Submission No 6

INQUIRY INTO MINISTERIAL PROPRIETY IN NEW SOUTH WALES

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Submission to Legislative Council Select Committee Inquiry into Ministerial Propriety in NSW

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LEGISLATIVE COUNCIL SELECT COMMITTEE INQUIRY INTO
MINISTERIAL PROPRIETY IN NSW

1. INTRODUCTION

Centennial Consultancy welcomes the opportunity provided by the Committee to make a submission on ministerial propriety in NSW. The submission focuses on the following Terms of Reference:

(a) Ministerial responsibility to Parliament, including the doctrine of individual ministerial responsibility

(b) Measures to reduce potential conflicts of interest between a minister's public duties, private interests and membership of a political party, particularly in relation to financial and commercial activities

(c) The operation and enforcement of the *Lobbying of Government Officials Act 2011*, and any associated codes of conduct, registers or administrative arrangements.

2. MINISTERIAL RESPONSIBILITY TO PARLIAMENT, INCLUDING THE DOCTRINE OF INDIVIDUAL MINISTERIAL RESPONSIBILITY

According to the Code of Conduct for Ministers:

> It is essential for the maintenance of public confidence in the integrity of the Executive Government of the State that Ministers of the Crown exhibit, and be seen to exhibit, the highest standards of probity in the exercise of their offices, and that they pursue, and be seen to pursue, the best interests of the people of New South Wales to the exclusion of any other interest.

Regrettably, this has not always been the case. It is of great concern that some major proposals affecting the people of this State have been allowed to proceed without appropriate Parliamentary or public scrutiny. Failure to expose such major proposals to Parliamentary scrutiny has meant that the public interest has not been at the forefront and has not been served.

2.1 Examples of failures of ministerial responsibility to Parliament

The Packer casino/hotel

The latest example of a significant matter that has not been presented to Parliament and in which the public interest does not appear to be at the forefront is the Packer casino/hotel proposal for Barangaroo. Apart from the financial considerations, there are the societal impacts. Leaving debates about gambling aside, and though the architects have done their best to hide this fact from the images provided, it is obvious that the proposed building will dwarf the Harbour Bridge and the Opera House. This in itself will change the character of the harbour as perceived by our community and the rest of the world from one dominated by the famous Opera house to one dominated by a casino. As an American journalist and author recently said:

> Australia is a fine country, and the world knows it. But modest Australia probably needs to remind itself of what it is. The Statue of Liberty watches over the harbour of my home city, and 4 million people from all over the world visit Lady Liberty every year because it means something. The Opera House was a great first step for a strong, young nation; I am hopeful Australia will think twice about making the second step a casino (*Crikey*, 19 July 2013).

The Danish urban designer, Professor Jan Gehl, who was commissioned by the government in 2010 to ensure Barangaroo's public areas were 'people friendly' resigned on 18 September 2013 reportedly because he was increasingly worried that economic pressures have created a strong urge to build as much as possible at the expense of people-friendly areas. He added that the Packer hotel-casino is contrary to what was needed (*The Sydney Morning Herald*, 5-6 October 2013, p. 1).

The part privatisation of the NSW electricity industry

The privatisation of part of the NSW electricity industry in the dying days of the previous NSW Government is another example. The transactions were as follows:

- the retailing arms of Country Energy and Integral Energy, along with the Generation Trading Agreement (Gentrader Agreement) for Eraring power station, were sold to Origin Energy for an aggregate value of $3,250 million;
- the retailing arm of EnergyAustralia, the Gentrader Agreement for Delta Electricity's Mt Piper and Wallerawang power stations, and development sites at Mt Piper and Marulan were sold to TRUenergy for an aggregate value of $2,035 million (*2011-12 NSW Budget Paper No. 2*, p. 8-9).

In a second round, no bids were received for Macquarie Generation's power stations and Delta Electricity's coastal power stations and these assets

remain in Government hands, along with four power station development sites.

In February 2011 the Bamarang power station development site was sold to Infratil for $9 million (*ibid.*).

To interested observers of government finances, it was noteworthy that the information available about the financial performance of state-owned electricity assets before their sale was comprehensively deficient. Our analysis of the profitability of six state-owned generators and distributors revealed that they were producing an average rate of return to the State as owner of 25.2% - a return that would be the envy of private sector investors. But financial information of this kind was never presented to Parliament. Rather, members were provided with scary stories about the investment required to 'keep the lights on'.

Moreover, published financial statements failed to reveal separately the financial contributions of the 'poles and wires' segments that were to be retained when some undertakings were slated for sale. (In the private sector, listed public companies and other reporting entities are required to disclose information about the contribution of business segments.)

The rushing of these transactions by then treasurer Eric Roozendaal without proper Parliamentary and public scrutiny led to significant losses to the State. Any positive impacts from these transactions, for example, debt reduction, were offset by negative impacts on the budget position across the forward estimates including:

- foregone ongoing dividend and income tax equivalent revenues from retail and the transacted generators;
- foregone ongoing Government guarantee fees from the transacted generators;
- lower dividend and income tax equivalent payments from the State-owned network businesses, as a result of the residual (stranded) and other unrecoverable costs associated with transferring customers to the new retailers;
- potential damages (Availability Liquidated Damages) that the generator businesses may incur if the availability targets in the Gentrader Agreements are not met (*ibid.*).

According to the Budget Papers, these factors together with developments subsequent to the completion of the transactions mean that the impact on the State's budget and fiscal position is expected to be negative. The table below shows that, rather than a financial gain from the sale of such significant assets, the expected impact of the transactions on the Budget result over the period from 2010-11 to 2014-15 will be a ***loss*** of $347 million (*ibid*., p. 10).

Budget Result Impact of Electricity Transactions

Budget Result Impact	2010-11	2011-12	2012-13	2013-14	2014-15	Total 2010-11 to 2014-15
	$m	$m	$m	$m	$m	$m
Reduction in Interest Expense @ 6%	75	233	244	259	273	**1,084**
Loss of Financial Distributions and Government Guarantee Fees	(51)	(317)	(252)	(106)	(106)	**(832)**
Availability Liquidated Damages, Separation Costs and Other Costs	(61)	(4)	(174)	(138)	(224)	**(600)**
Budget Impact	**(37)**	**(88)**	**(181)**	**15**	**(57)**	**(347)**

Source: Table 8.3, *2011-12 Budget Paper No. 2*, p. 8.10

At the same time, the loss of a stable source of revenues from these government businesses has left the State more reliant on relatively volatile revenues from property taxes.

Moreover, the claimed benefits of privatisation – lower prices for consumers – have failed to materialise. (This was entirely predictable.)

Sale of the State Bank

One of the worst examples of inadequate ministerial responsibility to Parliament is the sale of the State Bank by the previous Coalition Government.

In 1995 the State Bank of NSW was sold by the Fahey Government for a headline price of $576 million to Colonial Mutual, after the major trading banks were excluded from bidding, supposedly to promote increased competition in the banking sector. One of the conditions of the sale was that the NSW Government would assume most of the risks of bad debts on a $13 billion loan book. After the first $60 million in bad debts, prospective purchasers were to be reimbursed for 90% of any further losses.

The $576 million headline price paid by Colonial Mutual was quickly eroded by indemnity payouts. Details were recorded for a period in NSW Budget Paper No. 2. Subsequently information about payouts were recorded (without explanation as line items) in the annual accounts of the 'Crown Entity'.

The outcome was a financial disaster for the State of NSW.

The bottom line is that net sale proceeds ended up being as little as $80 - $100 million. That was less than one year’s profits - in its first year of private ownership, the bank reported a pre-tax profit of $146.9 million.

Before Colonial merged with the Commonwealth Bank in 2000, an Independent Expert's Report included a valuation of Colonial's banking business – which, (apart from very minor investments in Tasmania and Fiji), was for all intents and purposes the old State Bank of NSW. The valuation, only four years after the State Government's sale of the bank for what may be as little as $80 million, was in the range **$2.5 billion - $2.75 billion.**

In other words, the **State of NSW lost more than $2.5 billion** from the premature sale of SBNSW – it was sold at the wrong time, for the wrong reasons (to get rid of it before the story of bad debts and maladministration came to light) and on the wrong terms.

The major mistake was to evaluate the 'sell' or 'retain' options using a discount rate based on market-determined estimates of the private sector cost of capital. Arguably, NSW Treasury's continued advocacy of use of that methodology has led to similar losses – notably, in the form of a loss of profits from tollways such as the M2, that were established as PPPs.

Some details before the SBNSW sale were only brought to Parliament after the Independents demanded a review of the sale by the then Auditor General. However, because of time and resource constraints, he was forced to contract out the work. The resulting report presented to Parliament gave the green light for the sale and Parliamentarians gave their approval on that basis. However, the report that the MPs saw omitted the most crucial information which was claimed by a consultant to be 'commercial-in-confidence'.

It was only when that Auditor General was about to retire that he published this information which was previously withheld from Parliament. This revealed that the consultant's assessment of the sale presented to Parliamentarians arrived at a 'retention value' of only $100 million for the SBNSW. It needs to be understood that 'retention value' is calculated by calculating the present value of projected cash flows – and by adopting an interest rate to use in the discounting calculation. The higher the discount rate, the lower the present value. The discount rate selected by the consultant was the extraordinarily high figure of 18.9%.

The result of the sale proceeding, in the absence of full disclosure of information to Parliament (and consequential public scrutiny), was a loss to the State of more than $2.5 billion.

2.2 Recommendations on measures to protect the public interest

A notable deficiency of the ministerial Code of Conduct concerns the failure of the Code to present guidelines for the presentation of financial information sufficient to enable members of Parliament to make informed decisions.

It is noted that the submission from the Department of Premier and Cabinet avoids the question of whether a Minister should be individually responsible for some particular act, omission or outcome – claiming that this is 'primarily a

political matter on which it would be inappropriate for a public servant to express an opinion'. Centennial Consultancy does not labour under such an inhibition.

It is contended that the conduct of some Ministers in omitting to present relevant information to Parliament – and rather to behave 'politically' by unashamedly presenting purely advocacy material in support of major transactions – has in recent decades been at a cost to taxpayers of billions of dollars.

In order to protect the public interest, Ministers should be required to ensure that Parliament is provided with relevant information about major transactions – particularly those involving the proposed sale of public assets or businesses, or proposed private sector utilisation of public property. 'Major transactions' would need to be defined (e.g. all projects/proposals in excess of say $500 million). This information should be presented to Parliament and be available for public scrutiny before a government can execute contracts.

In the private sector, ASX listing rules prescribe that certain proposals to sell the 'major undertaking' of an entity be put before shareholders for their consideration. The common law has long provided that directors have a duty to give full and proper disclosure; hence notices of meetings of shareholders about the sale of major undertakings must disclose all information needed to enable them to assess whether they should vote ***for or against*** such a resolution.[1]

It seems anomalous that disclosure requirements intended to impose some discipline on dealings with private capital are far stronger than those adopted by governments in dealings with assets acquired with public funds.

It may be contended that, rather than make Ministers take some responsibility for the full and fair presentation of financial information about privatisations, PPPs or Bangaroo-style deals, that this should be the province of the Auditor General, an officer of Parliament. In other words, it may be argued that the role of the Auditor General includes taking steps to ensure that Parliament is appropriately informed about financial matters. Arguably this is outside the terms of reference of this inquiry, but it might be noted that the Auditor General was missing in action when the Legislative Council was about to debate the Labor Government's electricity privatisation proposals. On the very morning of that vote the Auditor General asserted on ABC radio 702 that he was not prepared to examine the merits of the proposals, and would only comment on the 'process'.

[1] See *Bulfin v Bebarfald's Ltd* (1938) 38 SR (NSW) 423, *Fraser v NRMA Holdings Limited* (1995) 127 ALR 543 and *ENT Pty Ltd v Sunraysia Television Ltd* (2007) 61 ACSR 626.

3. MEASURES TO REDUCE POTENTIAL CONFLICTS OF INTEREST BETWEEN A MINISTER'S PUBLIC DUTIES, PRIVATE INTERESTS AND MEMBERSHIP OF A POLITICAL PARTY, PARTICULARLY IN RELATION TO FINANCIAL AND COMMERCIAL ACTIVITIES

3.1 Failures of ministerial behaviour

Much has been said and written about the potential conflicts of interests for Ministers arising between their public duties, private interests and membership of a political party.

It is hoped that lessons have been learnt from the events which have been the subject of recent ICAC inquiries in relation to several Ministers in the NSW Labor Government.

A few more lessons are likely in the upcoming ICAC hearings into Australian Water Holdings, reportedly involving former Labor Ministers Michael Costa, Joe Tripodi, Tony Kelly and Eddie Obeid, and current Liberal Senator Arthur Sinodinos.

Just as important as potential conflicts arising ***during*** a Ministers' time in office are those conflicts of interest which may arise when Ministers ***prepare to leave office,*** and ***after they leave office*** i.e. offers of post-separation employment, and efforts to establish a consultancy business to provide services to third parties.

In these circumstances, the Ministerial Code of Conduct cautions Ministers to avoid a perception that:

- the conduct of the Minister or former Minister while in office is or was influenced by the prospect of the employment or engagement or by the Minister or former Minister's intention to provide services to third parties; or
- the Minister or former Minister might make improper use of confidential information to which he or she has or had access while in office.

The Code also requires Ministers to obtain advice from the Parliamentary Ethics Adviser before accepting any post-separation employment or engagement or providing services to third parties which relates or relate to their portfolio responsibilities (including portfolio responsibilities held during the previous two years of ministerial office).

However, it is less than satisfactory that this requirement applies only for the period of 18 months following the date on which Ministers ceasing to hold that office.

It is similarly unsatisfactory that the *Lobbying of Government Officials Act 2011* which imposes additional restrictions on a former Minister's capacity to engage in lobbying activities applies only in the first 18 months after leaving

office that concern his or her former portfolio responsibilities that were in place in the 18 months prior to leaving office.

These requirements are flawed in a number of respects including the restrictions relating only to former portfolio matters and the period during which they apply.

3.2 Recommendations

Accordingly, it is recommended that the restrictions apply:

- to former Ministers not only in relation to their former portfolio responsibilities ***but also to any other portfolios***. This would avoid the operation of the old boys/girls network whereby ministerial colleagues give preferential treatment to their former colleagues post-separation; and

- for at least the previous five years that he or she held any ministerial office and five years post-separation from ministerial office.

4. THE OPERATION AND ENFORCEMENT OF THE *LOBBYING OF GOVERNMENT OFFICIALS ACT 2011*, AND ANY ASSOCIATED CODES OF CONDUCT, REGISTERS OR ADMINISTRATIVE ARRANGEMENTS

There are a number of flaws in the NSW lobbying legislation and they are dealt with in turn.

4.1 Definition of 'lobbyist' – exemption of associations

The first flaw relates to the exclusion of associations from the definition of 'lobbyist'. According to the NSW Government Lobbyist Code of Conduct:

> "Lobbyist" means a person, body corporate, unincorporated association, partnership or firm whose business includes being contracted or engaged to represent the interests of a third party to a Government Representative.

It goes on to say that:

> "Lobbyist" does not include:
>
> (a) an association or organisation constituted to represent the interests of its members.

This exemption has meant that organisations which undertake extensive lobbying with the aim of influencing government policies have not been required to register as lobbyists.

It is absurd that this exemption has allowed organisations such as the Australian Hotels Association (NSW Branch) and Clubs NSW to escape this requirement. Both are widely recognised as devoting much of their efforts and resources to lobbying activities. Indeed, a former chairman of the AHA (NSW) unashamedly remarked, 'democracy does not come cheap'.

The impacts of their lobbying have been documented elsewhere. One example presented here for illustrative purposes is the impact on the State Budget of lobbying by Clubs NSW[2] which openly states on its internet site that its staff (of which there are 45) 'actively lobby across a wide range of related issues for more than 1200 member clubs'.

Clubs have traditionally paid a concessional rate of State gaming machine duty which by the time of the end of the Carr Labor Government was costing the State Budget some $500 million per year. Before leaving office Premier Bob Carr and Treasurer Michael Egan announced an increase in the club duty

[2] For more details refer to Betty Con Walker, *Casino Clubs NSW – Profits, tax, sport and politics*, Sydney University Press, 2009.

rates to be introduced over a period of seven years. This would increase Budget revenues but still leave clubs with lower tax rates than those paid by hotels - their main competitor. The reaction by the club industry to the proposed increase was fierce. There were public protests in the city and outside MP's offices, advertising campaigns, personalised attacks on individual MPs and on the Treasurer – to name just a few. However, by the time Premier Carr and Treasurer Egan left office, they believed that they had won the fight and the annual increases were proceeding.

Nevertheless, after Premier Carr announced his retirement from State politics, one of the candidates for his replacement, Morris Iemma, in order to get the necessary numbers for the premiership, had apparently made commitments to several MPs that he would end the remaining scheduled increases in club gaming duty. To the detriment of the Budget bottom line, Premier Iemma kept his promise so by the time of the last election, the cost to the Budget of the club concessional tax rates had increased to $654 million per year.

However, things were to get worse under the current Coalition Government which in Opposition signed a Memorandum of Understanding with Clubs NSW to, amongst other things, reduce the tax rates of clubs.[3] The O'Farrell Government has kept its promise to reduce rates. The cost to the Budget of concessional club tax rates was shown in the latest Budget Papers as $739 million in 2011-12 increasing to $777 million by 2012-13 and $805 million by 2013-14 (*2013-14 Budget Paper No. 2*, p. 6-25).

4.2 Definition of 'lobbyist' – exemption of certain technical or professional occupations

Another exclusion from the definition of 'lobbyist' which creates problems and which has already been the subject of comment involves technical or professional occupations as follows:

> (c) an entity or person whose business is a recognised technical or professional occupation which, as part of the services provided to third parties in the course of that occupation, represents the views of the third party who has engaged it to provide their technical or professional services.

This exclusion has the obvious flaw that a person who happens to have technical or professional qualifications and who is employed to lobby the Government on a particular policy escapes a listing on the Lobbyist Register and avoids the various requirements of its ethical code – requirements apparently intended to promote greater transparency of government decision-making.

[3] It should be noted that the club gaming tax rates included in the Memorandum of Understanding are exaggerated since they are inclusive of the GST.

Moreover, this particular exemption is applied inconsistently. Partners and staff of accounting and legal firms do not need to register – even though they may represent major commercial interests seeking to do business with government.

On the other hand, other professionals (for example, self employed economists whose work may be predominately focused on analysis of government policies and making representations to politicians and government officials with regard to the public interest) have been advised by the Department of Premier and Cabinet that they should register.

4.3 Definition of 'lobbyist' – does not capture in-house government relations advisers

In addition to the exemption of certain technical or professional occupations, the Register does not capture those in-house government relations advisers who are employed by large corporations largely to lobby governments on specific policy issues. It has become evident that corporations are increasingly adopting the practice of employing political party aligned individuals in those positions.

4.4 Monitoring compliance and imposing sanctions

A Code of Conduct is only as good as its application and enforcement. It is therefore disappointing that the Director General of the Department of Premier and Cabinet, Chris Eccles, failed to take action against a lobbyist, Joe Tannous, who the Director General found to have breached the Lobbyist Code of Conduct.

Mr Tanous had boasted on his LinkedIn profile that his position on the Liberal state executive could ***'attain the desired results'***. This was in clear contravention of the Lobbyist Code of Conduct which states in part:

> (c) Lobbyists shall not make misleading, exaggerated or extravagant claims about, or otherwise misrepresent, the nature or extent of their access to institutions of government or to political parties or to persons in those institutions;
> (d) Lobbyists shall keep strictly separate from their duties and activities as Lobbyists any personal activity or involvement on behalf of a political party;

Given that the Code was adopted in light of concerns that lobbyists may have excessive influence and privileged access to politicians and government officials, it is hard to think of a more blatant breach of the Code.

And yet, surprisingly, Mr Eccles decided not to take any action against Mr Tannous or his company, First State Advisors & Consultants Pty Ltd. While apparently not finding any evidence that Mr Tanous had not kept his lobbying and party activities separate, he found that the LinkedIn statement breached the section of the Code forbidding lobbyists from making 'misleading' claims.

It is not clear what evidence Mr Eccles relied upon to reach this particular conclusion. It is not clear whether it was based on any empirical evidence concerning Mr Tanous' lobbying activities and potential outcomes. (It is noted that Mr Tanous has provided details of the contacts made with NSW politicians, ministerial staff or government officials. Did the Director General find that First State's lobbying on these occasions had been singularly unsuccessful? How else could the statements made by First State be regarded as 'misleading'?)

Even so, Director General Eccles apparently did not consider that the breach was sufficiently severe as to de-register some or all of First State's representatives.

The Committee may wish to invite Mr Eccles to identify exactly what conduct he would consider sufficiently egregious to warrant the imposition of the sanction of de-registration? And what other sanctions he might consider appropriate in certain circumstances?

Perhaps the Government believes that its decision to amend the Code so as to require that a registered lobbyist:

> … does not occupy or act in an office or position concerned with the management of a registered political party

sufficiently addresses such a blatant abuse of the Code.

However, this will hardly satisfy concerns about the influence of party activists in seeking favoured treatment for their clients. Party activists would be known to a government of the same party whether they are party office holders or not. Simply resigning from party executive positions would not extinguish their connections from members of the government of the day.

4.5 Administrative requirements

The requirement for registered lobbyists to provide three returns a year imposes unnecessary and burdensome requirements – not only on those who are obliged to furnish returns so frequently, but also on taxpayers, as presumably public servants devote time to sending out notices, following-up with reminders, filing responses and compiling reports on response rates, together with advice about de-registration if appropriate.

The Committee might consider whether requirements for such frequent reporting 'adds value' and are cost-effective.

4.6 Recommendations

It is recommended that:

- the exemption of industry associations (such as the Australian Hotels Association and Clubs NSW) be removed;

- the exemption regarding technical and professional occupations be removed;

- in-house government relations advisers be included on the Register;

- requirements for reporting three times a year be withdrawn and replaced with a system of:

    - annual reporting, in conjunction with

    - requirements for ‘continuous disclosure’ (say, within 14 days) whenever there are any changes in the personnel or other matters related to registered lobbyists.