PUBLIC ACCOUNTS COMMITTEE

OFFSHORE AND OFF-TARGET

Why NSW lags the field in overseas projects

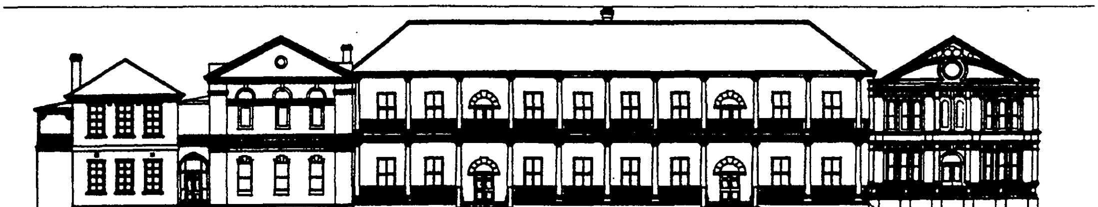

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Figure 1

Revenue from Overseas Projects ($m)

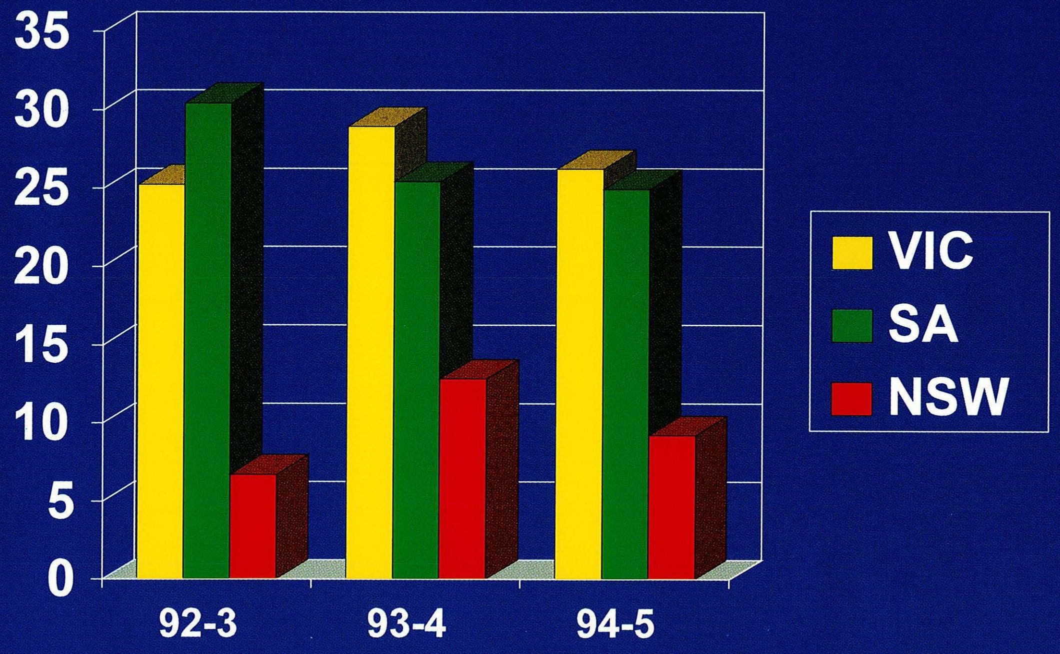

Figure 2

Profits/Losses from Overseas Projects ($m)

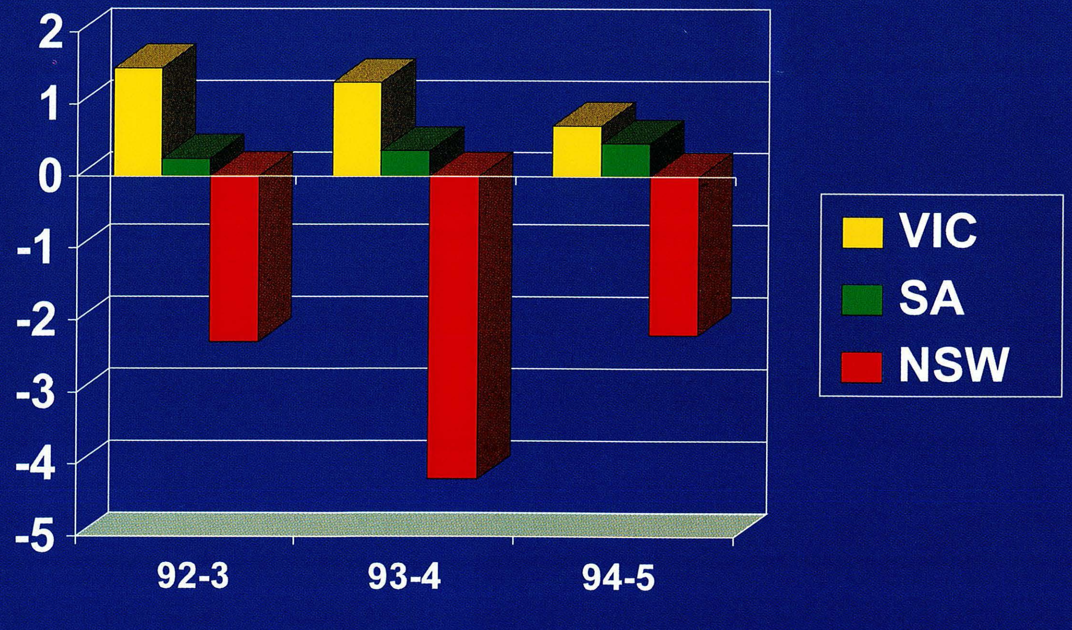

TABLE OF CONTENTS

The Public Accounts Committee
From left seated: Pat Rogan (Vice-Chairman), Terry Rumble (Chairman)
standing: Peter Cochran, Ian Glachan and Joe Tripodi

MEMBERS OF THE PUBLIC ACCOUNTS COMMITTEE

Mr Terry Rumble, FCPA, MP, Chairman
Terry Rumble was elected Labor Member for Illawarra in March 1988. Before entering Parliament he qualified as an accountant and was employed in public practice and in the coal mining industry. He has served as a member of the Regulation Review Committee and is the Chairman of the Premier's Backbench Committee which involves Treasury, arts and ethnic affairs. Mr Rumble was elected Chairman of the Committee on 24 May 1995.

Mr Pat Rogan, MP, Vice-Chairman
Pat Rogan has been member for East Hills since 1973. He has been active on numerous parliamentary committees in that time including the Joint Committee upon Public Accounts and Financial Accounts of Statutory Authorities. This was the Committee that reactivated a dormant Public Accounts Committee in 1983. Pat Rogan has also served as Shadow Minister for Minerals and Energy with a background as a senior sales engineer in automation.

Mr Joe Tripodi B.Ec (Hons), MP
Joe Tripodi was elected to Parliament in March, 1995 as the Labor Member for Fairfield. Before entering Parliament he worked as an economist with the Reserve Bank of Australia and as a union official with the Labor Council of NSW.

Mr Ian Glachan, MP
The Liberal Member for Albury since 1988, Ian Glachan has had a varied background. He served five years at sea as a marine engineer, was a farmer for ten years, and operated a newsagency in Albury for 18 years. Mr Glachan is also a past president of the Albury-Hume Rotary Club and a Paul Harris Fellow, an active member of the Anglican Church, and was the Legislative Assembly member on the Board of Governors of Charles Sturt University. He was Chairman of the Public Accounts Committee in late 1994 and early 1995.

Mr Peter Cochran, MP
Following a background in farming, the Army, the Commonwealth Police, ASIO, and the Cooma-Monaro Shire Council, Peter Cochran won the seat of Monaro for the National Party in 1988. His previous parliamentary responsibilities have included the chairmanship of the Minister's Advisory Committee on Land and Water Conservation, deputy chairmanship of the Committee for Police and Emergency Services, and membership of the committee for the Environment and the Select Committee on Public Sector Superannuation. He was also the Premier's representative on the Anzac House Trust and the Anzac Memorial Trust. He is currently Secretary to Shadow Cabinet.

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CHAIRMAN'S FOREWORD

The concern that NSW may have been seriously outperformed by other states in the export of government services has been shared by all leading political parties in this state. All parties in NSW have suspected that other major states may have been earning more revenue, profits, foreign exchange, and returns on taxpayers' investment in public sector skills from overseas projects than has NSW; that other states may have been creating more jobs; incurring fewer risks; burdening their taxpayers less; providing a bigger boost to their private sectors, and, in general, managing the export of their services more economically, efficiently and effectively.

All parties have sought to learn whether NSW has fallen behind and if so, how far, and why, despite the undoubted technical excellence of NSW specialised agencies.

This report is in response to a reference from the Treasurer, obtained soon after the change of government in March 1995. This reference enlarged on similar terms of reference given by the previous government in October 1994. In both cases, the Committee was asked to examine the performance of NSW government bodies in the export of their services and make recommendations for future improvements.
The Committee's report is unanimous and takes its place in our long history of bipartisanship.

The Committee's work on this project has been thorough. Every one of the 21 NSW agencies presently trying to export their skills was interviewed, some at considerable length; the Overseas Projects Corporation of Victoria and SAGRIC were visited several times by members and staff, and interviewed when on visits to Sydney; interviews were also held with Western Australian and Queensland authorities, with some of them several times; Commonwealth government authorities, both past and present, were also interviewed; two sets of detailed questionnaires were sent out to NSW agencies involved in this field; two Round Tables were held at Parliament House, with scores of participants from the public and private sectors; extensive interviews were also carried out with numerous Australian and overseas aid authorities; formal hearings were held with ten sets of witnesses from the private and public sectors. In all, members of the Committee and its staff have spoken with hundreds of individuals and organisations. This is the first time such thorough work has been carried out on this subject, and the Committee feels confident that its conclusions are supported by an overwhelming weight of evidence.

In addition, the Committee has greatly benefited from the expert assistance provided by Mr Kevin Fennell PSM, recently retired Deputy Auditor-General of NSW. Mr Fennell personally visited most agencies exporting their services, examined their financial statements and compiled the NSW statistics set out in this report. The Committee greatly appreciates his contribution.

The Committee has also benefited considerably from the advice of Mr Robert Hogarth, Economic and Business Development Consultant, who brought his twenty-two years' experience of this field, and an imaginative approach, to this inquiry. Mr Hogarth also materially contributed to Part II of the report.

Dr Mike Lisle-Williams, D.Phil., Partner, Deloittes Touche Tohmatsu, Canberra, who prepared for the Victorian Government a fine and detailed report on the Overseas Projects Corporation of Victoria (issued in June 1995), provided a pivotal input to this inquiry. Dr Lisle-Williams' report influenced the Committee very considerably, partly because it was not commissioned by the OPCV and provided an objective view of the operations of that agency, and partly because it was begun in a spirit of scepticism.

The Committee thanks all those who co-operated with it during the course of the inquiry. We acknowledge that our main conclusion, that NSW now needs an International Projects Corporation (IPC), run by experienced professionals on business lines, may not be a popular one with individual agencies currently exporting their services. However, in this report, as in all Public Accounts Committee reports, we have sought to keep in view the interests of the State as a whole rather than those of individual agencies.

After considerable debate and reflection, the Committee has come to the unanimous view that the interests of the State as a whole are not being well served by the current fragmented arrangements, and that the most economic, efficient and effective way to achieve better co-ordination — and financial and economic results — is through a stand-alone, but accountable, business run professionally and facing bottom line pressures rather than through the creation of another bureaucratic entity.

The Committee believes that all business decisions on overseas projects should be left to the corporation, while the technical agencies should be free to concentrate on their core business and their specialised expertise. Here the Committee envisages a partnership where the agencies contribute their technical excellence and the IPC its commercial acumen.

The Committee considers that the problems with the present situation are more those of structure than of individual failings. The constraints of the system, rather than the shortcomings of individuals, are responsible for the overall level of performance shown by NSW agencies.

We stress in this report that export of government services is not the core business of state agencies. Indeed, it is precisely because it is not their core business that some agencies have been dabbling in it in such an inexpert way.

However, all Australian states, as well as the Commonwealth, do export their services and have done so for years. Many overseas governments are doing so too. The market is vast (if highly competitive) and the benefits to a State's economy are many - substantial revenue, jobs in both public and private sectors, competitive sharpening of NSW skills, foreign exchange, and a range of others set out in this report. It is pointless to try to pretend that export of services is not happening, or to try to turn back the clock and prevent agencies from doing it at all. The challenge is to do it properly and earn better benefits for NSW.

The Committee believes it is time to take the commercial and management side of exporting NSW government services into a new era of professionalism and business incentives, away from the government departments whose business it is not, to a dedicated, professional organisation whose business it is.

This is why the central, bipartisan, recommendation of this report is the establishment of the NSW International Projects Corporation.

The Committee notes that the establishment of this corporation is current Government policy, as expressed in a number of public policy statements. We have made a number of recommendations aimed at clarifying the role, structure and legal status of the future Corporation so as to assist the Government in setting it up.

I would like to thank my fellow members, Pat Rogan, Peter Cochran, Ian Glachan, and Joe Tripodi, for their unfailingly bipartisan spirit, commitment to this inquiry and hard work.

The report was researched and written by the Committee's Director, Patricia Azarias, and our thanks go to her for her dedication and critical spirit.

Jozef Imrich assisted with data collection and logistical matters, and Caterina Sciara prepared the draft for publication. Assistance was also received from Vicki Mullen of the Parliament's Library, and from Sharon Quant of the Parliament's Information Technology Services. Mr J. Rooney of Tress, Cocks and Maddox, and James Phillips and Denis Rouast of Minter Ellison provided legal advice. To all of them our sincere thanks.

Terry Rumble

Terry Rumble
Chairman

MAIN FINDINGS AND RECOMMENDATIONS

During the period June 1992 to June 1995, NSW agencies actively working in the overseas project market earned revenues of $28.7m, incurred costs of $37.3m, and accumulated an overall loss of $8.7m to the state from their overseas activities. This compares unfavourably with Victoria, which had revenues of $80.3m, costs of $76.8m and profits of $3.5m from overseas projects during the same period, and with South Australia, with revenues of $80.7m, costs of $79.6m and profits of $1.1m.

In Victoria and South Australia, overseas operations are managed by experienced professionals working in one fully commercial corporation, facing constant bottom-line pressures, adopting a market-driven business approach, benefiting from economies of scale and limiting risk professionally.

In contrast, management of NSW agencies' overseas operations has, with some exceptions, frequently suffered from fragmentation, duplication, lack of commercial pressures, consequent amateurism, and the absence of economies of scale. The general approach, again with some exceptions, has been bureaucratic and supply-driven rather than market-driven, seeking to create markets for the existing supply of expertise rather than trying to meet existing demand. Government agencies have seldom sought to inform themselves of what constitutes best practice in this market. This comparative lack of professionalism has incurred greater risk to the State than has been the case in Victoria and South Australia.

The main reason for NSW's comparatively poor performance is that in NSW, each agency attempts to attack the overseas market alone, whereas Victoria and South Australia have both established a single dedicated and focused body to market expertise and manage all agencies' overseas projects commercially. Thus the failure can be attributed more to systemic and structural factors than to individual shortcomings. .

Despite this, most NSW agencies judge themselves to be doing a good job in this market and wish to continue their current operations.

The benefits for NSW from entering the overseas project market in a professional way could be many. They include tens of millions of dollars more revenue to the state; considerable benefits to the private sector co-operating with the state overseas; thousands of new jobs and maintenance of existing jobs; enhancement of public sector skills; improvement in productivity in NSW; foreign exchange; downstream procurement opportunities, profits and, potentially, dividends and tax equivalents to Consolidated Revenue.

The potential for NSW in the overseas projects market is considerable. At present, the effective demand overseas for services traditionally provided by state governments is escalating sharply, particularly in Asia; and the NSW public sector is bigger than that of any other state, and has a high level of taxpayer-funded skills.

To introduce commercial pressures, professionalism and economies of scale into this market, and to reduce the risk to the State, the Committee recommends that the NSW Government set up as soon as possible an International Projects Corporation of NSW as a State-Owned Corporation TOTALLY INDEPENDENT OF THE PUBLIC SERVICE to market and manage all of NSW agencies' overseas projects, and to remove these operations from agencies whose core business it is not, to a corporation whose core business it will be. The Committee thus envisages a partnership between the technical agencies, which will contribute their technical knowhow, and the IPC, which contribute its commercial expertise to overseas operations in a demonstration of the proper use of comparative advantage..

RECOMMENDATIONS ON THE IPC

The Committee recommends that the IPC have the following chacteristics:

1. *It should be a state-owned corporation, totally independent of the public service.*
   The five shareholders of the Corporation could possibly include the Minister of Urban Affairs, Planning and Housing, the Minister for Education, the Minister for Health, the Minister for Land and Water Conservation, and the Treasurer
2. *It should have a small board (ideally about five).*
3. *The chairperson of the board should have commercial experience overseas but should not be actively involved in any competitor of the IPC, nor should any other member of the Board.*
4. *The IPC staff proper should number about 11. Senior management should not be public servants but should be on contracts of three years. Some staff should be seconded to the IPC from technical agencies, but this should be up to the Managing Director.*
5. *The corporation should receive an initial capital injection from Consolidated Revenue of $2m to $2½m.*
6. *For the first three years, the corporation should not concentrate primarily on profits but on establishing a presence in the marketplace and on setting a track record. Thereafter, it should make profits its primary objective.*
7. *Initially, the Corporation should concentrate on the aid market especially AusAID.*
8. *All agencies should work through the Corporation. The Corporation will provide the business, and the agencies the technical, judgement on the advisability of a project opportunity. Agencies wishing provide their own commercial, as opposed to technical operations, should have the right to request the IPC's managing director for authorisation; the managing director should respond with the interests of the state as a whole in mind. If refused, agencies should have the right to appeal to the IPC's Board.*
9. *Within one year, the IPC should initiate co-operation with other state agencies with the aim of setting up a national association of state agencies involved in promoting overseas projects.*
10. *The corporation should concentrate on selected sectors: housing and other infrastructure, water and other environmental services, education, health, and lands, and should focus on Asia.*

EXECUTIVE SUMMARY

During the period June 1992 to June 1995, NSW was outperformed in overseas project activity by other major Australian states. It earned $28.7m revenue and made an $8.7m loss, while Victoria earned $80.3m revenue and made $3.5m profit and South Australia earned $80.7m revenue, with $1.05m profit over the same period.

This comparative failure has occurred despite the undoubted technical excellence of many of the NSW specialised agencies. The main reason is structural: each of the 21 agencies involved in overseas projects has sought to enter the field, "learn the ropes" and operate on its own, with consequent duplication and inefficiencies, whereas both Victoria and South Australia have established dedicated, professional, commercial government corporations whose sole business is to operate overseas projects.

Why try to export government services at all?

All other Australian states, as well as the Commonwealth, are seeking to enter the international projects market. There are many reasons for doing so:

- revenue (because international demand for government services is strong);
- profits;
- jobs;
- earning a return on taxpayers' investment in public sector skills;
- sharpening NSW skills in competition with world best practice;
- boost to the private sector;
- improvement in productivity in the state concerned;
- foreign exchange;
- downstream procurement opportunities;
- prestige and goodwill;
- internationalising of the State's economy; and
- dividends and tax equivalents paid to the State's Consolidated Revenue.

Not core business of agencies

It has been argued that it is not the core business of agencies to become involved in overseas projects. The Committee agrees with this position. However, the financial and economic benefits to be gained from the international projects market make it more useful to manage the process properly than to pretend it is not happening or to try to turn back the clock and prevent it from happening at all. Clearly the process is not being managed properly at present: agencies are branching out into areas they were never set up to do, some of them with no commercial discipline, and have been learning on the job.

The question of risk

When properly managed, exporting of government services has in the past proved to be in general a low-risk business. No Australian government body exporting its services has ever been sued for poor performance overseas. There are several reasons: clients are large governmental or international institutions which normally pay in full; most projects are won after rigorous competitive bidding; many insurance mechanisms are available. However, all business entails risks. In NSW, the risks should be limited as far as possible by good management and appropriate legal structures.

The size of the world market

The market is large. The demand comes from development banks, grant assistance agencies, both multilateral and bilateral, commercial development financiers and the capital of global corporations. Currently the international demand for services typically provided by State agencies (such as water, health, educational and environmental services) is escalating sharply. The World Bank is the biggest single source of demand, spending over $20 billion a year on goods and services; the Asian Development Bank is next, with about $5 billion; the UN system next, with about $3.5 billion; AusAID spends about $1 billion. A major relatively untapped source of finance is Japanese untied aid, which amounts to about $1.2 billion a year. The amount spent for services alone is about $10 billion annually. Australia does not get its proportionate share of these global expenditures, and NSW does not get its proportionate share of AusAID finance.

How other Australian States have approached the world market

Other Australian States have adopted different models for meeting this demand. In 1985, Victoria established the successful Overseas Projects Corporation of Victoria (OPCV) , which carries out the marketing, and project bidding, negotiation and management for VPS technical agencies. OPCV has made a profit every year since 1986. In the early 1970s, South Australia established SAGRIC, a similar organisation, which has set up a number of subsidiaries to commercialise SA technology. SAGRIC has also been consistently profitable. The smaller states have adopted different strategies: Queensland has set up a unit in the Premier's Department, a logical development given the small size of its overseas activities; Western Australia is currently negotiating an agreement with a large private sector organisation to market its expertise abroad, again a logical development given its size.

How NSW has approached the world market

NSW has approached the market in a haphazard and piecemeal fashion. Each agency has begun operations abroad on its own. Some have set up autonomous businesses for the purpose, some have not. There have been virtually no economies of scale but instead considerable duplication and inefficiencies. There has been little co-ordination: large multidisciplinary projects have had to go by the board. There are currently 21 agencies seeking overseas work. Significant dollar amounts are involved for 16 of these. 8 have made a profit, 8 a loss. The largest profit ($2.7m over the 1992-1995 period), has been made by the RTA, which did not actively engage in any overseas marketing on its own. The next largest was made by TAFE ($802,000). Asian interest in English training is particularly high, and competitors are fewer than in engineering, health or other disciplines. The largest loss was made by Prospect Electricity ($3.9m) and by the TAB ($3.4m).

The overall figures, despite good performances by some agencies, notably TAFE, do not match those of Victoria or South Australia.

Taxpayers have carried nearly all of these losses, although they were probably unaware of their extent. Partly this lack of awareness was due to the absence of accounting standards or Treasury requirements which would compel separate reporting of overseas expenditures and revenues. Partly it was due to the fact that some agencies did not bring their losses out in their Annual Reports.

The reasons for the losses were several. First, agencies in NSW began their overseas operations later than their counterparts in Victoria and South Australia. Second, there has been a comparative lack of professionalism in many agencies in NSW. This want of professionalism has stemmed from the lack of bottom line pressures, the absence of economies of scale, and the adoption of a supply-driven, rather than a market-driven approach. Mistakes made include the reaching of break even point many years after starting operations; the entering of markets without studying them in depth first; the employment of staff even after their programmes have failed; the running up of significant foreign currency losses; the undertaking of travel and promotional expenditure without any positive outcome; the failure to appoint independent directors, and the failure to evaluate competitors properly.

The preferred future approach to the world market for NSW: the International Projects Corporation of NSW (IPC)

The Committee believes it is time to look beyond these failures into a new era of professionalism and commercial acumen. This will involve structural change. Various options for this structural change were evaluated: through the public service, through a licensed private sector corporation, and through a government corporation. The public service solution, involving the creation of a central public service unit to "co-ordinate" agencies' overseas activities, was rejected because the problem was originally caused by a non-commercial public sector approach. The private sector solution was also rejected for a number of reasons, the main one being that of potential conflict of interest. The Committee settled on the government corporation as being unequivocally the best option for the marketing and managing of NSW government agencies' expertise. This International Projects Corporation (similar to the OPCV, which has a proven record of success) has already been foreshadowed in government policy statements, and the Committee expresses bipartisan support for it.

The Committee recommends:

- that the IPC be a State-Owned Corporation, to combine freedom with accountability;

- that it provide the full range of services (marketing; collection and centralising intelligence on projects, funding sources, countries, regions, administrative practices); preparing bids; putting consortia together; negotiating of insurance; foreign currency management; recruitment of subcontractors, both individuals and firms; total project management, including scheduling, and relations with governments;

- that it operate with the minimum of staff consistent with efficiency, with senior management on contract, a small board, and the CEO not being a member of the board;

- that it receive equity seed money as a grant from government to cover the initial equity required (between \$2m and \$2½m, which should be repaid as dividends), but that running costs be met from revenue after three years;

- that in order to derive the full and appropriate benefit from the IPC's commercial expertise, there be no exemption from working through the IPC for any agencies operating any overseas activities unless, after negotiations, the

Chief Executive of the IPC grants an exemption on the grounds that it would be in the best interests of the State as a whole to do so; and that appeal may be made to the Board;

- that the IPC link up with private sector bodies on a case-by-case basis;
- that profits be distributed between the IPC and an agency according to negotiated and agreed formulas, set at the appropriate level for each project;
- that the IPC should initially concentrate on revenue maximisation, moving after about three years to profit maximisation;
- that it concentrate on AusAID and Asia initially, without prejudice to other sources;
- that it concentrate on five sectors: infrastructure (including urban affairs), environment (including water); education; health, and lands;
- that it work towards the establishment of a national body of state corporations involved in overseas work, and of an overseas post in that context.

The Committee stresses that it envisages a partnership arrangement between specialised agencies and the IPC, with the agencies contributing their undoubted technical excellence, and the IPC its commercial acumen. Projects should be undertaken jointly. The IPC should not be viewed as an unwelcome "another layer" but rather as an essential provider of commercial experience and expertise. There is no doubt that this is what is needed now in NSW.

ABBREVIATIONS

ABS	*Australian Bureau of Statistics*
ADB	*Asian Development Bank*
AUSAID	*Australia's official aid programme*
AUSTRADE	*Australia's official trade promotion body*
CIS	*Commonwealth of Independent States (the former Soviet Union)*
DIFF	*Development Input Finance Facility*
EBRD	*European Bank for Reconstruction and Development*
EFIC	*the Export Finance and Insurance Corporation of the Australian Government*
ESCAP	*the Economic and Social Commission for Asia and the Pacific of the UN*
FAO	*the Food and Agriculture Organisation of the UN*
FTE	*FullTime Equivalent*
IAPSU	*Inter Agency Procurement Services Unit*
IBRD	*International Bank for Reconstruction and Development (the World Bank)*
IDA	*International Development Association (linked to World Bank)*
IFC	*International Finance Corporation (linked to World Bank)*
IPC	*International Projects Corporation (of NSW)*
MLAs	*Multilateral Lending Agencies*
OECF	*Overseas Economic Cooperation Fund (Japanese untied aid)*
OPCV	*Overseas Projects Corporation of Victoria*
OPS	*Office of Projects Services (of the UNDP)*
PPI	*Pacific Power International*
SAGRIC	*South Australia's overseas projects corporation*
SMEC	*Snowy Mountains Engineering Corporation*
SOC	*StateOwned Corporation*
UNDP	*United Nations Development Programme*
UNESCO	*United Nations Educational, Scientific and Cultural Organisation*
UNIDO	*United Nations Industrial Development Organisation*
VPS	*Victorian Public Service*
WAOPA	*Western Australian Overseas Projects Authority*
WHO	*World Health Organisation*

PART I: SETTING THE SCENE

A. SOME PRELIMINARY STATISTICS

1. Outperformed: NSW vs Other Australian States

Table 1

REVENUES FROM OVERSEAS PROJECTS WITH STATE GOVERNMENT AGENCY INVOLVEMENT JUNE 1992 - JUNE 1995 ($M)

	1992-3	1993-4	1994-5	TOTAL
Victoria	25.2	28.9	26.2	80.3
South Australia	30.4	25.4	24.9	80.7
New South Wales	6.7	12.8	9.2	28.7

Table 2

PROFITS FROM OVERSEAS PROJECTS WITH STATE GOVERNMENT AGENCY INVOLVEMENT JUNE 1992 - JUNE 1995 ($M)

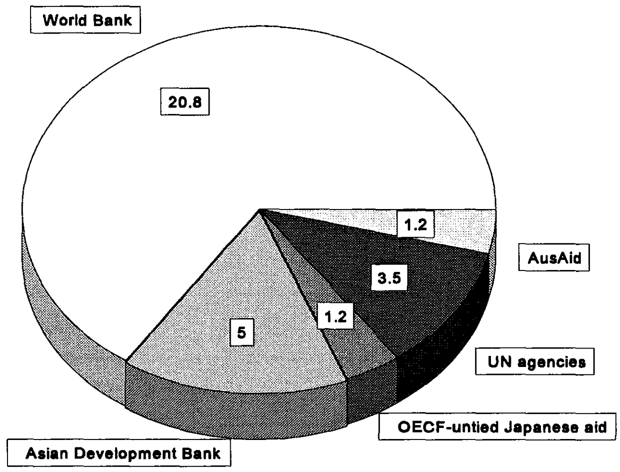
	1992-3	1993-4	1994-5	TOTAL
Victoria	1.5	1.3	0.7	3.5
South Australia	0.24	0.35	0.46	1.05
New South Wales	(2.3)	(4.2)	(2.2)	(8.7)

Sources: Victoria: Annual Reports of Overseas Projects Corporation of Victoria; communications provided by State Electricity Commission of Victoria (International) and Gas and Fuel Corporation of Victoria; for South Australia: Annual Reports of SAGRIC; for NSW, revenue and expenditure figures provided to Committee by 21 agencies (see Table 3).

2. Large But Changing: The World Market

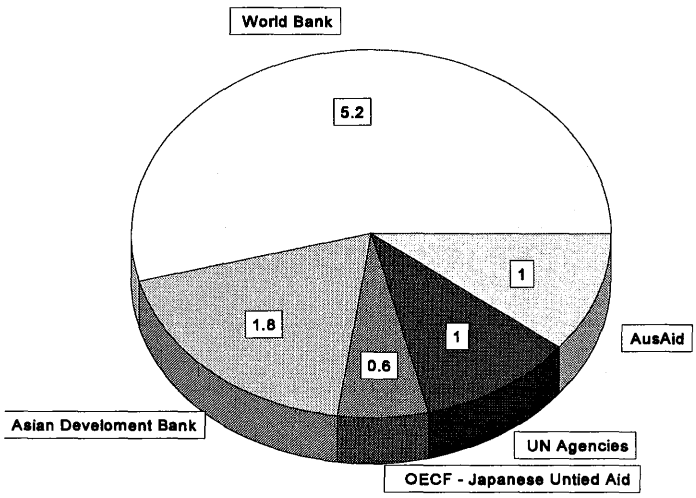
$ Billions (1994 Expenditure)

Figure 3



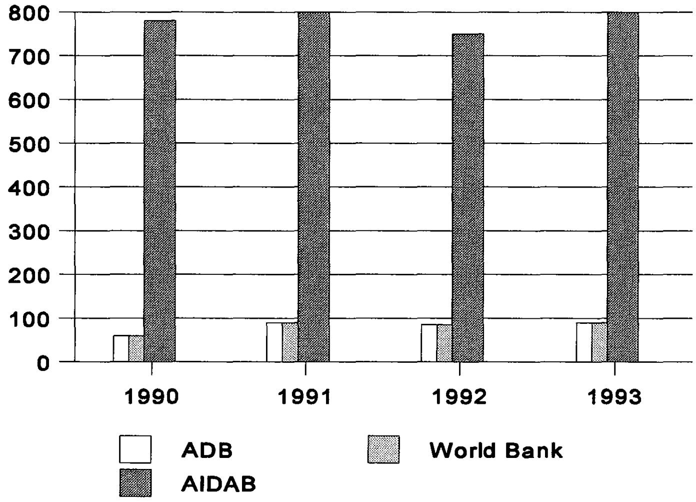
Sources of official aid finance potentially available to Australian firms for goods and services

Figure 4



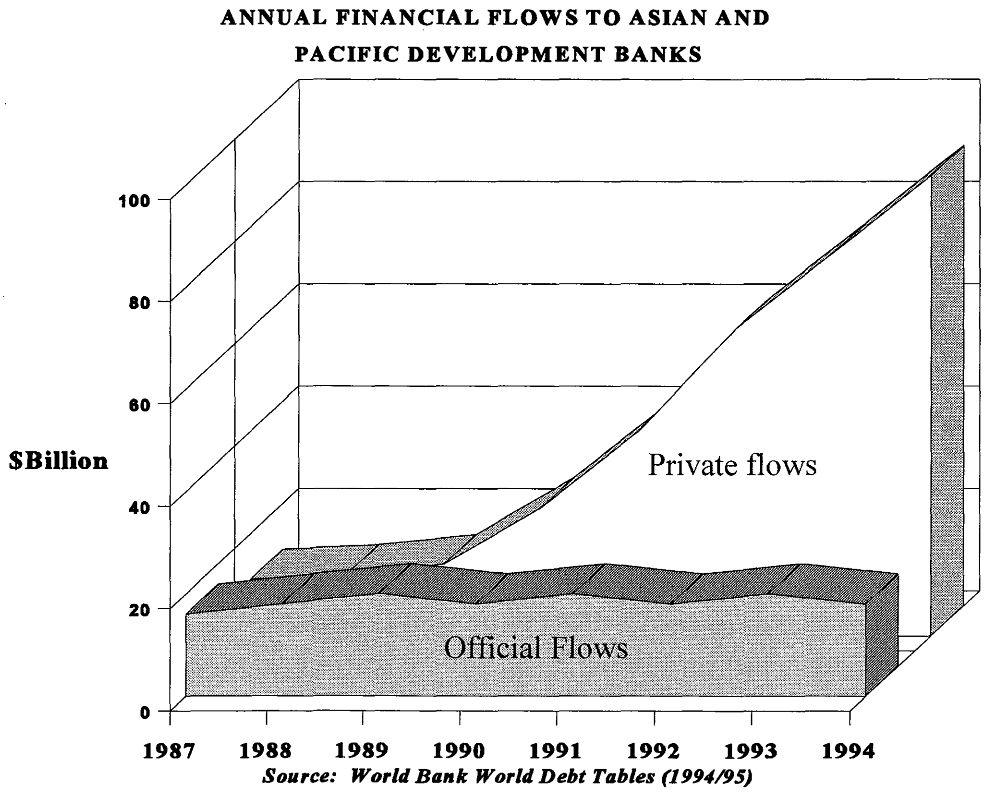
Sources of official aid finance potentially available to Australian firms for technical services only

Figure 5



Past Value of International Official Aid Market for Australia

Figure 6



Public and Private Flows: The Emerging Private Market

B. SOME PRELIMINARY ISSUES

1. Why try to export government services at all?

All Australian states, without exception, as well as the Commonwealth, are currently seeking to expand the export of their services, as are governments in Canada and Europe. There are many reasons why, some of them interlinked. They include:

- Substantial Revenues - because international demand for government services is strong
- Jobs
- Profits
- Earning a return on taxpayers' investment in public sector skills
- Sharpening NSW skills in competition with world best practice
- Boost to private sector
- Improvement in productivity in NSW
- Foreign Exchange
- Downstream procurement opportunities
- Prestige and goodwill
- Internationalising of the State's economy
- Dividends and tax equivalents paid to Consolidated Revenue

These reasons are powerful ones. The fact that many governments are trying to get into this business proves that they see substantial benefits to be won. It is pointless to pretend that this process is not happening, or to try to turn back the clock. The challenge for NSW is to get the process right.

The benefits listed are discussed in turn below.

- ***Substantial Revenues.***

Overseas activities can earn significant revenue which benefits the economy of the state as a whole. For example, the Overseas Projects Corporation of Victoria has earned a total of $110m revenue in its ten years of existence, culminating in revenue of $26.2m in the 1994-95 financial year; SAGRIC has earned $70m *for South Australian entities* since 1980. Much of this revenue remains within the state which earns it, through the employment of state public servants, private sector bodies based in the state, and the purchase of goods and other services.

This is direct revenue. The multiplier effect of this new revenue is also significant. The ABS estimates[1] that an extra dollar income in administrative services (the closest equivalent to our case) generates $3.23 in additional income. Thus the $110m earned by the OPCV over ten years would have generated something like $300m for the Victorian economy as a whole.

The revenues accrue to both public and private sectors. SAGRIC estimates that only 18% of its disbursements are to South Australian public service bodies; 40% go to the private sector, and the rest go to other states' public service bodies, including those of New South Wales.

Revenues have been so strong because demand for the services that state governments typically provide is itself very strong internationally at present. Asian Governments, in particular, are now in the process of modernising their entire economies, with considerable stress on institutional strengthening. This is precisely where state public servants are skilled and in demand. They come from fields such as environment protection, health, education, water treatment and so on, and it is just these areas which Asian countries are now seeking to develop.

There is a window of opportunity at present which could enable significant revenues to be earned by State Government bodies in the next five to ten years from the activities they have been doing anyway for decades. And through the multiplier effect these revenues will generate further revenues and further jobs, our next category.

- ***Jobs***

Overseas projects typically create jobs, both in the public and the private sector, and both directly and indirectly.

There are four main types of jobs they create:

1. **They generate new contractual positions**. These are filled both by advertisement and by direct recruitment, and those who fill them may be public servants or private sector contractual personnel. OPCV estimates that between 300 and 500 contractual personnel are hired each year, which over the ten years of OPCV's operations would give between 3000 and 5000 new contractual jobs created.

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1 ABS 5237.0 table 2.

2. **Positions in the field are often long-term, and are often filled on a rotating basis.** For example, a project might last six years, but OPCV would be unwilling to leave one single person there for so long. The position might be filled by three people each working there for two years. This creates new jobs at home.

3. **The positions left behind by those departing on contracts also need to be filled.** This can be, and often has been, used by public and private sector managers as a good career development tool for staff.

4. **Jobs are created in industries that serve the contractors and subcontractors.**

The ABS estimates that for every $1m injected into service industries related to the public service, 36 new full-time equivalent jobs are created[2]. This is roughly consistent with the OPCV figures.

The ups and downs of the normal business cycle means that agencies which are run as businesses, either wholly or in part, will often experience varying needs for staff. Overseas projects can provide an alternative to making staff redundant, as was pointed out by the Land Titles Office in the answer to its questionnaire:

> The overseas assignments provide a . . . means of redeployment during periods of downsizing or downturns in normal business.[3]

- ***Profits***

If properly managed, overseas projects can earn profits. For example, OPCV has been profitable every year since 1986 and has generated about $3½m in profits (on $80.3m revenue) in the last three years. SAGRIC has earned smaller profits in relation to revenue ($1.1m on $80.7m revenue), but has done so consciously in conformity with a government policy requiring that the provision of jobs should be a major objective for the company.

Profits are distributed among participating companies and individuals according to negotiation and agreement on a case by case basis. Breakdowns vary according the

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2 ABS 5237.0 Table 3.

3 Ibid p. 2.

projects, ranging from 50-50 in simple cases, to more complex formulas when several contractors are involved.

Out of profits, SAGRIC has paid tax equivalents to the South Australian government. Over the 1992-4 financial period, the group as a whole paid over $100,000 to the government in tax equivalents.

Profits may also be retained to finance future development. This is the strategy adopted by OPCV, which now has over $6m in reserves.

- ***Earning a return on the taxpayer's investment in skill development***

The skills of the State public service have been developed over the years at considerable cost to the taxpayers of the State. Earning export dollars means earning a return on the taxpayer's long and expensive investment.

- ***Enhancement of public sector skills***

This is achieved in several ways:-

> ***Sharpening NSW skills in competition with world best practice***
> By competing for contracts overseas, the state's public service is vying with some of the best companies in the world. Competition sharpens its skills, allowing better service to the people of NSW.
>
> ***Exposing public servants to other cultures***
> The benefits of this to NSW were outlined by TAFE at hearings:
>
> **MR LLOYD:** Certainly once we send somebody offshore in our opinion their skill level increases dramatically. Their ability to interact in a NSW multicultural classroom is enhanced. By operating in a different environment their teaching skills are certainly enhanced, as is their exposure to technology ...[4]
>
> Other agencies like the Board of Studies and the Department of Health made similar points in interviews.

[4] Minutes of Evidence, 4 October 1995, p. 48.

Development of international links

A number of agencies made this point in their replies to the questionnaire. The Department of Agriculture, for example, said:

> Officers undertaking overseas consultancies will attest to the benefits gained in terms of professional development, international recognition and network development.

Sometimes of course these can lead to new projects, as happened in the case of Pacific Power's Pha Lai project in Vietnam, where the presence of one individual from Pacific Power on a small technical assistance project led to the securing by the agency of a very large follow-up project in the same field.

- ***Sale of new skills acquired overseas***

A snowball effect can occur in the development and sale of newly-acquired skills: once staff have been able to obtain new skills abroad, they are now more marketable both internally and externally, and are in a better position to earn new revenues for the state.

- ***Improvement in productivity in NSW***

An example of how productivity in NSW can benefit from overseas contacts was provided by the Department of Agriculture, which, in its reply to the questionnaire, said:

> Consultancies involving international crop breeding institutes have contributed to the successful operation of the institutes and there is clear benefit to the Australian economy from the incorporation of new lines of genetic material from overseas in the local crop breeding programs.
>
> Overseas activities have in some cases led to improved productivity resulting from activities such as importation of [various crop strains].[5]

- ***Foreign Exchange***

A significant proportion of the earnings from overseas projects comes in the form of foreign exchange. This helps Australia's balance of payments and constitutes some return on Australia's international aid contributions. OPCV is one of Australia's 500

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[5] P. 3.

largest exporters, and the Committee believes that NSW has the potential to catch up and even surpass this record.

- ***Boost to Private Sector***

The private sector can gain considerably when state government entities get involved in overseas projects.

Innumerable times during the inquiry the Committee was told that a government crest on a business card ensured access to the highest levels overseas, and that it could often make a difference whether the project was won or not.

The private sector frequently "piggy-backs" on this access. It is included in consortia stitched together by the state government entity to bid for projects; it secures its proportion of the profits; it gains employment for its staff, and a boost to its reputation and track record.[6]

- ***Downstream procurement opportunities***

As the September 1993 Guidelines for the Export of the Skills and Expertise of NSW Public Sector Agencies issued by the Premier's Department pointed out:

> Successful bids for international project work can lead to valuable downstream procurement opportunities for NSW/Australian manufacturing and service firms, which in turn can create significant "spin off" benefits in terms of increased production, exports and employment.

2. Not the Core Business of Agencies

Many agencies made the point that exporting their services was not their core business, which was to deploy their expertise for the taxpayers of NSW. The Committee fully agrees.

However, export of government services is already happening. Other Australian states are doing it, and have been for years, and so has the Commonwealth; NSW agencies are doing it; and Government entities from overseas countries are doing it, simply because there are ample benefits to their economies from doing so. The Committee

6 The reverse can also occur, where the private sector is the lead bidder and includes the public sector in the consortium. An example of this is the Indian Water Resources project managed by a British firm, Sir Alexander Gibbs and Associates, where the NSW Department of Water Resources has been included the bidding consortium.

believes it is useless to try to pretend it is not happening, or to try to turn back the clock. As pointed out above, the challenge is to do it properly and get as much economic and social benefit from it for the State as possible.

This is not happening in NSW at present. At present, agencies in NSW have branched out into areas they were never set up to do. Operating alone without much guidance, public servants have tried to become overseas marketers and managers of overseas projects. It is all a far cry from their original technical purpose, which was to develop and deploy technical expertise for NSW.

However, the fact that they have strayed from their original purpose into overseas projects does not mean that NSW should not try to tap into the overseas project market at all. As was just pointed out above, there are great benefits for the NSW economy as a whole, for the people of the State, for its public service and its private sector, in moving into this market. Furthermore, the benefits of the market should not accrue only to other states.

The most logical conclusion to be drawn is *not* that NSW should stay out of this market, but rather that pursuing this market should be left to professionals whose business it properly is, rather than public service officials whose core business it is not.

Another point is occasionally made in this context. This is that while exporting may not be the core business of *agencies*, the core business of *government as a whole* should be more broadly defined than that of individual agencies:

> **Dr LISLE-WILLIAMS**: . . . individual departments have as their core business service to the residents of the State and the interests of the State. The interests of the State are defined a little more broadly than direct service to the residents, and include the attraction of investment to the State, maximisation of productive economic activity, perhaps the achievement of certain objectives in respect of equity and access, and so on. That goes beyond purely direct service.
>
> Our view is that, while the individual departments need to focus on their core activities, and therefore probably should not be involved in the business of marketing and trying to sell their skills directly, there is some basis for having a State body, a government-owned body, that can pursue project opportunities and involve both public and private sector skills as appropriate from the State. That ensures that those departments that provide resources for the projects are recompensed fully for the cost of employment and receive a share of the profits so that there is a net benefit to the Treasury, or at least the State. It also ensures that ongoing services are not

jeopardised by the loss or absence of people from the State during the time that they might be working on projects.[7]

The Committee agrees.

3. The Question of Risk

When properly managed, exporting of government services has in the past proved to be in general a low-risk business. There are several reasons for this.

- with few exceptions, the clients for large overseas projects are major governmental or international institutions. Buyer insolvency or repudiation of contract are rare in this market, although certain governments (well-known and -documented in the industry[8]) have occasionally failed to make the required payments. If the organisation still wishes to deal with those clients, upfront payments would be more advisable. With organisations such as AusAID or the World Bank, failure to pay does not occur.

- the risk that poor services will cause death or serious injury is very small, in projects won after competitive bidding and managed by sizeable teams of experts. In fact, to the Committee's knowledge, no Australian government body exporting its services overseas has ever been sued for poor performance overseas.

- most risks can be insured against (or avoided, or managed effectively).

This does not mean that exporting services overseas entails no risks at all. All business entails risks. Most companies, however, find ways of offsetting these risks. The old official guidelines[9] list the ten major categories of risk and match each of them with an offsetting mechanism:

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7 Minutes of Evidence, 4 October 1995 p. 11.

8 EFIC publishes market risk assessments which identify areas of high political and commercial risk.

9 Guidelines for the Export of the Skills and Expertise of NSW Public Sector Agencies, issued September 1993.

Risk	**Offsetting mechanism**
Buyer insolvency	Export credit insurance
Delay in payment	Export credit insurance
Repudiation of contract	Export credit insurance
Exchange transfer delays	Export credit insurance
Professional error	Professional indemnity insurance
Public liability	Public liability insurance
Currency fluctuation	Forward exchange cover, currency hedging
Imposition of controls on repatriation of profits/capital	Overseas investment insurance
Expropriation	Overseas investment insurance
Property losses resulting from war/civil disturbance	Overseas investment insurance

There is also political risk, which can be insured against through EFIC. EFIC also offers "unfair calling" insurance against the unfair calling up of performance guarantees by clients who may be unduly disgruntled or just in bad faith.

All these mechanisms are available to limit risk.

In hearings, the Committee asked a range of witnesses about the question of risk.

> **Mr GLACHAN**: There is a great deal of concern in New South Wales about the question of risk. In your report you talk about overseas operations being low risk. What would you say to the people who talk about risk in New South Wales?
>
> **Dr LISLE-WILLIAMS**: Again, we did not come to that conclusion lightly. We started off with the assumption that perhaps it was a risky business. However, the financial risk is quite limited. The elements of that risk include the possibility of non payment—which is very low—and the possibility of slow payment, which leads to some exposure to foreign exchange risk. Payment occurs in overseas currencies

quite often, but that can be managed by sensible treasury functions. The sovereign risk involves the possible dangers arising from a drastic and sudden change in government and a change in the rules of the game. Again, these have not impacted upon OPCV over the past 10 years. Nevertheless, it must be taken into account. No risk has been involved with equity development leading to public funds going down the gurgler in that sense; that is, through the investment in other firms. There is necessarily some normal operating risk in the sense that the firm may not be successful, not win enough projects and prove not to be viable. That is a normal commercial risk.

Mr GLACHAN: What if a firm wins a project, makes a mess of it and is sued?

Dr LISLE-WILLIAMS: There are a couple of steps along the way. Decent project management should ensure that the relationship with the host government and the representatives of the host government at the regional level will ensure feedback regarding the performance of people on the ground. In that way action can be taken to sort out problems before they develop into that type of incident. It has not happened in OPCV's history, although people have been replaced on the ground. The likelihood is real, but the risk is not high.[10]

Another view was provided by a private sector competitor of OPCV:

Mr COCHRAN: Do you consider overseas consulting work to be high risk? What types of risk might be involved? What types of risk have you yourself run into, and how have you managed these?

Mr TUCK: Overseas consulting has to be broken into two markets: I suppose the Australian aid market or any market where you do work for some element of an Australian government; or non-Australian work. In the non-Australian work, the risk differs according to whether you are dealing with a multilateral agency but the big market is outside those agencies. Then the risk is quite significant and it relates to non-payment, foreign exchange, and it is not possible to get total hedging in a lot of this business even though you may try, and it also relates to the volatility of governments and so on—the very reason why you are there in the first place. This also adds to risk. In the Australian-funded market, up to five years ago I would describe it as being virtually riskless. Increasingly the main player in the market, AusAID, has moved to shift the balance of risk on to the managing contractor. It does this by having certain outputs contracted and a lump sum of money is paid to achieve the outputs. In a service delivery, where many more factors are beyond your control than there are if you are working in Australia, that is adding to risk. It is still not high risk but it is significantly riskier than it was. The risks we have run into have mainly been to do with non-payment or very late payment—up to two years late in paying—and currency movements which we are not able to hedge against, because you cannot hedge against all of them. Another one is a major change in a government policy or some of the corruption and similar things that apply with some

10 Minutes of Evidence, 4 October 1995 p. 17.

developing country governments. You can be working on a project and suddenly the project is being wound down. Short of going through an Indonesian or other foreign court you have little redress.

Mr COCHRAN: I have noted from the AusAID publication that we were given that your company manages a PNG project for AusAID, PNG police phase two. Would that be considered one of those high-risk projects you were talking about? How would you manage that particular type of project when it is integrally tied to the government of the day, and given the whims of the PNG government and the politics of PNG? How do you cater for that?

Mr TUCK: The contract we have with AusAID was written about three years ago and it was under the prior rules where there was not quite so much risk put on to the contractor. So, it is not quite as risky as if we were contracting it today. The risks are certainly there. We have had several major losses on foreign exchange. As you know, the kina was floated and there was almost a one-third depreciation—it is probably more than that now. The changes of Government and government policy and the Government suddenly not being able to fund its part of the contract have led to the project being substantially scaled back pending a review. It has now been started up and that has cost us a lot of money. The other risk we faced was an act of God, which was the eruption of the Rabaul volcano. We had a team of people to evacuate from the area. It was quite an expensive business going through that.[11]

Proper professional management can minimise risks by rejecting involvement in situations where governments are unstable, by paying for insurance to cover the major risks, by providing close supervision of project activities, and by ensuring high quality of delivery.

One major failing of agencies which are relative beginners in the field of overseas projects is that lack the ability to make a critical, professional assessment of the technical risks of operating overseas. These risks can be quite different from those the agency would have faced in Australia.

In NSW, however, proper professional management has been somewhat thin on the ground. As we saw from Table 1, NSW has not been as successful as Victoria or South Australia. The relatively unsophisticated efforts of some NSW government agencies thus cause the Committee some concern in the context of risk. It could plausibly be argued that a lower level of skill leads to a higher degree of risk. Indeed, as Part IV of this report shows, many risks have actually eventuated for NSW agencies operating overseas, and have led to sizeable losses for the taxpayer of the state. Thus the present arrangements expose the state to substantial risk.

11 Minutes of Evidence, 4 October 1995 p. 21.

The Committee would thus argue that NSW can best limit its risk not by avoiding involvement in overseas projects altogether, but instead by getting involved in these projects and managing the risks with proper professionalism.

However, it should not be forgotten that even with the best professional management, there is still a possibility that a major risk will eventuate. The worst of these could well be the risk of the state's being sued for faulty technical advice which led to death, disability or severe economic loss (although as far as the Committee is aware in the provision of services, the risk of the state being called on as implicit guarantor has never eventuated).

Here the legal structure of the risk-taking enterprise is important. The entity must be structured so that the government's risk is minimised. The Committee makes recommendations on this matter in Part V of this report.

There will always be risk attached to any business. If Governments wish to get into this business, as all Australian governments have sought to do, then the important task is to limit the risks as far as possible by good management and the appropriate legal structure.

PART II
THE WORLD MARKET

A. THE NATURE OF THE MARKET

The market in which developing counties obtain the entire range of technology and capacity to develop their economies is a rapidly changing and diverse one.

- It embraces the needs not only of governments but also of private bodies seeking to provide services and facilities hitherto primarily the preserve of governments.

- It includes the activities of international development agencies as well as the development assistance activities of developed country governments.

- It satisfies the need of countries at all stages of development - from those calling for assistance in the provision of basic human needs to those with powerful private corporations seeking to provide development on strictly commercial terms.

- Increasingly it involves the co-operative activities of commercial entities from both developed and developing countries.

- It is driven by a blend of grant, loan, commercial and internally generated funds.

- While there are clearly humanitarian aspects to the market, proven commercial principles applied equally by developing and developed country bodies govern its operation.

Probably the most common failing in assessing this market is the adoption of too narrow a view of its scope and a failure to recognise its many faces. A narrow view of the market can seriously understate its magnitude and potential.

The development market many be classified in many ways. One way of looking at the market is to consider the sources of finance for development projects, Those sources include:

1. *Official Finance*

- Development Banks
- Grant Assistance Agencies, both bilateral and multilateral
- Bilateral Development Finance Agencies

2. *Private Finance*

- Commercial development financiers
- The capital of global corporations

Increasingly, funds from these prime sources of finance (and often others) are blended to attain a development objective. It is not unusual to find a project identified by a multilateral grant finance agency, prepared for implementation (i.e. specifications drawn up and plans fleshed out) by a bilateral grant assistance agency, financed in its initial implementation by a development bank and generalised to many other users through loan finance arranged jointly by bilateral development finance agencies in concert with commercial financiers.

Official and private finance are discussed in turn below.

1. Official Finance

One way to consider the market is by outlining the activities of the major agencies financing development activities in Australia's sphere of interest,

(a) Development Banks

(i) The World Bank

Located in Washington DC, the World Bank Group is the largest lender for development in the world processing around $US 20 billion in new loans each year, it comprises four agencies which operate in closely related fields:

The International Bank for Reconstruction and Development (IBRD) which provides loans and development advice to the majority of the world's developing countries.

The International Development Agency (IDA) which was formed in 1954 as the soft loan window of the group to lend to the least developed countries. In practice many loans to the poorer countries are a blend of IBRD and IDA monies, The two agencies have the same staff and are essentially the same organisation.

The International Finance Corporation (IFC) which was formed to assist in providing finance to the private sector of developing countries, While IBRD and IDA can only lend to central governments, IFC typically contributes equity and debt finance for projects involving companies from both developing and developed countries.

The Multilateral Investment Guarantee Agency helps mitigate the risk of investing in developing countries.

In their Fiscal year 1993/94 IBRD and IDA made new loan commitments of $US 20.8 billion making a total portfolio of almost $US I 50 billion. Disbursements in 1993 totalled $US 17.7 billion.

The Bank also maintains good relations with its developed country shareholders and its officers are generally willing to provide advice and information to those wishing to participate in the development market. Australia maintains an AUSTRADE post in Washington and provides either an Executive Director or an Alternate Executive Director on the Bank's Board of Directors. Australia also provides a Consultant's Trust Fund to facilitate Australia's becoming involved in project identification and related activities.

Although preparing projects is a responsibility of the borrowing country, the Bank is often able to arrange to help the borrower in this task by working with bilateral development assistance agencies to make available grant funds for this purpose. Most countries (including Australia) "tie" such funds to agencies from their own country in the hope that this will lead to added work. Some countries (such as Japan and some European countries) provide "untied" funds.

These preparation opportunities can provide major opportunities which can lead to significant work under the eventual loan and even beyond.

Overall the World Bank offers a significant business opportunity to enter into the development market. Australia is generally regarded as not having built the linkages to later development work through the World Bank as well as have some other countries. Often those who have built strong linkages have had significant involvement of their public sector agencies in the early stages of project work.

(ii) Asian Development Bank

Founded in 1966, the Asian Development Bank is located in Manila. The Bank typically lends $5 billion to its developing member countries in the Asia Pacific each year.

Operations are similar to those of the World Bank, with each institution following a related project cycle but applying its own procedures. Even within the Asia Pacific the World Bank lends significantly more than does the Asian Development Bank.

An important difference is the operation by the Asian Development Bank of a Technical Assistance Special Fund which grants money for both advisory and project preparation purposes. This fund has provided an attractive opportunity for a large number of developed country organisations to become involved in developing country and development bank work. As such they are a very attractive target for organisations entering the market.

Again AUSTRADE maintains a post in Manila to assist those seeking to work with the Bank, and Australia provides an Executive Director to the Bank.

In general the Asian Development Bank has been the next step for Australian organisations who have entered the market through Australia's aid program. It is close to home, reasonably understandable and provides an attractive mechanism for market entry through its Technical Assistance Program. It is surprising therefore that Australia has a somewhat disappointing record with the Bank and, as with the World Bank, has not built the links into major loan projects and co-financed projects that one might have expected.

(iii) European Bank for Reconstruction and Development

The European Bank for Reconstruction and Development was founded in 1991 to foster the transition toward democracy and market oriented economies in central and eastern Europe, including the former Soviet Union. Unlike other development banks, it operates in co-operation with private and public financiers, directing some 60% of its financing to the private sector. The remainder is focussed on public infrastructure. It offers a much wider range of financial lending instruments than do other such institutions. It also operates a technical assistance program.

The European Bank therefore operates much more in the style of a merchant bank, considering proposals from a wide range of proponents rather than exclusively from governments as is the case with other development banks,

Australia is a member of the Bank and therefore Australian organisations are eligible to participate in the Bank's activities. However, few Organisation have chosen to do so, probably for these reasons:

- the cultural affinity, language facility and physical proximity of European-based competitors makes it very hard for Australian organisations to compete, and

- the co-operative work of many European grant assistance agencies, for which Australian organisations find eligibility criteria difficult, make the competitive gap even wider.

Despite this, some Australian organisations have been successful, particularly in fields where Australia has a significant competitive advantage. Most Australian organisations are likely to concentrate on targets nearer home where they can compete more favourably.

(b) Grant Assistance Agencies

(i) Multilateral

The United Nations operates a large number of specialised agencies covering most fields of development. In recent years funding restrictions, exacerbated by the added diversion of funds to the United Nations' increased peacekeeping role, have limited the impact of many agencies. Some have been able to replace some lost funds by special grants. Often in such cases there is a tacit understanding that procurement based on such funds will be tied to the donor country. A sample of these agencies is outlined below. Figures are taken from the United Nations General Business Guide (IAPSU Copenhagen May 1994).

- UNDP (Contributions 1993 $US 903 million). The core of the system is the United Nations Development Program which provides grants of around $1 billion annually. With offices in 137 countries, it provides grants to over 170 countries. Grants are biased towards the least developed countries and are focussed on projects with a social content. Projects in the program are normally carried out either by an agency in the recipient country or a specialised agency of the United Nations.

- UNOPS (Disbursements 1993 $US 222 million). Located in New York The Office for Project Services manages technical co-operation projects on behalf of multilateral and sometime bilateral agencies. Much of the focus of the office is on Africa, although some of its projects are in the Asia Pacific region.

- ESCAP (Disbursements 1993 $3.7 million) The United Nations operates four regional economic commissions- for each of Africa, Latin America, the Caribbean, West Asia and the Asia Pacific. The Economic Commission for Asia Pacific is located in Bangkok and manages projects in fields such as natural resources, transport, industrial development and social development.

- FAO (Disbursements 1993 $US 84 million) The Food and Agricultural Organisation located in Rome focuses on food production and manages projects from various funding sources.

- UNESCO (Disbursements 1993 $US 42 million) Located in Paris, the United Nations Educational, Scientific and Cultural Organisation covers a broad range of activities centred on science and education and purchases goods and services in those areas.

- WHO (Disbursements 1993 $US 108.5 million) The World Health Organisation lets major contracts from its head office in Geneva but makes significant local purchases from regional offices in Washington DC, Alexandria (Egypt), Copenhagen, New Delhi and Manila,

- UNIDO (Disbursements 1993 $US 58 million) The United Nations Industrial Development Organisation seeks to promote and accelerate industrialisation in developing countries and is based in Vienna.

In aggregate the United Nations System procured in 1993 over $US 3.5 billion worth of goods and services. Around 30 % (or over $1 billion) of this sum was for professional services. The average value of United Nations contracts was $US 24,000 and only 5% exceeded $US100,000. The aggregate estimated value of business springing from the United Nations system, including development banks, approaches $US 30 billion annually.

(ii) Bilateral

AusAID

The Australian Agency for International Development Australia conducts a major development assistance program through AusAID. The program has an typical annual value of approximately $1.5 billion and is focussed on the Asia Pacific Region. The program seeks to deliver ecologically sustainable development in response to Australia's humanitarian, foreign policy and commercial interests.

The program covers many facets including food aid, project grant assistance (covering natural resources, infrastructure and human development) and the support of a major blended credit scheme which is discussed below. The needs of each country are considered in designing a program suitable to that country. Asia's rapid growth is causing continual changes in the mix of development assistance used for each country and these changes are likely to continue.

Most Australian providers of goods and services have taken their first steps towards exporting through AusAID's program and it remains an attractive and low risk, if highly competitive, means of doing this.

(iii) Bilateral Development Finance Schemes

DIFF (Australia)

Australia's Export Finance and Insurance Corporation operates a mixed credit scheme in conjunction with AusAID. The scheme allows Australian organisations to provide commercial loans at concessional rates to approved projects in selected developing countries. This is made possible by blending an AusAID provided grant element of 35% of the project value with EFIC's commercial finance. The program's value is around $120 million annually and has been increasing in recent years. It is intensely competitive with many more applicants than the available funding can cover.

OECF (Japan)

Japan's Overseas Economic Co-operation Fund has made large numbers of concessional loans on a similar basis to that of Australia's DIFF Scheme. In 1994 these loans had a total new loan commitment value of $11,3 billion. Of this 98.3% were designated "general untied", meaning that there was no restriction on the nationality of the bidders for the projects the loans supported. The remaining 1.7% was limited to bidders from the developing country concerned. While 27% of the contractors working on the projects supported by the loans, 57% came from the developing country concerned and 16% from other OECD countries.

UNTIED JAPANESE LOANS REPRESENT A SIGNIFICANT OPPORTUNITY FOR CONTRACTORS FROM AUSTRALIA AND OTHER COUNTRIES. Success generally calls for co-operation with both organisations from the developing country and from Japan.

2. The Private Market: Characteristics of the New Frontier

In the developing world in general, and in the Asia Pacific region in particular, the level and the rate of increase in the international flows of private finance have been significant, as was shown in Part IA.

This increase in private finance has occurred at a time when official flows are declining slightly. With the region's ongoing economic reforms and steady growth it is difficult not to see these flows continuing to increase.

The sources of such finance include:

- the capital of foreign companies investing in the region, and
- debt finance from commercial sources, largely in support of such ventures.

A significant factor in the demand for such capital is essentially fuelled by the major shift in the financing of infrastructure from the public sector to the private sector. The World Bank estimates[12] a world-wide need for infrastructure of US$ 1.3 - 1.5 trillion over the next ten years and, as this is clearly beyond the resources of governments, there is little alternative to private finance if growth rates are to be maintained. Development banks are making an effort through their lending programs to establish the essential preconditions for such financing to occur.

For those seeking to enter or work in this new privately financed market, the challenges are many. Rather than expertise being provided by the publicly-financed, widely-advertised, competitively-bid fee-for-service systems that have prevailed to the present time, new systems of winning work are emerging. Some of the bases on which work is now won are these:

- Alliances between planners, designers, builders, equipment suppliers and financiers are now much more important. Being part of the winning alliance will now be more important than being technically the best in any of those fields.
- The central player is shifting from being the designer or builder of infrastructure to being the financier.
- Large players will tend to succeed over small players. A well rounded record of achievement will count for more than how well one can do the particular job.
- Less formal markets will obtain, making it mandatory to have better intelligence systems rather than rely on published opportunities from development banks
- Nationality will continue to diminish in importance. Perceived value, responsiveness and reliability will be the key determinants of success.

Many more options for the provision of infrastructure are emerging, Rather than simply providing infrastructure through various utilities, provision through various forms of

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12 Private discussions with senior Bank officials, July 1995

ownership and operation is now possible. Concessions or selective contracting out with or without public ownership are added options.

B. THE SIZE OF THE MARKET

By any measurement the market is large.

The sources of official aid finance potentially available to Australian firms for goods and services amount to over $28 billion a year. This is composed of $20.8 billion from the World Bank, $1.2 from AusAID, $3.5 billion from all UN agencies, $1.2 billion from OECF (Japanese untied aid) and $5 billion from the Asian Development Bank. There is also potential from the European Bank for Reconstruction and Development, the African Development Bank and the Latin American Bank.

For NSW government agencies, however, the only real interest is how much of this market is directed towards buying technical services. The total is much smaller, of course: about $5.2 billion from the World Bank, $1 billion from AusAID, $1 billion from UN agencies, $600 million from OECF, and $1.8 billion from the Asian Development Bank, totalling about $9.6 billion. To this should be added the technical services expenditures of the EBRD, the ADB and the Latin American Bank.

Private flows, as pointed out above, are also increasingly important, especially for infrastructure. Here the Asian region is dominant. It is difficult to obtain estimates of these, although the World Bank's Debt Tables for 1994-5 give a figure of $111 billion for the total of private and official financial flows to Asia Pacific developing countries on an annual basis. This of course excludes any local financing or matching funds that developing countries, or Japan, might provide.

The main point is that the market is very large, and is financed by both official and private sources.

C. MAJOR TYPES OF PARTICIPANTS IN THE DEVELOPMENT MARKET

These are:

- development institutions both bilateral and multilateral (which plan and supervise projects)
- consultants (who plan design and oversee particular activities),

- contractors (who carry out major endeavours),
- equipment suppliers (who provide many of the tools and equipment for development)
- financiers of the types described above.

All these players can come from developed and developing countries, depending on the complexity of the task at hand. In most cases they will come from the source that provides the best value. This is likely to result in several sources providing the inputs for each project.

Again it is important to view the process broadly and not to expect that any one agency is likely to undertake all aspects of a project on its own. Rather a project will almost certainly involve a blend of developed and developing country inputs (as appropriate to the level of technology called for and the state of development of the country concerned) from all the groups listed above.

The potential of the development market, when viewed in this light, for a state such as NSW, assumes considerable importance. The market has the potential to offer opportunities to, and provide significant benefits for, most segments of the NSW economy.

However, most project activity in this market begins as an initiative of, or at least with the active support of, the government of the developing country. The early skills needed in formulating development activity centre on skills which are held largely in the public sector. It is these skills that NSW government entities are well placed to provide.

This can be done not only on commercially attractive terms but also in a way that fosters the future involvement of other organisations, both public and private, in the follow-on activities. In other words, this market offers not only the potential for commercial return, but also the opportunity to focus industries on the comprehensive aspects of the market.

D. THE SIGNIFICANCE OF THE MARKET FOR NSW

For NSW there are a number of issues that need to be considered in appraising the significance of this information. They are:

- the profitability of the market,
- the ease of winning work in the market,
- the capacity of NSW Government entities to compete in the market, and
- the significance for the remainder of the economy of the involvement of Government entities in the market.

These are discussed in turn below.

1. Profitability

Major Organisation have been active in the market for many years. Significant contractors, consultants, equipment suppliers and, latterly, operators have found the market to be durable, if lumpy, over many years. It has provided a sound base of profits to provide for exciting growth for such organisations. Such global organisations as French water companies, US contractors such as Bechtel, European consultants such as NEDECO, and major equipment suppliers such as Japanese trading companies bear witness to the durability of the market.

Within Australia, contractors such as Leighton Holdings, consulting organisations such as the Snowy Mountains Engineering Corporation, operators such as Telstra and project management organisations such as the Overseas Projects Corporation of Victoria all demonstrate the size, durability and diversity of the market.

The fact that such commercial organisations from both Australia and overseas continue to operate in the market demonstrate that its profitability must be adequate to continue to attract them when in all cases they could choose to operate in many other markets.

One cannot fail to conclude that the development market must offer an adequate return to retain such large commercial organisations.

2. Ease of Entry

The market is characterised b a significant number of new entrants. Several NSW Government agencies have been able to enter the market successfully over the last decade. The growth record of the Overseas Projects Corporation of Victoria, as described elsewhere in this report is further testament to the way in which organisations have been able to establish a place in the market in a relatively short time frame.

3. Capacity to Compete

Australian organisations are well able to compete in most segments of the market. In some areas, notably the manufacturing sector, it has proved difficult for Australian industry to match the price competition for high demand items such as motor vehicles, but as our competitiveness in manufacturing improves so does our capacity to win work.

In competing for the Asian Development Bank's Technical Assistance Projects Australian engineering, architectural, education and management consulting organisations have proved able to win work against world wide competition. Similarly, Australian contractors such as Hawker Noyes Pty Ltd, Clutha Ltd and John Lysaght Ltd have also won significant work against world competition.

4. The Role of Agencies

It is clear that the development market currently represents a major opportunity for a developed economy to win significant work for its companies and citizens. With the rapid growth being enjoyed by much of the Asia Pacific region and the move towards the private provision of many public services, as demonstrated by the rapidly increasing private capital flows to Asia, the market is set to change in nature and develop in size. This will increase its significance and potential to provide economic benefits to countries participating in it.

It is increasingly important to see the components of the market as a whole. Grant assistance may well be used in identifying and preparing a project. Development banks may finance an initial project to prove a concept or a technique and to assist developing countries in getting policy and institutional structure into workable shape. Their activities may well be co-financed by a bilateral grant agency. Further co-financing between export credit agencies and commercial financiers may well see the project replicated several times. Ultimately purely private finance may be used to undertake similar projects on a private or concession basis.

In this chain there are several important roles where government agencies can participate:-

- In project planning and identification many of the skills needed are found within the public sector:

- In the provision of much of the infrastructure developing countries need, the only source of experience at this time is the public sector.

- In the operation of infrastructure the public sector has, at the present time almost a monopoly on much of the experience needed.

- Most of all, in encouraging and partnering its own private sector, a public sector organisation can do much to encourage the growth of an aggressive development industry.

There would therefore seem to be a profitable, legitimate and useful place in the development market for public sector agencies.

PART III
HOW OTHER AUSTRALIAN STATES HAVE APPROACHED THE WORLD MARKET

A. VICTORIA

In late 1994, the Victorian Minister for Industry and Employment commissioned a review of the performance, charter and current role of the Overseas Projects Corporation of Victoria (OPCV). A team of consultants from Deloitte Touche Tohmatsu was selected to undertake the review, which began in 1995. It should be stressed that it was not the OPCV which commissioned this review.

The section which follows hereunder is based, first, on the Deloittes review, which is thorough, critical and objective; second, on numerous visits to the OPCV by members of the Committee and its staff, third, on evidence provided to the Committee in hearings; and fourth, on documents and other information generously provided by OPCV staff.

Measured by the bottom line, OPCV is a success story. Since 1986, it has earned revenue of $110m for Victoria. This translates into a benefit of around $300m to the state as a whole, assuming a multiplier of around 3.23[13]. Its earnings in FY 1994-5 were $26.2m. It has an Operating Profit:Project Income ratio of around 7.5%.

OPCV was established in 1985 as a company limited by guarantee, with $1.5 million contribution from the Victorian Government. In 1988, it was converted to a company limited by guarantee and shares. The OPCV has thus always run as a business, with the bottom line paramount and driving all its activities. The founding rationale was that OPCV would be the central point of contact for Victorian institutions dealing with multilateral aid agencies. The agency was never intended to enter the government-to-government or the private market and it has not done so to any significant extent. Its primary expertise is thus in the aid market, and it is very familiar with the procedures, priorities and personnel of the main funding sources, particularly AusAID.

Essentially, its functions can be described as marketing and project management.

In the early years, OPCV concentrated on AusAID projects, as being the cheapest to access. It took the smallest assignments, even modest jobs of $30,000 or $40,000, simply in order to establish a track record. In the first two years, it made a loss, but has made a profit every year thereafter, keeping steadily to around the 7.5% ratio of Operating Profit:Project Income. It consistently adopted the normal commercial

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13 ABS 5237.0.

philosophy of going where the demand already was, instead of trying to create demand out of thin air.

Gradually, and from these modest beginnings, OPCV has become a substantial consulting organisation which sources and brings together a wide range of public and private skills in projects funded by AusAID and Multilateral Lending Agencies (MLAs). It has established the benchmark in Australia for government involvement in overseas projects. Its FTE equivalent staff of 35 are professionals employing the latest project management techniques. It employs sectoral marketers/project managers who are very familiar both with the supply of expertise in their field over the whole of Australia, as well as with the demand for that expertise abroad. These marketers travel constantly, particularly to Asia.

It is significant that the OPCV has included in its consortia several NSW government agencies, notably the Land Titles Office, and has thus profited from NSW skills.

The OPCV employs agents in selected countries. One very successful agent, who is highly-regarded at senior levels of the government of his country, has been instrumental in securing for the OPCV a number of projects in a variety of sectors.

Five countries and five sectors account for most of the OPCV's activity:

- the countries are China, Indonesia, Pakistan, Papua New Guinea and the Philippines;
- the sectors are health, education, agriculture, water and urban development.

In terms of profitability, OPCV compares favourably with other firms operating in its field, and is perceived to be among the good performers in the development assistance market, essentially on a par with two of its main competitors (SAGRIC and ACIL).

The Deloittes report into the OPCV has the following to say about its relations with Victorian public service agencies:

> VPS agencies which have worked closely with OPCV have positive views about the benefits of the involvement, and generally favourable perceptions of OPCV and its staff. These include Agriculture, Planning and Development, Health, TAFE, VicRoads and Emergency Services. Negative views were expressed by a small group of agencies which had not worked successfully with OPCV or which had not had reason to deal with OPCV. In several cases, the negativity arose from the desire of some staff within the agencies to undertake the export of skills activity without recourse to OPCV, while in two instances, attempted collaboration had gone awry and

> OPCV was blamed. *On balance, the major VPS participants in the international projects market are satisfied with OPCV's performance* and supportive of its continuation, albeit with more attention to continuity of involvement with each agency. The Board and management of OPCV are advocating the establishment of a subsidiary which can apply retained earnings to assist on a more continuous basis with the development of project track records and country experience for agency staff.[14](emphasis added).

The report also found that "OPCV does not crowd out private firms in the overseas consulting market, but provides effective access to public sector skills for large projects".[15]

The report went on to state:

> The State Government has good reason to continue with OPCV, because: it provides direct net financial benefit to the VPS; it adds to the private sector's ability to export services and goods; it assists in ensuring that Victoria will obtain a fair share of work funded through the lending agencies; it enjoys support that would not be available to commercial competitors from vital VPS agencies; and it provides legitimate competition with overseas firms. In addition, OPCV provides opportunities for skill exports to VPS agencies at a lower cost than they could achieve individually[16].

The main success factors for the OPCV were:-

- Low infrastructure costs e.g. rent, plant and equipment;
- Good sellers, project directors and managers - there is a need for quality submission writers, technical and country specialists, relationship builders, project directors and managers;
- Low operating costs - appropriate leverage and margins on projects: controlled discretionary costs etc;
- Flexible and committed staff - relationships are important and therefore continuity of staff also mobility and ability of staff to meet tight deadlines;
- Thorough analysis and qualification of opportunities to maximise the strike rate - good understanding of ILA/client requirements, current country and sector

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14 P. iii.

15 P. iv.

16 P. iv.

knowledge; good knowledge of resource availability; competitor analysis for each opportunity; exemplary analytical skills;

- Databases/Information systems - comprehensive, user-friendly databases;
- Efficient management information systems - emphasis on forecasting, management of proposals, project management, reporting to clients and Board;
- Reputation and track record - this includes effective communication with the market (ILAs and other participants), including use of the Government imprimatur for competitive advantage;
- Relationships - long term relationships with ILAs, consultants and VPS agencies;
- Access to relevant skills - sector and country specialist positions;
- Access to funds for long-lead project development;
- Focus on strategically important areas.

In numerous visits to the OPCV, the Committee was impressed with its high level of professionalism and commercial acumen. It believes that there is considerable potential for NSW to move to these levels itself, now that the pioneering work has already been done elsewhere.

B. SOUTH AUSTRALIA

In the early 1970s, the Department of Agriculture in South Australia, which had accumulated considerable expertise in dryland farming, identified a number of dryland farming project opportunities in North Africa, some financed by the World Bank.

The projects ultimately eventuated, and were successfully executed by the Department. This was South Australia's first venture into the overseas project market, and its success led the then Government to consider replicating this achievement not only in agriculture but in other fields.

The Government decided to set up a corporation for the purpose, and to give it as wide a brief as possible, although agricultural projects would clearly be its mainstay. The only proviso was that it should not make a loss. The new corporation was named SAGRIC, in recognition of its primarily agricultural base.

No other SA government department in those early years had attempted to work internationally, and the new managing director of the corporation did not face the situation prevailing in NSW, where many departments have already entered the field. Instead, the managing director had to go from department to department attempting to convince them to submit bids for overseas work, to join together with the private sector, and in general, to become interested in working overseas.

From these small beginnings, a highly professional and diversified corporation has arisen. The corporation now works in training, health, environment, agriculture, planning, mining, innovation management, and land administration, and operates in Vietnam, Indonesia, Fiji, Libya, Nepal, Solomon Islands, Thailand, Philippines, Middle East, Namibia, among other countries. It has formed several subsidiary companies:

- Innovation Management, formed in 1989 with a charter to create opportunities for investment in intellectual property assets with potential to yield high returns. This has "been an effective broker between research and industry in the commercialisation of technology. In this time it has serviced 5,000 inquiries relating to all aspects of the innovation process; negotiated licence agreements on behalf of State Government agencies and assisted in generating $6.5m . . . for the State's income".[17]

- the Innovation Management subsidiary MRad, which aims to be the leading international supplier of Integrated Sensor Environment Generator and Radar Environment Generator Products by 1998 and "is well on its way to achieving that goal"responsible for innovation management;

- CMTEK, to conduct research and development to establish top level process control of growing cadmium mercury telluride (CMT) material for infrared sensing.

- AUSTRAINING, which is involved in vocational training, and which SAGRIC operates together with the SA and NSW TAFEs.[18]

- the Centre for International Education and Training, which undertakes contracts in the field of tailored training for clients.

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17 SAGRIC Annual Report 1994, p. 9.

18 Ibid.

SAGRIC's aims are:

- to operate commercially
- to provide employment
- to develop international markets for South Australian services
- to promote South Australia's technical capabilities at international level
- to provide professional development for State specialists.[19]

The second of these two is the key to interpreting SAGRIC's results. The need to provide employment has meant that SAGRIC has not always kept profit uppermost in mind as a principal objective. It has had to carry proportionately greater overheads than OPCV. It has about 35 staff in Adelaide.

C. QUEENSLAND

The Queensland Government has also affirmed its commitment to pursuing overseas project opportunities. In April and May 1994, the Trade and Investment Development Division of the Department of the Premier, Economic and Trade Development issued a Review of Policy on the Export of Government Services and Products. This review said:

> significant potential exists for services and technology exports, particularly to the Asia-Pacific Region . . . it is appropriate for Queensland Government departments to continue to engage in international business activities[20]

The Review examined the various mechanisms used by other states (e.g. OPCV and SAGRIC) to manage their international business activities, and concluded that they were inappropriate for Queensland. The Review

> concluded that none of these approaches would satisfy Queensland's particular requirements in a cost-effective manner[21]

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19 Ibid, p. 6.

20 Ibid, p. i, ii.

21 Ibid p. iii

Thus in Queensland the Premier's Department has an international projects section which co-ordinates the various technical agencies' overseas activities.

For Queensland, this is logical. Queensland agencies have less than $20m worth of overseas projects in hand at present. This low level of activity could not provide enough commercial support for a separate corporation along the lines of OPCV or SAGRIC, and there is good reason in Queensland to have the taxpayer finance the co-ordination.

D. OTHER

1. Commonwealth

In the late 1970s the Commonwealth Government established the Australian Overseas Projects Corporation as a statutory corporation. The Corporation was founded on the premise that it was desirable to have an Australian "flagship" for international project work. A national body, it was argued, would be able to co-ordinate a single Australian bid for major projects rather than the several competing bids that had been tending to volunteer and which were thought to divide and thus destroy Australia's efforts at winning such work. By adding a government imprimatur to a single Australian bid in countries where that was perceived to be important, there were high hopes for a much better win rate in international projects.

Concurrently, however, a need was seen to guard against "unfair" competition from this potentially powerful body for other Australian organisations engaged in the international project market. Stringent restrictions were placed on the new corporation to ensure that it only bid in response to requests from other Australian bodies and that it did not compete with other elements of the industry from Australia.

The Corporation won some significant work but, overall, failed to satisfy the original vision. The safeguards against competition proved so onerous for the Corporation that it lacked many of the essential freedoms necessary to succeed in this complex market. The Corporation was subsumed by, and became a division of, the Australian Trade Commission in 1986. The thinking by this stage was that the Commonwealth's role in international projects should be more as a facilitator than as a principal and, while the capacity to act as the "head contractor" for major bids remains, this has seldom if ever been used.

2. Western Australia

The Western Australian Overseas Projects Authority (WAOPA) was formed in 1978 to commercialise the technical knowledge of Western Australian government departments. WA had significant advantages in distance education, dryland farming and land titling, and it was felt that this expertise was marketable to developing countries. WAOPA was a success. In the early 1980s, as an attractive vehicle providing steady revenues, it was sold to Exim Corporation. Thereafter, its interest overseas flagged and it became moribund.

Until late 1992, WA's interest in overseas projects remained dormant. However, in that year, the then WA government established an "InterAsia Strategy", part of which was to set up a public sector body which would mainly utilise public sector skills and expertise for overseas projects. With the change of government in 1994, the WA Department of Trade and Commerce proposed a series of options in a paper popularly known as the "Son of WAOPA Report". The Department's strategy was to use the private sector to market the expertise of WA government departments overseas. This was a logical position to take given the relative smallness of the WA overseas programme.

In September 1994, the government advertised for private sector interest in this programme. Private sector firms were not required to pay a licence fee, but instead to bear all the costs of marketing. Interest from private sector firms was high, and negotiations began with the Snowy Mountains Engineering Corporation (SMEC). It was felt in WA that this was the way to insulate the state from possible legal action.

The Committee believes that this is not necessarily the appropriate way for a large state like NSW to proceed, for the reasons outlined in Part V (B) 7.

3. Northern Territory

The Northern Territory concentrates on Asia for obvious reasons. It has a Ministry of Asian Relations and Trade within the Department of Industries and Development. Within this Department, a marketing centre, Territory Perspective, is concerned with marketing the Territory's special expertise.

PART IV
HOW NSW HAS APPROACHED THE MARKET

REVENUES, EXPENDITURES, PROFITS AND LOSSES FOR THE SIXTEEN NSW AGENCIES WITH SUBSTANTIAL SERVICES EXPORTS FOR THE THREE YEARS JUNE 1992-JUNE 1995 (based on figures supplied by agencies)

	REVENUE ($000)	EXPENDITURE ($000)	PROFIT (LOSS) ($000)
RTA	5,601	2,866	2,735
TAFE	1,967	1,165	802
Agriculture	8,322	7,745	577
PPI	8,813	8,319	494
Public Works	1,104	746	358
Sydney Water	266	129	137
Board of Studies	784	680	104
Water Resources	2,682	2,539	89
Soil Conservation	1,507	1,647	(140)
Land Titles	516	761	(245)
Health	-	300	(300)
Land Information	897	1,268	(371)
State Library	228	641	(413)
Sydney Electricity	193	2,619	(2,426)
TAB	817	4,236	(3,419)
Prospect Electricity	624	4,550	(3,926)
TOTAL	**34,321**	**40,265**	**(5,944)**

Note 1: The RTA's results considerably increase the revenue and profit figures. However, unlike all the other agencies, the RTA did not actively engage in any overseas marketing on its own. Instead, this work has been done by AWA and Philips on the RTA's behalf. Because we are seeking to evaluate agencies' performance in marketing overseas, it is worth looking at the figures without the RTA. They are:

TOTAL	**28,720**	**37,399**	**(8,679)**

Note 2: Other agencies (the Opera House, Hunter Health, the Australian Museum, State Rail and Waste Recycling) also sought overseas work but the figures are too small to be included.

The Committee thanks Kevin Fennell PSM, former NSW Deputy Auditor-General, for these figures.

A. TWENTY-ONE AGENCIES: A FRAGMENTED APPROACH

1. Agencies' strategy

NSW has approached the market very differently from the two other major Australian states exporting their services. Victoria and South Australia have both decided to create a single, professional and commercial organisation to centralise the risks, to benefit from economies of scale in project management and marketing, and to be driven by the bottom line. In NSW, instead, each agency has:-

- carried out its own marketing;
- undertaken its own overseas trips;
- tried to develop its own expertise in foreign exchange management;
- established its own insurance;
- done its own project management;
- endeavoured to create its own connections with the wide range of funding sources; and
- tried to develop regional and country expertise on its own.

The duplication (or multiplication) of effort has been considerable.

A significant proportion of the agencies have not operated their overseas projects through an autonomous business, although some, notably Pacific Power International, have set such a business up, with some success. None has seriously attempted to co-ordinate with any other agency. There have been virtually no economies of scale. Large internationally- and AusAID-funded multidisciplinary projects have had to go by the board.

The results of this strategy have been mixed. Of the sixteen agencies with significant overseas activity, eight have made a profit, and eight a loss. Some agencies, notably TAFE, have performed very well. Some have performed poorly. The overall picture, however, is not one of success when compared with Victoria and South Australia.

From June 1992 to June 1995, the revenue earned by NSW was less than half that earned by Victoria and by South Australia, and, during the same period, each of the latter two states made a profit while NSW made a sizeable overall loss as colour figures 1 and 2 show.[22]

Table 3 shows the 16 agencies currently involved in one way or another and the financial results for the years 1992-1995.[23]

2. Little Transparency: Taxpayer mostly ignorant of Losses

The taxpayer has carried nearly all of these losses. The only exception were the losses incurred by the TAB, which were the funds of the racing industry (although the TAB is a government agency paying a large contribution to the government).

It would probably be fair to say that successive governments, and the taxpayer, were unaware of the extent of these losses over the State as a whole until the publication of this report. There are several reasons why the public, and the Parliament, remained in ignorance.

First, in the case of agencies which have not set out to operate commercially overseas under the umbrella of a dedicated company, there are no accounting standards or Treasury requirements currently in force which would compel separate reporting of overseas expenditures and revenues. As a result, most agencies have considerable difficulty extracting the figures for overseas operations from their general accounts the figures for overseas operations. However, they were all able to give the Committee at least a reasonable estimate of the figures for revenues and expenditures relating to overseas operations.

Nevertheless, the Committee views these figures with some caution, particularly those for expenditures. The Committee believes the real figure for expenditures to be higher in many cases than the figure given by the agencies. This is because the proportion of many overhead expenditures, like rent, secretarial assistance, and even the cost of ministers' overseas trips, which should be attributed to overseas projects, has not been

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22 NSW did not appear to receive its proper share of the AusAID market. As the NSW Director of AusAID said in hearings: "There is an impression that New South Wales is not getting its fair share of aid business. This is borne out by figures in the larger of the two documents that I have circulated, which shows that of contracts valued at more than $1 billion, New South Wales companies received $193 million and Victorian based companies received $364 million." (Minutes of Evidence 4 October 1995 p. 1).

calculated separately and included in the figures given to the Committee. In most cases, such an exercise would have been virtually impossible to carry out anyway.

The exceptions to this rule are the agencies like Pacific Power International (PPI) which operate as a business. Because these are companies which run overseas projects professionally and commercially, they are required to disclose in the notes to their financial statements the results of their overseas activities.

This leads to the clear conclusion that agencies should not run overseas operations as a sideline to the ordinary course of their core business. This will almost inevitably lead to unavailability of the true figures. Instead, a professional and commercial approach is the only one which will yield to the Parliament and the taxpayer the true accounting picture of the agency's overseas operations.

Another reason why the Parliament and the taxpayer were ignorant of the extent of the losses incurred in NSW as a whole is that some agencies (even those which told the Committee that their overseas operations were separately treated) failed to mention their own losses in their Annual Reports, with rather misleading results.

An example of this is the TAB, which, during the year when it made a loss of $1.1m on its overseas operations, described the biggest loss-maker, its operations in Hungary, in the following terms in its Annual Report:

> The offcourse betting network has been extended from 12 to 28 locations. The first 'PubTAB' style outlet opened in May 1994 in an upmarket restaurant in a Budapest suburb. This was instantly successful and plans are underway for another 11 selling locations of this type.
>
> In April 1994 a private television network was commissioned, beaming live telecasts and odds display of local racing to the betting shops. The impact on turnover and transaction levels was immediate but more importantly, the telecasts raised public awareness of local racing and the availability of the betting service off-course. As a result turnover is up 17.5% and the number of bets processed is up 8.5% on the previous year.

However, it should be pointed out that in the subsequent year, the real position was clearly set out in the TAB's Annual Report and the difficulties and losses openly stated.

Another example of how taxpayers were left uninformed of the true position was provided by a recent annual report of Sydney Electricity. In 1992-3, it incurred a loss of $423,000 on its overseas operations, which was followed by another loss of $1.02m in 1993-4. Neither of these losses was adequately brought out in the appropriate Annual Report, either in the financial statements or in the body of the report. Energy

Management International, Sydney Electricity's international arm, did not appear to have put out any financial statements or annual reports of their own, as any company operating in the private sector would have had to do. Its accounts appear to have been buried in the much larger accounts of Sydney Electricity, which makes it impossible for the Board, the Parliament or the public to know the real position relating to overseas projects.

The Committee considers procedures such as these to be regrettable.

Again, the same conclusion presents itself. The Committee believes that only a fully commercial and professional approach to overseas operations can yield the true accounting picture to the Parliament and the public, because a commercial company doing nothing but overseas work is *ipso facto* obliged to account fully in its Annual Report for all its operations.

3. Reasons for Losses

Why were these losses incurred? There were two main reasons: lateness in entering the market and, more significant, comparative lack of professionalism and commercial pressures.

(a) Lateness in entering market

Agencies in NSW began their overseas operations later than their counterparts in Victoria and South Australia. In the eighties, there was no government policy from either side encouraging and setting the limits for such work, and in many cases agencies began their overseas ventures on their own, with little professional guidance and help, and ran into heavy, and often avoidable, losses.

The lateness of NSW in entering the overseas project market represents a wide range of missed opportunities. Since 1986, the Overseas Projects Corporation of Victoria has made revenues of $110m for the state. It has proved impossible to calculate the equivalent figure for NSW, but the three-year accumulated losses of $8.7m for 1992-1995 would suggest that during the eighties, losses would have been the norm too. Thus one result of beginning so late is that NSW is incurring losses now.

However, this is by no means the only reason why NSW is incurring losses. Many times during this inquiry, the Committee has been told that profits are just around the corner, that with a little more time, the profits will come. The Committee is sceptical about this, because of the second reason why the losses have occurred. This is the lack of professionalism in certain agencies, which itself can be divided into three aspects.

(b) Lack of professionalism: little real bottom line pressure

Many agencies operating overseas would have already ceased operations if they were operating in the private sector. For example, they have:

- predicted breakeven points many years after the start of operations;
- entered markets without studying them in depth first;
- continued employing staff when programmes have failed;
- run up significant foreign currency losses;
- kept funding visitors from overseas in the often disappointed hope that contracts will eventuate from them;
- travelled numerous times to selected destinations for promotional purposes without any positive outcome;
- failed to appoint independent directors; and
- failed to evaluate their competitors properly.

All of these errors have been made in NSW by one agency or another. For example,

- Sydney Electricity projected breakeven point a full ten years after beginning operations,[24] although one of its direct competitors, the State Electricity Corporation of Victoria (International) (now sold off) was able to break even in its first year of operation and earn profits of $200,000 in its second.[25]
- The State Library's Asian Partners in Training programme had to cease operations after it found it could not compete with similar subsidised schemes offered by competitors.
- Austinfo entered the Russian "market" - potentially a lucrative one - without first determining whether anyone was willing to fund a project, and had to withdraw at a loss when it could not secure financing.

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24 Minutes of Evidence, 4 October 1995 p. 25.

25 Communication to PAC from R. Touzel, Managing Director of SECVC(I)

- The State Library continued employing staff even when their main activity (an overseas project) had failed and been wound up.

- The TAB has financed a project in Hungary whose investment return is represented in Hungarian currency. This amount cannot be hedged against adverse currency movements due to the closed nature of the Hungarian currency.

- Many agencies e.g. Health and the Land Information Centre, continue to fund overseas visitors when the hope of actually securing a project from them may be slim[26].

- Extensive travel is undertaken and protocol agreements are signed, and at least so far the results have not materialised.

- Sydney Electricity's overseas operations are run by a company called Energy Management International, which has a three-member Executive Board. The Committee is concerned at this structure and believes it unsuitable for a company operating in a competitive environment. With an independent board, it may be that the losses so far incurred by Sydney Electricity would have been minimised.

- The State Library misjudged the market for one of its overseas operations and was able to secure only nine overseas customers.

These are examples of the kind of procedures which a professional approach, driven by powerful bottom line pressures, could have avoided. Unless there are structural changes encouraging bottom line pressures, the Committee is not convinced that given time, NSW agencies would catch up with their Victorian counterparts, partly because many of these procedures are now entrenched, and partly for the next reason why these losses have occurred.

(c) Lack of professionalism: virtually no economies of scale

The OPCV benefits from considerable economies of scale. It employs people who know how to write a bid that satisfies the very different requirements of the World Bank, the Asian Development Bank, the UN and its plethora of agencies, AusAID and other funding sources. They know the procedures, they know how to write a CV, and

26 Although the Land Titles Office has successfully compelled overseas visitors to pay all the Office's costs associated with the visit.

they know what a winning bid looks like. These services are used in all of OPCV's projects.

The OPCV also centralises insurance and currency management. In insurance, it can negotiate favourable rates; in currency management, it can professionally minimise losses. These services are used to support all of OPCV's bids.

The OPCV also has, inhouse, considerable accumulated corporate knowledge of doing business in various regions and countries. This knowledge is available for all potential projects.

In other words, the OPCV benefits from considerable economies of scale.

Over the years it has developed close relationships with various funding sources, both in Australia and overseas. Through many visits (which all have to paid for out of revenue) it has been able to target and nurture the right contacts which have then borne fruit. Again, this knowledge is available for all potential projects.

Being a single focal point, the OPCV is also able to stitch together bids from many bodies for multidisciplinary projects. The inability to do this in NSW could have cost the State dearly. For example, during this inquiry, the Committee was informed about a $12m multidisciplinary AusAID project in South Africa, whose aim was to train black public servants and carry out institutional strengthening across a wide range of departments. There was no single body in NSW which could have put together a proposal, and the project had to go by the board as far as NSW as a whole was concerned, although there were many agencies in NSW which could have feasibly contributed their skills and derived financial benefit and additional experience. The OPCV, in contrast, was able to prepare a multidisciplinary bid.

The result for NSW is that it is not in a position to bid on many of the large projects offered internationally, which are frequently multidisciplinary. This is probably a major reason for the poor result achieved so far by NSW.

Furthermore, the OPCV is able to centralise the employment of agents. In one country, their successful senior agent has secured for OPCV a number of contracts in a range of disciplines. It could be argued that it is wasteful for a number of agencies each to employ their own agents, as happens in NSW.

A major benefit from OPCV's central management position is the professionalism the agency achieves in project management. The Committee was favourably impressed with OPCV's well developed project management systems, and indeed by those of

SAGRIC, during its several visits to these agencies. Virtually none of the NSW agencies reached their level of sophistication and effectiveness.

Apart from these tangible advantages of professionalism and economies of scale, there are other less obvious but still important benefits which OPCV's position as a central agency can bring. For example, through its experience accumulated over a wide range of different projects, the OPCV has developed an "instinct" for which projects to avoid and which it will have a chance at, and this has led to the elimination of costly mistakes.

All the professionalism brought to bear by OPCV has led to the minimisation of risk. The risk is all centralised in the one organisation which knows professionally how to handle it. It is not spread over a score or more of agencies which are engaging in overseas projects as a sideline, and incurring the losses that such an approach can entail.

(d) Lack of professionalism: supply-driven rather than market-driven approach

Most fundamentally, many agencies have begun by saying "We have an excellent service to offer. Where can we find a market for it?" and then by going about the world seeking a market. This is the supply-driven approach. It is not a course which most businesses in this market take. However, government agencies with a single service to sell would find this a logical approach.

Organisations in this market which are run as a business turn this upside down. They try to look at what the real and effective demand is, as expressed in projects already approved and for which funding agencies are actually seeking bidders, rather than trying to create that demand out of thin air. They then develop packages to satisfy that market demand. In other words, they are market-driven rather than supply-driven. This has been probably one of the biggest single reasons for the OPCV's success.

This may be a truism, but the fact that it has been overlooked many times in NSW means that it needs to be stressed. The Committee believes that a business-oriented approach would avoid this fundamental error.

4. Analysis of Selected Agencies' Results

As Table 3 shows, the agency with the largest revenue was Pacific Power. However, according to the figures given to the Committee, it did not earn the largest profit. This was made by the RTA. However, this report examines only the performance of those agencies which have actively sought to enter the overseas projects market. The RTA, whose overseas activities are carried out on its behalf by AWA and Philips, is not actively engaged itself. This is why it is not been included in this analysis. However, this is not to deny the appropriateness of the original decision to award the overseas marketing work to AWA and Philips, a decision on which the RTA should be commended. After the RTA, the largest profit was made by TAFE. The largest losses were incurred by Prospect Electricity, the TAB and Sydney Electricity.

The ratio of revenue to profits for the most profitable agency, TAFE, was 5:2. This compares very well indeed with those of a significant competitor, IDP, which is 35:2. It also compares well with private sector companies in general which operate overseas.

This excellent result possibly reflects the unique position of education in the international projects market. Competition is more muted in education simply because the international competitors present in other markets (e.g. German, French, Scandinavian engineering firms) are not present. Competition is limited to English-speaking organisations. In addition, American and British competitors suffer from high costs and distance from the Asian market. Thus the natural advantages of Australian education put TAFE in a uniquely favourable position. This is of course not to deny the good management of TAFE's overseas operations.

It should also be pointed out that education is the OPCV's most profitable sector.

The next most profitable, Agriculture, has been involved overseas for thirty years. However, their ratio of revenue to profits was 1:40. This reflects the approach taken by Agriculture to their overseas operations, which they view principally as a training ground for staff.

The biggest loss maker was Prospect Electricity. These losses were incurred mainly as a result of developing and attempting to sell Prospect's customer information system abroad. Events proved that modifications to the programme were necessary to achieve overseas sales but were not economically feasible or technically sustainable in the long term.

The next biggest loss maker was TAB, which ventured into the Hungarian market only to find that the Government was changing the law on betting, making large losses inevitable. No hedging was possible on these amounts due to the closed nature of the Hungarian currency.

PART V: THE PREFERRED FUTURE APPROACH TO THE WORLD MARKET FOR NSW

A. COMMERCIAL RATHER THAN BUREAUCRATIC SOLUTION: A CORPORATION FOR NSW

Parts I and IV of this report have shown that NSW has performed poorly in this market relative to other Australian states. The problems can be summarised as: patchy commercialism, limited professionalism, virtually no coordination.

After considerable reflection over the many months of this inquiry, the Committee has come to the view that fundamentally, the possible solutions to the problems can be reduced to three:

1. **Through the public service**
2. **Through a licensed private sector corporation**
3. **Through a government corporation**

These options are examined in turn below.

1. Through the public service: the bureaucratically acceptable solution

The easiest solution by far would be to address the problem through the public service. This would involve the creation of another unit, probably in the Department of State Development, to co-ordinate agencies' existing activities, and letting the agencies go on doing what they have been doing. This unit could arrange insurance, collect data, help in preparing bids, provide advice on project management, and help to seek markets.

This solution would have the advantage of not disturbing the status quo. Many of the agencies, having established some kind of overseas activities, are reluctant to let them go. Frequently during the course of this inquiry the Committee was reminded of how hard it is for public service agencies to let go of an activity once it has begun and acquired its own staff, culture, interests, justifications and momentum.

This solution would therefore be bureaucratically the most acceptable one. However, despite its administrative attractions, the Committee firmly opposes the bureaucratic solution and recommends against its adoption.

The main reason for this is precisely that the solution is an extension of the status quo, where the market has been inappropriately handled by the bureaucracy. Overall, the status quo has led to losses and inefficiencies. The problem has been the bureaucratic approach, but this option leaves the solution to the bureaucracy. It introduces no commercial pressures into the market, yet these are needed to produce professionalism, higher revenue and profits.

2. Through a licensed private sector corporation

There is no doubt that a commercial approach, as opposed to a public service approach, is the most economical, efficient and effective one to follow in this market. There are two ways the commercial approach could be adopted: through the private sector, or through a government corporation.

The Committee explored in depth the possibility of the private sector being responsible for marketing and managing the overseas operations of NSW government entities. Several suggestions were made to the Committee in this context: that one of the existing private sector firms operating in this market should be invited to handle all these projects for the NSW Government, for a fee; that one of the existing private sector firms should buy the right to market and manage such services; or that various outside investors should be sought to set up a new private company which would then market and manage NSW government bodies' overseas projects.

The Committee carefully evaluated all these suggestions, inviting for discussions various firms already operating in this market, and others which might have an interest in making such an investment. However, after considerable debate and reflection, the Committee formed the view that NSW government bodies' overseas operations should not be marketed and managed by a private sector body.

The Committee's reasons were the following.

Many times during the course of this inquiry, the Committee was told how vital the government crest on the card was in securing access to overseas government decision-makers. Not only is access much easier, further communication is enhanced as well. Governments generally feel more comfortable and less wary dealing with other governments.

The private sector benefits as well from this privileged access. If a Government agency can open the door, the private sector can get its foot in afterwards in conjunction with that Government agency. Later, after the project has begun, the private sector firm will have established its contacts in that country and can use them to further its own interests.

Another reason why a government agency is preferable to a private sector firm is that the accusation of a "tilted playing field", where one player is favoured over others, is thereby avoided. If one private sector firm manages the access of NSW agencies to the overseas project market, other private sector competitor firms could legitimately complain that their access to the market has thereby been severely restricted. Government involvement facilitates a level playing field in this respect.

There could also be a concern that if a private sector firm manages the access of NSW agencies, it will inevitably further its own interests ahead of those of the State. Most private sector firms operating in this market have some similar skills to those obtainable from State agencies, and they could well (and indeed should) seek to secure contracts for their own staff in preference to giving the job to the state agency.

In short, if the private sector firm is experienced enough to carry out this role, it will probably have serious conflicts of interest; if it is not experienced enough, it should not be carrying out this role at all.

Furthermore, it is not really necessary for a large State like NSW to go to a private sector firm to manage its access to the overseas project market. A large state like NSW, with a big public sector and a wide range of skills to offer, has the resources to support its own project management team without having to have recourse to outsiders. Smaller States like Western Australia are in a different position.

Another reason why a government body should be managing this access is that it will mostly have better access to its primary source of expertise, that is the technical state agencies themselves than a private sector firm would. Intragovernment communications are often in practice far easier than those between the private sector and government agencies.

There is also a logic in having the state reap as many benefits as possible from the huge investment it has made in developing public sector skills. If a private sector firm manages access to overseas markets, it will derive some of the returns on an investment it has not made itself.

Having said all this, there are also a few cases where the private sector can manage access better than a government agency can. A case in point is the marketing of the RTA's SCATS traffic control system, which is managed by Philips and AWA, with the RTA deriving licence fees from successful sales, and Philips and AWA being able to sell their hardware.

These cases are not common enough, however, to constitute a pattern, and the Committee believes that the range of reasons set out above supporting government involvement in marketing and managing overseas projects is robust and convincing.

3. Through a government corporation

Based on the points in the subsection above, the Committee thus came ultimately to the view that the best way to pursue economy, efficiency and effectiveness in this market is through a commercial approach implemented by a government corporation.

In competitive markets, commercial pressures will normally create efficiencies. That this is true of the government services export market has been amply proved by the experience of Victoria and South Australia. A corporation which is compelled to at least break even, and preferably make a profit, will:

- operate commercially with no cross-subsidies and fully transparent accounting;
- benefit from economies of scale in travel and promotional expenditure;
- make a more rigorous assessment of the need for travel and promotional expenditure;
- explore markets professionally;
- avoid the very considerable costs of creating a service or a product for which there is no effective demand abroad;
- seek to make profits as early as possible;
- limit staff to those commercially justifiable;
- evaluate competitors in depth;
- organise insurance economically;
- run a professional currency management operation; and
- report to independent directors.

In short, it will run professionally, competently and commercially.

It will benefit from the access provided by the crest on the card; it will avoid the problem of the tilted playing field, which would occur if one private sector firm handled all the overseas operations of NSW government bodies; it will avoid conflicts of interest between the private sector and public sector entities operating in the same market; it will ensure that the State retains for itself the maximum possible revenues and profits from these operations, and it will ensure easy communications with government agency suppliers of services.

Thus the Government Corporation appears to the Committee to be unequivocally the best option for the marketing and managing of NSW government agencies' expertise.

It is the policy of the current New South Wales Government to set up an International Projects Corporation of New South Wales. This policy has been set out in major publicly-issued policy statements and reviewed in the press. The present report expresses bipartisan Public Accounts Committee endorsement for the policy of establishing the IPC.

B. TWELVE ISSUES FOR THE NEW CORPORATION

Given that the best solution is the commercial rather than the bureaucratic one, and that a government corporation is the best expression for NSW of that commercial solution, there still remain a number of issues relating to the objectives, funding, ownership, legal structure, and strategy for that corporation which need to be explored. The following section discusses twelve of the major issues which have arisen during this inquiry.

1. Legal Structure: Freedom with Accountability

There are several possible models for the legal structure

(a) An unlisted public company limited by guarantee
(b) An unlisted public company limited by shares and guarantee
(c) A statutory corporation
(d) A State-Owned Corporation
(e) Separate legislation specially designed for the IPC itself
(f) A Trust structure

These are discussed in turn below:-

(a) Unlisted company limited by guarantee

This structure is suitable mainly for non-profit organisations such as clubs and altruistic bodies, which have no need for fixed capital. The unlisted company limited by guarantee has no capital; if it is wound up, the members must contribute the amount which they have guaranteed. It is difficult for such companies to obtain funds commercially. However, these companies are usually not expected to pay tax on the grounds that they are not normally supposed to be profitable. If they make profits, they will be taxed.

It does not appear to be a suitable structure for a corporation whose aim is to make profits.

(b) Unlisted company limited by shares and guarantee

Companies moved to this structure when they wanted to access fixed capital and to obtain tax benefits. Limited liability is guaranteed. This is how OPCV is at present set up. But in both NSW and Victoria, the existence of the *State-Owned Enterprises Act* of Victoria and the *State-Owned Corporations Act* 1989 of NSW make this structure unnecessary for a government-owned business.

(c) A statutory corporation

A statutory corporation requires a specific act of Parliament. Its Board is appointed by the minister, and the minister can issue directions to the staff. This has potential for political interference in the workings of the IPC. The statutory corporation is also slow to set up. For all these reasons, the Committee does not favour this option either.

(d) A State-Owned Corporation (SOC)

There are two types of SOCs:

(i) the Company SOC, which is subject to Companies Law
(ii) the Statutory SOC, which is not.

The latter is the preferred model, because:-

- It combines relative (but not absolute) freedom of operation with accountability to Parliament.
- It can benefit from state government tax exemptions.
- The government is insulated from liability suits as long as it has no say in how the business is run.
- The SOC Act already exists, making it relatively quick and easy to set up the IPC under its provisions.

The State-Owned Corporation Act is familiar and does not have to be explained as a special case.

The Committee sought legal advice on the advantages and disadvantages of this structure. The relevant parts of this advice are reproduced below:

STATE OWNED CORPORATION

The *State Owned Corporations Act 1989* (NSW) commenced in September 1989. The purpose of this legislation was stated to be:

> to establish a framework for the corporatisation of selected government business enterprises. Corporatisation is a strategy aimed at improving the level of efficiency and accountability in government business enterprises for the benefit of consumers and taxpayers. ...

> Stated owned corporations will be under the same regulatory regime as companies in the private sector. ... Also, Stated owned corporations will have their performance measured in the same way as companies in the private sector. ... This will impose on State owned corporations the same incentives and sanctions which apply to companies in the private sector.[27]

It is important to note that the *SOC Act* has, from 1 July 1995, been amended by the *State owned Corporations Amendment Act 1995.*

The main purpose of this amending legislation is to establish a second model for the corporatisation of government business entities, namely statutory SOCs. The existing model of SOC, is now called 'company SOCs'. Essentially, statutory SOCs are statutory corporations (not subject to the *Corporations Law)* and company SOCs operate as State owned public companies (as they did before these amendments to the *SOC Act*).

The (eligible) shareholders of a company SOC are the Treasurer and 4 or more other Ministers as nominated by the Premier (the 'eligible Ministers' - see section 3 of the *SOC Act*). The voting shareholders are the Treasurer and one other nominated eligible Minister (section 3). Also, the two shareholders of a statutory SOC are to be the Treasurer and another Minister nominated by the Premier as a voting shareholder (see section 20H).

In terms of risk exposure, particular benefits for an international projects corporation ('IPC') based on the model of corporatisation for a company SOC under the SOC Act would include:-

- liability would be limited, and a company SOC is not and does not represent the State (except by express agreement with the voting shareholders of the corporation), and cannot render the State liable for any debts, liabilities or obligations of the corporation or its subsidiaries (see section 9);

- the obligations of a company SOC are not guaranteed by the State of NSW, except t on the extent that the board of the corporation and voting shareholders agree in writing (section 16).

For similar provisions relating to statutory SOCs, see sections 20F and 20U of the SOC Act.

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[27] NSWPD, 2.8.89, p. 9139

In addition, in the new competition environment, it may be assumed that it would be advantageous for an IPC, as a State owned corporation, to be treated as far as possible in a similar manner as a company in the private sector. For example, a company SOC is exposed to the federal regulatory regimes of the *Corporations Law* and the *Trade Practices Act 1974* (Cth).

Furthermore, the *SOC Act* provides for the payment of tax equivalents to the Treasurer (for payment into the Consolidated Fund) being such amounts as the Tax Assessor determines to be equivalent to the amounts that would be payable by the corporation if it were liable to pay taxes under the law of the Commonwealth (see sections 15 and 20T). In this way, a SOC does not have a federal tax advantage over competing companies in the private sector. However, sections 17 and 20V do provide for certain exemptions for a SOC from State taxes.

Disadvantages of the models under the *SOC Act* may include:

- the level of control of the activities of a SOC by the voting shareholders (which includes the Treasurer - see for example, in relation to a company SOC, sections 12-13, 16 and 18-20);
- the social responsibility objective (see sections 8 and 20E); and
- the requirement that a SOC performs activities of a non-commercial nature if directed by a Minister (with the approval of the Treasurer - see sections 11 and 20N).

Further features of the *SOC Act* that may be considered in relation to an IPC include:

- the board of directors of a SOC is accountable to the voting shareholders as set out in Part 4 of the *SOC Act* and in the memorandum and articles of association of the corporation (see sections 10 and 20J); and
- in relation to statutory SOCs, the portfolio Minister (see section 20I) has the power to notify the board of public sector policies (which the board must ensure are carried out) and to give (with the approval of the Treasurer) directions to the board in the public interest. These sections evidence a greater level of ministerial control over statutory SOCs than company SOCs.

Separate legislation

The option of establishing an IPC under its own legislation would enable the benefits of the *SOC Act* (set out above) to be adopted and adapted. This option would also permit required measures for accountability and the portfolio responsibility to be tailored to the very particular commercial needs of such an agency.

Although it leaned towards the SOC model, the Committee nevertheless had some reservations about it, because of the disadvantages outlined above, which mainly relate to potential political interference with commercial operations. The Committee notes that the early freedom of the OPCV, which operated as a company limited by guarantee with very limited supervision from ministers or the Victorian Treasury, was a major factor in its success, and is concerned that the SOC model might still have potential for political and bureaucratic interference.

However, there are the strong competing claims of accountability, and the Committee is very mindful of these. **For this reason, therefore, the Committee on balance favours the SOC model.**

For this reason, too, it prefers the SOC model to a trust structure.

The accountability of the Corporation to the Parliament and the public will be achieved because its responsible Minister is a member of the Parliament. The Public Accounts Committee will also have the right to examine its accounts.

2. What type of services should the corporation handle?

The OPCV handles the full range of services:

- marketing
- collecting and centralising intelligence on markets, projects, funding sources, countries, regions, administrative practices
- preparing bids
- putting consortia together
- insurance
- foreign currency management
- recruitment of subcontractors, both individuals and firms
- total project management, including scheduling, relations with governments, and a wide range of related activities.

Everything is provided in the one place, by the one organisation whose sole business this is, except of course the provision of the technical expertise, which is obtained from the agencies whose core business *that* is. The agencies do nothing else except provide their own technical expertise. In other words, they stick to their core business and leave everything else to the experts.

SAGRIC is the same. It provides the full range of marketing services, including agents and offices overseas, employing professional marketers and project managers.

This model has proved its success. The financial returns of both organisations speak for themselves.

However, the model does not find favour with NSW agencies. Some opposed the IPC as a full-service model, doing what OPCV does, which is basically making commercial judgements marketing and project management.

The Land Information Centre, for example, did not consider it should get into marketing, and the Department of Agriculture did not consider it should get into project management.

The Land Information Centre said in its response to the questionnaire[28]:

> The Centre is of the view that a central agency would be able to co-ordinate the activities of the public sector in partnership with the private sector for discrete projects with the bilateral/multilateral loan/aid agencies and maximise the return to the people of NSW commensurate with the size and quality of its infrastructure.
>
> The central agency could act as a focus for private sector contact with the public sector.
>
> It could also assist new agencies to become involved in international marketing through the knowledge base existing within experienced agencies.
>
> One of the great difficulties for inner-sector budget organisations is the use of profits from a project to seed another project. The Central agency could facilitate the provision of seed capital to project initiatives in a controlled fashion and to strict protocols.
>
> *It should not act as a marketing front end for individual agencies as it would not have the required knowledge base.* [Emphasis added]

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28 31 July 1995.

The Department of Agriculture said in its reply to the questionnaire[29]:

> A central body could act as a focus for contact from private sector or non NSW government agencies and between NSW public sector bodies.
>
> It should be a facilitatory body between public and private sectors . . . *it should not seek involvement in project management.* [Emphasis added]

Sydney Electricity said:

> **Mr MITCHELL**: . . we strongly believe that our success in dealing with our customers comes from our dealing directly with them. . . .It is the direct dealing, the direct relationship that we have with our customers that makes for success. I guess my response when I was asked that question initially was that if having an IPC was going to interpose something between me and my customers then I would have some concerns about that.
>
> However, . . . we have certainly found, and I know others in the business have found, that there are supporting services, back-end rather than front-end services, if you like, on which from time to time we could all draw and probably would be prepared to pay for them, which may be useful to us. I would not say I was categorically opposed to an IPC, it just depends on which [sic] it does. I think it could be very useful to us if it was the right sort of support. I have some quite serious difficulties with it taking the lead for me because I think I need to interact with my customers, not someone in between me and the customer.[30]

While acknowledging these views, the Committee is more convinced by the success already demonstrated objectively by the full service model, as exemplified by the OPCV and SAGRIC. Some of the agencies most energetically opposing the full service model are not able to demonstrate similar success, as can be seen from Table 3.

A partial service model providing back-end rather than front-end services would have the great advantage of not disturbing the status quo. It would leave agencies free to continue with marketing, project management and the like, which is not their core business (see Part I B(2) for a discussion on the "core business" issue). There would be no objections from agencies to this course of action.

But it would essentially mean the perpetuation of what has amounted to a fragmented and, broadly, a failed system.

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29 Undated, received 10 July 1995.

30 Minutes of Evidence, 4 October 1995 p. 27

Back-end services could just as well be provided by a bureaucratic unit inside the Department of State Development. Under this system, the agencies would continue what they are doing, and would get extra help (provision of information on funding sources, country and regional data, assistance in preparing bids) from the unit in the Department of State Development. However, as outlined in the preceding section (Part 5 A), there is far less advantage in involving the public service than in operating a fully commercial corporation where all these activities are carried out in the one place.

There is no logical argument why overseas marketing and project management should be left to agencies which were never intended to carry out those functions, and which have had to learn them on the job, instead of being given to professionals who can then tap into the agency's technical expertise, or bring it in on secondment, or on leave without pay, as happens in OPCV and SAGRIC.

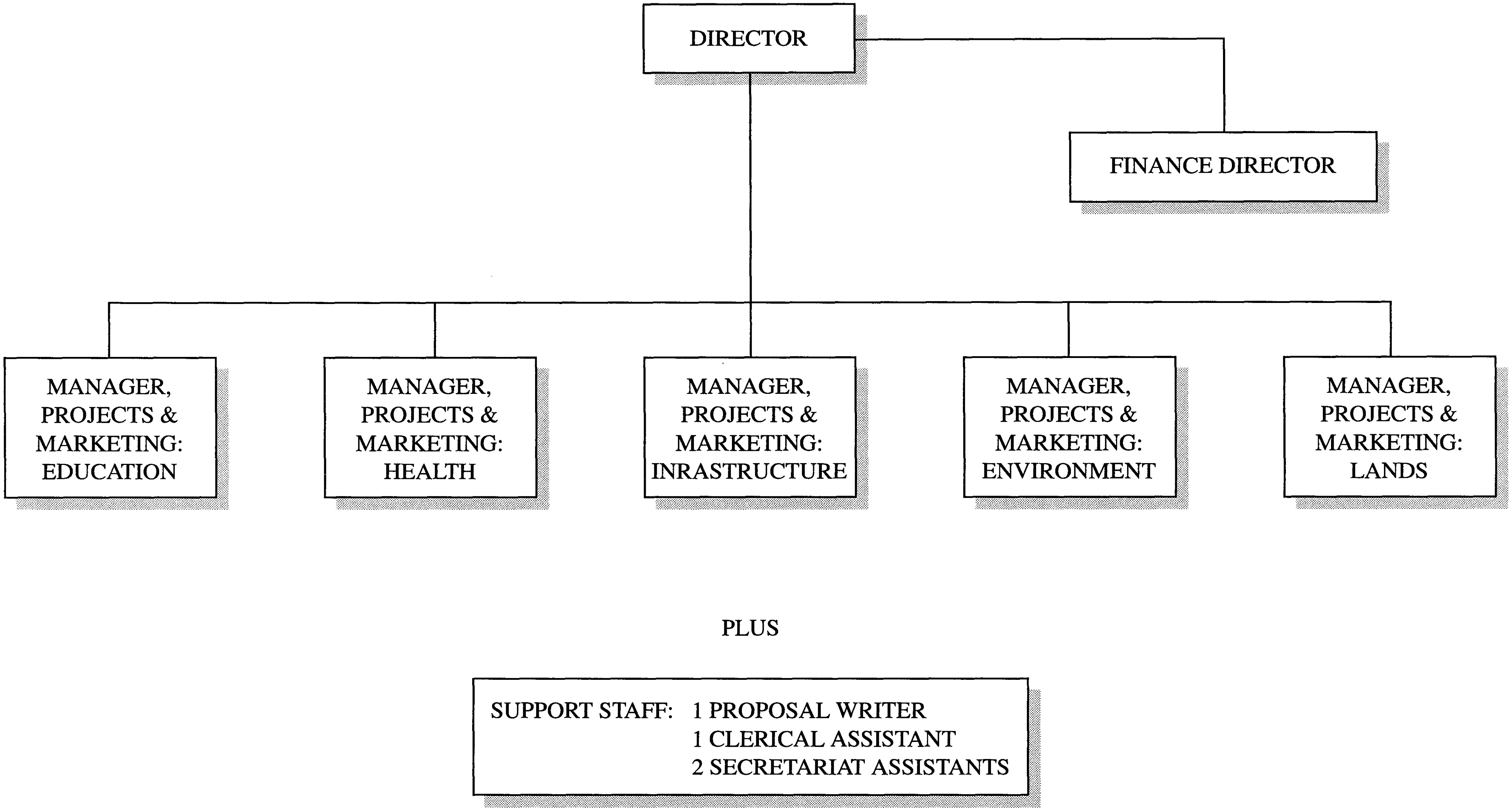
The Committee is not convinced that the partial service model will be the most economical, efficient and effective one for the economy of NSW and recommends against its adoption.

3. Structure and Staffing of the IPC

A priority for the IPC should be to operate with the very minimum of staff consistent with efficiency. The staffing structure could be something like the one outlined in the accompanying chart. However, funding should be proportionate to the agreed optimum level of staff.

Whether this staff should be drawn from existing operations run by agencies, or whether new people should be appointed, should be a matter for the new Managing Director. There are many staff from agencies currently running overseas projects who should be redeployed inside their agencies once the IPC is formed, but which individuals should be redeployed should be decided in consultation with agencies once the IPC's Managing Director is appointed.

Similarly, some agencies may send their staff to work in the IPC on secondment, or may pay for them to work in the IPC. This is a common practice in both the OPCV and SAGRIC. Again, the new Managing Director should decide, in consultation with agencies, who should be on the team and under what conditions.


DIRECTOR
FINANCE DIRECTOR
MANAGER, PROJECTS & MARKETING: EDUCATION
MANAGER, PROJECTS & MARKETING: HEALTH
MANAGER, PROJECTS & MARKETING: INRASTRUCTURE
MANAGER, PROJECTS & MARKETING: ENVIRONMENT
MANAGER, PROJECTS & MARKETING: LANDS
PLUS
SUPPORT STAFF: 1 PROPOSAL WRITER
1 CLERICAL ASSISTANT
2 SECRETARIAT ASSISTANTS

Senior management should be on contracts, preferably for at least three years, with provision for redundancy should the need arise. In the extremely competitive market of overseas projects, it will take time for the IPC to establish itself and set a track record. It took the OPCV two years to make a profit and the IPC will have to work in a much more difficult environment than the OPCV had to face. Therefore more time than two years should be allowed to the IPC and its staff to meet the objective of making a profit.

The Board should be small, with no more than five directors. It may be considered appropriate for some of the directors (also the Chairperson) to have successful commercial experience operating overseas. None of them should be either actively or passively engaged in a competing enterprise.

The Committee considers that the Chief Executive of the Corporation should not be a member of the Board.

4. Funding for the IPC

The IPC needs two types of financial resources:-

(a) Initial equity to cover initial costs (finance for guarantees, performance bonds required by international lending agencies and advance payments)

(b) Running costs

They are dealt with in turn below.

(a) Initial equity

For the first period of 2 to 3 years, it is not likely that the IPC will earn very substantial revenues. It will incur costs (salaries, etc). These costs will have to be covered by an initial injection of equity. This should be of the order of \$2m to \$2½m (OPCV received a capital injection of \$1½m in 1985).

There are several possible options for initial equity. The Committee lists them in its order of preference:

(i) Provision of equity seed money as a grant from government.
(ii) Provision of an advance repayable from the Treasury
(iii) Provision of a loan from Treasury Corporation.
(iv) Provision of part of the seed capital from private sources
(v) Provision of 100% of seed capital from private sources.

(vi) Subscription fees from agencies payable upfront.

These are discussed in turn below:-

(i) Provision of equity seed money as a grant from government

The Committee prefers this for the following reasons:

- It is the simplest, cleanest way .
- It is completely compatible with the IPC's status as a SOC.
- It demonstrates to potential customers in the most powerful way possible the government's commitment to the IPC.
- It allows the IPC more operational freedom in the early years, without the "strangling" that comes from having to pay back loans in early, loss-making period. It thus allows the IPC to move sooner to job creation and revenue earning.

The Committee expects that the IPC will be successful, and that dividends will be paid from operational profits.

(ii) Provision of an advance repayable from the Treasury

This is a possible option. Its advantages are:

- The terms of the advance can be tailored by agreement.
- The government and the taxpayer are probably more assured that the money will be repaid than if a simple injection of equity seed money were provided.
- It would look to outside observers as though the IPC were being treated as a business like any other in the private sector.

However, it is possible that a loan, which this effectively is, could hamstring the IPC in its early loss-making years.

(iii) Provision of a loan from Treasury Corporation

This is probably less desirable than an advance repayable direct from the Treasury, because:

- It introduces another player into the operations of the IPC.
- Another board may interfere with the IPC's operations.

(iv) and (v) Provision of all or part funds from private sources.

The advantages of this include:-

- Private ownership often means better management than public.
- Answerability to a private sector board will create a powerful incentive for IPC managers to perform well.

The disadvantages include:-

- Any private sector owner(s) would run the IPC in their own interest, which would not necessarily be that of the State as a whole. The potential for conflict of interest would be very high.
- The IPC would risk getting "swallowed up" by any private sector owner.

(vi) Subscription Fees from Agencies Upfront

The resistance from agencies to paying such fees would be considerable and it would be difficult to determine who should pay how much.

(b) Running Costs

After the initial three years, these would have to be found from revenues.

5. Should working through the IPC be compulsory for all agencies and for all types of projects?

This was one of the most challenging issues in this inquiry. In Victoria and South Australia, virtually none of the agencies had exported its services before the OPCV and SAGRIC respectively were set up. This made those corporations' task easy. In contrast, in NSW a number of agencies have begun moving into this area on their own initiative. They have assumed that overseas projects are a legitimate field for agency operation and now have a de facto presence. Without much background, many have now begun making business and commercial judgements on overseas project work instead of limiting themselves to providing technical expertise.

Many of them are unwilling to cede their ground to the International Projects Corporation. They are not willing to accept a full-service model, but only one which provides back-end services[31].

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31 Pacific Power International was a case in point:

> **Mr GRAHAM**: From our customer's point of view, the large, government-owned Asian utilities take enormous comfort from the fact that they are dealing with a large, integrated, government-owned operation in Australia. The direct relationship is the most significant thing. To impose an organisation between Pacific Power or the industry here and the customers would create some significant difficulties and greatly reduce our ability to win work.

Many other agencies, fearing that they would be forced at all times to work through the IPC, made similar points at hearings. These included TAFE:

> **Ms STEWART**: One of the aspects of dealing in the market is that the client needs to know where to go. The one-stop shop, the customer service focus, seems to be the one preferred by the customer. There is a need to consider the benefits, the advantages and the disadvantages of promoting New South Wales as a one-stop shop versus an institution like TAFE New South Wales. For example, perhaps international markets see TAFE New South Wales as a provider and a key player in the vocational education field and perhaps do not necessarily see New South Wales as a State but as a body

Sydney Electricity:

> **Mr GLACHAN**: I believe that you feel that an international project corporation in New South Wales would not really suit your purposes. Why is that?
>
> **Mr MITCHELL**: It depends on how an international corporation is conceived, I guess. I think my response to it was that we strongly believe that our success in dealing with our customers comes from our dealing directly with them. Substantially it is utility to utility, or utility to developer. It is the direct dealing, the direct relationship that we have with our customers that makes for success. I guess my response when I was asked that question initially was that if having an IPC was going to interpose something between me and my customers then I would have some concerns about that. When I look at the experience that others have had, for example, the Victorian experience where the electricity supply industry is separate from OPCV, they would share that view, I think

and Water Resources:

> **Mr URQUHART**: A point I would like to make is that within Water Resources we are enthusiastic to keep going the way we are. We believe that it is good for the department

However, as pointed out above, the Committee considers that the model which has the potential to earn the greatest benefits for NSW is the full-service model, that is, the one which leaves all business and commercial decisions up to the corporation. This is a model whose success has been proved in Victoria and South Australia.

There is not a great deal of logic in allowing all agencies to choose, in all their projects, whether to use the IPC or not. In that case, what will very likely happen is that agencies will simply go on doing what they have been doing up to now, that is, marketing and managing all their own overseas operations, in other words, taking commercial judgements on overseas operations, and will leave to the IPC only the unprofitable crumbs like taking care of visitors and accumulation of data.

Under these conditions, the IPC is likely to fail, professional though its staff may be. The end result will be a continuation of the largely unsuccessful status quo, and very little benefit for NSW.

The model envisaged by the Committee is different. It is based on the principle of comparative advantage and is designed to ensure the best of both worlds, by combining the IPCs commercial experience and judgement in overseas projects with the technical excellence of the agencies, in a partnership which the Committee believes should ensure NSW leadership in overseas projects.

Operations should be undertaken jointly by the specialised agency and the IPC. The IPC should be responsible for all commercial judgements on the viability and profitability of a project opportunity, together with its "winnability", and similar commercial judgements. It should also be responsible for all logistical and financial arrangements regarding bid preparation and project management. The technical

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for us to keep doing so, and I can talk about reasons if you would like. Having said that, I think there is an appropriate role for an international projects corporation as well because such a unit can add value to the State's overseas business activities by packaging up projects of a scale, size and complexity that probably individual departments cannot. I think there could be an appropriate synergy between our level of operations and an IPC level of operations, but I think they would be on a different scale.

Mr TRIPODI: Are there any conditions under which you would resist the formation of an IPC?

Mr URQUHART: If it added materially to my overhead costs I would resist it strenuously...

agencies, for their part, should be responsible for assessing both the technical viability of the opportunity, their own technical capability and their resource availability to take advantage of the opportunity.

The IPC should also be responsible for operating a comprehensive market intelligence system, for adding critical appraisal to raw information and producing proper evaluation of opportunities. In addition it should be responsible for whatever early general promotion is deemed appropriate, and should be responsible for prosecuting qualified opportunities, in concert with the appropriate specialised agency.

Far from interposing "another layer between me and my customers", it will be interposing an informed and professional commercial judgement, professional marketing, and, very important, professional project management.

The IPC will enrich the agencies' technical judgement with its professional business approach.

In other words, the technical agency should handle technical matters, and the IPC non-technical business and management matters. It therefore follows that the IPC should be closely involved with every project opportunity, because its business judgement will be indispensable.

After considerable discussion, therefore, the Committee formed the firm view that:

- there should be no exemptions from working through the IPC for any agencies operating any overseas activities, whatever the source of the funding, unless, after negotiations, the Chief Executive of the IPC grants an exemption on the basis that such an exemption would be in the best interests of the State as a whole.

- if the agency disagrees with the Chief Executive, it should have the right to appeal to the Board, and to receive a response within four weeks.

- Exemptions may be granted if the agency is working with OPCV or SAGRIC.

- Agencies should not embark on any overseas project opportunities unless the IPC is involved from the start. They should not, for example, undertake travel unless the IPC is in agreement.

It is not surprising that agencies are without exception opposed to an OPCV-style model. Clearly it would usurp their existing functions and there is a strong element of self-interest in their resistance. The Committee would be more convinced of the validity of the objections had the agencies been more successful in running their own operations, and had they informed themselves of how benchmark operations are run.

In conclusion the Committee stresses the cooperative nature of the model it envisages, with each party doing what it does best and exploiting to the full its comparative advantage.

6. Primary Objective: Revenue or Profit?

There are advantages and disadvantages to setting either revenue or profit as the primary objective of an agency.

The advantage of setting revenue as the primary target is that objectives can be satisfied which are not, strictly speaking, the commercial ones proper to the corporation itself. These are wider economic and social objectives, such as maximising the number of jobs created, exposing the state to international competition, improving productivity in the state, increasing downstream procurement opportunities, boosting the private sector and so on. Some of these objectives may be close to the heart of governments and they may seek to steer the Corporation in that direction. They may or may not be considered quite legitimate for a government corporation.

An agency may also have completely commercial reasons for going for revenue rather than profits. For example, it may be seeking to increase its market share for the longer term and making a commercial decision to do that by cutting margins. This could especially be the case in the cut-throat international projects market, where a slight cost advantage can make the difference between winning the bid or losing out.

One disadvantage of setting revenue as the primary target is that in the end this will erode the competitive position of the agency. As the Deloittes report on the OPCV says:

> It is also the consultants' view, although this is not shared by the Board, that OPCV should have clear and commercially acceptable profit targets, and that these, rather than revenue targets, should drive the business and support management discipline. This view is based on a concern that giving primacy to revenue growth will result in poor financial management among marketers and project managers, who will be rewarded for sales rather than realised profits. In time, this will erode the competitive position of OPCV. This matter, together with a range of other management issues, should be reviewed and addressed by the board, in consultation with the Minister.[32]

32 P. 56

An advantage of going for profit rather than just revenue is that the profits an organisation can earn can be put in a reserve fund which will then allow it to "meet some of the Government's broader objectives about benefit to the State".[33]

As a matter of fact, between 1988 and 1993, OPCV achieved a consistent ratio of Operating Profit to Project Income of around 7.5%. This is consistent with industry norms. It is now in a strong position and can afford to stress profit alone.

In contrast, SAGRIC has consistently opted for revenue growth rather than profit.

There is a strong case to be made for the new Corporation in NSW to adopt revenue maximisation in its early years, say the first three or so, when it will be battling to find its place in the market and build up a track record. In other words, an argument can be made that it should go for low profit margins in the early years. After that, however, with a good track record to point to, it should be in a stronger position and should probably be able to change strategy and stress profits. A caution should be sounded however, in that Governments should not seek to impose on the new Corporation objectives which the Board feels are inappropriate commercially. These could involve forcing the Corporation to handle visitors, or hire individuals, or work with certain agencies, or any number of procedures which could compromise commercial benefit.

7. Relations with Private Sector

Relations with the private sector have proved to be a double-edged sword for all participants in this market. On the one hand, the OPCV and SAGRIC have been in competition with a number of engineering and project management firms on many projects; on the other, on many *other* projects, OPCV, SAGRIC and the same private sector firms have joined together to form bidding consortia. In addition, the private sector has benefited from the privileged access of the government corporations. The lines are fluid and constantly changing.

Furthermore, the international project scene in Australia is turbulent and rife with allegations made by various parties against competitors who are erstwhile partners, and even against partners who are erstwhile competitors.

It is not a static or always tranquil scene. The private sector's relations with government are frequently uncomfortable. This should be borne in mind when reading this section.

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[33] Mr M. Lisle-Williams, Minutes of Evidence, 4 October 1995, p. 12.

The issue of relations with the private sector can be broken down into three parts:

(a) ***Unfair competition with the private sector***
(b) ***Linking up with the private sector: the corporation's need for a track record***
(c) ***Eventual privatisation?***

They are dealt with separately below

(a) Unfair competition with the private sector

Many times during this inquiry, the Committee received complaints from private sector competitors that a government corporation would undercut them because it could benefit from government subsidies. Typical of these complaints was the statement made in evidence by Mr Ian Tuck, Managing Director ACIL Australia Pty Ltd of Victoria:

> **Mr TUCK**: It is . . clear to us that OPCV does not have to meet the full range costs that we do in the private sector and it can operate virtually on a break-even basis.[34]

and by Mr Jack Boniface, Chairman and Chief Executive Officer, Snowy Mountains Engineering Corporation (SMEC):

> **Mr BONIFACE**: If NSW starts to run its own private aid program where the NSW Government departments are subsidising the organisation, we would have a lot of objection. . . .
>
> **COMMITTEE:** Does that mean that on every occasion OPCV beats you to the contract they are subsidising?
>
> **Mr BONIFACE**: Yes, I believe so.[35]

The Committee was concerned at these allegations and sought to find the truth. It asked a disinterested observer, Mr Michael Lisle-Williams, who had carried out a detailed study of the OPCV about the matter. He answered:

> **Dr LISLE-WILLIAMS:** We conducted a review of project costs, proposals and finances and we found no evidence to support that type of allegation. It is clearly the case that in some instance OPCV, like it competitors, agreed to a price that was sailing a little close to the wind, and it could not have afforded to operate on that basis on a

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34 Minutes of Evidence, 4 October 1995, p. 18

35 Minutes of Evidence, 4 October 1995, pp. 69-70.

whole range of its projects . . .[but] no evidence suggests that, taken as a whole, OPCV has been paying government departments less than the cost of employment and making costings which were less than they should have been for the projects.

COMMITTEE: Therefore the taxpayers have not been subsidising its activities.

Dr LISLE-WILLIAMS: There is no evidence that it is being subsidised by taxpayers in its activity.[36]

The Committee believes every measure should be taken to ensure that accusations such as these could not surface in the case of the NSW IPC and proposes transparent accounting systems to help meet this objective and to help ensure that there are no cross-subsidies from agencies' normal work.

However, the Committee accepts that such allegations will always emerge in a competitive environment, and that all that can be done about them is to make accounting systems as transparent as possible.

(b) Linking up with the Private Sector: the Corporation's Need for a Track Record

One of AusAID's major criteria when assessing bids is the track record of the bidder. Of course, the NSW International Projects Corporation would start out with no track record of its own at all. A suggestion was thus made to the Committee that in the early years, the Corporation should establish a link with one organisation which did have a strong track record, and one large private sector organisation was singled out as a possible candidate.

The Committee carefully evaluated this suggestion, but in the end felt that linking up with one organisation for all project bids would not be appropriate. First of all, there would be no guarantee that one organisation would be the best one to be associated with for all possible projects. It is possible that different organisations would be appropriate for different bids. Second, other private sector bodies might legitimately complain that they had been excluded from the picture. Third, there could be risk that the IPC would get "swallowed" by a competitor.

The Committee thus came to the view that while linking up with bodies with a strong track record was undoubtedly necessary, these links should be established with different bodies on a case-by-case basis at the discretion of the Chief Executive.

36 Minutes of Evidence, pp. 13-14.

However, the Committee wishes to stress that a major aim of the Corporation should be to foster co-operation with the private sector, and this aim should be stated clearly "up-front" in its charter.

(c) Eventual privatisation?

The Committee believes that the Corporation should strive to meet criteria for sale in about 7 to 10 years, irrespective of whether it will actually be sold or not.

8. Distribution of Profits between Corporation and Agency

This question was raised several times during the inquiry. Strong views were expressed that the IPC, or any central agency, should not keep all profits for itself but should share them with the agency providing the technical inputs, otherwise there would be no incentive for the agency to get involved.

This has never proved to be a problem in either South Australia or Victoria. The usual practice is for the distribution of profits to be negotiated and mutually agreed on as part of the bid preparation process. In a simple case, where the parties are just the OPCV and one agency, the distribution will vary from 50-50 to 60-40, or some similar range. Where there are more bidders, the arrangement will be more complex but no bid will go in until the distribution of profits has been mutually agreed on.

This should be the practice for the IPC.

9. Should the Corporation focus on selected countries and/or sectors?

In principle, the Committee believes that focusing of effort is necessary. First of all, the staffing of the IPC will be limited. All sectors cannot be covered. The main sectors which should be covered in NSW are: housing, other infrastructure, water and other environmental disciplines, health, education (potentially the most profitable sector), lands and infrastructure. These are the areas where international demand is particularly strong and where NSW has first-class expertise.

Asia should obviously be the main focus for the IPC, and within Asia, Indonesia is probably the most potentially fruitful market, in that it is receiving large volumes of aid from a wide range of sources, it is close, and it is already familiar with Australian consultants.

However, the whole CIS area has tremendous relatively untapped potential for NSW agencies. Austrade is becoming active in states such as Kazakhstan and others in the region, and if there are projects there, the IPC should certainly not ignore the region altogether.

10. Should the Corporation focus on selected funding sources?

The corporation will be in an excellent position to bid for multidisciplinary projects.

The easiest and most efficient way for the IPC to establish a track record is to seek AusAID projects first. This is the recommended course of action for the first year or two of the Corporation's life.

Thereafter, it can move to international aid agencies, like the World Bank and the ADB.

11. How should the IPC work with other States?
12. Should the IPC establish an Overseas Post?

During the Committee's visits to Asian countries, two theme emerged as paramount. The first was:

host countries make no distinction among Australian states

Indeed, in meetings abroad with even quite senior experts, Public Accounts Committee members sometimes had to show where NSW was on a map of Australia, and to point out that it was a state of Australia. There was frequent incomprehension, and at the next meeting members would again be introduced as having come from the Australian government.

In such a context, competition among Australian states for business overseas appears absurd. It could even be harmful to Australian interests if the image presented is one of disorganisation and fragmentation.

The Committee believes that a certain vision is needed in this situation. Specifically, members believe that very soon after the NSW International Projects Corporation is formed,

a national organisation of state government bodies commercially marketing and managing projects overseas should be created

Its members could be OPCV, SAGRIC, the IPC, the new West Australian body, the Northern Territory unit and any organisation the Queensland government would nominate for the purpose.

The new national organisation would at the minimum act as a clearing house for information about the capabilities of state agencies .This could help ensure coherence and order in international bidding. Of course competition among the state agencies for AusAID contracts would continue.

Another theme the Committee heard repeatedly in its visits to Asian countries was that

a local presence is vital for giving comfort to recipients and local partners

A local presence could hear about upcoming contracts sooner, could market more effectively, could network with potential local partners and, most important, with local decision-makers.

Local offices, however, are expensive, around $200,000 a year. This could be prohibitive for one single state agency.

But for all the state agencies together to set up say, two offices overseas in carefully selected countries (which would have to include Indonesia) would not be prohibitive. The gains in effective marketing would be tremendous, and the expense could be shared.

The Committee received informal evidence from Queensland that it would readily support such a concept. The smaller states like Queensland would obviously benefit Further study should also be undertaken to determine whether adherence to it should be compulsory.

The new organisation would be small, with very few staff, ideally less than five. It should be located in Canberra.

The Committee recommends that within one year of establishing the International Projects Corporation, the NSW Government take steps to determine the feasibility of establishing a national organisation of state government agencies which commercially market and manage projects overseas

C. THE INTERNATIONAL PROJECTS CORPORATION: SUMMARY OF OBJECTIVES, LEGAL AND ORGANISATIONAL STRUCTURE, AND OPERATIONS

To sum up, the Corporation should have the following characteristics:

1. It should be a state-owned corporation, totally independent of the public service. The five shareholders of the Corporation could possibly include the Minister of Urban Affairs, Planning and Housing, the Minister for Education, the Minister for Health, the Minister for Land and Water Conservation, and the Treasurer.

2. It should have a small board (ideally about five).

3. The chairperson of the board should have commercial experience overseas but should not be actively involved in any competitor of the IPC, nor should any other member of the Board.

4. The IPC staff proper should number about 11. Senior management should not be public servants but should be on contracts of three years. Some staff should be seconded to the IPC from technical agencies, but this should be up to the Managing Director.

5. The corporation should receive an initial capital injection from Consolidated Revenue of $2m to $2½m.

6. For the first three years, the corporation should not concentrate primarily on profits but on establishing a presence in the marketplace and on setting a track record. Thereafter, it should make profits its primary objective.

7. Initially, the Corporation should concentrate on the aid market especially AusAID.

8. All agencies should work through the Corporation. The Corporation will provide the business, and the agencies the technical, judgement on the advisability of a project opportunity. Agencies wishing provide their own commercial, as opposed to technical operations, should have the right to request the IPC's managing director for authorisation; the managing director should respond with the interests of the state as a whole in mind. If refused, agencies should have the right to appeal to the IPC's Board.

9. Within one year, the IPC should initiate co-operation with other state agencies with the aim of setting up a national association of state agencies involved in promoting overseas projects.

10. The corporation should concentrate on selected sectors: housing and other infrastructure, water and other environmental services, education, health, and lands, and should focus on Asia.

Appendix: Terms of Reference

Treasurer of New South Wales
Australia

27 APR 1995
ANS / /

21 April 1995

Mr Terry Rumble MP
Member for Illawarra
Chairman-Designate
Public Accounts Committee
39 Princes Highway
DAPTO 2530

Dear Mr Rumble

Under the terms of Section 57(1) of the Public Finance and Audit Act 1983, I would like to give the following reference, with a reporting date of 31 August, 1995, to the Public Accounts Committee:

* An inquiry into the handling of overseas projects by NSW Government entities.

I attach a term of reference for this inquiry.

Yours sincerely

MICHAEL EGAN MLC
Treasurer
Minister for State Development and
Minister for Energy

.../2

28th floor, State Office Block, Phillip Street, Sydney 2000
Telephone: (02) 228 3535 Facsimile: (02) 228 3476

THE WORLD AID DOLLAR: ACCESS FOR NEW SOUTH WALES

To inquire into and report upon the selling to overseas bodies of the expertise of New South Wales government entities, including an examination and analysis of:

* the market for such projects (including apparent and effective demand in developing countries, the emerging private market, and the competition New South Wales would face);

* the various public sector approaches to securing overseas contracts in

    * the rest of the world,
    * Australia, and
    * New South Wales,

with key lessons from this experience;

* the New South Wales context, including the environment for international public sector endeavour, and also including the results of an indepth survey of New South Wales agencies, and a comprehensive inventory of all the capabilities possessed within New South Wales government bodies.

* the essential principles which can be drawn from a review of all this experience;

* an analysis of the pros and cons of the alternative approaches;

* the preferred approach for New South Wales.

* the Committee to report by 31 August, 1995.

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