

JOINT STANDING COMMITTEE ON THE CORRUPTION AND CRIME COMMISSION

**INQUIRY INTO PUBLIC SECTOR PROCUREMENT OF GOODS AND SERVICES
AND ITS VULNERABILITY TO CORRUPT PRACTICE**



**TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
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Members

**Ms M.M. Quirk, MLA (Chair)
Hon Jim Chown, MLC (Deputy Chair)
Mr M. Hughes, MLA
Hon Alison Xamon, MLC**

Hearing commenced at 10.09 am**Ms CAROLINE SPENCER****Auditor General, Office of the Auditor General, examined:****Mr JASON BEELEY****Assistant Auditor General, Performance Audit, Office of the Auditor General, examined:**

The CHAIR: On behalf of the committee, I would like to thank you for agreeing to appear today. I am Margaret Quirk, the Chair of the committee. The other members of the committee are, to my left, Hon Alison Xamon, MLC; to her left is the Deputy Chair, Hon Jim Chown, MLC; and to his left is Mr Matthew Hughes, MLA, the member for Kalamunda. It is important that you understand that any deliberate misleading of this committee may be regarded as a contempt of Parliament. Your evidence is protected by parliamentary privilege. However, this privilege does not apply to anything that you might say outside today's proceedings.

Would you like to say anything to start with, in terms of the role that the Auditor General has in the operations of agencies?

Ms Spencer: Certainly, at its most simple, my role and the role of my office is to provide assurance to the Parliament around the financial management and performance of the public sector, which now includes local government. That is obviously a significant expansion of our role, and obviously a highly complementary one in terms of confidence of the Western Australian community. I did not have any opening statement prepared, Chair, but I am happy to take any questions.

Hon ALISON XAMON: When you took on the local government function—because there has been a lot of work that has emerged as a result of that—did you get sufficient resources to be able to take on that additional work, or any additional resources?

Ms Spencer: We did get additional resources to be phased in with the transition of financial audits. There are 148 local governments. We audited 46 for financial audits last year, another 65 this year, and the remainder next financial year. Those financial audit fees are on a cost-recovery basis. There has been a significant increase in financial audit fees for those local governments because they were underpaying and we have additional quality requirements. We also have additional reporting requirements to the Parliament. That costs us time so we add that to our audit costs, just like we do with the state sector. For the financial audits, we can cost-recover, with one caveat which I will touch on.

For performance audits we have been given additional funding which is phased in—\$2 million over a number of years. That gives us a certain number of performance audits that we can do within that budget. That is obviously spread across 148 local governments. We have found to date, with the four or five local government audits that we have done so far, those performance audits are taking about 25 to 30 per cent longer than the equivalent state sector performance audits because we do multiple entities at a time and those entities are just not familiar with the performance audit processes or how we do things as auditors. There is also staff turnover. We are just finding slightly different issues. Obviously, there is a budget process underway and those are matters for government. I recognise the fiscally constrained times. I have presented to government and our joint audit committee what I believe are our value-added services for the office to provide in the sector. It is really up to the Parliament and the government of the day to consider those in the context of other competing priorities.

But there is the issue that because it is a new sector for us to be involved in, and there are some fairly significant concerns around capability in that sector, that it requires additional engagement on behalf of our auditors. I look at how much effort my senior people put into engaging with those local government entities at every single point in a financial audit and in a performance audit, and it takes more time. They are crying out for resources, such as better practice guidance and other support from the office. We will do the very best we can within the resources we have available, but at the time that the budget was developed by the office—the budget figures put in for resources for local government auditing—we did not have experience in auditing the sector. It really was a bit of an unknown. We will continue communicating with the joint audit committee around our resourcing and the government of the day in current and future budget rounds.

The CHAIR: This is a public hearing, but I will take the opportunity, given that there is not anyone in the room. In terms of agencies, and your predecessor did name a few agencies who, in the context of procurement, were, if you like, the usual suspects and needed greater oversight in the future because of their lack of probity in some respects. We are wanting to do some case studies within our report. Are there any agencies that, if the file lands on your desk, you think, “Oh my goodness!”? I know this is still public, but not many people sit down and read the transcript, other than people who need to get a life. I think it is quasi.

Ms Spencer: Obviously, public administration is complex. The big stuff and the complex stuff gets left to government to pick up. There are some large agencies within the state sector in particular that are more complex and have become more so as a result of machinery-of-government changes. The ones that I would say at the moment we are doing additional risk assessment and devoting some additional time and audit procedures to in an annual financial statement audit sense are those larger, complex and recently amalgamated agencies.

Hon ALISON XAMON: The Department of Communities, for example?

Ms Spencer: Yes. Merging of systems is no simple thing. We would like it to be, but it is no simple thing. It is expensive, time-consuming and it takes a lot of resources of existing staff, as well as —

Hon ALISON XAMON: How about the Department of Justice, because that has incorporated corrective services now, which I know there have been some concerns about in the past.

Ms Spencer: Yes. We put additional resources in last year’s financial audit in particular on looking at those amalgamations and, obviously, health and education are always big. They are roughly one-third of the state budget each and they will always be complicated and complex. Recent health governance reforms really are only just bedding down and the health service providers, those boards, are getting across their roles. We will be looking at health governance from a performance audit perspective to really see whether those intended governance structures have been implemented and some of those anticipated benefits have been achieved.

The CHAIR: I do not want to put you on the spot. I was just curious more than anything else.

Ms Spencer: There are very few straightforward ones.

Mr Beeley: There are. It is a really difficult question. A big agency has got capability but it is complex and sprawling and therefore difficult to exercise the oversight for them. Then there are other agencies, often smaller ones, which do not have the capability and only infrequently might they do a major procurement, which means there is a risk attached to that because they are not quite clear what they are doing and how to governance those areas.

The CHAIR: One of the things that struck us as a committee is that there are not more standardised procedures within the departments. There is quite a lot of difference in how they go about their practices, how much they are oversighted, how much guidelines are followed, sanctions or lack of

sanctions if guidelines are not followed, and even some departments like PTA and Main Roads are just being exempted effectively or having a cap before they have to comply. That must make your job a lot harder.

Ms Spencer: It does. There is the overarching financial framework and Treasurer's Instructions but, certainly, looking at the different implementations of those, as well as any exemptions due to regulatory instruments or other mechanisms, it is complex, which is why every performance audit in particular, which is a fairly bespoke examination of a particular topic—it is not an annual thing in each agency—requires a lot of careful planning to make sure we get it right.

[10.20 am]

The CHAIR: How much contact do you have with the CCC?

Ms Spencer: Fairly regular. So, I can expand on that, if you like.

The CHAIR: Yes, please.

Ms Spencer: Look, so I am a disclosing authority under the Public Interest Disclosure Act and I have investigative responsibility for substantial misuse of public resources. We are often copied in where a whistleblower makes a disclosure; they may make it to a number of agencies. It could be myself and the CCC or to the PSC, and that goes directly to PID officers within my office and I make the decision as to whether we proceed with an investigation based on the work they have done, the advice they provide. So, we will refer matters that we think are best investigated by the CCC to the CCC as that arises. My predecessor, Mr Murphy, would meet with integrity officers periodically and I have met with the Public Sector Commissioner, the Corruption and Crime Commissioner, the Ombudsman and the Information Commissioner a number of times since commencing my role in May last year and will continue to do so just to keep up to date. But then at an operational level, my Deputy Auditor General and the CEO of the CCC have periodic quarterly catch-ups and as required on what is underway just at a broad level. I am obviously very conscious that the legislation that has been enacted by Parliament gives us each discrete powers that we must perform independently as independent integrity officers. We come at it with a different legislative mandate and a different perspective to relevant issues and we have to form our own professional judgements and be accountable to a Parliament for those. It is important. I think we are all mindful of our respective roles and keeping a healthy communication on what is happening, but not working too closely together.

The CHAIR: A good example is sort of north metro. Once that sort of broke, you have got three or four separate inquiries. I appreciate they are looking at different aspects, but it is almost ineffectual that people are kind of tripping over themselves, effectively.

Ms Spencer: Absolutely. Probably a more recent example is the Japanese trade office.

The CHAIR: Yes.

Ms Spencer: From my perspective, I think that was handled very well by the director general in terms of keeping me apprised as Auditor General of the anomalies that she had found and what she found when she got into the chair and got an investigation internally underway and telling me as much as she appropriately could. She had referred the matter to the CCC and that is really as much as directors general will tell me, as appropriate, because then it is up to the CCC as to what they do and they may be keeping the director general apprised of progress, but that is not for me or anyone else to know about, appropriately. Look, I thought that was handled very well by the director general so that a risk that I was aware of—my financial auditors understood the risk that that had been identified, the concerns of the executive team there, but making sure that we do not duplicate precious oversight resources is important.

Hon ALISON XAMON: That is Rebecca Brown, is it not?

Mr Beeley: Yes.

The CHAIR: My colleagues will have some other questions to ask, but it seems to me that the Auditor General's office is like the canary in the coalmine. On so many of these matters that are high profile, you look back and you would have done a report two or three years ago or last year and it has gone through to the keeper to mix my metaphors. So, that must be of some frustration to you or how do you reckon we can make sure your recommendations are taken a bit more seriously?

Ms Spencer: I think that is a really nice segue, chair, into a model that I think is very useful and I am promulgating throughout the sector in my discussions with leaders but also in speeches I give and in working with—we are going to be producing a better practice guide on some of these things. But, really, we are one line of defence in any sound governance framework—external audit is but one important mechanism—but there are many other mechanisms in a sound governance framework that must exist and work effectively to provide good control, in effect, but also provide assurance to stakeholders, external and internal, that things are working. If the committee is happy, I will pass around a model.

Hon ALISON XAMON: Yes, please.

Ms Spencer: I am happy to talk you through that. So, this four lines of defence model is one model that shows the role of my office as external auditor but also the very important role of parliamentary inquiries and regulator reviews and other external scrutiny mechanisms, including that of the CCC. They are external assurance mechanisms that really pick up things as a last—it should be as a last resort. What we want to see when things are working effectively is that management is implementing proper controls so that things do not go wrong. That is things like reconciliations, passwords on computer systems, proper protective security, locking doors and filing cabinets and having appropriate access controls around passes and things, all the things that you have in place to stop things going wrong, as well as training staff, including in OH&S so they do not injure themselves. All those controls to stop things going wrong, you want the frameworks in place up-front to be implemented by management but then you need monitoring of those as the second line of defence for management to do its own oversight to make sure they are reporting. So, management reporting and appropriate quality control within an organisation, if you like, around supervision of that—and that is management's job to see that those controls are properly designed and implemented. Then to give them comfort that that is working, having a third line of defence, which is internal audit, properly structured, resourced and authorised to provide information that will be the eyes and ears of the governing body, including the audit committee. Then we are that last line of defence. If it gets through to us, there is usually a problem.

We are in there every year for financial audit. We are in there periodically for performance audit and we do pick up a lot of control weaknesses on an ongoing basis and yes, it is frustrating that we can see these things. We see these systemic weaknesses and we point to them and they are not actioned. That is the really important role of a high-functioning audit committee that implements both the internal and external audit recommendations in a timely way. Agencies do not always have to agree with the auditor around prioritisations of controls and rectification of any shortcomings that have been identified because there are many competing priorities, but it is important that they give due consideration and at least understand the risk trade-offs. If they are not going to implement something, they understand the risks that poses and they think about any compensatory controls they have, and they are actively managing risks.

The CHAIR: So from your experience does every agency have an internal audit committee or not? Is that something that we need to recommend?

Ms Spencer: The jurisdiction I am most familiar with is the commonwealth and I have observed since I commenced in my role that audit committees in the Western Australian public sector are not as mature as they are in other jurisdictions, particularly the commonwealth but also New South Wales and Victoria and the ACT. So, I have identified in all my consultations with senior leaders around the sector, with board chairs, with directors general, CEOs and chairs of audit committees that are in place, I have said they could be strengthened to provide both advice and assurance to CEOs around not just financial and performance reporting within the organisation, but systems of risk management and internal control. Are they working effectively and are they using internal audit effectively to be their eyes and ears about things that could go wrong? Everyone agrees that they are not working as effectively as they could be. When I speak to the teams in the office that attend audit committees as observers, as external auditors to provide information where they are formed, they are not rigorously following up on audit recommendations. To be told they are not doing anything about it is really a waste of public resources. I understand competing priorities and complexity, but what we find is, as you said, Chair, that subsequently control weaknesses that we have identified have let things through that just could have been —

The CHAIR: There has been a bit of discussion about KPIs for DGs and agency heads. Is that the kind of thing that might readily be a performance indicator or something that a DG has to comply with or actively engage with?

[10.30 am]

Ms Spencer: At the moment I think the framework provides adequately for those structures to be in place. In the discussions I have had with directors general I think there is a recognition around a need to build governance capability—strengthen a government’s capability—in agencies. Part of it is at the most senior levels around how to appropriately manage complex risks. With the machinery-of-government changes, they have only got more complex. A larger span of control requires more sophisticated monitoring and, really, a culture of awareness of risks and good governance. I do not know if having a KPI with an audit committee in place—because how do you measure effectiveness—but I know just anecdotally, and I would like to test this in a future audit probably two years down the track, that since I have had my initial round of meet-and-greet discussions with all the directors general, I have had four call me to say, “Look, I’m revising my audit committee structure. I’m thinking of some independent members. I’m thinking of these skills and can you recommend anyone?” I say, “No, I can’t provide any recommendations, but the sort of skills you might look for is” et cetera. Some audit committees that I have seen that are functioning fairly well and sort of look, feel and smell like a well performing audit committee are some of the GTEs, just because they have that more private sector sort of corps act perspective and often private sector members—a few private members of those boards and audit committees who have some private and public sector experience. I think that is a useful perspective to bring, just around the discipline of a good functioning audit committee. So I am really pleased that they understand the reasons and now an increased awareness of the mechanisms for improving governance. No-one wants a Japanese trade office fraud or a north metro procurement fraud or a Horizon Power IT contracting fraud. If you have got the right culture and a culture in which people speak up, and they know why they are there—they are there for their public duty not for their private interests—and for people to speak up if they see people acting against those public duties, but also having proper controls and monitoring the effectiveness of those controls through various mechanisms and then acting on audit reports, internal and external, and other inquiries, as well as broader sector-wide initiatives. There is an awareness that that is what comprises a good governance framework. I am encouraged by the feedback I have had and the early indications of improvement.

Hon ALISON XAMON: Can I just ask, picking up on one of the points you just made, have you found that there is a correlation between morale and a willingness to speak up on whistleblowing matters, for example?

Ms Spencer: Definitely. If people think that there will not be any action—I see the effort and clear anguish that people experience—when they make a public interest disclosure—go through. I think the word “harrowing” would not be too strong for some of these people. If they have seen something or if they felt that that was not going to be acted upon, it is incredibly demoralising, and they will not go to the effort of providing it. These are extreme cases of some allegations of fairly serious misconduct, some of which have been investigated and reported publicly, some of which are in progress. But at the more minor level, and we saw this with the Japanese trade office and we saw it with north metro, there were earlier indications within the organisation of control weaknesses and they were not acted upon. There were good people who put their hand up and said something. So agencies need mechanisms for investigating those initially lower-grade concerns that have been flagged, to see whether there is anything there. That requires personal judgement to be exercised on an individual basis, often when their dance card is already full.

Mr M. HUGHES: You have mentioned the Japanese trade office on a couple of occasions. In terms of the way in which that came to light, it really was not as a result of a person pointing in the direction of maladministration, for want of a better word. It really is as a result of the changes of structures within the organisations of DPC—moved the responsibilities across to another department. My interest would be how over a period of 17 years none of that was picked up. We talk about red flags in terms of an indication of in fact where the gaps might be and allow for misconduct—serious misconduct. What do you take from the Japanese experience in terms of the kinds of red flags that should have been obvious to senior persons within the department?

Ms Spencer: I guess there is a couple of things. You know, one is that wherever we have people and money, unfortunately, there will be a risk of fraud and corruption—personal interest coming to the fore—and so it requires constant vigilance. Entities, which are just comprised of individuals, will have differing levels of awareness of those risks at different times. For example, I am not going to say this publicly, DPC has some of the best computer system controls that we see in our general computer controls assessments across the sector. They got a recognition in my last information systems audit report. But, obviously, the controls that they had around overseas expense claims were not as rigorous as perhaps other expenditure or other aspects of controls, and so the real lesson here, I think—this is one of the really important controls that is important in financial management, but also in other areas of an organisation—is that rotation of staff through functions. You know, we talk about segregation of duties as being really important. The same person that procures something cannot authorise the payment and release the funds and then write it up in the accounts. We need different people doing all of those things so that no-one has end-to-end control of the purse strings without scrutiny.

The other important aspect is that we need to rotate staff. A red flag for auditors and for fraud examiners is that if someone has been in their role for a very long time and has not taken leave and is really quite cagey, never fully hands over responsibility to someone, what are they hiding? This has always been a red flag. I said this to one of our senior financial audit directors as we were getting to the Horizon Power exit meeting last year. I said that as auditors we used to always talk about this: high levels of leave balance and people making sure that people took their leave and making sure there was rotation of staff, because it identifies a lot—just people asking different questions quite innocently, often just wanting to step into the role. We talked about how we are framing those findings in management letters to agencies around leave, and it really is around building liabilities in a financial sense, rather than a risk-management sense. You know, that is something that as an

office we are going to start framing a bit differently in this cycle of financial audits. But machinery-of-government changes can be very good for a number of reasons, but so can rotation of staff or moving the functions within an entity.

Mr Beeley: There is a slightly broader issue which comes back to agencies' risk factors. I think from the performance audit side of things we have often seen that agencies with regional structures, particularly where there is a lot of delegated authority into those regions, can be really vulnerable to pretty poor practice—Housing for a long time was not that great. It is that situation in which somebody has the capacity to put up the usual compliance reporting to head office but then say to their staff, "Well, actually, this is the way we are going to do things and that is going to be okay." It breeds a culture that can be really difficult to shift once it is embedded, unless you do move the people around or you have got really regular scrutiny of what is going on in those regions, and you know that you have transparency and you have accountability into them. Even a regional structure within WA—it is not even overseas—I think can be a risk.

The CHAIR: Obviously, in a more general sense, about Corrective Services—instead of them all just being at one prison, they need to have the capacity to change further.

[10.40 am]

Hon ALISON XAMON: Have you got any WA Health audits planned in the near future?

Ms Spencer: We do. Would you like to talk about the performance audit side?

Mr Beeley: Sure. We are currently finalising something on mental health, which we will talk to you about. We are doing an audit, which we are not far off finishing, on the procurement of a new laboratory information system for PathWest, which will report before the end of the financial year. That was actually something that the DG asked us to have a look at.

Hon ALISON XAMON: There have been issues there.

Mr Beeley: Yes.

Ms Spencer: And they are keen to learn any lessons that can be learnt.

Hon ALISON XAMON: Can I go back to the mental health one. I was aware the mental health one was coming, but when is that likely to be completed?

Mr Beeley: We would like to be tabling it by the end of May, hopefully.

Hon ALISON XAMON: I wait with anticipation.

Ms Spencer: It has got some very important findings.

Hon ALISON XAMON: Good.

Ms Spencer: One in particular.

Mr Beeley: We have the PathWest one. We also have something on improving ear health in Aboriginal children at the moment.

Ms Spencer: Ambulance services; so looking at St John again—it is a follow-up audit.

Mr Beeley: The contracts for ambulance services.

Ms Spencer: That is an example of our office using follow-the-dollar powers, where services are provided by an entity on behalf of the state. We go and look through to the entity.

Mr Beeley: Yes. That is also an example, in terms of recommendations, where we will go and follow-up and see if our recommendations from previous reports have been implemented or not; but also we try to drill that a little wider these days to say have our concerns, issues, in that space been more broadly addressed, rather than just ticking a box to say, "Did you implement specifically what we said you ought to do in the recommendations?"

The CHAIR: I sometimes think, in the procurement area, it is not the big amounts but it is the little amounts that can slip through. Have you any instincts as to how that can be more readily identified without creating a whole lot of extra administrative impost, or how that can be better identified?

Ms Spencer: As auditors, we focus in particular on material balances that will materially affect the financial statements or are material in value or nature on their own. When my audit teams do sample testing, they will often on purpose pick up a number of smaller value transactions. Then we do controls testing to look at the design and implementation of controls and walk through financial management controls, which will pick up supplier payments. It is very difficult to detect fraud where there is collusion. My auditors will look at valid contracts that are signed by an authorised delegate within the entity, that there are valid purchase orders raised within the system within the contract amount, that there are appropriately authorised invoices and goods received, and then the payment has been properly authorised by an authorised officer from end to end. If those documents are falsified and supported through collusion with external parties, it can be almost impossible to identify that, which is why we need other controls such as rotation of staff. That is why we need a culture embedded there that if there are red flags raised early on through internal audit or any other mechanism of management review, that they be actioned. External audit only identifies about eight per cent of frauds; internal audit about 16 per cent; but whistleblowers are almost half of frauds that are identified—47 per cent. The others are through various other means—discovered by accident or a management review or other staff or regulators.

Hon ALISON XAMON: So that really goes to the importance of culture then.

Ms Spencer: Absolutely, and all these mechanisms before you get to us or parliamentary inquiries on these matters. We all have an important role to play; we are all important cogs in the wheel. I could not say that one is more important than the other—they are complementary. That is where people need an appreciation of the overall framework and how it works together—their part in it and how to reach across to other parts and look to what others are doing, to do it in a complementary way and not duplicate resources, because they are precious and they could be used for frontline services instead of back-office stuff. This stuff is what contributes to effective and quality service delivery.

The CHAIR: The Department of Finance is working on procurement reform and they are doing it as part of the public sector reform program. They are going to implement this big policy which, I gather, is a couple of years hence. I know the Auditor General is independent, but have you been involved in that process to date?

Ms Spencer: The role of strong central agencies is critically important to good governance in the public sector, so Treasury with the financial framework and Finance with its procurement policies and guidelines, and the support they provide. Where we are invited to attend these working groups to develop, we typically say, “Thank you, we will attend as observer,” or we will receive drafts to see if there are any fatal flaws. But, really, so that we can come back and audit both the design and implementation and the role of central agencies in guiding and supporting agencies, we manage that self-review threat to independence and do keep separate. I have spoken with the director general Jodi Cant around the reforms that she is putting in place—she obviously sees that as a priority—but I do not think we have anyone observing on a working group for that particular reform.

The CHAIR: You would anticipate before it is finalised that there would be the ability for you to at least comment on it.

Ms Spencer: Yes. I expect so and we are happy to do so. It often falls to a limited number of people within the office. I am conscious that we have got a lot of knowledge in the office, and being able to

share that appropriately on framework issues—very happy to do so. But also it is not a stamp of approval in any sense; that really is the policy of the government of the day.

Mr Beeley: We would also hope that obviously we have a body of work, going back quite a long period of time, as you say, often on things that come up, so we would expect somebody like Finance putting something like that together to work their way back through reports that we have made and pick up the kind of recommendations or findings that we have and feed those in. Hopefully, that avoids us having to have that kind of specific input as they are putting it together. The experience that we have hopefully feeds in through the report base.

The CHAIR: One of the things that we found in this inquiry is the dearth of staff who are trained in procurement or the specialists. How does that get remedied without massive costs being incurred? Have you got any feeling about that? Is it something about raising the status of these people? How do we actually address that?

Ms Spencer: There are a couple of things, I think, recognising that these functions are important to good governance and making sure that there is a recognised capability need within the sector, and then there are materials for both training these people and supporting these people. There is support provided by the Department of Finance to essentially hold agencies' hands when they do not do procurements very often. That is a valuable service. With procurement, I think people are often aware of the risks; they do not want to get it wrong. It is then the contract management that is a problem, and that is when often all the attention goes off within agencies. It is not just effective contract management around getting what you paid for; it is also around contract extensions and any things that can go on there, but around also management of those risks to agencies. With information systems where we have got lots of vendors providing core government systems, contract management of those systems is one of those things that I think slips through too often. That lack of capability, often people do not know they are a contract manager, therefore they do not recognise the skills required to perform that function effectively. Raising the status of contract management as part of most public servants' jobs might be something that is recognised as an important skillset even if they do not do it full time, and then there are resources available for them to go to. That basic induction training and ongoing training around what is good public sector governance and what does good public sector administration look like, I think, is important.

The CHAIR: There was a case that came up with the commonwealth recently involving the security around Parliament House. That looked like it was a case of lack of really effective due diligence about the contractors. Is it a question of having more detailed diligence in that sort of situation? It seems to me people do a company search and maybe a google search and that is about it.

[10.50 am]

Ms Spencer: I think it is complex. People are trained in this and might be performing a job very well and then they move on, or roles change, and new people need to be trained. I guess this is a concern in fiscally constrained times where there are promises not to cut frontline services. It can be very challenging then for agencies to fill the gap in that middle around important governance roles, because you can essentially thin them or even do without them for a period.

Hon ALISON XAMON: But it is a false economy.

The CHAIR: That is what I was going ask. Are there any studies in terms of money saved through effective risk management? I mean, for example, in money laundering they can say it is estimated to be X per cent of GDP. But is there any work that you are aware of or you have attended any conferences where there have been any papers on the cost of not doing the good risk management and good corruption focus?

Ms Spencer: I cannot think of a straightforward economic model or statistic that comes to mind in that, but my experience is this often is not sexy stuff. You try to talk to people in your communities, I am sure, around the nuts and bolts of government and good lawmaking and the considerations in public policy and their eyes glaze over; they have one particular issue that they are interested in—same with good governance. We were speaking to a director general the other week, who was speaking to her ministers and saying, “Well, the reason I’m revising my audit committee and governance arrangements is because this will help us to pick up and control weaknesses that contribute to this.” When the ministers then have that, I guess, personal sort of recent awareness of risks to both public service delivery and reputation, then they are little more mindful of it. But everyone is subject to “recency” bias and we need constant reminders; we are human.

The CHAIR: Can you speak a bit about management of supplier master files—it is jargon-esque. I do not know whether you can talk to us about that.

Hon ALISON XAMON: Speaking of sexy topics!

Ms Spencer: Yes. This was a focus area audit done by our financial auditors as an addition, so beyond their financial audit work. Supplier master files are the vendor file that sits in the accounts payable system that contains all the details of the vendor or the supplier, so everything from the name of the vendor, the address, all important bank account details, ABN. It is the unique identifier within an agency’s system. What happens over time is, as agencies purchase from a number of suppliers, every time there is a new contract or purchase order, a supplier master file will be created. Over time, certain suppliers may change their details and a duplicate file might be put in, rather than a deletion or amendment of the original one, or that supplier no longer provides services and others do. These are important in control monitoring for a fairly basic, you know, critically basic financial management process. Any good CFO, finance manager or officer will understand the importance of keeping those details clean, but it is a job that often gets neglected. This audit found that often agencies did not have adequate policies and procedures around what should be done with supplier master files and their monitoring and reviewing to say, “Yes, there were duplicates. Yes, there were areas in that process” and the role of those files that can then subject the agency to either payment error or potential fraud, where they do not have a tight process that picks up an invoice issued either by a staff member who might be aware of a control weakness or external supplier who can commit a fraudulent act.

Mr M. HUGHES: Was there anything in particular that promoted that?

Ms Spencer: We call them hygiene audits. There are just basic financial management processes that we look at every few years. It is a great way of using our financial auditors after they finish their peak delivery for statutory reporting time frames. They go in and look at some common financial management processes.

Mr M. HUGHES: You had 10 entities selected. Why did you select those 10?

Ms Spencer: Those 10—part of it is to give additional coverage across entities that we look at in a bit more detail. We are in every state sector entity and will be in every local government entity every year for financial audit, but not every entity gets selected for performance audit, and obviously we look in a bit more depth or a bit wider in these audits in a number of agencies. Typically, it will not be that there are particular concerns. For the majority of our cross-agency audits it is not that there are particular high risks that we have identified in those entities, it is that we want to get a representative sample of a number of large entities, small entities, regional, metro—that sort of thing—or ones that we have not touched for a while just to remind them that we are there and we can come and look at anything at any time. We just keep people a bit vigilant and honest. Then also if we do see that there are particular concerns in an entity that we pick up during any other process

or information that we gather, we might include them in a cross-entity audit in that way to look at them in a bit more depth.

The CHAIR: I want to move on to a couple of things—that is, gifts. I can understand if there is some person coming from overseas that the culture might be different, but I really have to question whether we should just ban gifts altogether. In particular, whether if we trained tenderers better, this whole area of gifts can just be eliminated. Do you have any thoughts on that?

Ms Spencer: I guess there are certain classes of gifts that raise more concern than others—you know, invitations to high-profile or highly attractive events that are not related at all to the business of the entity or the provider. You have to question why those are being provided. I know in my office, and we probably have a hyper-vigilant reporting of gifts given the nature of our work and our awareness and having to be beyond reproach, we often get invited to our contract audit firms—big and second-tier firms—for technical updates. It is a morning or an hour for a presentation on accounting standards updates. We do those internally for staff, our technical team provides those to staff, but we often attend other firms to see whether they are looking at the issues in a different way. It is a really cost effective way to do that. Rather than engaging them to peer review our training or our technical materials, we can just go and get a quick overview of that.

Hon ALISON XAMON: What are you declaring there—the biscuits?

Ms Spencer: If a training hour of \$80, or whatever, if it is based on a \$700 average cost of a training day for professional training or conferences at that level. Look, that is why I say it is hyper-vigilant. We are invited to professional body dinners, which might be CPA or CA ANZ or the Institute of Public Administration—and we are invited to the Lonnie awards, because we are presenting an award.

Hon ALISON XAMON: Those things are tedious. We have to do them all the time.

Ms Spencer: They are. We want to say that we were invited and we declined for this reason or we accepted for this reason, there is no other potential benefit and how often do we get these things. I would say that banning entirely may not actually result in the most appropriate or efficient interaction or use of public resources and knowledge gathering and things. But it really is case by case and every public sector employee needs to be informed of and trained in a cultural awareness way around public sector values, code of conduct and that absolute vigilance around what is your public duty and are you allowing your private interest to conflict with that. I think that is a principles-based approach so people can exercise good judgement within a framework, rather than a rules-based approach to rule things entirely in or out. When we make those rules, we just cannot foresee every potential circumstance. I think it is a more appropriate way to manage that.

The CHAIR: In New South Wales I think the public transport people did a training session for tenderers—do not even think about doing this and all of that. That seems to be underdeveloped here.

[11.00 am]

Ms Spencer: I think those mechanisms where there is just the expectation amongst tenderers that they know when they deal with the public sector, there are certain things that are not appropriate. I know that in the commonwealth, when a tender is submitted, the tenderer must make a declaration to say that they have not contacted inappropriately officers of that entity to —

Hon ALISON XAMON: Taking them out to lunch.

Ms Spencer: Exactly. So there is that heightened awareness at all stages, both internally and with the private sector that provides services.

The CHAIR: That would be a good question on notice for you to ask, Jim, of all the ministers—how many members of your agency were guests in a box at the derby? I mean that quite seriously.

Hon ALISON XAMON: That is, of course, now recorded on our public hearing!

The CHAIR: Oh, sorry! I am just jealous, that is all!

Hon ALISON XAMON: In relation to the agency gift register, did that audit pick up any red flags, and were there any referrals to the CCC or the Public Sector Commission?

Ms Spencer: This was an audit before my time by my predecessor, Mr Murphy. I might hand over to Jason on that one, but I know that when I reviewed that report—this is based on recollection—that there is always improvement required in this area, constant training and awareness.

Hon ALISON XAMON: Of course. Were there any referrals to the CCC or the PSC?

Mr Beeley: I think we would have to take that on notice, Chair.

Hon ALISON XAMON: Yes, please. Apart from just the general comments, were there any specific red flags raised during the course of that investigation?

Ms Spencer: We will have to take that on notice.

Hon ALISON XAMON: Okay.

Mr M. HUGHES: In terms of the question about the master files, did you pick up any red flags there?

Ms Spencer: It is a useful way to think. In that particular audit there were some payments made through the accounts payable system to employees, which is always a red flag. When the team investigated those further, they were actually not terribly significant. In a regional council, Margaret River—Augusta regional council, it was to employees who provided after-school care who, I believe, moved from an employment relationship to a supplier relationship in out-of-hours school care or community fitness-type services. It is in the report that there was a more significant one where a board member—this was, I believe, in DPC procurement—did not fully declare an interest and we raised that with them, but I do not believe, when the team looked at the nature of that, it raised any significant concerns; it was more a matter of process and documentation to consider these, but interviews as well as documentation did not reveal anything that would indicate that it needed to be referred onwards.

Mr M. HUGHES: Thanks.

The CHAIR: You have found in various inquiries that sometimes common-use arrangements are ignored and contracts are made with another supplier. What is the rationale given for not using the common-use arrangements?

Ms Spencer: Often better specification, better meeting needs or better value for money.

The CHAIR: Right. In terms of the Buy Local policy, that creates another layer of complexity. Do you have any thoughts on that?

Ms Spencer: It does. The office did an audit into that. Was that in your area, Jason? Would you like to talk to that one? The other one now is Aboriginal procurement, but that we think of in a similar vein in terms of contracting.

Mr Beeley: For the Buy Local policy, yes, it layered in some additional complexity. My fundamental issue with it was that it really was not working in terms of delivering objectives; it was a precursor of multiple sets of trade regulations and those kinds of things, and the way it had been implemented meant that it was not generally enabling local companies to level the playing field. There were lots of avenues for non-local companies. The definitions of “local” were big, for instance; in regional areas they come from 400 kays away, which could be big. But also avenues to do things, like if you have a registered office in WA and that tends to count as local, even if they are not local. Also, because of some other trade agreements between states, in certain circumstances if a company chose to tender from an interstate office, that would immediately eliminate any consideration of

local content. It could not apply, so local companies, again, it does not give them any advantage in that procurement. I think our issue is, yes, it added complexity, but fundamentally what it did was not really deliver for local companies; it did not deliver the outcomes they were supposed to deliver.

The CHAIR: My impression, though, is that it could be used as a bit of a prop, especially by local government regionally—basically, giving their mates a hand up.

Mr Beeley: Going back a lot further, when we looked at Housing's implementation of its head contractor maintenance model, the implementation did not go awfully well and it got pretty messy, but one of the motivations I think behind that centralisation and then subcontracting out was to break some of that regional control over local procurement, and that that procurement was possibly a bit too local in some areas.

Ms Spencer: It is an interesting point. I think we will get to understand that issue more as our local government audit mandate continues. Jason and I were up in the Kimberley at a north west region local government conference and we toured some state and local government infrastructure in June last year. We had a shire president recounting an example of, I think, a seawall procurement in royalties for regions, saying that it was an interesting experience going through the procurement of that. There was tension in the advice from the administrators to council within the office saying we have to go through certain procurement procedures and do a common-use arrangement and the stone has to come from some thousands of kilometres away, rather than the local quarry, which was a bit more expensive because they have machinery that will cut it a bit wider or differently. In those cases, I think there may be, through proper consideration and careful diligence, the best value for money outcome for that particular procurement, both in terms of the council's expenditure but also the value to the community, maybe pay a bit more and having that very local content and the community can see that value. I am not saying that is the case in all situations, and it needs to be properly considered and documented as to the cost and the benefit of the relative suppliers, but I think sometimes there is a conflict of interest, not just around financial gain but it can be taking the path of least resistance, the easiest path, by going through a common-use arrangement that you know and everyone in your community knows and everyone around the table knows may not give the best outcome for the community, but it is less complex because you can just justify ticking it off and taking it off the panel, if you like. So I think this is where we need to work in a framework of principles around value for money and best outcomes for a community where we have some good practices and rules where necessary, but we are not so bound by those rules where it clearly makes sense to do something else. As I say, not endorsing a particular procurement in a particular part of the state without looking into it in detail, but there may be instances where going outside a common-use arrangement or a particular procurement process is actually the best value for money and in the best interests of the community.

Mr Beeley: I think that links back to your earlier point about expertise in procurement and the understanding about what procurement can legitimately do and how it can be legitimately done versus a very defensive or lowest-common-denominator approach or risk-averse approach, if you like, of just following the rules, almost regardless of what outcome comes out.

Ms Spencer: I have noticed in public sector across jurisdictions that there is this rules-versus-principles approach and it is safer often to follow the rules and not think, but this comes back to the audit that we presented to Parliament yesterday on record keeping in local government. If it is appropriately documented and those deliberations and decision-making can be appropriately evidenced and available for review and you are accountable to the community and any external reviewer who comes by to examine it around the basis of decision-making and why it was in the best interests and why it was appropriate in the circumstances and provided value for money, then

officers should be empowered and encouraged to do that, but they do need the appropriate training around why they are there and the tools available to them to do the best job they can.

[11.10 am]

The CHAIR: You have mentioned the extension of the contract. I believe that is an area of particular vulnerability. The other one that we seem to be coming up with a bit is leaving negotiations or executional contracts so late that you have to do it outside the process. Do you have any thoughts on those two?

Ms Spencer: It is often given as an excuse for proceeding in that manner. I think it comes back to not only what we were talking about—training and awareness and support and capability development in staff—but also that senior executive oversight around the practices that are going on in agencies about the proper scheduling and forecasting and managing risks so that best value for money is obtained. Senior executives within the organisation that are on a project board or looking at project or contract governance, there are all these last-minute extensions, and they must be asking these questions: Why? Is this good enough? Is it appropriate in the circumstances? Are we delivering best value for the taxpayer? Again, these things are not simple, and isolated examples on their own may not be bad, but that pattern of perhaps complacency or just of prioritisation and poor practice is a concern at a systemic level.

The CHAIR: With IT, I do not know whether people get blinded by science, the contract managers, but that seems to be something that over the years your office has certainly focused on. Is there any jurisdiction that does the IT procurement well that you are aware of?

Mr Beeley: I think we would probably have to take that on notice.

The CHAIR: If you would not mind because I think that is a particular area where people just go, “If you need this”, you know.

Hon ALISON XAMON: because who on earth understands it.

Ms Spencer: It is an ongoing challenge, I believe, across all sectors and jurisdictions here and overseas, and there are some good examples that might come up for a time in some jurisdictions or in some sectors. Something that has changed, I think, in the last while amongst executives in private and public sector and boards is that IT-side risk, and cybersecurity risk in particular, is a key business risk for all people charged with governance in any entity. I think that we are seeing initiatives to increase the cyber literacy of executives so that they can ask the right questions. We need to develop skills in the sector around cyber capability and security so that we have good people in agencies doing this. Contract management of information systems and outsourced systems is a concern. No doubt, it can be strengthened.

Mr Beeley: I think there is a crossover with some of the capital works work that we have done as well. Some of what happens, the poor performance in acquisition and procurements have some poor asset planning and I think to some extent in the IT space and the IS space, increasingly, I am not sure that people have yet got their heads around it. As an asset, it needs to be managed, reviewed and maintained, and cycles and processes and approaches for that is not dissimilar to what we would use for a building firm for other kinds of assets but because it is an IT system, they think it is different somehow so they do not necessarily apply some of those principles.

The CHAIR: There was a report in 2013, “Fraud Prevention and Detection in the Public Sector”. Is there any evidence that you found that those recommendations are being taken seriously or the recommendations are being acted upon? Have you any perceptions that agencies are lifting their game in terms of prevention and detection?

Ms Spencer: Without going and doing another performance audit across agencies that provide a bit of a representative sample, I do not think I could comment on that, Chair. At this stage, we are currently doing an audit of fraud prevention and control in local government, so that will give us an insight into the local government in coming months. But like all these things, recent CCC reports that raise the profile and make people aware that the risks are real and when they see some parallels with their own organisation perhaps, they start to pay attention to these things. This is an ongoing thing. We do not want the director general of Health or the director general of Education to stop focusing on patient care and quality or educational quality for students, but they need to be able to walk and chew gum at the same time around managing those corporate side risks as well. Matters like that raise awareness and make sure that there is some focus on these in a bit of a structured way.

Mr M. HUGHES: One is the resource. If there are practices and procedures that are not ensuring good value for money, that is a cost to the state.

Ms Spencer: Absolutely. It is a cost to communities. I think we see it more directly in local government with rates coming in and then the services that are provided and the direct impact on rates each year, but in the state, obviously, that is the same: can we be doing more, providing better quality services with the same or even a reduced tax burden? Those are important questions, particularly in fiscally constrained times.

The CHAIR: Thanks very much for your time. That was really valuable. Before I send you on your way with my closing instructions, I am sure the research officers would certainly like to incorporate that in the foreword. I think that is very useful.

Ms Spencer: I am happy for the office to provide a little more context around those speaking notes that we have.

The CHAIR: Thank you very much. It will also be made public, if that is not an issue. You will also give us some advice on the jurisdictions that seem to handle IT well.

Mr Beeley: IT procurement, and the other one I have is getting back to you with the authority management.

The CHAIR: Thanks for your evidence before the committee today. A transcript of this hearing will be forwarded to you for correction of minor errors. Any such corrections must be made and the transcript returned within 10 days from the date of the letter attached to the transcript. If the transcript is not returned within this period, it will be deemed to be correct. New material cannot be added via these corrections and the sense of your evidence cannot be altered. Should you wish to provide additional information or elaborate on particular points, please include a supplementary submission for the committee's consideration when you return your corrected transcript of evidence. Thanks for your time.

Good luck with your operation. We do not want to see a spineless Auditor General, so good luck and I hope it goes well.

Hearing concluded at 11.18 am
