

Australian Government Presentation to The Policy Dialogue on Governance in China

“The Transparency and Accountability of Australia’s State-Owned Enterprises”

Introduction

Following a number of highly visible corporate collapses around the world in recent years, scrutiny of corporate governance practices has become a major concern for governments, commercial organisations and shareholders. This has, in turn, focused particular attention on the performance of commercial entities that are government-owned, or SOEs as they are widely known. By virtue of their government ownership, SOEs are expected to practice the highest standards of corporate governance.

Governance is, in essence, about ensuring the success of an entity. Transparency of SOE operations, planning and reporting, and a clear accountability framework which also sets out the roles of Government (as owner), Ministers, Boards and senior management of SOEs, are fundamental principles that underlie good governance and the Australian Government’s governance framework for SOEs. Today I intend to discuss the Australian Government’s SOEs, the current governance framework that has been developed and how this imbues transparency and accountability in practice for Australia’s SOEs. I will close with some insights into future developments in the SOE governance regime in Australia.

Australia's SOEs

The Australian Government currently has a number of SOEs (the most commercial of which are known as 'government business enterprises') covering a diverse range of commercially focused activities in industries such as communications, health and defence. For example, Telstra (Australia's leading telecommunications provider), Medibank Private (the nation's leading private health insurer) and the Australian Postal Corporation. To clarify, under Australia's federal system of Government when referring to the Australian Government's SOEs I am only referring to those enterprises owned by the Commonwealth Government, not by the State Governments. The States own many SOEs completely independent of the Commonwealth Government and apply State Government governance policy to them. Almost all of the Australian Government's SOEs are fully owned by the Government. Australia has substantially reduced the size of its Government-owned commercial sector over the past two decades through the privatisation of enterprises across industries including airlines, airports, banks and rail. Even throughout this period of substantial privatisation there has been a strong focus on improving the transparency and accountability regime for SOEs. The need for good governance principles like transparency and accountability are universal and we appreciate that these principles are equally applicable to both a small Government-owned commercial sector, like Australia's, and a much larger public commercial sector like China's.

The current transparency and accountability regime applicable to SOEs (the details of which I will discuss in greater detail in a moment) is a product of some particularly important reviews undertaken over a number of years. The Australian Government is committed to the ongoing review and development of governance principles

applicable to SOEs. Notably the Government also conducts reforms of the governance regime applicable to the private sector, and Government entities not involved in commercial operations, through legislation and regulation. (For example the nine CLERP reforms and Financial Framework Legislation Amendment Act.) The Australian Government commissioned the *National Commission of Audit* in 1996 with a mandate to review all services provided by Government and, amongst other things, assess which of these services provided core and non-core functions of Government. In 1997 a review of the governance arrangements for SOEs, known as the Humphry Review, was also commissioned by the Government. This was a significant milestone in establishing the current governance regime for the Australian Government SOEs.

Governance framework for SOEs

Australia's governance framework is primarily based on the principles embodied in the Stock Exchange listing rules for Australian public companies and the obligations imposed by the Corporations Act. The key elements of this framework were implemented following the previously mentioned reviews of 1996 and 1997. The current governance arrangements for SOEs were established in 1997, when legislation was formed to govern those entities that are legally and financially separate from the Commonwealth (including all SOEs). This legislation is known as the Commonwealth Authorities and Companies Act (CAC Act). The CAC Act is drafted on the basis of applying legal principles rather than prescriptive rules about what can and cannot be done, and broadly mirror provisions of the equivalent legislation for the private sector, the Corporations Act. The other main document is the Government's current governance arrangement policy for SOEs, which was established in 1997 and

is entitled the *Governance Arrangements for Commonwealth Government Business Enterprises*.

Where the CAC Act legislates the basic reporting and accountability framework for SOEs the Governance Arrangements prescribes further details of reporting requirements and processes SOEs should undertake. The Governance Arrangements also outlines the Australian Government's key objectives with regard to its SOEs as: ensuring they are operating efficiently, pricing efficiently, earning a commercial rate of return and operating within their mandated industry sector. Both the CAC Act and the Governance Arrangement are publicly available, further promoting transparency of the Government's objectives for SOEs and how enterprises report their performance to the Government.

There are other more general elements of the Government's governance framework that provide additional layers of transparency and clarification of accountabilities for SOEs in Australia. SOEs have either a company constitution or enabling legislation, depending on the form of the SOE, and these documents are legally binding. The constitution or enabling legislation usually prescribes the SOE mandate and other details pertaining to the enterprise, such as Board structure and borrowing restrictions. Where Ministers have specific powers of direction over SOEs, these are also outlined in constitutions and enabling legislation. These Ministerial directions are required to be either disclosed in Annual Reports or tabled in Parliament. Guidelines from the OECD, Australian Stock Exchange and Australian National Audit Office also all expand the scope of the governance regime by providing guidance on best practice principles of corporate governance.

Beyond the formal requirements I have outlined, transparency and accountability of SOEs is also promoted through informal means, such as interaction between stakeholders. Frequent meetings that are held between the Board, and senior management, and relevant departmental officials on the performance and strategic issues facing the enterprise effectively maintains a ‘no surprise’ approach between parties and enables departmental officials to provide timely and informed advice to Ministers. Ministers also face scrutiny through practices that promote continual accountability. Questioning of the SOEs commercial activities and the performance of SOEs can occur at both a Parliamentary and public level. On the Parliamentary level this scrutiny predominantly takes the form of Parliament Question Time and the Senate Estimates Process, which involves Senate Committees questioning relevant Ministers and senior departmental officials.

Transparency and accountability in practice in Australia

To ensure transparency and accountability it is important to clearly define the boundaries, roles and responsibilities of stakeholders. This also promotes open and positive communication between parties. It is also particularly important for clarification of the objectives and targets for the SOE. This ensures that there is transparency in how public enterprises perform and who is ultimately responsible for the performance. Senior management of SOEs report internally to Boards. Boards are ultimately responsible for an enterprise’s day-to-day management and the enterprise’s performance to the relevant responsible Ministers. Ministers are accountable for SOEs to the Parliament.

Transparency of SOEs is ensured through rigorous reporting and planning requirements, outlined in the CAC Act and the Governance Arrangements. The key reporting requirements are progress reports and Annual reports. These reports are required to be produced under the CAC Act and the Governance Arrangements provide some further detail on the requirements of the reports. Progress reports may be produced on either a quarterly or six-monthly basis and are provided to Ministers on a confidential basis. That is, these reports are not made public due to the enclosed commercial information. The other key report that is produced is the Annual Report. This report reflects the performance of the enterprise for the financial year and is tabled in Parliament and is publicly available.

The key planning documents are the Corporate Plan and Statement of Corporate Intent. These documents set out the strategic and financial plans of the SOE over a forward period of between 3 and 5 years. As part of the Corporate Planning process, Key Performance Indicators, of both a financial and non-financial nature, are set in consultation between the SOE and departmental officials representing the responsible Minister. The Corporate Plan, as with the progress report, is a commercially sensitive document and is provided to the responsible Ministers. The Statement of Corporate Intent is a publicly available summation of an SOE's Corporate Plan. The SCI provides general information on the Government's objectives, key targets and the SOE's strategies for the business to the Parliament and public. Boards of SOEs are accountable for the performance of the enterprise against the targets set in the Corporate Plan and are required to report against these targets in progress reports to Government.

In addition to the forementioned framework, another important policy in promoting greater transparency for SOE's in the Australian context is having a well defined and publicly available policy in relation to community service obligations (CSOs). By CSO we mean: where a SOE is specifically directed to conduct an activity that it would not elect to do on a commercial basis (or that it would only do commercially at higher prices) and the government does not, or would not, require other organisations in the public or private sectors to undertake or fund. An open and transparent CSO policy, which encompasses appropriate costings ensures that the full effect of these CSOs on the SOE's operations can be identified, enabling a more meaningful assessment of the SOE's overall performance. It also reduces the potential for cross subsidisation between CSO services and the commercial business operations of the SOE. A best practice approach would be for CSOs to be funded from the budget with costs determined as if it were part of a commercially negotiated agreement.

The CAC Act also requires all SOEs to be independently audited by the Australian National Audit Office. This is another important element of the governance framework for SOEs that ensures transparency.

Correspondence between the responsible Ministers and members of GBE Boards is also an important element of the GBE governance framework. Such correspondence can be used to ensure that there is clarity in the roles and responsibilities of each party. In agreeing to become a Board member of an SOE, directors are advised in correspondence of the shareholder Ministers' expectations. This would include that directors implement the requirements of the Government's policy for SOEs, and adhere to the GBE's enabling legislation or constitution and the CAC Act.

The Minister for Finance and Administration is the responsible Minister for advice relating to SOEs, although for some SOEs he shares his responsibility with the relevant portfolio Minister. The Government Businesses and Private Financing Advice Unit (GBPFAU) is a unit in the Department of Finance and Administration that provides advice to the Minister for Finance on SOE matters. Our key functions are to provide strategic and analytical advice to the Minister for Finance and Administration, by engaging with the Boards and senior management of SOEs, analysing their operations and their environment, and consulting with stakeholders. We also action the Minister's decisions including communicating his objectives and ensure that there is a robust and sound governance framework in place by initiating change and contributing to policy development.

GBPFAU largely facilitates the relationship between the SOE and the responsible Minister. We do this by actively overseeing the Australian Government's investment in its SOEs and providing strategic advice to the Minister on various matters including:

- Performance, operations and financial returns of the SOE;
- the reporting and accountability arrangements that facilitate active oversight by the shareholder; and
- action the Minister may wish to take in relation to the strategic direction of its SOEs where it prefers a different direction from the one proposed by the enterprise.

This centralised unit, established in 1997, which oversees the Australian Government's shareholdings in SOEs, is a particularly important and practical element in ensuring their transparency and accountability. We analyse the businesses

and build strong open relationships with those that run them to ensure they are effectively monitored and to provide sound, timely advice to the Government.

Issues, room for improvement, international scenario

The Australian Government recognises that publicly listed companies are accountable to their shareholders for their performance. The governance framework in place for SOEs is intended to mirror the discipline and rigour to which publicly listed companies are subject. The additional obligations imposed on SOEs under the governance framework, are intended to substitute for stock market discipline, as well as to support the Government's policy that commercial entities should not receive a commercial advantage by virtue of their government ownership. The governance framework is not however, intended to prevent SOEs from operating efficiently and effectively, but rather it should promote improved operational performance of SOEs.

Today the Australian Government continues to review and implement changes to the governance regime for SOEs. During 2005/06 the recommendations of a recent whole of Government review (known as the Uhrig Review) are being implemented across many Government entities. This requires the governance arrangements of these entities to be reviewed against two detailed governance models and is intended to assess whether Government entities have appropriate governance arrangements in place. Implementation of this review gives the Government the ability to improve the performance of its entities and their accountability frameworks where necessary.

Changes in the political, economic, industrial and legal environments in which SOEs operate, inevitably lead to the need for change in how they are monitored and held

accountable. Accordingly, the Australian Government continually reviews the appropriateness of its governance arrangements for SOEs. This continual reassessment guides the Australian Government's approach to governance with the intent of maintaining a governance regime for its SOEs that is robust and clear but also appropriately flexible for SOEs to operate within.

To conclude, the Australian Government's governance framework for SOEs is based around two key documents in the CAC Act and the Governance Arrangements, however further legislative requirements and guidelines adds depth to this framework. Transparency and accountability of SOEs are promoted in this regime principally through: clearly defined roles and responsibilities of stakeholders; a prescriptive reporting and planning regime; and open correspondence and strong relationships between the SOEs, Departmental officials and responsible Ministers.