

REPORT ON PROCEEDINGS BEFORE

PUBLIC ACCOUNTABILITY COMMITTEE

TRANSPORT ASSET HOLDING ENTITY

CORRECTED

At Macquarie Room, Parliament House, Sydney on Monday, 8 November 2021

The Committee met at 10:00 am

PRESENT

Mr David Shoebridge (Chair)

Ms Abigail Boyd
The Hon. Scott Farlow
The Hon. John Graham
The Hon. Trevor Khan
The Hon. Daniel Mookhey
The Hon. Peter Poulos

* Please note:

[inaudible] is used when audio words cannot be deciphered.

[audio malfunction] is used when words are lost due to a technical malfunction.

[disorder] is used when members or witnesses speak over one another.

The CHAIR: Welcome to the second hearing of the Public Accountability Committee's inquiry into the Transport Asset Holding Entity, otherwise known as TAHE. Before I commence I would like to acknowledge the Gadigal people, who are the traditional owners of the land upon which the Parliament stands, and pay our collective respects to Elders past, present and emerging. Today we will be hearing from Mr Brendan Lyon, former KPMG partner, as well as representatives of the TAHE board. We will be looking closely into the circumstances in which TAHE was established—a very substantial venture and an organisation which holds some \$40 billion of public transport assets in New South Wales. I thank everyone for making the time to give evidence to this important inquiry and to explore the financial and ethical implications of the establishment of TAHE.

Before we commence I will make some brief comments about the procedures for today's hearing. Today's hearing is being broadcast live by the Parliament's website and a transcript of today's hearing will be available as soon as possible and placed on the Committee's website. In accordance with broadcasting guidelines I remind media representatives to take responsibility for what they publish about the Committee's proceedings. While parliamentary privilege applies to evidence given in the inquiry it does not apply to what witnesses say outside. Committee hearings are also not intended to provide a forum for people to make adverse reflection upon others and we request people, if possible, to stick to the issues rather than issues of personality.

All witnesses have a right to procedural fairness according to the procedural fairness resolution adopted by the House in 2018. If witnesses are unable to answer a question today and request more time to respond, they make take a question on notice and provide an answer within 21 days. If witnesses wish to hand up documents they should do so through the Committee staff. Mr Lyon, I note that you have produced a number of documents to the Committee under summons at the commencement of today's hearing. With reference to the audibility of today's hearing, I remind Committee members and witnesses to speak into the microphone. We have Ms Abigail Boyd attending remotely by Webex and, again, Ms Boyd, I note it is best to unmute your microphone at the commencement of a contribution and put it on mute at the end of the contribution. I ask everybody to put their mobile phones on silent for the duration of the hearing. Mr Lyon, I remind you that you are on your former affirmation that you made in the earlier in-camera session today.

BRENDAN CURTIS LYON, Principal, Project Partners, on former affirmation

The CHAIR: Before we commence, I acknowledge, Mr Lyon, that you have raised concerns in relation to confidentiality agreements with your former employer, KPMG Australia, and you should be aware that your evidence today is protected by parliamentary privilege and may not be used against you in any court proceedings. I also remind you that you are appearing under summons today and the effect of section 11 of the Parliamentary Evidence Act in providing answers to questions asked by the Committee. With that, Mr Lyon, you now have an opportunity to make a brief opening statement and I invite you to do so.

Mr LYON: Thank you. Chairman and members, my name is Brendan Lyon and I appear today, as you know, under subpoena to provide evidence regarding my work on TAHE, which concluded in December last year. While I appear under subpoena, I did not seek to avoid the Committee because of any concern or worry I have about the transparency of my work on TAHE or the validity or the ethics of my team across the engagement. Rather, I could not accept your invitations to appear out of respect, as you mentioned, for the legal constraints created within my partnership agreement with KPMG, out of respect for my client Transport for NSW, and due to specific non-disclosure terms that KPMG had me sign in return for beneficial terms of departure.

For the record, it is important that I note that the papers that I have provided were retained for a lawful reason and that they have been in the possession of my lawyers until recently when I received the subpoena. I was engaged by Transport for NSW to lead the development of an operating model for the planned Transport Asset Holding Entity that was capable of passing safety review, and to develop a sophisticated financial model to show TAHE's performance and its impacts on the budget. Both of my reports were provided as final reports of KPMG and were attached to the relevant Cabinet submissions. I reported to Fiona Trussell, the then deputy secretary of Transport for NSW. On a day-to-day basis my team and I worked with Peter Perdikos and several other Transport for NSW officials.

The risks and impacts of TAHE meant that the then secretary, Rodd Staples, was also heavily involved in my engagement. Again, for the record, I want to thank Rodd, Fiona and Peter, who are exceptional public servants and highly committed to ethics, safety and integrity in their work. And through them I thank the dozens of outstanding transport officials who contributed to the complex work that we undertook. The significance of TAHE to transport safety and the State budget also meant I saw Andrew Constance relatively frequently—and, again, I thank him for his decency and regard for me. I also reported to a joint committee of officials, chaired by the Treasury secretary, Mike Pratt, and, on his behalf, often by San Midha and Cassandra Wilkinson, who are Treasury officials.

My first report in June advised Cabinet of problems with Treasury's modelling of TAHE's costs and benefits and a range of safety risks. This allowed Transport for NSW to insist that the June Cabinet submission be changed to allow TAHE only to be "stood up", not to operate, but instead saw Cabinet require my team to develop two items to return to Cabinet later in the year, being a detailed operating model capable of passing independent safety review, and a robust financial model. This second detailed phase of work confirmed that Treasury's numbers used for the budget are wrong, and had essentially made up the benefits used in the June Cabinet submission—seeing, in round numbers, the budget some \$10 billion or more worse off than Treasury has claimed.

The Treasury secretary, Mike Pratt; deputy secretary, San Midha; and executive director Cassandra Wilkinson were understandably very unhappy with my work. This was expressed through very unprofessional, ongoing personal attacks on me and my team and repeated complaints to senior partners at KPMG. I finalised my report despite the pressure to change or remove the results. And when this saw continuing pressure from Mike Pratt, and when I asked him directly to stop bullying me—and you will see the email in my papers—he called for me to be sacked, and also asked that KPMG prohibit me from doing any further work for the New South Wales Government, to which I was advised the firm's CEO, Andrew Yates, agreed.

Because of Mike Pratt, San Midha and Cassandra Wilkinson's influence over KPMG's most senior partners, my papers also show the flurry of vexatious internal disciplinary processes that were launched into me some months after my work concluded. It was made untenable for me to stay, with the repeated attempts to discredit me personally and to discredit me professionally because I had exposed the failures of those senior Treasury personnel. I left KPMG with my team and most of my clients after I involved Rebekah Giles to negotiate my exit and terminate the vicious internal processes that are in the papers.

I have now established with my team a new financial and economic advisory firm called Project Partners. We have strong ethics and strong morals because we never want to be in the position again of having to choose between our jobs and our morals. Finally, I place on the record my deep thanks to my team on TAHE and particularly to David Russell and Jessie Hui, who have joined me in forming Project Partners; Nick Hudson, who

is now the senior adviser to Paul Fletcher, the Federal infrastructure Minister; and Gavin Harris, who remains at KPMG. These professionals and others were exposed to very poor behaviours and reprisals and they were tested and they stood firm. I thank the Committee for your forbearance with my opening statement and I look forward to your questions.

The CHAIR: Mr Lyon, thank you for that, and again, thank you for attending today. I think we will have a significant number of questions and, if possible, if you could assist by referencing the documents; I know that they have some sequential numbering which will assist. I might just ask the first question. I note there is a document numbered 266. This is an email from Mr Pratt, Treasury secretary, of 19 November 2020, and it commences, "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 earlier this year to provide fiscal and accounting advice that has now concluded in support of the TAHE work. That work provides the basis for Treasury advice. I expect you to take action. Mike." What did you think when you saw that email?

Mr LYON: Mr Pratt was asking for me to be sacked. He was asking for the senior partners in the firm—and you will see through correspondence preceding that all sorts of improper attempts by a partner named James Hunter, Heather Watson, also a partner at KPMG, to influence the work, to change the work, to have it removed. It was very clear to me in that phone call that Mr Pratt was asking for me to be terminated as a partner and was asking for reprisals because of the finalisation of my report.

The Hon. TREVOR KHAN: Can I just ask a question in regard to that? This is not to doubt your evidence but is there anywhere in the correspondence that you have provided under summons explicit wording by Mr Pratt that he sought the termination of your employment?

Mr LYON: There was certainly a statement made to me by David Heathcote, the head of the DTL division, in December that Mr Yates had agreed to a request by Mr Pratt that I be prohibited from doing further work, which certainly suggested to me that I should withdraw my email requesting that Mr Pratt stop bullying me improperly to change the results of a finalised report. That was why I sent that email; there are some contemporaneous notes of the phone call I made to Mr Pratt when I received it. But it was very clear because I had been facing ongoing reprisals for a significant period of time; there are documents throughout that reference, again, James Hunter and Heather Watson following the instructions of Mr Pratt in regard to all sorts of changes that were required to my work.

The Hon. DANIEL MOOKHEY: Can I just ask, the DTL, what does that acronym—

Mr LYON: Sorry. There are lots of acronyms involved in this. DTL is a division of KPMG; the divisional partners run those. David Heathcote and, prior to that, David Linke were the heads of my division.

The Hon. DANIEL MOOKHEY: But what is DTL?

Mr LYON: Deals, Tax and Legal, I think.

The Hon. TREVOR KHAN: Can I just ask a question with regard to Mr Lyons?

The CHAIR: Yes.

The Hon. TREVOR KHAN: Are you able on notice to identify those emails, documents, correspondence that you say supports—and, again, I am not trying to sound in any way derogatory—what you say with regard to the pressure that was being applied?

Mr LYON: Certainly.

The Hon. DANIEL MOOKHEY: Can I just follow up some questions on that?

The CHAIR: Yes, I just have one more question and then I will hand to you. That email that I read to you from the beginning, there were two emails that precede it. One is where you say to Mr Pratt, "Mike, I'm sick of being bullied by you"—

The Hon. TREVOR KHAN: Can you refer to it by number?

The CHAIR: It is 265. "Mike, I'm sick of being bullied by you. Grow up or tell the truth, it is up to you."

Mr LYON: It was supposed to be "and tell the truth", not "or".

The CHAIR: And that was in response to an email from Mr Pratt of 19 November at about 5.00 p.m. where he said, "Brendan, this needs your urgent attention. You either correct the errors or remove all references to Treasury model, which is not for you to comment upon. Please revert ASAP as this matter needs your urgent attention." What was the substance of that dispute?

Mr LYON: The dispute was a letter, which is also some way further back in the file, that I had received from San Midha that was instructing that the financial modelling results be removed from the report.

The CHAIR: And was that, if you like, the \$10 billion problem?

Mr LYON: Yes.

The CHAIR: So he wanted the removal of any reference to the \$10 billion financial turnaround?

Mr LYON: Yes.

The CHAIR: Mr Mookhey.

Ms ABIGAIL BOYD: Chair—

The CHAIR: We will go to Mr Mookhey and then to you, Ms Boyd.

The Hon. DANIEL MOOKHEY: On that email chain which the Chair has related to you, I am going to set out the time frame. Will you tell me if I am reading this correctly? The letter from Mr Midha instructing you to remove the \$10 billion discrepancy, or the part of your report that relates to fiscal impact, was sent to you on Thursday 19 November 2020 at 4.55 p.m. That is on page 264, correct?

Mr LYON: That is correct, yes.

The Hon. DANIEL MOOKHEY: Mr Pratt then emails you six minutes later at 5.01. That is on page 265. Is that correct?

Mr LYON: That is correct.

The Hon. DANIEL MOOKHEY: He says to you, "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 upon. Please revert ASAP as this matter needs urgent resolution."

Mr LYON: That is right and you will note that he is also copying in all of the senior partners of KPMG—Mr Hunter, Mr Yates, et cetera.

Mr LYON: I am sorry, you will have to forgive my ignorance of that firm. I do not know these people. Who are they?

Mr LYON: Andrew Yates is the current chief executive officer of KPMG Australia.

The Hon. DANIEL MOOKHEY: At the time?

Mr LYON: At the time he was the head of the audit division so he was the National Managing Partner in charge of Heather Watson's division.

The Hon. DANIEL MOOKHEY: Okay. Who are the others? James Hunter?

Mr LYON: James Hunter is a formerly very senior partner in the firm, very close to the chief executive, as I understand it and no longer on the National Executive Committee. A very close personal friend, by his own attestation, of Mr Pratt and the primary recipient and driver of the relatively substantial volume of work from Treasury to KPMG.

The Hon. DANIEL MOOKHEY: And David Linke?

Mr LYON: David Linke was formerly the head of my division and replaced by Mr Heathcote. He remained on this conflict panel for some time. He is now the global head of tax for KPMG.

The Hon. DANIEL MOOKHEY: I am inferring from this that you were engaged by Transport for NSW, Mr Staples ultimately, but reporting inside KPMG to the top leadership?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And they were supervising your work relatively closely?

Mr LYON: Yes, very closely.

The Hon. DANIEL MOOKHEY: And they were doing that for a period?

Mr LYON: They were. That structure was brought into place after Mr Pratt raised concerns to Mr Hunter with my first report that went to Cabinet in June. It raised both the fact that TAHE was not ready to be switched on in the form that Treasury were saying it was because there was no operating model. We called out prior structural reforms. In fact, I think the turn of phrase that we used in the report is that the history of rail largely

responds to two drivers—one is structural reforms designed to try to get product efficiencies and the second is the response to the resulting rail accidents that have happened. Then we put in two case studies—

The Hon. DANIEL MOOKHEY: We will explore that further, Mr Lyons, but just on this question—

The Hon. TREVOR KHAN: Sorry, before you go on, if there is a document that evidences that, it would be useful if that is identified now.

Mr LYON: The report?

The Hon. TREVOR KHAN: Yes.

Mr LYON: I have not brought the report with me. I will take that on notice and I will provide it. It was a report to Cabinet so if I am required to produce it, and that is legal, then I will take that on notice and produce it.

The CHAIR: I think what we might do is I might formally request you—in fact require you—to produce the document, Mr Lyon.

Mr LYON: I can probably get that brought across—

The Hon. SCOTT FARLOW: That would need a resolution of the Committee, would it not?

The Hon. TREVOR KHAN: Yes. That can only be done by the Chair.

The Hon. TREVOR KHAN: I know you are powerful, David, but—

The Hon. SCOTT FARLOW: We understand where you are going. We understand the numbers that you have.

The CHAIR: I think any member of the Committee can ask a question and the Parliamentary Evidence Act requires a response. If that requires the production of a document, I think that is also covered by the Parliamentary Evidence Act. But we can, if necessary, at the end of the hearing consider a resolution from the Committee.

The Hon. TREVOR KHAN: I think any member is entitled to request it. I do not think simply as Chair this witness can be left with the impression that you have considerable authority—

The CHAIR: No, I absolutely agree with you. There are no super powers in the Chair, thankfully, but it is also covered by the summons as originally drafted.

The Hon. DANIEL MOOKHEY: We will get into the substance of what your advice was but I am still trying to understand how it worked within your firm. I assume that it is not ordinary that every project that you do is oversighted by the level of leadership that was oversighting this project?

Mr LYON: It was highly unusual. As I was just mentioning, that first report that I delivered caused a very high degree of umbrage from Mr Pratt because it raised safety issues and it was said that he was not ready to switch on on 30 June and give it control of the rail system.

The Hon. DANIEL MOOKHEY: And on that basis—

Mr LYON: He complained to Mr Hunter.

The Hon. DANIEL MOOKHEY: And then Mr Hunter then took a more involved aspect of supervising your work?

Mr LYON: Mr Hunter formed something that they called the Conflict Oversight Governance Committee, or some such. It was a highly unusual structure. It is not something that is regularly done. It was done because Mike Pratt and I had lengthy conversations with Mr Hunter about this issue. There is correspondence in the file already around it. Mr Pratt complained, because we raised the safety issue and said it was not ready to proceed to a switch on on 1 July because there was no operating model and nobody knew what it was going to do. That caused a high degree of complaint and, as a result, Mr Hunter, without declaring what was later revealed, and again in my emails, that he was the originator of KPMG's accounting advice on TAHE. Without revealing that, he inserted himself as the chair of a conflict oversight committee despite the very obvious conflicts that he has in his relationship with Mr Pratt and the corresponding loss of independence that KPMG exhibited across this engagement.

The Hon. DANIEL MOOKHEY: Just reverting to the emails on page 265, as we established earlier, Mr Midha sent you a letter asking you to withdraw the section of the report that reports on the fiscal impact that shows that there is a \$10 billion discrepancy between your report and Treasury's.

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: At 5.01 Mr Pratt is emailing you. There is no intervening correspondence between you and Mr Midha but he then sends an email to you saying you either correct the errors or remove all references to Treasury's model. I presume you interpreted that as an ultimatum?

Mr LYON: Absolutely.

The Hon. DANIEL MOOKHEY: When you say at 5.03, at the top of page 265, you reply, "Mike, I'm sick of being bullied by you", the bullying that you are referring to specifically is the ultimatum that he sent you two minutes earlier?

Mr LYON: It is that combined with the preceding almost one year of highly unprofessional treatment by Treasury officials who were trying to—and they were in a conflict with Transport, no doubt about it. Transport had been a very resistant partner in taking TAHE on for all of the reasons that it is complex, that it causes breaks in chains of accountabilities which have a poor prior history—

The Hon. DANIEL MOOKHEY: You replied—

The Hon. SCOTT FARLOW: Can I just—sorry just let me jump in.

The Hon. DANIEL MOOKHEY: Last question please on this, because I think it is the final part of the email chain. You replied to him at 5.03 and the email by Mr Pratt to which the Chair made reference is sent to you at 5.12. That is the one in which Mr Pratt communicates to the senior leadership of KPMG—

Mr LYON: That I am a rogue partner.

The Hon. DANIEL MOOKHEY: He calls you, "a partner who refuses to take counsel and is out of control". To the senior partners, "You obviously have a partner who refuses take counsel and is out of control." He concludes with, "I expect you to take action." That whole exchange takes place within less than 20 minutes. Is that correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: In laymen's terms, that escalated fast.

Mr LYON: It did escalate fast. In particular, Mr Mookhey, this came after the advice was finalised. So the way that the accounting firms work, you issue a draft report, you get all the comments. So that is again in the report itself. We took extensive notes and attached them to it of all the things that came through. I finalised the report after—and again the documents will show that it went through every risk process. It went through all of the reviews that you would expect. It fully complied in every regard and yet not one of those senior partners, not one of them, would respond to say, "This is an output of the firm." You will see all the way through that KPMG on the one hand were telling me to stay at the poker machine and keep fixing their problem with transport, while on the other they were acting very directly against my interests, in my view, quite deliberately at the request and behest of the Treasury secretary and the other two officials.

The Hon. DANIEL MOOKHEY: Just to finalise—

The CHAIR: I am sorry, I think—

The Hon. DANIEL MOOKHEY: Literally, at this point in time Mr Staples is no longer the Transport secretary, is he?

Mr LYON: No.

The Hon. DANIEL MOOKHEY: Because earlier that week he was removed for that reason, correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And at this point, to the extent to which you were having dialogue and instruction from Mr Pratt, the person you were responding to was no longer in their position, correct?

Mr LYON: Yes.

The CHAIR: Mr Farlow had a question of clarification and then Ms Boyd has been waiting patiently.

The Hon. TREVOR KHAN: Can I just say—

The CHAIR: I hear what you say, and I accept it.

The Hon. TREVOR KHAN: Nobody is running interference but points are raised. This is not Mr Mookhey's committee. He is a member of the Committee.

The CHAIR: Which is why I am going to Mr Farlow now. I had thought that was going to be one question too.

The Hon. TREVOR KHAN: He got half dozen in, and that is not an uncommon exercise.

The CHAIR: Mr Farlow now as the opportunity and then Ms Boyd.

The Hon. SCOTT FARLOW: I want clarification on your engagement. Who were you engaged by? Was it by Transport or by Treasury?

Mr LYON: By Transport.

The Hon. SCOTT FARLOW: So Transport was your client throughout?

Mr LYON: Yes. Mr Pratt was not my client. Treasury was not my client. Another point would be that when I went through the risk process for the initial engagement I received assurances from KPMG that they had no prior conflicts and indeed an assertion from Ms Watson that she had no particular prior conflicts or anything else. What has been revealed in the testimony of estimates in the initial hearing of this Committee has shown the absolute fallacy of those assertions and, in my mind, shows that it was very clear that KPMG were 100 per cent committed to the success of TAHE because they have bet their reputations on this working.

It was very clear that I was fighting against—it became clearer and clearer as time went on that I was in an impossible position. On the one hand I was held to a contract that originated from the Cabinet that instructed that proper financial analysis and fiscal assessments be done and, on the other, a firm that was conflicted and a Treasury that was exerting very significant control over that firm. I feel like I had a real experience over the course of TAHE and again it was an ethically murky and very unpleasant period of time; nonetheless, we had a very simple job.

It was very clear we had to develop an operating model—and you have seen my paper that is up on the Committee's website—a very complex process of allocating more than 1,000 tasks for responsibility and accountability in rail. And then we were required, because we had identified the weaknesses—and indeed, the absence of any modelling at all to advise the Cabinet in June—it was always going to be awkward for Treasury because a dog ate \$7.3 billion of their homework, or more.

The Hon. SCOTT FARLOW: Mr Lyon, a point of clarification on that as well. In the documents that are referred to in attachments by Mr Midha, is that 247 letter part of the document pile that you have provided?

The CHAIR: The 11 November.

Mr LYON: There is a range of letters over time from Treasury. Let me just check.

The Hon. SCOTT FARLOW: But in that specific email that started the chain, which was the email from Mr Midha, was that attaching 247?

Mr LYON: I think so but, again—

The CHAIR: That strikes me; it is an 11 November letter from San Midha.

Mr LYON: Yes, that would be correct, I believe.

Ms ABIGAIL BOYD: Thank you very much for coming today. I know you were required, but thank you nonetheless. Just before we leave that email—266 is the one I am looking at—given that Transport was your client, not Treasury, when we look at those words, "You...have a partner who "refuses to take counsel and is out of control", do you interpret "take counsel" to mean take instructions from Mr Pratt?

Mr LYON: Yes, or from partners within KPMG who was acting for Treasury. This is fundamentally the problem, Ms Boyd. KPMG ended up being in every single part and ended up being in conflict against itself. Unfortunately, I found myself in the unpopular part of the team that was doing what I think of as the legitimate and best efforts that we could do to answer the problems we were given. But it is very difficult when senior partners have made commitments that they can produce or support outcomes that are not able to be produced or supported ultimately.

I think that might be where the Auditor-General—I certainly heard her statements the other night in the estimates. I certainly think that I the issues that I raised, you will note all of the internal turmoil within the papers about when I listed TAHE as being a fiscal risk. The risk registrar is required to provide—you will see all of the responses within KPMG—the direct emails from Treasury, KPMG accepting wording changes to project risk registrars sent directly by Treasury. This is highly inappropriate. I was not working for Treasury. KPMG as a firm accepted an engagement and it then took on conflicting engagement after conflicting engagement. It did it

knowingly, in my view, and it did it because it had made commitments at a senior level that it was going to be able to produce things that other accounting firms said would not be able to be produced.

Ms ABIGAIL BOYD: So "out of control" in that context is effectively an assertion that KPMG had lost control of one of their partners who was then acting against—

Mr LYON: Yes, I think it was an assertion. I think what Mr Pratt was expressing is his consternation that KPMG was not doing exactly as instructed, even in its work for another entity. I think that is pretty obvious. He was never my client. He was a stakeholder in it. I was engaged directly by Transport and directly through—and quite unusually through—Cabinet's decision in June which specifically references us having to do those two tasks: to do an operating model that is capable of passing independent safety review and to develop a detailed and sophisticated financial model.

We did both of those things. We did them extremely well. The firm was forced—and you will see again that all of the work that we produced was signed off as a final deliverable of KPMG. It went through every level of rigour and assurance internally. A higher level, indeed, because very powerful people within the firm did not want that work published or certainly wanted it changed. I guess we were in the unhappy position again of having signed a contract, given our word to a client that we would do our best efforts and it is very clear that Mr Pratt felt that he had the level of control over KPMG senior leadership that he could do as he pleased.

If you look through correspondence before that you will see, as I said, ongoing attempts to remove, to consolidate, an instruction from Treasury saying that they had now agreed with Transport that my work would cease; that there would be one report from KPMG only. You will see the responses from Rodd Staples and Fiona Trussell of Transport saying, "That is absolute nonsense", and KPMG will be expected to deliver the work that I was contracted and selected to do.

Again, I think KPMG has let itself end up in a position where it has the same level of internal control that one might have with a bad case of gastroenteritis. They have ended up with conflicts all over the place and, as a result, I was put through the mincer. But I do not feel I had a choice. It was either, "Do as I said" or it was sell out, and once you have sold out and changed your results on instructions from someone powerful, you have lost your credibility as a professional after that. So I do not feel I could do that.

Ms ABIGAIL BOYD: And it would have been unethical, would it not, to be taking instructions from someone who is not—

Mr LYON: Highly unethical.

Ms ABIGAIL BOYD: Just one last question before I pass back. Did you speak with Mr Staples about this? Did you talk to him about the bullying that you felt you were experiencing from Mr Pratt?

Mr LYON: Many times. You will see that I reported it consistently to people within KPMG. Nothing was done. It was acknowledged. You will see all the hollow thanks from senior partners after I completed my work, noting all the complexity and the unpleasantness and then you will see the flurry of formal investigations and allegations that I had bullied Ms Watson, including by referring to words like "ethics" and so on. Again I would encourage you to read those and it will give you a flavour of how it was.

Ms ABIGAIL BOYD: Do you believe Mr Staples lost his job because of this conflict?

Mr LYON: It is not a question I could answer, Ms Boyd. I do understand, and I did speak to Mr Staples when I received the subpoena the other day. I gave him a call. I also let KPMG know and gave a couple of members of the committee a ring as well. I am aware that he is likely to be called at some point. I would encourage you to direct it to him. I did not have visibility of really the political discussions. I was really just exposed to Mr Pratt and the people who worked for him and the senior partners, including the current chief executive officer that worked for Mr Pratt.

The Hon. JOHN GRAHAM: Thank you, Mr Lyon, for your evidence. What was Transport's concerns with this arrangement? I am looking at your document 297 where you say, "This was early on in the process. Transport for NSW were unable to support TAHE at that time because no safe operating model had ever been developed."

Mr LYON: Yes, and the intention of Treasury, the intention of Mr Pratt at that time was to move a Cabinet submission that established TAHE with full control over the railways and all the rest. Transport, again you should ask Mr Staples or others about the direct discussions with Mr Pratt. But it was certainly my professional view that without an operating model you cannot hand over control of a public railway that moves millions of people when you do not know who is in charge of what.

The Hon. JOHN GRAHAM: And at times you say that was a vigorous battle. At 294 you say, "TfNSW and NSW Treasury then had a vigorous battle over the substance of a Cabinet minute with TfNSW insisting on the inclusion of risks identified in our report and also a return to Cabinet in October."

Mr LYON: Yes. That is correct.

The Hon. JOHN GRAHAM: Just give us any more detail on that particular moment.

Mr LYON: My view is that senior transport officials would have resigned rather than accept the position that Treasury were in moving up to June. Treasury were frantic because they were very worried about last year's audit having done nothing to get TAHE ready and now, sort of, facing the prospect of having to urgently switch it on.

The Hon. DANIEL MOOKHEY: When you say "last year's audit" you mean the Auditor-General's report for 2020?

Mr LYON: Yes.

The Hon. JOHN GRAHAM: And you are specific about some of those risks at 293 where you say, "In particular the Treasury Secretary was reportedly furious with the inclusion of case studies on the Glenbrook Waterfall and Hatfield rail disasters in New South Wales and the UK respectively."

Mr LYON: Yes, that was communicated to me directly by Mr Hunter of KPMG. He rang me. I was sailing my boat down the channel in the middle of a storm and I got a call from Mr Hunter telling me that Mr Pratt had expressed extreme anger at the inclusion of case studies around safety. Again, my client was Transport. The issue was to look at whether TAHE was ready to be switched on, on 30 June, 1 July last year. The answer to that is clearly no. You have seen the report with the more than 1,000 tasks, the incredibly boring RACE allocations that we had to go through. It is a very complex system, public rail. In my view, I think, senior transport officials would have resigned rather than accept where Treasury were at last year.

The Hon. JOHN GRAHAM: Are you saying Mr Hunter conveyed the extreme anger of Mr Pratt? Can you recall the words he used to convey that?

Mr LYON: I cannot. It was lengthy phone call and that led to the formation the next day of this conflict group that was created to, sort of—

The Hon. JOHN GRAHAM: But you do recall it being specifically about these case studies in relation to Glenbrook, Waterfall and Hatfield?

Mr LYON: Yes.

The Hon. JOHN GRAHAM: And you go on to say, "In each case financially motivated structural reform was found to be a major contributing factor to the loss of lives in those rail accidents"?

Mr LYON: Yes.

The CHAIR: Mr Lyon that really gets to the nub of one of your core concerns, does it not, that producing an operating model, without understanding how it would impact on rail safety and how something as important as a rail network would operate, was plain reckless?

Mr LYON: I think where Treasury were at in April, May and June last year was highly dangerous. I think they had lost sight of what matters with the public rail system and it was all to do with the net fiscal presentation of the budget. We have to remember, this is all largely about a non-cash expense. If we summarise what we found in the financial model, because the asset size is much bigger than Treasury had modelled previously, the financials of it do not work. It is just too expensive and what they have done is turned non-cash expenses on the budget into cash expenses on the budget.

The CHAIR: I am trying to understand from your professional perspective the intervention of Mr Pratt in November 2020, asking you to rewrite what was, by that stage, a finalised report. Is that right?

Mr LYON: That is correct.

The CHAIR: Mr Pratt, having come from Treasury, being the head of Treasury, was not even your client?

Mr LYON: That is correct.

The CHAIR: From an ethical point of view have you seen that behaviour before—having a finalised report being directed to be rewritten?

Mr LYON: I have never seen the behaviours that I saw from Mr Pratt, Mr Midha or Ms Wilkinson ever before in the public sector. In fact, at the very front I have included a contemporaneous set of notes about a call I made to Mr Pratt in which I outlined a range of views around the professionalism of the Treasury over TAHE.

The CHAIR: I note as well in the documents there is another email on page 191, where you are raising concerns with a series of your partners. You are relaying the fact that in September 2020 it appeared the then Premier was raising questions about Treasury's behaviour.

Mr LYON: That is correct. That is some contemporaneous notes that I sent round internally. Again I was constantly trying to give people at KPMG a very expressed sense of the risk to the firm and also the conflicted position that they were in. I was constantly trying to give them a sense that this was an internal fight within government.

The CHAIR: Yes.

Mr LYON: These are contemporaneous notes that I circulated—sorry, Chair.

The CHAIR: No, I did not mean in any way to limit your answer to that. This was a very important contract for KPMG. Do you know what the value to the firm was?

Mr LYON: Which contract?

The CHAIR: First of all, the contract with Transport?

Mr LYON: I think my engagement was about \$1 million in total. I think probably the more material issues for KPMG—certainly my view of the material issues for them—would be the impact of all of the other work they do for Transport. But I have subsequently learned they are doing an enormous volume of work for Treasury and that that has continued to increase. So it is clear that certainly the powerful partners within the firm are very aligned to Treasury.

The CHAIR: And they have made effectively a bargain with Treasury that they would somehow get TAHE to work—

Mr LYON: Yes.

The CHAIR: And would provide the backing to do that?

Mr LYON: Yes.

The CHAIR: The problem with your advice was you pointed out how problematic that was.

Mr LYON: Yes.

The CHAIR: And then they basically dropped you like a gun?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Chair, I might pick up from where you left off. The Chair referred to an email on page 191 which, as you say, are contemporaneous notes you had that you emailed on Thursday 24 September 2020. Is that correct?

Mr LYON: Correct.

The Hon. DANIEL MOOKHEY: Would you turn to page 146?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: This is an email that you received from Mr Hunter. He sent it to you on Sunday 13 September 2020 at 7.47 p.m. Do you see that at the top?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And he cc'd it to self and to various other people in the firm including Mr Heathcote, Mr Linke, Ms Watson? Do you see that?

Mr LYON: Yes, and Mr Yates.

The Hon. DANIEL MOOKHEY: Can you see that this appears to be minutes of a meeting, or at least an update? Do you see that?

Mr LYON: Yes, I do.

The Hon. DANIEL MOOKHEY: I will read from the second paragraph. This is on 13 September which is 11 days prior to the other email to which the Chair referred?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: The second paragraphs states, "I was working in Treasury on Thursday and had face-to-face meetings with San and Mike. Further discussions with San on Friday and Mike called this evening as well. I have also spoken with Joel, David, Andrew and Paul on Friday over the weekend. This note outlines summary of key feedback and recommended steps I have discussed and agreed with David, Paul and with Mike and San. I presume that David and Paul is David Heathcote and Paul is—

Mr LYON: Paul Low, KPMG's head of government.

The Hon. DANIEL MOOKHEY: And Mike is Mike Pratt, and San is San Midha?

Mr LYON: That is correct.

The Hon. DANIEL MOOKHEY: It says, "1. Premier meeting. On Friday a meeting with the Premier" who at that time was Ms Berejiklian, correct?

Mr LYON: That is correct.

The Hon. DANIEL MOOKHEY: "Treasurer", who at that time was Mr Perrottet?

Mr LYON: Correct.

The Hon. DANIEL MOOKHEY: "Secretary of DPC" which you have identified as Tim Reardon.

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And "Secretary of Treasury, Mike Pratt attending."

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Were you at that meeting?

Mr LYON: I was not.

The Hon. DANIEL MOOKHEY: So you were receiving this email as a way in which Mr Hunter could inform you as to what took place?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: It says, "TAHE was discussed. Everyone was well across the challenges but also imperative." Do you see that? It says equally, "The Premier was unequivocal that TAHE will go ahead, as was Tim. Both wanted to accelerate work, including the ERC sub." I presume that is a reference to the Expenditure Review Committee submission?

Mr LYON: I would believe so, yes.

The Hon. DANIEL MOOKHEY: And then there seems to be italicised which is commentary, "This isn't a surprise. We have always expected strong endorsement and resolve to proceed with government policy to implement TAHE." Do you see that?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Paragraph 2 goes through the dot points, "Approach to finalise ER submission and the TAHE operating model which sets out the next steps", correct?

Mr LYON: Correct.

The Hon. DANIEL MOOKHEY: The remaining parts of the email are really just matters arising. Is that fair?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: To be clear here, 13 September 2020 is prior to you finalising your report, but not too much further?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: It is clear here that the Premier informs a meeting that you are not attending it. She is "unequivocal that TAHE will go ahead, as was Tim". Did you conclude that part of the

behaviour that you were then treated to, arose as a result of the Premier's unequivocal position that TAHE will go ahead?

Mr LYON: Again, I could not comment on that. I think it is very likely that Mr Pratt and his colleagues had been under an enormous degree of pressure because this is quite a material issue to the budget. I would not be surprised if any Premier would say something like this has to be fixed.

The Hon. DANIEL MOOKHEY: Of course.

Mr LYON: What I would expect is that a bureaucrat would not then breach, in my view, both ethics and potentially lawful behaviours to achieve something that is not achievable.

The CHAIR: I think Mr Khan has a clarification question at this point.

The Hon. TREVOR KHAN: Again, this is not an interference running exercise. Point 3 on that email numbered 146, "KPMG involvement. I reinforced to both San and Mike this evening we had the most knowledgeable and experienced team involved in TAHE.: I take it that is a reference to you, at least in part?

Mr LYON: In part but he carries on to basically say that and also emails Treasury and everybody else to basically say I have been replaced off the engagement by a second partner.

The Hon. TREVOR KHAN: That is what I was coming to. If you turn over the page it says, "We discussed further last week an agreement with San that we would provide further second partner support." Would you like to explain what the "second partner support" is?

Mr LYON: It is really not a thing, Mr Khan. The second partner is an internal position. It is usually not particularly prominent. It is the person that you use to sort of cross-check your work and so on. It certainly was not anything other than an attempt by Mr Hunter to discredit me to suggest that, and you will see again through the correspondence Treasury suggesting to KPMG—and then it being rejected each time by Transport—that there would be a single report, that it would be Heather that did it. This was another attempt, and you will see my response that I—

The Hon. TREVOR KHAN: And your response is 147?

Mr LYON: Yes, "This is unacceptable, James." Yes, that is the one.

The Hon. TREVOR KHAN: That was sent 10 minutes after the lengthy email?

Mr LYON: Yes.

The Hon. TREVOR KHAN: So the battle was on at that point?

Mr LYON: The battle started from the start. It started from the start because no-one told me that KPMG had already promised an answer, as it turned out, at the most senior levels. I do not promise an answer on something like TAHE. It is very complex. It takes a long time to get to grips with. It was very complex to model. It was very complex to reach the assumptions. I think the battle was on from the very start and it was extraordinary that a whole range of prior works that KPMG had done were not disclosed. We discovered them as we went through but it became very clear to me that I was in an unwinnable position. Again, I had to choose between my own professional ethics and my partnership at KPMG, and I chose accordingly.

The Hon. TREVOR KHAN: My question is this because it has arisen a number of times. I have never worked in a large firm—

Mr LYON: Congratulations.

The Hon. TREVOR KHAN: In the small firms that I have worked for or ran, if you have a conflict you just flicked one or other of the punters, or perhaps in many cases both.

Mr LYON: Yes.

The Hon. TREVOR KHAN: But we know in large firms they talk about this concept of Chinese walls. Where were the Chinese walls in this exercise?

Mr LYON: I suspect they were more Japanese walls because they were highly porous and papery. The fact that the most conflicted partner in the firm, James Hunter, the one who had sold this to Treasury, established himself as the overseer of a conflict management group, really shows that from the get-go this was not properly structured. It was an improper state of affairs and I think it reflects incredibly poorly on KPMG's internal controls. I think it reflects incredibly poorly on their HR department and its leadership and, particularly, on its ethics and risk division. I mean, this is really embarrassing for KPMG. It is humiliating for Treasury because they have got it so wrong. But it is embarrassing for KPMG because they did not have the moral strength to say no to one or the

other. They tried to back two horses or, to put it another way, they put two crabs with a carp and waited to see which one would emerge alive.

The Hon. TREVOR KHAN: Indeed. If the Committee accepts what you say, KPMG failed its client.

Mr LYON: One hundred per cent. KPMG has set up the New South Wales Government to fail because it has promised things that it cannot deliver. Clearly the scrutiny that is coming from audit, I mean, all of the things that I was subject to—opprobrium, discipline, active management, conflict management, whatever you want to call it—they are all the things I heard the Auditor-General say the other night are major concerns. I feel like we did our work well. We did it professionally. We did it under an incredible degree of inappropriate pressure from a whole range of places but, again, we did not have much choice, Mr Khan. Once we had signed the contract, once we had given our word to do our work professionally, we had no choice but to do it.

The CHAIR: Mr Farlow has a question of clarification.

The Hon. SCOTT FARLOW: In that email from Mr Hunter there is a suggestion that there are two partners, both for your work, or the work in which you were engaged for Transport for NSW and also for Treasury's work. Is that correct.

Mr LYON: Yes.

The Hon. SCOTT FARLOW: That would be an additional partner with Ms Watson. Is that correct?

Mr LYON: Yes.

The Hon. SCOTT FARLOW: Did this ever come to fruition or was it stopped in the internal machinations?

Mr LYON: No, the second partner exists. They exist on all—and Paul Low. On my initial engagement—

The Hon. SCOTT FARLOW: So Paul Low was your second partner?

Mr LYON: Initially my second partner was Heather Watson after she declared that she had no conflict. So she was originally the second partner on the work for Transport. I reported her in the second week to risk because it became very clear that she was trying to sabotage the work. She was removed as my second partner and replaced by Paul Low who is Queensland based and the head of government. I only have good things to say about Mr Low. Ultimately he and Mr Heathcote were wholly ineffectual in their promises to protect me and their reassurances that I was supported by the firm and doing the right thing. Nonetheless, both of those gentlemen showed a degree of decency that I did not see from the others.

The Hon. SCOTT FARLOW: And so then there was a second partner that was allocated who was already pre-existing with Ms Watson?

Mr LYON: Yes. Andrew King. He is Ms Watsons' boss in her accounting team and they both report to Mr Yates, or did both report to Mr Yates then as the head of the audit division, who is now the chief executive officer of the firm.

The CHAIR: Ms Boyd has a question of clarification and then I will briefly ask you about one document and then I will hand you back to Mr Mookhey.

Ms ABIGAIL BOYD: Thank you, Chair. I want to clarify something in relation to the conflict of interest issue. I used to work in large law firms and we very clearly had technological communications and even physical barriers when we were working on both sides or with multiple parties on the same transaction. Was it the case in relation to this transaction or this bit of work—

Mr LYON: I think it is right to characterise it as a transaction. It is the largest thing that happened last year. It was a \$40 billion corporation that got created. So "transaction" is not a bad way to think of it.

Ms ABIGAIL BOYD: Okay, so with this transaction was there an agreement with both clients that there would be some cross-communication or is this the standard process in accounting firms?

Mr LYON: Initially, that was the intent. As it became clear—and you will note all sorts of emails back and forth between Rodd Staples and senior partners in the firm and Fiona Trussell the same—as it went on, you will see very direct instructions from Transport that none of the conflicted partners, and particularly James Hunter, were to be given access, and you will see the repeated attempts to get access improperly. You will see the emails between me and James Hunter where he sort of verbalised and pressured me to produce Transport's confidential information to Treasury in breach of a non-disclosure agreement, and you will see that Transport actively and directly and by name rejected the inclusion of those individuals—James Hunter, Heather Watson, et cetera—from

access to their information because of their view of the highly improper state of affairs and the high degree of demonstrated conflict that KPMG were in.

The CHAIR: Mr Lyon, would you object to us forwarding these documents to the Auditor-General?

Mr LYON: I would not.

The CHAIR: Could I ask you to have a look—

The Hon. TREVOR KHAN: They are really within our gift now, seeing they are produced under summons. I know you asked Mr Lyon but I think it is not his call.

The CHAIR: No. Could I ask you just about the document on 142? As I understand your evidence, it was becoming apparent to you, at least by September, if not earlier, that this was a reverse-engineering exercise.

Mr LYON: Yes.

The CHAIR: The decision had been made.

Mr LYON: Decision-based evidence making is what it is called.

The CHAIR: So regardless of the risks, regardless of the concerns, the direction to your firm is basically "Make it happen."

Mr LYON: Yes.

The CHAIR: This is an email from Michael Pratt on 13 September 2020, it is at 2.17 p.m., to you and to San Midha and cc'ing in Rodd Staples.

Mr LYON: And Bruce Morgan.

The CHAIR: Bruce Morgan and Paul Low. It references an earlier note and then he says, "Our collective responsibility, Treasury, Transport and the TAHE board coming out of the ERC July approval, is to return to ERC in October with an agreed operating model. This is not about whether we do or do not progress TAHE, we are!"

Mr LYON: Exclamation mark.

The CHAIR: Yes. That really confirms that this was that reverse-engineering exercise, does it not?

Mr LYON: One hundred per cent.

The CHAIR: You responded to that. Do you want to indicate what happened after that?

Mr LYON: Yes. I received the email, I wrote back, I said that it was nice to hear from the secretary—given nearly all of the communications were from him to James Hunter and so on. At least he had communicated directly for a change. I said I did not agree that Mr Midha's email was a good summary, that I had told him that it was not a good summary. I told him that we were going through the detailed process of understanding what TAHE does and putting in place a clear plan for risks that came out of it. I also raised with him, and I will read from it, "As with other points over the past few months some of your people thought cause to complain to my partners about a supposed lack of professionalism was an appropriate response."

I understand there is a lot riding on TAHE for all involved but it is not helpful or a professional way to respond to a thorough draft. Mike, I think it would be good to get together in person to discuss TAHE. I will send a formal meeting request to your EA tomorrow. I would also appreciate if you and Bruce—that is the now chairman—"would communicate to your relevant staff to maintain appropriate professional courtesies toward me and my team in meetings and to respond professionally to drafts related to the Cabinet process. This is a complex job that is being made harder, not easier, by TAHE and Treasury at the moment. Thank you for responding and I regret I could not be more positive on such a warm spring day."

The CHAIR: A very polite pushback, Mr Lyon. Mr Mookhey.

The Hon. DANIEL MOOKHEY: Just to close that questioning out, Mr Pratt sent you that email on Sunday 13 September at 2.17. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And you replied at 3.27 p.m. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Did that meeting ever take place?

Mr LYON: No. I had my PA start requesting meetings; she requested one a day for about three days, until Mr Pratt wrote back and said he is not seeking a meeting.

The Hon. DANIEL MOOKHEY: Can we just return back to the document, after all the points of clarification, on page 146, which is the Premier meeting which takes place with Ms Berejiklian, Mr Perrottet, Mr Reardon and Mr Pratt? One omission is startling there. Do you have any explanation or did you make any inquiries about why Mr Staples was not at that meeting?

Mr LYON: I assume that Mr Staples would have been there, but I had not noted or remarked on that before, so perhaps he was not.

The Hon. DANIEL MOOKHEY: And you had no understanding why not?

Mr LYON: No. I mean, the main thing that I read from this email is actually section 2, which is effectively James Hunter saying he is about to change all of the reports that are coming out of KPMG because he agreed it with Mike.

The Hon. DANIEL MOOKHEY: When you say that, is that what you mean by dot point one and dot point two: "Mike indicated Bruce Morgan"—

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: —which is helpfully identified as the TAHE chair and the TAHE board—"Mike indicated Bruce Morgan and the TAHE board would be more involved in the weeks ahead." Then Mr Hunter—"I indicated we needed to change the approach of TfNSW reading and writing and others reviewing and criticising finites in reports." So that means basically Mr Hunter was taking away or suggested that Transport should lose the ability to author its own report?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Okay. That is what the reference is, right?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Just to close out on this dot point—

Mr LYON: There is more correspondence that follows there, but what Treasury were trying to do was to force KPMG to say there will now be a single report; it will be under the control of Mr Hunter and Ms Watson, that it would be consolidated. You will see the responses from Transport repeatedly saying, "We want what we—

The Hon. DANIEL MOOKHEY: When you say the responses by Transport—

The Hon. TREVOR KHAN: Let him finish.

The Hon. DANIEL MOOKHEY: I was just going to ask—

The CHAIR: I think Mr Lyon—

The Hon. DANIEL MOOKHEY: Just let me ask the question.

The Hon. TREVOR KHAN: No, let him finish.

The CHAIR: I think Mr Lyon had not finished his answer, Daniel.

The Hon. DANIEL MOOKHEY: The reference I was going to ask, when you said "Transport" you are referring specifically to Mr Staples resisted that as an option. Correct?

Mr LYON: Yes.

The Hon. TREVOR KHAN: I do not raise the issue that what Mr Mookhey is doing in his follow-up question is wrong, but the witness is entitled to complete his answer for all of us.

The CHAIR: I agree, and I think, Daniel, everybody thinks your questions are valid and relevant, but if you could just wait for Mr Lyon to finish, because, first, we are here to hear from Mr Lyon and, second, it is best for Hansard. But no-one is trying to stop your questioning.

The Hon. TREVOR KHAN: No.

The Hon. DANIEL MOOKHEY: Indeed. Can we turn quickly, just to close this out, to page 147, where you made positive references—

The Hon. PETER POULOS: Chair, just before Mr Mookhey continues, could I clarify whether there was only going to be one report?

Mr LYON: This was Treasury—when I say "Treasury" I do not mean the other hundreds of fine professionals that work in that organisation. When I am referring to "Treasury" in this evidence I am talking about Mike Pratt, San Midha and Cassandra Wilkinson, in particular.

The CHAIR: Did that answer your question, Peter?

The Hon. PETER POULOS: Just to clarify that further, so it was Treasury's—Mike Pratt, San Midha and Cassandra Wilkinson—view that there would be one report.

Mr LYON: Yes, that was their view and they kept pushing that to KPMG. There are emails from San saying it has all been agreed, and then there are emails back from Transport saying, "That is absolutely untrue. We expect KPMG to deliver on what it contracted with us to do." And then later there was a new scope of work taken on to directly contradict our work. There is quite a high degree of correspondence then between Transport and KPMG's senior partners, again about the conflict, the ongoing story of conflict.

The Hon. PETER POULOS: And your interactions were always on the basis that it would remain with Transport.

Mr LYON: One hundred per cent. Transport expected—in fact, Transport were required by Cabinet to return with an operating model, not Treasury. The Cabinet decision, the Cabinet minute in June says that Transport for NSW will lead the development of an operating and financial model in consultation with Treasury, because the truth—"truth" is not the right way to describe modelling—because the detailed modelling did not support the numbers and revealed a whole range of errors. Treasury were continually trying to take control of it, they were continually trying to remove the—

The Hon. TREVOR KHAN: The embarrassment.

Mr LYON: —the embarrassment, yes. And when that would not be removed I became the embarrassment and they wanted to have me removed instead.

The CHAIR: I am now going to go back to Mr Mookhey and give him some nice clear air to finalise this line of questioning.

The Hon. DANIEL MOOKHEY: Thank you. Just as we defined who specifically you are referring to in Treasury as Mr Pratt, Mr Midha and Ms Wilkinson, when you refer to "Transport pushed back" are you making a reference to Rodd Staples, the secretary, and Fiona Trussell, the deputy secretary?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Thank you. Just to close out this line of questioning, on 147 you made positive references to Paul Low, but on this email Mr Hunter communicates to San Midha at 7.33 p.m. an email. The only relevant part I want to ask you about is it says there, sort of midway through, just after the linked-in reference to Mr Low, which I presume you—

Mr LYON: Sorry, which page are we on, Mr Mookhey?

The Hon. DANIEL MOOKHEY: On page 147. It says here, "Paul is well-known to Tim Reardon and has been EQCR for two months and is across the TAHE issues." Do you see that?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: I infer from that, that it was important to KPMG to nominate a person who was well-known to the Department of Premier and Cabinet [DPC] head.

Mr LYON: I do not know if it was important in reality or it was more just the usual name-dropping that happens within big firms.

The Hon. DANIEL MOOKHEY: Fair enough, but either way, the implication here is that Mr Reardon was paying some attention to this.

Mr LYON: I would say Mr Reardon would have been paying an extreme amount of attention. I mean, this is material to the budget: it is tens of billions of dollars. So I would be very surprised—Mr Reardon was the Transport secretary when TAHE was formed; I do not think he was probably a fan of it then, but again, you change jobs and you change your perspectives. If I was the secretary of DPC I would be furious at a Treasury secretary who had brought in this level of error, and if I was the Treasury secretary I would probably be very motivated to try to make it true, and I think that is what we have seen; it is just that the systems and controls have not worked to control that.

The Hon. DANIEL MOOKHEY: Mr Lyon, one of the questions, to be fair, arising from the line of questioning that was 20 minutes ago was about Treasury's insistence that you change the report despite them not being your client. Do you recall?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Just on that, your client accepted the work. Correct?

Mr LYON: Not only accepted the work, was very impressed by the technical complexity. There was full agreement. So, again, the financial model that Treasury keeps saying had errors in it, the only errors that were in it, from their point of view, was the answer.

The Hon. DANIEL MOOKHEY: Transport never instructed you to make any alteration to the key section around fiscal impacts?

Mr LYON: Quite the reverse, Mr Mookhey. They felt that it was incredibly important that they respond honestly to the Cabinet's request, and I note that after my report was finalised it went through the Cabinet as an attachment, as did Ms Watson's competing work that found differently to ours.

The Hon. DANIEL MOOKHEY: Can I just table and provide to the witness a document that has been obtained?

The Hon. TREVOR KHAN: Is this a new document?

The Hon. DANIEL MOOKHEY: It is.

The Hon. TREVOR KHAN: Great.

The Hon. SCOTT FARLOW: As if we did not have enough already.

The Hon. DANIEL MOOKHEY: Just to that one, do you see that that is a letter from Mr Pratt to Mr Staples on 11 November 2020?

Mr LYON: Yes.

The CHAIR: You might want to take a minute to digest it, Mr Lyon.

The Hon. DANIEL MOOKHEY: I think the key section is the last paragraph on the first page.

Mr LYON: Yes, that has been in the paper a bit that one.

The Hon. DANIEL MOOKHEY: You have my copy of it, but Mr Pratt tells Mr Staples that as a result—perhaps could you read the last paragraph for us?

The Hon. TREVOR KHAN: I do not want to be rude, but is this for the witness to be doing this?

The CHAIR: I am going to ask Mr Mookhey to bring it back to what this witness can add, but I am sure we will get there. We will give Mr Mookhey the ability to—

The Hon. DANIEL MOOKHEY: Mr Lyon, can you read the relevant section that refers to you?

Mr LYON: Yes. "We do not see value in expending further time addressing these persistent errors. In the absence of Mr Lyon amending his report and deleting all references to Treasury and fiscal advice, and we have requested him to do so, we will provide fiscal advice to accompany the submission that supports our forward estimates. These fiscal issues have been addressed by KPMG finance and accounting partner Heather Watson in her report. We have determined preliminary approaches to each of these challenges which inform the FIS table"—which is the financial impact statement table.

The Hon. DANIEL MOOKHEY: I think that is the relevant section. Mr Midha made the earlier request to you almost identical in the letter that we discussed earlier. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And you refused. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And then from that we can infer that Mr Pratt then did not ask Mr Staples but instead told Mr Staples that he was now effectively going to submit an alternative report to Cabinet. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Is that after Transport resisted Treasury's attempt to merge the reports?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Were you aware that such a letter was sent?

Mr LYON: I was because I got one that was almost identically the same. I forwarded it to, I think, from memory—again, I do not have access to my old emails, but I am pretty sure I forwarded it immediately to Rodd Staples and Fiona Trussell.

The Hon. DANIEL MOOKHEY: Did you provide Mr Staples and/or Ms Trussell advice as to how they should respond?

Mr LYON: No, I did not provide them—

The Hon. DANIEL MOOKHEY: But you forwarded it—you basically drew to their attention that it was identical to a letter request that you had received?

Mr LYON: I sent the letter I received to them because it was absolutely germane and relevant to the ongoing pressure to change the results in work that was being done for Transport for NSW. Again, I think you could ask Mr Staples when you see him, but they were very supportive of the work. I guess the key points, probably the key point where everything stopped was when Ms Watson's contradictory report came out and at that point the Cabinet process stopped because, as Transport said, "We do not know what numbers to put in because we have two different reports saying two different things from one firm", that was when Mr Heathcote wrote his clarifying letter, which said that the firm stood by the modelled results and that it was the most complex operating model work done to date.

The Hon. TREVOR KHAN: Sorry, Daniel, you asked a question that left one out in a sense.

The Hon. DANIEL MOOKHEY: I let the witness answer the question.

The Hon. TREVOR KHAN: No, no, no, there was another one.

The CHAIR: I will go to you, Mr Khan, if you have a question.

The Hon. TREVOR KHAN: Mr Lyon, if you sent on the almost identical letter to Mr Staples and co., did you get a response?

Mr LYON: I do not think so. I spoke to them. I was down in Woomera actually at the time working on another—

The Hon. TREVOR KHAN: I suspect we should not ask what that is.

Mr LYON: —working on another engagement. I remember speaking to Mr Staples from there. I do not think we emailed back and forth; it was really just giving—because there was so much incoming interference from Treasury all of the time, and they were facing the pressure of needing to get an operating model that worked but tell the truth to the Cabinet around the financial performance of it, because ultimately the costs are the costs. We spoke about it. I think in the end the request from Transport was there must be a clarification from KPMG about what these two different figures mean. On the one hand you have got a report saying that it is all sweet and, on the other hand, you have got a report that is saying it is quite bitter actually, and Transport wanted to know whether they had wasted their million dollars or not and they wanted to know which numbers to take forward. Again I compliment Mr Heathcote—

The Hon. TREVOR KHAN: Can I just interrupt and get you to go back a step? If you spoke to Mr Staples from Woomera, are you able to say what he said to you?

Mr LYON: I cannot really remember. I think we were remarking—

The Hon. TREVOR KHAN: And that is all right.

Mr LYON: It was basically about the fact that they needed to get a figure to put into the Cabinet submission. All of the discussions at that time—remembering that the operating model sections of my report had been sort of completed, circulated, all of the rest—it was really this fight around the representation and modelling of what would happen once TAHE switches on. So most of the discussions were really about trying to manage the ongoing incoming interference allegations, everything else, from Treasury as they tried to sort of confuse the issue and avoid the embarrassment, I guess, of having to tell the Cabinet that they had made some material errors.

The Hon. TREVOR KHAN: I will pass the torch back to Mr Mookhey.

The CHAIR: Mr Graham has been waiting patiently.

The Hon. JOHN GRAHAM: I am happy to let Mr Mookhey continue.

The CHAIR: I have a short question too. Mr Mookhey, if you want to finish this line of questioning, then Mr Graham and then me.

The Hon. DANIEL MOOKHEY: I do. Can we turn to page 254 of your tabled documents? Do you see that this is an email you sent to Mr Staples, Ms Trussell and you cc'd to Mr Heathcote and Mr Low, in which you were providing advice to Mr Staples this is the appropriate way to respond to a letter he has received from NSW Treasury. Correct?

Mr LYON: So no. This is a draft of a clarifying letter to Transport. By this point in time my assurances as a partner of KPMG were not enough because, demonstrably, I was not able to hold the firm to its outputs; they wanted confirmation from a senior national executive member. This was the draft of what would satisfy Transport to be able to, with confidence, put the numbers in the Cabinet submission and return to Cabinet.

The Hon. DANIEL MOOKHEY: I infer from that, that Mr Staples had rejected, effectively, the invitation that was provided to him by Mr Pratt in the letter I just referred to you, to withdraw your report.

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And he took further steps to ensure that this advice was provided to Cabinet. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Thank you, Chair.

The CHAIR: Mr Graham.

The Hon. JOHN GRAHAM: Thank you, Chair. You made reference to Mr James Hunter as being one of the main sources of work for KPMG from Treasury, and that was, in part, due to the relationship with Mr Pratt—

Mr LYON: By his own statement—

The Hon. JOHN GRAHAM: —or perhaps what he claimed about his relationship with Mr Hunter.

Mr LYON: Mr Hunter has said all sorts of things, as he regularly goes around to Mr Pratt's house; every time you talk to him he has just been with Mike Pratt. He changed his email signature to "Cabinet in confidence" for a period of time until it made him look a little bit silly. He is very, very, very close indeed to Mr Pratt—I believe that to be true; it is an issue that is remarked on by the officials within the Treasury—and certainly he has been something of a rainmaker, from what I can work out, in terms of Treasury contracts.

The Hon. JOHN GRAHAM: When you say "a rainmaker", you have talked about the potential value of this contract, but just give us some sense of the scale of the work.

Mr LYON: I am not really sure because, again, I have never done work for Treasury, but, as I understand it, there are whole divisions of KPMG doing work on tax reform stuff and COVID stuff, and I certainly hear from other big-four firms that they view Treasury as pretty much a KPMG shop. I do not know what the volume of money is; I am sure it is reported somewhere and you can have a look.

The Hon. JOHN GRAHAM: Sure. Thank you.

Mr LYON: But it is definitely a very important relationship within KPMG—more so than Transport, as it turned out—and I would say that that is that strength of relationship between—

The Hon. JOHN GRAHAM: And how often would Mr Hunter physically work from the Treasury offices?

Mr LYON: I think he lives there, I am not sure.

The CHAIR: He is the El Niña partner.

The Hon. JOHN GRAHAM: I might just turn to the document 49 that refers to the engagement with the Audit Office, and this is a note of yours. It says, "Below is the latest email from the Audit Office. This points to a further deterioration in the likelihood of KPMG's accounting advice passing audit." I will briefly summarise the Audit Office's concerns in that attachment; they relate to: has a revised timetable been determined by Treasury about the transition plan? Does Treasury and the ABS need to revisit the classification of TAHE as a commercial entity? Is it for-profit or not-for-profit? What financial modelling supports that and its commercial returns? That is the nature of the Audit Office's concerns. Would you agree with that?

Mr LYON: Yes, and if it is the one I am thinking of—it is not, but certainly in one of the other emails from the Audit Office it is bolded, underlined and in red. I have never seen an Audit Office be that firm before.

The Hon. JOHN GRAHAM: They had serious concerns.

Mr LYON: Very obviously.

The Hon. JOHN GRAHAM: In this document 49 you go on, and I will quote this part to you, "San suggested"—I take it that is Mr Midha—

Mr LYON: Yes.

The Hon. JOHN GRAHAM: —"not responding to the Audit Office at all." A long-term Treasury officer, who I will not name, then put another view and you say that he suggested that the email was a very clear indication that the NSW Audit Office appear to view this is the year to tell the truth on TAHE", or similar words.

Mr LYON: Yes.

The Hon. JOHN GRAHAM: He further ventured a view that not responding would likely see rapid action by the NSW Audit Office to reclassify or qualify the State's accounts. How concerned were they in your interactions?

Mr LYON: There was a huge degree of concern, particularly amongst Transport officials who had to sign off and attest to the bona fides of the accounts. I do not think any of the finance staff at Transport for NSW would like to have the Transport accounts qualified. It was a huge issue of reputation for finance colleagues and so it was obviously a very real issue for them. For the Treasury office it is much more a real issue because I assume that it will be career defining—a bit like TAHE has been career defining for me in my relationship with KPMG. I suspect that some Treasury officers might find it career defining for them under inquiry.

The Hon. JOHN GRAHAM: You referred to the Transport accounts; as your note at the time recalls, it was not about the Transport accounts but actually about reclassifying or qualifying the State's accounts altogether.

Mr LYON: That is right.

The Hon. JOHN GRAHAM: I might finally just ask you about document 132. I think your view about Mr Staples and the Committee putting any questions they have got to him directly is a very sensible one, so I do not want to encourage you to comment on this at all, but I do want to draw your attention to document 132 on Thursday 10 September 2020 where you recalled a call from Rodd Staples. In one dot point you recall him saying, "warned me that TAHE and particularly the most exposed Treasury official are starting to play the man on him and on me."

Mr LYON: That is correct. That started really from April or May, and again, at and by and for and on behalf of Mr Pratt and particularly by Cassandra Wilkinson and San Midha. Again, I have never seen behaviours out of officials like I have out of those three. And Mr Staples definitely warned me in a discussion that they were beginning to really go after me personally.

The Hon. JOHN GRAHAM: I might just note that that document 49 was produced on Saturday 25 July 2020.

The CHAIR: And the reference to the "TAHE Mr Hit Squad" is 10 September 2020.

Mr LYON: When I said the "TAHE Mr Hit Squad", what I meant was effectively Mr Hunter, Ms Watson as well as the three Treasury officials and, as it turned out, almost everybody else in KPMG.

The Hon. PETER POULOS: I just have a point of clarification on that document.

The CHAIR: Go.

The Hon. DANIEL MOOKHEY: My colleague took you to the conversation with Mr Staples, but there is a report here of a conversation with Mr Peter Perdikos, at the bottom. Do you see that?

Mr LYON: Yes.

The Hon. TREVOR KHAN: And this is 132.

The Hon. DANIEL MOOKHEY: It is 132. It says, "Noted that I am being targeted by all the guilty parties again like last time. Rang to make sure I was okay."

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: So you had a conversation with Mr Perdikos?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And he said to you that you were being targeted again?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Did he say anything else?

Mr LYON: I think that followed a meeting where I was basically yelled at, spoken over, humiliated. I mean, that happened every single week; every meeting we had with Treasury that happened, but that was a particularly bad one and Ms Cassandra Wilkinson—I understand Fiona Trussell rang her afterwards and expressed to her how inappropriate her behaviour was. And there were many times when Peter or Fiona or Rodd would check in again because of their visibility of both the internal retributions and recriminations that were occurring and their sorrow over the targeting of me by Treasury officials. So again, it is worth asking them about it. But it was quite a concerted campaign. Again, I guess it is sheep stations when you are talking about tens of billions of dollars on the budget, but it did make for a very involved period.

The CHAIR: Mr Lyon, I think that is an underestimation. Could I ask you about the document at 140? At the bottom of that document you will see on 11 September last year—again, just prior to this series of missives coming to you from Mr Pratt—Mr Perdikos from Transport for NSW provides you with a PricewaterhouseCoopers [PwC] advice that Transport had got earlier this year.

Mr LYON: Yes.

The CHAIR: That made it clear that you were not on an island in raising these concerns. Do you want to tell the Committee about the PwC advice?

Mr LYON: Yes. I mean, the PwC advice was, I think, a very straightforward piece of work. It looked at the relevant accounting rules and it said that there is no way that TAHE on its current basis could work. And, a little bit like my initial report, it said really if you are going to get to that you are going to have to make it into a real corporation. That is not going to be rail, it is going to have to be all your assets, otherwise you are putting breaks in. So basically they said you either corporatise your transport department and set it free—and by "set it free" that means it decides what gets built, not Cabinet, not anybody else; it is a corporation and it decides what gets built. That is obviously a very big change. It has some good precedent—certainly the New Zealand Transit Authority for a time had a direct allocation of the Crown road tax to it, so that it made decisions as an independent corporation with a revenue base and all of the rest. But I think it is probably a pretty big step that we have not really done the preparation for and, as a result, PwC resolved the next best option was to close TAHE because it does not work.

The CHAIR: And, in fact, the TAHE model is kind of neither fish nor fowl. It holds all the assets of the rail, it does not hold the balance of transport assets, it is subject to the direction of the Government on major infrastructure and really does not have an independence on how it gets income stream either.

Mr LYON: The way I think about it is if it actually works for accounting rule purposes then it definitely does not work for safety.

The CHAIR: Do you want to expand on that a little?

Mr LYON: If TAHE actually has control over its assets, if it actually can make free choices, if it can actually decide the level of maintenance that gets spent on country rail versus everywhere else, for example, you are going to see different decisions made because it is not a profitable entity; it is there to provide a service that you cannot internalise the costs for. So I guess it raises that inherent challenge where if it works for the accounting rules where it has to make and visibly be able to make all of the decisions and all of the control, the experience would suggest you will see a hollowing out of the assets because it is trying to make a commercial return in an unprofitable environment, and you also put in the breaks—"break" is the wrong word—you fracture the accountability of the people who are operating the network and know what is needed and when and can manage the maintenance spend to keep it all safe and all of the rest, noting it is always underfunded.

When you give it to a bunch of people however well intentioned, who are not driving the trains, not operating the track—indeed, one of the bigger problems is not even from the rail sector, in large part; you have a misalignment and you have a misalignment of drivers because the corporation is going to be asked about how it has performed and how it has made its returns and all of the rest, and in making those decisions the experience is the assets get hollowed out, accountabilities get broken down. Noting that I was accused various times of using emotive or overly emotive language, I started referring to the consequence of it being an unscheduled overlap of

the kinetic envelope of two trains. What I in fact meant is that if you run the asset down and if you break the accountabilities, the experience in Australia and elsewhere has been that you have rail tragedies.

The Hon. DANIEL MOOKHEY: Can I just follow that?

The CHAIR: I will go to Ms Boyd and then come back to you, unless it is directly on that point.

The Hon. DANIEL MOOKHEY: It is directly.

The CHAIR: Then for clarification and then straight to Ms Boyd.

The Hon. DANIEL MOOKHEY: Just to clarify, when you talk about the fracture of the responsibility, it is your knowledge, is it not, that after Waterfall the royal commission or the commission of inquiry recommended that the two be merged.

Mr LYON: One hundred per cent, yes.

The Hon. DANIEL MOOKHEY: And that structure prevailed from then onwards until TAHE was formed.

Mr LYON: That is right. That is absolutely 100 per cent the finding of McInerney's review: it was that the accountabilities were broken once the rail system was fractured. It was done for a more honourable reason than hiding depreciation; it was a genuine attempt, I think, to get disciplines into the former State Rail Authority. Nonetheless, again, if you look at those thousands of tasks that we had to colour in boxes next to, there are a lot of things that happen on rail and if a couple of them get forgotten or they fall between the cracks, then you can get some pretty tragic outcomes as a result. Again, that is what has been driving the transport officers the entire way through: their focus on safety and no-one wanting to be the person who agreed to bring back the pre-Waterfall structure once again.

The CHAIR: Mr Lyon, could I ask your indulgence if possible to stay until quarter past 12? We were a little late starting.

Mr LYON: Yes.

The CHAIR: If that is amenable to the Committee.

The Hon. TREVOR KHAN: It seems fair.

The CHAIR: Ms Boyd.

Ms ABIGAIL BOYD: Thank you, Chair. Mr Lyon, I just wanted to round out a few issues so that we do not need to call you again, I guess. I just wanted to check your background.

Mr LYON: We have only just met, but I often have that impact on people.

Ms ABIGAIL BOYD: I understand that you started at KPMG in 2018. Is that correct?

Mr LYON: Yes.

Ms ABIGAIL BOYD: And before that you were at Infrastructure Partnerships Australia for a considerable period.

Mr LYON: Yes, about 13 years.

Ms ABIGAIL BOYD: Were you doing accounting work during that time or was that infrastructure and projects work?

Mr LYON: It was infrastructure policy, but a huge amount of infrastructure policy is focused on financing structures, both good and bad—noting again, and you would be aware of this from some of your career by the sound of it, there are very large capital items that are getting built and so on.

Ms ABIGAIL BOYD: And you were also part of the Transport for NSW board at one point. Is that right?

Mr LYON: I was, yes.

Ms ABIGAIL BOYD: How long was that for?

Mr LYON: For the entirety of its existence, which was about 2½ years or something, three years.

Ms ABIGAIL BOYD: So when you joined KPMG you did take—I do not know if you took Transport for NSW as a client, but you at least had an established relationship with Transport for NSW at that time.

Mr LYON: Very much. I guess the point I would make, Ms Boyd, is every single human that is involved in TAHE is someone I have known for a long period of time, with the exception of Mike Pratt and James Hunter, neither of whom I had heard of until I joined KPMG and Mr Pratt joined Treasury. I have known the former DPC secretary for, I do not know how long, since he was a director at Deloitte, so maybe 20 years. I have known the current CEO who has joined TAHE, I have known her for 15 years. I mean, the stupidity, in my view, of what KPMG did was get into the middle of what is effectively a family fight between two departments and not have the maturity or the risk awareness to understand the difference between providing professional advice and dancing around the Cabinet table and playing games.

Ultimately, as the point was made before, I think they have served their client very badly and I think that Treasury itself has served the Cabinet very badly because we are where we are, where I am turning up under compulsion when I am trying to set up a new business and all of the rest, and where I do not have my old job anymore because of all of this. So TAHE is a bit of a toxic entity; it has got toxic people that sit around it and it has certainly got some toxic consequences that are driving a lot of the behaviours that we have seen around it. I think it is a good old-fashioned stuff-up and then it has been followed by a pretty awful conspiracy to try to make it true.

Ms ABIGAIL BOYD: Just one final question from me because I have not been able to get a straight answer. Actually, I have got an answer, but I am not sure that it is the correct one, from various government officials. The question is whether the structure of TAHE could impact on the credit ratings of the State. Basically would there be a risk—

Mr LYON: Of a downgrade?

Ms ABIGAIL BOYD: —to our credit rating, yes?

Mr LYON: In my experience, Ms Boyd, and again I am not an accountant, I am not a rating agency guy or anything else, but I am reasonably familiar with what they do. You might remember the wrapped bonds and covered bonds and all that stuff that used to go on. The reality is that about 60 per cent of the metrics that are used are non-quant; they are qualitative, they are about the degree to which they believe the fiscal settings and policies and all of the rest. So I think Mr Midha is right when he says he cannot exactly tell you whether it is going to impact the rating or not. My view would be that the rating agencies have probably not accepted TAHE's legitimacy as a for-profit corporation from the start, and probably on the State's ratings they see through it and it is included on the liabilities, would be my guess. But if you rang Standard & Poor's I am sure they would be able to tell you. But they do not just reflect the accounting structures or the columns that Mr Pratt has written things down in. They do—and particularly since the Monoline triple-A wraps and all of that stuff—have a bit more of a focus on looking through the structures that sit there.

The other reality is, all of this was done really about trying to protect the triple-A and meet the Fiscal Responsibility Act and all of the rest. It is kind of a little bit like Treasury is the Japanese soldier they found in the seventies in the Philippines still fighting the Second World War: we do not have a triple-A credit rating anymore, that has been lost; it is probably time to bring TAHE to book, and certainly it sounds like Audit are trying to do it, but yes, I guess that would be my response. I cannot give you a clear answer either, but if you rang Standard & Poor's they will tell you. My suspicion is that they have never counted this as a legitimate for-profit corporation.

Ms ABIGAIL BOYD: Very helpful. Thank you.

The CHAIR: Mr Farlow and then Mr Mookhey.

The Hon. SCOTT FARLOW: Thank you very much, Mr Chair. Mr Lyon, in the original brief you got from Transport, in the report that you were supposed to provide for Transport, did that ever go into seeking for you to undertake a fiscal impact study or the like? How did that then become part of the report that was commissioned?

Mr LYON: It required us to model. So we did not have to do a financial impact statement; that is something Treasury does to go with Cabinet stuff. Cabinet definitely required us to develop an operating model and to subject it to detailed financial modelling because we identified in our first report the errors and the limitations of the existing Treasury model that had been used. So Mr Pratt is being quite cute when he says that it is not within scope. It was most definitely within scope and, if you look, I have included the scope within my papers: I have included it where I have circulated it to people inside KPMG; it is covered in the letter that Mr Heathcote wrote back to Mr Pratt in November. We were required, because of the limitations in Treasury's financial analysis up to that point, to build a detailed and sophisticated financial model that was able to tell Transport, Treasury and Cabinet the impacts of implementing TAHE as it is designed.

The CHAIR: I am going to go to Mr Khan, but then I want to go to Mr Mookhey.

The Hon. TREVOR KHAN: I do not want to take your time. What I am interested in is this: this is the Public Accountability Committee and I know TAHE is the direct point of interest for a whole series of reasons, but what I am interested in is, in a sense, what lessons can be learned, partly picking up from what Ms Boyd has said to you already. In a government sense, what should government expect from bodies such as KPMG when retaining them to do work?

Mr LYON: I think they should be using them as an extension of expertise rather than a bandaid to put over a weeping wound.

The Hon. TREVOR KHAN: I accept that. It seems to me—picking up from what you said before at my invitation, that is, that KPMG let down, essentially, the Government of New South Wales by playing both ends off—how does the Government from its side, as well as KPMG from their side, ensure that we do not replicate this time and again?

Mr LYON: I guess there are probably two things. I think back to some of the great Treasury secretaries that I have dealt with—and I have dealt with New South Wales, Commonwealth and Victorian Treasury for more than 20 years—there have been some amazing leaders in that time. Part of the basic governance structure of parliamentary democracy is that you have talented amateurs in a sort of professional sense as your Ministers, and then you could argue about how talented they are—I will leave that to you.

The CHAIR: We cannot resolve that.

Mr LYON: But you are supported by a professional public service that understands the risks and also understands the ethics of what needs to happen. I suspect to some degree Mr Pratt might come from a mid-level role in one of the big banks or something like that. I do not think he is an economist; you might want to ask him his professional qualifications. I do not think he is a finance guy either. But I think probably this reflects to some degree the lack of rigour in the Treasury. It should not be a surprise to them that there is this huge problem in the budget; they should know it. It should not be a surprise to them that there are accounting problems with making TAHE work. I mean all of these things should have been known. So to some degree it is—and again I am not seeking to denigrate all of the hardworking officials in Treasury, but certainly Mr Pratt, Mr Midha and Ms Wilkinson have let the Government down, and I think KPMG is probably a good reflection of this issue that comes up every now and again of the tension between being an accounting firm and the reality of being actually a Swiss Army knife consulting firm that does all sorts of things.

Probably the difficulty in this one for KPMG is that it is in their home patch of accounting. I think they have given advice—and certainly you would have to be brave to contradict two other big-four firms who were obviously equally under pressure to come back with an answer that worked. I guess KPMG just did not have the internal structures or the strength or whatever else. I think it has been an example of a Treasury leadership that has forgotten how to advise leaders on when things can happen and when they cannot. I think they have probably lost the ability to say no, that is not going to work, or to say it in a way where the Cabinet listens to it. But, in truth, this should never have been done at the start. Once it is baked—

The Hon. TREVOR KHAN: Well, I will ask—

The CHAIR: Sorry, Trevor, we have got a very short amount of time.

Mr LYON: Just let me finish for one second. Once something of that scale is baked into the budget, it gets very hard to tell the truth about it because all of a sudden things are very different, you have been making all these decisions. So I have always been sceptical—and Ms Boyd asked before about my background in accounting structures—I have always been sceptical of accounting-led financing models for infrastructure because they are usually about trying to hide costs and not about trying to fund them and pay them. I think this whole exercise is a regrettable one. Once it went into the budget, the lie—or the fiction, or however you want to express it—became too big for people to easily get off, and I think Mr Pratt was unable or unwilling or did not understand the risk that he was putting the Government in by doing it, and I think KPMG has really forgotten the purpose of the public service and the purpose of consultant advisers and probably tried to be a little bit too entrepreneurial in providing answers.

The Hon. TREVOR KHAN: I have used up my time. I did have another question.

The CHAIR: Mr Mookhey.

The Hon. DANIEL MOOKHEY: Mr Lyon, I want to take you now, in laymen's terms, to the basic differences as to why you said that this would actually have a net impact over the forward estimates of minus

\$5.3 billion and Treasury said it would actually have over \$4.7 billion. I am referring to your report. I do not know if you have got a copy with you.

Mr LYON: Unfortunately, I forgot my report.

The Hon. DANIEL MOOKHEY: While I am asking you the question I will table these for the Chair. The last question, or one of the last questions, will come from it. I have got three copies so we can follow—one for the witness, one for the Chair and one for the Government. I am sure you might recall this from memory, but you set out the differences in assumptions which lead you to conclude that it is going to have a negative impact of \$5.3 billion on pages 63 to 66. Let me go very quickly on this to start. As a matter of law, a State-owned corporation must return a profit for the taxpayer. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: That is termed a return on equity. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: There is a specific accounting definition as to what a return on equity is. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Basically, it is income earned, and a very simple term, over the size of the asset base. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: In addition, TAHE is required to recover all its costs under its classification. Correct?

Mr LYON: Yes, it has classified itself as a for-profit corporation.

The Hon. DANIEL MOOKHEY: That includes depreciation. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Then in terms of what it charges its customers, it has to charge its customers what is called an economically significant price. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: That means it has to recover its costs. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And enough profits to earn a return on its asset base. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And that is all legal. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And TAHE must satisfy every one of those hurdles in order to obtain its classification as off-book. Correct?

Mr LYON: Yes, or to sustain it.

The Hon. DANIEL MOOKHEY: Yes. And in truth, the advice that you were being asked to provide was what exactly is the economic return it is required to earn, amongst other things. Correct?

Mr LYON: In part, yes.

The Hon. DANIEL MOOKHEY: And you set out between pages 63 and 66, broadly speaking, your answer to that question. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: That the core of this difference, where this whole dispute comes down to, is you say that in order to calculate its profit as well as what it should charge Sydney Trains and NSW Trains, it should be using all its asset base. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: That is \$37.9 billion at the time you wrote the report.

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: That is set out on page 66 for people who are following. Treasury says that actually they only need to earn a return on \$10.8 billion. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Did they ever give you an explanation as to why they think \$10.8 billion?

Mr LYON: They certainly tried. The argument they put, Mr Mookhey, is that they are only required to earn a return on the equity they had contributed since 2015, which is not true.

The Hon. DANIEL MOOKHEY: Just on that point, to speed this up, that is not a practice that prevails at any other State-owned corporation. Correct?

Mr LYON: Nothing I have seen in the Western world does that.

The Hon. DANIEL MOOKHEY: In fact, Sydney Water—which you go on in your report to say is the closest parallel in terms of the size of the organisation, despite TAHE being, I think, four or five times the size of Sydney Water—Sydney Water calculates it over all its asset base. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Not the contributed equity?

Mr LYON: No.

The Hon. DANIEL MOOKHEY: There is no other example in the public sector as it currently stands in respect to any of the other State-owned corporations in which that definition is used. Correct?

Mr LYON: None.

The Hon. DANIEL MOOKHEY: Great. Thank you. The other aspect is what profit has to be earned. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: That is the other point of difference. You said that it was acceptable for TAHE to earn a 1 to 3 per cent return on its assets between 2023 and 2027. Correct? And then 4 per cent onwards.

Mr LYON: We did that, Mr Mookhey, not because we think that is the best—in fact, I think TAHE would actually perform worse—we were just trying to be as polite as we could and we were trying to not bring home a \$10 billion dead cat, I guess.

The Hon. DANIEL MOOKHEY: You gave a very generous—

Mr LYON: Set of assumptions, yes.

The Hon. DANIEL MOOKHEY: —set of assumptions yourself. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: But Treasury disagreed with you that that 1 to 3 per cent between 2023 and 2027 and 4 per cent onwards was acceptable. They disagreed. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: They said that you should have instead been using a flat 1.31 per cent rate—

Mr LYON: Forever.

The Hon. DANIEL MOOKHEY: —starting from financial year 2025 continuously. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Indefinitely.

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And that is because 1.31 per cent was, at the time, the 10-year bond rate?

Mr LYON: That is right.

The Hon. DANIEL MOOKHEY: So Treasury was saying to you that it was only important to them that it recover at that time the cost of the capital, regardless of inflation. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Once you factor in inflation, Treasury was actually saying to you that it was okay for TAHE to lose money?

Mr LYON: Yes. They were setting out to lose money, yes.

The Hon. DANIEL MOOKHEY: Just on a final question—

The Hon. TREVOR KHAN: Sorry, I do not want you to rush—

The Hon. DANIEL MOOKHEY: We were going fast.

The Hon. TREVOR KHAN: But I am concerned that Mr Lyon may have been going to add something.

The Hon. DANIEL MOOKHEY: Is there anything you would like to add to that?

Mr LYON: No, that is fine. Thank you Mr Khan.

The Hon. DANIEL MOOKHEY: Let me be very clear as I want to ask you the next question on this. In order for Treasury to make this work one of two things has to happen. Either it has to have TAHE accept the definition as to what amount taxpayers invested in them, which is around \$10 billion, correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Alternatively it has to have Treasury mark down the value of its assets. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And if they were to instruct either of those two things that would achieve the result that they desired to achieve. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Despite that not having any precedent that you are aware of?

Mr LYON: Yes.

The CHAIR: Mr Lyon, there were repeated efforts to try to have the asset base written down by 50 per cent.

Mr LYON: What we actually revealed in the work was that all of Treasury's advice to the Government before—which was actually done by KPMG which you will see in the papers—was a model that for no defensible reason, as we note in the report, assumed that TAHE's assets were worth half of what they really were. The problem with that is you cannot pay a distribution of returns until you have funded your depreciation. So, in fact, TAHE became an enormous cash-trap. I think by the time we got to the end of the 10-year period it was holding \$12.5 billion of taxpayers' money that would have to be released through some form of special distribution that would unpick the bona fides of its independence.

The Hon. DANIEL MOOKHEY: Before we go too far I have one more question that has just arisen. I just tabled a letter that you probably have not seen. I will only ask—

Mr LYON: I should say I know David Jurd too. I have also known him for 20 years.

The Hon. DANIEL MOOKHEY: I will ask for your response to this as an expert or as the person who produced the model, and in no other capacity. As we established, in 2020, at the time you wrote the report, Treasury was telling you that you should be calculating the equity at \$10.8 billion?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And you had rejected that proposition and that created the dispute. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: And that was the major part of the dispute?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Will you now look at this statement of expectation that then Minister Constance sent to the chief executive officer of TAHE as of 9 June 2021, which is six months after you have left KPMG. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: To the best of your knowledge this is what a portfolio Minister is required to produce under the statement of commercial intent every year. Correct?

Mr LYON: TAHE is a three-headed monster because the transport Minister is its portfolio Minister, but they changed it from the transport Minister being a shareholding Minister. So I think this is separate. I think there is a statement of corporate expectations that has to go from the shareholders and then there is a statement of expectations that goes from the portfolio ministries, as I understand it.

The Hon. DANIEL MOOKHEY: Yes, I think that is absolutely accurate because the letter then says, "Portfolio Minister priorities", on the front page. And then on the back page he cc's it to the Hon. Dominic Perrottet, Treasurer, and the Hon. Damien Tudehope, the finance Minister as well.

The CHAIR: The shareholders.

The Hon. DANIEL MOOKHEY: These were the shareholder Ministers. Correct?

Mr LYON: Yes.

The Hon. DANIEL MOOKHEY: Then the last dot point says, "Therefore, I provide to you guidance. The State's current equity investment in TAHE is projected to be approximately \$7 billion at 1 July 2021. Capital grants prior to corporatisation in 2015-16 to RailCorp do not constitute equity for the purposes of calculating government's return on investment." Do you see that?

Mr LYON: I do see that.

The Hon. DANIEL MOOKHEY: Is that not a direction from the then Minister to endorse effectively the set of assumptions that your report rejected?

Mr LYON: It appears to be precisely that.

The Hon. DANIEL MOOKHEY: But the variation is not the \$10.8 billion. It has been written down already. From what Treasury told you late last year that was \$10.8 billion to \$7 billion? Is that correct?

Mr LYON: Yes, it appears that he is wanting the \$7 billion to be the denominator for the calculation of return on equity.

The Hon. DANIEL MOOKHEY: That would allow them to achieve their result of avoiding the two impacts we discussed earlier. Correct?

Mr LYON: It would but only if audit—

The Hon. DANIEL MOOKHEY: If the Auditor-General agrees?

Mr LYON: —accepted such a novel construct.

The Hon. DANIEL MOOKHEY: My last question on this is: In the course of you producing your report did you have any evidence to conclude that the State's investment in TAHE for the purposes of calculating a return on investment was \$7 billion?

Mr LYON: Absolutely none. We did reject it out of hand in quite a detailed case study.

The Hon. DANIEL MOOKHEY: The \$30 billion less than what you said it should be?

Mr LYON: Well, what it is. It is not us saying what it should be. I mean there are rules around this, around the basis of valuation. Again, it is probably something to explore with the Auditor-General or with Transport at some point. But this is the real problem for Treasury. There are rules around asset valuation. It has been valued on a cost approach up until now. We did have a look at an income approach which would be an opportunity to revalue but we had to remove that from the model under instruction from Treasury because it actually showed that the value of the corporation would go up under an income approach and we were instructed to delete it entirely from the model, as I noted in my report.

The CHAIR: Mr Lyon. Thank you for your evidence today. On one hand it is very technical—asset valuations and fights over what the starting point is. But the heat and light in this case really comes down to the impact on the budget. If this all unravels it is a \$10 billion reversal on the budget. Is that right?

Mr LYON: Yes, or thereabouts. Again it depends where you measure it from but, yes, it is billions and billions and billions of dollars.

The CHAIR: On one view of it Treasury saw you and your team as what was standing in the way of that \$10 billion accountancy trick?

Mr LYON: Yes, that is correct.

The CHAIR: Thank you for your evidence today. Thank you for the frankness of the evidence.

The Hon. TREVOR KHAN: Even if it was compelled.

The CHAIR: [audio malfunction] people across the State. Thank you for the position you have taken. We genuinely appreciate it.

(The witness withdrew.)

(Luncheon adjournment)

BRUCE MORGAN, Chair, Transport Asset Holding Entity, sworn and examined

TREVOR BOURNE, Non-Executive Director, Transport Asset Holding Entity, sworn and examined

The CHAIR: Welcome to the next session of the Public Accountability Committee's inquiry into the Transport Asset Holding Entity which will be referred to as TAHE throughout this afternoon's deliberations. I welcome our next witnesses. You now have the opportunity, if you wish to take it, to make a brief opening statement.

Mr MORGAN: Thank you for the opportunity to appear before you today. I was appointed Chair of TAHE on 1 July 2020. Like my fellow directors, I took this role because I fundamentally believe in what TAHE was established to deliver. Each of us is excited to be a part of the board of TAHE and the opportunity it presents to unlock value in the State's assets, accelerate precinct development and generate sustainable revenue streams for the benefit of the New South Wales taxpayer and the community.

I have more than 45 years' experience working across accounting, corporate governance and business transformation across various sectors and more than 15 years as a non-executive director of public, private sector and not-for-profit organisations, including as chairman. My directorship experience includes companies such as Origin Energy and Caltex Australia, now Ampol. I have recently completed eight years as chair of Sydney Water. My role at Sydney Water, in particular, has afforded me the opportunity of seeing firsthand the expertise and value that State-owned corporations [SOCs] can deliver in essential services.

I believe my professional experience and board roles, including six years as chair of PricewaterhouseCoopers [PwC] in Australia, have provided me with the relevant skills and experience to guide and support TAHE as it operationalises and begins to create meaningful and long-term value for the people of New South Wales. The formation of TAHE is a significant reform for our transport system. It involves establishing a new organisation, transferring the majority of RailCorp's assets across, establishing the detailed arrangements with operators and other organisations, setting up financial structures, policies and processes that enable the organisation to function appropriately and, finally, ensuring the organisation is appropriately resourced.

Given the significant nature of this transformation, our first year or so in operation has inevitably been a year of transition. I acknowledge that in a complex transition of this nature, and given the broad group of stakeholders and agencies involved, not everything will be absolutely 100 per cent right from day one. We continue to actively monitor opportunities to make improvements and to implement them rapidly. Yet the board and management are firmly focused on delivering the clear benefits of TAHE for New South Wales taxpayers and commuters.

These include: maximising the value of our high-quality transport asset portfolio and developing economy-enhancing precincts for commuters and the State more broadly; freeing up Transport for NSW to focus on strategy, and rail operators to focus on providing better outcomes for public transport users and the New South Wales taxpayer; enhancing the safety governance framework by providing an additional line of assurance—and I will shortly ask my fellow director, Trevor Bourne, to say a few words on that issue; and applying an independent approach to asset management, building transparency and accountability, while maintaining a focus on financial discipline. Importantly, we are not involved in running the trains. As appropriate, the operators continue to manage the day-to-day operation and safety. Thank you again. I will hand over to Mr Trevor Bourne.

Mr BOURNE: Thank you to the Committee for the opportunity to make a brief opening statement. Like Mr Morgan, I was appointed to TAHE's independent board on 1 July 2020. I have spent the bulk of my career in large, complex, capital-intensive industries at senior management and chief executive level, across the manufacturing utilities energy, engineering and large-scale project management sector. Over the course of my career, I have worked in industries that involve complex and hazardous working environments. These included senior executive roles at BHP, the chemical firm Incitec Pivot and then a long career at Brambles, as well as non-executive directorships at public and private companies including Virgin Australia, Caltex which is now Ampol, Origin Energy, Senex Energy and one of the New South Wales Government's largest State-owned corporations, Sydney Water.

On just about every board that I have served on I have chaired the safety and risk committee, other than for the two boards where I am actually the company's chairman. You would appreciate in each of these businesses safety and risk management has remained a consistent and strong focus for me. At TAHE I chair the board's Asset, Safety and Environment Committee. I have no hesitation in saying to this Committee that TAHE's approach to safety is robust and builds on the pre-existing governance arrangements. All decisions around the maintenance and safety of TAHE's assets are subject to the same rigorous asset and safety standards that existed prior to July 2020.

In addition to this baseline, TAHE has legislated obligations to oversee and assure itself that New South Wales rail assets and infrastructure are safe, reliable and fit for purpose to deliver safe passenger and freight services. From my experience TAHE's approach to safety is best practice and comprehensive. It includes the board's subcommittee which I chair. The subcommittee has an independent member with deep technical expertise and experience in overseeing the safe operation, maintenance and management of heavy rail assets and infrastructure. We have a program of independent safety and asset audits underway. This year the international engineering firm WSP is executing our 2021-2022 audit program which has been endorsed by the board. We have established and are now currently implementing TAHE's asset management and assurance framework.

Safety and, more specifically our commitment to zero material safety incidents, is our leading non-financial performance indicator. We have established a set of asset and safety performance measures that the board and subcommittee review and monitor. Finally, there continues to be oversight by the independent Office of the National Rail Safety Regulator, who has oversight of all rail safety regulatory arrangements. But as noted by Mr Morgan, TAHE does not control the day-to-day operations of New South Wales rail assets. This continues to be the remit of Transport for NSW, Sydney Trains, NSW Trains and private operators. Our responsibility as asset manager is to assure ourselves that these organisations are complying with safety and maintenance requirements to make certain the New South Wales rail network is safe, reliable and fit for purpose to deliver safe passenger and freight services. Thank you again and I look forward to our discussion this afternoon.

The CHAIR: I will hand over to Mr Mookhey to commence the questions.

The Hon. DANIEL MOOKHEY: Thank you Mr Morgan and Mr Bourne for your attendance today. If you are in a position to table a written copy of your opening statements that might assist some of the questioning as well, if that is possible.

Mr MORGAN: Certainly.

The Hon. DANIEL MOOKHEY: Mr Morgan, you have been chair of TAHE since its commencement from 1 July 2020?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: As part of being chair you are required to produce an annual report. That is correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: And that obligation arises from both section 23 of the State Owned Corporations Act as well as the annual reports Act, I presume. Is that correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: You made such an annual report for the half-year period which covered as of 31 December 2020. Is that correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: And you signed that 29 January 2021?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: And that only covered six months because that was the only relevant part of operations that were in that period. Correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: When you signed that statement I presume you had a look at the report and it was correct at the time that you signed it?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: I presume that all appropriate policies around reporting your assets and income were followed in accordance with Treasury guidelines, to the best of your knowledge?

Mr MORGAN: To the best of my knowledge and recognising that it was in transition.

The Hon. DANIEL MOOKHEY: Yes, and that is fair. Your annual report does not include a certification from the auditor. I am assuming that arises because the auditor does not need to audit it under the State Owned Corporations Act?

Mr MORGAN: At the half-year.

The Hon. DANIEL MOOKHEY: At the half-year but he is required to do so at the full year. Is that correct? Have you completed this year's report?

Mr MORGAN: This year's report is not completed.

The Hon. DANIEL MOOKHEY: Okay, we will get to that. By any chance do you have a copy of that annual report for last year?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: I am sorry, I might just ask you these questions and provide you with my copy so you can follow it along. Is it correct that as of the date that you signed the statement of financial position as of 31 December 2020, TAHE has total assets of \$41,336,662,000 and total liabilities of approximately \$3 billion which means that its total net assets were \$38,000,265,020. Is that correct?

Mr MORGAN: You have got the report; I have not got the report in front of me.

The Hon. DANIEL MOOKHEY: Sure, but that sounds about right in terms of the assets?

Mr MORGAN: I presume so.

The Hon. DANIEL MOOKHEY: What is its current net assets position?

Mr MORGAN: Current net asset position has not been finalised because the audit of TAHE's accounts are not complete.

The Hon. DANIEL MOOKHEY: In the intervening period from this report to now, have the assets been revised upwards or downwards to the best of your knowledge—from TAHE's perspective not the Auditor-General's?

Mr MORGAN: They will be revised downwards.

The Hon. DANIEL MOOKHEY: To what?

Mr MORGAN: On the number that has not been settled because the Auditor-General is looking into a number of matters not yet concluded. It would be inappropriate for me to land on a number until that work is complete.

The Hon. DANIEL MOOKHEY: You have provided your report to the Auditor-General for inspection. Is that correct?

Mr MORGAN: Sorry, the draft account.

The Hon. DANIEL MOOKHEY: You have provided your annual report or the statement of financial position to the Auditor-General for inspection. Correct?

Mr MORGAN: In respect of 30 June 2021?

The Hon. DANIEL MOOKHEY: Yes.

Mr MORGAN: Draft accounts would be with the Auditor-General,

The Hon. DANIEL MOOKHEY: And that was provided by TAHE. Correct?

Mr MORGAN: In the normal course of the audit, correct.

The Hon. DANIEL MOOKHEY: Did you see those draft accounts?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Did you certify that those accounts were accurate to the point where you could provide them to the Auditor-General for her inspection?

Mr MORGAN: I was satisfied with being able to provide draft accounts to the Auditor-General.

The Hon. DANIEL MOOKHEY: Okay. I am going to ask you now only about the draft accounts, not the Auditor-General's opinion of them. You said that there has been downward revision?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: In the accounts that you provided to the Auditor-General there was a downward revision. Did I hear you correctly?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: What was the downward revision in the accounts you provided the Auditor-General?

Mr MORGAN: I would have to come back to you and take the question on notice because I do not have the draft accounts in front of me.

The Hon. DANIEL MOOKHEY: Would you term it as a significant revision downwards?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: A revision as in more than \$5 billion down?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: More than \$10 billion down?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Close to \$20 billion down?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: More than \$20 billion down?

Mr MORGAN: Well, not yet settled.

The Hon. DANIEL MOOKHEY: So somehow in the six months between 31 December 2020 and 30 June 2021, TAHE's assets are written down by up to \$20 billion. Is that correct?

Mr MORGAN: In the draft accounts, correct.

The CHAIR: Sorry Mr Morgan, I cannot think of another occasion where a State-owned corporation has written down their accounts by some \$20 billion in the course of a financial year. That must be a red flag issue for you as chair of the board.

Mr MORGAN: Chair, it is not a red flag issue; it is as a result of adopting the accounting policies which have to be adopted for a State-owned corporation. At our first board meeting when TAHE was formed we agreed to continue with the depreciated optimised replacement cost valuation method used within government agencies, knowing that as a standalone State-owned corporation, in keeping with all other State-owned corporations and companies operating independently in that way, we would have to move to an income-based valuation. That is the reason for the adjustment and there has been an activity gone on to determine what the valuation should be under that income-based valuation in accordance with the appropriate accounting standard 116.

The CHAIR: So by reason of moving the assets from within a government agency to within a State-owned corporation that has led to a halving of the value of the assets on the books within 12 months? Is that your position, Mr Morgan?

Mr MORGAN: Moving to a State-owned corporation requires—and the Auditor-General will confirm this—a different set of accounting principles to be applied. The writedown is a non-cash writedown. So it is a writedown from one method of accounting, appropriately used in its previous circumstance, to the appropriate method of accounting today.

The CHAIR: So because the value to the State-owned corporation is simply the return that the assets can provide, as opposed to the value for the public, the travelling public and the State of New South Wales, because you are required to value it only on the financial return that is why it has halved in value going into TAHE? Is that right?

Mr MORGAN: I am required to value those assets on the basis of the income streams into the future discounted that those assets generate.

The CHAIR: So that is yes, is it not, Mr Morgan to my question?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Mr Morgan, the circulatory of that logic—and tell me if I am wrong—is that you are valuing the assets on an income approach but you are determining the income you will earn according to the value of the assets. Correct?

Mr MORGAN: The income that is earned by TAHE has regard to a return rate on the equity injections that have been made into TAHE.

The Hon. DANIEL MOOKHEY: So, yes. Correct, is it not? The income that you earned—

Mr MORGAN: That is what we were determining it, plus—yes, essentially that is right.

The Hon. DANIEL MOOKHEY: So we are in a circumstance where having written down the assets we have now written down the income which supports the decision to write down the assets. Is that a fair summation from a layman's perspective?

Mr MORGAN: The assets are determined at the level they are based on the income streams currently, and projected in the future.

The Hon. DANIEL MOOKHEY: I appreciate that. That certainly accords with my knowledge of it. In respect to the decision to adopt the income approach and, therefore, adopt that accounting standard that you made reference to, was your board directed to adopt that standard and that approach?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: Did you decide to do that yourself?

Mr MORGAN: For TAHE to comply with the requirements of the State Owned Corporations Act, and the accounting principles that apply to the Act, it is non-negotiable; it has to be done. At 31 December 2020 we were transitioning towards that outcome and we had adopted the cost method for that purpose because we did not have the information together at that point in time. Nor did we know at that point in time what the revenue streams would be associated with access and licence agreements.

The Hon. DANIEL MOOKHEY: Okay, I appreciate that—

Mr MORGAN: Sorry, just to be very clear on this: it is a not negotiable. We could not sit as a State-owned corporation under the Act in which it operates on the basis of the previous valuation methodology because the Auditor-General would qualify our audit opinion on that basis of not complying with an appropriate accounting standard.

The Hon. DANIEL MOOKHEY: Did you seek the advice of the Auditor-General before you made that change?

Mr MORGAN: The Auditor-General and our management team had been discussing this change throughout the year ended 2020-21.

The Hon. DANIEL MOOKHEY: Did you obtain any other independent advice from any other firm that supported the approach that the board took?

Mr MORGAN: We do not need any other independent advice. The answer is very clear.

The Hon. DANIEL MOOKHEY: Okay, I am not disputing, Mr Morgan, whether or not you needed it; I am asking you whether or not you did seek any advice from any accounting firm?

Mr MORGAN: I am not aware of any, but I can take that question on notice.

The Hon. DANIEL MOOKHEY: Okay, fair enough, I accept your evidence on that. I return to the annual report. You made the point, did you not, that you were adopting effectively the cost-based approach to valuation?

Mr MORGAN: Only at—

The Hon. DANIEL MOOKHEY: At 31 December 2020?

Mr MORGAN: Yes, because we were in the process of standing up this company and transitioning.

The Hon. DANIEL MOOKHEY: In the note you say, in what I determine is not one of the more clear sentences I have ever read, "TAHE has applied...". I am referring to page 16 of your annual report. I will read it to you.

Mr MORGAN: Sorry, the half-year report?

The Hon. DANIEL MOOKHEY: The half-year report. The annual report for the half year.

Mr MORGAN: It is not an annual report, it is a half-year report.

The Hon. DANIEL MOOKHEY: Okay, I accept that if that is how you choose to refer to it.

Mr MORGAN: I apologise.

The Hon. DANIEL MOOKHEY: On page 16 it reads, "TAHE has applied the modified retrospective transition option in accordance with NSW Treasury mandates." What does that mean?

Mr MORGAN: I will take the definition of that on notice but my understanding of it is that that means that it is a prospective valuation adjustment rather than going back into the past and adjusting prior sets of accounts which would be incorrect.

The Hon. DANIEL MOOKHEY: Okay, so TAHE has applied the modified retrospective transition options which actually means "prospective"?

Mr MORGAN: I will have to take that on notice to give you a precise definition of that.

The Hon. DANIEL MOOKHEY: Thank you very much. So your assets are now circa \$18 billion or thereabouts for the purposes of your draft report. Is that correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: I will table and wish to have provided to the witnesses the earlier letter that we provided to Mr Lyons—the statement of expectation. Mr Morgan, I will give you a minute to look at that if you want. Have you had a chance to look at that, Mr Morgan?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Have you seen that letter before?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: This was a letter that Mr Constance sent to Mr Jurd, the then executive officer at the time which is his statement of expectations effective 1 July 2021. Is that correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Presumably Mr Jurd reported this letter or provided a copy to the board?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Did the board consider the letter?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Did the board deliberate on any aspect of the letter?

Mr MORGAN: I do not recall having done so.

The Hon. DANIEL MOOKHEY: Mr Bourne, do you recall?

Mr BOURNE: I do not have the letter.

Mr MORGAN: I have a copy.

Mr BOURNE: It is a bit hard.

The Hon. DANIEL MOOKHEY: Forgive me, Mr Bourne. You do not recall any particular deliberations?

The CHAIR: The questions assume that correspondence like that is distributed to the board and is the subject of discussion in the board. Is that right or wrong?

Mr MORGAN: The statement of expectations has been under development for some time and, therefore, it had been discussed at the board and I am familiar with it from other places.

The Hon. DANIEL MOOKHEY: Fair enough—

Mr MORGAN: Just to clarify, the statement of expectations is a document that each State-owned corporation receives annually—and it is a relatively new development—from the portfolio Minister.

The Hon. DANIEL MOOKHEY: Indeed. Did you recall receiving any like statements of expectations from the shareholding Ministers, either collectively or separately?

Mr MORGAN: The statement of expectations is not designed to come from the shareholding Ministers; it is designed to come from the portfolio Minister, in my understanding.

The Hon. DANIEL MOOKHEY: That is my understanding too.

Mr MORGAN: So the answer is no.

The Hon. DANIEL MOOKHEY: Yes. To the extent to which, therefore, under the State-owned corporations framework, there is communication between the shareholders, the Government and your organisation, it is fair to say it is expected through this letter. Is that correct? That is fair.

Mr MORGAN: There will be other communications but this is a formal communication, along with the operating the licence from the portfolio Minister.

The Hon. DANIEL MOOKHEY: Just by the by, has Mr Constance at any time attended the meeting of the board or did he discuss attending the meeting of the board in which this letter was discussed?

Mr MORGAN: No, he has not but I have formal meetings with the relevant Minister on occasions throughout the year and this would have been raised at one of those more recent meetings.

The Hon. DANIEL MOOKHEY: One of the more recent meetings. On notice will you provide the Committee with when you think that may have taken place?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Thank you. Presumably you would have discussed the letter both prior to its transmission and after its receipt?

Mr MORGAN: The detail of it, not so. Perhaps the general intent, yes.

The Hon. DANIEL MOOKHEY: Acknowledgement of receipt perhaps was communicated as well?

Mr MORGAN: Yes, I would expect so.

The Hon. DANIEL MOOKHEY: Can we turn now to the last of the dot points in the letter? That is probably the best way of describing it. It reads, "Therefore, I provide to you guidance that the State's current equity investment in TAHE is projected to be approximately \$7 billion at 1 July 2021. Capital grants prior to corporatisation in 2015-16 to RailCorp do not constitute equity for the purposes of calculating government's return on investment." Do you see that?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Did you at any point discuss with the Minister, or anyone else in the Government, about whether or not \$7 billion was an appropriate number around which to calculate TAHE's return on investment?

Mr MORGAN: It is not discussed with the portfolio Minister; it is discussed with Treasury officials.

The Hon. DANIEL MOOKHEY: Which Treasury officials did you discuss it with?

Mr MORGAN: I cannot recall off the top of mind because the discussion about capital, and the appropriate level of capital, is an issue for Treasury, on behalf of the Treasurer and finance Ministers. And at a board level we accepted the outcome of those deliberations.

The Hon. DANIEL MOOKHEY: Was there one discussion with Treasury, two discussions, a series of discussions—

Mr MORGAN: Management and Treasury would have had discussions throughout a period of time, which I would not have been a part of, as Treasury would have worked this out. But it is clear from that statement, and my understanding, of course, the question of how the equity was to be built in TAHE and its predecessor, RailCorp, was established in 2016.

The Hon. DANIEL MOOKHEY: Yes, we will turn to that. But just on the dialogue, I accept that there was dialogue between your management and Treasury but I am asking specifically about you and Treasury. Did you have discussions with Treasury about this?

Mr MORGAN: I would have been in discussions—I do not know when—with Treasury officials. But this is driven by Treasury, not by TAHE, as an accounting policy.

The Hon. DANIEL MOOKHEY: Yes, I appreciate that Mr Morgan. I understand that Treasury ultimately has quite a say about this. I will refine who the officials are. Mr Philip Gardner is the Deputy Secretary responsible for the commercial division. Mr San Midha seems to be the official who was responsible for the development of TAHE and, of course, NSW Treasury Secretary Pratt clearly has been involved as well. Were the discussions you had with either all of them or one them?

Mr MORGAN: I cannot say for sure.

The Hon. DANIEL MOOKHEY: Did you have discussions directly with Mr Pratt about this?

Mr MORGAN: Specifically about the equity, no, I do not believe so.

The Hon. DANIEL MOOKHEY: In general terms?

Mr MORGAN: I do not believe so.

The Hon. DANIEL MOOKHEY: Did you or your management team—I will do this in two steps; I will first ask you and then the management team—raise questions about how Treasury arrived at the \$7 billion figure?

Mr MORGAN: It is clear how they arrived at the \$7 billion figure.

The Hon. DANIEL MOOKHEY: You never had any doubt about the \$7 billion?

Mr MORGAN: No, the capital structure of TAHE is designed within Treasury on behalf of the shareholder Ministers in the design of this organisation. We, as directors, were appointed on 1 July and our job was to pursue the objectives of this company on that basis. The capital structure and the \$7 billion was settled some time during that period.

The Hon. DANIEL MOOKHEY: Mr Morgan is it correct for me to infer that it is your view that that capital structure, as I think you put it, that gave rise to the \$7 billion figure that is referred to in this letter, is purely a matter for Treasury?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: And the board has no ability to dispute that? Is that fair?

Mr MORGAN: If I had a concern about it I could raise it and discuss it but I understand the basis on which it was struck. I understand the history and we moved forward.

The Hon. DANIEL MOOKHEY: Just around that part of the discussion, is it fair to say you trusted that Treasury was doing that in accordance with policy?

Mr MORGAN: "Trust" is not a word I would need to use in the circumstances. It was determined by Treasury. I was aware of the background to the number. That is the equity number we are starting with. It will grow and it will grow because there is a schedule of fixed assets that will be put in place in accordance with Transport for NSW's projection of the assets it requires in the portfolio for the next 10 years. And that number will grow quite substantially as Treasury issues further equity to underwrite Transport's program of works. So this number will not be a static number. It is sufficient to accommodate the company as it was established and it will grow quite significantly.

The Hon. DANIEL MOOKHEY: I accept that that is your expectation but again, to be clear, that \$7 billion figure that you accepted was derived purely as Treasury because that is their responsibility and not yours. Correct?

Mr MORGAN: Primarily.

The Hon. DANIEL MOOKHEY: TAHE and the board were involved in the preparation of a report by KPMG entitled "TAHE long-term operating model—

The CHAIR: Before we go off the—

The Hon. DANIEL MOOKHEY: I am not going off it. TAHE and the board were involved in a report undertaken by KPMG partner Brendan Lyon, commissioned by Transport for NSW, entitled "TAHE long-term operating model assessment." Is that correct?

Mr MORGAN: Correct. Sorry, not entirely correct. The management of TAHE was engaged by Mr Lyon as part of the discussions and the various discussions that were held along the way on that report with not only TAHE but with Treasury and with transport officials. So it was developed at a management level, not at a board level.

The Hon. DANIEL MOOKHEY: Agreed. But Mr Lyon did attend board meetings at various points and made presentations. Correct?

Mr MORGAN: Yes, I recall him attending a board meeting, yes. There may have been a further briefing on another day.

The Hon. DANIEL MOOKHEY: And draft copies were provided to the board. Correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: And to you specifically. Correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: And I presume you had a look at them when they arrived?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: I presume that you also had a look at the fiscal impact part of the report that Mr Lyon produced. Correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: I do not know if you have a copy of it but we have copies of the report here. I do not know if it is possible to provide it to the witness. I will read the relevant section which contains Treasury assumptions and KPMG assumptions. Is that correct to the best of your knowledge?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Mr Lyon's component of KPMG modelled both scenarios with the KPMG preferred assumptions and the Treasury preferred assumptions. Is that your understand as well?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: In the Treasury's preferred assumptions Treasury instructs Mr Lyon to model according to contributed equity from 2015 of \$10.8 billion, not \$7 billion. That is a \$3.8 billion variance which I think we can agree is significant?

Mr MORGAN: I think you will find the difference is capital work in progress.

The Hon. DANIEL MOOKHEY: Yes, so in the intervening period between when Treasury provides that assumption to Mr Lyon—

Mr MORGAN: Sorry Mr Mookhey could I just correct one thing. The equity injection of \$7 billion at 1 July is in respect of assets that are in place and for which a return is sought.

The Hon. DANIEL MOOKHEY: Yes.

Mr MORGAN: The additional equity as at 1 July is about \$4.5 billion which is capital work in progress, not yet commissioned. I think you will find the difference between \$10.5 billion and the number we are talking about here is down to that. I am sorry, I will not interrupt—

The Hon. DANIEL MOOKHEY: That is actually very helpful, Mr Morgan. The issue I have with that is: When was that \$4 billion provided—the capital works that you referred to?

Mr MORGAN: It is ongoing.

The Hon. DANIEL MOOKHEY: But it was provided as of the State budget this year. Correct?

Mr MORGAN: There would be capital works that were in flight before TAHE was even stood up that would be part of that number.

The Hon. DANIEL MOOKHEY: Yes, but in this year's budget those capital works that were otherwise allocated to the predecessor organisations of TAHE were then allocated to TAHE. Correct?

Mr MORGAN: As the capital is required. So the budget will record a capital program and make allocations—

The Hon. DANIEL MOOKHEY: But the issue that I have with that—

The CHAIR: Had you finished, Mr Morgan?

Mr MORGAN: My point is that at 1 July in the budget year the whole amount of capital is not moved to TAHE. It will be drawn down as required as fixed assets and capital works are undertaken. So at any point in time the works in progress number will be the amount of capital which has been forwarded for programs approved over a number of budgets in the past, just to clear.

The Hon. DANIEL MOOKHEY: Yes, I agree with that. That does help a lot. I think I understand the evidence which is additional money was provided to TAHE which will mean this number will move.

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: The issue I have though is that this letter was sent on 9 June 2021 and it states that approximately \$7 billion is at 1 July 2021 which raises a further question. Why then is the State not seeking a return on the additional money that was provided in this year's budget?

Mr MORGAN: Mr Mookhey, the reason is quite clear that a return is not expected, nor derived on a fixed asset in any circumstance until it is put into operating position. So these assets are under development. They do not earn fair or access fees or other fees and that is entirely consistent with normal accounting principles, business principles.

The Hon. DANIEL MOOKHEY: I think it clears that part of it up.

The Hon. TREVOR KHAN: You are talking over the top of him. Let him finish his answer.

The CHAIR: I thought in that case he had finished. Mr Morgan, did you have more to add?

Mr MORGAN: I was going to say the \$7 billion refers to assets that are in place—effectively capital which has been expended under the method described there—and a return is expected on the other assets when they are put into commission, when they are commissioned.

The Hon. DANIEL MOOKHEY: That makes sense.

Mr MORGAN: We will be asked to get a return on those as well.

The Hon. DANIEL MOOKHEY: Mr Chair, I was going to then go to the return issue but if you have follow-up questions—

The CHAIR: I have some questions, if possible, about the half-yearly accounts as at 31 December 2020, Mr Morgan. They were accounts that you signed off in your capacity as chair?

Mr MORGAN: Correct.

The CHAIR: I say that because I see a letter from you signing them off on 29 January 2021. Is that right?

Mr MORGAN: Correct.

The CHAIR: At the time you signed off on those accounts in January 2021 the notes indicate that the total assets have increased by \$0.5 billion from \$40.9 billion as at 1 July 2020 to \$41.4 billion due to capital expenditure of \$1.2 billion offset by \$7 billion for depreciation, amortisation and asset impairment. Does that reflect your memory that the total assets that you acknowledged in January this year, at the end of last year total assets were \$41.4 billion?

Mr MORGAN: I do not have the accounts in front of me but I will have to take on notice those numbers but the logic is right.

The CHAIR: I am reading again from the report, "Total equity has increased by \$0.4 billion from \$37.9 billion as at 1 July 2020 to \$38.3 billion due to capital contributions of \$1 billion offset by \$0.6 billion for the unfavourable total comprehensive income for the six months ended 31 December 2020." Does that sound right?

Mr MORGAN: Yes.

The CHAIR: The difficulty I am having is I have read the report in detail and there is no indication anywhere in it that those valuations were going to be fundamentally rewritten. Indeed, the sign-off on it says that the accounts are signed off in accordance with all the appropriate Australian and government standards. Did you know at the time that you were likely to writedown the assets by 50 per cent?

Mr MORGAN: The accounts that were presented there were done in accordance with the board resolution to adopt the cost method of accounting until such time as we had an income valuation. In respect of the cost method of accounting, those accounts are correct. In respect of 30 June 2021 accounts they had to be developed on an alternative basis. The readers of those accounts are also effectively produced for the shareholders, being Treasury and the finance Minister. I would think you would find they would have been aware that TAHE was in a transitional state and that those accounts were produced basically for their purpose at that point in time. They are not public accounts at that point in time; they are public accounts at 30 June 2021 when the Auditor-General completes the audit.

The CHAIR: These were published on your website. In fact, I am reading them from your website. These were public accounts, were they not, Mr Morgan?

Mr MORGAN: Sorry, I was not aware they are on the website.

The CHAIR: I am reading them from your website. You signed off on 29 January saying the net assets were something of the order of \$38 billion. I am asking if you knew at the time when you signed off on those accounts that you were in the process of radically reviewing them and halving them? Did you know at that time?

Mr MORGAN: I think I have provided the only explanation I can provide to you.

The CHAIR: I am going to ask you to not provide an explanation but to answer the question.

The Hon. TREVOR KHAN: He has answered the question, with respect. It may not be the answer you want but he has answered the question.

The CHAIR: Mr Morgan, I will ask you again: Did the board have advice as at the date you signed off on 29 January that the figures contained in that report were out by a factor of 50 per cent?

Mr MORGAN: On the basis of those accounts being prepared on a cost basis, those accounts were accurate. I do not recall any advice to the contrary.

The CHAIR: Mr Bourne, did you ever question the signing off on accounts at the end of last year ceding the assets at some \$38 billion, given that you must have known, I assume, that you were going through a process of radically reviewing the assets and, from what I can tell now, at least halving the value of them when you, as a board member, saw these accounts?

Mr BOURNE: My understanding was that those were prepared on the basis of one accounting standard and, in fact, during this transition year they would be treated in the same manner as other State-owned corporations are treated and that would, in fact, change the valuation.

The CHAIR: Where do we find that in the accounts, Mr Morgan—anywhere, at any point?

Mr MORGAN: Chair, I do not have them in front of me.

The CHAIR: I am happy for you to take it on notice.

Mr MORGAN: I am happy to take it on notice.

The CHAIR: Can you explain how it is that you publish a set of accounts that you must have known was likely to be so radically wrong?

Mr MORGAN: At that point we had not commissioned a valuation of the assets. We had not settled the likely capital structure of the business and so I was not in a position to know where the valuation had landed at that point in time. We developed the move to an income-based valuation subsequent to those accounts.

The CHAIR: From whom did you commission a re-evaluation of the assets?

Mr MORGAN: The re-evaluation of the assets under the appropriate accounting standard for the year through a transitioning to was initially done by our own internal people. Treasury also was involved in the development of that valuation model. We then sought an independent valuation from PricewaterhouseCoopers.

Ms ABIGAIL BOYD: Mr Morgan, if we could just take a step back. I apologise for having less knowledge than you on accounting matters so if you can recap. From what I understand you are saying that when these half-yearly accounts were prepared it was on the basis of the accounting principles that were appropriate for something that was not a fully-fledged State-owned corporation at that time. Is that right? And then you subsequently became a State-owned corporation properly—I do not think that is the right wording but let us just go with that—on 1 July. So that is when the new accounting standards then took effect or was this a discretionary choice of accounting standards?

Mr MORGAN: TAHE was established as a State-owned corporation on 1 July 2020 so it was in transition in terms of operating policies and developing a range of matters. This is one example of where it was. I think you will find that the accounts for 31 December 2020 describe, in the basis of accounting or in the fixed asset node, the method on which the assets are valued. I cannot confirm where exactly because I will have to take that on notice.

The CHAIR: I can assist, if you like, Ms Boyd. It says, "The financial statements are prepared in accordance with the Australian accounting standards which includes Australian accounting interpretations, the Government Sector Finance Act 2018, the Government Sector Finance Regulation 2018, the State Owned Corporations Act 1989 and the Treasurer's directions."

Mr MORGAN: I would have to investigate that and come back to you.

The CHAIR: I am assuming it is accurate; I am reading from your report.

Ms ABIGAIL BOYD: The question I am asking is: When the valuations were done we had the cost method of accounting at the beginning and then we ended up with an alternative basis, an income basis, I think you said, of accounting, was that required by the accounting standards because something had changed within TAHE or was it a decision of the board to suddenly apply a different accounting method?

Mr MORGAN: Nothing had changed within TAHE. We had discussions with the Audit Office and it was clear that we needed to move to that basis of valuation for the year-end accounts.

Ms ABIGAIL BOYD: When you said "clear" on what basis?

Mr MORGAN: On the basis I described initially, Ms Boyd, where State-owned corporations are required to value fixed assets in that particular way—use the income method—and that is the progress we were making towards that.

The Hon. PETER POULOS: Chair, to be fair to Mr Morgan, I think this is the third time you have reinforced this issue.

Ms ABIGAIL BOYD: Why was that not the appropriate method previously? You said before it was not wrong to have the \$40 billion on there. Are you saying nothing changed yet it was not wrong to have it under that former accounting method?

Mr MORGAN: Thank you, Ms Boyd. The observation I made at the start of this process was that we agreed—and I think it is evidenced in the minutes of TAHE—that initially we would adopt the cost method, and those accounts were prepared on that basis of the interim. Following further discussions with the Audit Office, and our own knowledge of State-owned corporation requirements, we moved to an income-based valuation. As I said at the outset, this is not a cash transaction; this is a non-cash revaluation exercise.

The Hon. DANIEL MOOKHEY: Just to follow up on Ms Boyd's question, I think in the answer to the Chair you said that you resolved to adopt a cost-based approach, if I heard you correctly?

Mr MORGAN: Initially.

The Hon. DANIEL MOOKHEY: Initially, yes. That took place sometime between 1 July 2020 when you came into existence as a State-owned corporation and presumably the time that the accounts were prepared?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Did it occur to you that, according to your own evidence, that is a variation from standard practice that applies to State-owned corporations?

Mr MORGAN: Given that we were in a transition year, we had not had a deep discussion on that when the resolution was passed in July. It was more a question of then developing the methodology by which we needed to move to the other valuation which took place largely post 31 December 2020.

The CHAIR: I have not run an organisation with a \$40 billion net equity.

The Hon. TREVOR KHAN: Have you run any organisation, David?

The CHAIR: But I have never yet seen an organisation able just to choose its own accounting standards. Yet you seem to be saying that you as the board can just choose. You can choose what accounting standards to apply and it is a matter for the board. Am I misunderstanding your evidence?

Mr MORGAN: Incorrect, no. I think you are, Chair.

Mr DAVID SHOEBRIDGE: How so?

Mr MORGAN: The accounting standard is the accounting standard that needs to be developed for a State-owned corporation. The first audited set of these accounts will be 30 June 2021 and when you read those accounts you will see that we have properly applied the accounting standard in respect of valuation of assets. At the half year we were not in a position to do that so we retained the cost method. There is nothing more difficult or sinister in that, I assure you.

The CHAIR: Why did you not tell us that? Why is there no reference to that anywhere in your 31 December accounts? Why is the first we hear about it now?

Mr MORGAN: I would have to take that on notice. I have not got the accounts in front of me.

The Hon. SCOTT FARLOW: When you say you retained the cost method, that was what they were under the former entity. Is that correct?

Mr MORGAN: Yes.

The Hon. SCOTT FARLOW: So you were carrying over the value effectively as they were represented under the former entities, as they all came under TAHE.

Mr MORGAN: That is correct, Mr Farlow. The RailCorp accounts at 30 June 2020, which I had to sign, were prepared on the basis of cost method. The move to where we are now is part of the transition process of fully adopting what was required for a State-owned corporation.

The Hon. DANIEL MOOKHEY: Mr Morgan in your opening statement you cited your experience of Sydney Water as being, "giving you experience in how to operate a State-owned corporation". Did I hear that correctly?

Mr MORGAN: Absolutely.

The Hon. DANIEL MOOKHEY: And you prepared annual reports for Sydney Water. Is that correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Does your knowledge of standard practices for New South Wales State-owned corporations predominantly arise from your service as chair of Sydney Water?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Is it your evidence that this income standard is applied by Sydney Water?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: When circa 1 July 2020 you adopt a different accounting standard, did it not occur to you that there was a discrepancy in how you were reporting compared to how Sydney Water would be reporting?

Mr MORGAN: At that point in time, as I said previously, it was clear that we were in a transition towards accounting standards and other procedures for State-owned corporations. I have explained the position on that.

The Hon. DANIEL MOOKHEY: At the time did you have a company secretary?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Were they providing advice to the board?

Mr MORGAN: I look more to the financial control.

The Hon. DANIEL MOOKHEY: Okay. Was the company secretary also providing advice?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: I turn now to the actual return that you are required to earn on the \$7 billion. What is your target return on equity?

Mr MORGAN: It is 1.5 per cent at this point in time.

The Hon. DANIEL MOOKHEY: Is that a direction that has been given to you formally?

Mr MORGAN: I am not sure under what circumstances I have been advised, but it is the direction that Treasury, on behalf of the shareholders, requires.

The Hon. DANIEL MOOKHEY: When you say "a direction from Treasury"—can you repeat the phrase?

Mr MORGAN: It is not a direction. We have been advised that—I am not sure under what basis—from Treasury.

The Hon. DANIEL MOOKHEY: And that has been advised to you, presumably from management to management, or to the board directly?

Mr MORGAN: I could not say for sure.

The Hon. DANIEL MOOKHEY: It is 1.5 per cent per annum currently?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: You have also recently been required to complete a 10-year business plan. Is that correct?

Mr MORGAN: The 10-year business plan is in draft, awaiting the finalisation of the annual accounts.

The Hon. DANIEL MOOKHEY: Okay, but it is in draft?

Mr MORGAN: Under development, yes.

The Hon. DANIEL MOOKHEY: Presumably it sets out a plan for you to retain your return on equity. Correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: By the tenth year of your 10-year business plan, what is your expected return on equity?

Mr MORGAN: I am sorry. I will have to take that on notice. I do not have it in front of me.

The Hon. DANIEL MOOKHEY: Does the 1.5 per cent change at any time in your 10-year business plan?

Mr MORGAN: I cannot recall.

The Hon. DANIEL MOOKHEY: When did you complete the 10-year business plan in draft form?

Mr MORGAN: I could not say exactly; I would have to take that on notice. But it has been prepared over the last few months.

The Hon. DANIEL MOOKHEY: I think your management, when we last saw them, said that it was prepared as of the date that they saw us, but they made the point that they were then pending board approval. Has your board considered the 10-year plan recently?

Mr MORGAN: The board has reviewed it on the way through and had input to the plan. The plan cannot be finalised until the Auditor-General has finalised the position on the annual accounts.

The Hon. DANIEL MOOKHEY: Of course. But it is relatively recently that this 10-year plan has been agreed. Do you agree with that?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: But you do not recall what your return on equity is meant to be at the end of the 10 years?

Mr MORGAN: I do not have it in front of me. I cannot say for certain. I would have to take that on notice.

The Hon. DANIEL MOOKHEY: But to the best of your recollection, to either you or Mr Bourne, does a return on equity ever rise above 1.5 per cent in the next 10 years?

Mr MORGAN: I have given you my answer on that.

The Hon. DANIEL MOOKHEY: Mr Bourne?

Mr BOURNE: The same.

The Hon. DANIEL MOOKHEY: You do not recollect either?

Mr BOURNE: We have discussed it but I do not remember; I do not have it in front of me. I will take that on notice.

The Hon. DANIEL MOOKHEY: You do not have any recollection whatsoever as to—

The Hon. TREVOR KHAN: He is entitled to take it on notice.

The Hon. DANIEL MOOKHEY: Okay, that is fine.

Mr BOURNE: It starts at 1.5.

The Hon. JOHN GRAHAM: Can I ask you to take on notice how you were advised—the form in which you were advised about that and when that occurred?

Mr MORGAN: I am happy to take that on notice.

The Hon. DANIEL MOOKHEY: Did you have any input in negotiating what your appropriate return on equity should be?

Mr MORGAN: It was dealt with at a management level.

The Hon. DANIEL MOOKHEY: Yes, but did the board have any input on it or did you rely on management to do that for you?

Mr MORGAN: It was reported to the board. It was mostly done by management.

The CHAIR: Sorry, Mr Morgan, I think one of the key questions is whether TAHE management had any proactive capacity to negotiate up or down the return. Were they advised about what the return is or were they part of setting the return based upon their understanding of the business?

Mr MORGAN: Chair, I was not a party to the discussions that management had with Treasury in this instance that determined this return. I was advised and the board was advised that that is where the return was, which the board accepted.

The CHAIR: Sorry, did it relate to your management's understanding of the business and what a reasonable return on the business was, or did they just give you a figure?

Mr MORGAN: As I said, Chair, it was an iterative process between management and Treasury and that is the outcome of it.

The CHAIR: What about between management and board? Surely you went to the management and said, "Well, is this 1.5 per cent achievable? What is it going to do for our business? How is it going to work?" You must have had those—I mean, you are the chair of the board.

Mr MORGAN: The board was satisfied with the return.

The CHAIR: Sorry, did you ask management, did you get reports from management that the 1.5 per cent return was, first, achievable and, second, sustainable?

Mr MORGAN: We agreed with management that 1.5 per cent would be acceptable. It is in the draft business plan. We have also to the point we can sign off on the draft business plan and that shows profitability over the next 10 years and a satisfactory return for our shareholders.

The CHAIR: You see, Mr Morgan, the truth is this, is it not, that TAHE is in no way independent. You were given the 1.5 per cent return from Treasury and you just had to accept it, and it confirms the lack of independence of TAHE, does it not, Mr Morgan?

Mr MORGAN: I would not draw that conclusion at all, Chair.

The CHAIR: What conclusion would you draw from having to accept Treasury's figure as a so-called independent State-owned corporation, Mr Morgan?

The Hon. TREVOR KHAN: He has already disagreed with the proposition.

The CHAIR: I am asking you what conclusion you would draw from the fact that TAHE had to simply accept what was delivered to them by Treasury.

The Hon. TREVOR KHAN: He has disagreed with that proposition, David.

The CHAIR: Mr Morgan?

Mr MORGAN: Chair, TAHE is established with a separate board. We do discuss these matters at board, whether it be the return, the access fee amounts, the way in which the legal agreements are structured with the operators, how we go on safety and all the other things. We have a point of view, we can convey messages back to any of the shareholders or the portfolio Minister. I do not accept that TAHE is not independent.

The CHAIR: Mr Bourne, is it your understanding that the board questioned management about the 1.5 per cent return to determine whether it was sustainable or achievable?

Mr BOURNE: Yes, I think there was a discussion on the return rate, but in the current economic climate and the current interest rates, 1.5 per cent for a start-up business, as it is as a SOC, I thought was reasonable.

The Hon. DANIEL MOOKHEY: Just on that though, on the 1.5 per cent return, you accept that as a State-owned corporation it is your requirement to produce a profit?

Mr BOURNE: Mmm.

The Hon. DANIEL MOOKHEY: Is that affirmative, Mr Bourne?

Mr BOURNE: Yes, I agree with that.

The Hon. DANIEL MOOKHEY: Mr Morgan, you agree that it is your requirement to produce a profit?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: And you accept that producing a profit is a key test that is applied to the ABS as to whether it gives you classification as part of the public non-financial sector?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Did you ever seek advice about whether or not accepting a 1.5 per cent is a sufficient economic return for the purpose of the ABS test?

Mr MORGAN: The ABS confirmed in June this year that the projected returns and operating model and so on for TAHE would satisfy its test. So I do not need to go to the ABS specifically on a return number or whatever. The ABS would have had insight enough to confirm that decision in June.

The Hon. DANIEL MOOKHEY: Just on that though, you said you went to them in June. Correct?

Mr MORGAN: I did not go to them in June. They confirmed with Treasury in June.

The Hon. DANIEL MOOKHEY: But presumably you agreed to the target before June.

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: So you agreed to the target before you had access to the knowledge of how ABS was treated. Correct?

Mr MORGAN: Any discussion between ABS is not a discussion with TAHE, it is a discussion with Treasury. So public non-financial corporation [PNFC] status—

The Hon. DANIEL MOOKHEY: A matter for Treasury.

Mr MORGAN: —is a matter for Treasury, not a matter for TAHE or its board. It is obviously interested, but beyond that it has no direct discussion with ABS, to my knowledge.

The Hon. DANIEL MOOKHEY: On that though, you maintain a view that 1.5 per cent is an acceptable return. Correct?

Mr MORGAN: Correct, and Mr Bourne has outlined why that would be the case.

The Hon. DANIEL MOOKHEY: And that is predominantly because, Mr Bourne, you consider this to be a start-up?

Mr BOURNE: Yes.

The CHAIR: Do you consider it a start-up, Mr Morgan?

The Hon. TREVOR KHAN: Mr Mookhey asked a question, Mr Bourne is—

The CHAIR: Sorry, I thought Mr Bourne had answered.

The Hon. TREVOR KHAN: I do not think you can turn it into a machine-gun approach.

The CHAIR: I thought Mr Bourne had answered.

The Hon. DANIEL MOOKHEY: Mr Bourne, you think the 1.5 per cent is acceptable because you think TAHE is a start-up? Did I hear you correctly?

Mr BOURNE: Yes. It was the establishment year. We were trying to get a turnaround of the balance sheet and the incomes of the business and for starting at that point it does not mean it does not get reviewed down the road, but at this point in time in the history of TAHE it was accepted as the starting point, yes.

The Hon. DANIEL MOOKHEY: Mr Bourne, when then do you expect to review this?

Mr BOURNE: Sorry?

The Hon. DANIEL MOOKHEY: You just said it does not mean it does not get reviewed down the line. When is the board expecting to review the 1.5 per cent rate? Is there any plan to review it?

Mr BOURNE: We look at budgets every year and I suspect we will look at it every year possibly.

The Hon. DANIEL MOOKHEY: I just asked you about your 10-year plan, which is your key business plan and that your shareholder Ministers require of you. You were not in a position to recollect at that time what

the return of equity is. Is it now the case you recollect that you will be discussing this every year for the next 10 years?

Mr BOURNE: I do not remember what was said for 10 years. All I am saying is we were accepting 1.5 and we will look at it from time to time.

The Hon. DANIEL MOOKHEY: You are aware that 1.5 is, broadly speaking, at or below inflation?

Mr BOURNE: It is well above the Reserve Bank's interest rate at the moment.

The Hon. DANIEL MOOKHEY: But it is below inflation.

Mr BOURNE: Yes, that is correct as we speak.

The Hon. DANIEL MOOKHEY: So the return—we are actually losing money; we are not gaining money. Our real income is going down, and this is acceptable to the board, is it? Is that the evidence we are hearing?

Mr BOURNE: No.

The Hon. DANIEL MOOKHEY: Mr Morgan and/or Mr Bourne, can you explain to me therefore why the board agreed to a return on equity which is less than inflation, that results in us as a State losing real income?

Mr MORGAN: The board has accepted 1.5 per cent as an initial return on equity. We have not as yet built out the other revenue streams that we expect. We have got an idea where that is coming from in terms of property and so on. Our expectation is that we will beat that return, but at this point in time we have produced a 10-year business plan and the business plan will be reviewed annually and as we develop revenue streams, which we expect to have in TAHE, then that return may well be beaten. At this point in time, that return is satisfactory from where we are as a starting point. Why is it a starting point? Because this State-owned corporation is a brand-new State-owned corporation.

The Hon. DANIEL MOOKHEY: So just on that, on your answer there, Mr Morgan, can you give us any assurance that over the 10-year period the return is going to exceed inflation and we are going to make a real profit?

Mr MORGAN: I am not in a position to guess at that; it is hypothetical.

The CHAIR: Mr Morgan, the accounts you signed off in January, the 31 December accounts, had the half year ending 31 December 2020 net loss before tax at \$717,975,000. That was for the half year. Do you recall that?

Mr MORGAN: I do not recall it, Chair, because I do not have it in front of me and I have not looked at it for some time. I would offer that there is a fairly sizable depreciation number in there that probably drives that outcome which, again, is a non-cash item.

The CHAIR: Indeed. But you would recall, would you not, that the loss for the six months was of the order of \$717 million?

Mr MORGAN: No, I do not have the accounts in front of me. I do not recall.

The CHAIR: I am reading from the accounts published on your—

Mr MORGAN: That is fine, but I do not have them in front of me.

The CHAIR: Do you accept that is right?

The Hon. DANIEL MOOKHEY: We will provide them to you now, Mr Morgan.

The CHAIR: But do you accept that is right?

Mr MORGAN: Yes, fine.

The Hon. DANIEL MOOKHEY: Forgive the highlights.

Mr MORGAN: Sorry, Chair, your question?

The CHAIR: Is that the 31 December accounts?

The Hon. DANIEL MOOKHEY: That is the one he is reading from.

The CHAIR: If you have a look at page 12 at about point 7 on the page, you will see there "Net profit/loss".

Mr MORGAN: Yes.

The CHAIR: "After tax \$717,975,000" for the six months, tracking at an annual loss of just under \$1.5 billion at that point. Is that right?

Mr MORGAN: Certainly the loss for the six months was that, and it is actually slightly less than the previous period.

The CHAIR: The only way TAHE could continue as a business without liquidating was through having a letter of comfort from NSW Treasury to cover your losses. Was that not right?

Mr MORGAN: It is my experience with State-owned corporations that I ask for a letter of comfort on a range of issues, mostly relating to debt financing.

The CHAIR: My question was, the only reason you could sign off on the accounts and not liquidate was that you had a letter of comfort from Treasury saying they would cover your losses. Is that not right?

Mr MORGAN: Book losses do not equal cash, and the basis on which we as a board seek a letter of comfort from Treasury is on funding facilities to cover unforeseen cash positions. Whether or not there is a depreciation charge in here of \$736 million, it is a non-cash item. So the letter of comfort relates more to working capital comfort and to long-term debt facilities and potentially equity and it relates to the financial result of the company.

The CHAIR: Can I take you to page 16 of the report? At about point 6 on the page, a bit over halfway down—this is the notes to the financial statements—do you see there, "The financial statements have been prepared on a going concern basis which assumes that TAHE is expected to be able to pay its debts as and when they fall due and continue in operation without any intention or necessity to liquidate or otherwise wind-up their operations. NSW Treasury has issued a letter of comfort to TAHE in the current financial year to ensure its ongoing viability for at least 12 months." Do you see that?

Mr MORGAN: I do.

The CHAIR: Without that letter of comfort, you could not have signed off on the accounts, could you?

Mr MORGAN: I think it would be clearer to say without that letter of comfort, as an independent director with lots of experience I would not be signing off on that set of accounts on the assumption, because I will not assume that our debt requirements would be met by increases in Public Authorities (Financial Arrangements) Act [PAFA] limits or whatever, or that I would receive equity.

The CHAIR: That letter of comfort expired last week, did it not?

Mr MORGAN: Yes.

The CHAIR: Did you get a fresh one?

Mr MORGAN: We will. As part of the year-end process, before the accounts are signed for the current year there will be a letter of comfort for the same reason.

The CHAIR: Sorry, you have not got one yet?

Mr MORGAN: I cannot confirm today whether I have one, but I will be happy to take it on notice. There have been discussions with Treasury. I would be happy to take it on notice and provide information as to what we are doing on that front.

The CHAIR: What if you do not get a letter of comfort from Treasury? You are an independent State-owned corporation. If you do not get a letter from Treasury do you have to wind the thing up?

Mr MORGAN: If I do not get a letter from Treasury then the accounts cannot be completed. I would be pretty sure that a comfort letter from Treasury will be forthcoming.

The Hon. DANIEL MOOKHEY: Can I just ask on that question though: Is there an inconsistency with Treasury having to guarantee your position to the extent to which you just described and the ABS requirement that you be genuinely independent of government?

Mr MORGAN: Thank you for the question. Not at all, and the reason I say that is that—and this is the case with my experience of State-owned corporations elsewhere where a letter of comfort is also sought—the comfort is mainly around an undertaking from Treasury that access to capital and/or further debt facilities will be available and they will assist in that process—not that Treasury itself will provide grants or whatever. So it is entirely consistent with my experience elsewhere.

The Hon. DANIEL MOOKHEY: That makes sense.

The CHAIR: Before we move on from the letter of comfort, Mr Morgan, will you provide the Committee with a copy of the letter of comfort that expired last week?

Mr MORGAN: Certainly.

The CHAIR: And will you provide us with whatever correspondence you have had with Treasury about getting a fresh letter of comfort?

Mr MORGAN: Certainly.

The Hon. DANIEL MOOKHEY: Mr Morgan, I think this is my last question on the finances. Is it the case that Sydney Water—

Mr MORGAN: Sorry, Mr Chair, could I just add some clarification on this? If it is not clear already, one, this is a normal practice; two, State-owned corporations need access to debt facilities provided through TCorp or equity provided effectively from the shareholding Ministers. This is nothing which is out of the ordinary; in fact, I am a bit of a pain with Treasury because I insist on it, to make sure that the independence of the organisation, the independence of directors is assured and we are undertaking our work properly. It is no different to working in a normal public company where one of the main jobs of directors is to make sure there is sufficient liquidity into the future, particularly to cover the preceding year's operations. This is no different; this is exactly normal practice. This is nothing to do with TAHE being a brand-new company. I would be doing that in all circumstances.

The Hon. SCOTT FARLOW: Mr Morgan, just to pick up on that, you were talking about your experience before. I take it you have sought letters of comfort as well in your role with Sydney Water. Is that correct?

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Just on that though, Mr Morgan, what is the Sydney Water return on equity that is expected?

Mr MORGAN: I am not sure that we are really here to talk about Sydney Water. I can really only speak in the context of TAHE.

The Hon. DANIEL MOOKHEY: Mr Morgan, respectfully, you nominated Sydney Water as a key part of your experience.

Mr MORGAN: Sure, but, with respect, I am not going to talk about Sydney Water's returns in the context of here.

The Hon. DANIEL MOOKHEY: In the KPMG report that we referred to earlier, it lists it at the time as being 6.2 per cent and it listed this as a result of what is the appropriate benchmark for what the return on equity should be for TAHE. That is the reason why it is relevant. Equally, it lists Landcom as having a 14 per cent return, Newcastle Port Corporation 7.2 per cent, Forestry Corporation as 9.1 per cent, Hunter Water as 3.6 per cent, Essential Energy as 0.7, which, to be fair, is lower—it is the only State-owned corporation which is lower than yours as well.

The Hon. TREVOR KHAN: It is a bloody important one, I have to say—absolutely.

The Hon. DANIEL MOOKHEY: Did it not occur to you that there was a wide discrepancy between what you expected to earn from Sydney Water and what you expected to earn from TAHE?

Mr MORGAN: The question of returns depends very much on the sector in which you are operating and the circumstances that are there. So it will have had regard to what the returns are from the operators and it will have had regard to, effectively, the fares and the tariffs paid by customers and where they sit. I would also point out in the case of TAHE, of course, there are regulated businesses and unregulated businesses for which we receive significant access fees from Sydney Trains and beyond. There is also a country rail network, which in fact is not a positive net income asset.

The Hon. TREVOR KHAN: Probably far from it.

Mr MORGAN: Somewhat far from it, with a considerable number of the assets not in use. In fact, the Treasury is funding, through a normal grant program as opposed to equity, the cost to cover the Country Regional Network [CRN] contract for the next 10 years, which is in excess of \$1.5 billion, to provide appropriate maintenance for the CRN network. So you can see that in the portfolio there is a mixture of income-producing and otherwise assets that speak a little bit to the return that you are concerned about.

The Hon. DANIEL MOOKHEY: Indeed, but equally the State-owned—

The Hon. TREVOR KHAN: I would love to see you go out there and argue that Essential Energy should get some of those returns.

The Hon. DANIEL MOOKHEY: I am not, Mr Khan, but I think you just made reference equally to the non-profitable aspects of your operation. Under the State Owned Corporation Act are you not required to seek a declaration from the Minister for you to provide those services if you say they are unprofitable?

Mr MORGAN: If we were to be asked to embark on a new activity that was not commercial in our view, then we would probably seek a direction from the Minister. But these assets were transferred to TAHE on 1 July 2020 and their relevance is that on the basis they were supplied into TAHE, our job as an organisation is to enact or to carry out the policy requirements of government.

The Hon. DANIEL MOOKHEY: Do you have the power to cancel the country rail network independently of government?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: Is that because the operating licence requires you to provide that service?

Mr MORGAN: We, in fact, signed the CRN contract when it was put into place because it was a policy objective of Transport for NSW to have that put in place. So we have already been through the process of considering the new contract and signing as a board that contract, recognising the community obligation—which is one of our obligations in our objectives; regional is one of our five objectives.

The Hon. DANIEL MOOKHEY: That did not cause you to have to seek the declaration that you just referred to?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: Okay. So you are confident you can provide that service on a for-profit basis?

Mr MORGAN: The question for TAHE is not whether individual activities are provided on a for-profit basis, bearing in mind what has come across from Transport for NSW and RailCorp; it is a question of what we do as a portfolio organisation, the whole organisation, and you have referenced many times the 1.5 per cent return we are expecting on the contributed equity on that front.

The Hon. DANIEL MOOKHEY: Mr Morgan and/or Mr Bourne, were you aware that in August this year then Minister Constance had written to the Office of Transport Safety Investigations [OTSI] to undertake a comprehensive safety review of TAHE?

Mr MORGAN: Could I answer it and then ask my colleague?

The Hon. DANIEL MOOKHEY: Yes.

Mr MORGAN: Absolutely aware of it. Frankly, particularly for a relatively new company with a new management team and a new board, we welcome the opportunity to have a fresh pair of eyes in the organisation and to see where we had got to and to pick up any recommendations that we welcome to implement. But I will ask Mr Bourne to comment.

The Hon. DANIEL MOOKHEY: Is that also your answer, Mr Bourne?

Mr BOURNE: Yes, look, we were very comfortable to have a discussion with OTSI. We have not seen the report so we do not know what the results were, but I think the structure that is in place principally about the day-to-day, fundamental operations of the business sit within Transport for NSW. They do the operation, they do all the maintenance, they decide what capital they need. So all the responsibilities that existed there before TAHE were formed are still there.

The Hon. DANIEL MOOKHEY: Mr Bourne, in your opening statement you made reference to what I think you nominated as being an extra line of defence or assurance on safety. I heard you correctly?

Mr BOURNE: Yes, that is correct.

The Hon. DANIEL MOOKHEY: And you consider that to be a part of your responsibility?

Mr BOURNE: Yes.

The Hon. DANIEL MOOKHEY: Are you explicitly given that role in legislation?

Mr BOURNE: We have an oversight role, the day-to-day—and, as I said in my opening statement, the board of TAHE takes its obligations very seriously—it is the prime measure for us from a non-financial perspective.

The Hon. DANIEL MOOKHEY: Indeed.

Mr BOURNE: And we have put in place the various modes of oversight that any well-structured company that operates in a hazardous environment would do.

The Hon. DANIEL MOOKHEY: Can I ask you then—

The Hon. TREVOR KHAN: Let him finish.

The Hon. DANIEL MOOKHEY: Sorry, Mr Bourne, had you finished?

Mr BOURNE: We have created a specialist committee on which I am reasonably experienced but we also have a subject matter expert, and we have created a set of measurements that we can oversight the information coming up from Transport for NSW, that we can oversight the quality of the management of the work that is going on.

The Hon. DANIEL MOOKHEY: Indeed, and I presume, therefore, as you just said, that given you take this very seriously and it is probably the most important matter that you deal with, I am just asking what is the source of your legislative authority here? Are you aware that under the Act you have legislative authority in this respect?

Mr MORGAN: The Transport Administration Act sets out the five principles—this is the addition to the Transport Administration Act that was passed, I think, in 2017—and the first of those is to undertake its activities in a safe and reliable manner. We are the asset owner, we are the dedicated asset owner of these activities.

The Hon. DANIEL MOOKHEY: Can you order the operators to cease the practice?

Mr MORGAN: I will pass again to Mr Bourne because he is running the committee on this.

The Hon. DANIEL MOOKHEY: You cannot?

Mr BOURNE: We do not order them. We have an oversight role. They have the absolute level of accountability, that is Transport for NSW, to operate, maintain strictly in accordance with the many and varied regulations that exist for the operation of the network.

The Hon. DANIEL MOOKHEY: Indeed. You cannot order them to cease an activity; can you order them to undertake an activity?

Mr BOURNE: No, we cannot order them. What we do is we are providing a level of oversight to see that in fact good practice is taking place, but the absolute responsibility for the day-to-day operations and its maintenance exists with Transport for NSW.

The Hon. DANIEL MOOKHEY: Can you require them to produce documents to you?

Mr BOURNE: Yes. They provide us with a very well-structured monthly source of information.

The Hon. DANIEL MOOKHEY: But can you issue them, for example, a notice to produce?

Mr BOURNE: Sorry, what was that?

The Hon. DANIEL MOOKHEY: Can you issue them effectively a notice to produce about the practices or documents?

Mr BOURNE: We have never had to. They have been very, very cooperative and the relationship we have with them is extremely good.

The Hon. DANIEL MOOKHEY: But I am asking, Mr Bourne, do you have the power? Not whether you have to but—

Mr BOURNE: I cannot answer that, I am sorry.

The Hon. DANIEL MOOKHEY: Equally, what legal accountability does TAHE face should an incident occur on the network?

Mr BOURNE: The strict legal responsibility sits with Transport for NSW, but as managers we have that broad oversight to make certain that the assets that Transport for NSW are operating are operating in accordance with the various regulations, the original operator's requirements. So we take an interest in that; we take an oversight view of it.

The Hon. DANIEL MOOKHEY: Sure, no doubt, I am sure you are interested, there is no dispute about that, but in the event there was an incident like there was just two weeks ago which, to be fair, was created not by the transport operator by any means, but in any rail incident, what exactly is TAHE accountable for? Is it accountable for anything?

Mr BOURNE: We will oversight, but in fact the ultimate responsibility rests, as it always has done prior to the establishment of TAHE, with Transport for NSW.

The Hon. DANIEL MOOKHEY: Indeed, I accept that, but is it the proper rendering of the evidence, Mr Bourne, that it is not the ultimate responsibility; it is the sole responsibility that belongs to the operator.

Mr BOURNE: The sole responsibility sits with Transport for NSW.

The CHAIR: Mr Bourne, are you at all troubled by the conclusion following the Glenbrook train disaster, the long inquiry and the detailed report handed down by Justice McInerney where he said the division between the asset holder and the operator was one of the reasons we saw that disaster? Are you at all troubled that history is repeated with TAHE?

Mr BOURNE: No, I am not troubled at all.

The CHAIR: How do you overcome those concerns?

Mr BOURNE: Because, as I have said repeatedly, the responsibility for the operation, maintenance and the good management rests with Transport for NSW.

The CHAIR: So you own the asset.

Mr BOURNE: Yes.

The CHAIR: But all of the risk is handed over to the operator?

Mr BOURNE: Exactly right.

The CHAIR: And you negotiate with the operator what the access fee will be, is that right?

Mr BOURNE: That is correct.

The CHAIR: And you negotiate with the operator what the maintenance schedule will be?

Mr BOURNE: No, not the maintenance schedules because that is part of the responsibility of Transport for NSW.

The CHAIR: Is there any other network that the operator can negotiate with to get access? You have got a fairly captured market here, do you agree, Mr Bourne?

Mr BOURNE: Yes.

The CHAIR: If you ask for or require an unreasonable access fee and that puts commercial pressures on your one and only client in this space, how can you not be sure that they will not cut corners on maintenance in order to meet your return for business?

Mr BOURNE: They are the ones with the absolute responsibility and we will expect that they will spend what needs to be spent to meet that responsibility.

The CHAIR: What is the expectation based on? You have millions of people travelling on your assets that you own and you contract out all the risk and all the responsibility to a third party. That is the situation, is it not, Mr Bourne?

Mr BOURNE: That is exactly right.

The Hon. DANIEL MOOKHEY: Just on that though, in the cost of maintenance, is that the operator who pays for it or is it TAHE who pays for it?

Mr BOURNE: Yes, it is theirs. They undertake it, they pay for it.

The Hon. DANIEL MOOKHEY: And do they have to get your consent?

Mr BOURNE: No.

The Hon. DANIEL MOOKHEY: Are you not required to enter into maintenance agreements with them and set the standard levels?

Mr BOURNE: The standard levels are to do with the quality of the work and the fact that it meets the obligations of the manufacturers and the various regulations.

The Hon. DANIEL MOOKHEY: You set the standards of maintenance but they undertake the maintenance. Is that fair?

Mr BOURNE: No, the standards are agreed, but the standards are pretty much independently set.

The Hon. DANIEL MOOKHEY: I accept that they are agreed, but who is the decision-maker about what the standards should be?

Mr BOURNE: Transport for NSW.

The Hon. DANIEL MOOKHEY: Why do you say that?

Mr BOURNE: Because they are the ones who undertake the work and they are the ones who have the legal obligation.

The Hon. DANIEL MOOKHEY: But they are your assets.

Mr BOURNE: Yes, that is correct.

The Hon. DANIEL MOOKHEY: And you set the standards around which they are assured, do you not?

Mr BOURNE: No. They are the ones who are responsible and accountable for the operation and the maintenance in a safe and professional manner.

The Hon. DANIEL MOOKHEY: And that is after you entered into an agreement with them to that effect, is that correct?

Mr BOURNE: Yes, that is right.

The Hon. DANIEL MOOKHEY: You entered into the agreement with them. Yes?

Mr BOURNE: That is their responsibility.

The Hon. DANIEL MOOKHEY: I do not dispute that, Mr Bourne, that it is their responsibility. What I am trying to understand is what is the source of their responsibility. It arises from the agreement that they entered into with TAHE. Correct?

Mr BOURNE: Yes.

The Hon. DANIEL MOOKHEY: So TAHE is a counter-party to that agreement. Correct?

Mr BOURNE: Yes.

The Hon. DANIEL MOOKHEY: And you are required to enter into such an agreement, given that you own these assets. Correct?

Mr BOURNE: Yes.

The Hon. DANIEL MOOKHEY: And you technically would have the ability to have someone other than Transport for NSW or NSW Trains or Sydney Trains perform maintenance, would you not? You could enter into a maintenance agreement with someone else, could you not?

Mr BOURNE: No, because if we moved into that area we would separate them from—our job is not to intervene—

The Hon. DANIEL MOOKHEY: You would transgress the operators.

Mr BOURNE: —and tell them how to undertake the maintenance or who to undertake the maintenance. Their responsibility is to make certain it is done in accordance with the regulation and the manufacturer's requirements.

The Hon. DANIEL MOOKHEY: But you, under your operating licence that is issued to you by the transport Minister, have obligations in respect to maintenance, do you not?

Mr BOURNE: No. I keep repeating to you the maintenance is undertaken and its full responsibility rests with Transport for NSW.

The Hon. DANIEL MOOKHEY: Mr Bourne, I do not dispute that. I am working down the chain.

Mr BOURNE: Okay.

The Hon. DANIEL MOOKHEY: You are talking about the last part of the chain; I am asking you about the earlier parts. Let us start from the very beginning. You own these assets, do you not?

Mr BOURNE: Yes, we do.

The Hon. DANIEL MOOKHEY: You have an operating licence, do you not? You do not have an operating licence from the transport Minister?

Mr MORGAN: We have an operating licence with the transport Minister; we do not have operating certification with the Office of the National Rail Safety Regulator [ONRSR].

The Hon. DANIEL MOOKHEY: Thank you. You have entered into an agreement with Transport for NSW or NSW Trains or Sydney Trains, or a combination of the three, to perform maintenance. Correct?

Mr BOURNE: To perform the whole process of operations and maintenance.

The Hon. DANIEL MOOKHEY: And they are providing the maintenance on behalf of assets you own. Correct?

Mr BOURNE: Yes, that is correct.

The Hon. DANIEL MOOKHEY: And you set the standard around which the assets need to be maintained. Correct?

Mr BOURNE: Yes. The standards for maintaining equipment like that is generally set by either the regulations and/or the original equipment supplier. So it is a well-structured process.

The Hon. DANIEL MOOKHEY: Indeed. And in order to meet the standards that you have set, you have entered into those agreements. Correct?

Mr BOURNE: Yes.

The Hon. DANIEL MOOKHEY: And they recover under those agreements aspects of the costs of maintenance from you or they deduct it across other payments that they would otherwise provide you. Correct?

Mr BOURNE: No, the cost of the maintenance is all to their account.

The Hon. DANIEL MOOKHEY: Indeed, and that has some bearing on the access price you can charge them, does it not?

Mr BOURNE: No.

The Hon. DANIEL MOOKHEY: So you are saying to me that all of the costs of maintenance is incurred by them.

Mr BOURNE: Yes.

The Hon. DANIEL MOOKHEY: And there is absolutely no cost recovery whatsoever from TAHE.

Mr BOURNE: No, not from TAHE.

The Hon. DANIEL MOOKHEY: Do you have the ability to refuse or reject a request for them to do maintenance?

Mr BOURNE: No, I keep repeating—

The Hon. DANIEL MOOKHEY: If they come to you and say in order to meet your standard—

Mr BOURNE: Can I be clear? The total responsibility for the maintenance sits with Transport for NSW—both the delivery of it and the cost.

The Hon. DANIEL MOOKHEY: Did they disclose to you the maintenance that they are undertaking?

Mr BOURNE: Again the question, sorry?

The Hon. DANIEL MOOKHEY: Did they disclose or otherwise notify you of the maintenance that they are performing?

Mr BOURNE: We have a set of measures to do with fleet availability, overdue inspections—the sorts of safety-based measures that you would take to ensure that things like plant availability, reliability, that that is undertaken. But they do that at their cost.

The CHAIR: Ms Boyd has some questions at this point.

Ms ABIGAIL BOYD: Thank you, Chair. I want to pick up on that point. If, heaven forbid, there was a disaster and somebody wanted to take legal action in relation to it, would they need to go firstly to TAHE and to sue TAHE and then TAHE would, in turn, loop in Transport for NSW under the agreements, or are you saying that legally a person would be able to go directly to Transport for NSW?

Mr BOURNE: I am sorry, I am an engineer not a lawyer, so I cannot answer that question. I would need legal advice on it.

Ms ABIGAIL BOYD: I guess it goes to this point: If the maintenance obligation is on Transport for NSW by virtue of the agreements you have signed with it, that means that you must have ultimately the primary responsibility for maintenance legally, otherwise there would be nothing for you to—

Mr BOURNE: That is a legal question of which I have no qualifications to answer, I am sorry.

The CHAIR: I suppose this comes to the point: Have you had advice that you could just hand over all of your responsibility for maintenance and, through that, safety to a third party like this? Have you had legal advice that that is legally effective and will protect you?

Mr BOURNE: That was the structure that was in place and we have, yes, that is correct.

The CHAIR: Have you gone through the process of confirming that all known key risks and emerging contingent liabilities which could materially impact the current and future results of TAHE over the financial year that just passed have been fully disclosed? Has that happened?

Mr BOURNE: Yes.

Mr MORGAN: Yes.

The CHAIR: Who did you disclose them to?

Mr MORGAN: Perhaps if I could help on this issue. Advice was taken from a firm of lawyers in the design of TAHE's risk management and safety and asset management responsibilities to examine what we are and how we cooperate, and the design of what we have is informed by that process. So, as Mr Bourne said from the outset, fundamentally nothing has changed in respect of asset management or safety. Transport for NSW, and it is through the stand-up agreements, operates as our agent to do a number of things: one, to monitor asset management and safety; secondly, to ensure that Sydney Trains is spending the right amount on it or whatever other body, and report to us on risk. We are in the process of standing up our own risk framework, and we have had the fundamentals in place for quite some time, to identify what are the likely risks of harm and other risks to the corporation and we are managing those internally.

The CHAIR: You said that you had fully disclosed all known key risks and emerging contingent liabilities which could materially impact the current and future results of TAHE over the last financial year. So I ask again: Who did you disclose them to?

Mr MORGAN: It is a question that directors have to ask themselves in forming the accounts. I do not know where you are reading from exactly, but the directors go through a process of internal certification and internal discussion to ensure the risks that we might be concerned about that could have an impact on the financial statements have either been mitigated or quantified.

The CHAIR: This is from the statement of corporate intent [SCI] for the last financial year and it is a representation and commitment statement that you had confirmed. So I am asking you again: Who did you disclose all known key risks and emerging contingent liabilities to?

Mr MORGAN: It is up to the organisation and the management team to inform and debate that with the board. The individual risks that you are looking for me to talk about are not disclosed typically in the SCI. That is a confirmation to say have we done what we were supposed to do? The answer is yes, in the organisation that work has been undertaken.

The CHAIR: Mr Morgan, I am not telling you that they are in the statement of corporate intent. The statement of corporate intent that you have confirmed the board's commitment to required you to fully disclose all known key risks and emerging contingent liabilities. I ask again: Who have you disclosed them to?

Mr MORGAN: Any that needed to be disclosed to as part of that statement of corporate intent would have been added there.

The CHAIR: They are not in the statement of corporate intent. The statement of corporate intent requires you to do this. I am asking you first of all, have you done it? Have you fully disclosed, in accordance with your

obligations under the statement of corporate intent, all known key risks and emerging contingent liabilities which could materially impact the current and future results of TAHE for the last financial year?

Mr MORGAN: To the extent that any need to be quantified, they will be in the financial statements.

The CHAIR: What are the known key risks and emerging contingent liabilities, as referenced in the statement of corporate intent?

Mr MORGAN: Let me take that on notice, if I could.

The CHAIR: Could you take on notice when they were disclosed?

Mr MORGAN: Certainly.

The CHAIR: Are you saying the only place we will find it is in the financial results that are currently in draft and sitting with the Auditor-General?

Mr MORGAN: I will take that on notice.

The CHAIR: Given this was a confirmation the board made, do you have a requirement in monthly board meetings to check if you are meeting the statement of corporate intent?

Mr MORGAN: The board papers and the activities of the board will do that. But let me take that on notice.

The CHAIR: Mr Mookhey.

The Hon. DANIEL MOOKHEY: Mr Morgan, how were you recruited as the chair of TAHE?

Mr MORGAN: I was invited by a search firm, or I was rung up by a search firm to ask whether I would be interested in being considered as a director of a new corporation and then I entered a process, providing a CV and being interviewed by a panel and, as is the case with these appointments, you wait to find out whether they want you or not.

The Hon. DANIEL MOOKHEY: Indeed. Mr Morgan, we have heard from Treasury previously that the firm that perhaps contacted you was Korn Ferry.

Mr MORGAN: Correct.

The Hon. DANIEL MOOKHEY: Stepping it through, you presumably indicated that you would be favourable to such an opportunity?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: And you said that you then went through an interview process by a panel.

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Who was on the panel?

Mr MORGAN: I cannot recall exactly who was on the panel, but I do recall some of the members of the panel—Anne Hayes, who was to be the designated acting CEO was on it; there was certainly a representative from Korn Ferry; I would have to come back to you on notice to be accurate, but, typically, it is a representative from the Department of Premier and Cabinet, Treasury, Anne Hayes, as I mentioned.

The Hon. DANIEL MOOKHEY: Mr San Midha, the deputy secretary, I think has identified himself as being the chair of that panel. Does that accord with your recollection?

Mr MORGAN: I do not recall, although I have a feeling that I might have met with him separately to the panel for a separate interview, but, again, I would have to confirm that.

The Hon. DANIEL MOOKHEY: Okay. How many interviews did you have?

Mr MORGAN: One interview with the panel.

The Hon. DANIEL MOOKHEY: One interview with the panel and then a separate interview with Mr Midha. Yes?

Mr MORGAN: I believe so, but I would want to check that on notice.

The Hon. DANIEL MOOKHEY: Did you have a separate interview with Mr Pratt, the Treasury secretary at the time?

Mr MORGAN: I do not believe so.

The Hon. DANIEL MOOKHEY: On notice can you do a definitive check?

Mr MORGAN: Certainly.

The Hon. DANIEL MOOKHEY: And did you have any direct interviews with anybody from the Transport cluster?

Mr MORGAN: I believe that I caught up with Rodd Staples, but, again, I would have to take that on notice.

The Hon. DANIEL MOOKHEY: Thank you, if you could, that would be great. Did you have any direct conversations with Minister Constance, Treasurer Perrottet or Minister Tudehope?

Mr MORGAN: Not that I recall.

The Hon. DANIEL MOOKHEY: Mr Bourne, is this the same process you went through?

Mr BOURNE: Yes, a similar process.

The Hon. DANIEL MOOKHEY: In that process, were you required to attest to your experience with rail safety?

Mr MORGAN: Not specifically with rail safety.

The Hon. DANIEL MOOKHEY: Mr Bourne?

Mr BOURNE: They tested my broad engineering background, because I have spent most of my life in hazardous industries and I chaired the Virgin airline safety committee for four years. I also at this stage still do chair the Sydney Water safety committee.

The Hon. DANIEL MOOKHEY: I do not dispute that; you did identify that in your opening statement, but I am just asking you specifically was it a criteria—

Mr BOURNE: I recall questions on my background and my approach to safety and the experience that I had, yes.

The Hon. DANIEL MOOKHEY: But you were not specifically asked about your knowledge of the national rail safety law or any other rail safety aspect that I am specifically talking about?

Mr BOURNE: I did. I remember I spoke about—I actually worked in the rail workshop at BHP Steelworks, but during my Brambles years we were the largest rail equipment owner in Europe—we owned 40,000 rail wagons, and I have been to our workshops through Europe a number of times.

The Hon. DANIEL MOOKHEY: Of course. But, Mr Morgan, specifically to you as chair, were you at any time asked about what your experience was in the national rail safety law, to be very specific?

Mr MORGAN: I do not believe so. If I was, the answer would be no I was not familiar at that point in time with the national rail safety law.

The Hon. DANIEL MOOKHEY: What is your current understanding as to your responsibilities and TAHE's responsibilities under the national rail safety law?

Mr MORGAN: The primary responsibilities were the operator, which, as we have described extensively, is with Sydney Trains and so on. So it is an indirect responsibility with the rail safety operator.

The Hon. DANIEL MOOKHEY: Okay. But it was not explained to you as a key performance indicator or a key area in which you were required to have knowledge specifically about that.

Mr MORGAN: No, because the safety is the primary responsibility of others, as we have described.

The Hon. DANIEL MOOKHEY: Okay, fair enough. By the by, it is not disclosed in your annual report, as far as I can tell, but what is the actual remuneration of directors at TAHE?

Mr MORGAN: My remuneration is \$150,000 plus super guarantee levy [SGL] and the director's remuneration is \$80,000 plus SGL. If you go back and look at the Public Service Commission, that is relevant for all organisations of this asset base size.

The Hon. DANIEL MOOKHEY: As best as I am aware, that is consistent with the practice across all the State-owned corporations. Correct?

Mr MORGAN: Incorrect. No, no, no, there is a variety of practices which are basically based in history across all services. So you will find some of the newer ones have followed the model set down by the Public Service Commission; others are still stuck somewhat in the past.

The CHAIR: Mr Morgan, whilst we are talking about so-called practice and the like, there was not an historical practice with TAHE, is that right, in particular in commercial returns and the like?

Mr MORGAN: No, because it was—

The CHAIR: Is it correct that there is a modified version of the commercial policy framework that you have agreed with NSW Treasury?

Mr MORGAN: It is modified in the sense that it recognises that there will be a ramp up to full recognition of the commercial policy framework over time, which is, I think, about 18 months. It goes to things like State taxes in particular. You will recall, Chair, that last year there was no income from an access agreement in the year to 30 June 2021 because there was no access agreement until that time.

The CHAIR: And there was a waiver on certain State taxes for TAHE as well.

Mr MORGAN: Yes, in recognition that the income base of the organisation, the primary income base had not been established. So it was definitely in respect of land tax and other taxes. I could not describe exactly which ones.

The CHAIR: Could you on notice provide a copy, if it is in the form of a document, the modified version of the commercial policy agreement as agreed with Treasury?

Mr MORGAN: Yes.

The CHAIR: Thank you.

The Hon. DANIEL MOOKHEY: Could I just ask you on that land tax exemption that TAHE obtained from the Treasury, what is the value of that exemption? Do you know?

Mr MORGAN: I do not know at this point in time, and I knew it was a topic that you were interested in discussing with Mr Crimp as well. The way in which TAHE's assets are accumulated, some are regulated and obviously the ones that apply to the transport system will not be levied land tax because they never have been.

The Hon. DANIEL MOOKHEY: Yes, but to be fair, they were not regularly owned by a State-owned corporation with a requirement to earn profit.

Mr MORGAN: But they never have been and I am not expecting they will. I would think that the assets that should attract land tax are those which are separately commercially external facing, and that will be developed over time. I do not have a number in my mind as to what that number would be. What I do know is that when you see the accounts for 30 June I think we have started to pick up a land tax liability of smallish proportions.

The Hon. DANIEL MOOKHEY: Indeed, and that is part of the reason why I am exploring this topic, and there is a second reason as well. Is it your view that there is no difference between TAHE accessing this exemption and its predecessor organisation, RailCorp?

Mr MORGAN: Sorry, would you repeat that question?

The Hon. DANIEL MOOKHEY: Is it your view that there is no difference between TAHE accessing this exemption from New South Wales land tax for the \$11 billion worth of land that you own because RailCorp had the same exemption?

The Hon. TREVOR KHAN: This is like the land underneath the rail tracks that you are talking about.

The Hon. DANIEL MOOKHEY: I am asking the question.

Mr MORGAN: No, I would not concur with that point of view at all. I think this is—

The Hon. DANIEL MOOKHEY: Okay, because that was the view that was advanced by your management. Their view was that RailCorp had this exemption, therefore TAHE had this exemption.

Mr MORGAN: Never.

The Hon. DANIEL MOOKHEY: I am trying to understand, therefore, if you have a different view—which, to be fair, I probably agree with you, that you should be paying land tax at some point. Do you have any view as to whether this has been raised or discussed at the board specifically?

Mr MORGAN: Mr Mookhey, the board has talked about the commercial policy framework because we understand, and I am familiar with it from elsewhere obviously—but the question of whether or not we should pay land tax, we do not think that land tax should not be paid because we are really RailCorp with a different name. We think that land tax should be paid into the future in an appropriate way under the commercial framework. So we are not running away from land tax, I can assure you.

The Hon. DANIEL MOOKHEY: Mr Morgan, I 100 per cent agree with you, for what it is worth, on that specific point.

Mr MORGAN: Good.

The Hon. DANIEL MOOKHEY: But the reason I ask you this is do you know how long you have this exemption from land tax for?

Mr MORGAN: I believe that the commercial policy framework transition is about 18 months, but let me confirm that properly to you on notice, if I might.

The Hon. DANIEL MOOKHEY: Thank you. But the reason specifically now I am asking you about this, just to lay all the cards on the table, is have you ever obtained advice as to whether or not that exemption, which is a very valid point, constitutes a subsidy from the State?

Mr MORGAN: Not that I am aware.

The Hon. DANIEL MOOKHEY: As in you are not aware that you obtained that advice?

Mr MORGAN: No, I do not believe that anybody in the organisation has obtained advice, but I am very happy to ask.

The Hon. DANIEL MOOKHEY: Could you? Because one of the key tests that the ABS and the Audit Office applies to determine whether you are genuinely independent is whether or not you are receiving any subsidies from the State, and a land tax exemption on your asset base is worth a lot of money. I do wonder, therefore, whether, at least for the 18 months that you just described, that constitutes a subsidy. Can you shed any light on that or do you need to take it on notice? I probably need to pursue this with some other people as well.

Mr MORGAN: I am happy to take it on notice, but I would think also that in respect of assets that are in the transport system I would not be expecting land tax to be levied on that, but I may be proven wrong.

The Hon. DANIEL MOOKHEY: True, but, see, the ownership has changed and the ownership has changed to a for-profit organisation and it is meant to be competitively neutral. That is the difference about you obtaining the same exemption, however long, versus your predecessor organisation or the previous owner of the assets having it. It is fine for RailCorp to have had it because they were not required to earn a profit and be genuinely independent of government, but TAHE is. Are you aware of any other exemptions under that commercial policy framework in respect to any other taxes?

Mr MORGAN: I said to you I would be very happy to come back with a copy of whatever documentation we have that paints that story. But I mentioned earlier, of course, that the Treasury forwards us a grant to cover the cost of CRN, so not everything within the framework of TAHE in its integral parts—

The Hon. DANIEL MOOKHEY: Yes, but to be fair, the State-owned corporation provides the ability of the State to impose a community agreement. Correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: A community service obligation, I think is one way of describing it. And in circumstances where they have required you to perform a service for the community, they are required to declare in the *Gazette*. Is that correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: I cannot see any declarations in the *Gazette* about the CSO or the community service obligations that you are subject to. Are you aware of any declarations that have been made in the *Gazette* about TAHE?

Mr MORGAN: No, I am not, but, again, that can be taken on notice. But I am not sure that is a declaration that TAHE is required to make.

The Hon. DANIEL MOOKHEY: To be fair, you are not required to make it, TAHE is not required to make it; the Minister is.

The CHAIR: But it being made or not made would have a significant impact on TAHE. If that sets out your community service obligations, whether or not you are required to make the statement or gazette it, the fact of it being gazetted would have an impact on your operations, would it not?

Mr MORGAN: Now we are into the hypothetical Chair issue. I am not sure I am going to give you an answer on that one.

The CHAIR: It was a legal obligation, and once it is gazetted it formalises what your customer service obligations are, but until such time as it is gazetted, they are not formalised.

The Hon. TREVOR KHAN: That is an assertion you make.

The Hon. DANIEL MOOKHEY: No, under the State Owned Corporations Act is it not the case, Mr Morgan, that you are required to follow a community service obligation that you have been directed to follow at the point that it is gazetted?

Mr MORGAN: I agree and my experience of that is within Sydney Water. I am familiar with exactly what you are saying in the context of Sydney Water but I am not aware of anything in the context of TAHE at this point in time—not to say that might not be the case.

The Hon. DANIEL MOOKHEY: You see, I accept your view that in the transition you inherited these obligations. Correct? The community service obligations you effectively inherited.

Mr MORGAN: And whatever would have been in place would have been, yes, to the extent—

The Hon. DANIEL MOOKHEY: But then it has to be renewed under the State Owned Corporations Act. That is the issue: it has to be renewed periodically or otherwise withdrawn, which is why the question about when it is made is really important because usually what is in the *Gazette* contains how long the obligation lasts for or how it expires. Do you agree that is generally your experience?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: But we cannot find any. So your community service obligations, for example, to provide rail services in regional New South Wales, I presume it is indefinite. Yes?

Mr MORGAN: It is certainly government policy at this point in time unless I am advised otherwise.

The Hon. DANIEL MOOKHEY: Yes, unless someone was suggesting to you that we are withdrawing it. Have you made any inquiries about it? Are you expecting any further directions, because I could not see it in the Minister's letter of portfolio expectations that we were talking about earlier either?

Mr MORGAN: I am very happy to take it on notice and to find out what directions, if any, have been provided on that front.

The Hon. DANIEL MOOKHEY: How often are you talking to the portfolio Minister?

Mr MORGAN: I talked to the incoming portfolio Minister a couple of weeks ago; the previous portfolio Minister I spoke with several times a year in a formal sense, with the CEO.

The Hon. DANIEL MOOKHEY: In September last year did you attend any meeting where the then Premier was in attendance?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: Equally, have you attended any meeting in which the then Treasurer was in attendance?

Mr MORGAN: With the portfolio Minister?

The Hon. DANIEL MOOKHEY: You have?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: Just separately.

Mr MORGAN: No. I have seen the Treasurer.

The Hon. DANIEL MOOKHEY: The then Treasurer.

Mr MORGAN: The then Treasurer, in the context of Sydney Water, but not in the context—if I have, it would be in the context of a one-on-one meeting with myself and the acting CEO early in TAHE's existence, which is a very normal, regular meeting that I would ask for with the shareholding Ministers and the portfolio

Ministers throughout the year. But I did not participate in any meetings where they were both present at the same time or the Premier was present.

The CHAIR: Mr Morgan, did the board receive a copy of the two KPMG reports produced last year in relation to TAHE?

Mr MORGAN: I do not recall, Chair, receiving a copy of—there was a range of KPMG reports, I guess: one on accounting advice through Treasury and then the report that Mr Lyon prepared through Transport. Which specifically are you talking about?

The CHAIR: Those are the two I am talking about. One is described as the accounting report, which I think is the one that went through to Treasury, and the other is described as the operating and financial model report that went through to Transport for NSW. You would be aware of the two reports?

Mr MORGAN: Yes.

The CHAIR: Did you receive a copy of each?

Mr MORGAN: I certainly recall receiving a copy of the latter report.

The CHAIR: The operating and financial model report?

Mr MORGAN: Correct, and, in fact, we were involved in a briefing with Mr Lyon at a board meeting on 23 September, I think it was, last year, as it was drawing to some sort of finality. The other report I have read at some stage; whether it was presented to the board or whether the CEO shared it with me I cannot recall.

The CHAIR: Have you provided any form of written response to the operating and financial model report?

Mr MORGAN: I have not, but the management team of TAHE provided input along the way, including a written response.

The CHAIR: Has the board received advice on the conclusion set out in the operating and financial model report?

Mr MORGAN: I do not recall that we sought any advice.

The CHAIR: You are aware the report indicates substantial risks from the TAHE model. Are you aware of that?

Mr MORGAN: I am aware that the report speaks of substantial risks.

The CHAIR: Do you not think it would be prudent, as the chair of the board, to get a response to it from management? I mean, it sets out very significant safety risks from the structure that you are operating. Why have you not got a response from management?

Mr MORGAN: We discussed the report as it was being prepared, to the extent we had sight of it with management. The part of the report which I found particularly valuable was the question of working back to the legislation and the framework to work out where the responsibilities for a whole range of things lie. In respect of safety, I would probably ask my colleague Mr Bourne to comment on how he read and thought about it and interacted with the TAHE management on the report.

Mr BOURNE: My understanding was that the report addressed what was, I think, considered to be the TAHE structure that they were talking about through to 30 June before it was stood up. I think the model then was that TAHE would have a hands-on operating role; it would issue directions and oversee the maintenance and engineering. When TAHE was stood up from 1 July, in fact the decision had been made as we joined the board that, in fact, all those issues, which is to the heart of the maintenance and how it would operate and how much spending would take place, was all put back to the responsibility of Transport for NSW, which was, I think, a significant move from what had been the original intent.

The CHAIR: Have you had a report from management that that contracting out of all of those responsibilities to Transport for NSW addresses the safety concerns identified in the operating and financial model report, Mr Bourne?

Mr BOURNE: I looked into that personally and my view was that the way it was structured was sound.

The Hon. DANIEL MOOKHEY: Your management team has told us that TAHE has entered into a separate engagement with Ms Heather Watson of KPMG. Are you aware of that?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: Did the board have knowledge of it at the time that that engagement was entered into?

Mr MORGAN: I certainly would have.

The Hon. DANIEL MOOKHEY: Was that engagement subject to tender?

Mr MORGAN: No.

The Hon. DANIEL MOOKHEY: Who approached Ms Watson to undertake the work?

Mr MORGAN: I cannot answer that because it was one of the management team; it certainly was not me.

The Hon. DANIEL MOOKHEY: To the extent to which I think we have had separate evidence that this may have been recommended to them by Treasury, does that accord with your understanding?

Mr MORGAN: I do not know. You would have to ask Treasury for that, I do not know the answer to that question.

The Hon. DANIEL MOOKHEY: This took place earlier this year. Is that correct?

Mr MORGAN: Yes.

The Hon. DANIEL MOOKHEY: What was Ms Watson asked to do for TAHE?

Mr MORGAN: For TAHE? My understanding is that she had been part of the development of the model in 2017, updated in 2020, and that there was a requirement to update the model which KPMG had built, with the variables and the assumptions which had developed, and they had developed following the consultations with Mr Lyon and various other people, and that we, TAHE, were keen to see how the model had developed from that earlier one. She was also asked to provide a manual which would allow the management team of TAHE to operate and adjust and inform that model into the future.

The Hon. DANIEL MOOKHEY: Did TAHE either seek or did Ms Watson declare any conflicts of interest?

Mr MORGAN: I do not know the answer to that question. I think that would have been dealt with at the management level.

The Hon. DANIEL MOOKHEY: But given you had awareness of it, did it arise to you or your management team, to the best of your knowledge, or yourself, that Ms Watson was providing advice to Treasury at the same time she was providing advice to TAHE? Did that trigger any sense that there may have been a conflict of interest?

Mr MORGAN: My understanding on the conflict of interest question was that she was updating an existing model and providing information that was already in place.

The Hon. DANIEL MOOKHEY: True, but that was not for you. The original model was not for TAHE, it was for someone else.

Mr MORGAN: Correct. I totally agree.

The Hon. DANIEL MOOKHEY: So hence my question: Did it not occur that, given you are expected to be genuinely independent of government, why was it not a relevant consideration in the decision to directly source Ms Watson that she was providing similar services or had previously provided such services to Treasury, of which you are also meant to be generally independent?

Mr MORGAN: My sense is the opportunity here was for our management to become familiar with a model which had been developed by another party and that in doing so that she would input to that model and that our management guys would be able then to run with it. As part of doing that they were to be assessing the robustness of the model and the assumptions going to the model and bring in their own independent thought to the process. I do not really share a huge concern on that particular issue, I must say, Mr Mookhey.

The CHAIR: Unfortunately, we have run out of time. Mr Morgan and Mr Bourne, thank you for your attendance today and your cooperation with the Committee. I think you have taken a number of questions on notice. The secretariat will assist you with clarifying what the questions are, but I remind you there are 21 days in which to reply and respond to those questions taken on notice.

Mr MORGAN: Thank you, Chair.

Mr BOURNE: Thank you.

(The witnesses withdrew.)

The Committee adjourned at 14:30.