

Contact: Michael Pratt
Our Reference: TA21/2183
Your Reference: D21/6011

Mr David Shoebridge MLC
Chair
Public Accountability Committee
Parliament House
Macquarie St
Sydney NSW 2000

Dear Chair,

Inquiry into Transport Asset Holding Entity

Thank you for your correspondence dated 23 November 2021. New South Wales Treasury (**Treasury**) welcomes the opportunity to respond to the Public Accountability Committee (**PAC**) in relation to its inquiry into the Transport Asset Holding Entity (**TAHE**), in particular, the evidence provided by a former KPMG partner, Mr Brendan Lyon, and other witnesses at the inquiry.

We confirm that Treasury has no objection to the PAC publishing Treasury's response on the inquiry webpage. We consider it essential for procedural fairness that it be published, given public statements made under privilege by Mr Lyon and other witnesses, and the documents currently available on the inquiry's webpage.

Accounting treatment of TAHE

A critical element of TAHE that the PAC has been examining is its accounting treatment. In his testimony to the PAC, Mr Lyon made a number of statements in relation to the accounting treatment of TAHE. Under privilege, he attacked Treasury's professionalism and integrity in relation to Treasury's accounting advice. He not only accused Treasury of errors but stated that Treasury 'essentially made up' the numbers in its submission to Cabinet.

For close to 200 years Treasury has been supporting the NSW Government on financial and fiscal matters and is the lead agency responsible for financial management of the NSW economy. It has dedicated and highly experienced professionals who are properly qualified to advise Cabinet on accounting issues and interpretation of accounting standards. One of Treasury's core roles is to review, provide comments and where necessary propose corrections to all Cabinet submissions, including on fiscal and financial issues contained in consultant's reports that are attached to agency Cabinet submissions.

Treasury has openly acknowledged that TAHE raises complex accounting issues. Given the complexity, and to provide further assurance of Treasury's own advice to Cabinet, Treasury engaged Ms Heather Watson, who also gave testimony at the inquiry. Ms Watson is a highly qualified accountant, and an expert in the interpretation of the accounting rules applying to public sector financial statements. As mentioned in her testimony, Ms Watson is the National public sector lead for KPMG's CFO advisory practice. She has more than 25 years' accounting and auditing experience, including a decade at the NSW Audit Office. In advisory roles, she has directly supported the NSW Parliamentary Budget Officer with his work on state budget and

forward estimates projections. She is a fellow of Chartered Accountants Australia & New Zealand, and has held other roles, including chair and vice-chair of the NSW State Council.

Contrary to what has been alleged in the inquiry, Ms Watson was engaged by Treasury separately and her contract commenced prior to Mr Lyon's engagement by Transport for NSW (TfNSW). The suggestion that Treasury had engaged Ms Watson after Mr Lyon was engaged by TfNSW for the purpose of contradicting Mr Lyon's work is simply not true.

As to Mr Lyon's statements regarding the accounting treatment of TAHE, Mr Lyon stated under oath that he was "not an accountant". When Treasury and other KPMG staff had reviewed Mr Lyon's work and identified significant errors in his work (as outlined in Treasury's email to Mr Lyon on 10 September 2020 and subsequent letter of 11 November 2020) - particularly as it related to matters requiring judgment or interpretation of accounting standards - Treasury requested that Mr Lyon correct those errors. This was entirely appropriate because Treasury was qualified to advise on those matters and, as the lead agency appointed by Cabinet on fiscal and financial matters for TAHE, it had a duty to ensure that Cabinet was properly advised and not misled. To let advice go to Cabinet that Treasury genuinely believed to be incorrect would be a fundamental breach of our duties.

However, as the records show, Mr Lyon refused to make such corrections despite repeated requests. As such, Treasury proceeded to provide separate fiscal advice to Cabinet. This was the only way that Treasury could fulfil its mandate and professional obligations, given Mr Lyon's recalcitrance.

Cabinet endorsed the recommendations on TAHE jointly proposed by TfNSW and Treasury, and supported Treasury's views on accounting, recognising Treasury's lead and expertise on fiscal and financial matters. Treasury will continue to provide its professional advice to government and is currently closely working with the Auditor General in explaining Treasury's view on the complex accounting matters that are related to TAHE.

Treasury would also like to address the PwC advice dated December 2019 that has been submitted to the PAC and referred to by Mr Lyon. The TAHE structure that PwC advised on was different to the TAHE structure that was ultimately set up. Accordingly, it is not appropriate to infer that the PwC advice supports Mr Lyon's view of the accounting treatment of TAHE.

Safety

Treasury acknowledges that a number of questions were raised by the PAC during the inquiry about safety of the rail network under TAHE.

On this issue, just as Treasury was the lead agency for addressing fiscal matters on the establishment of TAHE, TfNSW was the lead agency appointed by Cabinet for ensuring that TAHE met all relevant safety and operational requirements. Indeed, the joint Cabinet Submissions recommending and progressing the establishment of TAHE were endorsed by senior executives of both departments, both Secretaries and both Ministers, with Treasury affirming the fiscal advice and TfNSW affirming the safety and operational advice. Mr Lyon's own report refers to advice from TfNSW that TAHE could be established safely. TAHE has since agreed new safety governance arrangements between TfNSW, TAHE and rail operators, as reflected in the legal and commercial agreements applicable from 1 July 2021.

As to concerns expressed in the inquiry about safety over the medium to long term, TfNSW will continue to have oversight over safety. We reject Mr Lyon's simplistic binary assertion that what works for accounting rule purposes will not work for safety purposes. The objective of the government on TAHE was to achieve optimum operational, safety and fiscal outcomes. It is for

this reason that Cabinet asked TfNSW and Treasury to jointly work on TAHE. One of the important structural safeguards agreed between TfNSW and Treasury to be built into TAHE was to have the Secretary of TfNSW sit on the board of TAHE so that safety issues could be addressed. The safety and operational aspects of the NSW Government submission to this inquiry have been reviewed and confirmed by TfNSW as subject matter experts.

Contrary to Mr Lyon's assertions, Treasury has not lost sight of what matters with a public rail system. Rather, Treasury was determined that the objectives of optimum operations, safety and efficient use of taxpayer dollars be addressed concurrently in designing the right operating model for TAHE – a role that is entirely consistent with Treasury's function. In line with government policy, Treasury has sought to ensure that transport assets not only support good safe services but are also professionally managed and good value for tax payer money.

Allegations of inappropriate behaviour by Treasury staff

Under privilege, Mr Lyon made numerous unfounded claims and personal attacks on Treasury staff, in particular Treasury Secretary Michael Pratt AM, Deputy Secretary San Midha and Executive Director Cassandra Wilkinson.

Treasury categorically rejects these claims and personal attacks and considers it vital that we set the record straight. In particular, we wish to provide the PAC with the full and proper context to the matters referred to by Mr Lyon on 8 November 2021 and which were missing from the original extract of emails submitted by Mr Lyon on 8 November 2021 and uploaded to the PAC website titled "Extract 1 from documents provided by Mr Lyon – 8 November 2021 – REDACTED" (which we note has been subsequently taken down and replaced with another document titled "Extracts from documents produced by Mr Lyon_Reduced size", which contains the apology referred to below).

Wrongful characterisation of Secretary's email to KPMG senior partners on 19 November 2020 5:12pm

The true nature of this email from the Secretary can only be properly appreciated when the entire sequence of events that transpired prior to and after this email is considered:

- Before Mr Lyon's report was finalised, both Treasury and other KPMG staff had on many occasions communicated to and sent correspondence to Mr Lyon identifying numerous significant errors in his draft report (one example of which is Mr Midha's note to Mr Lyon of 10 September 2020). As noted earlier, Treasury had the lead role in ensuring that correct fiscal and financial advice was being provided to Cabinet and it was appropriate for Treasury to make such comments, as it has done many times before on other consultant's reports going to Cabinet. However, despite Treasury raising these concerns, these issues were not addressed prior to Mr Lyon finalising his report.
- As a result, on 11 November 2020, in relation to Mr Lyon's final report, Mr Midha wrote a letter to Mr Lyon setting out that:
 - Although advice to Cabinet on how TAHE meets the government's fiscal objectives is the responsibility of Treasury, Mr Lyon's report appears to have opined on fiscal matters
 - Mr Lyon had included a section referring to Treasury's fiscal model and Treasury did not agree with this being referred to by Mr Lyon in his report. Treasury did not agree with Mr Lyon's assumptions and conclusions regarding the fiscal, budget and commercial impacts of TAHE. Treasury said:

"While you are entitled to make your own assumptions and scenarios for your client, we disagree with your references to Treasury's model and request that you remove all references to relying on Treasury's advice"

- Treasury further noted that the report did not address accounting considerations and could not be taken as fiscal advice. Treasury said it would provide fiscal advice to Cabinet supported by Ms Watson and did not need separate unsolicited advice from Mr Lyon.
- Treasury then asked Mr Lyon to confirm that he would remove all references to Treasury's model from this report.
- By 19 November 2020, when Mr Lyon had still not responded to the 11 November 2020 letter, Mr Midha wrote a follow up email at 4:55pm to Mr Lyon, those senior KPMG partners who were involved with TAHE, and the Secretary, stating:

"Dear Brendan,

I refer to my email and letter dated 11th Nov:

I still await a reply to my letter and confirmation on corrections to your report or removing incorrect references to Treasury's Model"

- The Secretary followed up Mr Midha's email to the same recipients at 5:01pm, stating:

"Brendan,

This needs your urgent attention. You either correct the errors or remove all references to Treasury's model which is not for you to comment on. Please revert asap as this matter needs urgent resolution"

- My Lyon then wrote to the Secretary, copying in all the same KPMG partners, stating:

"Mike – I'm sick of being bullied by you.

Grow up or tell the truth. Up to you."

- The Secretary then replied to Mr Lyon and the same KPMG partners who were on the email, as follows:

"To the Senior Partners on this email, you obviously have a partner who refuses to take counsel and is out of control. As you are aware we engaged KPMG (Heather Watson) earlier this year to provide fiscal and accounting advice that is now concluded in support of the TAFE [sic] work. That work provides the basis for Treasury advice. I expect you to take action"

The context of this email and prior correspondence makes it noticeably clear that the "action" the Secretary referred to was the action that Mr Lyon refused to respond on – that is, to correct the errors or remove all references to Treasury's model as per Treasury's prior correspondence and which other KPMG staff had also identified.

- Mr Lyon then subsequently directly called Mr Pratt on his mobile phone and spoke at the Secretary at such a volume and aggression that the Secretary's executive assistant outside his office could hear the nature of the call. Given the aggressive manner of the call the Secretary promptly ended the call with Mr Lyon.

- Following this call, on 20 November 2020, Mr Lyon wrote to the Secretary stating:

"Mike,

I am writing to apologise for my email and phone conversation yesterday. The tone was not appropriate or professional ..."

- In response the Secretary accepted Mr Lyon's apology and wrote back to Mr Lyon:

"Thanks Brendan"

These two last emails were missing from the extract of the email exchange originally available on the inquiry's webpage on 8 November 2021, and neither they nor his subsequent phone call were referenced during Mr Lyon's evidence, despite casting a different light on the nature of the email exchange and the behaviour of Mr Lyon. A copy of those emails are attached in the Appendix to this letter.

The omission of these two last emails from the evidence and witness examination, and the subsequent unbalanced depiction of events, resulted in highly negative media coverage that has inflicted unnecessary and unwarranted personal and professional damage to Mr Pratt, Mr Midha and Ms Wilkinson.

It is also important to note that Mr Pratt had very limited contact with Mr Lyon throughout his engagement on TAHE. Other than the correspondence above, Mr Pratt had only directly emailed Mr Lyon once previously and had never met or spoken to him in person during the TAHE engagement until Mr Lyon first called Mr Pratt on 19 November.

The above demonstrates the Secretary had not behaved unprofessionally or bullied Mr Lyon. Indeed, it is Treasury's view that it was Mr Lyon who behaved unprofessionally, as evidenced by his apology email. In addition, the suggestion in the inquiry that it was inappropriate for the Treasury Secretary to directly contact the KPMG senior partners in his 19 November 2020 email does not consider the context that the Secretary was replying to the KPMG senior partners who were all recipients of the email that Mr Lyon himself had sent to the Secretary.

Finally, contrary to what has been alleged, at no time did the Secretary or any other Treasury official ask KPMG for Mr Lyon to be sacked or to prohibit Mr Lyon from doing any further work for the NSW Government.

We trust that this fuller explanation of the actual events of 19 and 20 November 2020, shines the proper light to what transpired.

Unfounded claims of unprofessional conduct by Mr Midha and Ms Wilkinson

Mr Midha and Ms Wilkinson were key members of the cross-government team responsible for reporting to Cabinet on TAHE. They are highly respected and highly regarded senior executives within Treasury and across the broader NSW Government. Under privilege, Mr Lyon has accused Mr Midha and Ms Wilkinson of behaving in an unprofessional manner and has alleged that they had also subsequently apologised to him for their behaviour.

Treasury categorically rejects these allegations. Both Mr Midha and Ms Wilkinson have also confirmed that they have not behaved in the manner alleged and have never apologised to Mr Lyon.

Treasury staff principally engaged with Mr Lyon in formal meetings and in writing. In those meetings and in correspondence Treasury staff have always behaved professionally, and at times firmly, in putting their positions forward consistent with Treasury's duty to ensure that Cabinet gets the best advice. Treasury does not consider respectfully but firmly disagreeing or requesting corrections to be made unprofessional behaviour or bullying. The wording and language used by Treasury staff in their correspondence to Mr Lyon, which are on the inquiry website, confirms the professionalism and respect Treasury's staff gave to Mr Lyon in their interactions.

Treasury staff have always acted appropriately in regard to this matter.

We note that the Premier announced in Parliament on 9 November 2021, that he had directed the Department of Premier and Cabinet to contact Mr Lyon to invite him to formally lodge a complaint following the allegations he had made under parliamentary privilege.

To date, we understand Mr Lyon has not made such a complaint.

Other Statements by Mr Lyon

Finally, Treasury would like to address other key statements made by Mr Lyon under privilege or were contained in his submissions to the PAC that Treasury considers warrants a response:

- On the Secretary's professional qualifications, Mr Lyon stated publicly in his testimony:

"Mr Pratt might come from a mid-level role in one of the big banks or like that ... not an economist or a finance guy either ... reflects lack of rigour in Treasury."

Before Mr Pratt joined Treasury, he had an extensive and distinguished career in financial services including as CEO of a number of International and Australian Banks as well as being former President of the Australian Institute of Banking & Finance and Joint President of FINSIA. Mr Pratt was also honoured as a Member of the Order of Australia (AM) for significant service to the finance and banking industry.

- On James Hunter, Mr Lyon stated:

"Mr James Hunter said he regularly goes around to Mr Pratt's House"

Treasury cannot comment on what Mr Hunter allegedly said to Mr Lyon, but the Secretary can confirm that the statement is completely incorrect.

- On KPMG, Mr Lyon stated:

"Mr Pratt had control over KPMG ... current CEO worked for Mr Pratt"

To suggest that Mr Pratt has control over a global consulting firm such as KPMG is entirely incorrect, as is the statement that the current CEO of KPMG has ever worked for Mr Pratt.

Concluding Statements

Treasury is incredibly proud of the work that it does for the NSW Government and the people of NSW. TAHE is one of the more complex and important projects that NSW Treasury has worked on and has required diligent, demanding work by professional staff at Treasury over many years. Treasury has always acted professionally and respectfully, and in accordance with its mandate to provide the best fiscal and financial advice to Cabinet in support of establishing a safe, well-

managed transport infrastructure that efficiently uses taxpayer money. It is disappointing that personal attacks and unfounded allegations against Treasury and its staff have shifted the focus away from what TAHE is seeking to achieve, but we are grateful that the PAC has given Treasury the opportunity to properly respond and properly explain the work that Treasury has done.

Treasury would be pleased to assist should the PAC require further information or clarification.

Yours sincerely

Michael Pratt AM
Secretary

San Midha
Deputy Secretary

Cassandra Wilkinson
Executive Director –
Transport, Regions,
Infrastructure and Planning

30 November 2021

Appendix

From: Michael Pratt on behalf of Michael Pratt
Sent on: Friday, November 20, 2020 4:49:43 AM
To: Lyon, Brendan ; San Midha ; Linke,
 David ; Heathcote, David ; Low, Paul
 James Hunter (Contact)
CC: San Midha
Subject: RE: UPDATED FINAL KPMG TAHE REPORT (NSW CABINET IN CONFIDENCE)

Thanks Brendan

Michael Pratt AM
 Secretary

52 Martin Place, Sydney (enter via 127 Phillip Street)
 GPO Box 5469, Sydney, NSW 2001

From: Lyon, Brendan
Sent: Friday, 20 November 2020 3:08 PM
To: Michael Pratt ; Heathcote, David ; San Midha ; Low, Paul ; Linke, David ; James Hunter (Contact)
Cc: San Midha
Subject: RE: UPDATED FINAL KPMG TAHE REPORT (NSW CABINET IN CONFIDENCE)
Importance: High

Mike,

I am writing to apologise for my email and phone conversation yesterday. The tone was not appropriate or professional.

TAHE has been a very complex and trying engagement, for all concerned.

Looking ahead, I have decided it would be better for any correspondence on the TAHE engagement be addressed via my second Partner, Paul Low, to put in some appropriate space.

Sincerely,

Brendan