeting of the success of the project. If the costs in fact exploded, who would carry the responsibility for that? The individual agencies.

There are obviously some fairly fundamental issues in all of that. I have described it in my comments to Mr Humphry as probably one of the worst public policy examples in which I have been involved in 25 years. I stand by that description. And I have seen some pretty interesting examples in the last 25 years.

Senator LUNDY—You have raised quite a few issues. I will try to go through them pretty systematically. You mentioned that the NCA provided three per cent of the contract. Was that the value of the savings estimated for the cluster 3 contract?

Mr Broome—As I understand it, we comprised three per cent of the volume of information being held on the outsourced mainframe system. I think we probably represented marginally more than three per cent of the cost. In fact, we represented more than three per cent of the cost because our requirements for additional security meant that our costs to the provider were higher but we did not represent any more than at least three per cent of the actual value.

This was one of the problems. This was an initiative which was designed to ensure transparency in the provision of services and their costs, yet we were cross-subsidised substantially by the other major players, in particular DIMA. Because we were a small part of the total, the cross-subsidy was not a substantial amount of money, but there is absolutely no doubt that we were cross-subsidised. That was because they had to comply with the requirement which was extracted at great pain that this would actually cost the NCA no more than the previous arrangements—a requirement which they resisted for a long time. So having met that obligation, we paid no more, but my understanding is that, in terms of the total contract cost, there was some cross-subsidy because there were greater costs in relation to our data than its proportionate value to the contract.

Senator LUNDY—That was essentially the point I was looking for.

Mr Broome—Can I make one other observation for the record. My submission to Mr Humphry and my observations here today need to be taken on board on the basis that I have had no access to the NCA records that relate to this matter since I left in September 1999. I took no records with me, so I have had to rely on my memory as to what occurred. I say that not because I am in any sense unsure of most of the salient facts, but simply because I have not been able to go back and check documentation. I do not have access to it, so to some extent I am going to rely on memory. Where I am not sure of matters, I will certainly indicate that to you because you may have better means than I have of verifying some of those circumstances.

Senator LUNDY—Thanks for that. In terms of a dollar value of savings that the NCA were supposed to contribute, did you at any time ever have the opportunity to calculate for the NCA a quantified figure that this whole exercise was supposed to return to you? I ask that in the context that the whole program was designed so that, if you found savings over and above a conceivable agency deduction, you actually got to keep them theoretically.

Mr Broome—That was a problem that never confronted us.

Senator LUNDY—Was that equation ever done within the NCA?

Mr Broome—I do not recall ever seeing anybody do the calculations to work out whether we were in fact better or worse off. I think the answer has to be that we were worse off for two basic reasons. The first is that we paid exactly the same amount for the services we got from the outsource provider under the no extra cost deal. As I recall, the costs were virtually lineball with that, so we were basically paying the same dollars but we had already been subject to the predetermined efficiency dividend from the department of finance.

Senator LUNDY—That was my next question.

Mr Broome—So we paid first and then we paid second, and we certainly did not get any dividend back down the track. Bear in mind that the next stage of the process which was going to take place would have occurred after I left; that was the question of outsourcing the desktop equipment. In this contract, we were effectively only dealing with a mainframe service that had been previously provided by the old Department of Administrative Services here in Canberra, so it was basically a capacity to stick some information on and be able to retrieve it. We are talking here about a contract which I think from memory was something like $130,000-odd for a year or something; it was not sheep stations. That was the other silly part about this. It cost more of my time than major investigations did just trying to get some basic issues sorted out for what was quite frankly a very low value contract but a very important issue in terms of the concerns we had about security and so on. So that was what made the whole thing even more frustrating I think, because it was just a total waste of time and effort when you think about it in the overall scheme of things.

Senator LUNDY—Were you ever able to quantify the time and effort—that is, the human resources—that went into this contract, or are you in a position to estimate?

Mr Broome—I can give you very ballpark figures. We had people attending steering committee meetings in Canberra on a regular basis. One or two staff would come down, often from our IT area in Sydney. They would leave very early and drive down for the day, be here for a 9 o'clock meeting, and drive back at night. That was occurring, from memory, during the preliminary processes probably once a month; it was that sort of frequency. I had a band 2, general manager of corporate, who was involved in a number of the discussions at various stages. That meant trips from Melbourne to Canberra. In my own case, I attended some meetings. Certainly, when I was personally involved, it was not huge amounts of time but it was time that I could have better spent elsewhere. If you costed our time and put a dollar value on it, we probably spent as much time in the negotiating process as the entire value of the contract. It does not take long to get $130,000 worth of costs, let us face it.

Senator LUNDY—Yes.

Mr Broome—Again, that was part of the concern. Every time, you have to write submissions to ministers, come and visit them and talk about the issues. That is all very expensive in terms of opportunity costs.

Senator LUNDY—Did you have to contract in or get external advisers to help you through this process, or did you engage legal advisers or anything like that?

Mr Broome—We did not. Indeed, in relation to the contract itself, I wanted to have it independently examined because I believed that it was inadequate. I was told in no uncertain terms by OASITO that I was not to do that—the Commonwealth had paid for legal advice, and it would be a waste of resources to repeat that cost by having somebody else check their work. I am not a contract specialist by any means, but I found mistakes in it, and that was two days before the minister was due to sign it. They were mistakes of fact, and I thought there were poor provisions in relation to protecting Commonwealth interests. But we simply did not get it independently verified—I certainly had some people in-house look at parts of it. My

recollection is that we only got the contract on literally the Thursday or Friday, and it was due to be signed on the following Tuesday, so there was not a lot of time to have that work carried out.

There were two levels of participants in these contracts. There were the main agencies who were the core of the steering committees and so on. In our case, the Department of Immigration and Multicultural Affairs—DIMA—was the prime carriage agency; one of its officers was effectively chair of that committee and so on. They were obviously able to meet here on a daily basis if they needed to, but then there were a series of other agencies such as ourselves who were only listed in the contract—in a schedule. We were not, in a formal sense, contracting parties, so we were one step removed from the process in that sense as well.

Senator LUNDY—OASITO are claiming that they had already contracted legal advice on behalf of the government generally. Were you ever given access to them or were you in a position to ask them specifically for an opinion on the validity or merit of the contract that you were being asked to sign?

Mr Broome—No. Let me say that I did not ask to talk to them, either. There was—

Senator LUNDY—But you did ask to get access to independent advice?

Mr Broome—I did raise the question of getting independent advice and was told, in a sense, 'Don't do that.' There were some fairly clear messages. I was left in no doubt that, if we had spent money on getting legal advice, there would have been a square-off in the budget.

Senator LUNDY—Are you able to quantify the money that the agency lost in the budget deductions leading up to this process?

Mr Broome—I cannot remember offhand.

Senator LUNDY—We could pursue that.

Mr Broome—We could provide those figures to you, but I certainly do not have them offhand. Again, they were not large amounts of money, because the total value was not huge, but they would have been in the order of, probably, tens of thousands, no more.

Senator LUNDY—In your opening comments you say that, because you felt that you were effectively cross-subsidised by bigger players in the cluster 3 contract, as an agency you were not in a position to deliver back any quantifiable savings value to the pool. What were your thoughts at the time and what are your thoughts now as to the possible justification for the insistence that the NCA be part of cluster 3? I am not asking you to speculate wildly, but what were you thinking at the time?

Mr Broome—I think there were some very clearly expressed reasons by people involved in the process. There was a view amongst certain people that I had discussions within OASITO and Finance that the decision to exclude security and intelligence agencies and Defence at the outset was wrong because it was based on assertions about access to material that had not been tested. The next group of agencies making similar claims were the law enforcement and related agencies—the AFP, AUSTRAC, the Director of Public Prosecutions, the NCA and so on. I

believe, because it was expressed to me in as many words, there was a strong view that we were not going to 'get away with' a claim that we should be exempted from this policy for security reasons. This was seen to be a furphy or a red herring that we were running because we did not want to be part of an outsourcing process.

It was important to have the NCA in cluster 3, which was after all the first effective cluster, because if we were there then the arguments about security would be seen to have been dealt with. Equally, I had a number of agency heads say to me, 'You're the person at the front line. Your task is to make sure these issues are adequately addressed if it is possible to do so and hence require people like DSD to provide independent objective advice on the level of physical security and so on.' There was another agenda going—I have no doubt about that. The idea was to dispel the argument that security was an issue in these contracts.

When you think about other government agencies—Tax, for example—there were going to be real concerns if the tax database was suddenly held in a box that belonged to a private company and which may have been held offshore. As I understand it, the original rules for the outsourcing arrangements did not require that the data be actually held in Australia. That was a change in policy that was made fairly early in the peace and was made after certain agencies—and we were one of them—raised objections to the fact that the information could actually be held outside Australia. If you go back to 1997 there was a lot of discussion about the fact that the cheapest places around the globe to hold data were in some of the operations being established in Malaysia and so on.

So there was an issue there. That was addressed but the reason it was not addressed at the outset was that most agencies were not even involved in the consultation process about the original cabinet submissions. So we did not have a chance to be heard on the first round. We were faced with, 'Here is a decision. It is a fait accompli. You will live with it.' When we asked, 'What about the following considerations?' we were told 'Well, the decision has been made.' So with a lot of this we were raising issues that I believe should have been considered at the outset in a proper process but simply were not. Assertions were made by people in Finance that within the US government, even in security areas, all this stuff is outsourced. Comments which were patently nonsense were just being thrown into the debate, because it was about getting the product outsourced; it was not about considering all the issues.

Senator LUNDY—Did you have any contact with representatives of the company Shaw Pittman Potts and Trowbridge?

Mr Broome—Yes, I think I did. There were two gentlemen present at a meeting I had at Mr Fahey's office with his chief of staff, officers of Attorney-General's and OASITO, who I think were from the consultants—that was how they were described. It was they who, interestingly enough, seemed to be the most concerned about no net cost component in the deal I was trying to broker. Eventually Finance admitted it was a reasonable thing to do. That was the only contact I can recollect having with them.

Senator LUNDY—You say they expressed concern about no net cost. Were they contending at that meeting that it was unreasonable to claim that there be no net cost by engaging in this process?

Mr Broome—They were contending that by definition, as far as they were concerned, the bureau service that DAS had provided was not provided at market cost, that it was cross-subsidised—they could not specify how, but they asserted that it was—and, therefore, to maintain the same costs would have continued the subsidy and it would not have represented a market price. Yet at the same time the assertion was that in-house systems are inevitably, intrinsically and absolutely over the top in terms of their cost structure and they could not possibly be as efficient as the private sector model. So they had it both ways.

Senator LUNDY—It was contradictory.

Mr Broome—Yes.

Senator LUNDY—There are still quite a few points I want to go through, including the issue of ministerial involvement. You have just described a meeting that occurred in the minister's office. Was the minister present?

Mr Broome—No.

Senator LUNDY—Was Minister Fahey's chief of staff present?

Mr Broome—Yes, and the Attorney-General's chief of staff.

Senator LUNDY—Can you describe to me the purpose of that meeting at that ministerial chief of staff level and why, if there was a process that had a multitude of committees to handle the negotiations, you were actually in the minister's office with the respective chiefs of staff discussing this with consultants present? What was the issue?

Mr Broome—And departmental officers were also present. The purpose was quite simple. It was to try to resolve the impasse. The impasse had arisen because the Attorney-General agreed that the concerns we had were concerns that should be addressed. There was an exchange of correspondence with the minister for finance. It was in the course of these exchanges of correspondence that this meeting was held in an endeavour to resolve the impasse—that is, I was supposed to roll over and die. That was the purpose of the meeting. It was fairly forthright, but I can give as good as I get, so that was fair enough. There was in fact a subsequent discussion with some of the same players. There was a telephone conversation just before the contract was signed where I was also being told, 'We know what the deal was but the deal is now changed. DSD has said the security is adequate so therefore the contract will go ahead and you will be part of it—end of story.'

This was seen, and quite properly so, to be a major government policy initiative. My objections were perceived—I think wrongly—to be somehow an attack on that policy. It was really an attack on the process, not the policy, but people were very committed to getting the outcomes. So to get part of the resolution that was being sought it was elevated to the level of getting ministers' staff involved. That is the way these things are done. I have been through that in various roles over various years, both as a departmental officer and as in fact somebody working for a minister, so I know how it is done. I understood what was going on. It was an attempt to try to work a solution out. I was not prepared at that stage of the process to give up on the views that I had, but that was the purpose of it—to see whether we could crash through

and get a resolution, which in fact did not happen. There was an exchange of correspondence and there was an agreement reached as to what the preconditions would be to the NCA's involvement. In my view—others will have a different view—those arrangements were not in it.

Senator LUNDY—In other words, the concerns expressed by the Attorney-General to the minister for finance were not, in your view, adequately addressed.

Mr Broome—No.

Senator EGGLESTON—I am interested in this question of data being held offshore. Do you have any evidence that that actually occurred, that this outsourcing process was held offshore?

Mr Broome—I have absolutely none. Indeed, the reason I raised it was that when the first decisions were being advised to agencies, one of the problems which was raised—I cannot remember who raised it but I think it was actually raised at a fairly senior level amongst agency heads—was that there seems to be nothing in these rules which says that data has to be held in Australia. The obvious question was asked, 'Is that part of the rules?' The answer was, 'No, it is not.' There was lots of discussion and as I understand it there was then a change.

There was no attempt to do that. I had a very basic concern about it being held offshore, as the only remedy was a breach of contract at the end of the contractual period if you wanted to get your data back. You may be dealing with a company which had no assets in Australia. If the data is offshore, what are we going to do to get it back—send out the gunboats? There was a fundamental question over where it was physically held. That is a valid concern.

CHAIR—Were you more concerned about that than security?

Mr Broome—There are two issues if it is physically held offshore. Using tax as an example, if you took the whole tax database and held it in Labouang, a free trade zone in Malaysia, and the contract was to run out in five years time, when the contract renegotiation commenced, the former contractor would have a very substantial advantage in the renegotiation process. He could say, 'You will take my price or I will keep your data.' We could argue that that is a breach of contract and there would be remedies for that, but where would that leave you? That was an obvious and practical concern. If the material is held in another country, there must be concerns about the degree of security that could be afforded to that information. That was my concern in Australia because we wanted to ensure both system and physical security.

Senator EGGLESTON—You said that later on you had a meeting in the minister's office with the chiefs of staff of the Attorney-General and minister for finance and you said that the Attorney-General had apparently agreed that your concerns about security were legitimate. How did the Attorney-General know about your concerns? Had you written to him?

Mr Broome—As an agency head under his portfolio, I had raised the issue with him. I had made submissions about our concerns. I said that we believed that they should be handled in a particular way. As I recollect, I had discussions with him and his chief of staff, and there was general agreement that I was expressing a reasonable point of view. The Attorney-General certainly thought that it was sufficiently reasonable to write to the minister for finance proposing that those conditions be accepted as the criteria for our involvement in the contract.

He certainly thought that I was not being unreasonable. That was not a view shared by Mr Fahey or his staff and hence the disagreement.

Senator EGGLESTON—I see. Are you aware of any subsequent role of the Attorney-General or his department in this matter?

Mr Broome—The Attorney-General and his department were involved in this exercise up to the final signing of the contract, because there was still a lot of toing-and-froing in the last two or three days. It is a reasonable representation of what occurred to say that, despite my concerns, I needed to be satisfied about adequacy of security in relation to the agreement; it was my judgment call and no-one else's—and that was a view that he had been prepared to back. However, at the end of the day I was told that, because DSD had signed off on the deal in what I still regard as an interesting way, I could therefore have no reasonable objections—and therefore I could have no objections—and therefore all the preconditions had been met. The deal went ahead and we were regarded as part of the contract.

To make sure that we were part of the contract—and this is critical—you need to understand that the department of finance had become the custodian of the computer system we had been using until July 1998. When DAS was abolished, the administration part of admin services went across to finance and administration and the bureau service went with it. There was an MOU between the NCA and admin services for the provision of those services. About a month before the new arrangements were due to come into force, I wrote to the secretary of finance and told him that he was now the occupier of the other half of this arrangement. I said that I was not satisfied with what was being proposed. I asked him whether he would honour the agreement we had to continue to provide those services and the answer was, 'No, I will not. The switch will be turned off on 30 June.' In other words, we had no option but to go down the track of the contract. That was the way it was finally made sure that we had to transfer because plan B did not exist. My concern about this as a process is that when you have an apparently independent office of asset sales which is, in fact, nothing more than part of the department of finance, in a legal sense, and the department of finance as a service provider seeking to achieve one outcome, then you are not going to get an independent objective analysis of user needs and so on. There were other games being played.

Senator EGGLESTON—You mentioned tax records, which implies the Australian Taxation Office might have had concerns. Is that the case or not?

Mr Broome—I do not know whether Michael Carmody had concerns. Bear in mind that the tax office was going through, at this stage, its own total revamp of its computer system. The figure of something like $700 million was involved so, in a sense, it was not part of it. But it was tax type information that I would have thought was an issue. It was information held by Centrelink and a whole range of government agencies you can think of that involved sensitive personal information to which the same issues applied that I was concerned about. That is not to say that you cannot outsource the equipment; I am not saying that one bit. I am saying that if you do outsource it, you should make sure that you have very adequate control over the data. You should have adequate arrangements for getting the data back and, in particular, I thought that some of the contractual remedies were inadequate protection if there was wrongdoing.

You all know, as politicians, that if in an outsourced situation personal information from, say, the Health Insurance Commission found its way into the public domain there would be hell to pay. The fact that you could sue the provider for damages is no remedy. The public could say, 'So you can get paid two and sixpence for my personal information.' That is not a remedy. This is one of the fundamental problems with using a contractual framework to protect this kind of material. What is, in fact, the appropriate remedy? It is very difficult to conceive how you can do that in a contractual sense.

Senator EGGLESTON—Thank you.

CHAIR—Earlier on you were referring to both DOFA and to OASITO. Can you outline for us how you see the role of both those agencies in this whole process?

Mr Broome—As I understood the role that they were supposed to perform, DOFA was the policy development area, the department of state that had the role of advocating the outsourcing policy and OASITO was established as the body to do the work—a distinction that could be drawn between the policy and operation. But the reality was that you had DOFA being a provider of services at the same time. You had the fact that while these bodies were generally seen to be, and acted as if they were totally different entities the staff of OASITO—and I may be wrong about this—are, in a formal legal sense, staff of the department of finance and, constitutionally, they have to be. You are either a member of staff of a department of state or of a statutory authority, and there was no statutory authority. You really had this false dichotomy between two entities. It seemed to me, when issues like disputes arose, the classic example was when the contract did not provide who would pay the cost of security vetting for staff. We refused to pay and the contractor refused to pay. In order to make sure the deal did not collapse on day one the department of finance, as I understand it, paid the vetting cost. I think there is a convergence of roles and functions in all of that that is perhaps not desirable.

CHAIR—Have you had the opportunity to look in detail at the Humphry report and the government's response to that?

Mr Broome—No, I have not. I am generally aware of the thrust of it. Certainly, from a number of comments that I noted Mr Humphry raised, he seemed to accept that security was a genuine issue. I felt that a number of his conclusions seemed to support the view that I expressed. In terms of the government's response, it seemed, as the minister has said, that the review was in fact a vindication of the policy. I just have some difficulty reconciling Humphry's conclusions, as I understand them, with that comment. I do not think they were vindicating; I think they showed that there were some substantial issues, as indeed I think the Auditor-General's report did.

CHAIR—In terms of budgetary savings, what sort of input did you, as an agency head, have into that process?

Mr Broome—When the initial savings were being determined?

CHAIR—Yes.

Mr Broome—None.

CHAIR—None at all? So you were just given a figure and told, 'This is a saving; this is what you've got to generate'?

Mr Broome—'This is the calculation that's been made and it's coming out of your bottom line.' It was not a huge amount of money so it was not going to make or break us, but in the case of other agencies it was very much larger. Talking to other agency heads, I think that, for some of them, there was a very genuine concern that—

CHAIR—Do you acknowledge that the same process occurred with them?

Mr Broome—Yes. I do not think we were given any special treatment. I think they were all given the same treatment.

Senator LUNDY—When you made your submission to the Humphry review—and I know that you asked that it be treated in confidence—did you specifically request that your submission not be listed on the list of submissions that Humphry then notified publicly in his report?

Mr Broome—Absolutely not.

Senator LUNDY—But you did ask that your submission remain in confidence?

Mr Broome—I do not know that I said that in the covering letter to Mr Humphry. You should have a copy of both the submission I sent to him and my covering letter.

Senator LUNDY—The structure of the submission is that the submission itself and the letter are one and the same.

Mr Broome—Yes, and I did not, at any stage in that—

CHAIR—Your introductory remarks did not appear to draw any reference to confidentiality.

Mr Broome—No. I did not ask Dick Humphry to treat this confidentially. I was happy for him to use it—I did not know whether or not he would—but I certainly did not ask that it be treated confidentially, nor did I ask for it to be returned, and I was quite surprised when it turned up in the mail.

Senator LUNDY—Were you surprised, or did you subsequently query with Mr Humphry why your submission was not listed in the Humphry review?

Mr Broome—No.

Senator LUNDY—So you had no other contact with him.

Mr Broome—He did not contact me following lodgment of the submission, nor did any of his staff. The only sense I had of what had been dealt with in the submission was essentially

getting the original back and finding the highlighting, which I found quite interesting and which is why I thought I should send you the original because it does not photocopy.

Senator LUNDY—Going back briefly to the issue of Shaw Pittman, you raised doubts about the capability and expertise engaged by OASITO with particular reference to consultants. This morning you have already mentioned what seemed to you to be contradictions in the advice they were providing. Can you provide any specific examples as to what fuelled your doubts about their competence or capability in providing advice to OASITO or, indeed, as part of the process?

Mr Broome—As I understood it, they were effectively an American law firm. I was not sure whether they had been engaged to provide legal advice to the Commonwealth or whether they had been engaged for some other purpose. They seemed to have been given a much broader brief, and I guess my initial reaction was, 'What's the expertise of a US law firm in IT outsourcing of government activities?' That was the first question. The second question is that, if they are going to be the ones providing advice on contract, I would have thought it would have been desirable to have an Australian legal capacity involved. To be fair, I understand there was in fact a subcontract, or a second contract, let and one of the major law firms did get involved in the drafting of the contracts. That is why I was surprised at the quality of the product.

Senator LUNDY—At the advice that Shaw Pittman were providing.

Mr Broome—The quality of the contract in particular. I would be very surprised if any reasonably good commercial lawyer would have signed off on it. From my brief contact with these people I just was not sure what they were bringing to the table. I have to say that, with the discussions at which I was personally present, the people who I think were from Shaw Pittman seemed to be there as advocates of the policy and not as advisers on the issues.

Senator LUNDY—On process?

Mr Broome—On the process. They were there trying to take me head-on about my concerns. That was more so in the context of 'Why are you trying to undermine what is going on here?' I was saying, ' I am just trying to get some sensible results. You tell me on the one hand that this must produce savings; you have already taken them off me, but you do not want to even commit on paper to the fact that this will not cost us any more money.' They were quite strong advocates in that discussion.

Senator LUNDY—Okay, I think I have all I need there. I have a couple of other points. About your responsibilities under the financial management act, you expressed concern in your submissions today and to the Humphry review, that you felt, that despite that act determining that you were the responsible party, you were disempowered and not able to effectively make the decisions that you were statutorily responsible for. Did you specifically raise that concern that with your minister, the Attorney-General?

Mr Broome—I am sure I made that point in the submissions that I put to him, but I cannot say categorically I did because I have not gone back and looked at them. It is certainly a concern that I have had. Let me say on the other side of it that I do not take the view that

statutory authority heads sit there and are answerable to no-one. As Senator Campbell knows from another life, I have a very strong view about our accountability to the parliament; I have a strong view about our accountability to government. The government had every right to determine a policy about outsourcing. I will defend its right to do so whether I think it is good or bad. My concern is that, within a policy framework, you have to be able to let agency heads exercise their legal responsibilities in ways which they feel are consistent with those responsibilities or at least address them in some way. You cannot just say, 'You will carry the can, but we will make the decisions anyway.' That is my basic concern.

Senator LUNDY—Are you familiar with the recommendations from the Humphry review?

Mr Broome—I have not been through them in detail.

Senator LUNDY—Okay. The first three recommendations relate to the responsibilities of chief executives and boards in accordance with the FMA and CAC acts. If you are familiar with them, are you satisfied that that acknowledges your concerns and will resolve the issues about the ability or otherwise of chief executives and chairmen of boards of statutory authorities to actually take control and make the appropriate decisions with respect to future IT outsourcing?

Mr Broome—I will take that on notice and have a specific look at each of those and provide you with some subsequent comment if you like. I think we have to be very careful that we do not try to get into a situation where we become so prescriptive that there is not some sensible capacity for discussion. What we sought to do in this exercise was to raise genuine concerns and have them accommodated. It was not a question of take the NCA out of the process; it was, 'Let's see if we can meet our concerns.' I thought that the problem was that there was no recognition that these were even genuine concerns. There was an ideological debate that was created. I was supposed to be totally anti-outsourcing by definition; they were all for it, hence, never the twain should meet. In fact, I believe it was all about satisfying my legal responsibilities in a way which was consistent with the policy. I think that is the way you meet those challenges. You do not just sit there and stand on your dig and say, 'We won't be in this.' You have to have rational argument and you have to take it through and debate it.

Senator LUNDY—Do you believe that, had the minister's office not got involved, the NCA would have found itself in a position of having to participate in cluster 3?

Mr Broome—Yes, because the department of finance would have acted the way that it did, and that was irrespective of any involvement from Mr Fahey's office, so that we would never have had an alternative capacity come 30 June. We would have been just taken off the machine, as other agencies were.

Senator LUNDY—Thank you.

CHAIR—Thank you, Mr Broome.

[10.05 p.m.]

BOSHIER, Mr John, Chief Executive, Institution of Engineers, Australia

YATES, Mr Athol, Senior Policy Analyst, Institution of Engineers, Australia

CHAIR—I call the meeting to order and declare open the sixth public hearing of the Finance and Public Administration References Committee inquiry into the government's information technology outsourcing initiative. I welcome my Senate colleagues and witnesses. Before we commence, I wish to advise for the record that all witnesses appearing before the committee are protected by parliamentary privilege with respect to evidence provided. The committee prefers all evidence to be given in public. However, you may at any time request that your evidence or part of your evidence be given in private, and the committee will consider any such request. I point out, however, that evidence taken in camera may subsequently be made public by order of the Senate. I also remind witnesses that the giving of false or misleading evidence may constitute a contempt of the parliament. I now invite representatives from the Institution of Engineers, Australia to the table. Do you wish to make an opening statement?

Mr Boshier—Yes, I do. Good morning, Mr Chairman and senators, and thank you for the invitation to join you this morning. The Institution of Engineers, Australia is an association representing 60,000 members of the engineering profession. Of the Australian-based practising engineers, about 25 per cent work in the public sector and 75 per cent in the private sector. So contract management in the Australian Public Service is a significant issue for our members in both sectors, because government engineering contracts are mostly delivered by the private sector.

Over 8,000 or 14 per cent of our members practice in the communications, computing, software and electronics engineering industries. Improving the contracting process increases the efficiency and effectiveness of the public sector. It also reduces the cost of government and aids the development of Australian industry and encourages private sector innovation if the government is an informed buyer. The institution is interested in the IT outsourcing initiative, because so many of our members are directly involved in this industry and they have learned lessons that we wish to convey to this committee.

To ensure that governments get value for money for their outsourced IT activities, it is of critical importance that government is a smart buyer of IT goods and services. Being an uninformed buyer puts at risk the ability to select and justify an innovative option which offers best value for money; it puts at risk the ability to reduce contractor risks, and therefore price, by providing relevant technical details in tender documents; and it makes it more difficult to prevent unscrupulous contractors taking advantage of the buyer's lack of knowledge. This issue is not only relevant for IT procurement but also applies generally to engineering and professional services both in government and in the private sector. We produced a report in the year 2000 called *Government as an informed buyer*. It identified the cost of being an uninformed purchaser based on a series of failed contracts. More recently, we published an indicative survey to identify the cost and frequency of inadequate IT contracting practices based on a survey of government and private sector IT professionals that are contracting to government. This survey forms the basis of our evidence to this inquiry and has been given to you.

Mr Chairman, thank you for the opportunity to discuss these issues with you as a means of ensuring that the benefits of outsourcing are realised. Athol Yates and I both look forward to the discussion.

CHAIR—Mr Yates, do you want to add anything?

Mr Yates—No, I do not.

CHAIR—Could you, Mr Boshier or Mr Yates, briefly describe to us the background to your survey, its methodology, its key findings and recommendations?

Mr Boshier—Mr Yates was the author, so I will defer that question to him.

Mr Yates—The survey was completed late last year. We surveyed members of the Australian Computer Society and members of the institution, so they are professionals in the area of IT. The major findings of it were that, according to the industry respondents to it, they considered that the government was below average in being an informed buyer for 32 per cent of contracts. We asked the same question of the government contracting officers, those actually involved in the procurement activity from the government's perspective, and they said it was lower but it was still 24 per cent. So that indicates that between a quarter and a third of all contracts are examples of where government was not an informed buyer in the procurement of IT.

The survey found that 42 per cent of industry respondents would charge a hedge if they considered that the customer did not know what they actually wanted. This hedge would be between five and 50 per cent of the final contract price with the arithmetic mean being 21 per cent. So that is basically in 42 per cent of the cases where the government is not an informed buyer, according to the industry, they would charge a premium. According to the government contracting officers, in about 10 per cent of all contracts, the winning tender was based on the lowest upfront cost rather than overall value for money. The industry believed that this figure was actually low and it should have been closer to 27 per cent.

When the survey asked the government IT officers, 'How did you rate the competencies of the IT contractors?' Twenty-eight per cent believed that their own rating system for the competencies of the contractors was below average. Two more findings of significance were that the industry IT professionals stated that, in about 18 per cent of contracts, the RFTs were below average in that they did not provide the required information. When we asked the government respondents, 'Did you think that the private sector providing the information were an informed seller?' So this is the reverse, it found that in about 23 per cent of contracts the industry was not an informed seller.

CHAIR—Thank you for that.

Senator EGGLESTON—I do have some questions about your survey. Do you understand the difference between government contracting of IT and IT outsourcing?

Mr Yates—Are you referring to the outsourcing initiative or just outsourcing?

Senator EGGLESTON—To the outsourcing initiative, yes.

Mr Yates—Yes.

Senator EGGLESTON—Is it not a fact that contracting involves much smaller contracts over a much shorter time whereas government outsourcing involves contracts worth many millions of dollars over a much longer time, and the two things really are not the same?

Mr Yates—The IT initiative was a series of very large contracts—

Senator EGGLESTON—Indeed, it was.

Mr Yates—You can have outsourced contracts or contracted-out activities that are both large and small in terms of dollars.

Senator EGGLESTON—But IT outsourcing, as I understand it, is specifically about infrastructure, which means hardware, whereas contracting is really about software. They are very different things.

Mr Yates—With respect, no, I do not think that is correct. Your IT outsourcing can include hardware and software. Most contracts are on the end-to-end basis and provide networking, provide hardware, provide maintenance of legacy systems—all of them have components of both software and hardware.

Senator EGGLESTON—You put out a press release when you released the survey entitled 'Engineers survey highlights the need for more expertise for government IT outsourcing'. Do you think that title was an accurate representation of the substance of the survey or not?

Mr Yates—The survey's title is 'Quantifying the cost and frequency of inadequate IT contracting practices by government'. The press release—it was an issue of semantics. The outsourcing we are referring to there was not the outsourcing initiative; it was outsourcing per se, which we see as a subset of contracting. So it is a semantic issue.

Senator EGGLESTON—So in effect you are really talking about contracting rather than the outsourcing initiative; that is really what you are saying, is it not?

Mr Yates—Absolutely. It is all about IT contracting.

Senator EGGLESTON—Would you agree that, in those circumstances if it was about contracting rather than about the IT outsourcing initiative, it was fitting that the minister's office brought to your attention that the media release did not accurately reflect the survey?

Mr Yates—Again, I say it is a semantic issue. He interpreted it to mean that it was referring to the IT outsourcing initiative. It is about outsourcing as a subset of contracting.

Senator EGGLESTON—And this committee's inquiry is about the IT outsourcing initiative, not about contracting. Would you agree with that?

Mr Boshier—I would like to make a comment on that, Sir. I was involved in those discussions with the minister's office. You are absolutely correct that our survey is not politically motivated in any way. We are concerned in general terms about the perceived run-down of government's access to engineering expertise and the cost that that is having to our profession and to the success of engineering ventures in general terms. A lot of our members are involved in the IT industry, so Athol broadened his inquiry to look at IT contracting. The report makes it quite clear that it is not involved in IT outsourcing; it is involved in IT contracting. You are quite correct that IT contracting is a subset of the IT outsourcing initiative. The minister's office was quite sensitive to this and requested that we change that word in the tittle, which we did.

Senator EGGLESTON—Yes, I understand that.

Mr Boshier—So the press release that went out—I have it in front of me—dated 17 January 2001 was called 'Engineers survey highlights need for more expertise for government IT contracting'. That was the media release that was used. Sir, we have been quite careful to not comment politically on the IT outsourcing initiative. The source of our evidence to you, the reason we are here, is that we believe that the survey we have done on IT contracting has something to say about the IT outsourcing initiative. We believe there are some interesting lessons, but obviously we do not want to comment politically in any way on the IT outsourcing initiative.

Senator EGGLESTON—Just for the record, I understand that IT contracts, which you are referring to, have a median value of about $1.2 million and the contracts are over a two-year period; whereas, in the case of IT outsourcing, the value of the contracts is worth hundreds of millions of dollars and the duration is over five years. They are really very different things. You talk about your survey, and I would like to go to page 21 of your submission where you have a section on the validity of the survey results. Do you have that page?

Mr Yates—Yes, I do.

Senator EGGLESTON—I just refer you to paragraphs 3 and 4. I will read those two paragraphs for the record and ask you to comment at the end. Paragraph 3 states:

> A total of 111 responses were received giving a response rate of 5.3%. 80 responses were received from those working on behalf of the government and 31 for those contracting to the government.

Paragraph 4 reads:

> There are three uncertainties in the survey results. Firstly, the number of survey responses was small which may mean the results may not be statistically representative of the population. Secondly, the questions require value judgements, which may mean the results may not reflect reality. Thirdly, the questions require individuals to rate their own projects, which may mean the results are biased. These uncertainties mean that the results cannot be categorically said to be representative of all government contracts.

Would you like to comment on that in terms of the value of this survey to this meeting today?

Mr Yates—I would be delighted to talk about this. Firstly, let us take the low response rate. This has been highlighted in the minister's press release and I think that indicates a lack of understanding of statistics and sampling techniques. I know they are focusing particularly on

the raw numbers, so before I came I looked at my shelf for a number of survey reports and I brought along one called *Information technology outsourcing practices in Australia*, a joint report prepared by Deloitte Touche Tohmatsu, the University of Oxford and the University of Melbourne. The report came out early this year. It refers to this report being a:

landmark study ... expected to be the first point of reference for information on IT outsourcing in Australia for some years to come.

If we turn to the data on which this is based, it says that part 2 of the survey was focusing mainly on problems in various stages of IT outsourcing processes, contracting issues and some big picture issues on the state of IT outsourcing practices in Australia and that, 'After one follow-up letter in April, 78 responses were received.' That was in 2000. These 78 responses form the basis of the detailed analysis here. They maintain that it is valid, and I have looked at the data and I believe that it is valid. It is valid because of the sampling technique. The raw numbers do not have a great deal to do with the validity of a survey.

Senator EGGLESTON—You must have done a different course in statistics from me, I think. You had 5.3 per cent who responded of 2,020 sent out. That is really a very inadequate result to draw broad conclusions on.

Mr Yates—The population on which this is based, if you read further, indicates that their response rate was artificial lowered because of the failure of identifying the sample population. The reason for this was that the Australian Computer Society could not identify those who were involved in government contracting practices—and we had some problems, too, with that because of the narrow definition—so we had to send it out to all IT professionals in Canberra. As I say in the following paragraph, I am confident that the results are reasonably reflective. The same survey that we did earlier in the year went out to the engineering profession as a whole. Because we could target it, we got a response rate of 15 per cent, which is pretty reasonable. That is the response rate we would have got had we been able to target this survey more appropriately.

I will now go into the second issue: the uncertainties here. The questions require value judgments. You tell me what survey does not require value judgments when you have to put a rating on something.

Senator EGGLESTON—These are your comments, though. You said that the value judgments may mean that the survey does not represent reality. You have put these qualifiers in.

Mr Yates—Indeed. It is my responsibility as a professional working in this area to state what uncertainties there are in it. I am not in the game of trying to make up results and then hide information from the readers to allow them to interpret it. I am stating that these are the facts—these are the uncertainties in it—as I am stating the sample population and the response rate.

Senator EGGLESTON—But in effect you are saying your survey results may not be worth anything.

Mr Yates—No, I am saying what the uncertainties are.

Senator EGGLESTON—In other words, they are not related to actual events. That is what you are saying.

Mr Yates—No, I am not.

Senator EGGLESTON—It may not reflect reality.

Mr Yates—You tell me what survey does not state the uncertainties in it. Any quality survey will say why there may be some problems.

Senator EGGLESTON—What you seem to be saying here is that you only got a five per cent response and the survey results are not reliable or real and that they are biased.

Mr Yates—No, I am saying that these are the uncertainties in it. If you like, I can provide an uncertainty percentage in it or I can provide a degree of probability of reliability of the figures. It does not matter how you do it; I simply chose to do it in written words. Normally you see a plus and minus and a probability rating.

Senator EGGLESTON—Yes, I agree with that.

Mr Yates—This is just a verbal way of doing it. Let me refer to the last uncertainty, which is that the individuals are required to rate their own projects so the results may be biased. Yet again, anybody who has a direct interest in something is always going to have their perception of it shaped by that, unless they are a completely objective person. But, again, we are asking somebody to rate something, so of course there is going to be uncertainty or bias in that. That is inherent in the very nature of asking a question.

Senator EGGLESTON—I must say again that—

Mr Boshier—I would like to make an additional comment, if I may. Senator, I think what you are doing is trying to overturn the entire results based on the low sample size. That seems to be where you are coming from. I put it to you that really what you should be doing is questioning the error bands on the numerical answers which Athol has provided to you. What I think he is saying as author is that those error bands may be fairly large.

In other words, our answer may be 21 per cent of premium—that is the hedge—plus or minus a large number. We know that the answer we got is between five and 50 per cent, with an arithmetic mean of 21 per cent. What we are saying here is that the error bands may be large. I do not think it is valid to draw the conclusion that the entire results can be overturned and are of no value.

Senator EGGLESTON—I come from a background in an area of science where statistics are used a lot too, and I think that a survey which had a five per cent response and has error bands as large as you are referring to is of very dubious value. I will leave it at that.

Senator LUNDY—I am interested in the substance and findings of your survey, and I want to indicate my concern about the challenge to the validity of the survey. It seems to me that it

was quite a timely analysis on an issue that, in various ways, is related directly to the policy challenges faced by the coalition government with respect to their IT outsourcing. I would like to ask you about some of the extrapolations of the findings contained in your submission, particularly with respect to contracting expertise or sourcing expertise from outside of agencies or departments. You have highlighted various advantages and disadvantages, and I would like you to make some comment on the ability within agencies and departments to retain not so much the people with the IT skills per se but the actual contract management skills that accompany an outsourcing exercise, where the skills may be sourced outside of the agency or department. How important is it in the view of your members—who are the actual IT skills people—to have that relevant contract management expertise within agencies and departments?

Mr Boshier—That is very perceptive. Again, can I emphasise that we do not wish to comment politically on the IT outsourcing initiative but, having said that, we do offer some comment. These are comments that are made to me in my role as chief executive, I suppose. Firstly, the issue that you are asking about is retaining contracting skills inside the agency and how difficult that is. A subsidiary question, of course, is about the IT expertise itself.

Senator LUNDY—Yes.

Mr Boshier—The difficulty is the market in operation. IT is an exploding industry and it is estimated that knowledge is doubling every two years in this industry, if not more often. A new computer comes out every 18 months with an almost double clock speed. Therefore, there is a shortage of skills in the industry. The government has addressed this issue in several fora and we applaud these efforts, not the least of which is the innovation package. As a result of this situation, the market is paying a premium for people with contracting skills. In fact, it is paying a premium for people with IT skills. Therefore, people with contracting skills are in high demand.

Naturally—and you might hear this later this morning—a company wishing to protect itself and to make a contract work is prepared to pay good money for a person skilled in IT contracting. They will, generally speaking, outbid or offer pretty attractive remuneration for a person with those skills. In my view, the government is struggling a little bit to retain people with sufficient technical expertise in IT contracting. There are two skills involved: one is the legal project management skill, and we have not detected a lot of shortage in government in that area. Where we have detected a shortage in government is in the technical IT contracting skills. That is the bottom line answer to your question.

Senator LUNDY—Still talking about those with the skills to manage IT contracts, how important is it for those people to have that ability to be objective when it comes to a technical assessment of what is being sourced? I will give some examples—issues like the capacity of technologies, for example software, to be operable on different IT platforms. It is that kind of technical issue, so it is about what software is compatible with what hardware, what potential there is for interoperability perhaps at the next phase of development for the technology. Do you see where I am coming from?

Mr Boshier—Senator, I am not sure that it is a question of being objective. In my experience, I have not found people who are terribly unobjective. I do think it is a question of knowledge, though. As I was saying, the knowledge is increasing so quickly that a person maybe has

intimate knowledge of one platform but not so much of another emerging one. So you tend to use what is familiar to you and what you know rather than what you do not know. I think the trick is to try to find people who have got a very catholic knowledge, an all embracing knowledge, of all the platforms. No, I have not detected what you are saying as actually being too much of a problem. Athol may have a different perspective.

Mr Yates—The issue here is that the team involved in the IT contract must have the subject matter expertise and the contracting expertise. With the downgrading of the importance of having procurement competencies as a mandatory requirement for contracting officers, that may have reduced the incentive for people to get contracting procurement qualifications. With respect to the issue of subject matter expertise, which is obviously critical, a lack of subject matter expertise has been a contributing factor in a number of recent disasters. In the area of IT, the figures for the reduction in the number of IT officers in the Public Service indicates that the lack of subject matter expertise may be of significance. Let us not forget that the reason we have not focused on subject matter expertise in the past has been because governments have had this, so they focused on improving the procurement side of it. Now we have had such change in the composition of the APS over the last decade that maybe we have neglected focusing on the subject matter expertise side of it.

I also draw your attention to the fact that Humphry did refer to this issue of lack of IT expertise. It has been highlighted by some agencies as a contributing factor to the difficulties in implementation. The ICAC report released earlier this month found that a manager in charge of a large IT project on behalf of the New South Wales rail corporation, because of his lack of knowledge, allowed a fraud to occur. An audit report of the tax office last year revealed that the risk of fraud had increased through outsourcing IT system functions, and that the office had not monitored these arrangements. Again, I think we are seeing that a lack of subject matter expertise is contributing to a number of difficulties with contracts.

Senator LUNDY—How does that lack of subject matter expertise emerge with respect to your survey? Is it an issue that was covered in that survey? I am trying to clarify how that issue is related to a perception by industry that government, at least in a percentage of instances, is not an informed buyer. Do you think it is directly related?

Mr Yates—It is absolutely fundamental. The nature of being an informed buyer refers to the subject matter expertise. We were not looking at the procurement competencies. That was completely different. This was simply looking at the technical expertise. We asked questions such as, 'Did you believe that you had the required subject matter experts on that contract? Did you have the adequate input of technical expertise?' So it was purely focused on that, because that is our interest.

Senator LUNDY—That is what I wanted to clarify. In evidence to date we have heard about the IT outsourcing program specifically. I appreciate the points you make about this survey applying to IT contracting generally, but we have heard that many agencies and departments not only found themselves in a position of not having the expertise necessary but also were not allowed to make decisions for themselves. The decision making process for those contracts under the IT outsourcing program was handled by another agency, in this case Finance, through OASITO. Do you think that is a contributing factor in your survey's analysis, or are you able to maintain that it might be symptomatically related but not particularly captured by your survey?

Mr Yates—Let us remember that the IT outsourcing initiative has a small number of contracts but, under that, there are dozens of other contracts.

Senator LUNDY—That is my point. I do not accept Senator Eggleston's assertion that there is a big difference between all these small contracts that your survey obviously captures and the huge IT outsourcing contracts that are worth hundreds of millions of dollars, because there is a multitude of subcontracts within them. I am working from that premise, and I want to clarify that. But my question still stands: do you think that the perception by industry that the government is an informed buyer has been fuelled or enhanced by the way the program is structured to effectively take away the decision making abilities from agencies and give them to the department of finance?

Mr Boshier—I am not sure that we have enough statistical or explicit knowledge from this survey to answer that question. One would have the thought that in theory, so long as any agency had access to technical expertise, it would not matter which agency was managing the contracts, provided it had enough access to expertise. In our submission all we are saying is that, by and large, an agency that is responsible would be expected to have more access to expertise than, say, the Treasury. But I would offer that that is only hearsay. Our sole concern is to make sure that, when you write a contract, you have good access to technical expertise whether or not you are in the Treasury or in the core department.

CHAIR—You are not necessarily arguing that that expertise has to reside within the agency?

Mr Boshier—No. It could be a consultant as long as that consultant is on tap, available and retained properly, with the right terms of reference and enough authority to get into the works and tinker with them properly. We are not advocating against privatisation. In fact, we are in favour of it so long as you have access to technical expertise and it is carefully protected.

CHAIR—This is a follow-on question. The set of circumstances that applied previously under the IT outsourcing will probably apply in part under DOFA. Do you see the introduction of a third party sitting between the agency that requires the services and the provision of that expertise enhancing the process or taking away from the process?

Mr Boshier—My view is that the interpolation of that third party would not assist the retention of technical expertise; it would tend to dilute it. There may well be cases in which, for other reasons, you want a third party involved, maybe to force the pace or that kind of thing. But in introducing that third party I think your inquiry should focus on whether the third party had sufficient technical expertise to carry out that job. Athol may care to comment on that.

Mr Yates—I will comment on that and also on Senator Lundy's previous question. Humphrys, in his report, referred to a dominance of legal and contracting issues associated with the signing of the contracts. There was not any mention of the technical teams that were involved in each of the individual contracts. Secondly, to find out the answer to that question you would have to talk with OASITO about the priority that was given to the technical assessments of the teams that worked up the contracts. I have only anecdotal information on that, which I do not think it is appropriate to discuss here.

With the transferring of responsibilities for the contracts to agencies for the contracts, provided the agencies still have the internal expertise or they can obtain consultants to represent their technical best interests, it may lead to a more appropriate balance between legal, technical, procurement and other issues associated with the contracts.

Senator LUNDY—Mr Boshier, following up on that issue of where you source the expertise, you said that that expertise does not necessarily have to come from in house, as long as it comes from somewhere. Do you have a view as to the validity or the credential of advice if it is sourced externally from the private sector in the form of consultants and/or legal firms? Do you have a view, or are you able to reflect a view of your membership, as to the relative quality of that advice compared with advice that has previously been afforded in house or through the public sector?

Mr Boshier—We could spend a day talking on that topic. It is a huge question. Do not forget that many of our members are consultants and are in the position of offering advice. Let me first offer a personal view. I was chief executive of an electricity supply company. You have to be quite careful about advice offered by consultants in the sense that sometimes the consultant is not entirely impartial about the advice that they themselves are offering; in other words, there may be succeeding work that is contingent upon the first advice that is being offered. The consultant does not necessarily want to torpedo the chances of having future work. That is the first thing I would say.

The second thing is that, for a person to be able to offer impartial advice to the chief executive of a major company or of a major government department, it really helps for that person to be in house in the sense that that person can speak without fear or favour and can give decent policy advice to the chief executive or the secretary of that department. Therefore, I feel that it is important to retain sufficient expertise in any privatisation or contracting out or, at the extreme, outsourcing exercise. You can always audit the process as it goes and be absolutely sure that you are getting what you paid for and what you want. There are break points where you can stop the process and say, 'We're not happy with the way this is going. We are going to audit it to make sure that we are getting what we want.' Having said that, by and large I have not detected any systemic fault in the advice that consultants or contractors offer. There is nothing that has leapt out at us to say, 'There is a conspiracy going on here.'

I will answer a question that you have not actually asked but which is relevant. An area that I personally would say would be very difficult to contract out or, at the extreme, outsource would be where that activity was a core competency to that organisation—where that agency was not involved in writing all the code, in doing the modelling and carrying out that function—such as parts of CSIRO and the Bureau of Meteorology. In areas where designing a model and coding it up is a core competency, it would be very difficult to contract out that expertise because you cannot really outsource a core competency.

Senator LUNDY—You have anticipated my question well, which was about the issue of strategic control, the direction of information and communications technologies within agencies and departments—that is, the degree to which it is core business and the degree to which it should be outsourced and strategic control lost within the agency. You have effectively answered that, but let me take it a step further. If you reflect on the range of IT contracting out of information technology, or indeed the outsourcing programs, are there any examples of

where—either in your view or in that of the institution or your membership—it has gone too far and there has been a loss of strategic control within the agencies and departments that has perhaps prevented them from achieving best practice?

Mr Boshier—Athol should definitely comment on this because he has his ear to the ground as well. Yes, I do have a strong personal view on it, and I think the institution has a view that to outsource a core competency area is by and large not in the interests of an organisation. You gain your credibility in the market, you gain your sales and you gain market share by core competency. To outsource that is to outsource your brain. However, we outsource all sorts of things we do in our personal lives. To carry that anecdote a bit further, you can outsource where you eat, to restaurants. You can outsource a lot of what you do, but to outsource the way you think is a big mistake. The areas that I have seen that would not be good for outsourcing, or for contracting out in a more micro scale, are those technical areas of government, which would certainly include the Bureau of Meteorology and CSIRO. Where IT processing is not core activity—in other words, it is the means to an end—there are companies out there in the market whose core activity is processing large amounts of data. It is their core competency. They are better at it than government departments and should be allowed to get on with the job, in my view.

Mr Yates—There is an issue associated with that. It appears that a number of agencies are hiring IT officers because they realise they have gone too far in outsourcing. These people are not employed to undertake the work but are more to do with contract management. I have tried to obtain these figures from the Public Sector Merit Protection Commission. The problem with it is that, since the banding together of various categories, specialists are no longer identified as an individual group. However, it would be very useful if there was consideration given to breaking down the collection of statistics so that we could check this rather than having to ask each individual agency. I have asked a few of them, and the answer I got was, 'None of your business.'

Going to your earlier point regarding the accessing of external expertise, one of the issues we have found in analysing disasters, and also from this survey, was that there seems to be a problem with assessing the competencies of contractors. They say that they can do this work. Something like 27 per cent of government respondents—that is, government IT officers—said that the quality of the assessment of the competencies of the tenderers was below average. That is very concerning because this is the same issue that came up with Bruce Stadium, the hospital implosion, and so on. It was worthwhile noting that the Auditor-General in the ACT government has stated in his analysis of Bruce Stadium that it is not acceptable for senior public servants to say they are relying on the advice of the external consultants solely. It is their responsibility to check this—not in detail but certainly the general thrust of it. I think that is one of the reasons why we are seeing more IT subject matter experts being brought in. It is not to second guess the tenderer or the contractor but certainly to provide some advice that is in line with the agency's directions and not in line with the contractor's perspective.

Senator LUNDY—That issue takes us to the question of transfer of risk from the public to the private sector by virtue of the existence of a contract. What you are describing to me is that, by virtue of an example like the Bruce Stadium issue in the ACT, the government found out the hard way that it was not possible to transfer the risk in public accountability or political accountability terms to the contractor. Is that a fair observation?

Mr Yates—Absolutely. You can try to contract out your responsibilities, but accountability still lies with the agency. There is no way that that should be attempted at all; it is just ludicrous.

Senator LUNDY—You made some comments in response to earlier questions about the minister's involvement following the release of your survey and the press release that accompanied that. Can you describe the way in which the Institution of Engineers was approached by the minister's office following the release of the survey and the press release and the subsequent action that the Institution of Engineers took and why?

Mr Boshier—We would like, as an institution, to have close contact with ministers offices and we believe that it is very important for us to keep ministers in touch with what we are doing. Therefore, we have close relationships. Being rung by a minister's office is entirely normal business for us. We made the press release public at an agreed time, but within a very short time we were rung by the minister's office, not by the minister but by the minister's staff, requesting that we change a word in the title of the press release. The issue is what Senator Eggleston raised, which is how we talk about outsourcing or about contracting. I sought advice and decided that we wanted to assist the minister and assist the minister's office and that we were happy to change the word in the press release.

Senator LUNDY—What was the word?

Mr Boshier—The word that we initially used was 'outsourcing'. The minister's office suggested that the survey was really about contracting and that the word should be 'contracting'. After thinking about it I said, 'Fair enough,' and changed the word in the press release. The interesting thing though was that the media got to hear about this. The reason they did was that the minister's office got in touch with the media. We then issued a clarification in the press release. We also made it quite clear what had happened and that our motive was solely to assist the minister's office and get our message out.

Senator LUNDY—You have gone to great pains to stress that the Institution of Engineers is independent, and I acknowledge and respect that. Why did you find it necessary, or why did you make the decision, to change the word on the basis that it assisted the minister's office? What interest did you have in assisting the minister?

Mr Boshier—That was the reason for my short preamble, which was that I personally, and the institution, like to have good and productive relationships with ministers. We feel that if we can help the minister's office and at the same time get our message out—we would generally bend over backwards to try to do that. The minister's office was not criticising or getting into the actual survey itself. They did discuss the validity of the survey a little. We gave them the answers which Mr Yates has given this inquiry and the minister's office was quite happy with that, but we did agree to change some of the words, just to avoid the perception that we were taking sides in a political debate.

Senator LUNDY—So it was effectively to help the institution preserve their relationship with the minister and the minister's office, to keep it on good terms. You took that action to preserve your good relationship with the minister's office?

Mr Boshier—That was our primary reason.

Senator LUNDY—Can you detail any other specific changes that were made to the press release at the request of the minister?

Mr Boshier—We changed one word in the heading of the release from 'outsourcing' to 'contracting'. We added two words in the first paragraph to clarify that the report was about IT contracting as well as outsourcing. So the first paragraph was modified from 'government IT outsourcing' to 'government IT contracts, including outsourcing'.

Senator LUNDY—Were they the only changes?

Mr Boshier—Yes.

Senator LUNDY—When you mentioned outsourcing, you did not say specifically that it was the coalition outsourcing program; you just used the generic term 'outsourcing' in your release.

Mr Boshier—That is correct.

Senator LUNDY—In your view—and this does to some degree go to Senator Eggleston's points earlier—did you have a definitional explanation for the difference between the terms 'contracting out' and 'outsourcing'? Did you see a definitional issue in the way you had expressed your press release?

Mr Boshier—We initially used the word 'outsourcing' because that was the common parlance in the media at the time.

Senator LUNDY—For contracting out.

Mr Boshier—Yes. As Athol said, we viewed it as a semantic issue at the time. So we used the word 'outsourcing' initially because we felt that the media would understand that word. When I really stop and think about it, with respect to the point that Senator Eggleston made earlier, I actually thought he was correct—there is a bit of a difference between contracting out and outsourcing. Outsourcing is a whole initiative, a whole program, an outcome, a policy—it is a major thing. What we were focused on was individual contracts. As we have discussed in this inquiry, the sum of these entire contracts equals outsourcing, but we were only interested in contracts. So we decided that we would clarify the thing. In our view, it was a bit semantic, but it was not without good reason and justification that we changed that word.

Senator LUNDY—Were you under the impression that if you did not make those changes your relationship with the minister's office would deteriorate?

Mr Boshier—No, I was not under that impression. The minister's office put no pressure on me at all. I thought it was a very cordial, productive discussion and I was happy to have that productive relationship. There was no pressure and there was no hint that there would not be a positive relationship.

CHAIR—You have published material on outsourcing and government contracting processes for some time now. You would be aware that the previous head of OASITO complained about some work that was published by the institute. Has that issue been resolved?

Mr Boshier—No, it has not been resolved completely. It is in the hands of a senior office bearer of the institution who will be making a ruling on the matter.

CHAIR—That concludes the evidence from the Institute of Engineers. Thank you, Mr Boshier and Mr Yates.

Mr Boshier—I would like to thank the inquiry for your very penetrating questions.

[11.00 a.m.]

DURIE, Mr Rob, Executive Director, Australian Information Industry Association

LARSEN, Ms Bridget Anne, Manager, Legal and E-Policy, Australian Information Industry Association

LINDSAY, Mr Richard, Manager, Government Relations and Public Policy, Australian Information Industry Association

CHAIR—Welcome. Do you wish to make an opening statement?

Mr Durie—No, Senator. We have appeared before and we have made a submission. We are happy to take questions.

Senator LUNDY—Since the Humphry review was released, the government has released an industry development proposal. Can you describe the consultations that have occurred between the government and your association surrounding the development of those industry development objectives?

Mr Durie—We have participated in consultations on an ongoing basis since the announcement of the response to Humphry until, and following on from, the announcement of the new ID arrangements. Richard Lindsay, from our office, has been the prime participant in those consultations and I have been involved from time to time. We had an initial meeting with officers from DCITA. It was essentially to have an open discussion about the issues. We put some ideas on paper; they put some ideas on paper. No doubt they were talking to others as well. We had several other meetings and we had several meetings with our members. We had one roundtable meeting which involved about a dozen AIIA members and officers from NOIE, DCITA and Minister Alston's office. They then released a draft proposal which we had the opportunity to read and discuss but not to circulate and not to take away. That was about four days before it was announced. We got a final copy an hour or two before the media release went out. From the association's point of view, we had a very full and productive consultation which enabled us, both at the secretariat level and with the member companies, to fully engage with DCITA, primarily, in the development of the new arrangements.

Senator LUNDY—I know you made a public statement at the time of the release of that new ID framework, I think it is called—the ID strategic framework. Can you summarise your response to that framework by giving us a strengths and weaknesses type of analysis.

Mr Durie—Overall we are extremely pleased. The position we have maintained throughout this process—going back to before the IT outsourcing program was instituted—was that the ID element of it should be conducted within the broader strategic industry development arrangements that the government had in place. Unfortunately, that was not the initial position. In fact, they created a new class of ID, if you like, in outsourcing. For many of our members, that caused difficulties. Our overarching objective in the review of these arrangements was that they would come back into a broader arrangement which covered all aspects of procurement

and ID, not just outsourcing, and particularly put ID on an ongoing strategic basis where companies made ongoing, medium-term commitments about investment in Australia, rather than putting specific ID offerings on the table for an individual contract.

That is essentially the nature of the arrangements. Overall we are very pleased. Where are the weaknesses? The weaknesses are in the inevitable tension between centralised management of these issues and the devolution that underpins the federal government's approach to financial management. This is not a recent phenomenon; it goes back 10 or 15 years. The central agencies—in this case, DCITA and to a lesser extent the Department of Finance and Administration—have less power to assert control. This is one of the issues at the centre of outsourcing. In fact the agency heads are paramount in many things. Obviously they have to comply with government policy, but they have to comply with it in terms of their agency not in terms of the guidelines or determinations of a central agency.

One requirement of the new arrangements which we pushed for is that suppliers be endorsed suppliers. The Department of Finance and Administration has not got the resources or the power to demand that agencies buy only from endorsed suppliers. In fact, agencies are able to say, 'We did not buy from endorsed suppliers because ...' as long as their agency head signs off on it. Our experience is that there is a certain amount of leakage—I am not sure what the quantum is—around the endorsed supplier arrangements. In an imperfect world we think that is probably as good as we can get it unless we go back to a centralised approach, which I do not think anyone on either side of politics is proposing and we are certainly not proposing.

There are two other elements which are weak. The announcement relates only to outsourcing. There is a broader framework that needs to be put in place to cover other elements of procurement. They have fixed one side of it, but they have alerted that there will be further review of what happens with the partnership program, which has been in place now since 1987. There are some issues there that need to be resolved.

The final issue is where we are most disappointed—but not extremely disappointed. Our view of the world is that it is insufficient for the government to make small business policy a burden for industry to deal with. Obviously there are things that the industry can do, particularly from the multinational point of view, in terms of partnering and assisting SMEs. A lot of that is happening, but the government and the individual agencies have to take responsibility. Our view is that the best thing that the government can do for small business is buy from it. One of the things we put on the table was that there should be a more explicit direction to agency heads in relation to their dealings with SMEs. So it was not only the industry's business to bring forward the SME involvement; the agency had some responsibility, perhaps with the assistance of our association, NOIE or DCITA, to seek opportunities to source from SMEs.

That is the part that has slipped through the net. At one point we thought we had some traction on that issue, but obviously it slipped through. We will not let it go away, because one of the commitments in the media release is that the government is going to be looking at the barriers to SMEs selling IT and IT services into the federal government. We will certainly be coming back again on that issue—to put it simply, that the government takes its share of responsibility for developing the SME sector.

CHAIR—Are you arguing, Mr Durie, for the reintroduction of the old policy that used to apply in the telecommunications area on the carriers of the 70 per cent local content?

Mr Durie—No. It just seems to us that there is still a lot of resistance. It is a bit like the partnership program itself. It came about because one of its objectives was to give the multinationals the experience of doing things here on the basis that, if they did, they would find—for example, in the area of R&D—that this was going to be very successful for their business. If you look around the landscape now, you see half a dozen companies employing about 4,000 or 5,000 Australians in product development, which is an outshoot of the partnership program. So having been required to look for opportunities here, they have found them and now they are expanding in response to market forces, not in relation to anything the government requires those companies to do. So a similar case would apply to the agencies. I think if they were required to seek out opportunities to work with SMEs, they would find that there are a lot of good suppliers out there that they can work with, and they might, for example, require their prime contractor, their outsourcer, to involve these companies in their infrastructure provision.

CHAIR—Is this one of the issues that you see as being central to the objective of building a world-class ICT industry sector?

Mr Durie—Absolutely. If you like, there are two elements. Obviously, there is a creative tension, if you like, between the two. You can dice the industry many ways, but one way you can dice it is between the multinational companies and the Australian companies or the local companies, whatever the term is. There is tremendous creative tension between that. There is a lot of interaction between those companies. The more we can provide positive experiences of customers buying from SMEs and multinationals working with SMEs, the better opportunity we have to create a world-class industry here.

CHAIR—How would you actually do it in practice? Would you look at each agency having a better role for their purchasing officers? Would you set up an ISO to organise that purchasing?

Mr Durie—I am not sure about the ISO, because the experience of our industry with the ISO is totally negative. Their exposure, involvement and interest in our industry has been pretty minimal.

CHAIR—That is interesting. That is the first time I have heard that.

Mr Durie—I think I saw an ISO person about four or five years ago. They do not darken our door at any time, so I am not sure what they do in the IT space. Obviously, their history is from engineering and so on. It has never been raised with us from our members about the role of ISO. I think there is certainly a role for some organisation. One thing that AIIA is working on as part of our new portal is promoting the capabilities of local companies. I think there is certainly a role for an agency—maybe DCITA or NOIE—to act as the point of intelligence, if you like. If a government department has a requirement to investigate opportunities to work with SMEs, it needs some information.

CHAIR—Do you prepare a handbook on the services provided by your members? Is that available to purchasing officers in government departments?

Mr Durie—No, we do it on our web site. At the moment, it is undeveloped and we are launching a new portal in July. One of the elements of that will be a capability directory of our members which we will be publicising to government offices as well as to industry. There are also a couple of initiatives in the private sector providing a networking portal, if you like, for the industry around government contracting. There has been in the past a capability directory maintained by DCITA, but I am not sure that that is up to date.

CHAIR—I must say to you that after some of the information from questions that we put to DCITA I was at a loss to understand what they were doing in terms of industry development. Maybe the situation has improved in the past month or so but the officers who were here did not seem to know very much of what they were doing, or what they were supposed to be doing, in industry development.

Mr Durie—This is historical. The directory was initially created when Australia was a partner country in CeBIT in 1995. There had been several updates of that over the years. I am not sure that that has been updated since this function went from ISR to DCITA, but we would be delighted to work with them to make sure there was a centralised directory. Certainly it would be one of the issues we would be raising with them in this investigation of what the impediments are because I think that lack of knowledge of what local companies can do is a huge barrier.

CHAIR—It seems to me to be a fundamental issue. One of the experiences that we had in the 1980s, not in this sector but in engineering generally, was on this whole question of local purchasing and local content. A lot of the purchasing officers in major companies had very extensive sets of information on overseas firms but virtually nothing on the capability that was available within Australia. In addition, they also got trips overseas to go and do the purchasing which was another incentive to go and buy over there. It just seems to me that having that knowledge in a centralised unit is fundamental to being able to promote the capability of local industry and actually to sustain an argument that there ought to be a preference given to local industry over what can be sourced elsewhere.

Mr Durie—I would certainly support such a directory. We will be doing one for our own members. We have had one but it has drifted out of date over the last year or so. Our new web portal will have the capacity that members will be able to keep their own information up to date and promote it in the way that they want to promote it.

Senator LUNDY—Just on that, I have been intrigued over the last 18 months or so to try and get some responses from DCITA about a company which claims to have been contracted by DCITA to construct a capabilities database called IT Source. If you have any more luck finding out information about it I would be pleased if you would let me know. It is certainly there and it is something that appears to attract some charge to access that information.

Going back to your general comments, how do you reconcile what seems to me to be a contradiction between your call for central, overarching control of the development of a world-class information communications technology industry plan, strengthening the role of DCITA in determining a clear agenda forward for the development of those industries, and, in the same breath, arguing that individual agencies and departments need to target specifically opportunities for small business? I know you are not actually contradicting yourself but I want

to understand how you are effectively advocating a model of very clear overarching policy direction but, within that, subsets of very specific activity or intervention that will enhance the involvement of SMEs.

Mr Durie—It is typical of strategic planning. Our concern has been—and this has been an ongoing concern of industry—not just about ID and procurement but more broadly about government policy for our industry. Whilst there have been statements at various times about what the sets of programs are, a vision of the sort that has been articulated in Singapore, India, Ireland and just about every other country in the world, has not really been articulated here. Some of the documents have got closer and closer to it, particularly the work that NOIE has been doing. I cannot remember the name of the document but NOIE puts one out every 12 months which pulls together all the things that the government is doing. Our concern has been about the policy response and this goes back decades so it is not a criticism of the present government. I think it is a criticism of the Australian approach to these things.

We are not in favour of industry planning. But, given that governments are inevitably going to make a lot of interventions in our industry because of their use of IT, its importance right across the economy and the importance of IT in this society, it is inevitable that they are going to have policies. What we are saying is that that needs to be done in a strategic framework: where are we trying to get to? It is not that we are saying that governments should invest and intervene. But as governments are going to do a whole range of things—to buy, to set policy for R&D, and they are the prime funders of public education—our plea is that should be done in a strategic context.

We were really heartened by the innovation action plan because, for the first time, we saw a document that actually sketched out the government's understanding of the central role that information technology plays rights across the economy and in R&D and that addressed some of those issues. It did not go far enough—we are hard to please; we are always going to want everything—but it was a great start. When I look at the opposition's approach now there is a much greater recognition right across the board of the importance of our industry. That is the sort of strategic framework we need before we dive down into the detail of what we are going to do about this particular issue.

Senator LUNDY—Thank you for that. Now I would like to dive down into a bit of the detail and ask a couple of specific questions. First of all, do you think it would be appropriate in public policy terms to determine a percentage of involvement by companies by virtue of their size—that is, small or medium—as opposed to their local attributes or Australianness?

Mr Durie—We have had some internal debate about this. I said that maybe we should ask agencies to report, and I was howled down by somebody who is well known to you, Senator, who runs an SME in Canberra. I cannot repeat his exact words in this forum. What he is looking for is the opportunity to sell to these people. He does not want them writing reports or meeting targets. He wants the opportunity to get in front of them, on a fair and equitable basis, and sell his product. If they do not want it, that is fine; but he wants the opportunity to sell. So I suppose that, rather than a requirement of agencies—and I am not even sure how you would implement this; we would have to work through it—there should be some sort of expectation that agencies will explore opportunities with SMEs. And maybe there should be some level of reporting of what the outcomes have been: what SMEs they are sourcing from, et cetera.

In relation to measuring, the target that the government set before and after it came into government, of 10 per cent, was not seen as particular relevant by our industry because we knew we were well in excess of 10 per cent already. Similarly, our response to other mooted targets is that the number we are looking at now is somewhere between 25 and 30 per cent, if not more. So I am not sure that targets are what we need. It is an information issue. As Senator Campbell was saying: where do people go to get information about potential suppliers? At the moment, the answer to that question is: nowhere.

The other issue about targets is: how do you measure it? If you look at the outsourcing program, we had a lot of numbers flying around and I think it was based on Australian value add and revenues flowing to SMEs. That distorts things totally. Particularly if you look at the revenue side of things, it tells you nothing about how profitable that business is and it tells you nothing about whether it was helping that SME get into other markets. So we have tended to shy away from those sorts of measures. I think you need a much more holistic approach and a report on what companies an agency is dealing with and actually giving some business. That is probably of more relevance than what the percentage is.

Importantly, the other cry we have from SMEs is the question of reference sites. We had a great example yesterday. We are doing our best to promote the government's new intellectual property guidelines in IT contracting, because we think there is a lot of existing IP and IP that is going to be created in developing government systems. It has got great potential worldwide. We have been working for years to get this policy in place, and it was announced in February. We had a great presentation yesterday from ScreenSound Australia and their local partner, Wizard Information Services, about how they have worked together to develop their information and library system, which is now the system in archives around the world—it is used by the Library of Congress et cetera. What happens is that ScreenSound Australia and all these other organisations are the best salesmen that Wizard have ever had. That is the sort of outcome you need. That has not come about by people setting targets or whatever.

Senator LUNDY—Could I just clarify that ScreenSound Australia participated in IT outsourcing as a small agency, so that contract with Wizard was not part of a bigger cluster.

Mr Durie—No, it was not; in fact, I do not think Wizard won the outsourcing with ScreenSound. This is an application development project that goes back seven or eight years. So it is totally outside outsourcing.

Senator LUNDY—That provides a good example for the question I want to ask you. Do you think that the answer, rather than specifying degrees of involvement, could be in the way the contracts are constructed and presented to the market, and do you think that there is an opportunity there for public policy to effectively predetermine the types of participants or responses from the market they will get by the way they present, and the structure of the contracts they present, to the market? I say that in the context of the intense criticism that has come about the clustered approach and the magnitude of the contracts under the current—or, I should say now, previous—IT outsourcing structures.

Mr Durie—You have identified one important issue, and that is the size of the contracts. That is obviously important. So one of the things we see flowing out of the new approach is that

there will be smaller scale opportunities which will be easier for SMEs to participate in as partners, or even as primes or handle totally themselves.

Senator LUNDY—Sorry to interrupt, Mr Durie. A fine point on that: I have certainly made that assumption based on anecdotes, stories and views of SME participants. Are you of that view that smaller contracts will in fact allow for greater participation of those businesses?

Mr Durie—Certainly that is the view of our members. But there are also a whole range of issues surrounding contracting which make it harder for SMEs, like the cost of contracting. Again, if you look at the—

Senator LUNDY—So it is like financing a bid?

Mr Durie—If you look at the numbers in the Auditor-General's report on the cost of contracts, no SME can afford seven-figure sums to participate in the bidding process. But even on a smaller scale we have been arguing for much more simplified contracting in federal government.

There are issues about liability and financial guarantees. I think we've made some progress on the liability front, but we would like the government to take a much more commercial approach and not simply to insist on unlimited liability. We would like the government to take a more generous view about financial guarantees. What is the point of tying up an SME's working capital in bank guarantees? It is useless. So what we find is that many of our members cannot understand why AIIA puts so much emphasis on government procurement, because they would not try to sell to the government if they were paid to: it is too hard. Again, this is what we hope will come out of the review of the barriers—the time scales, the cost, the government's insistence on non-commercial terms and conditions, unlimited liability, financial guarantees and the like. We have made some progress in that, but it is incremental rather than stepping into a brave new world.

These new IP guidelines are an example. That is great policy, but what we really need is a cultural change in the way the government goes about doing business, both in its approach to contracting and its approach to IP. At the moment, both from a technical and an emotional point of view, if you like—a cultural point of view—government assumes that they need all the IP. They are not looking for partnerships where a company might develop the product for them and then commercialise it elsewhere, with the agency's support. The new guidelines provide a framework for that but, from the evidence we have, they have not even sent them around and, even if they do send a copy of this 100-page set of guidelines to every purchasing officer, that is not going to change behaviours. We need some proactivity. Firstly, we need to get the policies right, in terms of contracting, cost of contracting, length of the bidding process et cetera Then we need to put a concerted effort in to change the culture.

Senator LUNDY—I have a couple of specific questions. What is your view of the role of the project register that has been managed by DCITA, and how does that affect your membership's ability to establish a credential for getting government work?

Mr Durie—My understanding is that it has lost a certain amount of relevance since the change to the new arrangements.

Senator LUNDY—I am interested because that was certainly flagged as a way of allowing, effectively, out of scope industry development initiatives to be identified, prior to contracts being in place.

Mr Durie—It is just that that is no longer relevant in the new arrangement.

Senator LUNDY—Is the project register still in existence, as far as you are aware?

Mr Durie—I have never seen it. I cannot comment.

Senator LUNDY—What is your association's view on the demise of the Partnerships for Development arrangements for these contracts or potential contracts?

Mr Durie—My understanding is that for a multinational it is still the case that they have to be a partner in good standing to be an endorsed supplier. So, while the Partnerships for Development program is, if you like, on its last legs, it is still alive. This other element of what the government needs to do is what is coming after Partnership.

Senator LUNDY—I appreciate that. Does your association have a view on the future of Partnerships for Development? Should it prevail in some way, or do you see it being superseded by another holistic approach to what would emerge as, perhaps, some sort of prequalification for IT multinationals to participate in the Australian market?

Mr Durie—We have always been of the ticket-to-play persuasion, which is why we supported a Partnership style. I am not sure what substantive changes you could make. It probably needs a makeover, but I suspect that what we will end up with will look broadly similar in the sense that we would expect—and I think from a WTO point of view we would need to expect—all companies that want to participate in a federal government market to make appropriate investments in the Australian economy. I think that is how the system works at the moment. A local company that wants to be an endorsed supplier has to demonstrate its credentials as well, and a multinational demonstrates its credentials by being part of the Partnerships Program.

Senator LUNDY—Going back to the endorsed suppliers, to what degree does your association believe there is a place for perhaps strengthening credentials to become an endorsed supplier, and to what degree should that be enforced, given your earlier comments about your scepticism about the powers that an agency like DCITA might have to make sure that individual agencies and departments use those endorsed supplier lists?

Mr Durie—At the moment, it is split between DCITA and DOFA, I believe. DOFA have overall responsibility for the endorsed supplier; DCITA has responsibility for the IP on it. The view of the association is that, if we are going to have these arrangements, they should be enforced. There is always a certain amount of frustration to find that the company that won the deal is going to be an endorsed supplier.

Senator LUNDY—As has happened with IT outsourcing.

Mr Durie—As has happened, and a special arrangement was introduced for outsourcing that gave companies a period of time—I cannot remember the details—after they had won business to become an endorsed supplier. As I said earlier, our preference is for a ticket-to-play system, which means you buy a ticket and then you can play.

Senator LUNDY—You buy it or you are qualified by virtue of your actions?

Mr Durie—You qualify by virtue of your investments.

Senator LUNDY—I thought I had better clarify that.

Mr Durie—That takes money—and then you can play. You meet the endorsed supplier requirements and then you can bid for business.

CHAIR—That is a variation of the meal ticket and start rule.

Mr Durie—I have been in there!

Senator LUNDY—To what degree does becoming an endorsed supplier present a barrier for SME participation in tendering for government work?

Mr Durie—The major barrier is the financial assessments. I am not sure exactly what they are, but that is where you end up with the financial guarantees.

Senator LUNDY—That goes back to your other issues like liabilities and capability to service whatever the contract bond arrangements are.

Mr Durie—The other thing in terms of endorsed supplier is that, in the period since it was introduced, we have noticed that there has been a multiplicity of panels of suppliers set up for various purposes by various agencies. Many agencies feel that they have to go away and do due diligence on suppliers, despite the fact that they are already endorsed suppliers. There are two comments about that: firstly, if you do the endorsed supplier process properly, agencies should be able to trust it and not do undue due diligence, if you follow me, on suppliers; and, secondly, if the endorsed supplier process is done properly, there should be no reason for any agencies to set up a panel for Internet payment systems or whatever. All of these things should be encompassed—or can be encompassed and will be best encompassed—within the endorsed supplier program.

Senator LUNDY—Do you think they should scrap the panel system whereby different suppliers are grouped and could be listed on a multitude of panels, depending on the type of contract that is being considered?

Mr Durie—I tend to take a holistic view of things.

Senator LUNDY—It is converging.

Mr Durie—I cannot see why it cannot be encompassed in the endorsed supplier program. In fact, we have had a bit of a discussion with NOIE, who are setting up a special web site for companies who want to sell e-government services. We are saying, 'Hang on a minute; why would you do that outside the endorsed supplier program?'

Senator LUNDY—So you are not looking for a duplicated system to be conducted in NOIE or DCITA on top of that?

Mr Durie—No. In fact, leading on from that, that is where the capabilities directory needs to be built into that system.

CHAIR—Thank you, Mr Durie, Ms Larsen and Mr Lindsay.

Proceedings suspended from 11.40 a.m. to 11.50 a.m.

BOTTOMLEY, Professor Stephen, Director, Centre for Commercial Law, Faculty of Law, Australian National University

CHAIR—Professor Bottomley, do you wish to make an opening statement?

Prof. Bottomley—If I may. I will begin by explaining why I am appearing before the committee. I was contacted by research staff for the committee. I have done some work on accountability issues as they relate to government business enterprises and government corporations. To some extent that overlaps with similar issues in relation to outsourcing contracts. The use of the company form and use of a contract raise similar issues about integrating private sector business practices with public accountability requirements. What I have to say today relates to paragraph (a)(ii) of the committee's terms of reference—the issues of transparency and accountability of these processes. I will not be offering any opinion on any of the other terms of reference.

At the outset let me say that it was a bit of a surprise to see that the committee is investigating these sorts of issues. The surprise is because there have been a number of reports handed down or published in the last three to five years that have looked at just this issue—the question of the intersection between accountability to parliament and claims of commercial-in-confidence. Those inquiries, although they differ in the details of the recommendations they have made, have all generally come to the same conclusion, which is that, except in limited cases, claims of commercial-in-confidence should not be used to impede the process of accountability to parliament. The evidence that this is still an ongoing problem suggests that there is a need for more concerted action there.

CHAIR—For the purposes of *Hansard*, if you have available the names of those reports, can you name the reports that have been handed down?

Prof. Bottomley—I do not have a full list here, but this is an indicative list: the Joint Committee on Public Accounts and Audit published a report in November 2000 entitled *Contract management in the Australian Public Service.* This committee has published two previous reports—one in 1998 entitled *Contracting out of government services*—and there are the issues that it raised in its interim report in the course of this inquiry. The Administrative Review Council in 1998 had a report entitled *The contracting out of government services.* In 1995, the Senate Committee of Privileges, in its Casselden Place reference, raised similar issues. The ANAO, in a number of different reports, has raised similar concerns. I do not have the details of each of those reports.

It seems to me that part of the problem stems from a misunderstanding about the nature of confidentiality and claims to confidentiality. It might help if I can quickly give a brief synopsis of what the law says. There are some equitable rules which apply to claims about confidentiality. Broadly, in order for somebody to be successful in claiming that something is confidential, they have to prove three things: firstly, that the information has the necessary quality confidentiality, that it is inherently confidential information—trade secrets would be a good example of that—secondly, that the information was given in circumstances that implied an obligation to keep the information confidential; and, thirdly, the concern must have arisen

where there is about to be an unauthorised use of that information—so the person who has given the information has not authorised its release. There are legal arguments as to whether it must also be shown that there will be detriment incurred if the information is released. There is no clear conclusion on that.

The situation, though, is much clearer in the case of government information. The High Court has said now on two occasions that there is a reverse onus that applies in relation to government information and that government must prove that the public interest requires non-disclosure. To put it another way: will the disclosure harm the public interest? In other words, there is a presumption of disclosure of government information, and the onus is on the information holder then to make the case that it should not be disclosed and, in order to make that case, they have to demonstrate that it is in the public interest. What the courts have said indicates that that is a heavy onus to overcome. All of that can be overridden, however, if in the course of making a contract the two parties agree between themselves that some or all of the material in the contract will be confidential. The law does not then inquire into whether it is inherently confidential information; it is simply up to the parties to decide that for themselves. When that is done, then any subsequent disclosure of that information involves a breach of contract, and there could be action for that.

The problem that arises then is the overuse of that process, the overuse of claims about commercial-in-confidence. Therefore, my suggestion is that we need to ensure that government contracting practice reflects the reverse onus; that is, when the government enters into contracts, it has in mind what would otherwise be its legal position, which is a presumption of disclosure unless it is in the public interest not to do that. I suggest that the way that could be done is, firstly, that whenever the government enters into an outsourcing contract it should advise the private sector contractor before the contract has been entered into that the resulting contract will become a public document, that it will be part of the accountability processes of government, except for any matters in the contract that would be classified as inherently confidential—trade secrets, information of a sensitive commercial nature, sensitive business and financial information about the affairs of the person—the sorts of things that ordinarily we would regard as confidential.

If the outside contractor enters into the contract on that basis and government enters into the contract on that basis, it seems to me that we have a much more open system. There would need to be a process to resolve disagreements where it is claimed that something should not be disclosed because of confidentiality. The reports that I mentioned earlier have all generally been in agreement with a process along the lines of an in camera hearing by the relevant committee to discuss that. If the in camera hearing does not resolve the issue or, indeed, if it is not possible to have an in camera hearing, as I understand is the case with estimates hearings, then a third party or an independent arbitrator could be called in. Most of the reports indicate that would be an appropriate role for the Auditor-General. I think it is appropriate for the Auditor-General to consider the matter and to make a recommendation as to whether the matter then should be disclosed or not.

I suggest that the best way to achieve all of this is to codify it in some way, whether in the form of a set of guidelines or a code of conduct. The Committee of Public Accounts and Audit considered this question in its November 2000 report and recommended against codification. It saw it as being too inflexible or too difficult to get these things written down. I am not so

convinced that that is the case and I think that a code of conduct could nevertheless have some inherent flexibility. But, at any rate, it seems to me that because these issues continue to surface despite recommendations of several committees, it may now be time to actually take the next step and be more concrete about the way in which these contracts are entered into.

The final thing I want to say is to make reference to the freedom of information legislation. It is possible that even a provision in a contract that is classified as commercial-in-confidence could be required to be disclosed by an order made under the Freedom of Information Act. That act does protect information that is confidential, but there can always be argument about what 'confidentiality' means—and at any rate the act also does contain some exceptions where the information needs to be disclosed in the public interest. The Freedom of Information Act has a couple of limitations. Firstly, it only applies to government information. In the case of a government contract with a private sector party, there might be some argument about whether the information is government information or private sector information. It was for that reason that, in its 1998 report, the Administrative Review Council recommended an amendment to the FOI Act which would deem any information held by the other contractor relating to the performance of the contract to be held by government, so it would bring it under FOI.

The other reservation I have about FOI is that to base a system of accountability and disclosure on FOI is going about it the wrong way. I think disclosure of this information should be voluntary. Governments should be leading by example rather than being forced into disclosure through FOI actions. FOI is appropriate in cases of genuine disagreement about whether something ought to be disclosed or not. But as a matter of course to base a system around FOI I think would be wrong in policy terms.

A trade-off has to be made between wanting to conduct operations on a commercial basis and the demands of accountability to parliament and, like all proper trade-off situations, each side has to yield something. There will not be full commercial operations because of the demands of accountability. It is just not appropriate, in my view, for government contracts to be performed as though they were ordinary private sector contracts—the obligations of the executive to report to parliament and for a parliament to report to the public dictate that. Equally though, there will not always be full accountability because of the demands of commercial operations, the need to protect things such as trade secrets and genuinely confidential matters. There will always be some no-go areas. But I think those areas need to be much more clearly defined and have been more clearly defined in the reports that I have referred to, but ought to be more obviously put into practice.

Senator EGGLESTON—You talk about codification as a proposal. In your position as a professor of law considering these issues of commercial confidentiality, do you feel that the system as it exists now is really seriously deficient and causing problems which ought to thereby be revised?

Prof. Bottomley—The only evidence I have to go on is the number of occasions upon which different bodies and committees such as this confront these sorts of issues. I cannot speak with any knowledge about how widespread these concerns are. But the fact that this committee's inquiry, and other committees making similar inquiries in different areas, keep bumping into this problem I think is a matter for significant concern. I have got to say that it is not just a concern at the Commonwealth level. State governments have had to face up to similar issues as

well. Certainly, in the case of Victoria, they have responded quite well in terms of publication of contracts and disclosure.

Senator EGGLESTON—You referred to the fact that the Committee of Privileges published a report a few years ago—in 1995, I think you said. It is an issue that arises quite often in committees but, as with the law itself, the system of protecting commercially confidential matters tends to evolve by precedent and so on. I find it a bit hard to accept that there really is a substantial issue in terms of the failure of the system as it exists now. I say that because one does not find there are in practice a great number of complaints about the way the system operates. I feel that the onus should lie with the people who hold a trade secret or have matters to do with finance which they are reluctant to place on the record instead of entrusting the responsibility for respecting their confidence to the vagaries of a group of parliamentarians.

Prof. Bottomley—I have two difficulties with that. Firstly, to trust the people who hold the information to make the judgment about what is confidential invites problems about a conflict of interest. Where the information might adversely affect on them if it was released, there may be an understandable temptation not to release the information. Secondly, even if it is difficult to get clear evidence of the magnitude of the problem, it is incumbent on government to hold itself out as an example of best practice in contracting activities. When problems arise, it seems that they have arisen because, over time, a set of understandings has grown up about the use of commercial-in-confidence clauses. It would be better if the government took steps to clarify the appropriate range for the use of those clauses instead of leaving it to the discretion of contracting agencies.

Senator EGGLESTON—In asking government or parliamentarians to clarify what is confidential, you are asking the body or company concerned to trust the parliamentarians to act with propriety in these matters. As we all know, quite often there are leaks from parliamentary committees. I suppose one can understand that corporate bodies might be very reluctant to place that kind of trust in a parliamentary system.

Prof. Bottomley—My proposal would limit the sort of information that could properly be claimed as confidential to what I would call genuinely confidential information and that information would not be put forward. If a committee called for information arising from a contract, and the holder of the information did not want to disclose it, their task would be to explain to the committee the grounds upon which they did not want to disclose that information and why it should not be disclosed, and to make that claim in terms of the public interest argument. If the committee was convinced of that at the end of the day, the matter would not be disclosed further. I am not in a position to say whether members of the committee might nevertheless leak the information. That will always be a risk in doing business with anyone. There has to be some level of trust with the other person. What needs to be made clear to private sector contractors who wish to contract with government is that it is not the same as contracting with another private sector person. The very nature of government as a contractor raises a different set of concerns.

Senator EGGLESTON—I agree with your last point. With regard to your earlier comments, we already go through a process where parties argue the reasons for the confidentiality of information being respected. You are proposing to codify what already happens.

Prof. Bottomley—And I am trying to limit the range of issues about which those arguments are going to be raised.

Senator EGGLESTON—Indeed. But, in effect, the onus still remains with the parliamentary group. In a Senate inquiry, we say that evidence may be taken in camera but that it may subsequently be made public. I suppose one can understand the great reluctance of groups, for example, in respect of IT outsourcing where their commercial information is sensitive, not wishing to place it before a committee knowing that there is a long track record of leaks from these sorts of committees. I know there is no answer to that, but it is a difficult, practical problem.

Prof. Bottomley—The backdrop to it is the basic presumption of disclosure. The onus is not on the committee to prove why disclosure should be made; the onus is on the holder of the information to prove why disclosure should not be made.

CHAIR—Are you familiar with the US system?

Prof. Bottomley—No, I am not.

CHAIR—They seem to be able to manage a more open process of government contracting than people here are able to do. We have greater concerns about confidentiality provisions than they do. I understand that the joint audit committee which produced the report on the Victorian matter looked at this question of commercial-in-confidence provisions in government contracts. I think they made the statement that their experience was that it was government agencies that were initiating the commercial-in-confidence requirements rather than the private sector. Do you have any information on that aspect? Have you looked at that aspect of it?

Prof. Bottomley—Just anecdotal evidence which suggests that that is the case—that it is government agencies that seem to be more keen to use commercial-in-confidence arguments than private sector people. Also, on occasions when these matters have been argued out and the information has finally been released, it is remarkable how often the information is quite mundane. One wonders what on earth the concern was all about initially. The other aspect is that keeping a system of confidentiality in place is very expensive. It costs to put in place mechanisms and processes to ensure that documents remain only in certain hands; that people do not speak out of place or out of turn. A system of open government is much easier to maintain.

CHAIR—The other issue that is of concern to the committee—I think we refer to it in our interim report—is that this is not just a question of looking at commercial-in-confidence, because there are many issues that can be legitimately argued are commercial-in-confidence: trade secrets, sensitive financial information about companies' performances et cetera, which they may not wish to have disclosed. But in many instances that we have come across, and specifically on this inquiry, it has been more about public servants determining whether or not they will provide information to the inquiry, quite apart from the commercial-in-confidence issue, and in some respects even determining who will or will not appear before the inquiry. This seems to be taking the issue way beyond even what was envisaged by you in your initial comments about how you genuinely provide for commercial-in-confidence issues to be separated out from the right of the public to know how public moneys are being expended,

which lies behind the open government issue. Is that something that you have had any familiarity with?

Prof. Bottomley—It is not something that I have looked at. I cannot speak with any authority in terms of public service employment or conditions, but I would have thought that there is an outside view that the very term 'public service' must imply an obligation to give information, to report information, particularly when, as we so often see, the information itself has no inherent confidential quality about it at all.

CHAIR—With respect to the use of commercial-in-confidence, one of the mechanisms in the parliament for guaranteeing public scrutiny is the Senate estimates committee process. More and more we seem to be confronting arguments about commercial-in-confidence following requests for the provision of documentation or information, to the extent that, on one occasion, at a committee hearing which I attended, there was a claim regarding the use of the common law doctrine of commercial-in-confidence to deny access to information on the names of companies which had applied for government funding.

All that simply meant was that we then had to go a circuitous route to actually get the information by seeking returns to order in the parliament to eventually get it on the public record. If you had an independent party, such as the Auditor-General, to determine whether or not it is a legitimate claim, how would that work in practice, for example, in the process of a Senate estimates committee hearing? You would have the Auditor-General or his surrogate sitting there permanently giving advice on a whole raft of issues which come up on a regular basis before Senate estimates committees.

At the legislation committee hearing of this committee, for example, Dr Boxall from DOFA took 160-odd questions on notice. Most of those questions we thought were fairly mundane to have asked of a secretary to a department. Nevertheless, that is the way in which they were handled. I can understand the logic of that approach, but I do not know how it would operate in practice in the context of Senate estimates committees and the probing of government departments and ministers about public expenditure.

Prof. Bottomley—Part of the problem is that outsiders dealing with government are being led to believe that they can deal with government on a similar basis to that which they would deal with any other private sector person—that the same practices and understandings will apply. I do not have any hard evidence about how this is being conveyed. It just seems to me to be a valid conclusion to draw from the information we have got. I would surmise then that, when government officers are entering into these contracts, that is very much the opinion they ought to create. My impression is that people on behalf of the government entering into contracts want to behave much more like their private sector counterparts. You do not find private sector counterparts wanting to act very much like government. The whole tone of these sorts of commercial dealings is being modelled on a private sector set of assumptions.

That underlines the point I made about needing to codify practices and guidelines in this area to make it quite clear that that is not the way it should be. This is not an instant answer to the problem of how you effectively run an estimates committee, but hopefully the result of that down the line would be fewer spurious claims about what is and what is not commercial-in-

confidence, leaving then the genuine issues to be sorted out by reference to somebody like the Auditor-General.

CHAIR—If the claim is made, it is very difficult for us on this side of the table to contest it. If we do not have the information, it is difficult to contest whether it is a legitimate claim or not a legitimate claim. There is a strong argument to have a third party make that test. The practicality of doing it is another issue and that is where the difficulty comes in. Perhaps codification might go part of the way in doing that. The other side of it may be that there is an educative role here for perhaps the Public Service Commissioner—and we might raise that with her when she comes before the committee—in terms of public servants generally having both a codified set of rules governing it and an educative process to ensure that they understand the necessity for public disclosure to the extent that it is possible in every given set of circumstances.

Prof. Bottomley—In all of that it really is important to keep emphasising where the onus lies. The onus lies on the government officer holding the information to show why it should not be disclosed. They are the one who has to make the argument; it is not the committee who has to prove otherwise.

CHAIR—Yes, not the reverse.

Senator LUNDY—On the general question of accountability, like Senator Campbell I want to ask some questions about your knowledge of how it works in the US. What is your understanding of the extent of the requirements of the financial management act when it comes to disclosing the contents of a contract if the question were asked in the Senate estimates or the parliamentary committee environment?

Prof. Bottomley—My understanding of the act is that there is an obligation—I would have to check the act— and it does underpin a system of open accountability and reporting. Again, the fact that resort then has to be made to something like the FMA Act to prompt the disclosure to me suggests that the problem lies before then. People just do not realise what their underlying obligation is, which is to disclose the information. The fact that they have to then be pushed into it by reference to either FMA Act responsibilities or FOI Act claims I think tells us about the magnitude of the problem.

Senator LUNDY—One of the issues throughout this inquiry relating to IT outsourcing has been the extent of responsibility of the agency heads, chairmen of boards of statutory authorities, et cetera, under the provisions of that act, and it has been evoked on several occasions including in the Humphry review recommendations. Do you think it would be useful to perhaps use that piece of legislation to specify to a greater degree the responsibilities relating to disclosure and use of commercial-in-confidence provisions? I take your point about the fact that it should not come to that, but it has come to that, effectively. There have been a multitude of experiences within parliamentary committees where commercial-in-confidence has been evoked by members of the administration and the bureaucracy, unjustifiably in my view and in the humble view of various parliamentary officers. I am looking for clues as to where the solution is.

Prof. Bottomley—When I speak about codifying best practice, I stop short of suggesting that it should be put into legislation, partly because I think a more flexible approach at first step might be appropriate and partly also because the JCPAA would be lucky to have any form of codification at all. It seems to me that a more code of conduct type approach initially might be the way to go.

As for using the FMA Act to do that, there is a sense that the FMA Act is all about financial accountability. The question of parliamentary accountability or accounting to parliament must extend beyond mere matters of financial reporting. Financial reporting tells you what is being done; often what the committee needs to hear is why it was done or indeed how it was done. That is why using a more flexible body of rules or procedures might be more productive.

Senator LUNDY—On the question of financial accountability versus parliamentary accountability, one of the specific issues or reasons used for the prevention of disclosure by virtue of commercial-in-confidence has been the actual dollar figures contained in those contracts. So it is very much argued that it is a financial issue that is creating the cause for concern. I am just exploring further whether it is possible to specify that that perhaps more formal codification by way of legislation be corralled to financial management matters as opposed to the broader issues. I can understand the concerns about why you would not want to embark down a pathway codifying that with too much specificity and inadvertently preventing the scope of parliament to pursue accountability. I am just curious about your thoughts.

Prof. Bottomley—Clearly, I think reporting on the financial details of these contracts lies at the heart of what needs to be disclosed. And, yes, there could be merit in at least taking that particular element and clarifying that in the FMA Act, but not to the exclusion, I would hope, of other forms of accountability.

Senator LUNDY—One of the areas where this committee has, I suppose, faced a particular challenge in getting information is in contract evaluations where different figures—dollar figures, financial information—were compared with others. So it was really the bridge between the sensitive financial data provided by tenderers, if you like, and the department or agency's calculation of best value as a result of that. Can you comment, very specifically, on the status of those evaluation reports in that they effectively form the basis of how a decision would be made for any claim for commercial-in-confidence?

Prof. Bottomley—To the extent that disclosure of that information—and I do not quite understand how those documents work—would reveal sensitive financial information about unsuccessful tenderers and the sorts of claims they put in, I would not support the disclosure of that information. To the extent that it would provide sensitive financial information about successful tenderers—about their profit and loss position, that sort of thing—I think there is a need for caution there. To the extent that it is simply revealing information about what the government's commitment is in terms of financial expenditure, that must be disclosed, in my view. There are going to be some areas that would be better dealt with by FOI type claims, I think—where there is some doubt about whether the disclosure will actually prejudice parties in that way.

Senator LUNDY—In advocating an FOI type approach, my understanding is that the appropriate level of scrutiny of these committees goes beyond what the FOI guidelines or

methodologies actually provide for. That is one of the reasons why we find ourselves in this position. FOI theoretically provides the assessment approach you would take as to what constitutes commercial-in-confidence. But, in fact, we cannot even get to that level in terms of our inquiries, or are being prevented from having access to information even to FOI level by virtue of our inquiries. I did not ask you a question, so you do not have to say anything.

Prof. Bottomley—I am not sure how to respond to it.

Senator LUNDY—I guess I am just reflecting on your comments in terms of the experience that we have had. As far as the information provided by tenderers goes, to what degree is it appropriate that requests for confidentiality from tenderers or external companies be given consideration by either the departments themselves or, indeed, the parliamentary committees?

Prof. Bottomley—I think the answer to that is that, when government releases the documentation requesting tender, it must made very clear what will be confidential and what will not be confidential, and that is part of the codification process I am talking about. It is a matter of sitting down and saying, 'These are the following matters that will be considered confidential'—the sorts of matters we have already referred to—'and anything else falls within the obligation to report to parliament.' It is going to be open to public scrutiny and people will enter into the tender on that basis.

Senator LUNDY—I hate to put hypotheticals to you, but what if the government, in releasing that RFT, misleads the participants in the tender and they provide information on the basis of being given an inaccurate assurance by the government—in that the government has misrepresented the powers of the committee or this obligation to disclose information? What is the legal standing of that?

Prof. Bottomley—To the extent, at the end of the day, that a contract is concluded between the successful tenderer and the government, and one of the terms of that contract has now become that certain information will remain confidential, then that is it.

Senator LUNDY—In essence, what you are saying is that contractual obligations arrived at by virtue of contract law actually override the accountability rights of the parliament. That is what you just said.

Prof. Bottomley—What the parties have agreed to in their contract as to what is confidential can only be disclosed if parliament has a clear statutory mandate to do that.

Senator LUNDY—Which it has.

Prof. Bottomley—Otherwise, the claim of commercial-in-confidence agreed to by government and the other contracting party as a matter of contract law is enforceable.

CHAIR—But surely a public servant can contract the way they are rated—

Senator LUNDY—This is the point I want to get to. This is the situation I believe we may have found ourselves in—where the government by virtue of omission or active statement in the request for tender has implied a level of confidentiality beyond the scope that they can

technically provide. When that is subsequently being tested, the government, the department and the officers are making an assessment that their contractual obligations override the powers of parliamentary committees. That is the key question. Who, in your view, prevails? The key question is that, if information is released by virtue of the powers of the parliament as prescribed in the Constitution, does that expose the government that gave those inaccurate contractual obligations to some form of liability?

Prof. Bottomley—It could do, yes.

Senator LUNDY—So, a government, in your view, is therefore capable of contracting away the powers of parliamentary committees, by virtue of the fact that they immediately and by default evoke a situation in which the Commonwealth can incur liabilities.

Prof. Bottomley—The desirable situation is that—

Senator LUNDY—The desirable situation is that the government does not release RFTs that inaccurately represent the powers of parliamentary committees. You have made that clear. What I am getting to now is the question of just how vulnerable the process of parliamentary scrutiny is to a decision by a government to make an inaccurate commitment about scrutiny in a contract, thereby creating a very difficult situation down the track where, despite the parliament being entitled to that information, the Commonwealth may well incur a liability. That is a construct of a government decision at the time.

Prof. Bottomley—The consequences are that, if a contractual promise has been made and has been broken, there is potential liability. The question of whether government officers have been given the understanding that they are at liberty to do away with those sorts of constraints is again an issue that needs to be dealt with. This goes back to my argument that what is demanded is a code of conduct, explaining quite clearly what their parameters are.

Senator LUNDY—Yes, I appreciate that you have some constructive ideas about how to deal with it. If a Commonwealth officer—a member of a department, a minister, or whoever is signing off on the contract—knowingly inserted those clauses into the contract on the basis that the Commonwealth could incur a liability if a parliamentary committee requested that information, what recourse would be available, either through the financial management act or other laws of the Commonwealth, to hold that person accountable? Is there any pathway back to holding them accountable for knowingly constructing a contract that would force the Commonwealth to incur a liability?

Prof. Bottomley—I do not know the answer to that question.

CHAIR—I think we will bring it to a conclusion there. I think the Clerk of the Senate may have a strong difference of opinion with you in terms of the legal liability of the Commonwealth being incurred. I also just want to clarify one point, in case there is a misconception. We have not been denied access to any information; there is just an ongoing debate about what information we should have access to, and that remains unresolved in the context of this inquiry. Thank you, Professor Bottomley.

[12.41 p.m.]

MARKS, Mr Stephen Graham, Managing Director, Stephen G. Marks & Co. Pty Ltd

CHAIR—Welcome. Do you have any comments to make on the capacity in which you appear?

Mr Marks—Yes, my company were the probity auditors for the whole of government IT outsourcing initiative.

CHAIR—Thank you. Do you wish to make an opening statement?

Mr Marks—No, Mr Chairman, I am basically here at your request to answer any questions which you care to put to me.

Senator LUNDY—Mr Marks, my recollection of previous estimates hearings was that you were engaged by OASITO without having involved yourself in a competitive tendering process. Could you clarify that for the committee?

Mr Marks—Other than what I have read in *Hansard*, I am not familiar with what actually transpired in that. My involvement came about because I was contacted and asked if I could go through an interview process with OASITO. My understanding, from what I have read and heard, is that that may well have come about due to the fact that there was difficulty in obtaining a probity auditor who had no conflicts of interest. By way of background, I am a dedicated probity auditor. My whole existence is spent probity auditing, and I act—or have acted—for six different governments around Australia. I act only for government. I have no private sector clients, so I do not put myself knowingly into any situation of conflict. I therefore cannot act for bidders or in any situation because I am only contracted to governments. That was a strategic decision that we took as a business because we did not want to place ourselves in a situation where we were exposed to that. My knowledge of that side of it is anecdotal, basically.

Senator LUNDY—From whom and what was the nature of the initial approach from OASITO?

Mr Marks—The initial approach was from Ross Smith. I was interviewed by Ross Smith and Gillian Marks, who is no relation to me.

Senator LUNDY—I know. We clarified that years ago.

Mr Marks—I presented them with basic details—CV and experience, et cetera—so there was a formal process of interview.

Senator LUNDY—In terms of the issue that you were involved in—the probity of the IT outsourcing process—had you had any previous experience of outsourcing by governments, whether it was in IT or in another area?

Mr Marks—Yes. I think that is probably why I was initially contacted. I started in this business doing the electricity sales in Victoria, and it moved on from there. Over a period of time, I have acted in probably most of the major outsourcings in government contracts, where probity auditors have been required, throughout Australia. I have had considerable experience.

Senator LUNDY—Did you have a role to play in the South Australian whole of government IT outsourcing?

Mr Marks—No.

Senator LUNDY—You did not?

Mr Marks—No.

Senator LUNDY—Have you done any work for South Australia?

Mr Marks—I have worked for South Australia. They established a panel for IT work—I think it was called the AMD panel. They put together a panel of contractors whom they would then call upon to do work for them, but that was the only involvement I had.

Senator LUNDY—Was that pre or post their whole of government outsourcing to EDS?

Mr Marks—I cannot tell you.

Senator LUNDY—In performing your duties as a contracted probity auditor, were you contracted specifically to OASITO to monitor the probity of their processes? Or was your role to reflect on OASITO's conduct? Do you understand the distinction I am trying to make? I am not sure whether I do! I am trying to work out whether you were observing and assessing OASITO's conduct or you were observing the conduct and processes initiated by OASITO but primarily involving the whole range of other parties in the tender process.

Mr Marks—My appointment was to oversee the probity of the whole of government IT outsourcing, which meant that, whilst I was contracted to OASITO, my responsibility was effectively to the government to ensure that the process was fair and equitable, that it was defensible and transparent, that the bidders were all given equal opportunity and that nobody was disadvantaged by the way in which the process was conducted—if you go to the lowest common denominator—so that at the end of the day the losing bidders would walk away feeling that, although they may have been unsuccessful, at least they were in a fair contest. My responsibility was to ensure that the process was fair to everybody. I was not there to pass judgment on OASITO per se, but I was there to make sure that the processes they undertook ensured proper probity.

Senator LUNDY—Who did you report to if you were contracted by government to audit the probity?

Mr Marks—I reported to OASITO, which I was contracted to.

Senator LUNDY—You describe yourself as being given the role or brief of probity auditor into the IT outsourcing program per se. The policy was driven, appropriately, from the minister's office. OASITO had an implementation role, yet the policy advice was driven by DOFA. How did you report to government? Did you report to the department of finance, either through their policy people or the minister's office? Or were your reports delivered only to OASITO as implementors of the project?

Mr Marks—That is a question you would have to ask OASITO. I reported to OASITO, which I believe then reported to the minister on what I had said, but I think that is something that OASITO would have to answer directly. My direct reporting was to OASITO, but I had the reserve power to report directly to the minister if an occasion presented itself—but it did not present itself.

Senator LUNDY—It did not present itself?

Mr Marks—No.

Senator LUNDY—Can I ask you specifically about the investigations into the health group contract?

Mr Marks—Yes, certainly.

Senator LUNDY—That was a case where, obviously, OASITO had played a role in the processes potentially breaking down: I am referring to the inadvertent distribution of tender documentation to an inappropriate party. To whom did you report back, in terms of your probity assessment of that incident, given that OASITO was, at least in the eyes of some, perceived as a perpetrator in something having gone wrong? To whom did you report?

Mr Marks—The history of events with that was that, once OASITO became aware of the occurrence, they immediately notified me, and I held discussions with them in regard to the approach that needed to be adopted. They fully carried out my instructions, requests and advice in regard to that. At that stage, I was quite satisfied that they had done everything that needed to be done in accordance with the advice that I had provided to them. I do not believe that there was a separate sign off as a result of that occurrence, because the matter was dealt with and resolved but, at the end of the day, when I signed off on the health tender, that said that there were no probity issues outstanding. Presumably, therefore, that had been dealt with. So, if my recollection is correct, I do not believe that there was a separate sign off to anybody after that, because it was all dealt with and resolved.

Senator LUNDY—So you only reported to OASITO? You did not provide an independent probity audit assessment to anyone higher up in the department?

Mr Marks—No. I should just add that that should not denigrate the outcome

Senator LUNDY—I am not suggesting it would. I am just drawing out the facts.

Mr Marks—Okay.

Senator LUNDY—You will have to help me to understand the role that you played. My general understanding of a probity auditor's role is that it is to make observations about conduct—management conduct and process conduct—after the event and to judge and assess the degree of probity that was actually applied. The process you have just described was that your role with respect to the health bid was not to make an independent assessment of the conduct of OASITO in resolving that after the effect. You were, in fact, consulted when the problem occurred and you provided advice and were then satisfied that they acted on your advice. Do you see the distinction? I am just trying to clarify your role here as a probity auditor or a probity consultant and to find out how the two things meet or whether they meet or whether it is my problem, because I have a perception that an auditor sits out here.

Mr Marks—Perhaps I can explain that to you. Probity auditing is not the same as financial auditing. Probity auditing, as it has evolved, is not where you come along at the end of something, in normal circumstances, and sign off on it. Probity auditing in the way in which this was conducted—where there were milestone sign offs—meant that there was always an involvement in that point. A lot of the probity auditor's role is confused with probity advice, in a sense—and this is a common fact throughout all assignments—because OASITO would, for instance, provide a draft of an RFT and say to me, 'Are you satisfied with that from a probity perspective?' as distinct perhaps from a financial audit, whereby at the end of the day you get the final RFT that was sent out, and six months later you come back and review it and then say whether you agree with it or disagree with it.

The way in which probity auditing is characterised basically is by dealing with issues before they become issues. You would look at the draft RFT, make your comments on that, go back to them and say, 'Look, I don't think that if you put the RFT out in that form you're going to have proper probity or process. I would recommend to you that you change the wording of this particular section or that particular section to ensure that there is no disadvantage to any other bidders.' It is a very different role than that of a financial auditor as everybody knows it. Therefore, you are quite involved in the process, while sitting over the top of it. You do not get involved in the day-to-day side of it, but you involve yourself in a review process.

One of the things that I did very frequently was sit through steering committee meetings because quite often the probity issue would arise at a steering committee. I would then comment on that during the meeting and say, 'The course of action that you are proposing to take is going to lead you into trouble with probity.' The role is very much a proactive role, not a reactive role, as you would get with a financial audit.

Senator LUNDY—Thank you. That was very helpful. The way your activities have been described and presented at various committee tables by OASITO was that it was an external, overseeing and post-event analysis, so I am glad that we have clarified that.

Mr Marks—I am not involved in the process per se. I do not get involved. On very rare occasions would I have any exposure to bidders, for instance. My role is very much one of

looking at the pure process and ensuring that the agency—whether it be OASITO in this case or in other cases with other agencies—does not cause a breach of the process by its actions.

CHAIR—What happens, Mr Marks, in a set of circumstances where you come across a breach of process? What is the role of the probity auditor? I presume that one role is to point out the breach of process. In terms of the correction of that breach, what role do you have in that, if any?

Mr Marks—If I came across a breach I would bring it to the attention of OASITO, in this instance—or a potential breach, hopefully, before it became a breach. What we are trying to do here is to make sure we have a clean process and that, at the end of the day, someone does not turn up and say, 'Your process was flawed.' I would then recommend to them what remedy they should take to ensure that the breach was remedied. Alternatively, they would go away and come back and say, 'This is what we propose to do. Do you agree that this acceptable and will prevent a probity type occurrence?'

CHAIR—Would that set of circumstances go to damage control, as opposed to perhaps taking a step back in the process, correcting the breach and moving on from there?

Mr Marks—I don't think that I have ever been involved in damage control. That is not the sort of role that I would have. I was called in when we had this situation that Senator Lundy referred to before. Whether you call that 'damage control' I do not know, but you have to be careful with the terminology. We are not in there to fix problems that occur, but ultimately we have to form a view as to whether a process, if it is not dealt with correctly, has breached the probity of the whole tender to the point where the tender should be disbanded. Let us say hypothetically in the case you raised earlier that had OASITO not taken my advice and the circumstances had been different, it may well have been that I would have had to come out and say, 'I am sorry, but you have got a process here which is irreparably damaged and therefore requires a termination of the tender.'

Senator LUNDY—How would you have expressed that to OASITO?

Mr Marks—If that had occurred, which it had not, I would imagine I would have written to OASITO advising them accordingly.

Senator LUNDY—I appreciate this is hypothetical, but what under your contract would you be then obligated to do if OASITO rejected your advice?

Mr Marks—I think it is dangerous to deal in the hypotheticals.

Senator LUNDY—Was there anything specified in your contract as far as your notifying of higher authorities if in fact they did not follow your advice? This comes to that key point I asked earlier about whether you were working for OASITO or the Department of Finance.

Mr Marks—As I said to you, I have always been under the belief that in the event that I needed to meet or approach the minister on a particular issue I had the right to do so. That was never exercised. I always took that as being a given.

CHAIR—Were you aware, Mr Marks, of your accountability to the parliament, the fact that your reports could be made available and sought by the parliament or by these committees?

Mr Marks—I am not particularly aware of that aspect.

CHAIR—You did not have any discussions with OASITO about that aspect?

Mr Marks—I do not believe so.

CHAIR—They did not raise that matter with you? Did they raise the matter of commercial-in-confidence with your reports?

Mr Marks—I do not believe so.

Senator LUNDY—In terms of your contract with OASITO, can you describe how you were paid and at what rate? Did you have an hourly rate?

Mr Marks—I was paid an hourly rate of $275 to a maximum of $2,200 per day pre-GST and then GST on top of that. That was for the life of the contract.

Senator LUNDY—Did your contract include, apart from providing advice and doing probity auditing, being paid for appearances before committees?

Mr Marks—My original contract did. I spoke to the secretary about this yesterday. Somehow that clause disappeared on a revision of the tasks which came out as a result of the Auditor-General's report when a couple of additional tasks were added into my contract. For some inexplicable reason that clause just happened to disappear and was not picked up by me until I looked at those tasks again before I appeared here. There is some question still as to whether or not I should be paid for this appearance.

Senator LUNDY—It certainly presents some interesting questions that go to the very heart of parliamentary accountability and the relationship between contracted provisions for consultants such as yourself and their appearance before committees like this.

Mr Marks—If I can just explain why it was there. It was there at my instigation. I have made a number of appearances before parliamentary committees in line with the work that I do. It is not uncommon. I did the ACTEW-AGL merger in the ACT. One of my responsibilities was to appear every second Friday before the Public Accounts Committee of the ACT Legislative Assembly. It is not an uncommon occurrence for me to do that. I therefore request, upon appointment, that it goes into all my contracts. It is there at my instigation, not theirs.

Senator LUNDY—Given the nature of that role, did you anticipate at the time that that provision would extend to Senate committees and federal parliamentary committees of inquiry such as this?

Mr Marks—It was there because I think you are always in this role—that is, potentially able to be called—and therefore I just felt it was something that should be included in my tasks. It

was not specifically envisaged, but when you are dealing in the area that I deal in, you must always appreciate that that likelihood is there.

Senator LUNDY—Given that you are a probity auditor and given the nature of the inquiries—with the Senate estimates committees, this inquiry and previous inquiries of the Finance and Public Administration References Committee—do you think the existence of that clause could conceivably construe a conflict of interest in terms of your evidence and the fact that you have been paid for your appearance?

Mr Marks—I don't understand why.

Senator LUNDY—Virtue of the fact that it is part of your contract to appear.

Mr Marks—But why would that cause a conflict?

Senator LUNDY—I am asking you. I would make the observation that appearances before parliamentary committees are to pursue matters with witnesses that relate to issues of parliamentary accountability, and if there is a financial contract that is underpinning that appearance, then, yes, it could be perceived that there is a conflict of interest.

Mr Marks—I would not have thought so. If you are undertaking a role where you are responsible to government for the work that you do in the probity sense, then you have to accept the fact that, because you are dealing in a political environment, you may well become embroiled in a committee such as this. Accordingly, I think it is unrealistic to expect somebody who is exposed to that type of situation—and let us say it was a royal commission which could go on for years—to do it without having proper remuneration for the time they are required to prepare for it and attend. That was the basis upon which I have always requested that that clause be put into the contract.

CHAIR—If you are under contract to OASITO to provide them with advice and you come along here, presumably on the payroll—that is, they are paying you to appear—

Mr Marks—Not at this point in time.

CHAIR—I understand you are not today. But if they were and if you perhaps gave us advice or information that compromised OASITO, couldn't that put you in a position of a potential breach of contract with them?

Mr Marks—I have not thought about it, but I think you are less likely to be in breach if it is part of your contract to attend and provide evidence or whatever to parliamentary inquiries. As I say, without thinking about it too deeply, you are probably more exposed if it is not in your contract.

Senator LUNDY—Can you give any reason why probity auditors' reports, including your own, should not be made fully available to this or other parliamentary committees?

Mr Marks—I have not really considered that previously. It is a bit difficult for me to give you an off-the-cuff answer to that. I have not really thought about it before.

Senator LUNDY—I cannot help making this observation about your full understanding of the perhaps appropriate role of your appearing before committees: that you accept that as part of your responsibility, to the degree to which you will believe that you are entitled to remuneration or payment for that.

Mr Marks—I am not sure that is quite accurate. What I am providing for is the occurrence that I may be called. That is a more accurate statement of it.

Senator LUNDY—Okay. If you are an independent probity auditor, can you provide any reason why your reports should not be made available to the parliament?

Mr Marks—In fact in Victoria currently, the government has brought out a statement on probity where they have decided that probity auditors' reports will, as a matter of course, be made available to the parliament. So that is something which is happening.

Senator LUNDY—I would request that your probity audit reports associated with the government's IT outsourcing program be made available to the committee.

Mr Marks—I am not sure I am in a position to do that. I do not know whether I am permitted to do that.

Senator LUNDY—Are you prevented by virtue of your contractual relationship or by your previous contract from providing those reports to this committee?

Mr Marks—I may well be. I do not know the answer to the question but I believe there is a commercial-in-confidence element about those contract as well.

Senator LUNDY—Sorry; I am not asking for your contract: I am asking for the probity reports.

Mr Marks—I think there is a commercial-in-confidence element about that as well. I do not believe in principle that it is appropriate for those sorts of reports to be submitted. I think you have also had this debate before at the Senate estimates, and it is one that I do not really wish to get into. I do not believe I have an obligation or a responsibility to provide those reports, for the commercial-in-confidence reason which you have just been through previously.

CHAIR—I understood you to say previously to a question from me that there was no commercial-in-confidence provision in your contract.

Mr Marks—Did I? I do not recall saying that.

CHAIR—We will check the *Hansard*. but I understood that was a response that you gave me earlier on to the question when I asked you if you had a commercial-in-confidence requirement in your contract with OASITO.

Mr Marks—I do not recall answering that previously, but the answer is that I would have to check my contract to establish whether that exists or not. But, irrespective of whether that does exist or not, I would think that the answer to Senator Lundy's question is that a lot of the information that I provide is provided on that basis.

CHAIR—Can we ask you to take Senator Lundy's request on notice and have a look at your contract and advise us as to what the grounds are where you believe that you should not provide your reports to this committee.

Mr Marks—Okay.

CHAIR—Senator Lundy, I draw your attention to the fact that we are 15 minutes over time.

Senator LUNDY—Sorry. I want to ask this question again. Are you aware of any requirement in your contract that specifically prevents you from providing your independent probity auditor reports to this parliamentary committee?

Mr Marks—I would have to check the contract.

CHAIR—As there are no further questions, we thank you, Mr Marks. That concludes the morning session of this committee hearing.

Proceedings suspended from 1.14 p.m. to 2.03 p.m.

GIBBS, Mr Ian, Assistant Commissioner, Commonwealth Competitive Neutrality Complaints Office/Productivity Commission

WILSON, Mr Stuart, Manager, Commonwealth Competitive Neutrality Complaints Office/Productivity Commission

WOODS, Mr Mike, Commissioner, Commonwealth Competitive Neutrality Complaints Office/Productivity Commission

CHAIR—Welcome. Do you wish to make an opening statement?

Mr Woods—Thank you very much, Mr Chairman. As the committee is aware, competitive neutrality policy seeks to ensure that government businesses do not enjoy competitive advantages over private sector competitors simply by virtue of their public sector ownership. As part of the policy structure, the Productivity Commission Act establishes a capacity for persons to complain to the Productivity Commission in relation to competitive neutrality issues. In particular, people can complain when they consider that a Commonwealth government business or business activity is not being conducted in accordance with competitive neutrality arrangements or that in fact they should be required to be conducted in accordance with those arrangements.

For the purposes of receiving complaints, the Productivity Commission has established the Competitive Neutrality Complaints Office, which can receive complaints in relation to Commonwealth business activity. When a complainant first approaches the office, the staff discuss the nature of the complaint with the complainant and wherever practicable attempt to resolve the matter directly between the complainant and the relevant business activity. Where that is not possible, the complainant can proceed to a formal complaint. In that case, the staff of the office, under my guidance, undertake an investigation into the matters. If during that process the matter is resolved then the complainant can, if they so wish, withdraw the complaint. If not, we then proceed to a formal report to the Minister for Financial Services and Regulation. In a number of instances we have proceeded to issuing a report to the minister.

They are our formal requirements under the Productivity Commission Act. We do, however, feel that it is appropriate to embark on a broader set of activities of an educative nature, and to that end we produce research papers. Papers the committee may be interested in include one on cost allocation and pricing by the Competitive Neutrality Complaints Office and another on rate of return issues. These are available on our web site, but I am happy to make copies available to the committee if it would assist them. We publish those broadly. They are used not only by Commonwealth agencies but also by state entities—we have had positive feedback from them—which draw upon our research to assist them in their competitive neutrality dealings.

We also conduct seminars and have an advisory service, albeit informally, to Commonwealth agencies where they wish to discuss competitive neutrality issues and to ensure that they are complying with the government's policy. CSIRO, AUSLIG, Australian Hearing and the Commonwealth Rehabilitation Service are some of the agencies with whom we have worked closely to ensure that they are complying with the CN policies. It is in that context, in the sense

of providing advice, that we have had dealings with the Office of Asset Sales and have provided them with advice, both at meetings and then subsequently formally in correspondence. Last year they asked us certain questions relating to competitive neutrality policy and we provided them with a written response on those matters. The three matters in particular related to the weighted average cost of capital that they were utilising, the appropriate asset base and cost allocation. We have made available to the committee some matters of principle that we consider are relevant to the issues before the committee and its current terms of reference. I have also made available to the committee a pamphlet which you may find of use to understand the background of the Competitive Neutrality Complaints Office and the functions that we undertake.

CHAIR—Thank you, Mr Woods.

Senator LUNDY—Have you had the opportunity to familiarise yourself with the findings of the Audit Office report into the whole of government information technology outsourcing?

Mr Woods—We are aware of that report and have read the relevant areas of it.

Senator LUNDY—Obviously it deals, reasonably extensively, with the issue of competitive neutrality. Are you in a position, as a complaints office, to offer a view or an opinion about the different financial methodologies used to construct a competitively neutral environment in terms of both the methodology advocated by the Audit Office and the financial methodology used by the department of finance?

Mr Woods—We can certainly advise you of ours and indicate to you where that coincides with the audit office, if that would be helpful.

Senator LUNDY—Yes, please.

Mr Woods—Perhaps I can deal with the question of the weighted average cost of capital first. The Audit Office looked at that question in their report as to the degree of commercial risk that tenderers were likely to be undertaking in tendering for IT business with the government. The Audit Office came to the view that the level of risk that was being undertaken by successful tenderers was less than normal commercial risk in that the government was accepting some capital risk directly. In that case it would be appropriate for an evaluation of the in-house cost of providing IT services to similarly adopt a lower level of risk. The consequence of that would be by having a lower risk factor. It would reduce the cost of capital and, accordingly, it would reduce the apparent cost of providing services in-house relative to having a normal commercial level of risk. That would therefore close the gap on the apparent difference between in-house provision and provision by whomever is the successful tenderer. In that instance we agree with the Audit Office or would adopt a similar methodology to that pursued by the Audit Office.

Mr Wilson—I will just elaborate on that slightly. Conceptually we certainly accept what the Audit Office is saying, but we ourselves have not seen the data or the documents that the Audit Office has, so we are not able to form an independent judgment on whether—

Senator LUNDY—So you have not audited the auditor?

Mr Wilson—That is right.

Mr Woods—Our role is activated in a formal sense when we receive a complaint from an entity but, as I explained, we also have this role that we see as appropriate of providing general principles and guidance to agencies because our preference is that they comply in the first instance rather than get caught up in a formal complaints process at the back end.

Senator LUNDY—Has this process, by virtue of that general role that you describe, led you to develop a guideline or a proforma on how an agency or department could construct a methodology to assess competitive neutrality, particularly in the context of the government's market testing initiative now being handled by the department of finance?

Mr Woods—We have developed some research papers that agencies draw on quite extensively, such as dealing with particularly the more vexed questions of cost allocation, pricing and rate of return. We also publish, through this pamphlet and other material, their requirements across all areas of competitive neutrality. We do not develop some of those—such as regulations that businesses would be expected to comply with by paying directly either local government rates, state taxes or making tax equivalent payments—in detail because we consider that they are fairly self-explanatory. We are focused on some of the more technical issues that are quite often very familiar in the commercial world, but government agencies which have, particularly prior to the last few years, grown up in a cash environment would not necessarily be familiar with those. We have focused on those areas where we think we can add greatest value and those are technical issues.

Mr Gibbs—To elaborate on that, a lot of elements of competitive neutrality policy are specified in fairly general terms, such as an agency should earn a commercial rate of return and it should allocate its costs appropriately. Those are actually pretty complex issues. As Mike said, we have attempted to unbundle some of the more complex areas and to say, for example, if an agency is going to allocate costs properly: what does that mean? As this publication sets it out, it is a bit of horses for courses. You might want to do it one way in particular circumstances and do it another way on another occasion. In that sense, there are difficulties in developing a general pro forma, which is why we typically respond informally to government agencies when they say, 'Are we doing the right thing? Is this appropriate?' or give them a view through written advice.

Senator LUNDY—In terms of being a complaints body, from whom do you normally get complaints?

Mr Woods—Usually from the private sector when it considers that government businesses are winning business and may not necessarily be fully complying with the Commonwealth competitive neutrality policies. For example, one of our early reports was into the Australian Institute of Sport swim school, where private providers of pools in Canberra—I think Senator Lundy might recall the general issue—considered whether they were unfairly dealt with by the success of that swim school in making its facilities available to the public. We undertook an investigation and produced a report which drew attention to several small matters which would assist the Australian Institute of Sport with fully complying but which were not material to their overall position in the marketplace. That illustrates the types of complaints we receive. We receive more informal or front-end complaints and we are usually able to put the two parties together and resolve the matters, but sometimes we go right through to a formal report.

Senator LUNDY—In relation to the document of which you have just made me aware, how long has that information been available in that form, in the context of the IT outsourcing program?

Mr Woods—The cost allocation and pricing document was produced in October 1998 and the rate of return issues document was produced in December 1998. They have been around for several years.

Senator LUNDY—And arguably they have been available to agencies, departments and private companies?

Mr Woods—Yes, they are publicly available documents. They are on our web site and anyone can access them.

Senator LUNDY—Is it reasonable to observe that agencies and departments, for example OASITO and the department of finance, would be familiar with the specifications and detail of those documents?

Mr Woods—Our records show that we first had informal discussions with OASITO in 1998 and that there were informal discussions right through until mid-2000, at which point in time they formalised a set of questions to us and we responded to them in writing.

Senator LUNDY—So between mid-1998, or thereabouts, through to about mid-2000, you had—how would you describe it?—monthly or quarterly contact with OASITO?

Mr Woods—No. There were probably only three or four contacts during that period when they asked general questions of principle, but it demonstrated that they were aware of what we were doing and were conversant with our material.

Mr Wilson—Those meetings were prefaced with, 'We're happy to discuss things on an informal basis, but if you want CCNCO views you should write to us and we will provide advice.'

Senator LUNDY—They did not write to you until when?

Mr Woods—On 5 September 2000.

Senator LUNDY—On 5 September?

Mr Woods—Yes.

Senator LUNDY—So that was the first opportunity that they sought to formally seek your advice on issues relating to competitive neutrality?

Mr Woods—Yes. That was the culmination of several meetings that were held with my staff in July of that year. They put their questions to us in writing on 5 September, and we responded on 5 October.

Senator LUNDY—You say that on 5 September they—

Mr Woods—That is when they wrote to us.

Senator LUNDY—It is interesting to note that the Australian National Audit Office report was released publicly on 6 September 2000. It is not an issue for you, but believe me it is an interesting one for the committee.

CHAIR—That was a very precise answer; you must have been expecting the question.

Senator LUNDY—Are you able to make available to the committee the advice that was sought and provided to OASITO?

Mr Woods—Yes, we are happy to table the correspondence.

Senator LUNDY—Thank you.

Mr Wilson—We had also attempted to distil that correspondence in the submission we provided.

Senator LUNDY—Yes.

Mr Woods—In what we put to you is the key—

Senator LUNDY—The substance of it—I appreciate that.

Mr Woods—It is the correspondence itself, and certainly our response to them. I would need to consult with them, presumably, on their letter to us, but it has been received by us. We responded, so I am happy to—

CHAIR—Are you in a position to table that now?

Mr Woods—That is our letter to them. If you do not mind, I will consult with them about releasing their letter to us, but I do not envisage any difficulty. Our response is fulsome in understanding both sides of the correspondence, anyway.

Senator LUNDY—Thanks. Had you offered previously, in writing or informally, to provide more formal advice to OASITO prior to the second half of 2000?

Mr Woods—We preface our conversations with people by saying that we are happy to discuss things at meetings or on the phone, but, if they would like a definitive and considered position, then in writing is the best way of achieving that, and we have made those points to OASITO during that time.

Senator LUNDY—So is it reasonable for me to ascertain from that that OASITO chose not to seek formal advice from your office prior to 5 September 2000?

Mr Woods—That would be a matter for you to ask them, Senator.

Senator LUNDY—Going back to your view that the government was accepting a level of capital risk associated with outsourcing by virtue of—

Mr Woods—That was the view of the auditor in the auditor's report.

Senator LUNDY—But you concur with that view.

Mr Woods—Our view is that if that is the case, then—

Senator LUNDY—You need to offset that?

Mr Woods—on CN grounds, the risk built into the evaluation of an in-house costing should similarly reflect that lower level of risk.

Senator LUNDY—I accept that clarification, thank you. What reasons could be behind using different valuation methods for competitive neutrality? Provided the offsets are equal, what else could conceivably constitute a reason or justification to vary the methodology that you use?

Mr Woods—The only answer that I can provide to that is that our advice to all who ask is that to ensure competitive neutrality, even in the case where it is not an in-house bid but an in-house evaluation of costs, you should adopt the principle of like with like. Any deviation from that is not a deviation that we would support.

Senator LUNDY—So you are not in a position to, or choose not to, cast judgment on the various merits of different methodologies?

Mr Woods—I can cast judgment on the methodology which says that the methodology should adopt like with like. The motives for such are beyond my ability to respond.

Senator LUNDY—Because it is not part of your scope or because you do not see it as your professional role?

Mr Woods—We are there to assist them to comply with competitive neutrality, and competitive neutrality requires like with like. We do not encourage or entertain people going beyond that somewhat simple principle.

Senator LUNDY—Within your office?

Mr Woods—In our advice to others.

Mr Gibbs—You will note in that letter we have just tabled that we have said in a few cases, 'You could, for example, value assets this way or you could value assets that way, but the key thing is to make sure that you are valuing the same way for both the in-house tender and the out-house supplier. You can probably mount arguments for either particular methodology, but from our point of view the key thing is that those methodologies are the same.' You will also

notice in that letter that we actually raise a possible argument that could have been used to justify a difference in methodology and we go on in that letter to knock it on the head.

Mr Woods—And draw the obvious inference that different methodologies applying to an in-house costing versus external tendering could lead to a wrong conclusion about the relative merits of the two.

Senator LUNDY—Do you have a comment on the DOFA whole of government's response? I am referring to page 33 of the Audit Office report, where it says:

ANAO *recommends* that, to ensure competitive neutrality adjustments are consistent with the conditions on which tenderers' pricing is based, OASITO, in consultation with DOFA, review the methodology to be applied in future IT outsourcing tenders for the calculation of adjustments for the required rate of return on agency assets in situations where the Commonwealth underwrites the asset risk of tenderers.

DOFA disagreed with that recommendation.

Mr Woods—Which recommendation number is that? I do not have the report in that form; I have it in a different form.

Senator LUNDY—It is recommendation No. 15, paragraph 7.78.

Mr Woods—I have that here, thank you.

Senator LUNDY—Could you read that quickly, note that DOFA disagreed, and give me your view on DOFA's disagreement?

Mr Woods—It is difficult to understand whether DOFA are disagreeing that there is a need for a review or disagreeing with the underlying principle. We would support the underlying principle of consistency in pricing and costing. I do not know from this what it is that DOFA are disagreeing with.

Senator LUNDY—The way I interpret that is that they are disagreeing with conducting a review. You are quite right; it does not indicate whether or not they are agreeing with the underlying premise.

Mr Woods—They produced, and I assume the committee is aware of it, a competitive tendering and contracting document in March 1998 which has an attachment which deals with competitive neutrality. That is perfectly consistent with the position that the Competitive Neutrality Complaints Office adopt. We do not have a disagreement with DOFA's own published documentation on competitive tendering and contracting, as set out in that attachment B, so I would not understand any disagreement between us on that principle.

Senator LUNDY—I have just realised that I do have an extrapolated response here from DOFA in relation to recommendation No. 15. DOFA disagrees and says, as part of justifying that disagreement:

OASITO has previously reviewed the methodology having regard to asset risk allocation issues and has obtained expert advice that no change to the ROI—

return on investment—

component of the competitive neutrality calculation is required. This approach is consistent with Government policy on IT outsourcing.

So I was actually incorrect when I interpreted its previous disagreement as being in association with the review. It is actually making a formal comment on challenging the underlying premise of the recommendation.

Mr Wilson—That goes to the issue of whether the Commonwealth is accepting a greater degree of capital risk, as the ANAO suggests. As we suggested earlier, that is not something we are privy to any information on. We are not disagreeing in any sense, but it is just not something we are able to form a judgment on. The point Mike has made is that, if that is the case, then it is appropriate that a lower rate of return be built into the business costing.

Mr Woods—I think people reading *Hansard* would appreciate understanding where that document you were just quoting comes from.

Senator LUNDY—I was quoting from page 178 of the Audit Office whole of government information audit report.

Mr Woods—Chairman, you might note that in that letter we draw upon a third area relating to cost allocation and just draw the attention of the Office of Asset Sales to the conclusion in our correspondence that if you apply fully distributed costing you can in some circumstances get a different answer about long-term avoidable costs. In our research and publications, we prefer the latter. That is a not a comment on which form of costing they have utilised or what in that particular case the outcome would have been, by way of comparing the two, but we find that that is quite often an area that agencies are not always conversant with and understand the detail of. That is why that particular issue has been raised in our correspondence.

Senator LUNDY—I will move on to a different area. Have you examined any complaints either prior to 5 September or after about competitive neutrality issues associated with the IT outsourcing program?

Mr Woods—No, we have not received any complaints from any party in relation to this process.

Senator LUNDY—What about inquiries?

Mr Woods—Only inquiries from the Office of Asset Sales and the Audit Office, and one consultation with Commonwealth Treasury to confirm with them a particular approach we were taking; but not from the private sector in relation to the complaints mechanism. It might help the committee if I point out that in preparation for this we noted that there are no in-house bids, at least evidenced by the number of departments that were drawn on through inquiries by you and, I suspect, the estimates committees. In-house businesses are not putting bids in, in which case—

Senator LUNDY—They are not permitted to. That is right.

Mr Woods—it would not come before us in a formal sense. It is only when there are in-house bids that there is an ability for an external party to then draw a complaint if it considers that a Commonwealth business is not complying.

Senator LUNDY—Just to clarify the process of initiating a complaint, does it work in the reverse as well; that is, a department could award a contract to someone in the private sector that the in-house bidding team felt was unfair?

Mr Woods—That is possible. For the record, we actually have not had any such complaints.

Senator LUNDY—I was not sure whether you had or not. I just wanted to clarify that you are a complaints body for in-house bidders as well as outsource bidders.

Mr Woods—We are there for all, Senator.

Senator LUNDY—It is like with like, isn't it?

Mr Woods—Indeed.

Senator LUNDY—The other question I have—and I do not know how involved you are in this and, if you are, it is probably more about the proactive work that you do in considering possible scenarios: we heard from an officer of OASITO that, once these contracts are in place, their structure and design led the agency or department to be effectively locked in—I am paraphrasing. It implied that there was some restriction on post-contract competitiveness of other bidders coming in and participating in that next round, if you like. Do you see what I mean?

Mr Woods—I understand your point. That is not an area that would come within our area of responsibility.

Senator LUNDY—Right, okay.

Mr Woods—The length of contract, the renewal of contracts and the like are not CN issues in that strict sense.

Senator LUNDY—Once it has been contracted out, if it is an argument between, for example, the incumbent contractor and a new contractor over the terms and conditions of the request for tender, it does not come near you.

Mr Woods—That then goes back through contract law and they have certain remedies.

Senator LUNDY—Right. Just a final question about the procurement guidelines that you held up: what is their title?

Mr Woods—It is headed *Department of Finance and Administration competitive tendering and contracting guidance for managers, March 1998*. I was drawing on attachment B to that, which is headed 'competitive neutrality'.

Senator LUNDY—I wanted to ask you a question about that. My understanding is that it contains a clause in it which provides for ministerial discretion and having an ability to override a range of competitive tendering provisions.

Mr Woods—I am not familiar with that. I am familiar with attachment B and I cannot recall any such phrase in that particular attachment.

Senator LUNDY—All right. It is not in the attachment; I understand it is in the body of the document. My question to you is: do you have any role in handling complaints where people feel that generally the competitive tendering process has been not adhered to with due diligence—for want of a better phrase?

Mr Woods—Only in so far as the powers of our act which allow a person to complain where they have been competing with a Commonwealth government business or business activity and they consider that it is not conducted in accordance with competitive neutrality arrangements or, indeed, that it should be required to be conducted in accordance with CN. So that creates the boundaries of our legislative responsibility.

Senator LUNDY—So conceivably it could be related, but you have not done that yet.

Mr Woods—No, we have no such instances that I can recall.

Senator LUNDY—Thanks, Mr Chairman.

CHAIR—Senator Eggleston?

Senator EGGLESTON—I am fine, thank you.

Senator LUNDY—Have you had the opportunity to assess each of the recommendations in the Audit Office report for the degree of relevancy to the scope of work you do?

Mr Woods—We have looked at the ones that relate to our area of responsibility. As I said, in the case of the weighted average cost of capital, it was consistent with the position that we would adopt.

Senator LUNDY—I do not think I have any more questions.

CHAIR—Just one question. Did you have any discussions with DOFA with respect to the competitive neutrality factor to be applied that they used in calculating the savings out of the IT outsourcing initiative?

Mr Wilson—I cannot remember any discussions with DOFA over the rate of return calculations. We have discussed issues with Treasury. We have discussed issues with DOFA on other aspects of competitive neutrality in the last few months, but that was not related with outsourcing at all. There have been no discussions with DOFA on rate of return issues.

CHAIR—Thank you Mr Woods, Mr Wilson and Mr Gibbs. I call the representatives from the Australian National Audit Office.

[2.41 p.m.]

BARRETT, Mr Patrick Joseph, Auditor-General, Australian National Audit Office

CRONIN, Mr Colin, Executive Director, Australian National Audit Office

LONG, Ms Tina, Senior Director, Australian National Audit Office

McPHEE, Mr Ian, Deputy Auditor-General, Australian National Audit Office

CHAIR—Mr Barrett, do you wish to make an opening statement?

Mr Barrett—No, thank you, Mr Chairman.

CHAIR—Mr Barrett, we had a discussion just before lunch with Mr Marks who was the probity auditor. It certainly left in my mind some confusion as to what the difference between a probity adviser or probity consultant and a probity auditor is. Is there any definition as to what the functions of a probity auditor are? Or is there any difference between a probity auditor and a probity consultant or probity adviser?

Mr Barrett—I cannot help you very much on that, I am afraid, Mr Chairman. Certainly we have a view about what a probity auditor is. Probity consultant and adviser, to my mind, connotes some lesser role than the actual audit. With an audit, there is clear independence for a start; there is usually a requirement to report in some way. An auditor needs to deal equally with all parties and needs to ensure that issues are brought to the immediate attention of the relevant people so that appropriate action can be taken. And at the end of the day I would expect a probity auditor to ensure that issues are made available to all parties so that not only has justice been seen but also justice appears to have been done. There are quite technical aspects, of course, of auditing such as the criteria that you have for a start, the fact that you make those criteria available and then you report on those criteria. The criteria in this case would be accepted by the parties concerned and, in my opinion, that would be the discipline associated with an audit process.

Mr Cronin—There has been a very good report done in South Australia by the South Australian Auditor-General on the electricity business disposal process. We can make available that report. It covers the issues relating to probity advisers and probity auditors and runs to the question of sign-offs that are provided, probity principles and the need for those in the context of an overall probity plan. We have a short extract of that report and we can provide that to the committee now.

CHAIR—Does it make a clear distinction between the role of a probity auditor and a probity adviser?

Mr Cronin—Yes, it does. It says that a probity auditor independently monitors the conduct of the outsourcing, while a probity adviser provides advice to those conducting the process. So

one is totally independent—it is the nature of an auditor to be independent. It is quite well spelt out there. We actually drew on this report for the comments we make in the audit. We do not have the full report but we have a small extract here. It gives you an idea about sign-offs, the importance of the probity sign-off and about agreeing to that at the beginning of the engagement.

CHAIR—Are you giving that to us or do want us to copy it and give back to you?

Mr Cronin—You can have it. It is available on the Net anyway.

Ms Long—In that report, the South Australian Auditor-General actually recommended that there be a clear separation between the roles of probity adviser and probity auditor, to ensure the probity auditor's independence from the actual tender or sale process, as it was in that case. That is footnoted in our report on page 88, in footnote 94, as part of the contextual material that we presented about the need for a clear delineation in the roles.

Senator LUNDY—I want to clarify a point. I do not know whether it is contained in the summary of your report and I am not familiar with that report so you might have to help me, but I was sure I heard Mr Marks say this morning that he was in fact engaged by the South Australian government with respect to electricity in South Australia.

Mr Cronin—He may have been engaged by the South Australian government. The South Australian Auditor-General looked into the process of engagement of the probity auditor and there was a separate report to parliament. That is what his report relates to.

Ms Long—If it assists the committee—and obviously you will need to check the *Hansard*—we did observe that evidence, and my recollection is that Mr Marks was referring to engagement in terms of the panel of IT contractors in South Australia.

CHAIR—He was involved in the Victorian electricity set-up, not the South Australian electricity set-up.

Senator LUNDY—Thank you for that clarification. You are quite right. I would like to go further on this issue of the definition of an auditor. In your view, and in the context of your traversing this issue in your report, is the role that Mr Marks played within the organisation of OASITO consistent with what you would describe as a 'probity auditor' or with what you would describe as a 'probity adviser' or 'probity consultant'?

Mr Cronin—I think there are a number of aspects. He was initially advised to perform a range of functions, which were those of an auditor. The scope of his assignment subsequently changed. If the committee has available the schedule of work that he was required to undertake, you will see that it changed at various stages. I think that in terms of what is being conveyed to us about him providing advice, it would appear that he was more in the nature of a probity adviser as opposed to a probity auditor. There is a deal of confusion about what these terms mean and I believe that in the South Australian Auditor-General's case, they had the Australian Government Solicitor provide extensive advice to them, hence the clarification of the question of roles of auditors and advisers. That is probably the most comprehensive coverage of the subject that we are aware of.

Ms Long—The other area where there was scope for some confusion as to the role goes to an issue that Mr Barrett raised, which is that in terms of an auditor you would normally expect there to be clearly articulated criteria that form the normative model that the auditor would expect to see in place if the process were being conducted in the manner that would be expected. The auditor would then audit against those criteria and provide a report that would make it clear what the criteria were, what work was undertaken to form an assessment, and what the assessment was. We have discussed in the audit report the fact that we were not able to identify where those of the probity principles that were being considered—or the criteria or the testing being done to assess how they had been complied with—had actually been articulated by the probity auditor in this instance.

Senator LUNDY—You have commented in the audit report on DOFA's response to recommendation No. 6. I am looking at pages 91 and 92 of your report, who go to that issue of the sign-off. Are there other aspects of concern that you have with the DOFA whole-of-government response to that recommendation? Can you be more specific about what you would see as the ideal arrangement in terms of having a genuine probity auditor role in place?

Mr Cronin—I think the role is split into a number of phases. We would see the role of a probity adviser or auditor as being to provide a high level of assurance. The final outcome is essentially the auditor's sign-off. We are probably looking there at three steps. You need to look at what the sign-off is actually to consist of. What is agreed between the auditor and the engaging party that will be signed off? What is the certainty you are looking to, so that the person who is relying on it knows the coverage that is under way? What is the totality of it? So the sign-off would incorporate that, and that would feed into your probity principles, because that would tell you about the scope and the job that was done.

You would need to look at the report that was done. As we are aware, there was no report; a series of one-page sign-offs were provided. To rely on that, you need to understand the overall context. So the person who is relying on it would need to know: what were the criteria against which judgments were made? What were the exceptions that were brought forward, if there were any exceptions? In auditing, you can have a qualified report, an adverse report or an unqualified report. All these things mean something to the party receiving them. In probity auditing, there are no standards as such laid down. So it is very important to have principles which you can be judged against.

Mr Barrett—I would expect the probity auditor to be quite proactive in this arrangement. When issues come up that deal with fairness, equity and fair handling, I would expect the probity auditor to comment on the criteria that are being used and, as necessary, give advice based on probity principles, to ensure that the people who are taking the decision at the time take those into account. This is one of the reasons why my office has been reluctant to engage in probity audits. We have been asked many times to do so. We see that this starts to get into potential conflicts of interest, particularly if we are latterly going to audit the process.

Senator LUNDY—In terms of the role of a probity auditor, do you have a view—reflecting on the arrangements with Mr Marks in OASITO—that availability of those, in this case, one-page sign-offs, should be beyond just the agency that engages the probity auditor? Would a probity auditor normally sit outside the organisation that they are actually auditing, for the purposes of accountability and reporting? I am not sure whether I have expressed myself very

well but I am trying to ascertain whether there would normally or appropriately be someone higher up that the probity auditor reports should be supplied to in the course of their duties.

Mr Barrett—My colleagues might have a view on this but let me make a comment first. One of the issues which applies, particularly in the light of what I have said about an advising probity role, is that you cannot transfer responsibility and accountability. One of the problems here is that people think that because you establish a probity auditor, somehow you do not have to worry about that anymore; that risk management is finished. Of course, the risk management starts and finishes with you. So when you are looking for someone to report to, of course the people who are in place who are responsible for this contract cannot absolve themselves of their responsibilities. All the probity auditor can do is to say, 'I've looked at these things; yes, it was done in accordance with the criteria,' and then sign off accordingly. But that does not take the responsibility that is on the probity auditor's head away from those people who are rightly responsible for the contract, for instance.

It may obviously be a comfort, an assurance, to have that but, at the end of the day, in the normal reporting process within organisations, particularly the chief executive officer—at least, in the Commonwealth sense—as the final person responsible for the efficient, effective and ethical use of resources would need to have that kind of assurance, both from the people immediately involved in the contractual arrangements, the parties involved, and the probity auditor. You cannot just simply have the expectation that the probity auditor will take over all responsibility.

CHAIR—I think the issue that Senator Lundy was really referring to was the set of circumstances that occurred in respect of the IT outsourcing where OASITO was the agency responsible for managing the process. They also were the agency that contracted the probity auditor. Should that then consequentially be a situation where the probity auditor reports to OASITO on a commercial-in-confidence basis?

Mr Barrett—The only reason I am hesitating slightly is the commercial-in-confidence situation. At the end of the day I think there has to be transparency, particularly in the public environment. Unless some issues had come up that impacted adversely on an individual contractor or the tenderer in terms of conflict of interest with regard to their intellectual property or the like—some commercial aspect of the arrangements they had made—in the normal course of events I could not see why that would happen, frankly, unless my colleagues correct me on this. In terms of the probity audit process, we are not talking about pricing; we are not talking about the assets that are involved or the particular way in which the business is going to be conducted or intended to be conducted by the potential tenderer. Also I would think that the agency involved would deeply want to have some kind of assurance, for the reasons that I have indicated to you, and of course is at the heart of the Humphry review. Clearly, while OASITO had that responsibility, at the end of the day the agency and the agency head are the ones who have to deliver.

Senator LUNDY—That is probably a good point to raise with you. I want to go to the issue of the Humphry review and the recommendations contained in that. Given that they highlighted the issue of responsibilities by heads of departments under the FMA Act and the CAC Act, is it the Audit Office view that you concur with the findings and the recommendations in relation to that?

Mr Barrett—As you know, it is not our role to agree or disagree in these respects. Quite clearly, there were issues that corresponded quite closely with the issues we raised in the audit. Some of the implications were taken up more directly by the Humphry review than we had made clear in the audit report, because the review had a different focus. Generally, we are in broad agreement with the thrust of the Humphry review. I would not want this to be taken that, somehow or another, we are against outsourcing. I have to say—and it might be defensively—that that is not the case at all. We are sometimes accused of being against outsourcing, but that is not the case.

Senator LUNDY—I know the feeling, Mr Barrett.

Mr Barrett—Certainly in this environment—where, at the end of the day, we are asking for clearer responsibilities, accountability, and greater transparency—I think the Humphry recommendations, as obviously agreed by the government, are much more likely to ensure that the people responsible will have to stand up and be counted for the result.

Senator LUNDY—Going to a technical point about the competitive neutrality factors that we were discussing with the previous witness, the competitive neutrality factor applied by DOFA was 0.5 per cent. Are you of the view that that had a significant impact on the calculation of savings by DOFA?

Mr Cronin—Does this relate to the actual DOFA IT outsourcing?

Senator LUNDY—It relates to the DOFA methodology.

Mr Cronin—We did not review the DOFA IT outsourcing, which is swung off the DVA. But we do know from the competitive neutrality applied that it generally accounts for 20 per cent to 30 per cent of the overall savings. Turning to figure 1 on page 19 of our report, for example, we do not agree with OASITO's views on cluster 3, but they reported $33.2 million out of $60 million. So, essentially, it was nearly half of their financial savings. A factor of 0.5 is an incredibly low number on any of them. The competitive neutralities are quite significant in terms of the notional savings. So, while we have not looked at DOFA, 0.5—which is half of one per cent—would be 40 times what we have seen. The numbers on competitive neutrality that we would normally expect would be much higher than that.

CHAIR—That would give you an inflated savings outcome, obviously.

Mr Cronin—On ours, but the DOFA figure that Senator Lundy mentioned is extremely low. It does not come within the normal bounds that we saw on the three major tenders. The tenders we looked at had much higher significance for CN, as you can see in figure 1 there.

CHAIR—Setting aside the IT outsourcing, are there any other areas where you have looked at this issue of competitive neutrality?

Mr Cronin—I am not aware of it coming up in audits that I have been associated with.

Mr Barrett—I cannot remember, offhand.

CHAIR—What about the commercial support program in Defence?

Mr Barrett—I would have to check out that one for you and let you know.

CHAIR—Could you let us know whether the figure is in the similar sorts of bounds that Mr Cronin is talking about?

Mr Barrett—Yes.

Mr Cronin—Applying competitive neutrality rate of return to anything involving assets will generate significant outcomes. So, if you actually have assets in play there, you would expect a significant number. If we look at the ATO and group 5, you will see that the numbers are quite significant. There are special circumstances that relate to cluster 3, where the competitive neutrality was applied to the turnover not to the assets; but we believe they were overstated by a factor of about two. Normally, you would expect competitive neutrality to have a significant impact.

Mr Barrett—It is highly likely when I think about it, because a lot of Defence in-house bids one in-house version. We will get back to you on that one.

CHAIR—Thank you.

Senator LUNDY—Further on that question of competitive neutrality calculations, following your report and the Humphry review are you confident that a consistent methodology will now be applied through Commonwealth agencies and departments for assessing the competitive neutrality component of any proposed outsourcing? Is there any evidence to give you confidence that that will occur?

Mr McPhee—No, we have not seen any guidance issued for the benefit of agencies in this area. It would seem to me that it would be beneficial if that were to occur.

Senator LUNDY—Have you been asked to provide advice to the government in any way to resolve and bring clarity to this issue of how agencies and departments assess their competitive neutrality components of any proposed outsourcing?

Mr Barrett—No, but we would not expect to be either.

Senator LUNDY—Okay.

Mr Barrett—We would always obviously respond if we are asked on any technical grounds on any issues that deal with our audit processes, but certainly with the agencies involved I would not expect that we would normally be asked.

Senator LUNDY—Can I just clarify that. I saw recently what I took to be a better practice guide from the Audit Office in another area—I think it was related to the Internet—

Mr McPhee—Yes, Internet service delivery.

Senator LUNDY—So is it conceivable if you were requested by government to prepare a better practice guide on assessing competitive neutrality that you could do that?

Mr Barrett—Why do we do better practice guides? If you can bear with me for a minute while I ask it around the other way. It is because we have the opportunity of looking across a range of agencies in particular audit areas in which a particular issue comes up, like Internet service delivery. We gave the one I have here on contract management to all members of parliament. In the absence of anyone else having an interest in producing such material, it is important not only for guidance but for audit purposes, because we use the better practice guides as the basis of audit criteria. In this case, you have a separate agency responsible; the portfolio agency has a clear interest—that is, DOFA. In the normal course of events in the past, if we were doing a number of audits in this area where this issue came up, we would have approached the agencies concerned and said, 'In the absence of any guidance in this area, we recommend you do guidance, but we would be happy to join with you on the basis of the information we got out of this audit and do a joint better practice guide.' In fact, we are just about to do another one with Comcare and it will be out in the next few weeks. So, in the absence of a situation of that kind, the answer is no. But, clearly, if we see that as a significant audit issue, you could expect us to raise the issue with the relevant agencies.

Senator LUNDY—Do you see the potential for myriad competitive neutrality assessment formulas emerging from different departments being such an issue?

Mr Cronin—If the departments follow the Competitive Neutrality Complaints Office's December 1998 paper, I do not think there should be any problems. That seems to set out a reasonable basis on which to assess competitive neutrality. As we report in the audit, OASITO's approach has changed over time. While we differed in terms of the question of risk, the general approach of applying a rate of return to assets gets down to the actual numbers which should be used; and this is the basis. But the Competitive Neutrality Complaints Office have a three-part thing. They say low, medium and high risk, and they have different risk weightings they apply. That seems to be a reasonably robust means by which you would apply competitive neutrality.

Senator LUNDY—Do you think that, given we know that DOFA plans to keep a residual unit of OASITO in their department and capitalise on what they consider to be their considerable expertise, and given the fact that DOFA have effectively rejected criticism of their methodology, there is a chance that DOFA will, through that residual part of OASITO, continue to provide advice to agencies about competitive neutrality formulas that is inconsistent with the approach that you see as being appropriate?

Mr Barrett—I would hope that is not the situation. History shows that where agencies get more knowledge and understanding of the approaches that are being taken and the guidance provided by some central agency there usually comes to be agreement on the proper approach to be taken. It does not do anyone any good to have different approaches that are not agreed, and constant tensions with people using different figures, particularly when they are coming to the parliament and asking the parliament to arbitrate on one person's views about a particular set of figures and another person's views about the same figures. So commonsense really should prevail in those sorts of situations.

Senator LUNDY—I would hope so. I would like to go to a different issue now. Can you tell me the status of the audit inquiries into Group 8 and the health group IT outsourcing contracts?

Mr Barrett—As you know, we are into a different ball game now. While we were intending to look at that one reasonably soon in the normal course of events, that will now probably not occur until 2002, will it?

Mr Cronin—No. In fact we have dropped it off the program.

Mr Barrett—Yes, but it is not likely to come back in. We are talking outside our immediate program; that is what we are talking about.

Senator LUNDY—Correct me if I am wrong, but my understanding is that it was the office's intention to pursue a report into both of those contracts.

Mr McPhee—We certainly had it in our draft forward program. Our feeling is that, the world having moved on following this report and the Humphry review, we would be better to allocate our resources to looking at one of the new outsourcing proposals after it has occurred under the new arrangements. We have highlighted quite a range of issues in this report and we felt that in some ways we would be covering very old ground by just looking at the previous model again. Having said that, if the committee had any particular interests in any areas we do have a mechanism whereby we get the views of parliamentary committees on our audit programs; so, if there were any residual interest, obviously the system would allow the Auditor-General to take that into account in confirming the program. I should say that we have not yet settled the program. It is out there in draft form, and so there is still opportunity for feedback to the Auditor-General on the program.

Mr Barrett—It is really looking at how it is working. We are not going back to how it was done—that is old history—but, in a sense, to how it is working now or at some stage. It is not insignificant in the scheme of things, and so consequently we would look at any of these kinds of contractual relationships from time to time.

Senator LUNDY—You can guess my view on that, anyway.

Mr Barrett—Yes.

Senator LUNDY—I think it would be particularly useful for that work to be done. Nonetheless, there are other avenues where we can pursue that.

Mr Barrett—Do you mind if I get some clarity on that? When you say that it would be useful to look at it, are you talking about how it was done or how it is operating now?

Senator LUNDY—It is a combination of both. There is a specific interest in the tendering processes and applying the tests that you have effectively constructed by virtue of this previous report to both of those contracts for the sake of completeness of your analyses. That is one part of it, certainly. The second part would be a somewhat separate exercise in assessing the ongoing merit of those contracts and their operation, and that raises another series of questions which was not addressed in this report, but it stands out now as each of those contracts has progressed.

The tests you have constructed provide some benchmarks at which you could assess the ongoing implementation of those contracts. That work and that information can continue to inform public policy development in this area. It is important work for those reasons, but I acknowledge that there are two almost separate tasks in conducting those assessments.

Mr Barrett—Yes. As I was trying to say to you earlier, we will use this better practice guide on contract management as a basis for looking at these sorts of contracts and assessing them against that better practice. Obviously, any embedded arrangements that influenced the better practice in the sense of adversely impacting on it will be reported on. A question then would be: how do you deal with it? You have to wait until the next iteration of the contractual arrangement to deal with that issue. Another question, for instance, would be: can you renegotiate, and, if so, what are the implications of doing that?

Senator LUNDY—Yes. One issue of concern that is worth highlighting is: what happens at the termination of the first stage of these contracts, one of which is obviously coming up in the not too distant future, but the others will progressively come up? Considering that we have had an interesting statement from an officer of OASITO—that is, that these contracts were constructed with the view that they would effectively remain in perpetuity—I expect that some very serious accountability issues, including the way in which departments find themselves potentially captured by those contracts, will be of significant interest to the Audit Office as well as to the parliament.

Mr Barrett—The better practice guide has a lot of comment on transition, and not surprisingly. Better practice in this industry, as well as in other industries in Australia and overseas, says that you should be planning for transition literally from day one—in other words, you should be looking at it. That does not necessarily mean that you are going to go to a different contractor, but you should be planning for transition, whether it is with the existing contractor or a replacement contractor. These issues are for agency management to start to plan and work on. I would expect that, if genuine partnerships are being created with the private sector—and I hope there are—the private sector contractor would see it as being in their interest to ensure that if there are unsatisfactory aspects of the contract to which a solution can be agreed, that would be done, rather than wait until such time as there is a transition arrangement.

That is really what I think the world is moving towards—trying to get a better partnership arrangement whereby people can address problems as they arise and actually deal with them rather than waiting and then deciding on a different tack the next time around. If that is the case, then both parties should be advantaged in that respect. It is another way of sharing the risks with those people who are actually in the best position to be able to manage particular risks. If the case is that you have something that is not contributing to your business to the extent to which you would have expected, then that is a risk for you and it is really a case of you and your contracting partner trying to come to grips with that and to come up with some solutions. The flexibility, hopefully, would be there to allow that to happen without incredible increases in cost.

Senator LUNDY—You reflected on the industry development components in your report, and no doubt you are familiar with the subsequent recommendations and activities in the industry development area of IT outsourcing. Is that something you have kept across? Have you a comment or a view about the audit implications of the way the industry development

component of the IT outsourcing contracts has developed with the release of the government's new ID framework?

Mr Barrett—There is obviously an accountability issue here in terms of ensuring that a major outcome was expected to be some kind of industry development. The problem is to get the necessary information to back that up. This was not an aspect of the report per se.

Mr Cronin—We do have an audit planned for 2001-02 into the Department of Communications, Information Technology and the Arts management and monitoring of the ID framework.

Mr Barrett—That is where the responsibility would lie, Senator, as you would know. Really it is to see what agencies are doing to harvest those kinds of gains from these initiatives. At the end of the day it is not up to us to make a judgment, but it is certainly the accountability of agencies that are responsible to ensure that whatever was expected to be delivered is being delivered. The problem there is the quantification—in a changing environment trying to associate particular means with particular ends or particular things that created the change in this changing world.

Senator LUNDY—I do not know in how much detail we can discuss this, but do you have a view about the use of measurements, such as Australian value add and the proportion of revenues to, for example, small to medium enterprises, as adequate measurements that then provide the basis upon which you match outcomes with commitments?

Mr Barrett—They are very broad measures, as I said. You are talking about means and ends or what contributes. There are other factors obviously that enter into that equation for both the particular parameters that you mentioned and they are changing, literally day by day. It is like any type of indicative analysis: if there is evidence, at least in a qualitative sense, to indicate that activities that were undertaken by small to medium sized enterprises would not have otherwise occurred or certainly not at that level, then it is not unreasonable to take value added and a proportion of their revenues as a surrogate measure, in my opinion, as long as you are not claiming that necessarily there is a one-to-one relationship.

If the industry itself is agreeing that there was a favourable impact, and if people who are in the business are prepared to say that, in the scheme of things, the contribution of this was probably in the range of 20 per cent or 30 per cent of the value added or of the revenue generated, then at least that gives you some measure. But I certainly would not want to decry any efforts in this. I am simply thinking back to where in the past we have tried to do similar kinds of measures in performance measurement, and things like productivity and value added have always been difficult, in terms of attributing the factor that created it and isolating that out in some reasonably sensible fashion. It has always been a difficult exercise. But I think this is where you need to have a strong, ongoing monitoring role, so that you can get the intelligence from those who are involved, and the opinions and whatever more tangible evidence you can get, to ensure that at least you have some indicative indication. That is really all you can say, at the end of the day.

CHAIR—There are two issues I would like to raise, and I am interested that Mr Cronin said that you are going to do an audit in 2001-02. Traditionally these things have always been

measured in terms of what share of the cake Australian industry has received as a result of whatever spend. In the old days, I think there was a requirement placed on Telstra to abide by a 70 per cent local content rule, which is a fairly tangible and measurable outcome. But the more complex issue, which has been argued for some time now in respect of industry development, as opposed to local industry share, is the recipe for making the cake. There was a lot of argument in the late 1980s and early 1990s, for example, around the North West Shelf project about trying to get access for Australian engineers into the front end of the project, to get the experience and expertise to be able to bid for ongoing work. I do not know whether the Audit Office has applied its mind to that area, or whether it is thinking about applying its mind to how you actually measure that in tangible terms. What I am talking about is the opportunity that is provided to Australian industry to develop in these areas and to be able to access contracts, because in many instances a lot of the contracts are not accessible to Australian industry because it does not have the technology and technological expertise to make the bid. In some circumstances, for small to medium enterprises, the cost of making the bid is prohibitive too.

Mr Barrett—Again, I am not trying to be defensive here, but this is not the role of the Audit Office per se. It is the role of the people who are responsible for policy and who have operational responsibility in these areas. What we try to do is to assess what they are doing, and we look at the best information we can get on overseas experience and experience in the private sector. We then try to relate that to the Australian situation, and we ask the experts in the area how relevant that is in terms of the Australian situation. If we are convinced that there is some degree of relevance, then we will make suggestions or recommendations along those lines, but we are not a prime agency, in terms of going out and making assessments on behalf of agencies about the performance measures that they themselves are responsible for. We do review the performance measures, and we try to assist them in getting proper performance measures, but we are not responsible for determining the nature of those performance measures.

So, in the case of the Department of Communications, Information Technology and the Arts, we would be reviewing what work they had done in this area to try to get sensible measures. As I was saying to Senator Lundy, the problem here is how to make a distinction between skills transfers, which come in the normal course of events in relation to the environment we work in, and the environment that is being is created by an initiative such as this. It is a cause and effect situation; it is very difficult, but I think that if you are talking on an ongoing basis with the industry at least you can get a reasonable feeling for it. Firstly, it either happens or it does not happen—that is the easy thing, but people who are in that particular skill group can give an indication as to the extent to which they did get involved in that kind of project when they would otherwise never have had an opportunity to do so.

The same would go for the exports area. The theory is that by getting the small and medium sized enterprises involved and in partnership agreements with some of the large producers also gives an opportunity to get into export markets which we would not otherwise have. There should be a tangible way of assessing the extent to which they did get involved in contracts, for example, in South East Asia, which they had not participated in before. As I said, you must be careful in a changing environment. Australia may be very competitive internationally speaking at the moment and opportunities might arise now which did not arise in the past. I do not want to quibble about this because, in relation to gains in this area, on a reasonable judgment everyone would be prepared to give them the benefit of the doubt and say, 'Look, that might be something we wouldn't have achieved otherwise.'

CHAIR—The point I am making is that the measurement in relation to the access to the recipe and the cake is a fairly critical one. I think it is a valid point you make; it is not really your role to make those judgments. I am flagging the point because there is a question mark over whether any agency at the moment has the capacity to make an objective evaluation of that element of industry development.

Mr Barrett—Unless there is a close liaison with the industry, I am inclined to accept your view on that point. This is the whole nature of greater government and private sector partnerships. If there is greater trust and confidence, and this monitoring review process can be seen as a win-win situation for government and the private sector, I would hope that there would be more transfers of this kind of intelligence that would encourage governments, of whatever persuasion, to engage in these kinds of partnerships in future.

CHAIR—I want to raise a couple of issues before we run out of time. What requirement needs to be satisfied before there is expenditure of public moneys?

Mr Barrett—Usually there is some kind of authority in the first instance and, typically, that comes from the parliament. It then relates to the individuals who are legislatively responsible for those spends. That is clearly articulated under particular legislation applying to the individual agencies or collectively to us under general legislation. For example, in the chief executive's instructions, you would normally expect clear sets of delegations and authority limits. That is what we would look for in an agency.

CHAIR—In respect of an independent review initiated by a minister, what would be an appropriate basis for the payment of related expenses?

Mr McPhee—Whatever the agreement or contract in place suggests are the terms.

CHAIR—Would that be the letter of appointment?

Mr McPhee—Yes, it could be or it could be a separate contract following the letter of appointment. The letter of appointment may be sufficient.

CHAIR—That would be the basis for authorisation of any expenditures arising out of that?

Mr McPhee—Certainly, when the claims for payment come in, it would be normal practice for the person to certify that the payment to be made was consistent with the terms of the contract.

CHAIR—Would the person who is certifying have to have a copy of that letter of appointment or contract, or be aware of it?

Mr Barrett—They should preferably sight it.

CHAIR—They should sight it?

Mr Barrett—They should preferably sight it. Certainly, in the first instance—I am telling you what I would do in the normal course of events and what I was taught virtually from the first time I came in the door of the Public Service—you look for your authority. The first thing any person would do in authorising payment would be to look for authority. That is the first step.

CHAIR—A press release from a minister or a press report would not be sufficient?

Mr McPhee—Generally not. If that is all that the person had, they would probably check with the minister what the nature of the agreement was. It is probably not sufficient. The person certifying has to undertake reasonable inquiries, fundamentally. I think running off a press release is probably a bit light on. If the person was not aware exactly, they should check with a minister to seek confirmation of the terms and conditions under which the arrangement was made.

CHAIR—Is it correct that material generated or received by an independent contractor engaged by the Commonwealth is not the property of the Commonwealth unless the contract specifically provides for it?

Mr McPhee—It is certainly fairly normal practice, having regard to material that is generated as a result of a contract with the Commonwealth, that the information would be Commonwealth information.

Mr Barrett—I am not sure how far you want to go in this area but there is—

CHAIR—I am not going much further than that.

Mr Barrett—the issue of intellectual property. There has been an issue for many years about what residual asset the Commonwealth has in any system that has been developed with the assistance of the private sector. For the most part, the criticism has been that the Commonwealth has given away its intellectual property—in other words, the development has occurred because the contractor has taken that intellectual property away with them, into the next job, and the job after that; unless it is attempted to be obtained through the contract clauses, and the contract specifically states that there is an arrangement that if there is any development of the clear information or approaches that have been developed within the organisation, some kind of royalty payment, for instance, would accrue to the Commonwealth.

In the past there have been suggestions that the Commonwealth should establish some kind of organisation in order to ensure that it can both develop and sell its intellectual property assets. To my knowledge, this has never been very favoured. There are examples, of course—cooperative research is one. But there has never been a favoured measure. In essence, the Commonwealth has tried to achieve returns through royalty payments in the past, to the extent to which they can be identified and agreed. This would normally be part of a contractual relationship. Unless there is a contractual relationship, I think the private sector would simply say, 'Whatever we generate in this is generally available to us to use elsewhere.'

Mr McPhee—Just to give you a concrete example, we use the private sector to undertake some audits on our behalf. The working papers that they produce are working papers that

belong to us, so we make sure under the contractual arrangements that they are papers of the Commonwealth.

CHAIR—That is specified in your contract?

Mr McPhee—Yes, it is specified.

CHAIR—There being no further questions, thank you very much.

[3.40 p.m.]

BALNAVES, Mrs Susan Mary, Manager, Program Delivery, People and Organisation Development Team, Public Service and Merit Protection Commission

HARRISON, Ms Jennifer Dorothy, Team Leader, Values, Conduct and Diversity Team, Public Service and Merit Protection Commission

ISAACS, Mr Kevin Graham, Team Leader, People and Organisation Development Team, Public Service and Merit Protection Commission

LAMOND, Mr Jeffrey George, Team Leader, Staffing, Structures and Performance Team, Public Service and Merit Protection Commission

OATES, Mr Christopher John, Team Leader, Reports and Review Team, Public Service and Merit Protection Commission

WILLIAMS, Ms Helen, Public Service Commissioner, Public Service and Merit Protection Commission

CHAIR—Ms Williams, do you want to make any opening comments?

Ms Williams—I am aware that you have time constraints and I do not think there is anything particular I want to place on the record, so we are open for your direction.

CHAIR—Thank you. We will go to questions.

Senator LUNDY—The Humphry review identified a role for the PSMPC. Ms Williams, how do you see this operating, and do you have the resources, the statutory power and ability to enforce it?

Ms Williams—It is a big question. Perhaps I will talk a bit about the way we are thinking about it. We are still deciding how we will approach it for this coming year. For this first year we probably will do a bit of a benchmarking of where the whole situation has reached at this point. As you know, the responsibility has just been passed back to agency heads. I therefore think it would be very difficult to do too much of a retrospective in terms of an evaluation of where things had gone. But we do want to do a bit of the coverage of what has happened up till now and we will be asking agencies some questions on how they think they will cope with the change and particular areas they will address. We have not worked out the particular questions at this point.

Also, when we are doing the state of the service report we will depend very much on the kinds of reports that are done by our colleagues—for example, the ANAO and the Department of Employment, Workplace Relations and Small Business—because the state of the service report is so all-encompassing we simply have not got the resources to go very deeply into particular issues. It is a relatively small agency; and it is a major production.

Senator LUNDY—That concern is part of the motivation for the question. When do you envisage having a clearer view on the resourcing implications for you?

Ms Williams—It is one of these issues that is developing. The state of the service report is mentioned in the Public Service Act 1999 as part of the annual report. It does not give any specific guidelines on how wide the coverage should be. That has really developed, I suppose, on the basis of my view of what kind of coverage we can cope with. We are thinking very closely at the moment about whether in future we will pick out particular areas to follow through in more detail. That, of course, is sometimes difficult because issues come up during the year that you want to follow through and they may not have been the ones that you identified in the beginning. So far there is no doubt the way we are doing it is quite a load, but we have coped. The fact that IT has been added to our terms of reference, if you like, means that we will probably focus on that, perhaps it will be one of our particular areas, which means that one of the other areas will wait till the next year. It is going to be a difficult one. We will probably be clearer after we have done this first benchmarking as to exactly where we go from here.

Senator LUNDY—What is your timetable for this first process?

Ms Williams—We go out with questions for agencies probably at the beginning of next month. That will be on everything—IT outsourcing and other areas that we are interested in. But the report itself, of course, is in the same time line as the general annual report so it will be tabled in October.

Senator LUNDY—To go onto a different tack for a moment, I am very interested in your own experience as an agency with IT outsourcing. This is as good an opportunity as any to ask you some questions about that. As part of the Group 8 contract, can you describe for the committee the relevant status of savings achieved, of initial budget reductions, and what your current view is on how that is affecting your ability to operate with greater efficiency, less efficiency, more resources, less resources?

Ms Williams—As you will know, Senator Lundy, we are a small player in the Group 8 outsourcing. I would say at this point in some areas we are not operating as successfully as we did, but it is early in the contract. We are talking to our provider. Some areas are going well, others are going less well. Really, I would say at the moment it is in a state of discussion and I could not give you anything like a view about where we will settle down. We probably are spending roughly the same resources as we did before. When I say 'roughly', of course because we are in the same building as Agriculture, Fisheries and Forestry Australia—we really went in together with them—we probably benefited from that arrangement. Simply because we were in the same building we were able to have people on site. As a small agency that is more difficult, so we have had to use other methods, such as training some of our own people, not in major IT in the way that the outsource provider would, but we have certainly worked on some of our own people to give them a little bit more expertise so that they can fill in. I will ask Mike Jones to go into some of the more detailed questions for you.

Senator LUNDY—I note Mr Jones is listed as representing the agency on the Group 8 steering committee.

Ms Williams—Yes.

Mr Jones—Do you want a sort of general view of how we think things are going?

Senator LUNDY—Yes, please.

Mr Jones—I think Helen has covered it pretty well. We are just coming to 12 months into the contract. It started in June last year. You go through a bit of a rocky period early in pretty much any new contractual arrangement, particularly with something of this scope and particularly when you are a small agency. I think things obviously dipped a bit in the first few months. We have discussed those issues closely with the provider along the way, and I think the service we are getting now is better than it was six months ago. I think it can still improve a little yet, but it is going in the right direction. It certainly looks a lot better than it did six months ago.

Senator LUNDY—Have you had cause to apply service credits—which, for everyone's benefit, is a euphemism for financial penalties?

Mr Jones—Yes. We do not regard them as penalties. We regard them as recovery of payments where the service was not fully provided, so it is taking back for what you did not receive as opposed to a penalty.

Senator LUNDY—It is all a matter of perspective.

Mr Jones—Yes. Yes, we have recovered service credits in relation to the performance of IPEX—IPEX is our provider—from the period in July last year, and that is the only period for which we have recovered service credits.

Senator LUNDY—Are you able to put a dollar figure on those service credits?

Mr Jones—Yes, within a few hundred dollars, anyway. It was approximately $12,000 which, to put it in perspective, is about 22 per cent of one monthly payment for the commission. It is not overly significant in the scheme of things.

Senator LUNDY—What is your contract, or your part of the Group 8 contract worth?

Mr Jones—About $2.5 million over the five years, but there is a very big 'about' in front of that because that is an estimate made by OASITO at a point in time and it is for a basic set of services. So you can be sure it will end up being a bit more than that.

Senator LUNDY—We have detailed and comprehensive knowledge of the failings of some of those early methodologies used by OASITO, Mr Jones. Did the commission have any budget deductions in anticipation of IT outsourcing?

Mr Jones—Yes, like all other agencies we had a budget deduction in, I think, 1998-99.

Senator LUNDY—Was it just for one year or did those deductions extend across the out years?

Mr Jones—They were removed from the base allocation, so they extend.

Senator LUNDY—Are you able to give both an annual breakdown and a total of those budget deductions?

Mr Jones—It is once removed but removed forever. It was $112,000.

Senator LUNDY—Have you been able to recover that loss of allocation through savings achieved through the contract to date, or did you anticipate you would recover that money by the time this contract was due to terminate?

Mr Jones—That is a bit of a tricky question, Senator. I do not think we could quantify savings of that order from the contract to date. As to the out years, again that is very difficult because you can only compare what you spend on a new provider with what you spent previously, but you are talking about a different set of services and you are talking about a different IT platform. You would not even be comparing apples and oranges. You would not even be comparing fruit and vegetables. I am not quite sure that you could do it.

Senator LUNDY—I understand and accept what you are saying because it is a common problem. To your knowledge, did the minister ever attribute a dollar figure to the savings the government anticipated out of your specific agency? I know he certainly did with the Group 8 contract, but were specific savings identified attributable to the commission?

Mr Jones—Are you talking about the minister for finance?

Senator LUNDY—Yes.

Mr Jones—I am not aware that the minister for finance attributed savings on an agency by agency basis.

Senator LUNDY—Were you ever advised of the proportion of savings you were expected to contribute to the pool of the Group 8 savings?

Mr Jones—Sorry, I should have gone on to talk about that but your question picks that up anyway. OASITO attributed savings on an agency by agency basis.

Senator LUNDY—So what were they for you?

Mr Jones—They were of the order of $180,000, but if you want to quote that figure I would have to verify it. I am pretty sure that is over the five years of the contract, so it is about $35,000 a year.

Senator LUNDY—So it is $180,000—

Mr Jones—Over the five-year period.

Senator LUNDY—Given that you have lost $112,000 in your budget allocation, the difference between that and $180,000 is $68,000. Do you anticipate your ability to achieve savings of that nature? Indeed, I should ask the fundamental question: do you expect to be able to combine your costs to achieve any savings at all, acknowledging the fact that it is not about comparing apples with apples?

Mr Jones—I think it is difficult to attribute a saving. The comment I made earlier stands, but also the cost of IT, just by its nature, increases year by year. And it would continue to increase, no matter who your provider was.

Senator LUNDY—I have one final question about costings. Are you able to identify the proportion of that nominated $180,000, which OASITO said you would save, that went to competitive neutrality factors?

Mr Jones—No. The way that the tender evaluation process was undertaken was that the agencies were involved in, if you like, a pure evaluation of the tender's tenderer against tenderer against RFT. Issues to do with competitive neutrality to do with ID were undertaken as a separate process. At the very end, those considerations were brought together and a decision was made by the minister.

Senator LUNDY—I think you may be misunderstanding my question and I will try to be clearer. Out of the nominated savings figure by OASITO such as $180,000 attributable to the commission, within those figures the Audit Office report into the other IT outsourcing contracts—not Group 8—found that a significant proportion of that savings dollar figure could be contributed to a competitive neutrality calculation. So it is not related to the industry development component; it is actually within that sort of financial methodology that OASITO applied to how they got those savings figures in the first place.

Mr Jones—I am not able to answer that off the cuff.

Senator LUNDY—If we could leave that with you, it would be useful to get that figure. Just for your information, page 19 of the Audit Office report contains a table that identifies the competitive neutrality component of the other three contracts that they did audit. That might give you some guidance as to the actual figure I am looking for.

Mr Jones—I am happy to do that, Senator.

CHAIR—Ms Williams, on a slightly different line of questioning, you would be aware of the report that we tabled in April, the interim report in respect of accountability issues—an issue that has been emerging out of this committee's inquiry. Another issue that has joined that list is the question of what constitutes Commonwealth records. Can you just for my edification explain to me what processes or programs are in place within the Public Service to train prospective public servants, new public servants or existing servants—or all public servants for that matter—on APS processes, procedures and principles? Particularly, what specific programs are there that deal with the issue of public accountability, the right of parliament to have access to information, et cetera?

Ms Williams—Chairman, we have a range of programs right across the levels. I should also back this by saying that we run programs when agencies want them. We have to earn our own income here. I am adding this only because I have explained to committees before that it is not a case of running them in the hope that people will go. We tend to have a consultative process with agencies to make sure that they are interested in the programs we are running. Then we make quite sure that we run high-class programs but we are in contest with the providers out in the industry.

CHAIR—I do not want to break your chain of thought, but what happens in a set of circumstances where there is an issue, such as we have raised here, and a very identifiable need for training to be provided? Does it still rely on individual agencies reacting positively to that agenda before you can run the programs?

Ms Williams—Yes. I will take two examples. One, it was raised with us about a year and a half ago that project management was an area that was a high-level need. We discussed that with agencies, both at my level with agency heads and at different levels in organisations, and we have developed some courses to meet those needs. We did it like that simply because otherwise we would find that we had courses that we had spent money in developing and we could not recoup the costs.

Another example is the program we run called 'Public servants' accountability, rights and responsibilities'. It was identified as a major issue for senior executives, that senior executives in the service did not understand their accountabilities to parliament. We have run that course now for two years, and a large proportion of the SES officers have been through that course. But that particular one was because there was a very strong hint from the Senate itself that it was a requirement that senior executives came to the course. So we really have to focus our own efforts where the demand is but even then, of course, we want to be certain that we run high quality programs in those areas. So we still are in competition with the rest of the market.

CHAIR—I have to say some of the senior executives that I have come across in estimates probably have not done the course.

Ms Williams—It is still running, Chairman.

CHAIR—We can recommend it to them then.

Ms Williams—I think it is a very good course. We do it together with the Department of the Prime Minister and Cabinet, Attorney-General's and the two houses of parliament.

CHAIR—Are you looking to extend that beyond the Senior Executive Service?

Ms Williams—We certainly could, yes—we have done for particular agencies. We have put a large number of my agency through that course. I will ask Mr Isaacs to comment but we have run it in the Department of Defence for beyond the SES, is that right?

Mr Isaacs—That is correct. We have also run it in Centrelink for the SES and beyond the SES. As the commissioner mentioned, in response to requests from individual agencies, we are certainly more than happy to provide the course in-house to cover the range of their people.

CHAIR—Has this course been run in all agencies now for Senior Executive Service personnel?

Ms Williams—We run it ourselves every so often, and the senior executive from across agencies come to go on that course. But if a particular agency asks us to run it in their department, we will do that also.

CHAIR—Are you aware of any agency whose senior executive personnel have not attended the course?

Mr Isaacs—I am not aware of any particular agency, Mr Chair. I can mention to you that so far we have had 756 senior executives go through the course in its two-year period. So against a proportion of the entire SES, we have had almost half of the SES go through the course over the past almost two years. My guess would be that we have had a fairly wide coverage of agencies as that number has gone through.

Ms Williams—I should add, however, that we also have that kind of segment on some of our other courses. For example, I talk to our ELDP—Executive Leadership Development Program; I tend to use the letters—on the values. And on some of the other major courses we run, I or my deputy Lynne Tacy, or Kevin himself, will run those sorts of courses, or Jenny Harrison who runs the values team.

CHAIR—This particular course looks to be going on on a continuing basis; there is still demand for—

Ms Williams—That is the accountability, rights and responsibilities course—yes, we are still running that course.

Senator LUNDY—Mr Jones, as a member of the steering committee, can you tell me if the final decision on the awarding of the tender for Group 8 was consistent with the recommendation that emerged from the steering committee?

Mr Jones—That is a bit of a difficult question. The steering committee was split pretty much down the middle, except that you cannot be down the middle when there are seven agencies. They came out in favour of a provider other than the one that was ultimately chosen.

Senator LUNDY—I am sorry, I cannot hear you.

Mr Jones—They came out in favour of a provider—four to three—other than the provider that was ultimately chosen when the Australian industry development factor was taken into account.

Senator LUNDY—I appreciate the steering committee was before the evaluation committee where the ID aspects are brought into it. In terms of that subsequent process where the ID component is factored in, how was the commission, and how were you specifically, consulted in that subsequent process that, from what I understand, you were not involved in at all? The agency was not represented on the evaluation committee or any committee beyond the steering committee?

Mr Jones—The steering committee signed off its report in the way I just described, and that went forward to the minister with a separate evaluation which was based on the Australian industry development aspects. We were not a party to that process.

Senator LUNDY—Was that of concern to the agency?

Mr Jones—You are always curious when you have a strongly vested interest but, against that, we do not have any expertise in that field.

Ms Williams—As I mentioned earlier, we were in a fortunate position when it happened in that we were running closely with AFFA. In fact, we depended on them quite heavily for some of the assessments. That does not mean to say that we did not make our own assessment but, as Mr Jones said, we did not have the kind of expertise that a major agency would have.

Senator LUNDY—Was AFFA represented on the evaluation committee? I would expect it was.

Mr Jones—You are referring specifically to the consideration of the Australian Industry development or the technical evaluation?

Senator LUNDY—The evaluation committee that would have made the ultimate decision on which contractor was recommended.

Mr Jones—The ultimate decision, which took account of the AusIndustry development, did not include any of the seven agencies that were involved.

Senator LUNDY—It did not include anyone from the agencies?

Mr Jones—None of the Group 8 agencies, no.

Senator LUNDY—I am just trying to dredge up from the bottom of my mind whether that was standard in terms of the way the evaluation committees were actually constructed. Maybe you can help me there.

Mr Jones—I can only comment that it was the processes as we expected it to run.

Senator LUNDY—I think that is right. I think the evaluation committees were constructed at a layer beyond that of the agency involvement.

Mr Jones—Yes.

Senator LUNDY—And it was at that level that the decision was ultimately made?

Mr Jones—That is correct.

Senator LUNDY—That is very interesting. What was the PSMPC's assessment of the impact of that decision, given it was not the recommendation emanating from the steering committee?

Mr Jones—I mentioned earlier that a recommendation had been made by the seven agencies, but that they had been split in coming to it. We were not overly unhappy with the result that was achieved.

Senator LUNDY—I suppose I am asking now for you to reflect on the deliberations of the steering committee. Were the concerns of a technical nature, a technical ability? If we had the evaluation reports we would probably have the answer to these questions.

CHAIR—We have them, but they are all blacked out.

Mr Jones—You will be familiar, I think, with the fact that there were four major contenders for Group 8. That dropped down to two, and they were neck and neck.

Senator LUNDY—So it was pretty close anyway. That is all I have on that, unless there is anything else you want to add.

Mr Jones—Thank you for the opportunity, Senator.

CHAIR—Mr Williams, can I just come back to this issue of training again. Do all new APS employees do a compulsory training course in APS values?

Ms Williams—No, there is no compulsory training course. Do you mean at graduate level or at any level?

CHAIR—At any level. When you get a new person starting within the APS, is there a standard course or orientation that they go through?

Ms Williams—No. We have no courses that everybody has to go through. We have options at all levels. Even for people coming in at senior levels we have a system, which Mr Isaacs may wish to add to. We have senior people who have left the service that will actually coach them on a one-to-one basis and talk to them about the kinds of ways we act and the kinds of values we run by. I think that is a very valuable course. It has not, I would say, taken off as yet but we are making it clearer in the current prospectus that that is an option.

CHAIR—How many new APS employees would you take on in a year? Is it a fairly substantial number?

Mr Oates—It would be somewhere between 5,000 and 10,000, off the top of my head.

CHAIR—What does that represent as turnover?

Ms Williams—We can get you that figure. We might have to come back with it. Mr Lamond has just mentioned that there are 110,000 ongoing staff. We could do some work for you on that.

CHAIR—That is around 10 to 15 per cent. Theoretically, you could have within a very short period of time a substantial number of APS employees who have no knowledge of the history of APS values.

Ms Williams—We could.

CHAIR—I am intrigued that there is no orientation courses.

Ms Williams—We have courses, but there is just no requirement to go on them. Agencies can run their own courses and they can, as I said, get other providers, apart from the Public Service and Merit Protection Commission—

CHAIR—Do they?

Ms Williams—Yes.

CHAIR—Is it substantial?

Mr Isaacs—There is a substantial amount of in-house provision of these sorts of orientation courses. If I could add to the commissioner's comments, we run an SES orientation program for new entrants to the SES. That is beyond the one-to-one induction that the commissioner mentioned. On the SES orientation program they get a session specifically on the SES and the parliament. That is delivered by the Clerk of the Senate when he is available.

At the other end, where people are entering the Australian Public Service—the graduate entrance—this year we have developed a series of development and awareness activities for incoming graduates that will cover specifically APS values, ethics and accountability issues. This is the first year that we have run this specific graduate series, but it builds on some work that we have done in previous years with incoming graduates. As the commissioner mentioned, attendance is not compulsory for individual agencies and individuals entering individual agencies on these particular offerings. But certainly on orientation and on the graduate series we do again get a fairly wide coverage of agencies participating.

CHAIR—With the APS principles and values—I think there are two separate—

Ms Williams—Values and the code of conduct.

CHAIR—I am sorry, values and code of conduct. I knew they were two separate documents but I was not too sure what they were. They are pretty central to how you see the service. I am wondering how you are confident, with a degree of certainty, that all public servants are familiar with that code of conduct and with the values?

Ms Williams—It is an ongoing effort on our part. We have printed bookmarks, for example, and 50,000 of them have been distributed in the service with the values on one side and the code of conduct on the other. We have developed a booklet on the values, including the kinds of indicators that would say that the values are being followed in the agency. Of course, I have my directions which spell out what the values mean in a bit more detail.

Going to the centre of your question, for this coming state of the service report we have already told agencies that this year we want them to run surveys within their agencies asking questions which we hope will give us a bit of a lead on whether staff believe that the agencies are running by the values and whether they understand the values. Of course, those kinds of surveys are sometimes difficult. Sometimes they do not produce exactly the results that you expect, but it is at least a start in getting some kind of feedback on whether the staff themselves believe that the agencies are running according to the values.

CHAIR—When will that information be available?

Ms Williams—That will be part of the coming *State of the service* report.

CHAIR—How will that information be gathered? Through the consultative committees?

Ms Williams—We have sent out a list of questions to agencies. We sent it out at the beginning of this financial year. We asked them, when they are running their own surveys, if they would add those questions and report back to us at the end of this financial year.

CHAIR—On another issue, do you conduct competency based training?

Ms Williams—Yes.

CHAIR—In what areas do you do that?

Mr Lamond—We promote competency based training through the public sector. We do not run it per se through Public Service and Merit Protection Commission courses. As part of a joint jurisdictional effort across Australia, the PSMPC, representing the Commonwealth, participated in a development exercise whereby an organisation called PSEETA, Public Service Employment, Education and Training Australia, put together a set of core competencies that cover classifications across all jurisdictions, APS 1 through 6. I will probably pre-empt a question: in those competencies there is not a specific element addressed to APS values, but that is in the context that this was a seven-sector, cross-jurisdiction exercise. It was specifically addressed to occupational competencies rather than the values that underpin necessarily a public sector. That is developed elsewhere.

With respect to the things in which you might be particularly interested, there are a couple of elements in that package that go to the basics of procurement and contract management. The intention there is to give people at very basic levels as they enter the Public Service and necessarily work their way up a set of core skills, because contract management and procurement in the modern Public Service is a much more valuable skill than perhaps we needed 20 years ago. So we give people those skills. The development and appreciation of the values is really an organisational specific exercise.

CHAIR—You did not quite predict the question I was going to ask, Mr Lamond. My follow-up question was: to what extent is competency a measurement in terms of your wages structure, and to what extent does competency form a measurement in terms of promotion within the service?

Mr Lamond—Competencies do not form a measure of the wages structure. As I understood the competency based awards that were established more than a decade ago, the fact that a person has the competencies does not qualify them for a higher level of pay. If you have the competencies, they are recognised and then you apply them to a particular assignment of duties, you will be paid at the appropriate level. The mere possession of those competencies does not qualify you for a wage rate. That was the basis of some early discussions with a number of the unions who were represented on that task force. They have stepped away from that argument because they recognised there was some history to it and it was not run again. In terms of your progression through a classification structure, there are probably two elements to that answer. The first is that the possession of the competencies does not automatically qualify you for progression. Advancement in the Public Service is quite clearly based on the fundamental concept of merit, which is indeed one of the core values.

CHAIR—I would have thought having competencies was of substantial merit.

Mr Lamond—I agree entirely because, when you are testing a pool of applicants on the basis of relative merit, certainly the obvious possession of a set of competencies and the capacity to put them into place in the workplace will obviously give you a substantial ranking in comparison with other people. So it will be part of identifying in the individual merit that will qualify you for promotion; that is, promotion not across broadbands but across classification levels. A number of agencies in the APS now have somewhat broadbanded structures; they might have two or three elements of a broadband within their organisation. Again, possession of competencies will be essential to movement within that broadband, but another essential element to movement within the broadband will be the existence of a job of work at a senior level. So again, if an individual has the competencies and can do the work and a job is available, they will be progressed to the appropriate level within the broadband and will be paid accordingly.

CHAIR—Does that also apply to performance pay?

Mr Lamond—I am not aware that possession of competencies had been made a particular feature of assessment of performance. They might play a role or have an impact on an individual's capacity to perform at an outstanding or a fully competent level; but certainly within our organisation, for example, we do not use that as a benchmark or a test. In terms of other organisations, I simply am not qualified to answer.

CHAIR—What role has the PSMPC played in the IT outsourcing program, in terms of facilitating redundancy packages or facilitating the transition of staff from the public sector to the private sector?

Mr Lamond—We have played a role insofar as our responsibilities require and allow. The commission has a particular interest in HR policy matters, and we have over a period of time, particularly in partnership with DEWRSB, the Department of Finance and Administration and OASITO, put together a number of publications which are in their second iteration and which provide guidance to managers and to organisations about better practice approaches and appropriate approaches to handling staff movements that might be associated with outsourcing. I would also signal that all of those publications—which are available on the Internet and, if the committee has not had access to them, we have them in hard copy which we can hand over

today—are going through another iteration because the commission more generally, with the advent of the new Public Service Act, is reviewing and updating its related publications. So we provide guidance but we are not involved in the decisions to outsource, nor are we involved in selections of staff who may be transferred. As I said, we provide the policy guidance, and then the operational arrangements are put into place at an agency level.

CHAIR—You are familiar, obviously, with the setup of OASITO and the fact that it is a separate agency reporting directly to the minister. In assessing the manner in which they have operated, what conclusions have you drawn in respect of that particular model?

Mr Lamond—To be quite honest, I have not reflected on OASITO's performance. In terms of an earlier and fundamental decision about whether there should have been an organisation such as that, a number of important factors were addressed by the agency and there probably was some consultation with Prime Minister and Cabinet about the usefulness of setting up such an organisation. Those decisions were answered in the positive, and so in fact that organisation was set up. It is one of seven executive agencies that have been set up since the Public Service Act has been put into place. But, as an external observer, I simply cannot answer your comment about how well OASITO has performed and whether it measures up to the expectations of the executive agency model.

CHAIR—Have you done an assessment of the executive agency model?

Ms Williams—I would say that it is really not the kind of thing—particularly at this stage, unless we do it later in, say, the service report—that is within our competency. This is really one for Prime Minister and Cabinet. Executive agencies are quite new, and it is something that we really do not get involved in.

CHAIR—As there are no further questions, I thank the witnesses.

[4.53 p.m.]

HARMER, Dr Jeffrey Allan, Managing Director, Health Insurance Commission

MORAN, Mr Peter, Assistant Secretary, Corporate Services Division, Department of Health and Aged Care

PODGER, Mr Andrew, Secretary, Department of Health and Aged Care

THOMAS, Mr Robert Septimus, General Manger IT Services, Health Insurance Commission

CHAIR—Welcome. Before we commence, I wish to advise for the record that the witnesses appearing before the committee this afternoon are protected by parliamentary privilege with respect to evidence provided. I also take this opportunity to remind the witnesses that the giving of false or misleading evidence may constitute a contempt of the parliament. Do you want to make an opening statement, Mr Podger?

Mr Podger—No.

Senator LUNDY—I want to ask some questions about the tender evaluation process relating to the health group. The best way to do this is to tell you what I have been led to believe: during the latter stages of the tender evaluation process there were some significant shifts in the price being offered by the tenderer that was ultimately chosen, IBM GSA. I want to specifically inquire—and I know I have done this through other forums, but I have not felt satisfied generally in terms of the response; I suspect that was because of the way I was asking the questions—whether you could describe for me your knowledge of any variation in the tender price being offered by the participants in the closing stages of negotiations; and, if in fact that did occur, the basis for the changes in price.

Mr Podger—I will make a few comments, but Mr Moran might be able to expand on them, as he was more involved in the detail of the evaluation process. The process did involve three opportunities for the bidders to revise their bids. That was done in an open fashion with all three tenderers. By having such an approach, it made the process a little more like a BAFO arrangement—a best and final offers type of process. It was not quite like that, but it was near to that. Clearly, at each point when there was an opportunity to retender, the bidders would have taken into account the discussions they had been having and their impressions of where their bids were not as good as the purchaser would prefer them to be. These were not just in terms of price; they were also in terms of the other two dimensions of the bid process, on the technical and on the legal aspects. So it is true that the bids did move around at each point in that process.

Senator LUNDY—Thank you. That probably covers off generally the information I was getting about significant movement in the price in the closing stages. I am interested in more detail about that. You mentioned the opportunity to effectively resubmit the tender: that occurred three times?

Mr Podger—I understand that it was three times, Mr Moran.

Mr Moran—Not strictly speaking. There was one tender which was closed for all three bidders on 15 February. It became quite clear very early on that there was mismatch between the understanding of all of the tenderers in terms of exactly what was being asked for—and that is not unusual, as it was a very complex tender document. It is also the case that the prices were far in excess of what we thought we would have a business case for. So it was decided fairly early on that there would be one or possibly two repricings. I should stress that OASITO made it clear that these were for repricing, not rebidding. They are not an opportunity to fundamentally recast the process but simply to reprice their bids on the basis of a number of clarification processes that went on. That happened three times. So effectively there were four prices put on the table: the initial tender price and three reprices.

Senator LUNDY—In specifying that that subsequent process was to reprice and not to rebid, was that subject to a probity assessment, given that it is actually a very important technical point of contract law that they did not allow people effectively to modify their bid? What confidence do you have about this determination by OASITO that it would be a repricing exercise and not a rebidding exercise?

Mr Moran—The case for repricing—in my view and certainly on the advice of OASITO and its advisers—was very clear from shortly after we understood the actual initial tenders. I stress that it is not unusual with a services agreement this complex that there is a considerable amount of misunderstanding or lack of understanding by the tenderers of what was being sought. There was a considerable amount of detailed non-compliance—in other words, they either chose not to comply or, by accident, did not comply. This is all of the tenderers. It is also the case that there were, to be blunt, many mistakes in the bids by all of the tenderers. Some of them were quite fundamental; some of them were simply arithmetic errors.

So the process that we went through in the first, second and third repricing was to consistently refine each of the bids. There were two main streams of activity: the first was to remove ambiguity to ensure that the tenderers actually knew what they were bidding for and to adjust prices so that all of the tenders were being assessed on the same basis; there were a range of financial adjustments applied to our cost model as well as to the tenderers' bids. The probity auditor obviously—to the best of my knowledge; certainly he was always on the place—sat through this process and provided advice to OASITO and Shaw Pittman that this process was kosher. I have to say that I have been involved in not necessarily services agreements but where this sort of clarification process becomes necessary, otherwise you simply do not have a live tenderer at the first jump.

CHAIR—Did the three rebids that occurred all occur after the leak?

Mr Moran—No. It might be useful if I give you a very simple chronology: the tender closed on 15 February 1999; the first repricing was due and received on 21 May 1999; the second repricing—that is, the third bid—was received on 22 June 1999; the leak or probity breach occurred on 27 July 1999; and the third repricing, the final bid, was received on 2 August 1999. I can give you a copy of this, which is just a very basic chronology, if that would help.

CHAIR—It would be useful if you could, just to keep things in perspective for us. Did the material or information that was leaked go to the totality of the bid or to just the revised pricing bid?

Mr Moran—As I understand the situation as described by OASITO subsequently, the material—and I do not believe it was a leak; an 'inadvertent disclosure' I think are the words that they are using—

CHAIR—You describe it as you like.

Mr Moran—Thank you. A floppy disk containing all three tenderers' penultimate pricing material—because you will recall that the ultimate pricing material had not been received until after the event—was sent to IBM GSA by OASITO by mistake. I understand that it was essentially the financial bid which comprised a number of draft schedules and their response to the request for tender.

Senator LUNDY—I have a couple of clarifications. What was the last date on that document you gave about the third reprice in September?

Mr Podger—The third reprice was 2 August; and the probity breach was 27 July.

Senator LUNDY—Just remind me: did the probity breach contain the financial details of the CSE bid?

Mr Moran—It contained the financial details of all three bidders' bids.

Senator LUNDY—In terms of the process of initiating the repricing, up to the point when tenders first closed on 15 February, did you feel as agencies or departments that the process of tender evaluation had proceeded—I do not know how to describe it—without incident, adequately and with your full confidence? Sorry, it is not the evaluation process but the preparation of tender documentation by those companies. Also, to what degree were you, as an agency, involved in providing information either to OASITO or to bidders to inform their bidding process?

Mr Moran—The answer to the first question on behalf of the department of health is, yes, we were satisfied that the document that we released to the market—that was actually on 30 November 1998—was, within the framework provided to us by OASITO, as robust as it was possible to make it in terms of what we were asking for from the market in terms of a technical specification and the way in which we wished them to construct their response in terms of pricing, legal compliance and a response to the statement of work.

Dr Harmer—The same would apply to the Health Insurance Commission; we had adopted similar processes in developing the tender material, and I think it was the same time.

Mr Moran—It was the same document with a few business variations to suit the business of the Health Insurance Commission. I think it is fair to say that all three agencies in the health group added a lot to what was put before us. So if the question is about us rather than about

OASITO, the document we released reflected an enormous amount of work by the three agencies—

Senator LUNDY—That is really my question. You are in this situation in February after the close of tenders where it became very clear very quickly that there were problems with the bids. I am trying to backtrack to whether you anticipated that, what degree of diligence was applied with respect to the preparation of the RFTs, how involved you were and how involved OASITO was. I do not know whether that weakness in those early bid responses was because they had an inadequate brief or because they were just not good enough. Do you know what I am saying? It is a very blunt question really.

Mr Podger—I think what Mr Moran is saying is that the problems with the initial bids related to the complexity of the RFT.

Senator LUNDY—So they just were not good enough?

Mr Podger—No. It is not surprising when you get something as complicated as this that there are some levels of misunderstanding of aspects of it. That is not a surprising thing to get. But, going back to our involvement in it, both the HIC and the department were extensively involved in the preparation of the RFT. If I can backtrack even further, one of the things about this cluster which I have mentioned in I think Senate estimates evidence is that we were able to have a cluster of the health agencies who have a considerable similarity of business interests. I think that helped us to make sure that this one was a bit more driven by the business end than perhaps some of the others. There was a lot of work done in identifying what our requirements were. That did involve some toing and froing with OASITO because they were questioning on some aspects, both of the HIC and the department, about what we were identifying as our base level requirements. But we had an extensive involvement with that and we were both satisfied that our requirements were met in the final tender.

Dr Harmer—Just to add to that from the HIC's perspective: to the extent that the department's tender documents were quite complicated, ours were even more so because it was bigger and it was, I believe, more related to the detail and the complexity. We believe that we did it very well, and I think the department would maintain that they did theirs very well. We put an enormous effort into the preparation of that documentation. The fact that the initial bids perhaps misinterpreted it or got some things wrong, as Mr Podger said, probably reflects more the complexity of the business. They may not have bid for something quite like our business before.

Mr Podger—I do not want to sound as though we think the tenderers were all sweetness and light in terms of their tenders being as best as anybody could ever expect under the circumstances. I think it is fair to say that we were disappointed in aspects of it, and maybe Mr Moran could say a couple of things on that.

Mr Moran—The bids also reflected in our view from each of the three something of a different strategy. One of the bids was focused very heavily on price and was quite silent—not entirely silent, but very silent—in a number of key areas about what was actually being offered for that price. That reflects a corporate approach by that bidder to come in with a competitive price and then negotiate about what you can buy for that price. One of the other bidders clearly

had no idea what the business was worth and tendered an extremely high price. The negotiation with that tenderer was to reduce the price. The technical bid was in fact quite sound; there was a clear understanding of what was on the table. The other bidder sat somewhere in between, where there was a very high price and a very poor understanding of our technical requirements.

Running through all of those three bids, there were clear areas where some of the bidders had bid for Commonwealth work before and understood the requirements that we had of them in a legal sense—that is, the terms and conditions. One of the others had not, and a lot of the negotiation was moving that bidder to the point where they were compliant. While it was fair to say that bidders made mistakes and there were some genuine misunderstandings, a lot of the unsatisfactory nature of the tenders when they were first received was also a case of tactics or strategy adopted by each of the three bidders.

Senator LUNDY—I guess what I am trying to find out is to what degree OASITO, their strategic advisers, Shaw Pittman, or anyone else in that office influenced you in the construction of that RFT or the merits or otherwise of the degree of prescriptiveness.

Mr Moran—The document was unique to the health group. During the very early stages of the project, from about June 1998, the three agencies were presented successively with draft tender outlines based on Cluster 3—I think I have them in the right order—the aborted DETYA RFT outline and then the tax one. It was Health's view, and it was agreed by the Health Insurance Commission, that none of those documents—in terms of their presentation and indeed the content in terms of the many schedules—adequately described and would therefore seek what it was we wanted. So the shape of the tender document reflected very much our views on what we wanted. I understand, although I could not be certain, that certain parts of it have been adopted subsequently, but that is not unusual. These things tend to be a bit of a learning exercise.

Mr Podger—In terms of 'Was there any influence from OASITO's end as well?' yes, there was. First of all, we were starting with some suggestions that they had made from their experience; and, secondly, in the nature of this, OASITO were questioning both the department and the HIC as to whether some of our requirements were overstating what we are currently getting from our in-house arrangements. That was part of the toing and froing, the settling process.

Senator LUNDY—I want to ask you specifically about that. In terms of the questions OASITO were asking, was that post the receipt and closure of the first bid?

Mr Moran—No.

Senator LUNDY—It was prior to that.

Mr Moran—OASITO had seen that their central plank of this initiative was to get competitive pricing. The major comparison in the entire tender evaluation process—not the sole one, but the major one as advertised—was the best price or a competitive price. Implicit in that was that it would be competitive with the agencies' cost baselines—in other words, the costs which the agencies as a group were delivering those same services to themselves. OASITO had, in my recollection, not a lot to say about the nature of the services we wished to purchase, more

about the way in which we had costed them in terms of establishing our baselines. They went to an enormous amount of trouble and it was not a pleasant process; it was a very rigorous process. Certainly the department of health's cost baseline had been thoroughly gone over and signed off by independent auditors prior to going to the marketplace and the Health Insurance Commission, as I recall, shortly after that. As Dr Harmer has suggested, HIC is a very complex business. But that was what the vast majority of the focus from OASITO and their advisers was on. In simple terms they wanted to know whether we were understating our costs so as to, frankly, manipulate the tender price. Well, we were not.

Senator LUNDY—I find that very interesting, because the way it has been presented is that it has really been up to the agencies themselves to establish their cost benchmarks for the purposes of then embarking on this whole market testing preparation of RFTs, et cetera. What you are telling me is that OASITO had a key role in effectively negotiating with you what constituted a realistic cost benchmark, but they also had the knowledge of what the political expectation was in terms of savings outcomes. At this point, it is only appropriate to make an observation that they were privileged to have that knowledge, and by and large it was generally made public. You had already had your budget cut, which created another environment in which an expectation could be contrived, yet your cost benchmarks were being challenged so they fit that mould. Is that a reasonable observation to make? How would you say it?

Mr Podger—I can only say that I believe it was entirely appropriate that OASITO would wish to have a rigorous ruler over our assessment of our costs and be satisfied—

Senator LUNDY—But did they override you?

Mr Podger—In part, no doubt, they had to do this because there had been a whole of government expectation of savings, and therefore they were charged to make sure that, if there was an opportunity for savings, those were realised. That was quite a responsible—

Senator LUNDY—But did they do that through a rigorous tender or by putting the heat on you as an agency and as a department to change your baseline costs?

Mr Podger—We had a process where they were ensuring that there was rigour in our estimates for our baseline costs. As Mr Moran said, we also had processes of our own to ensure that we were satisfied that we got that right. It was not just internal. I know the Health Insurance Commission went through a similar process.

Mr Moran—Senator, I can assure you that, while there was a lot of heat placed on the process by which we established our cost baselines, the department of health did not concede under pressure. We were as confident as it is possible to be—subject as I said to a separate audit of those costs—that the cost baseline against which we started the financial evaluation part of the tender evaluation was rigorous. OASITO certainly questioned certain elements of the Health baseline, and I will not comment on whether it was an attempt to artificially depress that cost baseline, but where we felt that it was costing us X to deliver a service, we did not agree at any time to go to the market with a cost baseline of less than X.

Senator LUNDY—You said at the start of the evaluation process. What about prior to that? When you first opened up discussions with OASITO and you had done some cost baseline assessments, did they decrease between that time and when the evaluation began?

Mr Moran—I do not believe so. I can certainly say not materially. By the time we understood the cost model that OASITO was using, and it was a cost model which I understand they had run past Finance and Treasury and so on—

Senator LUNDY—Believe me, that does not inspire my confidence.

Mr Moran—No, I understand what you are saying. What I am saying is that we did not invent the cost model. It was a cost model that was applied to this initiative. By the time we understood what was required of it—and that certainly was not at the start of the process, it was much closer to the time the tender went out—OASITO had not officially or materially caused us to understate our costs. And certainly they went to an awful lot of trouble so that we would not understate our costs. As I have indicated before, that was a primary benchmark for this initiative. Depressing your costs would distort that.

Senator LUNDY—Absolutely. Can I apply that same series of questions to the Health Insurance Commission?

Dr Harmer—Senator, my answers would not be any different. We did not give any ground to OASITO. I am sure OASITO would say that we were quite a thorn in their side as they were, understandably, looking to get the outcome they wanted, but we in the Health Insurance Commission, I and my people had a very significant responsibility under the CAC Act body to make sure that we did not give any ground unless we agreed, and we did not. We got some significant assistance on our side with some international consultants that were helping us, and we held our ground on all the significant things. That does not mean that we did not make some changes from time to time when we were convinced that perhaps the way the costing model was working meant that we had stated it in the wrong way, but in terms of the material specifications we had lots of very rigorous debate. We held our ground as well.

Senator LUNDY—You said you had international consultants. Were they the Shaw Pittman group or did you engage your own?

Dr Harmer—No, we engaged our own.

Senator LUNDY—Who was that?

Dr Harmer—The Mitchell Madison group based in the US.

Senator LUNDY—Were they available to the health group or just HIC?

Dr Harmer—They were engaged by the HIC, and Mr Podger, who is a commissioner of the HIC, was present. We did not have any IT expertise on our board of commissioners at the time, and yet we were going through this enormously important exercise so we engaged Mitchell Madison, a top-class international consultancy firm on IT outsourcing, to assist us with the process and essentially to advise the board. We had them in many of the significant board

discussions on this issue, and Mr Podger was present, so therefore I assume that it would have helped him with his assessment within the department.

Mr Podger—The Mitchell Madison group were advising on the HIC part of the bid. There was no doubt, the department having been privy to their advice all the way through, that we did get some benefits from that advice as well, but their advice was not based on the health department's part of it.

Senator LUNDY—Can I ask Dr Harmer if you had to pay as much for their advice as OASITO had to pay for Shaw Pittman?

Dr Harmer—In total I very much doubt it, but they were not cheap. They were top-class consultants. We went through a bidding process. We wanted someone—

Senator LUNDY—You actually competitively tendered?

Dr Harmer—We did.

Senator LUNDY—I am impressed. How many bites did you get for that process?

Dr Harmer—Two or three, I remember. We were after someone who had considerable experience in managing something as big as this or in working with a big IT outsourcer.

Senator LUNDY—Someone to take on Shaw Pittman.

Dr Harmer—Your words, not mine.

Senator LUNDY—I would be interested in the details of that contract with the Mitchell Madison group if you could provide them. Where was I before I went after that?

Mr Moran—There is a question that I think has been left hanging about the extent to which the tenderers satisfied themselves prior to submitting tenders. The due diligence process—again speaking on the part of the department of health—was fairly rigorous in that the department had, at the point the decision was made that we would at some point go to the market to oursource our IT infrastructure, adopted—I suppose in defiance of OASITO—a process of briefing all the likely bidders, and we included several. We told them that we would be going to the market in a few months under the auspices of the IT initiative, that they ought to come and talk to us now before essentially the probity shutters came down.

Senator LUNDY—Right.

Mr Moran—We ran a series of briefings, including walkarounds to the various parts of the department. We made available to them a fairly significant briefing pack on the nature of our architecture and infrastructure—all intended to do precisely what you are alluding, to get the best bid on the table. We made up little show bags for them to take away and all that sort of thing. When the tender became live and the probity process cut in, we obviously stopped doing that. But there was a fairly lengthy formal due diligence process overseen by OASITO wherein

the bidders were at liberty to satisfy themselves of any of the claims that we were likely to make. It involved a large amount of printed material held securely in OASITO for them to read. Each tenderer spent many days in the due diligence room, as it was called.

Senator LUNDY—That was material that you had provided to OASITO?

Mr Moran—Yes. The due diligence process continued past that, because a large part of the early evaluation of tenders involved clarifications—and again this is quite normal—and assumptions on their part were corrected or augmented and then they sought additional material at that point. Certainly, that material where it was proper was provided to each of the tenderers.

Mr Podger—Can I just make one comment. Mr Moran said perhaps in defiance of OASITO. I think OASITO may have been initially a bit uncomfortable with some of the things we did. But, to be fair to OASITO, I can recall in particular a presentation that we proposed to the industry ahead of the RFT going ahead that Dr Harmer and myself spoke to and OASITO were present at. I know after that OASITO were in fact were very impressed with that process. We spoke to the industry not only about the business we are in, in terms of the detail we are doing now, but we took the opportunity to talk a bit about where we saw our business going in the future and that we were looking for a partnership arrangement to come out of this which would help us in our business directions. There was quite a lot about that in that presentation. As I said, following that, I think there was a lot more comfort from OASITO because they saw that this was extremely useful and caused a lot of interest in the market.

Senator LUNDY—Okay. At the time when you were engaged in this rigorous process—it would have been pre the release of the RFT—with OASITO establishing your benchmark, were you intrigued as to why OASITO were obviously spending so much time and money arguing with you over your cost benchmark analysis?

Mr Moran—No.

Senator LUNDY—Did you have an explanation as to their motivation?

Mr Moran—It was very clear. Certainly from my perspective, there was no misunderstanding. OASITO believed that the agencies were artificially understating their internal costs so as to make it harder for tenderers—

Senator LUNDY—Do you not mean overstating?

Mr Moran—No, what OASITO thought we were doing—whether they thought we were doing it or not, their job was to ensure that we were not doing—was grossly understating our actual costs. The reason being, obviously, that it would make it much harder. As I said earlier, to the best of our knowledge, belief and professionalism, the department of health did not understate its costs—

Dr Harmer—Nor did we.

Senator LUNDY—In terms of the motivation to engage the Mitchell Madison Group, was it during that process and period that you engaged them and what was the motivation for engaging them?

Dr Harmer—I cannot recall precisely when it was, but we will cover that in the note we give it. The board of the HIC was concerned, as I said earlier, that we did not have sufficient expertise on the board to help us make this very significant decision. We were even concerned initially whether the in-scope services that were proposed for outsourcing were actually in the best interests of the HIC. So the first task we gave Mitchell Madison was to come to the board to advise us on whether in fact it was in our interests to go to tender for the scope as planned. We were all very conscious in the HIC about responsibilities under CAC Act to act only in the best interests of the organisation. So we sought their advice on that first issue. They were able to convince us that it was in our interests to do exactly that, that they had seen agencies like ours without the need to have in-house infrastructure and mainframe management, and that was the reason the board agreed to go ahead with the development and release of the tender.

Mr Podger—Clearly, that work was done before the RFT went out.

Senator LUNDY—Yes.

Dr Harmer—I am not sure of the dates.

Mr Podger—But it was certainly before the RFT though.

Senator LUNDY—Mr Podger, just on that issue of the board of the HIC—you would be familiar with it because you were a commissioner there—how did the same concerns that they were dealing with and their obligations under the CAC Act compare with your obligations as a departmental head with respect to the financial management act?

Mr Podger—A couple of points on that: the FMA Act has provision for my responsibilities about managing the affairs in a way that promotes proper use of the Commonwealth resources for which the chief executive is responsible, and 'proper' meaning efficient, effective and ethical. But there is provision there for working within the instructions that we get as a department; whereas under the CAC Act there is a bit more that they have to satisfy themselves and the board directly in their arrangements. But I certainly saw my general responsibility as being very similar to those of the HIC in being satisfied that it was in the best interests of the program and the programs we were responsible for. But I am also the portfolio secretary and I also took into account my obligations to ensure the best deal for the Commonwealth for this cluster. So it was not just a matter of what was in the best interests of the department; I was also mindful of the best interests for the portfolio. Even though technically that is not written into the FMA Act, you can read the FMA Act about my obligations towards proper uses of Commonwealth resources as implying a slightly wider view than just the department itself. So I did take a cluster view in the advice I provided and the way we operated.

Senator LUNDY—Just going a bit further on that: in terms of the analysis that has been done by people like me who look at what you lost in your budget and what you hoped to make in your own assessments that you have put on the record about the potential or otherwise of

savings, how do those anticipated outcomes; that is, the fact it is unlikely you are able to make any net cost savings to the—

Mr Podger—I think what I said in my answer to a question on notice was that, at the time I answered that question, there was no net saving to the department itself. But my responsibilities are not just to the department's resources because there were also impacts on competitive neutrality—that is, tax issues—and, taking those into account, there were savings. But at the point when I was asked the question and my guess is that the answer today would be exactly the same; that is, in money terms to the department, there was no net savings so far.

Senator LUNDY—Okay. Does that present an issue or a conflict to you in terms of your responsibilities as department head under the FMA Act in that you could not demonstrate a net cost-benefit to the department?

Mr Podger—No, I do not believe so. It does not say to the department; it says the 'Commonwealth resources for which the chief executive is responsible'. It would be a matter of checking with the Audit Office, but I can remember this issue arising in previous lives before the FMA Act. I have assumed that those things still apply, but it is a matter you might want to test elsewhere. My obligations are not to look narrowly at just the cash or resources for the department. If there are implications for other parts of Commonwealth resources impacted by my decision, I have to take that into account. So if there is a tax impact to my decision, that needs to be taken into account; if there is a flow-on implication to another program run by another department, I cannot say, 'Look, it does not matter if it costs another department a whole lot of money. If it is a saving to me, everything else is not my responsibility.' I have to look at the overall impact on Commonwealth resources. That is my understanding of the situation. I believe that is the right interpretation of the situation.

Senator LUNDY—Thank you for that. Just going back now to the probity issue. You ran through a chronological order relating to the second and third repricing. I just want to get a little more detail about the first, second and third repricing exercises. You have mentioned quite a level of non-compliance over pricing and sort of mistakes in the bids, and I appreciate that the three bids had different strengths and weaknesses. Are there any other areas that you can nominate which helped build the case as to why a repricing round was necessary—in reasonably general terms?

Mr Moran—There was no business case at the time that the tenders closed to let a contract to any of the bidders for a range of reasons, many associated with high bids and very high costs; others associated with a range of non-compliance, both general and specific; plus some fundamental misunderstandings of what it was that the bidders were actually offering. As I suggested, it seemed to us that the strategy in one of the bids was to put a fairly competitive price on the table but with almost nothing behind it. In other words, we were not quite sure what we were buying for our money. So at that point it was quite clear there was no business case to let a contract.

Senator LUNDY—Okay. From that point, why did not the health group then determine on the basis of those bids that there was not a business case and abandon the project, given it was effectively demonstrable to OASITO, the Department of Finance and indeed your own minister that a business case had not been established and yet the market test had been performed?

Mr Podger—As I said, in a very complex thing like this, sometimes the initial bids need to have an opportunity for refinement—

Senator LUNDY—That is not the core of my question. I think you understand the core of what I am asking here.

Mr Podger—With respect, the responsibility of all of us—OASITO and all the players in the cluster—was to look for best value for the taxpayer and to turn the system off at that point without seeing whether a further stage of the process may well deliver something that was in the best interests of the taxpayer and was worth while rather than the status quo. You do not abandon the process unless and until you get to the point where you do not believe you could get a good business case against the status quo.

Senator LUNDY—So effectively there was a decision somewhere that these bidders—this revered private sector who theoretically had expertise, at least two out of the three had expertise in this field—should be given another chance to get their bid right or improve their bid and that they would actually get access to the resources of the Commonwealth to help them out, to help them come up to scratch with their bids.

Mr Moran—I have to say again that this is not abnormal. I know what you are driving at.

Senator LUNDY—I know it is not necessarily abnormal. But so much of the political rhetoric associated with this is about the supremacy, capability and availability of expertise in corporations who have positioned themselves in the market to do precisely this job. I find it quite extraordinary that the length—in fact, three specific lengths—of three repricing processes where these bidders were given chance and chance again to get it right.

Mr Podger—Mr Moran and I have both worked in the defence department on major contracts and complex contracts, and from time to time it is in the interests of the taxpayer to allow further work on bids in order to get an acceptable business case that it is in the interests of the taxpayer to finance. Or in this case it is in the interests of the taxpayer to purchase this one as against the status quo or an in-house arrangement. But you would stop the whole process if you came to a judgment that that is not likely to occur.

Senator LUNDY—What you are saying makes sense if in fact what was on offer what was being offered by the private sector constituted a more cost-effective solution. But the chances and chances again were related to actually getting the price down as well as the technical specificity. I do not know how much further we can go on it. What it indicates is that the overriding policy of the government, the coalition, in pushing this forward was the driving force, because show me where there was a best outcome for taxpayers in your then spending a six months in time, resources, energy and effort to come up with something which is arguably not going to save you any money in the first place. I take the point about your competitive neutrality and other considerations, but even they are under challenge. Those calculations are under specific challenge by the Audit Office, and I do not accept that they stack up as being a overriding cost-benefit back to taxpayers either.

Mr Podger—I do not really want to comment on aspects of your observation because it would be improper for me to do so. But I will pick up this point about the department's position.

The question I answered was about the department and whether there were net savings in the money to the department. I picked up the point earlier about the issue of competitive neutrality, but another issue is that it was a cluster. In the cluster arrangements on the basis of the base-level financing in the bids, there were greater savings to the Health Insurance Commission than there was to the department in this particular chosen bid. The question I was asked was what it was to the department. If I looked across the cluster, the projected savings were more substantial from the competitive tendering.

CHAIR—Can I just to indicate, more from the point of view of my colleagues than you, Mr Podger, that we have to finish this hearing at precisely 5.45 to allow time for setting up of these cameras.

Senator LUNDY—That is two minutes. Can I ask you to provide to the committee copies of the probity report conducted by OASITO into the leak of the tender documentation?

Mr Podger—Yes, I am willing to provide that to you. I have a copy of that here. I understand that OASITO has already given you a copy of the letter they sent to me. I think there were things left out of that, but essentially you have the letter. I am happy to provide the probity audit report that was also provided. That was provided to us a bit after the initial letter sent to me.

Senator LUNDY—Thank you. Are you aware of the existence of another report or any report relating to that leak that was either provided to the minister's office either by yourselves or any another party?

Mr Podger—The day after I was advised of the improper disclosure, probity breach, Dr Harmer and I met to discuss our response to the matter, and I then spoke to the minister. I did not provide him with a document but I did speak to him about the matter and discussed the nature of the matter, what I proposed to do and what Dr Harmer proposed to do.

Senator LUNDY—If there is any documentation or minutes associated with that meeting, if that could be provided to the committee.

Mr Podger—There is one short note of mine which refers to the fact that I spoke, but there is not a file note in detail about the discussion. There is a note of mine, which mentioned that on that day I spoke to the minister.

Senator LUNDY—Perhaps if you could provide that, that would be useful.

Mr Podger—I will have a look at that.

Senator LUNDY—Finally, I know I have asked the question of whether the scope of the contract was varied between these various stages of repricing and, from recollection, the answer was no. I want to re-ask that question, hopefully more accurately, as to what change in terms of the prescriptive nature or tasks required under that contract that allowed the prices to significantly vary through the course of negotiation. In essence, I want to know what changed.

Mr Moran—Nothing as far as the department of health is concerned. We went to the market with a specification and, subject to the answers to questions which I have answered two or three times, we took voice management out of scope and IT training. We did not change the scope.

Senator LUNDY—Okay. So you removed requirements—

Mr Moran—It would be material but not significant. I would be guessing and I would need to correct myself, but a few percentage of the total value—perhaps seven or eight per cent of the total cost base line, of that order. It was material but by no means significant.

Senator LUNDY—Dr Harmer, did you want to add to that?

Dr Harmer—I do not think we even made that much change to ours. I think it was more sort of market pressure, et cetera, on the companies rather than changes to scope. In our case we held firmly to our scope. We had lots of debates and arguments, as I said before. We did provide, in answer to a Senate estimates question, some detail about what changed.

Senator LUNDY—Yes. We do not need to go there.

CHAIR—Unfortunately, we have to conclude the hearing at that point. There may be some other questions, Mr Podger, that committee members may want to raise. We will put them in writing and ask you to respond to them in that form.

Mr Podger—Certainly, Senator.

[5.59 p.m.]

WILLCOCKS, Dr Leslie, Andersen Professor of Information Management and E-Business, University of Warwick, United Kingdom; and Associate Fellow, Templeton College, University of Oxford

CHAIR—Dr Willcocks, can you hear me?

Dr Willcocks—Yes. Senator George Campbell?

CHAIR—That's right. I have with me Senator Eggleston and and Senator Lundy.

Dr Willcocks—I appear before you as an expert witness having done academic research into IT outsourcing since 1991. I have written about six books now on the subject and over 35 refereed papers on it. We have researched the USA, Europe and Australia—in fact I have in my hand the recent IT outsourcing practice survey we did in Australia, published in about March 2001—so I think my capacity is really as an independent academic researcher on a global basis. I think all that material has been summarised in the recent book called *Global IT outsourcing in search of business advantage*, published in 2001, so I am pretty contemporary.

CHAIR—Fine. Thank you, Dr Willcocks. Do you want make an opening statement to the committee?

Dr Willcocks—My opening statement really was in the written submission that I gave you. You have that, do you?

CHAIR—Yes, we do.

Dr Willcocks—It was really a comment on the way in which deals are structured and what our findings have been, on the cost issue especially, and the degree to which there are hidden costs in IT outsourcing. My overall feeling, from my experience of government IT outsourcing in the UK in the early 1990s and in the Australian case, was essentially that it was very much driven from a cost savings agenda and that was not a very good basis to do IT outsourcing. Just to verify that, the recent survey that we did in Australia, in terms of what organisations are mainly doing—their main reasons for outsourcing—I think the cost reduction issue comes ninth as the rationale, not first. There are a lot of other very good reasons for outsourcing. Cost savings as the dominant one has not been the overall picture in most outsourcing deals that we have seen that have been effective. That is my opening statement.

CHAIR—Thank you. Any questions?

Senator LUNDY—Thank you. Just on that issue of cost reduction and its relative merits as an argument for outsourcing, I am presuming you have had the opportunity to observe the IT outsourcing program of the federal government here. I would like a comment from you as to the

merit of them choosing to identify cost savings as the base motivation for that whole project. Is that, in fact, an informed policy position to take?

Dr Willcocks—I think my opening statement said no, it really was not. If you go back to 1993, when I was involved in the UK Inland Revenue Service outsourcing deal with EDS, I think we spent two years getting that final contract together. There were up to 20 people involved in that. The chief executive now in Inland Revenue, Geoff Bush, was our key director. I well remember him saying, 'Look, we have been told cost savings are important by the government, but we need to have a much broader agenda than that because things will change over the next 10 years after we sign this deal. We need a multiple set of objectives.' He was indeed very clear about what those objectives were, so even then we knew that cost savings as the primary objective was not a very sensible one.

Looking at your Australian outsourcing results, I think only 35 per cent of the organisations we surveyed in Australia—and a considerable number were public sector—get moderate savings, seven per cent get substantial savings and the rest have no change or actually higher costs as a result of outsourcing. But we knew from our research of about 1995-96—and we published *Harvard Business Review* and *Sloan Management Review* papers on this—that the earlier deals that mainly had cost savings as the rationale in the early 1990s were not really getting them or, if they were getting them, they were getting them at the expense of service or at the expense of other things that you could get from IT in terms of leveraging the business or, in the case of government, leveraging the government service more than it otherwise could have been.

When I first started coming to Australia in 1996-97 and I heard about this, it seemed to me like it was repeating some of the mistakes that the UK government had been making in the early 1990s when they had a massive private finance initiative and outsourcing initiative. A number of those did not reveal the savings that were supposedly there when they were first announced. The problem seems to come from actually not having the right degree of IT outsourcing experience to be able to look at the sums that you have at the front end and say, 'Yes, but we know what is going to happen five years down the line in the next phase.'

We structure outsourcing deals in terms of six phases. What is interesting is that we now know enough about those six phases to know where the hidden costs are likely to arise. Experienced people in the IT outsourcing business understand this; they understand that there are hidden costs at every phase. Too many of the deals that were struck in the early 1990s—and I suspect that this is a good example too—looked at the figures given by suppliers and did accounting calculations but did not understand that operationally there are a lot of significant hidden costs buried in the process of IT outsourcing. For example, I did a review of 250-plus outsourcing deals. The cost of managing outsourcing deals is between four and eight per cent of the total deal, and that is even before you take into account the effectiveness of that management.

I understand from the figures I have been looking at in the various reviews here, at the ANAO document, that your getting to contract costs were 3.4 per cent of the total revenue going to the suppliers. That seemed to me to be quite a high figure. We have been finding getting to contract costs are anything between 0.4 per cent to 1.4 per cent of total revenue to the supplier. Too many of these deals focus on very much the front-end calculations, not understanding

exactly where the management and operational costs are going to rise and rise. Every deal we have looked at that has happened.

Senator LUNDY—Apart from you and the work you have done with colleagues, how widely available was that kind of information, that intelligence that could have informed the federal government here of those pitfalls around that time,1995-96? I think this program was introduced formally in 1997.

Dr Willcocks—Firstly, my colleagues and I were very widely published. If you were going to look for information on outsourcing, the *Harvard Business Review* and *Sloan Management Review* were pretty substantial management journals. There were books published in 1993, and Lacity and Hirschheim wrote the 1995 *Beyond the IT outsourcing bandwagon*. I know a lot of consulting firms—for example, I knew KPMG very well at that time—had an outsourcing practice. Deloitte Touche in those days had a very strong outsourcing practice. The informed people in those consulting firms were saying very similar sorts of things to what we were. At the same time there were other consulting firms that had more of a vested interest in outsourcing and not providing strictly independent advice that probably were much more pro it and went into less of the detail of where the hidden costs might be. They would stress much more the positive aspects of outsourcing rather than the giving of a complete rounded picture.

The information was widely available. I think the problem was that there was mixed information around at the time and one could go in several different ways. Certainly there was information around about people pushing strategic outsourcing, big deals and signing strategic relationships. There was certainly a debate around at that time about which was the way to go. For me the weight of information fell very clearly on the side of being much more careful than some of the strategic outsourcing proponents suggested.

Senator LUNDY—Just for the record, are you aware of any of your colleagues being approached by representatives of the federal government seeking your expert advice on IT outsourcing?

Dr Willcocks—Not at all, no. I am not aware of that. If I have not made it clear in the documents I sent you, I have given expert witness advice to the UK government with regard to public sector IT projects; to a congressional committee in the USA on restructuring the internal revenue service—and I think one of your representatives from the tax office gave expert witness in 1997 to that committee—and we have had some research dealings with the South Australian government and the Australian government EDS arrangement which we wrote up in our latest book. However, apart from that, our contacts have been nil.

Senator LUNDY—Thank you for that. Can you express a view on the relative merit of consultants Shaw Pittman Potts and Trowbridge who were engaged by the federal government here to provide advice?

Dr Willcocks—I am not really in a very good position to express a view. I am aware that they have a reputation for being very good legally. I do not know what advice they gave the government or the body appointed to manage this, and I do not know the detail, so I cannot comment on that. By reputation, they are one of the strongest legal firms in this field. The advice that I have given to people regularly since 1996 is that, if you are not a mature user of

external supply, you need advice not just from legal outsourcing consultants, but from IT experts in outsourcing. Some of the best people tend to be ex-supplier managers who have set up independently. For example, the Inland Revenue in the UK hired a firm of about 20 consultants—I think they used about three of them—who were very experienced in the IT outsourcing business to sit above, if you like, the process of getting the contract, and also to sit above the operational aspects of the deal in the first three years to say, in almost a semi-audit role, 'What's happening here? Why are they saying this? Are we doing the right thing in this respect?' I suspect—and again I cannot be absolutely certain about this—that a certain amount of this IT practitioner-outsourcing expertise was lacking in the advice given. That is my reading of the documents.

Senator LUNDY—With respect to your research, can you shed any light on the issue of competitive neutrality assessments and how various governments or corporations construct their cost baselines, and the financial methodologies they apply to them, to establish whether a business case can be built?

Dr Willcocks—I am very suspicious of the manipulation of accounting procedures to justify doing anything with IT or in business. I re-read that last night. It seemed to me that it is an argument over an accounting procedure. The truth is that, however you account for things, what matters ultimately is how much things really cost and what they are really worth to you. Speaking as a qualified accountant, I looked at the argument that the NAO was having over the accounting procedures you are referring to. The weight of my sympathy was with the NAO argument, I must confess, but actually the weight of my sympathy is not with any of those arguments. The written paper I gave you suggests that what is significant is the real costs and the real benefits that you are actually getting, and that is what you should be looking at, not just the manipulating of accounting procedures to justify going down A route or B route. Although I recognise that that is a useful thing to do, it is not a sufficient thing to do.

Senator LUNDY—I have another question in relation to security and privacy concerns associated with the outsourcing of information technology. Particularly in the public sector, what has your research shown as to the validity of concerns about security and privacy of data once it is being managed by a contractor or by an external source?

Dr Willcocks—I do not think you need to restrict it to the public sector, because private sector companies equally have real problems about security and privacy—probably less so about privacy, but certainly about security. There were a number of worries in Britain about this—for example, the Inland Revenue deal. EDS started sending data processing abroad, which caused a bit of a ruction in the media at the time. As far as I am aware, having looked at a number of these deals—not in Australia, but certainly in the UK and the USA—there are strong provisions in contracts to guard against many of those worries. Governments are wise to put in those provisions at the front end. I am aware that people have talked a lot about the potential problem of that, but I am not aware of actual problems as a result of IT outsourcing in the public sector—as yet. Whether there is a real latent problem there, I do not know, but I have not yet encountered anything significant in nine years, and we have looked at quite a few public sector agencies that have outsourced.

Working in the field, a number of outsourcing suppliers make the point that, quite often, data is more secure now because they are more security conscious than the previous regime could

have been. Certainly, one interesting thing that I have been finding recently, working in the market of application service provision in the legal profession, is that the legal profession is very concerned about data security and data privacy. When we went into small legal firms, we found that frequently their security and privacy arrangements were awful and that by outsourcing information technology we could give them a level of security and privacy that they previously did not have. Indeed, that would be one of the benefits that we could have offered in these situations. This is working in Los Angeles. I am not saying that that always happens in IT outsourcing deals, but there is potential for improving security and privacy arrangements.

Senator LUNDY—On the degree to which outsourcing and the nature of the contract can restrict innovation in information technology and how it is used by entities—

Dr Willcocks—Yes.

Senator LUNDY—what does your research show in terms of the pitfalls, perhaps, in what I have described as putting a technology straitjacket on some organisations if their contracts are too prescriptive, too narrow or do not provide for enough flexibility in the progress of the technology?

Dr Willcocks—One of our significant findings is that there is a massive lack of innovation as a result of IT outsourcing. That is not to say that, very often, outsourcing companies have not refreshed infrastructure and replaced poor systems with better systems. But in terms of real innovation coming through and in terms of getting that level of flexibility and new technology in place, I am hard-put to think of a particular deal where that happens from the initiative of the outsourcing supplier.

I can think of a number of deals where the explicit complaint from the client organisation was, 'Where is all this innovation that we were promised? It is not actually coming through.' I will give an example of what was supposedly a good deal: BP Exploration in 1993-1998, which I mentioned in my written evidence. I knew the IT director quite well. He said there was no innovation coming through from the three suppliers even though they were chosen as world-class suppliers and could innovate. The reason seems to be that it takes a lot of effort and time for the supplier to think through how to innovate. It needs the knowledge of the business, which they do not often have to the degree required.

Also, they get so buried in the operational problems and issues on a day-to-day basis that thinking more strategically out of the box by the supplier is quite a difficult thing to do. The answer to the question is that generally speaking the innovation has not come through in most of the deals that we have looked at. But should it be the IT outsourcing company's responsibility anyway? It seems to me one of the core capabilities of an in-house operation of a business or government agency is to control the agenda in terms of innovation and what they want to do as a business or agency. Where the responsibility should lie is an interesting question.

Senator LUNDY—To follow up on that, one of the issues in the Australian federal government's IT outsourcing has been whether or not to include applications development as part of that vertically integrated and clustered contract. I would be interested in your comments on the inclusion of applications development as part of these packages. Also, I am interested in

any observations you have about how organisations can procure in such a way to provide opportunities for innovation as part of that whole process. Are there any structures or approaches you can identify that do in fact facilitate innovation at both applications and infrastructure level?

Dr Willcocks—The point I made earlier is a true one. To look to the outsourcing supplier to initiate innovation is probably a losing game. If we take the issue of applications development, all our research suggests that in situations of what we could call low technology maturity—that is, where you have got a new technology that is pretty unstable and you are not quite clear what you want to do with it or it is an existing technology but a radically new application or there is just not the expertise available to develop and run with this application—the worst thing you can do is outsource application development in that climate. That is pretty true of most applications development.

What you should do is to run an in-house team, which is largely run by the in-house group, including business people, not just IT people. Where you need expertise and resources you should buy them into that group rather than outsource it to them and look for an outcome from that group. We have plenty of failure cases where you basically put application development over the wall to the outsourcing supplier or even just the IT function. It needs to be a multidisciplinary team business, with IT people involved and external suppliers involved as resources to work on the team if you are going to do application development well. That is certainly a very strong finding out of all our research. You use the market but in a buy-in rather than outsourced way.

In terms of innovation, the point I am making is that the responsibility should lie with the in-house operation—and I do not mean just IT; I mean the business or government agency side as well. To actually innovate should be seen as the core capability. That innovation should be tied into your overall strategic intent as an agency or business. From then you can actually pull out what the critical success factors are, what you need to do and where IT fits with that.

From then you can give pretty detailed instructions to a supplier as to what is required from them and how their expertise can be used. What we are finding is that all too many organisations do not quite understand this. They hire an outsourcing supplier who promises innovation and says, 'We are world class on applications in social security'—or something like that—'and we have done them in the USA and we will get them up to scratch and we will show you innovations.' What actually happens is that this gap occurs because there are no real mechanisms, processes, funding or ways of remunerating that actually support innovation coming through from that source. In fact, it is probably not a very good source from which to expect it anyway. I think that would be a good summary of where we are on that.

Senator LUNDY—Further to that point, with the latest developments in technology and service delivery for government agencies and departments going to an Internet or web interface, do you think that this issue of the capacity of these organisations to innovate is becoming even more important or more essential to their service offerings? I am thinking of the latest technological trend to place services and create new interfaces with clients and customers online.

Dr Willcocks—Absolutely. But it is the capability that is the key here. What I think that I am seeing is that if an agency is very clear about its strategic direction and about who its customers are and how it can service them in a better way, then the innovation occurs around that issue—the clarity of strategy, the clarity of how better service can happen. It is then that you start looking at the technologies as one way forward. There might be other ways of doing it, but web based technologies are enormously capable in the things that they can do. What you are looking for is the business clarity and the innovation and the imagination coming from the agency to actually identify the capability you should be caring about. Unfortunately, there is all too much capability but not very much detailed perspective on how to use it. That is the issue. I do not think you can look to outsourcing suppliers to actually do the thinking for you. They cannot actually be the agency. That is not their core business.

Senator LUNDY—Going back to the state of play in Australia in 1995, 1996 and 1997, are you able to offer an opinion as to the relative maturity of the Australian market to cope with the big contracts that were presented by the federal government to the market here? I am looking for your observations on the maturity of the IT outsourcing market here at the time that this federal government program was initiated.

Dr Willcocks—That is not something I know a lot about, I have to say. It is not something I analysed in 1995-96. I would have a better opinion, I suspect, of what is going on now. I was aware that a number of big players from the USA and Europe were looking at the Australian market. I was aware that they were desperate to get contracts and to get a footing, especially in the lead cities in Australia. My sense when I was there—and again this is not a well-informed sense—was that there was a burgeoning market in Australia in terms of Australian suppliers, that they were reasonably small and that there could have been a market for them in terms of smaller deals. One way forward, I thought at the time, was for government to break down the different contracts into quite small deals that were sort of Australian-supplier-sized, if you like, and proceed in that way in order to develop those suppliers further, with a view that there would be consolidation amongst them three or four years down the line when it became clear that they had to offer something much bigger to clients. It seemed to me at the time that that would have been one way forward.

I do not think it was that mature; the local set of suppliers was fairly small and there would need to have been consolidation amongst them in order to offer service on larger contracts. At the same time, one of the government's missions was to develop the economy. That might have been a route worth taking—or something like that. I have not thought that through in any great detail. I am sure one could have put some good minds to work on that and an alternative approach could have been thought through.

Senator LUNDY—In terms of your observations at that time, the contracts as they were offered to the market were clustered or grouped in such a way that prevented smaller Australian suppliers and companies from tendering, and really put the offering into the ballpark of the larger international, multinational IT corporations. With respect to that clustered or grouped approach, bringing together multiple agencies, where does that fit in terms of the wisdom at the time as to how to cleverly procure IT from an external source?

Dr Willcocks—The logic seemed to be based on the notion of economies of scale and standardisation. Of course, there are aspects of information technology that can be standardised

and there are limited economies of scale to be had from doing that. At the same time, IT is a very complex area. One has to disaggregate IT activities. Certainly, in 1996, we wrote a paper which talked about IT not being a homogenous commodity in an organisation. In fact, it also integrates extremely strongly with various business processes. So one has to look very carefully at what IT activities are and where they integrate with different systems and different parts of the business. In 1996 we had arrived at a pretty mature view that one has to disaggregate IT activities and decide what is best done with each IT activity. Some things will point towards outsourcing, some will point to buy-in contracts and with respect to some things you will say, 'You should never outsource this; not for the next five years, anyway, because it's a critical differentiator of the agency.' So we got a pretty subtle, mature perspective on that in about 1996.

Some of that logic now sees itself in the thinking about the groups that have not yet been outsourced and that are on hold. The Humphry report makes what I think are sensible statements about those groups. Getting into the detail of it, it becomes obvious that it is not that simple. Whereas at the front end, economies of scale arguments and cost savings arguments seem to be quite persuasive, at the time, in 1996, we never bought that. So I was a bit surprised that the government did. There is a logic to economies of scale, but I think it is more limited than people thought in terms of the clusters in the Australian scene.

Senator LUNDY—The issue of industry development had a key impact when this whole process was started but now it is again the subject of discussion, debate and consultation with industry as to what degree you can link an outsourcing strategy with industry development objectives, from a public policy point of view. Can you provide us with an insight as to what degree other jurisdictions link industry development opportunities with procurement in this way? Can you give us some idea of how that is occurring, if it is occurring?

Dr Willcocks—The problem does not arise quite so much in the areas which I have mainly looked at, which are the United Kingdom and the USA. They are a bigger set of markets and there are a lot more players. There is usually room for home-grown players in the marketplace, if not as first-tier suppliers, certainly as second-tier suppliers. There is plenty of work in those terms. Much more interesting would be to look at Singapore and India as parallels for Australia. The Indian IT industry is taking off and it is quite heavily supported by government. You can be pretty sure that the contracts that are being drawn up within India are with Indian companies, to support that process. In Singapore, the government has taken an intervention-type strategy. They will do things that will support developing the IT industry. That means they will use external suppliers from other countries, because they are an international entrepot. They will also not do that to the point of harming their own trajectory, as it were.

I think Australia can learn from them, because I do think that you do have a problem. You have a problem in terms of the IT companies not developing fast enough and the skills base of your country not developing fast enough. If you look to those two countries, you might get some detailed leads on exactly what the role of government could be in the circumstances in which you find yourselves. Certainly the use of external suppliers in government work would be one area that you could look at constructively.

Senator EGGLESTON—What other things might the government do to facilitate industry development? The question asked by Senator Lundy, which you have just answered, is one that

I was interested in asking you in terms of international comparisons. What other things have governments done in other countries to facilitate industry development in the IT area?

Dr Willcocks—In so far as it has happened, it has happened at the regional level rather than at the central government level. Singapore is an exception, because it is a city-state and the government is both a central and a regional government. I cannot give you chapter and verse on it, but certainly in the USA I am aware of three or four states where whole sections of the IT industry have been supported by regional government. They have developed a capability in those particular states which previously they did not have and which has brought an awful lot of work and jobs to those particular states. In India there is a stronger central government thrust in supporting local industry in many ways. That would be regional based as well. It would operate on both fronts. Personally, I think that central government can create a framework for industry development, but it has to be delegated to regional areas and, in Australian terms, into state governments. That is where the benefits are felt, if you understand my meaning. It is also where the details of how to do that actually work themselves out and can be managed to an appropriate level. Am I answering your question?

Senator EGGLESTON—You are, in a general way, saying that in some parts of the United States, the state governments—maybe in places like California—have sought to facilitate IT industry development. The general issue of outsourcing as a facilitator was one of the government's objectives. It was to facilitate industry development. I suppose that outsourcing has acted as something of a catalyst, would you not agree, in promoting the development of the Australian IT industry?

Dr Willcocks—I do not know enough of the detail. I have read in the reports what has been outsourced and to whom. There was a figure of something like 75 per cent of products and services that are Australian based. I read another figure of 30 per cent, but I am not quite sure what the 30 per cent was. Was it that 30 per cent of the revenues go to Australian IT suppliers? Is that correct?

Senator EGGLESTON—It is something like that. But you said that the Australian industry was characterised by a lot of small companies, which would, with the requirements of outsourcing, lead to amalgamations and the development of bigger, more effective companies that are able to take on bigger contracts.

Dr Willcocks—Over time, yes.

Senator EGGLESTON—That seems to imply that outsourcing over time has acted or will act as a catalyst for the further development of this industry in this country.

Dr Willcocks—Yes—I am not quite sure what you want me to say.

Senator EGGLESTON—I think you probably do, but never mind. You also mention hidden costs. You sort of say that outsourcing can be seen as a cost-saving measure, but also indeed that there are lots of hidden costs that have to looked at and borne in mind. Although it is in your submission, could you please go through some of those hidden costs and discuss the fact that outsourcing may not end up being as cheap an option.

Dr Willcocks—Vendors usually sell their services on the basis that they can achieve economies of scale and that they have superior management practices. I would put some question marks against each of those because economies of scale are pretty achievable at low size levels, in fact. We found plenty of examples of organisations that were quite small achieving quite significant economies of scale by reorganising the way that they actually operated, for example in consolidating their own mainframes and doing it in-house. The other economy of scale is meant to be that they have IT skills expertise; this set of resources and skills, which they can employ and they can hire out, which are not available as cheaply in-house. That has turned out to be a bit of a myth because in fact IT skills are quite scarce amongst IT suppliers as well as in-house functions, and actually those prices that the IT suppliers now have to charge are market based and quite high. I am not saying that there are not economies of scales and that there are not superior management practices in certain circumstances which suppliers can give. I am saying that it is not always the case; there is nothing inherent in that and it depends on the specific circumstances. Quite often cost savings that come from that are stated initially but are not there when you actually come to run through a five-year contract. That is one thing.

The second is that if you actually go heavily into cost savings then one thing that you will try to hit on the head is the profit margins of the supplier, by definition, because you want to reduce costs as much as possible; so you eat into their profit margins. Suppliers can actually sign deals that are on very low profit margins and sometimes sign loss leader deals in order to get contracts, knowing that later on there will be various ways in which the contract can be reinterpreted and additional services can be charged for—for example, the contract makes statements about what will be supplied, and there are certain things that are not in the contract that you know the client is going to need and that can be charged a different price for. That amounts to additional costs. So there are various ways in which the supplier will seek to actually bolster its profit margin, and if the client is not aware of this—having signed a cost saving deal which is on very low profit margin for the supplier—then these will come through as hidden costs across the lifetime of the contract in various ways. We know plenty of deals where that has happened.

The other issue that I raised in the written evidence was that cost savings are there, but that there is invariably a trade-off between cost savings and the level of service that you get. You can achieve cost savings in an outsourcing deal, but—as I think I raised the question—at what cost? In terms of a government agency's responsibility to provide a level of service to the public, how far does that ability erode as a result of a primary focus on cost savings within that particular agency? These are just some.

I have a document called *Best practices in information technology sourcing*, which is dated 1996 and lists 12 hidden costs additional to the ones that I have just outlined. As I mentioned in the written evidence, it was published in the 1997-98 IT outsourcing guidelines for the National Health Service. We have done a lot of research on that. There are, manifestly, many hidden costs that come through. Some of them are very difficult to predict—that is why we call them hidden costs. We are aware that there are now a number of things that one should look out for, but frequently there are other things for which it is difficult to legislate. The point is that you should know that there are going to be unanticipated hidden costs, and when you create a rationale for outsourcing you should allow for that before you make statements about significant cost savings. In the surveys that we have done in 2001 there is no evidence that many

organisations are experiencing significant cost savings from IT outsourcing. In Australia, of the ones we looked at, only seven per cent are getting significant cost savings.

Senator LUNDY—I have one final question, and it refers to issues that you have raised in your written submission. You identify a big danger in the Australian context in that it is easy for the government to become captive to a few big companies, basically, and you list a series of implications arising from that, including the consolidation of expertise and the pricing of that expertise out of the market and so forth. How strong is that concern in relation to our potential to develop and grow an Australian information and communications technology sector? You have identified it as a big danger. I ask the question in the context that we know that 40-odd per cent of procurement of information communications technologies in this country can be attributed to governments and government purchasing.

Dr Willcocks—Yes.

Senator LUNDY—I am just asking for an extrapolation on that point or any additional observations that you can make at this time.

Dr Willcocks—Remember that I am not acting for any government here, but Australia needs to concentrate on creating and developing further second-tier suppliers within the Australian context that operate initially in Australia and then can operate abroad successfully. Again, India is a very interesting example to look at in terms of how they have managed to take off in their IT industry. I am sure that there are things that government can do proactively at central level, and particularly at regional levels, to encourage that. It needs very deep thought about how to develop a strategy for that, if that is what government is going to do in Australia. What worries me is the alternative. If government does not do anything, how will the thing unravel in the next five to eight years in an Australian context? I have done a bit of thinking on that and I do not think it looks good—in terms of being an Australian, anyway. The government has to either create a framework in which things can happen or intervene in more detail than it has done in the past.

Senator LUNDY—Thank you for that. I take this opportunity to acknowledge your work and that of your colleagues, including Mary Lacity, over the years because it has contributed greatly to an informed public debate about these issues.

Dr Willcocks—Thank you very much, Senator.

CHAIR—That concludes the questions from this end. Do wish to make some concluding remarks?

Dr Willcocks—No. I think I have said as much as I can in the present circumstances. I wish you all the best with your report and inquiry, and I hope they lead to some good outsourcing in future.

CHAIR—Thank you for making your time available. That concludes the public hearing for the day. The next public hearing of the committee has been scheduled for tomorrow, 18 May. Those interested in following the inquiry should refer to the committee's Internet page, which will provide information about the progress of the inquiry on an ongoing basis.

Committee adjourned at 6.50 p.m.