REPORT OF PROCEEDINGS BEFORE

PUBLIC ACCOUNTS COMMITTEE

RISK MANAGEMENT INQUIRY

At Sydney on Friday, 24 June 2005

The Committee met at 9 a.m.

PRESENT

Mr M.J. Brown (Chair)

Ms G. Berejiklian
Mr P.E. McLeay
Mr G.R. Torbay
Mr J.H. Turner
Mr S.J.R. Whan

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DAMIAN COSMOS JOHN FURLONG, Acting Executive Director, Corporate Services, Department of Infrastructure Planning and Natural Resources, 10 Valentine Street, Parramatta, sworn and examined:

PETER GORDON LUCAS, Chief Financial Officer, Department of Infrastructure Planning and Natural Resources, 10 Valentine Street, Parramatta, affirmed and examined:

CHAIR: I have been advised that you have been issued with our terms of reference as well as the relevant standing orders; is that correct?

Mr FURLONG: It is.

CHAIR: We have received a submission in terms of a survey and a letter from your organisation. Is it your desire that this form part of your formal evidence today?

Mr LUCAS: Yes.

CHAIR: Firstly, would you like to make any opening statements?

Mr LUCAS: No, we do not wish to make any opening statement.

CHAIR: How difficult has it been to implement an enterprise-wide risk management approach in an agency with such a wide diversity of activities?

Mr FURLONG: I think, Mr Chairman, that the department being barely two years old, we saw some tasks as having to be achieved before we even commenced that process. We were formed just on two years ago from four quite separate disparate agencies and it was apparent very early on that some downsizing of the department itself was necessary and some major tasks faced us before we could even contemplate moving into the program you directed our attention to, namely, when the department was first formed it had perhaps 500 staff more than it needed, so we took action to make ourselves a more compact, more efficient organisation in terms of numbers.

We took some action to rationalise the differing systems, including IT systems. We found, because we had two major systems operating in the department, they were not capable of speaking to each other. Further, we established a major natural resource operational arm, the Catchment Management Authorities, to which we devolved some 350 staff.

Having done those things then, we have begun to implement a much more far reaching approach in terms of risk management, so I think we have the more difficult elements at least of the department's establishment behind us and, particularly in the last 12 months, we have commenced to more fully integrate a risk management approach into the department's main business.

CHAIR: In downsizing and then looking at certain risk management measures afterwards, did that downsizing create any risks for you to manage? I am suggesting maybe lack of corporate knowledge in your department. How has that been handled.

Mr FURLONG: I think it is true that that certainly would have been a risk. However, we were careful in approaching the whole downsizing exercise that although the program was predicated as a voluntary redundancy one, it was still open to the Director-General to choose whether to offer the employees the opportunity to take up a voluntary redundancy, so we did not offer it in areas or allow it to be taken up where we might have exposed ourselves to unacceptable corporate risk. Surprisingly enough actually, of the approximately 500 people who have left the department since it was formed, they have in fact in large been people who have chosen to take a sea change, which somewhat surprised us. If you look at a graph, a very high proportion were people who had not long been in the public service and were in their thirties, but simply chose to take advantage of the redundancy to either move out of Sydney or to take up other opportunities that more suited their interests, so we were fortunate, I think.

Mr LUCAS: Perhaps, Mr Chairman, I might add that whilst this process was ongoing, there was a parallel process occurring of trying to define the objectives and strategies of the new department and that business planning, strategic business planning, and then down to business plans, was going on through this whole period over the two years, so we see that our risk management approach is embedded in that business planning approach and strategic planning approach and we had, in parallel with the downsizing, the development and formation of our views about what our business was really about.

This was aided by the results and services plan that the Treasury now requires departments to publish and because we had effectively started as a new department with a blank bit of paper with inherited aspects from various other departments, the results and services plan has gone through a number of iterations and has helped us to understand and define more precisely what our business is about.

Mr MCLEAY: Have you found that results and services plan has significantly contributed to the development of your risk management or improvement of risk management and, if so, what other policies or directives and guidelines from Treasury or other central agencies have assisted significantly?

Mr LUCAS: Dealing with the results and services plan first, as I indicated before, to the extent that it enabled us to have a structure that tried to define what our business was about, and because of the structure and the context of the business, the objectives we are trying to achieve will therefore lead us to define what risks we are involved in, we found that the results and services plan, particularly in an iterative manner where we were going through a number of iterations of this particular plan, and are still going through a number of iterations, lead to a realisation of what risks were involved in our business and what rankings were involved in the business.

We also had, connected with that results and services plan, a process to try to embed that within, as I said before, our strategic business plan and our individual business plans, and roll that down to team plans which allowed the dissipation of that vision of the objectives down through the organisation, and then the collection up of the results of that and in fact embedded in our business planning area is a part to identify business risks that are there.

CHAIR: Where is this results and services plan published? How often is it updated?

Mr LUCAS: I am not sure whether, Mr Chairman, the results and services plans will be published. They are documents between ourselves and Treasury, which I understand all other departments have to do as well. It is updated on a continuing rolling basis. I guess once we get to a base level of, let us say, an agreed results and services plan, then I would envisage that Treasury would want us to review that on an annual basis so that it keeps rolling over. In fact our board of management is meeting on Monday and the latest iteration of our results and services plan is before that board of management to be confirmed before being sent up to the Treasurer and Treasury as our 2005-06 results and services plan.

Mr MCLEAY: What other document from Treasury, a Toolkit perhaps?

Mr LUCAS: Yes. We are aware of the Toolkit. In the former Department of Land and Water Conservation, which is one of the entities that came across, the Toolkit was taken on board and commenced. I started with the new department. I am not a former DLWC or a former planning person or any other entity that came in. I understand that in the former DLWC the Toolkit was taken on board. The DLWC did ask to be a part of the pilot of that Toolkit. They were not part of that and there was a process that was commenced, but I think overrun by the change in the nature and structure of the organisation.

Mr MCLEAY: Are there any other central agencies that significantly talk about risk?

Mr LUCAS: Not that I am aware of at the moment. One of my former lives was with New South Wales Treasury Corporation and in that place I have used the Toolkit extensively to develop an understanding of the risk involved in the organisation of TCorp and I am very familiar with it and the results of it, the process of surveying internal staff, understanding our risks in all of those quadrants within the circle, to come up with a diagram that gives us an overview and understanding of risks, and that did go from TCorp to the auditor. I am familiar with that document in detail.

Mr MCLEAY: Do you use a matrix?

Mr LUCAS: Our current one ends up developing a risk matrix with impacts and likelihood and from that we can get to a layer of ranking of risks so that we can understand what are our extreme risks, our high risks, our medium risks, and our low risks.

Mr FURLONG: The other thing which we should say is that the thread which runs through our approach is of course the Australian Standard in relation to this matter.

Mr WHAN: With your risk management framework across the department, does that also cross over the Catchment Management Authorities as well, or are they developing independently their risk management?

Mr FURLONG: The CMAs are indeed established by the Parliament as independent statutory authorities. However, DIPNR is engaged, currently in a process of establishing or helping the individual boards of the authorities establish an appropriate corporate governance framework that will include risk management but, properly, it is not something that we can impose upon them, but we have offered them our resources and assistance so that they may do so for themselves in each individual authority.

Mr WHAN: They would be very early in that process at the moment?

Mr FURLONG: Somewhat.

CHAIR: In relation to your matrix.

Mr FURLONG: I should add that we have engaged on their behalf, or with them is perhaps the better way to express it, the services of Deloittes to assist in the exercise.

CHAIR: In relation to your matrix we would not mind looking at it. We would keep it confidential. If that is possible we would appreciate that.

Mr FURLONG: We have brought some with us.

CHAIR: You can let us know what you would like to remain confidential.

Mr LUCAS: What we have here is our generic overview of the rating, the overall ranking and the matrix.

Mr MCLEAY: Before we go into it, do you think there is any benefit in having a sector wide matrix?

Mr LUCAS: I don't think that there is a benefit in having a Government wide matrix because the risks and the impact or the consequences of those risks are probably unique to the business. Whether there is some benefit in having a sector area, so a natural resources or a planning type area or whatever, a transport sector, an electricity sector, there may be some merit in that. You would want to be careful how you define organisations within that sector. Take DIPNR as an example, we cover the built and natural environment. We are not really a department of environment, conservation, green organisation and we are not really a department of primary industries brown organisation, we are somewhere in the middle as the balancing pivot. If you tried to put us in a sector there would always be the inevitable mismatches there.

Mr FURLONG: I think that broadly captures it.

Mr WHAN: In terms of your assessment of risk with your own activities, there are a lot of areas of DIPNR's organisations that can impact on the other departments. If you do not do a good job planning that could effect the provision of education and health services, is that something which you take into account in looking at the risks of your activities?

Mr LUCAS: So as to not mislead this Committee, because we are only two years old this is an ongoing process. As my colleague, Mr Furlong, advised initially we have been going through a process in the first year of down sizing which is really just coming to a completion, but we always recognise the need of starting to develop our risk management process and that is going through a process at the moment. It is developing. It is not complete and, in fact, no risk process is ever complete, it should always have a feedback loop. We are going through the early stages of that. Notwithstanding that, one of the early risks we did identify is the various aspects of a failure to deliver on the new objectives that were set for DIPNR and, exactly as you mentioned, the failure has ripple down effects on other areas.

If you take part of our role is to advise in relation to infrastructure placement with the Treasury in relation to the allocation of scarce resources, and clearly our process in trying to roll that through has major impacts on all sorts of infrastructure provision. We are also involved, for instance, in the assessment of strategic sites, about where you should be placing various types of industry and that has impacts in the Government but outside the Government as well. We did identify those in an early draft and it is in our current one as one of the major risks.

CHAIR: I have got a question regarding your survey response.

Mr LUCAS: The matrix you have in front of you is our current process for going through them. The first sheet which has "Rating and Description of Control" is a way of rating our current controls that address risks and how they minimise them.

The second one is a guide for people about how do you determine what the likelihood is with frequency numbers and these are fairly standard out of the standard itself.

The third one is a description of how you assess the consequence and we give guidance in a number of areas.

So, you draw people's attention that consequence is not merely a financial consequence, there are other ones that you actually have to take into account that may have an impact.

The fourth one in the major box at the bottom is the matrix to bring those consequences and likelihoods together and depending upon where a risk lies you then have in the top right hand box the risk level we have assigned to it; high, significant, moderate or low. As I say it is a fairly generic one but it is the one we are using and we have distributed that around our organisation.

Mr MCLEAY: You said you offered assistance to the CMAs, are there any other guidelines or impacts on risk that DIPNR have to other sectors? You can assist CMAs, do you assist anyone else? Do you have a broad impact on any other agencies?

Mr LUCAS: Our relationship with other agencies is dependent upon the agency. For instance, we supply accounting services to Honeysuckle Development Corporation. Honeysuckle Development Corporation is an organisation that has been in existence for some time and has a mature board that has a full grip on the business risks that face that organisation in Newcastle and, therefore, we do not necessarily have much to do with them other than processing their accounting side. We also provide accounting services to the Lake Illawarra Authority. That is an organisation that really exists as a partnership between Wollongong Council, Shellharbour Council and the Government. We would identify any risks that come up out of that organisation, perhaps slightly informally, because it is a very small organisation, the Lake Illawarra Authority. We do the accounting and other services for the 13 catchment management authorities.

The Growth Centres Commission that was talked about in the budget process by the Treasurer, when it comes into existence we envisage they will be a fully fledged board taking on its own evaluation of risk. It depends on the relationship we have and services we provide. I trust that answers your question.

CHAIR: In relation to your survey response maybe you could address the lack of business continuity plan or the disaster recovery plan.

Mr LUCAS: Again, as Mr Furlong mentioned, DIPNR is a new organisation and the two principal parts that came together were the Department of Land and Water Conservation and the Department of Planning or Planning New South Wales. They had separate and unique systems of, principally, IT and other processes as well. I guess the first year or so has been in trying to deal with those day to day practical issues of getting everybody on to the same network so we can send e-mails one to the other and communicate in an effective way, for instance.

If I can deal with the disaster recovery plan; at the moment one does exist, it is a rudimentary or basic one, which was principally based on the DLWC process that was available and envisages two sites that we run that are geographically separated and allow us to be able to move processes from one server to the other server if we have to. It is not as sophisticated as perhaps mirroring would require but the question needs to be asked about do we need to have those sorts of mirroring capabilities in a new organisation. Planning was principally serviced by CCSU, by the Department of Commerce, and had its own separate disaster recovery.

In relation to business continuity, in the formative two years that we have been in existence so far, what we have sought to do is to start to collect information based on our new processes about what are the critical steps that would need to be taken if we did have a break in some way, we had no access to a building or a computer system went down or there was some other impact on our business, and how would we continue on. There were surveys and questionnaires sent out to a variety of people to identify these particular critical business areas and to end up with a financial impact statement about what would actually need to be done to get around various things.

For instance, in the accounts payable area, which is centralised, we would need to be able to process fairly quickly all sort of urgent cheques, those sorts of things. Whilst in, say, an area of assessment of a major site there is a reasonable expectation that the critical period would be four or five or six days before you needed to access essential data that you needed to get to, because you were locked out of the building or the computer system went down, or whatever.

Mr FURLONG: The other thing we might add, Mr Chair, is we are exploring, in the alternative of establishment of a mirror system, the opportunities that exist with us of other departmental users of the SAP, the disaster recovery, business shared opportunities which seems to us a more achievable practical approach under the circumstances.

CHAIR: In relation to executive performance agreements, what type of key performance indicators do you use to measure whether the executives are meeting their risk management objectives?

Mr FURLONG: Principally we would measure against, firstly, the corporate plan and then drilling down from that the individual business plans for each of the constituent areas of the agency's operation and drive in to the specific performance contracts of individuals themselves would be achievement against those various targets.

CHAIR: Would you be able to submit a pro forma agreement to support that response?

Mr LUCAS: The document that Mr Furlong is alluding to is, in fact, two documents.

One is the business unit plan, which as we said before, identifies what are the flagship projects that they want to undertake in a particular year, what are major initiatives and what are other activities that they need to undertake. One part of that form is to then document out the risks that are involved in that. The other document is the agreement between or the review of the performance against that business plan by the Director General, which for certain SES offices is required to be summarised up and put into our annual report. I am of the view, I would perhaps want to take it on notice, that we may not want to disclose those but I am not sure, I would have to check. Perhaps a further part to that, I was just advised that the ProForma agreements for executives are available on the Premier's web site. A pro forma is available which would give you an idea what we base ours on.

CHAIR: Do you have any comments or recommendations that you would like to make in respect of risk management for the New South Wales public sector?

Mr FURLONG: Mr Chairman, I think we would say, as a young agency, that it was perhaps not incumbent upon us to advise others.

CHAIR: Do you have any other closing comments you would like to make?

Mr FURLONG: No, Mr Chairman.

(The witnesses withdrew)

(Short adjournment)

ROBERT JOHN SENDT, New South Wales Auditor-General, 1 Margaret Street, Sydney, affirmed and examined:

ANTHONY THOMAS WHITFIELD, Deputy Auditor-General, 1 Margaret Street, Sydney, and

STEPHEN JAMES HORNE, Assistant Auditor-General, 1 Margaret Street, Sydney, sworn and examined:

CHAIR: I have been advised that you have been supplied with our terms of reference and the relevant standing orders; is that correct.

Mr SENDT: That is correct.

CHAIR: Is it your desire that your submission form part of your evidence today?

Mr SENDT: It is, Mr Chairman.

CHAIR: Would you care to make an opening statement?

Mr SENDT: Only very briefly, Mr Chairman. We welcome the opportunity to appear before the Committee in its inquiry into risk management. We have always held the view that risk management is a very important part of good governance of public sector entities and we welcome this review. As the Committee will be aware, we conducted an audit in 2002 on risk management. Three years down the track we think that it is a very opportune time to look at the subject again and we are happy to help the Committee in any way that we can.

CHAIR: As you are aware of many of the processes that the Committee has taken place for this inquiry, I would like to put on the record. Thank you for your assistance and also for your secondee, who has been of great assistance to the Committee in following up your original report. Over 85 per cent of the agencies that we have surveyed so far have claimed that they have based their risk management framework on the Australian and New Zealand standard 4360:2004 Risk Management. Is this consistent with your observations?

Mr SENDT: We have not surveyed the field since our 2002 report. In our submission we do note the competing standards or approaches of the Australian New Zealand standard and the Committee of Sponsoring Organisations standard, of which a version 2 has been released. We understand that the Australian New Zealand standard has found a lot of favour both in the public sector and in the private sector in Australia and indeed overseas as well. Certainly at the big end of the market in the United States and hence flowing perhaps to some extent to their subsidiaries in Australia, there is perhaps a tendency to use the COSO model, but the Australian New Zealand standard does seem to be a more simple model to implement and we were not surprised by the findings of the survey.

CHAIR: In your opinion what would be the most effective way to ensure all agencies apply the best practice requirements of the standard?

Mr SENDT: I will leave my colleagues to add to that. A very brief answer to that would be that there should be a greater requirement on CEOs or boards, where there are boards, to report on risk management approaches and activities they undertake and an obvious place for them to report on that would be in their annual report. I think those requirements should be strengthened.

Mr WHITFIELD: I would agree with that, Mr Chairman. I think whilst there is an existing requirement under the Annual Reports Act to report on risk management, I think there needs to be more direction given from central agencies, such as Treasury, as to the type of information that should be reported and the frequency of it and I think if you look at the way that agencies have adopted risk management across the sector, there are some that have built in with their audit committee so that the audit committee is an audit committee and a risk management committee, whereas others are treating it separately.

Some are using the old Treasury Toolkit but that has not had a great deal of use. A number have opted for the Australian New Zealand Standard. A good example would be Sydney University where they have appointed a risk manager. Their audit committee is a risk management committee as well as an audit committee, and at each meeting they are updated as to the progress that has been made and the risk manager has gone out to various business units within the university, the faculties and schools, briefed the people and helped them assess the risk from a bottom up level as well as the audit committee looking at risk from the top down.

If that type of structure was used more widely throughout the sector, together with reporting requirements, then it would strengthen the whole risk management within the public sector.

Mr HORNE: When risk management first became an identified practice, it was very much an internal thing, a management technique. Of course it is, but I think that one of the important changes to make to push it along further is to make it part of the governance and reporting expectations for all organisations, and I do not just mean Government, I mean the private sector too. Indeed that has become the case and it would now be considered absolutely essential for any private sector organisation to include risk management as a fundamental part of their corporate governance and their reporting externally to their shareholders and to the world. We should do the same and Government agencies should report externally about what they are doing with risk management.

By turning it from an internal management practice into external reporting issue it focusses the mind on it quite clearly. It elevates it to the executive level somewhat more and I think that by those mechanisms we could then see better audit committees pick this up and address it more vigorously than they have done in the past.

CHAIR: I am pleased that you raised the issue of the private sector. You have probably answered in part the next question I was going to ask, but as you are aware, a number of major corporate collapses have been linked to inadequate corporate governance and risk management practice. You have suggested that this can be strengthened in the ways just mentioned. How do you see that that could be done? Do you think you would need amendments to public sector legislation, or Premier's memorandum, or what do you think would be the appropriate way to try to address that?

Mr SENDT: Certainly legislation would be one way to approach it. The danger with that is that techniques, expectations, can change over time. I this it is probably preferable to have a central agency, Premier's Department or Treasury, driving the change. It could be by way of Premier's memorandum, Treasurer's direction, Treasury circulars, but I think that whichever central agency takes up the role if that does happen, they can give far stronger guidance as to their expectations and what good risk management means and what good reporting risk management means.

I think that the advantage of approaching it from the reporting end is that while it may be the end point of good governance or good risk management, it does give that very public focus and very strong expectation that behind the reporting there would be substance to the risk management.

Mr HORNE: Could I draw a parallel to the work we recently did on fraud control? We were suggesting there be a significant legislative change to support fraud control. We had audited it three times over 10 years and found it had not gone ahead as quickly as we would have liked. The argument at the time was that fraud control, along with risk management and other things, is already a requirement. It is already implied in the existing legislative requirements. Without taking a too technical discussion along that line, that could be inferred. Without it being a specific requirement, as is often the case in other jurisdictions, it is not focussed on as keenly as we wanted. Our suggestion was on fraud control that we should have a specific legislative requirement, despite the fact that it might be inferred in what is already there, to focus more on it. That is what is done in the Commonwealth and it is common elsewhere.

At the time we did the fraud control report there were mixed views in the central agencies about that. Treasury have now agreed with us that it is in fact useful and they will go ahead and do that. I would suggest that risk management is an even more significant issue overall and so there are grounds for legislative requirements to give it that stronger footing. That is only the beginning. Legislative requirements do not achieve anything often in themselves, they just get it on the notice board better, and then there is a question of guidance and monitoring, and that is where I agree with what the Auditor-General has been saying, that there is a role for central agencies to keep that as a pressure issue and external reporting requirements help bring that along too.

CHAIR: Another area where we found there is conflicting opinion is that best practice standards require the use of consequence and likelihood matrices for analysing risks and some agencies have suggested that there should be a standard matrix across the public sector and others have suggested there should be a matrix specific to that particular agency. Do you have an opinion on that issue?

Mr SENDT: I think that implies that there is going to be a matrix approach, and while some version of likelihood and consequence is fundamental, it is all risk management techniques. I think specifying there has to be a particular approach and that particular risks would apply across all the public sector. I think it is not the best approach. There may be some risks that are indeed common across most public sector agencies, but to prescribe those either in legislation or in some central agency direction runs the risk that agencies would concentrate perhaps on those and ignore other risks that are more specific to their organisation. My preference would be it should be an agency by agency approach and the agency then takes responsibility for the risks it identifies.

Mr HORNE: The Australian New Zealand Standard is one model that is very popular. The COSO model is another model that is very popular.

CHAIR: COSO?

Mr HORNE: Committee of Sponsoring Organisations. It is an American model. It will probably become the leading model on risk management in the world, largely because it has been driven out of reforms under Sarbanes Oxley, so all of the American multinationals will be pushing it along that framework. It is a very complicated model and they have just updated it to version two. It is also the model that the Treasury Toolkit is based upon because at the time the Australian New Zealand Standard had not been issued. The Australian New Zealand Standard is a much simpler method.

The Treasury Toolkit adapted the presentation of risk into another version, which was almost like a radar map, a circular diagram, so you can present it in lots of different ways. I think I have spoken to as many consultants as you have, and they all have different view about how one should present these things. I think that the argument is best left simple. The Australian New Zealand Standard provides a relatively simple process to move through risk management, which most managers seem to find sensible, and then the visual presentation of it in whatever form flows from that, rather than that being the end of it.

That, in my view, is the weakness of the COSO model. It is a very structured cube-like methodology which is pretty hard to sit down and sensibly look at, but the Australian Standard does it, I think fairly simply, and I have not spoken to anyone who has used the Australian Standard who has found it too complicated.

Mr MCLEAY: You have mentioned the Treasury Toolkit. Would it surprise you that we have had several respondents say that the agencies are aware of the Toolkit but that they do not use it.

Mr SENDT: I do not think that would surprise us. The Treasury Toolkit was based on version one of COSO, so the Toolkit is now out of date, even if you want to go down the COSO line. It has been superseded. As Stephen said, the Australian New Zealand Standard does appear to be a simpler approach, more straightforward approach, and for many organisations I think it is probably the preferable way to go. As Stephen mentioned also, the COSO model is really being driven out of the US multinational, very large corporate end of town, and the degree of complexity to it probably reflects the fact that very large organisations can afford to put a large amount of resource into implementing a model that a smaller organisation probably cannot and that is why smaller organisations tend to find the Australian New Zealand Standard easier to implement.

Mr HORNE: When we did our review of risk management in 2002, and I was trying to look up the numbers as you were talking, we found that of the 24 agencies that we surveyed, in the general Government sector 54 per cent did not use the Toolkit and in the public trading enterprise sector 73 per cent did not use the Toolkit.

Mr MCLEAY: Did not?

Mr HORNE: Did not, and that was in 2002 when the Toolkit was more recently in the marketplace. We made a number of recommendations at that time. Things could have gone one of two ways from there. Agencies could have been strongly encouraged by Treasury and others to use the Toolkit and adopted it more rigorously or gone away from it. Your findings suggest that they have gone away from it and the other thing that we can see is since then the Australian New Zealand Standard has emerged and become very popular. That suggests where people are going.

Mr MCLEAY: It may not surprise you that a few respondents claim that the Audit Office of New South Wales reviews and monitors their risk management processes. Can you explain the current role of external audit for monitoring risk management in the public sector? Would you like to comment on that?

Mr SENDT: I am not sure what they were meaning when they answered that question. Many of them would have been aware that we have reviewed their practices as part of the performance audit. That is only an irregular occurrence. As far as financial audit goes, which is an activity that we carry out with all agencies every year, we do not review their risk management practices per se. We look at what risks there are in the compilation and derivation of their financial report, but that is only part of the risk that any organisation faces.

We certainly would not look at, for example, risks of reputation, risks to an entity's reputation. We would not look, as part of our financial audit, risks that the services the organisation is supplying are inappropriate, are inequitable, are lacking in equity and access, for example, a whole range of risks that an organisation should consider. We would not look at that and Tony might want to add more.

Mr WHITFIELD: What we do look at is the risks that are associated with the financial aspects of the organisation, so the preparation of financial statements, in terms of determining what sort of controls they have put in place to mitigate those risks so that we can conduct the audit in an effective way. As the Auditor-General has said, we do not look at the entire risk profile of the organisation. When we are doing an audit we are assessing risks from an audit perspective, not from an organisation operational perspective from the agency's viewpoint.

Mr SENDT: In fact we might find shortcomings in the controls that an organisation has. That does not mean we will give an adverse audit opinion, because if any auditor finds that controls are not working as they should, or not as strong as they should be, the auditor will apply other procedures to gain enough evidence to demonstrate that the financial report is materially free of misstatement, so I think organisations need to understand that a clean audit opinion is not a guarantee of their risk management approach is sound or the controls are in place.

Mr HORNE: I think your question has touched upon one of the key issues with the whole question of risk management. Risk management in its origins was defined very narrowly with very limited terms of financial risk. It basically used to be things one could insure against or otherwise mitigate against financially. If I could read a couple of words from the current standard as to what risk is, which I am sure you are aware of, but risk is simply the chance of something happening that will have an impact on objectives. Risk in our view, very broadly, is anything that will stop the organisation achieving the things it is there to achieve.

Auditing of financial statements is one component of that but there are many, many more so you would want an organisation to be managing itself, managing its risks on a very broad front, hence why what we want in annual reports of organisations is management attesting to the fact that they have considered all of the risks, which include opportunity risks, of not doing something and moving forward, and we want them to make a statement that they have had a structured way of looking at and thinking about those things so that we can see that it is being managed dynamically.

The question of the role of audit in risk and what risk is, is all part of the discussion of where risk management has moved to and it is very clear that it has always been management's responsibility to look at risk and the auditor is a part of a chain of processes which assist him to do that, but the whole nature of risks has expanded and if an organisation is not looking at risk in that broader way then they are not attacking it at all.

Ms BEREJIKLIAN: My question relates to one of your opinions. Do you think there is a huge gap between agencies in terms of best practice and worst practice risk management procedures and how would you suggest that gap be reduced, if you do think it exists?

Mr SENDT: I think the 2002 audit we did, while it only looked at 24 audit clients, did show a significant degree of variation in the attention they give to risk management. Stephen can quote the percentages, I don't have them in front of me. There were considerable percentages who acknowledged they did not have a risk management strategy in place. There were a considerable percentage who did not have a methodology they used, whether it was the Treasury Toolkit or another methodology.

I certainly accept your point. There is a large variation. To the extent that is continued is more anecdotal. Tony mentioned some new approaches that have been taken at Sydney University which have certainly given greater prominence to the role of risk management. We have not looked across the field to see again what proportion of agencies are adopting better practice in the area.

Mr HORNE: There are some specific references. It is a good question. In our last report, I will give you a reference to it so you can look at it in more detail, page 29 of our 2002 report, gives a measure of how the varied the pattern is. There is an exhibit there, exhibit 19, *Development of Risk Management Practice*. It shows a significant variation between some agencies in the general Government sector being, as far as risk management goes, nonexistent, virtually doing nothing, up to well developed. One agency was in well developed. No agency was in best practice. In the public trading enterprise sector no agencies were nonexistent with risk management, so everybody was doing a little bit of something, but no agency was best practice.

DEPUTY CHAIR: Is this in their opinion or your opinion?

Mr HORNE: Our opinion. We can see quite a spread. We do not have updated data on how that is looking but that shows, I think, there was also a subsequent section on page 30 of our report about the extent to which agencies were risk averse. One of the problems with public sector agencies being risk averse, which most of them generally agreed they were, you would hope that would lead them to manage risk better, in fact it did not do anything of the sort. Being risk averse did not lead to a good risk management outcome either. We want them to be more risk aware than risk averse and to manage it and certainly in 2002 that was not the case.

Ms BEREJIKLIAN: In your opinion, for example, we heard evidence of a very critical Government agency that delivers a service to the entire community did not have a business continuity plan. At the end of the day whose role is it to highlight that this is a huge issue because the public interest is at stake. Who then fixes the issue and who is ultimately responsible for identifying and fixing it in your view?

Mr SENDT: It should be the CEO of the organisation or the board if there is a board.

Ms BEREJIKLIAN: Failing that?

Mr SENDT: Failing that or in addition to that there is a role for central agencies to take an active, more active role in promoting what is best practice in these areas, whether it is risk management or business continuity, and the Premier's department is providing some leadership on that at the moment. You might be aware, Tony, of the business continuity requirements that the Premier's department is putting out. There is also some leadership being shown from the central agencies in terms of IT security where there are requirements being placed on agencies to reach certification by a particular time.

Mr WHITFIELD: As the Auditor General mentioned there is a requirement from Premier's to have a business continuity plan in place by December this year. There has been a reporting back process through the Director General as to the progress the agencies are making in terms of achieving that goal. One of the things we do in our audit is look at the agencies and see whether they have disaster recovery plans, business continuity plans, particularly where there is a dominance of the computer within the running of the agency. And we have reported that back through to agencies that they have not got it or they need to update their BCPs or disaster recovery plans on a regular basis.

Ms BEREJIKLIAN: Do you think it is of concern that agencies have to rely on directives from the Premier's department? I am concerned about the culture which exists in the agencies. If you are meant to be risk averse and you do not have a culture which tells you, you are a senior executive, that you should have a risk management strategy, that to me is of enormous concern and the fact that it has to take a central agency to say you need to have a risk plan in by December does not really allay my fears because it is almost under duress that these organisations feel they have to submit it. I guess my question relates to, I don't expect you to give your opinion on this specifically, but relates to the culture which exists at very high levels in the public service about risk management. It is certainly not a culture which exists in the private sector. Do you have any comments in relation to that?

Mr SENDT: I think what comes from central agencies can be a mixture of directives and education. Certainly in the private sector there are plenty of organisations who provide information and education to directors and senior management on best practice, again whether it is in business continuity or otherwise. Various organisations such as the Australian Institute of Company Directors provides information to directors. What is coming out of the central agencies is a mixture of the directive approach and the education approach. I would agree this certainly would be a concern in the major entities if they were only tackling issues such as business continuity or risk management because of a directive.

I can understand perhaps more in the smaller agencies why they may need a greater degree of direction from central agencies, as well as education, but certainly a greater degree of direction. I take your point, a large organisation that only takes account of business continuity plans, risk management, fraud control et cetera, because of a central agency direction is probably only doing the minimum to satisfy that direction.

DEPUTY CHAIR: Can we talk about your review into universities, risk management practices at universities. I understand that you did recently review risk management practices at universities. Did you hit all of them?

Mr WHITFIELD: Yes, we did that as part of a compliance review. Because we do the audit ourselves of the ten universities it is a good group to actually trial some of our new diagnostic tools and one of them was a risk management tool that we are going to be rolling out over the top 50 agencies. We trialled it on the universities to make sure that we had the right package. What we did find was that it varied. I quoted the example of Sydney University is probably up one end of the spectrum and down the other end there are some of the smaller universities that are just starting to get in to the swing of putting together a risk management plan.

One of the issues, I guess it applies right across the sector, is in putting such a plan together Sydney University has gone out of its way to appoint someone on to their audit committee who is considered to be an expert in risk management. I guess one of the issues is that there is not too many of those type of people around, and for some organisations it is difficult to go through the process of identifying the risks and then coming up with the strategies and putting in the controls. They really need some assistance. It can be an expensive exercise to get that assistance. Where in the past they tended to review, as Steven has said, risk as being something that was purely financial and something that was insurable, by taking a broader approach, particularly with the universities they are looking at loss of reputation, they are looking at plagiarism, effective marking of the papers and keeping information confidential. So, there is a whole broader spectrum which requires a different mindset to that that was previously exercised.

DEPUTY CHAIR: Could there be a university wide risk management matrix or framework?

Mr SENDT: There probably could. Of the 450 agencies that we audit there is a huge variety amongst those. We tend to use universities quite often as a test area for new auditing tools, for example, in this case on risk management, because they are fairly homogenous in terms of what they do. They have similar sorts of governance arrangements in place, in terms of establishment of senates or councils or whatever they are called. By and large what each university does is fairly similar. It may have greater exposure to overseas markets; some may have greater exposure to different types of vocation or different types of fields, but certainly I think the risks that universities face would be pretty common. I would not expect to see too much variation between them in the risks they identify.

Mr HORNE: You can identify risk profiles by industry sector. There is a lot of work done by academics and researchers on those types of things. If you are in the mining sector, you can do that. The public sector is immensely diverse and you only have one of most organisations, so you can not develop a standard risk profile across all different sorts of activities because they are so different, but where you have a sector that is quite large, such as the university sector, then there are some traits. Even then there is a big range, because you get large university doing very big things and smaller universities doing others, but you perhaps can. We should also remind ourselves that the universities do need to address risk management quite significantly because in our fraud control survey the university sector was the worst of all of them.

DEPUTY CHAIR: You said that one of the tools you are developing is for the top 50, can you elaborate on that and whether or not there should be a similar review carried out on say the top 50 or top 20?

Mr WHITFIELD: The tool we have developed we have used on the ten universities, the intention is now to use it on the top 50 agencies on the public sector and then expand it.

DEPUTY CHAIR: Have you given the tool a name yet?

Mr WHITFIELD: We call it a Management Assistance Diagnostic Tool, MAD for want of an another acronym.

Mr SENDT: This is a tool for us to use in assessing agency performance in a particular area. It is not a tool for agencies to use in assessing risk.

DEPUTY CHAIR: A lot of internal reporting that they do and particularly their risk, there is no external reporting of their risk. Do you think there is a need or a benefit in any external or even to other stakeholders reporting of their risk exposures or do you believe it should be kept internal? And for example, what do you do with your risk matrix?

Mr SENDT: There is an implied obligation to discuss risk in annual reports. I think that needs to be enhanced. There is a requirement to report on governance arrangements which is one aspect of risk management. I certainly think the reporting needs to be improved. Now, whether each organisation should be required to report its risk management matrix or cube or circle, or whatever particular technique it derives, I think I would probably want to think about that. In some of the more commercial areas of Government you would have to be wary of requiring an electricity authority that happens to be State owned to disclose more information about how it treats risks than its private sector competitor, for example.

Mr HORNE: Take, for example, the annual reporting awards, they have a section in there on governance and a section within that on risk. So it is a standard requirement for anyone to win an annual reporting award that they look at how to report externally risk. They have a special subaward on the best way to report on risk because it is an important issue these days.

Mr SENDT: Stephen is one of the judges for the annual reports.

Mr HORNE: The issue with that then is that it is not necessary to report to the community what the risks are you face, it is more important to explain to the community how you go about identifying those risks and managing them so that someone who is looking at your organisation, either in the private sector as an investor, or a community stakeholder, or in the public sector as an interested party, can see that they think that you as an organisation have taken this seriously, know what you are doing, and are addressing it in an active manner. That does not need to take a vast amount of space in an annual report. There is lots of good examples of how that could be done without becoming a slave to detail. It is important that you present a clear image of how you are dealing with that. There are lots of good examples, models, on how to report risk management and I think public sector agencies should do it for sure.

Mr TURNER: Should there be a formula to be able to determine any financial or personal benefits from the risk management operations?

Mr SENDT: I am not quite sure I understood the question, Mr Turner.

Mr TURNER: It is probably academic. Do we need to know by implementing risk management practices that we are going to enhance the business?

Mr WHAN: Is it worth it?

Mr TURNER: Is it worth it on a personal or financial basis to be able to assess what those benefits have been?

Mr SENDT: In the private sector there is a clear indication from some of the examples where things have gone wrong of being able to demonstrate that you have a sound risk management practice in place, as well as a whole range of other risk practices in place that would lead to greater investor confidence. It is possibly not quite so clear cut in the public sector. Although I would suggest that an organisation that demonstrates good governance generally, of which risk management is a part, is probably more likely to inspire greater confidence, for example, in the central agencies in supporting proposals that the organisation might put forward. It is probably more likely to inspire confidence in customers, clients and taxpayers to the extent they do take an interest in those. It is a bit more difficult to assess in the public sector than the private sector.

Mr HORNE: There are now quite a few studies around, all private sector, of the market value that is added to a company by good corporate governance. I don't think there has been a study specifically of risk management, but I guess if you took that as a key element of the thing, there is now very clear studies around the premium that an investor, particularly large institutional investors, will pay on stocks in a company that they regard as well governed as opposed to one that they think is perhaps a bit dodgy because of the safety of their investment and the performance.

That exact question you are asking was very important a couple of years ago an and there weren't any good answers. Trying to convince someone to spend money on all of this stuff was a little more in principle than in reality. Those studies have shut the door on that one saying there is a clearly a market value that can be attributed to good governance. In the public sector there aren't those market mechanisms, but we can assume that public interest maps that and if you ascribe a value you get much the same sort of profile.

DEPUTY CHAIR: Would you like to make any additional comments or recommendations you wish to make in respect of risk management in the public sector?

Mr SENDT: No, I think we have covered everything we wanted to say, Mr Acting Chair.

DEPUTY CHAIR: We might move on to corrections. We are currently conducting an inquiry into value for money for New South Wales correctional centres. This is a follow up of your comments in volume 4 of your 2004 report to Parliament. Do you have any additional comments in relation to this inquiry that could be of assistance?

Mr SENDT: It is certainly an area that was of interest to us, you may remember that last year when we met with the Committee around May or June we had thought of doing a performance audit into the way the Department of Corrective Services managed the outcomes it expects from the Junee prison and the way it gains value or does not gain value from that prison. The Committee indicated that it was interested in doing something like that so we removed that from our program. It is certainly something of interest. I think there is a lot of interest in the way governments deal with the private sector in providing services. Perhaps more so in other states than New South Wales to date. Certainly much more in places like the United Kingdom where there has been a vast number of services that are being undertaken in a partnership arrangement with the private sector. We were very interested in looking at this.

We were concerned that the department did not seem to have the ability to make an assessment of the value it was getting from the service. It knew how much it was paying. It knew how many prisoners were in the gaol at one time. Beyond that it did not seem to have any capacity or ability, or perhaps even interest, in assessing whether it was good value for money.

Mr MCLEAY: When you say good value for money, do you mean compared with the private sector?

Mr SENDT: Compared with its own services, compared with best practices, compared with privately run prisons in other States of Australia, compared with publicly run prisons in other States in Australia.

Mr TORBAY: Are you referring to the capacity of the public sector, to match it with the public sector in terms of those negotiations?

Mr SENDT: There are two issues. One is negotiation of the contract and that is always an issue which is difficult if you are in an area where there is not a lot of negotiation happening because it is difficult to maintain expertise. Organisations such as the Roads and Traffic Authority are continually negotiating large contracts with the private sector so it will build up a level of expertise. Other organisations in the public sector quite often only go into these sorts of arrangements once a decade, and it is difficult for them to develop, maintain or even contract in, buy in, the expertise in needs in negotiating those contracts.

Mr TORBAY: One of the problems I found when looking at the subject was when there was strong expertise which was developing in the early days of these private finance initiatives and public private partnerships is that where there were good skills shown in the public sector to protect that public interest, often the private sector would come along sometimes midway through the negotiations and we would find those people sitting on the other side of the counter not long into those negotiations. I felt that the public was quite exposed in many of those arrangements because it simply could not match it because where they did have skills they were being poached fairly readily.

Mr SENDT: It is certainly an area that always concerned me when I was in Treasury and as Auditor-General that the public sector cannot match, either in terms of the numbers of people or the quality of people, the private sector and cannot match the remuneration which the private sector provides. The costs of negotiations, while they may be large, are often a very small part of the overall contract, so paying someone who is an expert in the field, poaching them from the public sector at double the salary for example may still be a very small investment. That was one aspect of what we were interested in, the contract management, but I think we were more interested in, on an ongoing basis, is there an assessment of how the public of New South Wales is getting value for money from a privately run facility.

Mr TORBAY: Which takes you back to the risk evaluation, where you put the risk and what the impacts of that are.

Mr SENDT: Certainly where the risks were apportioned from the initial contract is one aspect. There is information which we quoted in our report on the average cost per year or per day of a prisoner, but that is only a partial indicator because the Department of Corrective Services itself needs to bear the cost of overheads that apply as far as Junee prison would be concerned, but are not reflected in the daily costs that the Junee prison operators charge. We were more interested in seeing if they had good measures of outcomes in terms of rehabilitation, recidivism, prisoner education, prisoner health, security, et cetera, as well as purely financial measures.

Mr MCLEAY: No other comments?

Mr SENDT: I do not think so.

(The witnesses withdrew)

(Short adjournment)

MARK ANTHONY RONSISVALLE, Deputy Secretary, NSW Treasury, 1 Farrer Place, Sydney, and

IAN WILLIAM NEALE, Executive Director, NSW Treasury, 1 Farrer Place, Sydney, and

BRIAN MARK PELLOWE, Acting Senior Director, NSW Treasury, 1 Farrer Place, Sydney, sworn and examined:

CHAIR: I have been advised you have been provided with the terms of reference. We understand how busy you have been with preparation of the budget and thank you for providing us with your submission today. Is it your desire that this submission form part of your formal evidence?

Mr RONSISVALLE: Yes, it is.

CHAIR: Would you care to make an opening statement?

Mr RONSISVALLE: Firstly, I apologise for the lateness of the submission. To be honest with you there are parts of the submission that do need brushing up. I don't think the submission at this stage clearly articulates the framework around which risk management is being handled in the public sector in New South Wales. We ran out of hours in the day.

CHAIR: Just on that, so we can leave all those issues aside, we would welcome any amendments or additions you might want to make, or deletions for that matter. We would appreciate if, once we have read this document or any other documents, that you will take some questions on those.

Mr RONSISVALLE: This is not a good time of the year for Treasury, as such. The budget consumes huge amounts of resources and lots of things get pushed back and during late June/July there is a lot of catching up required.

CHAIR: We understand.

Mr RONSISVALLE: Since 2002 Treasury has focused its resources on the implementation of a performance planning framework, first through the results and services plans. The results and services plans process is part of our overall financial management framework which includes a requirement to better manage resources. Managing risk is a key part of better managing resources. In the past Treasury has published a number of guidelines. The Committee would be well aware of the Toolkit and the Total Asset Manual guidelines, procurement guidelines. Specifically within that there is the information communications technology guidelines and the Treasury Management Fund guidelines. However, in the end, risk management is an agency responsibility and Treasury can provide guidance material and even mandate its use, but that does not necessarily improve agency's risk management. We do not have the capacity to audit if they are doing it right. We can provide the guidelines but we can not audit.

In the case of the Toolkit there has been a favourable response to the Toolkit when we issued it. Agencies have suggested that they would like to apply it. However, the take up of it has not been as much as we would like.

CHAIR: How do you measure a favourable response?

Mr RONSISVALLE: Feedback from agencies.

CHAIR: In a formal or informal process?

Mr RONSISVALLE: In an informal process.

Mr PELLOWE: There is an informal survey. We actually ran three or four pilots to test the

Toolkit out and it shows it works very well as a Toolkit itself.

Mr RONSISVALLE: We feel that the Toolkit had a favourable response, however, its take up and its application has not been as much as we would like. Again that, in part, relates to the fact that it does require a fair commitment of resources from agencies and agencies have many pressures on them and at this stage they probably have not seen enough value to commit resources to that aspect of their business.

CHAIR: That Toolkit was developed in 1997.

Mr RONSISVALLE: It does need some updating. There have been a few standards that need to be updated. It needs to be integrated with the other documents we have put out since then.

Mr PELLOWE: It is on our web site and although it needs updating it is still highly usable as a Toolkit for the development of risk management.

Mr RONSISVALLE: I suppose what we focused on in the last couple of years is trying to provide incentives for the way agencies actually behave. The results and services plans provide an incentive to actually consider risk management as a key part of an agency's operations. The results and services plan does not deal with all risks. It tends to more deal with service delivery risks, but we found that the results and services plan process has seen agencies having embraced it enthusiastically and as part of that they have embraced the risk management part of that process. The Auditor General made some recommendations in 2002 which we acknowledge in themselves are good things to do.

CHAIR: Just on that, what improvements have Treasury made in response to that performance audit?

Mr RONSISVALLE: Mark is going to take you through the submission and we will cover that issue. While the Auditor General has made some recommendations our focus has been mainly on the performance framework and getting the incentives right for agencies; it is in their interest to do these things, that is where our resources have been focused. There has not been, let's say, sufficient resources available to do everything the Auditor General would like. Mark is going to take you through a few aspects of the submission. I appreciate you have not had time to obviously read the submission but he will briefly summarise it.

CHAIR: Would that be useful to the Committee? We might have a bit of a read, unless you can do it fairly quickly. I don't want to run out of time for questions overall. Will it be a lengthy summary?

Mr PELLOWE: I can shorten it. I will show you one or two of the key documents. It might pre-empt what you ask as well. The first recommendation that the Auditor General made was Treasury ensures that there is a consistent standard for risk management across the public sector. In our submission we have addressed that. One of the things we want to provide as an addendum is a diagram that shows how the various things fit together in one framework. That is the main thing that Mark talked about.

I guess the key thing that we have done since the Auditor General's report is to, as Mark has said, develop results and services plans as part of the budget process. The first attachment that we have provided in submission is the guideline on how to develop results and services plans. I might refer you to page 23 onwards. There is a broad guideline of the generic risk management process. That is taken from the risk management standard. The important thing there is what we are trying to do is link the management of risk, at the enterprise level, to what an agency is trying to do and how they go about doing it.

One of the key things, when the Auditor General talks about a standard and developing adequate risk management, he is principally talking about an enterprise wide risk management system, integrated into planning, and that cascades down to the management. It shows how agencies need to report to Treasury and what the key risks are at the service delivery, strategic level of the organisation.

After the Auditor General's report was issued one of the big accounting firms ran a seminar to get feedback from risk managers on the overall framework. One of the key comments back was public sector organisations, unlike the private sector where there is a bottom line which is profit or loss and, therefore, you can refer risk back to that, whether you lose money, in the public sector you have that dimension as well but it is more complicated in that we have service delivery type objectives. Until organisations are actually clear about what their service delivery objectives are then it is very difficult to define what the risks are.

This is our framework for ensuring that risk is actually properly integrated in an organisation's planning processes. When you come to read our submission, a lot of it focusses on this, and the individual initiatives we have in terms of specific mismanagement guidelines should really fit within the context of this particular tool. The Toolkit is one way of implementing what is required.

Mr RONSISVALLE: The Toolkit tends to be generic and what Treasury has done is it has issued specific guidelines in areas where we consider there is need for further elaboration with further guidance material, such as the procurement and guidelines of Treasury operations, those sorts of things are areas where the Toolkit is not sufficiently detailed.

Mr MCLEAY: What is the third attachment?

Mr PELLOWE: It is one of those examples of, I guess, specific risk management documents that come under this framework and that is actually issued as part of Treasury management framework for agencies.

Mr NEALE: The Treasury Managed Fund, this is in association with an organisation called the Public Sector Risk Management Association and that is a grouping of agencies who come together and talk about how they can manage risks insofar as they affect their costs through the Treasury Managed Fund, which is our self-insurance scheme, and the TMF has money set aside, about $1.5 million per annum, which we use to sponsor projects promoted by agencies where they want to look at a particular area of risk and how to manage it, and we do that on the basis that the lessons get spread throughout the agencies and they can learn from them. This was one of the projects promoted by that association and jointly funded by the TMF, and it is basically quite a comprehensive document giving guidance to agencies as to where they can find assistance to develop proper risk management plans.

Mr MCLEAY: This is not just financial risks?

Mr NEALE: No, it covers the whole gamut of risk management basically.

Mr MCLEAY: I notice it is February 2005. Has that only been launched since then?

Mr NEALE: That is when it was released. It is available on the web site through what we call Risk Insight, which is a TMF risk web site for people to refer to.

Ms BEREJIKLIAN: I am interested in Treasury's opinion of what their role is, for example, if there is an omission or if an agency in particular has not developed sufficient risk management plans according to the guidelines and Treasury sees this as a potential risk in terms of public interest. Do you approach the CEO or have any direct involvement with the agencies if you see huge holes in their risk management plan, or strategy, or do you know what they are about?

Mr RONSISVALLE: The short answer is yes. We obviously have a number of analysts who continue to monitor agencies. If they see a problem in an agency which they feel is not being addressed, Treasury will through either direct discussion with CEOs, or at a Ministerial level, raise issues they see need to be managed. From an aggregate budget perspective there are various risks that the budget faces and they relate back to specific agencies. Wage risk is an issue for the budget and if we do not feel an agency is managing its industrial relations correctly we will raise it with the agency and tell them that they need to improve their game.

Ms BEREJIKLIAN: Does that extend to operational risk as well, oversights?

Mr RONSISVALLE: It gets back to what we actually become aware of. There is a limited amount of people in Treasury who are able to spend the detailed time necessary to get behind some of the agency operations. For example, it might be that some agencies go into contracting with non-Government organisations and they may not be doing that as well as we think they should be. If we become aware of it we will often sit on a steering committee or an oversight committee which will look at that aspect of their operations and give them suggestions about how they can improve their performance in that area. We are actually involved in one of those at the moment.

Mr PELLOWE: The RSP process will help because for all 64 agencies we are getting this information coming up and when we see this we do not think it is capturing the real risk of the agencies, or we do not think that the risk strategy which has been proposed is very good. That may be indicative of the fact that there is a problem with the risk management further down, therefore this provides a possible area of concern that we would follow up.

Mr RONSISVALLE: From our perspective agencies do not have every skill they actually need to operate. In the case of procurement of capital works, we have a rating system which allows them to do certain things on their own and then to do other more complicated things they have to seek outside assistance. We have that in the case of capital works procurement. In the case of contracting, if we feel that they do not have that expertise we will offer to provide that expertise to them to the extent that we actually can.

Mr MCLEAY: A lot of agencies in their surveys have indicated that they strongly agree that the results and service plan is essential and certainly feel that it helps them manage risk. Is the results and services plan compulsory and how many agencies are doing it now?

Mr PELLOWE: It is compulsory for all budget dependent agencies and there are 64 of those so everyone who gets funding from the budget has to do it as part of budget process. All 64 are doing them. We have an internal assessment process in place where we have a team of policy people going through them. We have a self-assessment process going on where we are trying to get agencies up through certain stages. We see this as a fairly long-term process in terms of developing these agreements so each is given an internal rating and we feed that back to our analysts and we are trying to get the rating up.

For example, at the moment we are really targeting on getting these so they really do epitomise what an agency does and build a good set of performance indicators around that. The risk management stuff is a bit further down the track in terms of getting that up to a standard we would like. We need to be clear about what they are trying to do and what they are trying to do first, and you can articulate the risks around that framework.

Mr RONSISVALLE: That is a five point scale, if I remember, and most agencies when we first did this were about two and a half. Now we have got the average probably closer to a bit over three.

Mr PELLOWE: Three is where this really epitomises what an agency does and why and five is where all the performance information cascades down through the organisation, so there is a performance management system in place which feeds up through this, and this is clearly linked to other plans like the risk management plan and those kinds of things. We are trying to get to that stage.

CHAIR: Can you briefly talk about the service and resource allocation agreements, and how they are linked in with the results and services plans?

Mr PELLOWE: They are not. The service and resource allocation was very much a predecessor of the results and services plans.

CHAIR: They are no longer there?

Mr PELLOWE: They no longer exist. Service and resource allocation agreements applied to the 11 biggest agencies. They are long agreements which we know adopted a results logic approach and this really captures in a much more succinct way what an agency's business is about. We learned from the services resource allocation.

CHAIR: Did those agreements form the basis for whole of Government risk management?

Mr RONSISVALLE: The short answer is no. They were agency specific agreements. They were not collated into one whole of Government document. As Mark said, the documents were not particularly successful because they ended up being seen by most agencies as a compliance exercise and they tried to be too much and cover too many things and, narrowing it down, we have the results and services plan which made the thing digestible to management, both at the agency level and the Treasury level.

Mr MCLEAY: Are we talking about tools that may not be used as widely as they once were? Regarding the Treasury Toolkit, a lot of agencies in their surveys have indicated they are aware of it but do not use it. You mentioned in your opening stage that it is still widely available. From my reading of a lot of the evidence, a lot of agencies do not use it any more. This tool has replaced it. Is that the situation?

Mr RONSISVALLE: The way that I characterise it, this is the sort of document which gives them the impetus to do something about risk, and the Toolkit is something they can use to develop their strategies associated with the risks.

Mr MCLEAY: You still expect them to use the Toolkit?

Mr RONSISVALLE: As far as we can see, the reason the Toolkit was not used was there was not enough incentive to apply the resources that were necessary to be used under the Toolkit. The results and services plan hopefully provides sufficient incentives to allow them to go back and look at the Toolkit. To be fair, the Toolkit probably needs a bit of work to update it. There have been a few standard changes since it was issued. Like most things it could probably be simplified a bit and that is one thing which is on our forward agenda. It is not something that we are actively working on at the moment.

CHAIR: Can you also address the issue of the Australian New Zealand Standard on risk management and how that fits in with the Toolkit and the results and services plan?

Mr PELLOWE: The toolkit was based on the COSO framework, which is a US frame. When we did the Toolkit the Australian Standard was not out. It was a Toolkit based on the COSO framework. They are very similar. They are similar in what they are trying to do. One of the principal differences is the standard is a kind of typical Australian Standard. It is quite a succinct standard. It just takes you through a number of simple processes and provides you with a structure for developing risks. The COSO one is similar, apart from there is masses of supporting information about questions to ask on specific areas of risk, and because the Toolkit actually does that, it provides a series of questions to facilitate discussions with agencies, a lot of the questions in the Toolkit are based on what was developed in the US under COSO.

CHAIR: I will just read to you from a submission to us from the Audit Office. It says that the Treasury Toolkit is now out of date and does not reflect the current best practice. Given it is based upon COSO, which has been significantly updated, if the Treasury guidelines and Toolkit are in turn to be the standard for New South Wales public sector agencies they need to be updated now and on an ongoing basis. That could be based on either the Australian New Zealand Standard or on COSO version 2. The Auditor-General would probably lean towards the former, or they could determine best features of both. However this is a matter for Treasury to determine. Have you a comment on that strong submission, further to what you were just saying?

Mr PELLOWE: It comes back to the issue of where we actually direct our resources, and at this stage we have been concentrating on the results and services plan framework, which provides incentives for agencies to start using these tools. As Mark said before, the problem with the Toolkit was we ran three or four pilots. Everyone who went through the pilots loved it, claiming that it was very useful, and we were happy that it worked. The problem was take-up because they insisted on lots of other things to do and there was no incentive for them to do that. As opposed to other things, they may not want to do it.

Mr RONSISVALLE: The development of the Toolkit itself was a very resource intensive process for us. If we were committing resources to that we would have to take resources away from the results and services plan.

Mr MCLEAY: Why not take just it away and say use the standard?

Mr PELLOWE: Because they are different things. The standard provides a way of developing a risk register and risk management plans and it is quite a high level. The Toolkit is actually that, it is a Toolkit, so it facilitates for somebody to act as a internal consultant within an agency and it provides wheels and a series of questions where agencies can self-assess where they are currently and decide where they want to be in terms of best practice and costs benefits for them and gives them guidance on developing some strategies to get from A to B. The Toolkit and Standard are more complementary.

We still see that the Toolkit is not obsolete. It is still useable. It provides a generic set of questions that agencies can use, but we make it clear that they are just a generic set and agencies need to customise those for their own particular circumstances and that might mean looking at the Standard or specifically the Treasury risk management guidelines at a more detailed level, to come up with a set of customised questions they can use.

There is no problem in upgrading the Toolkit and using the methodology of the Toolkit, but upgrade it themselves to reflect the fact that parts of it do need upgrading. There are two or three specific areas that need improving in the Toolkit. It is certainly not obsolete.

CHAIR: The current guidelines for preparing results and services plans include consequence and likelihood matrices for analysing risks which you put in as a guideline for preparing results and services plans. Is it your intention that all agencies use this matrix or are you providing that simply as an example?

Mr PELLOWE: Simply as an example.

CHAIR: Do you encourage them to use a matrix?

Mr PELLOWE: I guess those are the standards we would expect. If you are looking for a methodology to develop a risk management plan the standard is the place to go and that is why we have highlighted it. It is a guideline. We have not made it mandatory that they use that particular standard.

Mr MCLEAY: Do you think that there is capacity for a service-wide matrix to be developed, not necessarily by Treasury but obviously they are the only ones that would.

Mr RONSISVALLE: People are toying with the idea of a Government-wide results and services plan. People are baulking at that. In an ideal world I suppose the answer is yes. It is just the development. It is the resources that it would require for such an exercise.

Mr NEALE: A lot of agencies are different sizes, of course. The Department of Education may spend more time on risk management than a smaller department. I would like to point out too that the Toolkit, when it was developed, which I had a little bit of involvement with, was never mandatory. It is something put out there to assist agencies and there are other ways to go about assessing risk, which is still the case today. At lot of agencies rely on their internal auditors to get involved in some of those aspects and Treasury staff used internal auditors to facilitate it within our organisation.

Mr MCLEAY: Now for the in budget agencies the results and services plan is mandatory.

Mr NEALE: Yes.

Mr MCLEAY: That has an essential component of risk management. Whatever mechanism they use to do that is up to them.

Mr NEALE: Yes.

Mr MCLEAY: Would it be easier for you to assess their results and services plan if they were using a matrix, or it really does not matter?

Mr RONSISVALLE: It is always easier for the other side to assess something that comes in a standard format, but whether that standard format is the most appropriate format for that agencies, there are variations in the nature of the agency, which means you may have a slightly different methodology.

Mr MCLEAY: In the results and services plan, the consequence and likelihood of risks, what level of detail are they required to achieve; semi qualitative or qualitative assessment of risk, how deep do they have to go?

Mr PELLOWE: In the results and service plan it is qualitative. We have tabled the results and services plan.

Mr RONSISVALLE: Page 14 of the Southland Department of Law Enforcement. I should point out that this is what gets in the document, for example, the results. At the agency level there would be more behind this. This is what gets in the summary document, which is the results and services plan.

CHAIR: What is the role of the recently issued TMF Guide to risk management in the New South Wales public sector risk management framework?

Mr NEALE: It is guidance to agencies that assists them in managing their risk. The aim of the Treasury is to offer incentives to them to do better, particularly with their insurable risks.

CHAIR: What sort of incentives?

Mr NEALE: Monetary incentives basically. When agencies join the fund we assess their risk and how much they should pay in premiums and we set premiums having regard to benchmarking from other states, where that is possible. The bigger departments certainly are influenced by the performance of other states and we set a benchmark premium for them. At the end of the day what they actually pay to the TMF for their insurance cover depends on their actual performance. If they do badly they will pay more and if they do well they get rewards. The Department of Health on a regular basis does well on managing its insurable risk, the primary one being worker's compensation.

CHAIR: Do all agencies have their insurance with the Treasury Management Fund?

Mr NEALE: No. When the fund was set up it was designed for government sector agencies. The Auditor General did a report a few years back saying that he thought we should consider extending it more widely to other agencies, and we have done that. It is voluntary to the other agencies if they wish to join. We have the Hunter Water Corporation. Sydney Water Corporation is currently considering it.

CHAIR: Those who are not in the Treasury Management Fund, do they have access to this guide?

Mr NEALE: I am not sure about that. This guide was published on a TMF site which is password protected. I am not sure whether agencies outside that family have access to it. There is no reason why they should not.

Mr MCLEAY: We could not get access.

CHAIR: How does Treasury ensure that agencies follow those guidelines, is there an expected time frame for implementation, for instance?

Mr NEALE: No. As I say, they are just guidelines, they are not obligatory. If we perceive an agency is doing particularly poorly with managing its risks we will focus on that agency and try and give it assistance and we will talk to the agency about how they can improve their performance in that area.

CHAIR: With the upcoming restructuring of the Treasury Management Fund, can you explain the risk management services in the restructure?

Mr NEALE: It is fairly similar to what it is now. What we did with the new structure is we brought in more claims managers, rather than having just one. As a result of that we also split off some of the other services. Risk management is a separate service which is provided. We currently have tenders, which are closed, and we are evaluating them at the moment to get in someone to handle that area. The thing is with the new arrangements Treasury has established a unit within Treasury of about 17 people who will be more involved in analysing the data that has been provided by the claims managers and assessing their performance and also the performance of agencies. We will be much more hands on than what we have been in the past in that area.

Mr RONSISVALLE: Just as an example, I will not talk about the specific agency, some agencies are very poor, and have high worker's compensation bills and that is a budget pressure on that agency, because we only fund them to benchmark premium. It does cut into their service delivery or other parts of their operations. When that has been identified we say to that agency, your worker's compensation is too high, your TMF premiums are too high, what are you going to do to get them down? We require them to give us strategies. Sometimes it takes a while for those strategies to bear fruit. In the case of the Department of Health those strategies have proved very effective in the last couple of years. I would like to think that another couple of agencies would follow their lead.

Mr MCLEAY: Are there mechanisms for you to become aware of the way agencies manage risk? For example, for procurement of ten million there is a gateway testing? Is there other mechanisms like that procurement device, like a flag that sets off to say go and look at it?

Mr RONSISVALLE: There is a number of guidelines. There is Treasury operations guidelines, if that is what you are referring to. There is the TAM guidelines, procurement guidelines, within that there is the total asset management guidelines, how you manage your assets to get the most out of those assets to keep the balance between maintenance and capital upgrades, those sorts of things are covered in the manual.

Mr MCLEAY: I am not asking for a self selection on their side. When you become aware of agencies not managing a section of their risk well then you will give assistance. How do you become aware of it?

Mr RONSISVALLE: I think the short answer is that it does require the analysts we have, the monitoring agencies in their discussions with the agency to become aware of that. The results and services plans gives you some clues and requires a report back on some items but that is not every risk that they are exposed to. Therefore, it becomes a relationship issue between the agency and the analyst that Treasury employs. Those analysts do pick these risks up, sometimes not as early as you would like, but those risks are identified.

Mr MCLEAY: When we spoke to the Auditor General they suggested that there could be legislative changes in order to ensure compliance.

Mr RONSISVALLE: The Auditor General tends to like legislative solutions to problems. I suppose there is the argument about does regulation actually work. I think our experience is it is better to provide the incentives to get agencies to operate in a way you want them to operate rather than mandate it. If you mandate it you still don't know whether they are actually doing it or not. You have to have a framework for reporting back or auditing. If you provide the right incentives, from a Treasury perspective, we think that provides a better hit rate than them actually complying with what you would like them to do.

Mr MCLEAY: It seems there is an awful lot of faith in the results and services plan. Has there been a risk analysis, is this the best way to go? What is the risk if this does not work?

Mr RONSISVALLE: To be fair, the feedback we get, you have had the same feedback, that the agencies like this approach. It is a tool that will not work in all cases. The fact that some agencies are still on the low end of the scale on these plans, and they are the ones we tend to want to focus on, some of those agencies still struggle to actually define what their purpose for being in existence is. There are always the traditional means of picking up risks at agencies which may not get reported through the results and services plans.

Mr MCLEAY: You are confident that the results and services plan, a tool of Treasury, is the best way to focus risk, not legislation?

Mr RONSISVALLE: That goes back to what I said earlier, that mandating things does not necessarily ensure compliance with guidelines. The best mechanism, in my view, is to give them a reason that they want to apply the guidelines themselves.

Mr MCLEAY: You can not enforce good management.

Mr RONSISVALLE: No. There is probably a few examples of that on an annual basis.

CHAIR: What messages would you like to leave the Committee in respect of risk management in the New South Wales public sector.

Mr RONSISVALLE: I would not sit here and pretend it could not be improved, there are obviously things that can be done. It becomes a choice about where do you think your efforts should be focused. The results and services plans focus on service deliveries, that is a very big risk which the Government is exposed to and in some ways that is more important than worrying about whether every voucher has been signed correctly. I suppose it is targeting your efforts in the areas which produce the biggest return for Government and at this stage we think we are doing that. I am happy to take the Committee's views on whether they think that is correct or not. I suppose that is our assessment at this stage.

Mr MCLEAY: The results and services plan is a document from the agency and their relationship with Treasury.

Mr RONSISVALLE: Yes.

Mr MCLEAY: Is there any proposal that that should be published over time?

Mr RONSISVALLE: In the longer term what we would like to try and do is connect together the results and services plan, what appears in budget papers and what gets reported in annual reports. That is the sort of the linkage we would like to establish.

Mr MCLEAY: Are we at the beginning of stage one of that process?

Mr RONSISVALLE: You will find that the budget papers are evolving over time to start picking up the things that are in the results and services plan. For 2006/07 we are intending to modify some of the layout of the budget papers to pick up a montage from the results and services plan framework and part of that is also then we need it reported that the indicator is reported in an annual report so there is some accountability.

(The witnesses withdrew)

(Luncheon adjournment)

ALASTAIR JAMES HUNTER, Chief Financial Officer, Department of Commerce, 2-24 Rawson Place, Sydney, affirmed and examined:

MARCUS FRANCIS TURNER, Manager Corporate Risk Services, Department of Commerce, 2-24 Rawson Place, Sydney, sworn and examined:

CHAIR: I have been advised that you have a copy of our terms of reference for this Committee and the chamber, is that correct?

Mr M TURNER: That's correct.

CHAIR: We received a submission from you. Thank you for the effort you put into that. Is it your desire that that submission form part of your formal submission? Would you like to make an opening statement?

Mr M TURNER: Yes. I will make an opening statement. I have been with Commerce now for only four or five months. Marcus has been there for some time longer.

CHAIR: You were with Treasury before?

Mr HUNTER: Yes. I did the presentation over here on the budget papers. Commerce treats risk management very seriously, both internally, in terms of how we manage our own risks, and also how we manage the risks for what I see as Commerce's objectives. Commerce's objectives are to minimise costs for other agencies, increase value for other agencies and manage the risks for other agencies in terms of the ICT projects and the construction work that we do. Internally there has been an ongoing development of risk management within Commerce. Marcus might want to touch on that in more detail.

We are at a stage at the moment within Commerce, and I guess it is partly due to the fact that some new people are there, that we are actually reassessing our objectives and reassessing our risks, especially at a corporate level. There has been some work carried out there in terms of the appropriate models and a reassessment of what were thought to be previously the risks of Commerce to see they are currently the risks in place at the moment.

CHAIR: We have heard evidence that maybe Commerce shouldn't be taking risk for your client agencies; is there any weight to the argument that they should be a little more involved in managing their own risks rather than throwing the ball to you?

Mr HUNTER: It is a partnership. Say with the Department of Education and with the major ICT projects, they own the asset. They maybe do not have the expertise. We have the expertise and, therefore, in trying to look at this from a whole of Government perspective I think it is important that they do not pass over the risk to us but in turn we are responsible to ensure that the risk is managed properly.

Mr MCLEAY: Give us an example?

Mr M TURNER: Traditionally with the way risk has been approached across the State has been that New South Wales Commerce, or previously what was DPWS, have provided, through procurement and on the construction side, certain frameworks to assist client agencies to manage their risk. Some of these things have included the principal arranged insurance. Insurance, as you are no doubt aware, is what you would do in order to mitigate the risk. It is a risk transfer to the insurance company.

What we have found is that for some of the construction type works that we were required to undertake on behalf of the State, some of the contractors weren't able to get appropriate levels of insurance. In order to do that we have then gone to the market place, through brokers, to basically form various products so there will be effective risk transfer between the client agency to the contractor undertaking the works. If that is in relation to a schools project then, setting aside the schools maintenance area, but the Department of Education may engage us to project manage a particular body of works for them and we will have the contractor undertake to do various activities and through contractual provisioning, and that sort of risk transfer, and also through the insurance provisioning, look at effectively shifting this and sometimes sharing it between the State and private sector.

CHAIR: You are saying that one of your risks as a department, one of your significant risks is managing the client's risks?

Mr M TURNER: To supply them with an appropriate framework to manage their risks.

Mr MCLEAY: Strategic advice. Do they understand that?

Mr M TURNER: The relationships we have got with the departments, they certainly seem to understand the nature of the relationship. That includes recognising that New South Wales Commerce has been the principal contractor in relation to various bodies of works. If you look at it from a procurement perspective then they seek our advice in relation to engagement of either broad frame procurement arrangement or, alternatively, on specific projects like the IT type projects.

Mr MCLEAY: Give us a real life example; school X wants to build four class rooms or something?

Mr M TURNER: There was some work undertaken at Mt Colo public school.

Mr MCLEAY: Close to home.

CHAIR: Got kids there?

Mr M TURNER: Yes. There is clearly no conflict of interest in this. Having said that what occurs in relation to that is that the school required a body of work to be undertaken and that was identified by the Department of Education. The scope of works was mapped out by the Department of Education and they then put it to New South Wales Department of Commerce saying we have got this body of work that we need to have undertaken. We understand that there are contracts for the provision of such services with a variety of organisations.

Mr MCLEAY: The body of work, like a building?

Mr M TURNER: Yes.

Mr MCLEAY: Try to make the example as real as possible.

Mr M TURNER: Building the hall at Mt Colo school. From that perspective New South Wales Department of Commerce then enter into an arrangement with The Department of Education to ensure that this work is undertaken within their specifications and to an appropriate level. We also have the principal controlled insurance, which is an arrangement through Marsh Brokerage, where the contractors and subcontractors are appropriately covered in order to shift the risk from New South Wales State through to contractors and, therefore, their insurers. In effect, what we then do is in the event of something going wrong - which did not happen in this case, the works proceeded before time and under budget - in the event that something goes wrong, and we have not had many of these, then there would be recourse through the insurance arrangement back to the insurance sector. The risk that we are trying to manage in this whole process is that it is not in the organisation's interest any more than it is in the State's interests.

Mr MCLEAY: Which organisation?

Mr M TURNER: New South Wales Department of Commerce. To be embarking on extensive legal action against contractors and subcontractors. Principally because, in the event of something going horribly wrong, they are typically not able to carry that against their balance sheet and profit and loss. You end up bankrupting them. In the event that they do not have appropriate insurance in place that then falls to the State to pick up the lag. The approach that we have taken with that is to ensure that there is an appropriate level of insurance so that that risk is then transferred away from the State through to a pool of insurance companies.

Mr MCLEAY: One of the queries we have got is that this is still a Department of Education and Training building.

Mr M TURNER: That's correct.

Mr MCLEAY: If they say to you, please build us a hall, a covered outdoor learning area. Once you have agreed to take on that job, Department of Commerce has agreed to take on that job, does the Department of Education and Training say it has gone to Commerce now, they will do it? We know that within 12 months we will have a new building and then you take the risk and make sure that is managed, or are they still very much part of the process? It is their bit of property, it is their building, they are still very much responsible for their risk. It is in their matrix or does their matrix say it is low risk because it is in Commerce's hands?

Mr M TURNER: It is in their matrix, in that we will take a degree of ownership of it from the perspective of our management of that project. Part of our management of that project would be to relate to the client entity, in this case the Department of Education, they are aware of how it is all going because one of the issues they need to deal with is how well that project is progressing in relation to disruption to school environment and the ability to continue to deliver educational outcomes. They have still very much got a vested interest in how well the project is going, or indeed how poorly. Also an obligation that in the event they become aware of problems they certainly get in touch with project management in New South Wales Department of Commerce to say we may have an issue coming up here, let's work it through.

Mr MCLEAY: That is one of the things we have been getting mixed evidence about. It is obviously a lower risk to go with Commerce, because that is your speciality skills, than to use someone else. Once they have chosen to use your services to get the building, or whatever it is, does that mean that risk is now, for them, finished or is it still part of their job? It is still building a big hall in a school playground. It is a high risk activity you would have thought.

Mr M TURNER: I agree. The risk is never reduced to nil and the risk is always then shared across the State for whatever we retain and are not able or prepared to shift to a private sector entity, including the insurance sector. From that perspective what we are doing is through an assessment of the risks, through identifying what those risks may be, as to whether they are occupational health and safety issues or interruption to the school, in looking at a likelihood and an impact, managing those through various activities such as the divestment of the insurable risk to the insurance sector, to then come up with a residual impact and likelihood. As a result you never reduce these things to nil because we do not have inexhaustible funds in order to do those types of things.

Mr HUNTER: I can not tell you when but the funding mechanisms were changed. The Department of Public Works used to get funded directly. Now education gets funded directly. It is their asset and it is their dollars. Setting up behaviours for them to take ownership and get involved in that construction, it is that they do not have the expertise, and that is what they are buying from Commerce. Their asset is still their asset. If the school hall does not get built Commerce have an issue but it is education's asset, they are the ones that can not deliver on the outcome, which was to provide a learning facility for their children. It is going to flow up through the principal and the administration at education and up to the Minister, I suppose. That was changed some time ago. By them owning the asset and them having the funding does keep some of the risk with them.

Mr MCLEAY: Did that structural change, do you think, made people much more aware of risks, agencies aware of their risks?

Mr M TURNER: You are talking about?

Mr MCLEAY: The budget change. Instead of Commerce getting all the capital expenditure budget that actually agencies got it instead.

Mr M TURNER: If you think about it, education puts up its capital program and it is approved in the budget and it gets funding for that, they have an interest to make sure that it is spent properly or they do not get it next year.

CHAIR: That hs been happening for some time, has it not? It is not new that agencies have their own capital works budget.

Mr M TURNER: It is definitely not in the last five years.

CHAIR: When I was on the Public Works Committee last Parliament the Department of Public Works and Services seems to be nearly self funding in charging out for services to these agencies.

Mr MCLEAY: I think the change came when there was a big public works restructure.

Mr HUNTER: I cannot say.

CHAIR: You have had a major restructure of your department. How does that impact on your risk management framework?

Mr M TURNER: Significantly, in a word. In 2003 Commerce was brought about, in about April I think it was formed. Prior to that New South Wales Commerce was a Department of Public Works and Services and had undertaken a facilitated series of workshops with PriceWaterhouseCoopers in order to identify organisational risk. Part of the challenge that was then thrown to what was then Commerce, was to determine the risk management framework across the board. Broadly, the approach that we have taken within Commerce is to have a look at AS/NZS 4360:2004 which is the risk management standard and that is the policy that was then endorsed by the risk and audit committee in December of last year and promulgated thereafter. On that basis, we have then been developing the principles and model which was put before the risk development committee in April of 2005.

The intention behind those things was, rather than take a fragmented approach, to ensure that there was a consistent approach, so to deal with some of those management type issues. We feel that this is important because unless there is a consistent understanding of not only the framework but also the definition and identification of risk, you can end up with an inconsistency of treatment. From that perspective what we are trying to do is to ensure that risks across the State are mitigated in terms of commerce's ability to have an influence over the management of those risks, whether it is in a construction arm or whether it is in procurement, in making arrangements for broad based contracts for goods or services across the State, but also as it pertains to the workplace relations through the Office of Industrial Relations and also to fair and equitable trading with consumers and between businesses through the Office of Fair Trading.

Mr MCLEAY: Do you use a matrix?

Mr M TURNER: We do have a matrix and our perspective is that that sets the risk as to what is acceptable across the organisation. That was one of the things that was then subject to review by the executive and we are again going through that process at the moment.

CHAIR: Which camp are you in, industry specific matrices or a generic one for the whole public sector?

Mr M TURNER: I would like to see one for the whole public sector.

CHAIR: You do not think it would be unwieldy and other agencies might not fit into that matrix?

Mr M TURNER: I do not believe that it needs to be unwieldy. One of the elements that we are trying to deal with in Commerce is a microcosm of what you are talking about. We have a diversity of operations from construction through to industrial relations and through to fair trading and procurement across the State, so the types of activities we are undertaking is something we have sought to address in setting our risk at the time.

CHAIR: Do you have an example of such a beast?

Mr M TURNER: The beast that we have at the moment is basically a five by five matrix and that is available within Commerce. I do not have a copy with me at the moment. That is looking at defining impacts of risk across a variety of indicators and that was previously a methodology that was endorsed within the risk management standard, but I take that on notice.

CHAIR: If it is not commercially sensitive we would like to have a look at it.

Mr M TURNER: Yes.

Mr HUNTER: We are not talking about the commerce risk, we are talking about the definitions. I do not see that that is a problem.

Mr MCLEAY: If you use the matrix and you are talking about the standard, I guess that you would say that you are aware of the Treasury Toolkit and you did not use it, is that right?

Mr M TURNER: No, I would not agree with the statement.

Mr MCLEAY: You are aware of it and you did use it?

Mr M TURNER: Yes.

Mr MCLEAY: You still use it?

Mr M TURNER: Between the Treasury Toolkit and the standard, together with discussions that we held with other agencies within the sector, the Commonwealth agencies and also the private sector, we then developed our framework from that and in addition to those elements there is also the insurance provisioning arrangements and other risk management frameworks that had been made available previously under Public Works and Services.

Mr MCLEAY: You said that you think that the Toolkit could be revised to more strongly reflect opportunity and to strengthen communication and effective risk management. Would you elaborate on that?

Mr M TURNER: With the opportunity to bring it back to a real example, with the Office of Fair Trading you can look at the downside risks that are associated with undertaking particular activities. Part of the weakness associated with that is that you tend to miss some of the opportunities that are available. The broad strategic direction for fair trading is to provide for fair and equitable trade within New South Wales. An opportunity in relation to that is that with improved communication methods for both industry and consumers, we can then improve the achievement of that objective, so from that perspective we are then saying we perceive an opportunity here to better achieve what we set out to achieve through the identification of particular strategies.

Mr HUNTER: Most people, when they think about risk management, think about all the bad things that can happen and how we stop the bad things from happening whereas how we are looking at it in Commerce is looking at what the opportunities are as well.

CHAIR: That is why Commerce is leaps and bounds ahead, positive outlook, risks and opportunities.

Mr MCLEAY: Do you use the risk results and services plan?

Mr HUNTER: Very definitely. The results and services plan developed by Treasury clearly sets out, if you follow the logic behind the results and services plan, it very clearly as you apply it to Commerce, clearly sets out what the objectives of Commerce are and then it cascades down and it keeps coming down and down and down until each person within the organisation can put their hand up and say that is what I do, and that is how it feeds into an objective way up here which relates to improving the Government performance generally. You have got to have that first, and then once you know what your objectives are and your results logic is within the organisation, then you can say what risks or impediments are there to delivering that, and as you said earlier what opportunities are to try to enhance it. You cannot do it without the RSP.

Mr MCLEAY: You have a results and services plan?

Mr HUNTER: Yes.

Mr MCLEAY: You have the Toolkit, you have the standard?

Mr HUNTER: And you have the total asset management plan which sits with that as well, and then you have your financial plan, which is your budgets, and you have your corporate plan, and it should all be lined up with RSP sitting on top of it so within each document you know where you are headed, so you do not go off and purchase, sell or do something with assets which do not meet your corporate objectives.

Mr MCLEAY: Does that framework suit you? Do you think it could be enhanced with any particular legislation saying you must manage risk, or should there be policy saying you have to manage risk?

Mr M TURNER: If you are to draw on what has occurred within the US and have a look at the Sarbanes Oxley legislation, the 404 provision of that basically says you have to have these various things in place. The problem associated with that is that you can end up with a view to risk management which is strictly a compliance basis. I feel that in pursuing a standard approach we are looking at best practice rather than simply meeting a compliance issue.

CHAIR: So you think culture is more important?

Mr M TURNER: That is right, and that is one of the things we are addressing within Commerce, to get a uniformity of understanding or awareness so that we can say at any particular point in time risk management becomes an integrated part of the day to day decision making process. Ultimately what we are getting towards is a rigorous decision making process as distinct from a rigid one.

CHAIR: We understand that the Government Procurement Services Unit are performing gateway reviews for major procurement by general Government agencies. What methodology is being applied to assess the risk management for projects being reviewed?

Mr M TURNER: The gateway assessment project is something that is undertaken by Commerce on behalf of Treasury and at its essence Treasury set the criteria against which these are measured and that includes the approach that is being used for risk management. From Commerce's perspective, after having spoken with some of the officers who undertake these reviews, the approach that they take is to determine whether there appears to be an appropriate risk management mechanism in place. In terms of pulling that apart and determining whether that is a completely integrated or very rigorous process, that does not tend to fall within the mandate of what the gateway reviews are meant to be.

CHAIR: Have you noticed any consistent or common oversights identified in that process?

Mr M TURNER: Oversights in terms of omissions?

CHAIR: Yes, by the agencies in that process.

Mr M TURNER: I would not be able to comment on that but I can certainly seek information and advice.

CHAIR: Do you think agencies are quantifying major risks?

Mr M TURNER: I think, yes and no, for a balanced answer.

CHAIR: Tell us which ones are and which ones are not.

Mr M TURNER: Again I am not able to tell you which agencies are and which are not. The principles of what you are getting towards, there are some risks inherently able to have a value placed against them and other ones that are far less able to have financial values placed against them and hence the approach that we have taken within the matrix that we are developing within Commerce, is not to simply focus on a financial element but also to look at social responsibility and occupational health and safety, environmental type issue, principally because those last couple have strict liabilities associated under legislation, so it is not only within Commerce's and the State's interest to manage those, but also you can tie a direct relationship back to individual manager's responsibilities.

Mr HUNTER: Treasury also has an ongoing process there to do risk management plans. I think it might have been highlighted in the Budget Papers a few years ago.

Mr MCLEAY: I guess that is the point. There is plans to do it and people that are doing it all agree that it is a great idea, we should do it, but there is nothing to say any Government agency should. Not even in budget agencies have a mandated requirement to do risk management. Obviously with the results and services plan you cannot actually do your results and services plan without doing risk management.

Mr HUNTER: Certainly it is the other way around. You need to do your results and services plan first.

Mr MCLEAY: That is what I meant. You cannot complete it without doing the other.

Mr HUNTER: You almost can. You can look at your results and services plan and say this is the result that I want to achieve, and it might be an outcome. Say in health it might be to make people healthier, but it is a very hard thing to measure because there are lots of factors contributing to that. You bring it down a step to the things that you know that you are doing that are contributing to that and you say can I measure that. That still might even be hard to measure, but you keep coming down until you actually perform what we call intermediate results, and that is where you measure it. Once you have established that, you then work out what do I need to do in order to achieve that, and then your risk management strategy sits under that. You need the RSP done first to then do your risk management, but agencies should not wait until the RSP is complete.

It sounds easy but it is a difficult task, having been on both sides of the fence and tried to instruct agencies on how to put it together, and then being on the agency side and trying to put it together. It is a difficult thing to do. You cannot wait until it is all done and all Ts are crossed and Is are dotted and then go and do your risk management strategy. You need to start it.

Mr MCLEAY: You are saying you have to do it. Everyone should do risk management. The Auditor-General said in 2002 that less than half of Government agencies had a risk management plan.

Mr M TURNER: How do we resolve that?

Mr MCLEAY: How do we get more compliance?

Mr HUNTER: You could have legislation and that would just mean that whatever you put in the legislation that is exactly what you will get, but I think the Government probably wants a bit more than that. I think you said it is culture.

CHAIR: Who is going to drive that, you or Treasury?

Mr HUNTER: Within our own organisation it is the Commerce executive, but within the public sector generally, Treasury, Premier's, Cabinet Office. It is probably a central agency that will drive that. I cannot really comment on that. If you get health in here you might find they have a robust risk management plan in place.

Mr M TURNER: One of the failings with putting things in place and saying you must do this is that there was a process that was embarked upon within Family and Community Services at a Federal level and they implemented a risk management framework which I was able to have a look at, and it was very good. Notwithstanding the fact that it then ceased to be something at the forefront of their consciousness, in that it wasn't then we will do this, and again you end up with a cultural issue of the management of those risks and monitoring them tended to fall away a little bit, and the staffing levels associated with ensuring it was done, also tended to fall away accordingly.

Whether those things are part and parcel of budgetary redistribution may well be the case, but as to how we can best deal with that and manage it, my personal view is that risk management has available to it a whole range of benefits, including knowledge management, which typically is not handled very well across most sectors, including the private sector.

The reason I say this is because if you go through a process where you identify what can go wrong and what can assist you to achieve objectives, you assess them and then record even just briefly what actions you undertake to either mitigate those risks where there is an adverse effect, or augment them where you have got an opportunity. In the absence of recording that information, you can repeat the same mistakes or miss capitalising on opportunities.

Mr HUNTER: Maybe the wrong impression is being made, but Commerce does manage its risks. I think that the important thing is, as I said right at the start, from my point of view as Chief Financial Officer you have got to keep reviewing it and that is what we are doing at the moment, especially in an organisation that has gone through some fairly significant organisational changes, you have to keep going back from my point of view, from a financial point of view, and reassessing where we are at.

(The witnesses withdrew)

(The Committee adjourned at 4 p.m.)