

# VERIFIED TRANSCRIPT

## PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

### Inquiry into Victoria's Audit Act 1994

Melbourne—29 April 2010

#### Members

Mr R. Dalla-Riva

Ms J. Huppert

Ms J. Munt

Mr W. Noonan

Ms S. Pennicuik

Mr G. Rich-Phillips

Mr R. Scott

Mr B. Stensholt

Dr W. Sykes

Mr K. Wells

Chair: Mr B. Stensholt

Deputy Chair: Mr K. Wells

#### Staff

Executive Officer: Ms V. Cheong

#### Witnesses

Prof. K. Jacobs, Australian National University (via telephone).

**The CHAIR**—I declare open the Public Accounts and Estimates Committee hearing on the inquiry into Victoria's Audit Act 1994 and on behalf of the committee I welcome, from the Australian National University, Professor Kerry Jacobs. Members of the public and the media are also welcome.

In accordance with the guidelines for public hearings, I remind members of the public that they cannot participate in the committee's proceedings. Only officers of the PAEC secretariat can approach PAEC members. Members of the media are also requested to observe the guidelines for recording proceedings as they would if in the Legislative Council committee room.

All evidence taken by this committee is taken under the provisions of the Parliamentary Committees Act and is protected from judicial review. However, any comments made outside the precincts of the hearing are not protected by parliamentary privilege. There is no need for evidence to be sworn. All evidence given today is being recorded. You will be provided with proof versions of the transcript to be verified and returned within two working days of receipt. In accordance with past practice, the transcripts will then be placed on the committee's website.

I will now pass to Professor Jacobs for any opening comments and then committee members will ask questions relating to the Audit Act inquiry. I also ask members to make sure that their mobile telephones are turned off, but we won't turn this telephone off, Kerry, I assure you. Over to you for any introductory remarks you might wish to make.

**Prof. JACOBS**—Thank you for giving me a chance to talk to the committee. It is an area that I have had interest in for a long time. It is a very interesting document that you have presented to open discussion.

**The CHAIR**—We have made a range of questions, I suppose, with our document.

**Prof. JACOBS**—Sure.

**The CHAIR**—How do you see the role of the Auditor-General? He is an officer of parliament, but is his independence such that he is almost above parliament?

**Prof. JACOBS**—Yes, that is an interesting question. The nature of the Auditor-General goes back a very long time, so you are looking at auditors of the privy purse and issues like that in the UK. Is it separate from parliament? No. In the Westminster model, the authority of the Auditor-General was always derived from parliament, as opposed to maybe the French model, which is derived from the legal system. So in a sense they are not above parliament but they are really part of parliament.

**The CHAIR**—How do you define, then, the independence of the Auditor-General in the context of being part of parliament?

**Prof. JACOBS**—That is a really good question. It is almost that they are part of the institution. So are they accountable to parliament? To some extent, no. They are accountable for exercising oversight and that is part of a parliamentary function, so I would argue that they are part of the institution rather than part of parliament.

**The CHAIR**—In terms of being one of the three areas, being parliament, the executive and the judiciary, in the broadest sense of 'parliament', you are saying. Is that what you are alluding to?

**Prof. JACOBS**—No. The authority of the judiciary is separate and that has authority from the legal system. The Auditor-General derives his authority from parliament, but that does not mean that he answers to parliament.

**The CHAIR**—So what is the relationship between—and this is one of the things that interests us; the relationship between parliament—and, of course, the public accounts committee has been given the authority of parliament in regard to a whole range of activities in Victoria in respect to the Auditor-General, while at the same time parliament providing through legislation, and ensuring, the independence of the Auditor-General. In the case of Victoria, that independence, of course, is guaranteed in the Constitution.

**Prof. JACOBS**—Sorry, can you rephrase that slightly?

**The CHAIR**—I am just trying to get a further clarification, if it is possible, of the relationship between our committee and the Auditor-General. The Auditor-General has made a number of suggestions. For example, he thinks that he should not have the committee commenting on or discussing with him the terms of reference of his performance audit specifications. He would regard himself as being completely independent and say that there is no need for the parliamentarians to get involved at that sort of level, even though it is in the Victorian act at the moment.

**Prof. JACOBS**—Yes, from the comments I gave, I was inclined to agree with that. The point of an auditor is that they are independent and, in effect, that they can decide how to conduct their work. Even within the private sector, you would argue that the way the audit is conducted is actually the decision of the auditor. In your corporate governance framework you would not imagine a board of directors would be giving direction to an auditor on how to conduct their work, although they are required to meet and have discussion with maybe an audit committee or an audit director. I think, in the same sense, the public accounts committee should be discussing with the Auditor-General their work, their direction and their focus, and I think that is well established within the legislation.

**The CHAIR**—Yes.

**Prof. JACOBS**—But to tell the Auditor-General how they should do it and how they should conduct their work I think is not appropriate.

**The CHAIR**—The difference there is the committee talking to the Auditor-General about what to audit and what is relevant to audit—this is more in the context of performance auditing rather than a financial audit—to ensure that the Auditor-General is addressing subjects that are of relevance to the parliament; not necessarily telling him how to do it, but certainly entering into a discussion about what to audit.

**Prof. JACOBS**—I think there is a fine line between independent and not independent. Where you are giving suggestions to the Auditor-General, that is clearly within the scope of independence. If you are starting to tell the Auditor-General what to do, that's not independent. It would be a very foolish Auditor-General that ignored the advice of a public accounts committee.

**The CHAIR**—Interesting comment. The way it is done here, we think, works quite well. When you discuss the specifications for a performance audit, the Audit Subcommittee meets with the relevant officers of the Auditor-General's Office and there is often a useful exchange of ideas in terms of what might be the emphases, what other things to consider, extending, or perhaps saying, 'This doesn't need to be done because it's already been done somewhere else,' or, 'There's a parliamentary inquiry on X.' They are suggestions rather than directives. That seems to work quite well.

**Prof. JACOBS**—I think the suggestions are a lot safer than the directives.

**The CHAIR**—Absolutely.

**Prof. JACOBS**—Do you mind if I try and put this on speaker? I am getting a lot of echo.

**The CHAIR**—That is fine.

**Prof. JACOBS**—Is that clear?

**The CHAIR**—That is fine. Can you hear us? You are definitely on speaker here. Jennifer, do you want to follow up some particular issues?

**Ms HUPPERT**—I think this gets back to the relationship between the Auditor-General and parliament and the question of the audit of parliament. You have made a recommendation regarding financial audits, but some limitations on other issues that the Auditor-General should be authorised to look into. I

wonder if you could expand on that point.

**The CHAIR**—The Auditor-General in Victoria, and in most other jurisdictions, does not just financial audits but also performance audits, and we face the same issue when it comes to courts. To what extent can an Auditor-General look at the performance? Is this just in regard to administrative matters, rather than the functioning of parliament, and parliament debates, and arrangements themselves?

**Prof. JACOBS**—It was probably a question of practicality more than anything else. The concern was that if the Auditor-General started to address the broader functioning of parliament and the merits of that, the potential for political conflict is quite serious.

**Ms HUPPERT**—I think that raises a definitional issue that we are also addressing when we are looking at the powers of the Auditor-General in relation to the courts. One of the things that we have been looking at is the proposal to extend the power of the Auditor-General to audit the administrative role of the courts. How do you then deal with defining what is administrative and what is judicial? A view has been put that anything to do with any decision making by any judge by itself is necessarily judicial, even though to some people it would appear to be an administrative role relating to the administration of courts rather than the administration of justice. Do you have any views on extending the role of the Auditor-General and possibly how you would draw a line in the sand in the area of courts?

**Prof. JACOBS**—My suggestion on the courts was similar to my comments on parliament: that the administrative issues seem reasonable enough, but if they start to question judicial decision making, you are going to have a war between these different areas. How do you draw a line? I do not have a simple answer for that.

**The CHAIR**—Neither do we.

**Mr SCOTT**—In terms of how a line is drawn, would you see that being done in the legislation or by the Auditor-General themselves or by the parliament or the judiciary, depending on the example? Which body or which mechanism would you see as most able to make those distinctions? Or are you going to shy away from that?

**Prof. JACOBS**—I would shy away. I think it would be pretty confused. A simple principle is probably following the money. The role of the Auditor-General is to follow the public dollar. If there is money spent on the function in the courts, it is reasonable for the Auditor-General to look at how that money is spent, which is not necessarily questioning judicial decision making.

**The CHAIR**—But the judges may well argue that they are involved in the management of the courts and setting the case lists and following them through, using the IT system even, is a judicial function.

**Prof. JACOBS**—You could imagine the useful value-for-money review looking at how the case list is managed—hypothetically.

**The CHAIR**—This committee has recommended that to the Auditor-General.

**Prof. JACOBS**—Good recommendation!

**The CHAIR**—Several times actually. You talked about the acting Auditor-General. You mentioned that this seems to have been abused in the past, undermining the role of the Auditor-General. Did you want to talk a bit more about that?

**Prof. JACOBS**—Yes. It was more from a sense of danger: the danger that someone is placed in an acting role and either that acting role is rolled over or the failure to appoint somebody in the position proper is used to undermine the Auditor-General.

**The CHAIR**—Yes, I see what you are saying.

**Prof. JACOBS**—So if you had an evil jurisdiction that decided they wished to undermine the Auditor-General, you appoint their assistant in the role and you keep rolling that over.

**The CHAIR**—I see what you mean.

**Prof. JACOBS**—If he does something that you do not like, you just can him.

**The CHAIR**—Just take away all their staff!

**Prof. JACOBS**—That one as well. It has been done before.

**The CHAIR**—I think we have covered the independence of the Auditor-General. Performance audits of other officers of parliament is something which we put in because it is not just a philosophical question; there are other officers of parliament. Can you have one officer of parliament reviewing another officer of parliament?

**Prof. JACOBS**—I think I described it as a danger of a dog chasing its own tail.

**The CHAIR**—You did.

**Prof. JACOBS**—The first thing is that I would not require it, because they may actually be quite low risk and you want the A-G to spend the resources on things that are more important. So I would not put it in as a requirement. Secondly, it is another complicated area, particularly if one is required to answer to another.

**The CHAIR**—And all of them ultimately to parliament, although I think in some of them there is not a lot that parliament is involved in, to be quite honest.

**Prof. JACOBS**—It is probably safe to leave it open. An A-G could conduct a review and a parliamentary committee could request a review or initiate their own review.

**The CHAIR**—With the assumption that the way the act as written does not necessarily specify it but it could be assumed by the way the act is written.

**Prof. JACOBS**—I think it would be safest to leave it open.

**The CHAIR**—The Auditor-General's budget.

**Prof. JACOBS**—I did not have a simple answer for that.

**The CHAIR**—It is a perennial and controversial issue, you say. The Auditor-General would like to be completely independent.

**Prof. JACOBS**—Of course.

**The CHAIR**—And just report to the Speaker or the President. At the moment here in Victoria he is required under the act to discuss his budget with this committee and for this committee to provide their views to him, but ultimately the budget is provided under the parliamentary appropriation in the discussions that are held between the executive and the parliament. Can you see anything wrong with that? 'It ain't broke; don't fix it'?

**Prof. JACOBS**—It is broke, but I cannot see a suitable solution.

**The CHAIR**—Another alternative is to provide an open cheque.

**Prof. JACOBS**—That is not really acceptable either, is it?

**The CHAIR**—No, probably not.

**Prof. JACOBS**—I came up with a couple of speculations. I do not have a clear answer here. One thought was maybe an independent proposal that the public accounts committee then accepts or rejects; perhaps some kind of percentage of spending. None of them are really ideal.

**The CHAIR**—No.

**Mr RICH-PHILLIPS**—Are you aware of any alternative funding models?

**Prof. JACOBS**—Mostly it functions the way the Victorian situation does. Certainly having the public accounts committee reviewing and commenting on it is good practice. Beyond that, nothing that I know of. The Victorian context is probably good practice. Whether there are better practices? I do not think anyone has achieved that yet.

**The CHAIR**—We have just let a tender for a performance audit of the Auditor-General and the Auditor-General's Office. In that performance audit tender specification we included that the independent performance auditor of the Auditor-General should do a price review and that would give us a benchmark so that we could know whether the Auditor-General is pricing his services efficiently and effectively.

**Prof. JACOBS**—But coming back to my earlier comment, I will amend myself. There is a second model. You can either fund it from appropriation or you can give the Auditor-General the right to claim back the cost of what they are doing.

**The CHAIR**—That could be interesting on performance. He does claim back the costs of financial audits now, but not performance audits.

**Mr RICH-PHILLIPS**—But that would be a blank cheque too.

**The CHAIR**—An absolutely blank cheque.

**Prof. JACOBS**—Sure.

**The CHAIR**—Like a royal commission—not quite, but essentially.

**Mr SCOTT**—A standard one, yes.

**The CHAIR**—I think it remains a perennial and controversial issue, would you say, Kerry?

**Prof. JACOBS**—That is a good summary.

**The CHAIR**—The employment of ex-auditor-generals: what is your experience on that one?

**Prof. JACOBS**—I know a few of them and they seem pretty capable chaps!

**The CHAIR**—I think that is the message we have been given, yes.

**Prof. JACOBS**—I think I have suggested that there is some restriction on taking work that conflicts with the A-G's role, but it seems a bit tragic to have to ship them out of Victoria for them to be useful.

**The CHAIR**—What do you mean by that? Is it reasonable to be, say, the Auditor-General for seven years and then become the ombudsman for eight?

**Prof. JACOBS**—I think the question is: would the role of ombudsman be in conflict with the role of Auditor-General?

**The CHAIR**—That is what I am asking.

**Prof. JACOBS**—The answer is: not necessarily.

**The CHAIR**—But what you are saying is that they could not necessarily become a head of department?

**Prof. JACOBS**—I think that might be a conflict of interest.

**The CHAIR**—And would it be a conflict of interest to become a member of parliament?

**Prof. JACOBS**—I would put that one back to you. Is that poacher to gamekeeper, or gamekeeper to poacher?

**Ms HUPPERT**—It depends which way you look at it.

**Prof. JACOBS**—I think they worry about this. They have argued about whether they should take a role in the university following their Auditor-General role. I would not see that as a conflict.

**The CHAIR**—Here in Victoria, the universities are of course covered under Victorian legislation; therefore, they are audited by the Auditor-General.

**Prof. JACOBS**—True. Maybe if they were chief financial officer at the university!

**Ms HUPPERT**—That would be a conflict.

**The CHAIR**—Tongue-in-cheek.

**Prof. JACOBS**—Vice-chancellor?

**The CHAIR**—I think chancellor might be the better one. Chancellors have no power! Access by the Auditor-General is an issue we have been struggling with this morning. You have mentioned the 'follow the money' rule, but does that give him carte blanche entree into the premises of contractors?

**Prof. JACOBS**—I think if you take public money, you accept the deal that it comes from the public, so you need to answer for how it is used. So, prima facie, I would say yes, but that depends a little bit on the arrangement.

**The CHAIR**—We have had evidence given to us that having something in legislation in regard to access may well provide a disincentive for companies to tender. Do you see this as a possible disincentive?

**Prof. JACOBS**—I wonder why a company which is taking public money would object to having that followed up? What would they be hiding?

**Mr RICH-PHILLIPS**—Intellectual property. Commercial secrets.

**Prof. JACOBS**—That would be protected, wouldn't it?

**Mr RICH-PHILLIPS**—The argument put to us was that that would be the disincentive: that you would expose the IP of a private sector entity if you had open audit access and the Auditor-General could then report that.

**The CHAIR**—There may well be conflict with the Corporations Act in terms of disclosure.

**Prof. JACOBS**—I think there would be other legal consequences if the Auditor-General exposed intellectual property. But I think the first deal is: if you take public money, you need to accept accountability for it.

**Mr RICH-PHILLIPS**—But everything the Auditor-General reports now is protected, so if he

intentionally or inadvertently disclosed intellectual property, there would be no recourse for the aggrieved party.

**Prof. JACOBS**—Have you seen any evidence to date that, because there is a 'follow the money' principle, that an Auditor-General has undermined this?

**The CHAIR**—We have received evidence that the Auditor-General has found it difficult to obtain some documents, and obtain access, more in relation to public sector corporations than necessarily a public company.

**Prof. JACOBS**—I think honestly the risk is more that these things are used as an excuse to fail to deliver public accountability. If my tax dollar is being spent on some project, it seems reasonable that the organisation is called to account, and I think that is the much higher risk. Organisations that deal with the public sector know that that is the deal. Honestly, it is the easiest money. There is no risk of nonpayment. You are not going to go bankrupt or anything.

**The CHAIR**—There could be a situation where a company was going bankrupt and did not wish to be audited.

**Prof. JACOBS**—I think the failure to be audited implies there is something to hide, and I honestly do not buy the intellectual property or commercial-in-confidence argument, because normally it is a smokescreen for something else going on. I see many more examples of that than of abuse of these areas by an auditor-general.

**Ms HUPPERT**—We have taken some evidence about the operation of the provisions in New Zealand that give their Auditor-General the power to follow the money into private companies. Have you had any experience of looking at other jurisdictions that have that type of power for the Auditor-General and how those provisions operate?

**Prof. JACOBS**—I have not done a specific study of that, so I cannot give you a straight answer. It is a good question, though.

**The CHAIR**—You mention auditing state companies and suggest 25 per cent as the benchmark start, rather than 50 per cent. Any thoughts on that?

**Prof. JACOBS**—I think I was trying to come up with a rule of thumb.

**The CHAIR**—Yes. You suggested more than 25 per cent.

**Prof. JACOBS**—I think with more than 25 per cent you are getting into an argument of public interest. Certainly over 50 per cent you have got an argument of ownership. Between 25 per cent and 50 per cent there is a case to be made, or made against.

**Mr RICH-PHILLIPS**—You are making your argument on revenue, not on control?

**Prof. JACOBS**—I think the 50 per cent control is clear. Where you have control, it should be audited by the Auditor-General. When you have it significantly funded by the state, you have an argument for public interest.

**Mr RICH-PHILLIPS**—Even where there is no equity interest?

**Prof. JACOBS**—It is a question of: what is the public interest here? Should it be done or shouldn't it be done? I think it is an issue of debate rather than a clear answer.

**Mr RICH-PHILLIPS**—Thinking that one through to its full extent, there would now be a number of individuals contracting to government. It is particularly the case in the IT area—Synetix and other agencies—where individuals are hired as contractors and are often employed through their own private companies.



Probably 95 per cent of the revenue would be from the government agency and they are single-employee entities. Presumably you are not suggesting that they should be subject to audit by the Auditor-General?

**Prof. JACOBS**—I think the argument there is that it is not in the public interest that they be audited by the Auditor-General.

**Mr RICH-PHILLIPS**—So it would be a two-stage test? You would not just have the basic metrics; you would have to have the public interest test as well?

**Prof. JACOBS**—I think you need both arguments. I think with the 50 per cent or above ownership, it is clear that it should be audited by the Auditor-General. When you have less than 50 per cent but maybe a significant amount of the revenue, there is a debate: should you or shouldn't you?

**Mr RICH-PHILLIPS**—That is where the public interest test comes in?

**Prof. JACOBS**—That is what I would suggest.

**Mr RICH-PHILLIPS**—And below 25 per cent you would argue there is not a public interest?

**Prof. JACOBS**—There could be, but I think the chance of it is lower.

**The CHAIR**—Kerry, thanks very much for your submission, and particularly for going through all of the various issues. We have not asked you about all of them, but you have not been shy in giving us your views, which is really useful to a committee because we do like to have a range of opinions.

**Prof. JACOBS**—I hate to be boring.

**The CHAIR**—We are not always boring either. There are some interesting issues here, as you can see from the paper that we presented.

**Prof. JACOBS**—It was an excellent paper.

**The CHAIR**—Thank you for that. Some of them are just a bit of kite-flying, but that is okay; we needed to put the issues out there so that we could try and generate some responses and thinking about this, which is pretty central, we think, to any public administration.

That concludes the consideration of the evidence provided by Professor Jacobs and I thank him for his participation. It has been a very useful session. We do not have anything taken on notice, but we will send you the transcript in due course. Thanks very much, Kerry. Good to talk to you again.

**Prof. JACOBS**—Thank you.

**Witness withdrew.**

**Committee adjourned.**