Performance Audit of the Regional Partnerships Programme: Volume 3–Project Case Studies

Department of Transport and Regional Services
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1. Upgrade Sawmilling Capacity to Meet Export Demand and AUSGUM Furniture Expansion projects

This case study examines the application development, assessment, approval and contract management processes undertaken in respect to two applications for Regional Partnerships funding made in September 2003 and March 2004 by the same applicant. The case study highlights the importance of the department appropriately scrutinising applications in order to fully inform the Ministerial decision-maker of the outcomes likely to be achieved with any funding, the value for money those outcomes would represent, and the extent to which the requested funding would make efficient and effective use of the public money. As at August 2007, the department was examining its options in relation to the $117 000 (plus GST) in Regional Partnerships funding paid in May 2004, for which a financial acquittal had not been received in accordance with the terms of the Funding Agreement.

First application submitted in September 2003

1.1 A Regional Partnerships application for RP00203 Upgrade Sawmilling Capacity to Meet Export Demand project was signed on 26 August 2003 by the Managing Director of Mettalodge Pty Ltd, a private company trading as AUSGUM Furniture and the Emerald Sawmilling Company (AUSGUM). The application, submitted by the Central Highlands Development Corporation Ltd (CHDC) on the applicant’s behalf, was received by DOTARS on 16 September 2003. CHDC had also authorised to undertake subsequent discussions with DOTARS on the applicant’s behalf.

1.2 At the time of the application, AUSGUM operated a sawmill at Emerald in Queensland. In December 2000, it had started manufacturing outdoor furniture using Australian hardwood cut at the sawmill. According to the signed application, the Regional Partnerships funding was being sought to assist the company in undertaking the next stage of development in implementing a business plan to expand its furniture manufacturing capacity. The application described the project as follows:

For the next stage of development in pioneering this mode of processing our Australian native hardwood the Company will undertake the following:

- Expansion of the furniture manufacturing facilities.
- Upgrading our logging system to handle shorter logs.
Upgrade our sawmilling system to handle shorter logs.

Increase our solar kiln drying capacity.

This project is focusing on the expansion of the furniture manufacturing facilities through the installation of a large production capacity CNC Point to Point Machining Centre and associated dust extraction.

1.3 The application identified a project start date of October 2003, with a completion date of January 2004. The project methodology set out in the application stated that the purchase and installation of the new equipment was ready to commence as soon as funding was approved.

1.4 The application identified a total cash budget for the project of $297,936 (GST exclusive), of which $130,000 (plus GST) was sought from Regional Partnerships. The applicant proposed to contribute the remaining cash of $167,936 (56 per cent). The main cost item identified in the project budget was $222,557 (plus GST) relating to ‘Purchase lease cost’ of a Biesse Rover 30L2 machining centre.

**Genesis of the Regional Partnerships application**

1.5 AUSGUM started the furniture manufacturing aspect of its operations at Emerald in late 2000, with the purchase and installation of equipment including a Biesse Rover 27 machining centre and a larger capacity solar kiln. In November 2001, it unsuccessfully applied for a grant of $1.132 million for a project to upgrade its operations through the Farm Innovation Program.

1.6 AUSGUM’s Business Plan 2003–2005, dated 31 December 2002, provided to DOTARS in support of its Regional Partnerships application, set out an upgrade plan that closely reflected the activities set out in an unsuccessful 2001 Farm Innovation Program application. It also identified an intention to fund the purchase of new equipment through additional capital raised via a share issue, complemented by equipment and debt financing where appropriate.

1.7 The business plan objective of having the new equipment ordered, installed and running at full capacity by August 2003 was not achieved. On the evidence available, at that time, the company had not ordered the new equipment, nor had any additional capital investors been identified to fund the acquisition. As at August 2003, the furniture operation had 16 employees and operated with the Biesse Rover 27 machining centre acquired in late 2000.
1.8 At the time of applying for Regional Partnerships funding, the company was also in the process of establishing another furniture factory at Gympie. The applicant subsequently advised DOTARS that the strategy for establishing operations at Gympie commenced on 9 August 2003. At that time, there is no evidence of the company having lodged an expression of interest or otherwise entered into discussions in relation to any possible Regional Partnerships funding with the Central Queensland ACC (CQACC).

_Furniture factory and manufacturing equipment destroyed by fire_

1.9 The company’s Emerald furniture factory, including the existing Biesse Rover 27 machining centre, was destroyed by fire on 12 August 2003. The available evidence is that this was the event that gave rise to the company making an application for Regional Partnerships funding. A document prepared on 12 December 2003 by the chair of the Central Highlands sub-committee of the CQACC, and provided to DOTARS on the same day, indicated that:

- the applicant committed to acquiring an available second-hand Biesse Rover Model 30L2 immediately after the fire, with the opportunity being taken to upgrade to a higher capacity machine than the Biesse Rover 27 previously operated. The ACC encouraged that course;
- the applicant was also contemplating acquiring a replacement Model 27;
- the question of a Regional Partnerships application arose because the applicant was under-insured; and
- the amount of funding to be sought from Regional Partnerships was determined through a negotiation process involving the applicant; the Federal Member for Maranoa and the CQACC.

1.10 In November 2007, AUSGUM advised ANAO that:

Emerald Sawmill / AUSGUM pioneered the most advanced processing of Australian Hardwoods in the Country. International and National Awards including National Furniture Manufacturer of the Year were significant achievements for the business and the region within a short period of time.

The business was taken from 3 people when purchased to in the order of 40 when in August 2003 a devastating fire destroyed the whole furniture manufacturing facility including large quantities of stock prepared for dispatch in the forthcoming ‘season’. Through the guts, determination and significant and appreciated support of local and regional entities the business recommenced re-building.
Amongst other significant related investment this was undertaken via the procurement of 2 virtually identical items of necessary equipment being Biesse Point to Point Machining Centres for $245,000 and $187,000 respectively. The timing of the first purchase was absolutely critical otherwise all workers other than those engaged in the sawmill activities would have lost their jobs. By being proactive and procuring this machine as quickly as possible we were able to retain workers but to the detriment of the funding protocol which rejected the application submitted by the local Regional Partnership personal on behalf of the Company due to retrospectivity issues.

Concurrently to the above events unfolding the following was experienced:

- The demographics of Emerald and the region were undergoing significant change with the increase momentum of the resources and mining industries. Consequently we experienced significant difficulties in retaining staff and further recruitment processes. Meetings were even held at the time with members of the Regional Partnership program outlining these issues.
- The Queensland State Government commenced actions to shutdown large portions of the native hardwood logging industry with the Emerald Sawmill the first to experience this process and be ultimately shutdown after months of uncertainty and negotiations.

In light of the above it was determined that the timber processing business could not be maintained at Emerald and was subsequently transferred to Gympie where it now operates and at this point in time employees 27 workers utilising the equipment purchased after the fire in order to re-commence and expand operations.

1.11 On 19 September 2003, DOTARS wrote to the applicant acknowledging receipt of the application and advising that more clarification and development was required in relation to key criteria under the Regional Partnerships Guidelines, including in regard to:

- value for money for the Commonwealth in terms of community and regional benefit;
- the outcomes, including employment, that would occur as a result of Commonwealth funding, supported by realistic evidence;
- competitive neutrality; and
- evidence substantiating applicant co-funding, sales forecasts and sustainability of resources.

1.12 The applicant was advised that assessment of the application would be placed on hold until the additional information had been received.

Replacement machining centre already acquired

1.13 The Regional Partnerships Guidelines state that project proposals that are requesting funding for retrospective costs are not eligible for funding. Both
the departmental and ACC Internal Procedures Manual current at the time of this application provided the following guidance:

**Non-retrospective requirements in relation to project expenditure**

The Commonwealth will not fund retrospective costs in relation to a project. Regional Partnerships funding cannot be used to pay any project costs incurred prior to the date of the Funding Agreement being signed by both parties (applicant and Commonwealth).

1.14 On 22 September 2003, DOTARS advised the CHDC, in the applicant’s absence, that it had come to the department’s attention that an order for the timber machining centre was already in place. DOTARS requested further information on the issue, advising:

As the supply/purchase of the machine is a key component of the project outlined in the application, it is necessary for us to have the entire picture in relation to the overall project and subsequent outcomes for the Commonwealth. Any information clarifying the purchase of the machine outside the above questions would be welcome. You will understand that it is clearly identified under the Regional Partnerships guidelines that retrospective funding is not allowable hence the need to clarify the above to determine whether some other support for the project might be more suitable if retrospectivity is deemed an issue.

1.15 On 26 September 2003, the CHDC advised DOTARS that:

- on 14 August 2003 Allwood Biesse Australia had informed the applicant that it would take 6-8 months to manufacture and ship a new machining centre from Italy to Australia, and that Allwood had suggested that a second-hand demo/showroom machining centre was available from Melbourne and that this would be the best solution;

- the order was placed on 18 August 2003, with delivery to Emerald having occurred on 11 September 2003. The CHDC advised DOTARS that the applicant had informed it that assembly of the machining centre was underway; and

- no deposit had been paid as the applicant was acquiring the machining centre through a five year finance lease with monthly payments and a residual payment. The lease agreement had not yet been signed.

1.16 Despite its relevance, the fire and its impact on the need to source a new machining centre was not referred to in the advice provided to DOTARS.
1.17 The CHDC provided further advice to DOTARS on 21 October 2003, which advised in part:

Q. Would the purchase go ahead without Commonwealth funding?

A. Difficult to answer. Ausgum Furniture have placed high priority on the Commonwealth funding and if this failed it would face a desperate situation. Ausgum would most certainly investigate contingency funding in order to save the business from further impacts (loss of export contracts, loss of jobs, loss of reputation, loss of national industry leader etc). Commercially, Ausgum has considered all funding options and in this instance has placed high priority on the Regional Partnerships Program as their first choice…

Job outcomes:

20 direct employment outcomes will come of this export capacity development program. Additionally, this is on top of the re-employment of the 15 previous employees put-off as a consequence of the recent fire. So collectively, 35 direct employment outcomes will be attained…

Role of local Federal Member

1.18 On the day of the fire, the Member for Maranoa issued a Media Release stating that he was committed to pursuing every possible avenue of Federal Government financial assistance to help the owners re-establish the operation. The Member subsequently played an active role in the applicant seeking Regional Partnerships assistance to acquire a replacement machining centre, including in relation to determining the quantum of the funding bid. On 27 August 2003, the Member for Maranoa provided a letter of support for the Regional Partnerships application to the applicant for inclusion with its application. There was no reference to the 12 August fire at the applicant’s premises in the Member’s letter of support.

ACC’s role

1.19 The advice provided to DOTARS by the CQACC in December 2003 was that the Member for Maranoa’s Office had been advised on 2 September 2003 that the application had been ‘passed by the ACC’. It is unclear what decision of the ACC that advice referred to. ANAO’s review of documented CQACC decisions did not identify any record of a decision being taken in relation to the AUSGUM application on 2 September 2003, including no record of:

- a meeting or out-of-session discussion at which a vote was taken; or
- the names and votes of those who participated in the decision.
1.20 The Minutes of the CQACC Management Committee meeting of 10 October 2003 recorded the following in respect to the application:

Asgum: Moved by [one member] and Seconded by [another member]. Carried.

1.21 The Minutes did not record that a vote on the application had occurred at a previous meeting or that the Minutes were confirming an out-of-session decision taken at an earlier date.

1.22 The CQACC provided comments on the application to DOTARS on 3 November 2003, via facsimile. The departmental assessment was provided to the then Parliamentary Secretary on 17 November 2003. The ACC comments provided to the then Parliamentary Secretary advised that the ACC recommended the project and assessed it as a high priority for its region.

1.23 The ACC subsequently entered comments on the application into TRAX on 6 and 14 January 2004 (one month after the then Parliamentary Secretary had put the project on-hold – see further discussion below). Both the November and January versions of the ACC comments rated the project as ‘recommended and a high priority’, but the comments entered into TRAX in January 2004 were not the same as the comments originally provided in November 2003. In particular, the 3 November 2003 comments had made no reference to the fire or to the project being at least partly directed at re-establishing the business, rather than being solely focussed on expansion. The January 2004 comments, provided after those matters had come to the department’s attention, did make reference to the fire.

1.24 In addition, neither version of the ACC’s comments made any reference to the applicant having already acquired the equipment that was the subject of the application or commented on the question of the application’s eligibility in relation to retrospectivity.

ANAO conclusion

1.25 It is important that, in carrying out the dual roles expected of them under the Regional Partnerships Programme, ACCs ensure that all applications they support for Regional Partnerships funding are eligible under the Programme Guidelines, and that the comments provided in relation to an

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698 ACC comments are normally entered directly into TRAX. A DOTARS file note indicates that the comments were provided via fax on this occasion due to an ongoing error in TRAX.
application provide the Ministerial decision-maker with all relevant information that is known to the ACC.\footnote{On 29 August 2003, DOTARS advised the then Minister for Regional Services, Territories and Local Government that: ‘We have noticed that some ACCs are recommending projects for funding under Regional Partnerships and rating them as a high priority even though they clearly do not meet the programme guidelines….The Department will shortly be writing to all ACCs re-emphasising the critical role they have in providing advice to the Government on the quality and priority of projects from their region, and the importance of prioritising given the limited funds available this year. ACCs will also be reminded that projects must meet the Regional Partnerships guidelines before they can be recommended for funding by the ACC.’}

**Departmental assessment**

1.26 The departmental assessment of RP00203 recommended that the project not be approved due to the questions relating to value for money and retrospectivity arising from the applicant’s decision to proceed with acquiring the machining centre prior to applying for funding (see Figure 1.1).

**Figure 1.1**

**DOTARS recommendation that funding not be approved for RP00203**

<table>
<thead>
<tr>
<th>Other Considerations</th>
</tr>
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<tbody>
<tr>
<td>We understand that a new machine centre has been delivered to the company’s Emerald premises and that the company plans to enter into a 5-year lease/purchase arrangement with the vendor. At 30 September 2003, this lease/purchase agreement had not been signed by the company. Nonetheless, the fact that the machine has been transported all the way from Melbourne and delivered to Emerald suggests that some form of agreement has been entered into for the acquisition of the machine centre. By entering into such an arrangement, the company has demonstrated an intention to acquire the machine centre even in the absence of Regional Partnerships funding. This raises questions about the company’s need for Regional Partnerships support. Further, funding this project now, when the machine centre has already been delivered to the company’s Emerald site, may be perceived as retrospective funding. Retrospective funding is precluded under the Regional Partnerships guidelines.</td>
</tr>
</tbody>
</table>

**DOTARS Recommendation**

Not Recommended

Source: DOTARS assessment submitted to the then Parliamentary Secretary on 17 November 2003.

1.27 Apart from that issue, however, DOTARS assessed the application as satisfying each of the Regional Partnerships criteria, subject to confirmation of the applicant’s cash funding. However, the department did not adequately assess a number of aspects of the application.

1.28 In particular, a copy of the five year finance lease agreement under which the applicant would be acquiring a Model 30L2 machining centre (serial number 95258) had been provided to DOTARS on 2 October 2003. The lease
agreement provided for 60 monthly rental instalments of $2,831.91 (GST inclusive), a residual value of $59,895 (GST inclusive) and a $200 documentation fee, giving a total acquisition cost of $230,010 (GST inclusive) (see Figure 1.2).

Figure 1.2
Finance lease agreement for Model 30L2 machining centre

1.29 The Regional Partnerships application stated that the purchase lease cost for the machining centre to be acquired would be $222,557 (GST exclusive), and requested that the full amount of Regional Partnerships funds of $130,000 (plus GST) be paid in the first month of the project, for the milestone ‘Contract purchase of equipment.’ The application proposed that the applicant would provide $92,557 in the first month of the project towards the purchase of the machining centre.

1.30 In its assessment of the application against the partnerships and support criterion, DOTARS did not address the mismatch between the Regional Partnerships Programme being asked to contribute $130,000 (plus GST) in the first month of the project and the timing of the applicant’s financial contributions to the acquisition. Specifically, the Regional Partnerships
Upgrade Sawmilling Capacity to Meet Export Demand and AUSGUM Furniture Expansion projects

Programme was being asked to provide sufficient cash up front to fully fund the first 50 of the 60 monthly payments. Applicant funds would not be required until the fifth year of the lease (in order to fund the last ten monthly payments as well as the residual payment of $59 895 (plus GST)). Nor did the departmental assessment provided to the then Parliamentary Secretary comment on the inadequacy of the documentation the applicant had put forward as evidence of confirmation of proposed bank finance other than to indicate that satisfaction of the criterion was subject to the applicant providing such confirmation.

1.31 The department’s conclusion that the application satisfied the applicant viability criterion was based on documentary evidence provided by the applicant, including the December 2002 business plan and cash flow forecasts, and industry awards won. However, ANAO notes that the following comment recorded in the Regional Office assessment of this application was omitted from the assessment provided to the then Parliamentary Secretary:

Evidence of cash co-funding is inadequate. The applicant risk to the Commonwealth is therefore assessed as MEDIUM. For reasons detailed throughout this assessment, this application will not be recommended, so only a basic assessment of the proponent viability has been undertaken. [ANAO emphasis]

1.32 The departmental assessment recognised that whether the increase in demand, and resulting increased employment of 20 new positions over the following two to three years, claimed by the applicant would actually occur was less than clear and predominantly based on expressions of interest in the company’s products at overseas trade shows. However, the department concluded that the application satisfied the outcomes criterion because:

at a minimum, the project is expected to allow the 15 mill workers previously laid-off as a result of the fire to be re-employed much sooner than would otherwise be the case.

1.33 The department did not advise the then Parliamentary Secretary that the applicant had not mentioned the fire in its application and, therefore, had

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700 DOTARS also did not examine why the GST exclusive acquisition cost identified in the application was $13 457 more than the GST exclusive cost identified in the Finance Lease Agreement.

701 On 19 September 2003, the applicant had been asked to provide evidence of its co-funding. The only ‘evidence’ provided was a letter from its bank, dated 28 October 2003, to the applicant which stated: ‘The [bank] has managed Ausgum Furniture’s financial matters since the year 2000. To date we can confirm that Ausgum has honoured arrangements with the [bank].’ Although the Regional Office assessment of the application had identified this deficiency, it was not identified in the departmental assessment provided to the then Parliamentary Secretary by National Office.
not identified the re-employment of staff as an outcome that would be achieved from the Regional Partnerships funding. The issue of the fire had only come to the department’s attention when making inquiries in relation to information that the machining centre had already been ordered.

**ANAO conclusion**

**1.34** Although the department did not recommend this application for funding due to the retrospectivity issues, its approach to assessing an application of this nature did not ensure its advice to the then Parliamentary Secretary properly reflected the value for money that would be provided to the Commonwealth should the Parliamentary Secretary choose to approve funding. Issues that were not appropriately scrutinised in the department’s assessment of this application were similarly reflected in its assessment of a later, successful application from the same applicant, as is discussed further below.

**Decision-making process**

**1.35** The then Parliamentary Secretary did not agree with the department’s recommendation that the application not be approved. Instead, on 5 December 2003, the Parliamentary Secretary directed that it be put ‘on hold’ and requested that the department investigate options with the applicant (see Figure 1.3).
**Figure 1.3**

**Decision by the then Parliamentary Secretary to place the application for RP00203 on hold, rather than not approve funding**

<table>
<thead>
<tr>
<th>RECOMMENDATION:</th>
</tr>
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<tbody>
<tr>
<td>That you agree to the recommendations at Attachment A and sign the letters to the successful applicants, local Members and ACC Chairs advising your approval under Regional Partnerships (Attachment B).</td>
</tr>
</tbody>
</table>

![Image of decision document](image_url)

Source: DOTARS’ record of decision by the then Parliamentary Secretary to disagree with the department’s recommendation that RP00203 be not approved, placing the application ‘on hold’ on 5 December 2003. [Names deleted by ANAO]

1.36 The purpose of putting the application on hold and requiring the investigation of options with the applicant in December 2003 is unclear, given that it had been established that the equipment for which the application under consideration had sought funding had been installed at the applicant’s premises nearly three months earlier. Inquiries made by DOTARS in relation to the then Parliamentary Secretary’s request appear to have given rise to the 12 December 2003 ACC report referred to earlier.

1.37 Although the then Parliamentary Secretary had yet to take a decision in relation to this application, it appears that the local Member had been advised that it had been unsuccessful and had advised the ACC and applicant of that outcome. This is indicated in an email received by the CQACC Chair on 18 December 2003 from the Office of the Member for Maranoa, which referred to the ACC having requested that it discuss the lodgement by the applicant of a request for review of the decision. The Member’s Office advised the Chair that:
I have just spoken with [the applicant] at [an ACC member’s] request to discuss the revision of a letter from him to [the then Parliamentary Secretary] to request a review of his application and supply as much relevant documentation to support his request ASAP...

[The applicant] is also extremely upset that until my conversation with him this morning, no-one had advised him that the application had been rejected by the department, only that there were problems with the application...

[The applicant] has asked if a postponement in the request for review can be made until after his export order has been completed in January, as all his time is now dedicated to ensuring this is met on time.

1.38 On 19 December 2003, the then Parliamentary Secretary wrote to the then Minister for Transport and Regional Services seeking the Minister’s agreement to waive the Regional Partnerships retrospectivity guidelines in the case of this application. 702 On 1 March 2004, DOTARS recommended to the then Minister that he not agree to waiving the retrospectivity guidelines as it would set a precedent for other applications and would be inconsistent with other applications that had already not been approved due to retrospectivity.

1.39 DOTARS advised the then Minister that it understood that the applicant was developing a new, related project for which it planned to seek Regional Partnerships support, and that the new project did not involve retrospective funding. The then Minister was advised that this new project involved the purchase of a second machining centre for the applicant’s Gympie plant, and that it would be assessed against the Regional Partnerships Guidelines in the normal way as soon as a formal application was received.

1.40 On 4 March 2004, the then Minister wrote to the then Parliamentary Secretary advising that he was unable to accede to the request to waive the retrospectivity Guideline. The Minister further noted that the applicant was developing a new, related project which may be more suitable for support under Regional Partnerships.

1.41 On 16 March 2004, DOTARS wrote to the applicant advising that funding had not been approved because of the consideration of perceived retrospectivity. However, there is no record of the then Parliamentary Secretary making a formal decision to take the project ‘off hold’ and not approve funding.

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702 A copy of the then Parliamentary Secretary’s letter was not held in DOTARS’ documentation.
Second application submitted in March 2004

1.42 DOTARS held discussions with AUSGUM in late February and early March 2004 in connection with a new application. A Regional Partnerships application for RP00740 AUSGUM Furniture Expansion was submitted on 19 March 2004. The application advised:

This application is seeking assistance in lease/purchasing a second machining centre to enable items such as tables to be manufactured in Emerald where it is best suited to cutting, drying, machining and docking the required components.

An existing machine will be relocated to Gympie where chairs and other high volume items will be more suited to that facility.

1.43 The application advised:

Our focus on Gympie grew as a result of what I am terming the “funnel” effect for the hardwoods in Queensland. Rather than take product from regional centres such as Mundubbera, Theodore, Eidsvold back to Emerald for processing then back to Brisbane for sale or export through the port it became logical that for certain high volume items to keep the flow going in one direction. The particular items I relate to here are chairs for example. This application provides benefits for both the Gympie and Emerald region and will create employment in both...

Consequently, the operational plan being adopted now is one where items such as tables will be manufactured in Emerald where it is best suited to cutting, drying, machining and docking the required components. Chairs and other high volume items will be more suited to the Gympie facility.

In terms of equipment required for each respective operation we are intending to move the existing machine at Emerald to Gympie as it has slightly larger operating surface area ideally suited for chair production. A “new” machine is required at Emerald which will be customised to focus on the table production.

1.44 The application sought $130 000 (plus GST) from Regional Partnerships (the same amount as for the previous project) towards a total cash budget of $303 109. The application proposed that the applicant would make a cash contribution to the project of $173 109. However, the application also indicated that the second machining centre would also be acquired through a finance lease arrangement, with the first milestone being:

Contract lease purchase of equipment.
1.45 The departmental assessment recommending that funding be approved was completed on 30 March 2004, eleven days after the application was submitted. On 1 April 2004, National Office advised the Regional Office that the then Parliamentary Secretary had approved funding of $130 000 (plus GST) for the project. However, a version of the departmental Minute that had been signed by a departmental officer was not held in DOTARS records. Nor did DOTARS hold a copy of the then Parliamentary Secretary’s written approval.

1.46 Rather than being appropriately treated as a new application for a different project, the second application was in many respects treated as if it were a ‘replacement’ that overcame the retrospectivity issues that had earlier prevented the $130 000 in funding from being approved, as follows:

- both TRAX and the spreadsheet used by DOTARS to track the approval of applications treated the later application as ‘overlaying’ the first. This wasn’t rectified until 2006;
- DOTARS’ website recorded the approved project under the name attributed to the original, unsuccessful application. This was only rectified in November 2006, following the provision of ANAO’s case study of this project to DOTARS on 4 September 2006;
- similarities between the departmental assessments provided to the then Parliamentary Secretary in respect of both applications suggest that the first assessment was used as a template for the second; and
- the CQACC marked its file relating to the first application as having been withdrawn, rather than being unsuccessful.

1.47 This approach contributed to the application not being subjected to appropriate scrutiny in order to ensure any Regional Partnerships funding would make efficient and effective use of the public money, as explained below.

**ACC comments on both applications very similar**

1.48 Comments provided by the CQACC on 30 March 2004 in relation to RP00740 were very similar to the comments entered into TRAX on January 2004 in support of the earlier project. In particular, the comments did not distinguish between the first project, which was ultimately demonstrated to involve replacing equipment lost in a fire (and taking the opportunity to

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703 In commenting on the ANAO case study in December 2006, DOTARS ‘noted’ this finding.
upgrade to a higher capacity machine through the acquisition of a second-hand machine) and the second project, which proposed the acquisition of an additional machine for further expansion purposes.

**Additional outcomes not identified for the new project**

1.49 Funding for RP00203 was not approved because the applicant had already acquired the higher capacity machining centre to which it related. In those circumstances and in the absence of other information, it would be reasonable to expect that the outcomes the applicant had claimed would result from the acquisition of that equipment were already available to it. Accordingly, to represent value for money, providing Regional Partnerships funding towards the acquisition of a second machining centre under the subsequent RP00740 project would need to result in outcomes that were additional to the outcomes claimed under the earlier project. This is not apparent from ANAO’s examination of the two applications. Table 1.1 sets out the significant duplication and overlap between the outcomes and benefits that the two applications claimed would be achieved from the two, separate, projects.
Table 1.1

Outcomes claimed in August 2003 and March 2004 applications

<table>
<thead>
<tr>
<th>Application for a higher capacity machine for Emerald</th>
<th>Application for a second machine for Emerald, with existing machine re-located to Gympie</th>
</tr>
</thead>
<tbody>
<tr>
<td>The benefits this machine offers over previous methods is potentially a 3 fold increase in production capacity. In the past this part of the manufacturing process has been the bottle neck and with the rapid growth of our markets both domestically and export it is imperative that we are able to produce accordingly. (ANAO emphasis)</td>
<td>The benefits this machine offers over previous methods is potentially a 3 fold increase in production capacity. In the past this part of the manufacturing process has been the bottle neck and with the rapid growth of our markets both domestically and export it is imperative that we are able to produce accordingly. (ANAO emphasis)</td>
</tr>
<tr>
<td>Having entered the Australian market place via large national retailers, we are now launching into the international market. The goal is to increase sales to in excess of $10m pa within five years. The increase in sales and manufacturing will require 20 new full time positions to be created in 2003 through to 2005. Extensive training and up skilling will be required, bringing opportunities for young people</td>
<td>At the time of fire the Sawmill operation employed 14 and the Furniture operation employed 16 (ANAO note: 14 plus 16 =30 at 12 August 03) Immediately after fire the Sawmill maintained 14 and the furniture operation was reduced to 4. If not rebuilt the furniture operation would have lost jobs in the sawmill as they related to the preparation components for the furniture. As a result of the timely purchase/replacement of the equipment subject of a previous application to date the employment numbers have now advanced to the Sawmill remaining at 14, the furniture operation Emerald 11 and the furniture operation at Gympie 13. Marketing office in Brisbane employs 2 at this stage. The future trend is constantly increasing the numbers at both sites. As a general bench mark we are estimating employment numbers to be in the order of 1 job per $125,000 in sales revenue. With conservative forecast sales for the calendar year at approximately $4.5m for furniture alone we are expecting our employment numbers to be increased to around 36-40 by the end of the year for the furniture side of the operation. Subject to being able to install the 2nd machine in Emerald it is expected that 5-8 of the new positions will be created in Emerald.704 (ANAO note: 14 sawmill plus 36 furniture = 50, a total projected increase from pre-fire employment of 20 by end of 2004.)</td>
</tr>
</tbody>
</table>


1.50 Similarly, DOTARS’ assessment of the two applications against the outcomes criterion did not adequately differentiate between the employment

704 In requesting further information from the applicant to progress its assessment of the first, unsuccessful application for $130 000 in Regional Partnerships funds, the department had advised the applicant that: ‘For a $130 000 funding request, it would be expected that a number of these jobs (at least 8 full time equivalent – “direct” employment outcomes) would come on line within the contracted time frame.’ [Emphasis as per original]
outcomes that had been claimed would result from the machining centre acquired in August 2003 (for which Regional Partnerships funding was unsuccessfully sought), and the further employment outcomes that would be obtained through the acquisition of a second machining centre (see Figure 1.4).

**Figure 1.4**

**Departmental assessment of the September 2003 and March 2004 applications against the outcomes assessment criterion**

<table>
<thead>
<tr>
<th>November 2003 assessment of 1st application relating to acquiring a larger machining centre</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Outcomes</strong></td>
</tr>
<tr>
<td>The project will equip the company to take advantage of an anticipated increase in demand for its outdoor furniture, including from overseas markets. This increase in demand is estimated to result in 20 new positions being created over the next 2-3 years. Whether this will occur, however, is less than clear and is predominantly based on expressions of interest in the company’s products at overseas trade shows. Nonetheless, at a minimum, the project is expected to allow the 15 mill workers previously laid-off as a result of the fire to be re-employed much sooner than otherwise be the case. In fact, these existing jobs are expected to be filled within 3 months following purchase of the machine saw.</td>
</tr>
<tr>
<td>In the absence of this larger machine being acquired, the alternative for the company is to wait for a machine to be imported from Europe which could take anything up to 6 months. With this delay, many of the company’s existing workers could be expected to move on, including outside of the region, in search of other work. This would compound the company’s efforts to restore its operations as soon as possible.</td>
</tr>
<tr>
<td>The application satisfies this criterion</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>March 2004 assessment of 2nd application relating to a acquiring a second machining centre</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Outcomes</strong></td>
</tr>
<tr>
<td>The project will equip the company to take advantage of confirmed orders and an anticipated increase in demand for its outdoor furniture, particularly from overseas markets. This increase in demand is estimated to result in 20 new positions being created over the next 2-3 years. Within the project period (five months) there will be an additional 5 FTE positions created at the company’s Emerald site, and the possibility of additional employment at its Gympie operation.</td>
</tr>
<tr>
<td>The application satisfies this criterion</td>
</tr>
</tbody>
</table>

Source: DOTARS’ assessment of RP00203, submitted to the then Parliamentary Secretary on 17 November 2003, and RP00740, submitted to the then Parliamentary Secretary on 30 March 2004.

**Inadequate inquiries made in order to determine the nature of the equipment to be acquired, its cost and the timing of acquisition**

1.51 The departmental assessment did not accurately reflect the second project as it was set out in the application. In particular, the assessment differed from the application in relation to:
• the specific type of equipment that was proposed to be acquired using the Regional Partnerships funds (which had not been specified in the application, but which was specified in the assessment), and

• the manner of its acquisition (with the assessment being based on a capital purchase, whereas the application proposed a lease purchase arrangement).

1.52 The covering Minute providing the department’s assessment to the then Parliamentary Secretary on 30 March 2004 referred more broadly to the project involving ‘the acquisition of a second machine centre’. However, this was in the context of the more specific advice set out in the project assessment. There is no evidence of DOTARS seeking confirmation from the applicant in regard to these aspects of the application. As a consequence, its assessment did not take account of elements of the proposal that would have a material affect upon any value for money decision.

Equipment being acquired

1.53 The specific type of equipment to be acquired could be expected to have a material bearing on any assessment of the reasonableness of the project budget proposed and the associated Regional Partnerships funding bid. The Regional Partnerships funding of $130,000 (plus GST) sought under the second application was the same as the amount unsuccessfully sought in relation to the acquisition of the second-hand Model 30L2. However, the application did not specify the make or model of the additional machining centre that was to be acquired under the second project.

1.54 By way of comparison, the departmental assessment specified that the project was for the acquisition of a second Model 30L2. The Regional Office assessment reported that the project budget had included $222,557 for the purchase-lease of the machining centre. This was exactly the same cost as had been identified in the applicant’s first application (which did not reconcile with the costs set out in the relevant lease agreement). However, a detailed budget for the project was not held in DOTARS’ records and there is no evidence of DOTARS obtaining any supporting documentation from the applicant to substantiate the type of machine to be acquired and associated costs.

Cost and nature of acquisition

1.55 A ‘lease/purchase’ arrangement, as proposed in the application, represents a different financial arrangement from a direct capital purchase. However, as with the first application, DOTARS’ assessment of the second
application did not adequately examine the terms under which the machining centre was to be acquired.

1.56 As noted, the applicant had entered into a finance lease arrangement for its August 2003 acquisition of the Model 30L2, which involved 60 monthly rental instalments, with a residual payment at the completion of the five year lease term. Accordingly, there was no up-front capital cost associated with the acquisition of that machine. Despite this, as also noted, the applicant’s first application had sought the full $130 000 in Regional Partnerships funding in the first month of the project for the purchase of the machine.

1.57 The application for assistance with the lease/purchasing of a second machining centre sought $130 000 (plus GST) in Regional Partnerships funding in three instalments:

- $65 000 in month one towards the first milestone ‘Contract lease purchase of equipment’. The nature of any up-front costs associated with contracting a lease purchase arrangement was not identified;\(^\text{705}\)
- $40 000 in month two for costs associated with installing and commissioning the machining centre, and associated training. There is no evidence of DOTARS obtaining any documentation from the applicant substantiating the nature or timing of these costs; and
- a final payment of $25 000 in month four, upon project completion.

1.58 There is no evidence of DOTARS seeking any further information from the applicant in order to confirm the terms of the arrangements to be used for acquiring the machining centre so as to provide the Ministerial decision-maker with a reliable basis on which to form a conclusion as to whether the funding would represent an efficient and effective use of the public money. Instead, the department advised that the project would involve the purchase and implementation of the machining centre, with a project period of five months.

*Timing of acquisition*

1.59 As noted at paragraphs 1.38 to 1.39, DOTARS’ 1 March 2004 advice to the then Minister was its understanding was that the new, related project being developed by the applicant (ultimately submitted on 19 March) did not involve retrospective funding. However, there is no evidence of DOTARS undertaking

\(^{705}\) The normal arrangement under a finance lease arrangement is that the lessee is liable for periodic instalment payments from the date of commencement of the lease agreement, rather than an up-front outlay.
the inquiries necessary in order to be able to demonstrate the basis for that advice.

1.60 In particular, ANAO notes that the sequence of events in relation to the genesis of the first application reported to DOTARS in December 2003 by the CQACC included the following reference:

By the end of the day a contact had a Model 30 at $240 000 second hand (at same price as [the applicant’s] burnt Model 27 but 4 time as fast, available in one month in lieu of six month plus new Model 27. (ANAO emphasis)

14.08.03

1.61 On that basis, it appears that, in addition to upgrading to the second-hand Model 30L2, the applicant had contemplated also replacing the burnt Model 27 from the time of the August 2003 fire. On 23 February 2004, the applicant had advised DOTARS that:

A “new” machine has been located and is available for sale. In terms of timing we propose to place an order as soon as possible with the intended installation being mid-March. Clearly we look to your support and assistance so that this is not delayed. The timing is imperative to meet a quickly filling export production order schedule which needs to be manufactured and shipped within the next 3-4 months to be in time for the northern hemisphere summer.

1.62 On 1 March 2004, the applicant further advised that:

Please don’t hesitate to seek any clarification in the meantime as time is pressing on the commitment to this equipment and it needs to be committed to ASAP to support the production requirements.

1.63 Similar to the first application, the second application submitted on 19 March 2004 stated that the ‘purchase and installation of the new equipment’ was ‘Ready to commence as soon as funding is approved.’ It also proposed that the equipment would be contracted, installed and commissioned within two months of the project commencing. Despite the experience in relation to the first project and the information previously provided in relation to acquisition lead times for equipment of this nature, there is no evidence of DOTARS examining how the second machine would be ordered and installed in the timeframe proposed.

Partnerships and Support assessment criterion

1.64 As discussed, the application proposed that the applicant would make a cash contribution of $173 109. DOTARS’ assessment concluded that the application satisfied the partnerships and support criterion. This was despite
the applicant having provided no evidence supporting its proposed contribution. As discussed at footnote 701, the applicant had been requested to provide such evidence in support of the first application, but the documentation provided did not satisfy this requirement. There is no evidence of DOTARS seeking any further evidence from the applicant in support of the co-funding proposed under the second, successful application. Further, the department did not advise the then Parliamentary Secretary that any funding should be subject to confirmation of the applicant’s co-funding.

1.65 In this respect, monthly cash flow forecasts for the period February 2004 to January 2005 provided to DOTARS by the applicant in March 2004 only made provision for $50 000 in capital expenditure over that period, which was projected to occur in April 2004. There was, therefore, no provision for an outlay of at least $92 557 on the purchase of a machining centre.\footnote{Based on the $222 557 the Regional Office assessment had identified as the machining centre cost included in the project budget, less the $130 000 in Regional Partnerships funds.}

1.66 Further, the cash flow projections included the line item ‘Monthly Loan Repayments’, which provided for the same amount of $5 400 in payments each month from February 2004 (prior to the second application being submitted) to January 2005. Therefore, no provision was made for an increase in monthly loan repayments to reflect the lease purchase of a machining centre acquired through the Regional Partnerships project.

1.67 Scrutiny of this information would have highlighted to DOTARS the need to obtain further information from the applicant in relation to the means by which it would be acquiring the second machining centre, and the nature of its proposed co-funding contribution.

**Viability assessment criteria**

1.68 The department assessed the applicant as a low risk, as follows:

Documentary evidence (business plan, profit and loss statements, cash flow forecasts) suggests that the applicant is a well-experienced, viable organisation which is strategically placed to expand its outdoor furniture operations. The national awards it received in 2002 and 2003 demonstrate the company’s expertise in outdoor furniture design and manufacture.

No specific measures are proposed to manage the applicant.

1.69 DOTARS had similarly concluded that the first application satisfied this criterion. Indeed, the paragraph relating to documentary evidence and
awards in this second assessment was exactly the same as that included in the first. However, as discussed at paragraph 1.31, the Regional Office’s assessment of the first application had also recorded that, because evidence of cash co-funding was inadequate, the applicant risk was assessed as medium. As noted, there is no evidence of DOTARS seeking any evidence in support of the co-funding proposed under the second application.

1.70 The departmental assessment was that the second project was medium risk, but that it satisfied the project viability criteria. This was on the basis that:

The applicant has provided a detailed budget itemising the costs of the project which appear reasonable. There are confirmed overseas export market orders and strong evidence of sustainability through long term orders and a sufficient supply of necessary materials. The ability of the project to deliver the anticipated employment outcomes over the project period (five months) is assured.[ANAO emphasis] The achievement of additional employment outcomes beyond this period will depend upon the company maintaining strong growth in the export market.

1.71 The basis for this assessment is unclear, given:

- the Regional Office’s assessment of the first application had stated that, because it was not going to be recommended, only a basic assessment of the proponent viability had been undertaken. There is no evidence of DOTARS undertaking any assessment of the revenue projections put forward in the second application. This is of particular relevance in light of the disruption to production caused by the earlier fire;

- as discussed at paragraphs 1.65 to 1.67, there was also no evidence of DOTARS examining the cash flow forecasts provided by the applicant. A further issue in this respect was that the cash flow projections forecast a negative closing bank balance every month from February 2004 to December 2004, with that result being premised on a $400 000 capital raising occurring in February 2004. In completing its assessment in March 2004, DOTARS did not examine that issue or seek any advice from the applicant as to whether the capital raising had occurred;

- as noted, a detailed budget itemising the costs of the project was not included in the documentation held by DOTARS; and

- there was no evidence of DOTARS having obtained any documentation to independently validate the existence, nature and duration of the confirmed export market orders claimed by the applicant.
1.72 Further, the business plan relied on in the departmental assessment was prepared in December 2002, eight months before the August 2003 fire. DOTARS did not seek an updated business plan that took explicit account of:

- the circumstances and consequences of the fire;
- the strategies the company was proposing to pursue in order to re-establish production and maintain existing markets; and
- the impact that lost production and the cost of implementing the re-establishment strategies would have on the company’s position.\(^\text{707}\)

1.73 In this respect, ANAO notes that on 8 June 2005, the funding recipient advised DOTARS that it had re-located its furniture manufacturing operations to Gympie because:

> History will show that the momentum of Ausgum in Emerald (in fact everywhere) was halted when we experienced the fire in August 2003. We attempted for a significant period of time to re-build the operation however given a number of key factors this has not been successful:

- loss of key personnel to high paying jobs elsewhere in the district.
- lack of economic housing to enable further skilled people to be enticed to the town.
- inability to “match” pay rates elsewhere in the district and remain competitive in a very competitive global marketplace.

1.74 This advice is not consistent with the statement made in the second application of 19 March 2004 (some seven months after the fire) that:

> As a result of significant market advancements both domestically and overseas it has been a necessity for Ausgum to increase its production output. Despite the major setback of a fire at our Emerald facility in August 2003 we have been able to maintain the growth and continue our endeavours in creating a significant new regional industry for not only the Emerald area but now also Gympie.

1.75 Further inquiries by DOTARS at the time of assessing the second application would have improved the rigour of its assessment of the application.

\(^\text{707}\) In December 2006, DOTARS advised ANAO that: ‘A 5 year budget forecast through to 2008 was provided with the second application.’ That budget forecast was based on assumed sales growth for the furniture business of 50 per cent in 2005; 40 per cent in 2006, 35 per cent in 2007 and 30 per cent in 2008. No information supporting the basis for those growth forecasts was sought or obtained.
**ANAO conclusion**

1.76 DOTARS did not apply appropriate scrutiny to the second AUSGUM application. In particular, in preparing its assessment provided to the then Parliamentary Secretary eleven days after the application was submitted, the department did not:

- consider the extent to which the outcomes claimed from the second project would be additional to the employment the applicant had already claimed would be obtained through the machine acquired under the first project, for which it was unsuccessful in obtaining Regional Partnerships funding due retrospectivity issues;

- obtain documentation confirming the applicant’s proposed cash contribution to the project, despite the applicant’s failure to provide documentation of that nature in respect to its first application;

- undertake appropriate due diligence inquiries in relation to the applicant or the project, including obtaining updated financial and business planning that had explicit regard to the effects on the business of the August 2003 fire at the applicant’s premises; or

- obtain confirmation, including substantiating documentation, of the specific equipment to be obtained by the applicant, the manner in which it would be acquired, and the proposed timing of the acquisition.

**Management of the Funding Agreement**

1.77 The Funding Agreement executed with the funding recipient on 7 May 2004 stipulated that the Regional Partnerships funding was to be used for the following Activity:

The Project to be undertaken by You is **AUSGUM furniture expansion** – to lease/purchase a second Biesse Rover 30L2 Machine Centre (or similar) machining centre to enable items such as tables to be manufactured in Emerald where it is best suited to cutting, drying, machining and docking the required components. An existing machining (sic) centre will be relocated to Gympie where chairs and other high volume items will be more suited to that facility.

Regional Partnerships funding will contribute to the Project by assisting with **the purchase/lease of the Biesse Rover 30L2 Machine Centre (or similar), its installation and training of operators.** The purpose for which Regional Partnerships funding will be used shall be referred to as the ‘Activity’. *(Emphasis as per Funding Agreement)*
1.78 The departmental assessment approved by the then Parliamentary Secretary had identified that Regional Partnerships funding would be used to assist with the purchase and installation of a second Biesse Rover 30L2 machine centre. The Funding Agreement varied this such that the Regional Partnerships funding was to assist with ‘the lease/purchase of the Biesse Rover 30L2 Machine Centre (or similar), its installation and training of operators.’

1.79 Table 1.2 sets out the Milestones to be achieved and expected completion dates, grant instalments and proposed payment dates, and reports required and their due dates, as outlined in the Funding Agreement.
### Table 1.2

**Milestones, Payments and Reports set out in Funding Agreement signed 7 May 2004**

<table>
<thead>
<tr>
<th>Milestones</th>
<th>Expected Completion Date</th>
<th>Payment Purpose</th>
<th>Payment Amount Due (GST inc)</th>
<th>Milestone/s Covered</th>
<th>Proposed payment date</th>
<th>Project Outcome/s covered in Report</th>
<th>Activity Milestone covered</th>
<th>Report Due Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Purchase/lease Equipment</td>
<td>30 April 04</td>
<td>Machine Centre arrives on Emerald site</td>
<td>$75 000</td>
<td>i</td>
<td>15 May 04</td>
<td>Progress 1: Order placed, Machine centre arrived, installed, commissioned and operators trained</td>
<td>i &amp; ii</td>
<td>29 May 04</td>
</tr>
<tr>
<td>ii) Install Equipment &amp; Commission</td>
<td>30 June 04</td>
<td>Machine Centre installed and commissioned</td>
<td>$53 700</td>
<td>i &amp; ii</td>
<td>30 May 04</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>iii) Business Support – Completion final report and audit</td>
<td>30 Sep 04</td>
<td>Activity completed, employment outcomes confirmed, final report and audit</td>
<td>$14 300</td>
<td>iii</td>
<td>30 Sep 04</td>
<td>Post Activity Report: Additional Employment outcomes and final report and audit</td>
<td>iii</td>
<td>29 Sep 04</td>
</tr>
<tr>
<td><strong>Total Funds</strong></td>
<td></td>
<td></td>
<td>$143 000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Source: Funding Agreement in relation to RP00740 AUSGUM Furniture Expansion project, 7 May 2004.*
1.80 The Funding Agreement specified one contracted outcome from the project, as follows:

<table>
<thead>
<tr>
<th>Project Outcome</th>
<th>Performance Measure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Additional employment</td>
<td>On completion of activity, an additional 5 positions will have been created at the Emerald site. Evidence to be supplied by You through payroll records.</td>
</tr>
</tbody>
</table>

**Risks not adequately managed**

1.81 In December 2006, DOTARS advised ANAO that:

The Parliamentary Secretary’s approval did not specify that the Machine was to be purchased. The covering minute referred to the ‘acquisition of a second machine centre’ and the project brief referred to the ‘installation of a 2nd large Biesse Rover 30L2 Machine Centre (saw) and associated dust extraction equipment’. It would be reasonable to assume that the term acquisition could be fulfilled through a purchase lease agreement and therefore not in contradiction with the Parliamentary Secretary’s approval.

1.82 In this respect, the project summary submitted to the then Parliamentary Secretary for her consideration also explicitly stated:

Regional Partnerships funds will assist with the purchase and implementation of the machine centre.

1.83 As is discussed at paragraphs 1.55 to 1.58, a ‘lease/purchase’ arrangement represents a different financial arrangement from a direct capital purchase. While providing that the acquisition could occur through a purchase lease agreement, the payment of Regional Partnerships funds under the Funding Agreement executed in respect to this project was structured to reflect a capital purchase.

1.84 Specifically, the Funding Agreement provided for 90 percent of the total approved funding to be paid within 23 days of the Agreement being executed (see Table 1.2). In practice, this occurred within 14 days, with payments totalling $117 000 (plus GST) being made on 21 May 2004. This was done in reliance on a letter from the funding recipient dated 13 May 2004 which advised that the machine being obtained using Regional Partnerships funds had been ordered, received, installed and was operating (see Figure 1.5).
1.85 The Funding Agreement stipulated that the first payment of $68 181.18 (plus GST) would not be made until the funding recipient had provided written confirmation of arrival of the machining centre onsite. The 13 May 2004 letter satisfied that condition. The funding recipient provided DOTARS with an invoice for the first payment with its 13 May 2004 letter, with the description: “AUSGUM Furniture Expansion Project Machine Arrived At Emerald”. DOTARS approved the invoice for payment on 21 May 2004.

1.86 The second instalment of $48 818 (plus GST) was proposed to be made on 30 May 2004 for the purpose ‘machine centre installed and commissioned’. An invoice for the second payment was also provided by the funding recipient.
with its letter of 13 May 2004, with the description: ‘AUSGUM Furniture Expansion Project Machine Installed and Commissioned.’ Both the first and second payments were made on 21 May 2004.

**1.87** In December 2006, DOTARS advised ANAO that:

The Funding Recipient satisfied the first two milestones, i) Purchase/lease Equipment and ii) Install Equipment & Commission, entitling them to 90% of payments in accordance with the Funding Agreement.

**1.88** In making the payment on 21 May 2004, DOTARS based its conclusion that the funding recipient had satisfied those milestones on the advice set out in the letter of 13 May 2004. DOTARS did not request any further information or documentation from the funding recipient to substantiate the progress identified in its 13 May 2004 letter. In particular, the Funding Agreement did not require the funding recipient to provide, before payment would be made, any documentation such as invoices or purchase orders identifying:

- the type of machine acquired;
- when it was ordered and received;
- the manner of its acquisition (lease purchase or direct capital purchase);
- the actual cost of the machine centre and associated equipment; or
- what, if any, expenditure had been incurred by the funding recipient.

**1.89** Nor did DOTARS undertake any site visit to confirm the installation and commissioning the equipment prior to making the payment.

**1.90** ANAO provided DOTARS with a case study on this project on 4 September 2006. In December 2006, DOTARS advised ANAO that:

The Department requested further information by sending a letter to the Funding Recipient on 8 September 2005 requesting their outstanding Final Report and Independent Audit. A further letter was sent on 16 November 2006 (after the Department received legal advice) seeking outstanding reports. Receiving these reports will provide the Department with evidence of purchase of equipment.

**1.91** ANAO notes that the 8 September 2005 letter referred to by DOTARS was sent 16 months after the department paid the funding recipient $117,000 (plus GST). The legal advice referred to by DOTARS was obtained in response to issues raised in the ANAO case study.
ANAO conclusion

1.92 Given the nature of this project, involving the acquisition of a piece of portable equipment by a commercial entity, it would have been prudent for DOTARS to have formulated the Funding Agreement such that payment was made in arrears upon completion of a satisfactory site visit and/or the provision of documentation to substantiate completion of the relevant milestones.

Final reporting and acquittal

1.93 The Funding Agreement required that the final payment of $13,000 (plus GST) would be made upon receipt and acceptance by DOTARS of a Post Activity Report from the funding recipient that contained:

- a summary of performance against the project outcomes and activity milestones specified in the Agreement;
- an audited detailed statement of receipts and expenditure in respect of the Regional Partnerships funding and other financial or in-kind resources (other contributions) used for the Activity, which must include a definitive statement as to whether the financial accounts are complete and accurate, and a statement of the balance of the funding recipient’s bank account with an authorised deposit-taking institution in which the Regional Partnerships funds were held;
- an audited statement that the Regional Partnerships funds and other contributions were expended for the purpose of the Activity and in accordance with the Agreement; and
- a certificate from the funding recipient’s Chief Executive Officer that all funding and other contributions received were expended for the purpose of the Activity and in accordance with the Agreement and salaries and allowances paid to persons involved in the Activity are in accordance with any applicable award or agreement in force under any relevant law on industrial or workplace relations.

1.94 The Activity Period stipulated in the Funding Agreement expired on 30 August 2004. The Post Activity Report was due on 29 September 2004. On 12 November 2004, DOTARS wrote to the funding recipient requesting that the overdue reports be provided as soon as possible. As noted, on 8 June 2005, the funding recipient advised DOTARS that it had ceased furniture making operations in Emerald, and that the machine acquired with Regional
Partnerships assistance had been re-located to its Gympie site. DOTARS was advised that:

I look forward to this matter being concluded with an understanding that the funding has been for significant regional development and as such remains valid. Given all that we have dealt with I will far (sic) from enthusiastic for any other outcome than completing the rest of the transaction.

1.95 However, the funding recipient did not provide DOTARS with the outstanding final report, audited statements or certification.

1.96 On 24 June 2005, DOTARS advised the funding recipient that its reply regarding finalising the project was being deliberated upon by the department. DOTARS noted the original contracted outcome was five additional positions at the Emerald site, to be evidenced by payroll records, and advised that:

We can and will also take into account all the other issues that have impacted on the business since the time we contracted with you. So before we make a final deliberation can you please provide evidence of [the five positions] as is shown by your payroll records at the completion date of the contract (which was meant to be 30 Sept 2004). We will take it from there once we have your reply to the above.

1.97 No reply was received from the funding recipient to that request.

1.98 On 8 September 2005 (almost one year after the final report and audited acquittal was due), DOTARS advised the funding recipient that:

This will be the final request for completion of the Funding Agreement. You must submit by the 30 September 2005, the Final report, Independent Audit and evidence via payroll records of an additional 5 employees at the Emerald site as confirmation of the employment outcomes required under the Agreement. Failure to provide the documentation will result in forfeiture of the final payment and the Department instigating action to recover unacquitted funds already paid under the Agreement. [Emphasis as per original]

1.99 DOTARS did not receive any reply to this request. On 30 September 2005, the Regional Office sought approval from National Office to: ‘discuss the project with our legal people, with a view to winding up the project and recovering any unacquitted funds.’ On 8 November 2005, National Office responded as follows:

Can we ask the ACC to see if they can get the project back on track (in a month or less) and report back to us. My recollection is that they were very keen on this project.
1.100 A handwritten note made on the relevant Purchase Order on 30 November 2005 stated:

    Delivery Date of Payment Change. Reason: Trying to contact proponent to
    find out position of the project. Failing this – look at recovering money from
    Legals.

1.101 No further action had been taken in relation to this project at the time
ANAO provided DOTARS with the case study in September 2006.

ANAO site visit

1.102 On 10 June 2006, ANAO conducted a site visit to the funding recipient’s
Gympie site. Three machines were sighted, as follows (see Figure 1.6):

- one Biesse Rover 27, serial number 94602, manufactured in 2000
  (Specifications: 20Kw, 415V, 23A, 50Hz, 110 24 low tensions);
- one Biesse Rover 30L2, serial number 95258, manufactured in 2000
  (Specifications: 35Kw, 415V, 40A, 50Hz, 110 24 low tensions) (the serial
  number of this machine matched the serial number of the Model 30L2
  acquired under a finance lease agreement in August 2003, for which
  Regional Partnerships funding was denied); and
- one Paolino Bacci Double AB034, manufactured in 2004 (Specifications:
  415 volts, 50Hz, 31Kw, 6500Kg). The funding recipient advised ANAO
  that this machine had not been acquired using the Regional
  Partnerships funds.708

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708 It was later confirmed that this machine was acquired by the funding recipient after it had advised
DOTARS that the machine being acquired through the Regional Partnerships project had been installed
and commissioned (see footnote 709).
Figure 1.6
Machines observed at funding recipient’s premises during ANAO site visit of 10 June 2006

Source: Photographs taken during 10 June 2006 ANAO site visit to funding recipient’s Gympie premises.

1.103 The Funding Agreement stipulated that the Regional Partnerships funding was to be used to assist with the purchase/lease of a Biesse Rover 30L2

Biesse Rover 27
(manufactured 2000)

Biesse Rover 30L2
(manufactured 2000)

Paolino Bacci
Double AB034
(manufactured 2004)
machining centre or similar. The only machine sighted at the ANAO site visit that could have been acquired using the Regional Partnerships funding provided in May 2004 was a Biesse Rover 27 that was manufactured in 2000.

1.104 The ACC’s December 2003 advice to DOTARS regarding the genesis of the first application had advised that the applicant had, in replacing the Model 27 machining centre destroyed in the fire, taken the opportunity to acquire bigger machinery at comparable costs by acquiring a second-hand Model 30L2, which the ACC described as being four times faster than the Model 27. In this respect, the funding recipient’s August 2003 application relating to the first project involving the acquisition of a Model 30L2 had stated:

This project is focusing on the expansion of the furniture manufacturing facilities through the installation of a large production capacity CNC Point to Point Machining Centre and associated dust extraction...

The benefits this machine offers over previous methods is potentially a 3 fold increase in production capacity. In the past this part of the manufacturing process has been the bottle neck and with the rapid growth of our markets both domestically and export it is imperative that we are able to produce accordingly.

1.105 This suggests that the Model 27 would not be considered similar to the Model 30L2 the Funding Agreement required the applicant to acquire. However, the ambiguous terms of the Funding Agreement present difficulties in effectively administering this aspect of the Agreement. In this respect, there is no record as to what was intended by the inclusion of the term ‘or similar’ in relation to the type of equipment required to be acquired using the Regional Partnerships funds. Nor was that term defined in order to provide certainty as to the terms of the Agreement.

1.106 The inclusion of this non-specific term in a Funding Agreement executed on 7 May 2004 becomes even more problematic when considered against the background of the applicant’s advice to the department in February 2004 that: ‘A “new” machine has been located and is available for sale’ (see paragraph 1.61), and the subsequent speed with which the funding recipient advised the department that the machine had been acquired and installed following execution of the Funding Agreement (see paragraph 1.83). In that context, the department should have been in a position to ascertain the make and model of the equipment the applicant was intending to acquire, and the means of acquisition, prior to executing the Funding Agreement.
Outcomes

1.107 Following receipt of the ANAO case study in September 2006, DOTARS wrote to the funding recipient on 16 November 2006 in reference to its failure to satisfy its obligations under the Funding Agreement and requesting that it provide evidence in support of a number of aspects of the machining centre acquired with the funds provided and outstanding reports required under the terms of the Agreement DOTARS advised that:

I expect your response within 21 days of the date of this letter.

If your response, providing complete information and evidence as requested, is not received by me at that time, the Department may terminate the Funding Agreement and consider its options for the recovery of funds paid to you under that Agreement.

1.108 Between that time and August 2007, DOTARS undertook further inquiries in relation to the project and the options available to it. Those inquiries confirmed that ANAO’s initial conclusions had been correct in that:

- the only machine that could had been acquired using the Regional Partnerships funding provided in May 2004 was the Biesse Rover 27 that was manufactured in 2000; and

- if acquired under a lease purchase arrangement, as indicated in the application, it would involve monthly payments with a residual payment at the end of the lease term, rather than up-front capital costs.

1.109 The funding recipient had entered into a five year finance lease for the acquisition of the second-hand Rover 27 on 4 May 2004 (one month after the then Parliamentary Secretary approved funding, but prior to the Funding Agreement being executed on 7 May 2004). The lease agreement involves 60 monthly rental payments of $3,167.84 and a residual value payment of $46,750 upon expiration of the lease in May 2009. The department had not sought or obtained documentation of this nature from the funding recipient until February 2007.

709 The lease agreement in relation to the Paolino Bacci Double AB034 sighted by ANAO was entered into by the funding recipient on 30 July 2004, more than two months after the funding recipient had been paid $117,000 (plus GST) in Regional Partnerships funds by DOTARS in reliance on the funding recipient’s advice that: ‘The machine centre and associated equipment has been ordered, arrived on site, installed, commissioned and operator training complete’ (see Figure 1.5). As noted, the Model 30L2 was the machine acquired in August 2003 for which Regional Partnerships funding was not approved.

710 An additional single application fee of $165 was payable with the first rent instalment.
1.110 As noted, in being asked to approve funding, the then Parliamentary Secretary had been advised by the department that the project duration was five months, during which time Regional Partnerships funding of $130,000 (plus GST) was to be paid, with the applicant to contribute cash of $173,109. Further in this respect, the Funding Agreement involved an Activity Period of less than four months. Although the Funding Agreement allowed for the lease purchase of the machining centre, the payments of Regional Partnerships funds were to be made in a manner that reflected a capital purchase arrangement. As illustrated by Figure 1.7, a project conducted over four months involving total expenditure of $203,109 does not relate well to the acquisition of equipment over five years through a lease arrangement.

**Figure 1.7**

*Comparison of Regional Partnerships payments to terms of the finance lease under which the equipment was acquired*

![Diagram showing comparison of Regional Partnerships payments to lease payments](image)

Source: ANAO analysis of Funding Agreement and finance lease agreement entered into by the funding recipient for the acquisition of the machining centre funded by Regional Partnerships

1.111 In this respect, Clauses 5.1 and 5.2 of the Funding Agreement required that Regional Partnerships funding must be expended on the specified Activity (being the purpose specified in the Funding Agreement for the use of the Regional Partnerships funds) during the Activity Period, as defined in the Agreement. Schedule 1 of the Agreement provided that the Activity Period commenced on the date of the Agreement, being 7 May 2004, and ended on 30 August 2004. As illustrated by Figure 1.7, by the end of the Regional
Partnerships Activity Period, total lease payments for the Rover 27 amounted to $12,836. That is, by the end of the Activity Period, less than ten per cent of the $128,700 (GST inclusive) in Regional Partnerships funds paid to the funding recipient had been spent on the lease, with no contribution yet required from the funding recipient towards leasing costs.

1.112 Further in this respect:
- even without the payment of the final Regional Partnerships instalment, it would not be until 4 September 2007 that the funding recipient would start to make a financial contribution to the cost of leasing the Rover 27; and
- at the end of the lease, the funding recipient will have contributed $108,285 to the acquisition of the Rover 27, substantially less than its contracted partnership contribution of $173,109 (which was also to include relocation of the existing Rover 30L2, development of staff training and associated site works – as at August 2007, the funding recipient had not provided DOTARS with any acquittal demonstrating the costs met in this regard).

ANAO conclusion

1.113 The department entered into a Funding Agreement that did not provide the necessary specificity in relation to the purpose for which the Regional Partnerships funding could be used, such that it is difficult to determine whether the funding recipient has applied the public money in the manner approved by the then Parliamentary Secretary.

1.114 Further, the department agreed to a Funding Agreement that provided for the Regional Partnerships funding to be used towards the cost of a lease purchase arrangement, while at the same time providing for the Regional Partnerships funds to be paid in full between May 2004 and September 2004. In doing so, the department did not have due regard for the time value of money issues demonstrated by Figure 1.7 or the implications for the efficient and effective use of the public money it was responsible for administering.

Employment outcomes

1.115 In terms of the employment outcomes, in November 2007, AUSGUM advised ANAO that:

27 jobs now exist as a result of the assistance provided. The number could well have been NIL had support not been received.
1.116 As noted, the only outcome required to be achieved by the funding recipient from the $130,000 (GST exclusive) in Regional Partnerships funding approved for RP00740 AUSGUM Furniture Expansion project was the creation of five additional positions at the Emerald site.

1.117 Concern was expressed at the 3 August 2004 meeting of the Central Highlands sub-committee (CHACC) of the CQACC that the intended outcomes for that region from the funding provided to the funding recipient were not going to eventuate. The Minutes of that meeting recorded that:

CHACC requested a brief from CQACC and DOTARS be given on the full detail behind the Ausgum Furniture funding arrangements. There are concerns that the final funding has supported a machine being purchased for the Gympie side of the operations as opposed to Emerald, which was the initial intent.

1.118 As discussed, the funding recipient advised DOTARS on 8 June 2005 that it had been unable to re-build the furniture manufacturing operation in Emerald. The funding recipient advised that:

Essentially in the end we have just not been able to get workers, consequently the machine you assisted was re-located to a new facility in Gympie. Gympie was researched and now proven to have far better demographics for the type of industry we are in. With your support we have been able to commence re-building the manufacturing operation and recently had upwards of 25 personnel employed. Consequently there is a huge benefit to regional Qld albeit in a different location.

1.119 The additional inquiries undertaken by DOTARS following receipt of the ANAO case study in September 2006 identified that, contrary to the project set out in the application and Funding Agreement and the funding recipient’s advice to DOTARS in May 2004 (see Figure 1.5 and paragraph 1.85), it had installed the equipment acquired using the Regional Partnerships funds directly at its Gympie site, rather than Emerald. The existing Model 30L2 was identified as having been transferred to Gympie in November 2004.

Project status

1.120 The funding recipient provided DOTARS with a Post Activity Report on 23 February 2007. However, the report provided did not satisfy the requirements of the Funding Agreement. In particular, it did not provide the required audited financial acquittal of the project receipts and expenditures, including the partner contributions from the funding recipient, or the certificate from the funding recipient that all Regional Partnerships funding
and partner funding contributions received were expended for the purpose of the Activity (as defined in the Funding Agreement) and in accordance with the Agreement.

1.121 As discussed at paragraphs 1.109 to 1.112, the financial arrangements under which the funding recipient is acquiring the machining centre make it unlikely that it will be in a position to satisfy these obligations under the Funding Agreement.

1.122 On 8 October 2007, DOTARS advised ANAO that it had considered its options and would be undertaking the following steps:

- terminate the Funding Agreement;
- not make the final payment due to non-compliance with the reporting requirements of the Funding Agreement; and
- seek to recover the unspent portion of Regional Partnerships funding.

1.123 In November 2007, AUSGUM advised ANAO that:

The fact is the machines where procured. Significant costs over and above the costs of the machines were experienced at the times and directly relating to them (eg installation, dust extraction, programming, production of manufacturing jigs, education of new workers on the machines, purchase of other necessary ancillary equipment).

...Your report states in many areas that DOTARS have advised they are terminating the agreement. This in itself is very disturbing as prior to receiving a communication from them virtually simultaneously with yours on the morning of the 23rd October. I have been chasing them via email following communications from them earlier in the year which indicated they would be back in touch with me to work through completing the final reporting. They did not respond to my emails and unbelievably now I just receive a notice of default which I will strenuously defend as being totally inappropriate.
2. Jarrahdale Heritage Park

This case study examines RP00622 Jarrahdale Heritage Park, involving a local government authority developing a tourism park. The park itself is not expected to be sustainable on a stand-alone basis. Other key viability risks involve the majority of the Park land not being owned by the funding recipient, and unsubstantiated revenue and cost assumptions underpinning the funding application. These risks were not adequately identified or managed by DOTARS in assessing the viability of the project proposal. The project is significantly over-budget and well behind the original schedule.

Introduction

2.1 Jarrahdale is located 45 kilometres south east of the Perth Central Business District in the Shire of Serpentine-Jarrahdale, within the Peel Region of Western Australia. Jarrahdale was the site of one of the first major timber milling operations in Australia. On 14 July 1997, the National Trust of Australia classified the Jarrahdale Town site as an historic town.

2.2 The Jarrahdale Heritage Park lies within the Jarrah forest from which it derives its name. In 2002, the Shire of Serpentine-Jarrahdale completed a Conservation Plan for Jarrahdale Heritage Park. The primary aim of this Plan was to identify and assess the cultural heritage significance of the area and provide recommendations for conservation of the site and the existing building.

2.3 A Management Plan for the Heritage Park was completed in 2003. It was used as the basis for further studies including planning, initiating and guiding statutory planning procedures, and progressing development of an Implementation Plan for the project. It was also used to support funding applications, including the Regional Partnerships application.

2.4 The Jarrahdale Heritage Park is estimated to cost approximately $12.5 million when fully developed. Approximately half of this is intended to be provided by the private sector, including the following elements: development of the timber mill; the tourist railway to Jarrahdale; the Jarrahdale Interpretative Centre; the eco village development; and the commercial precinct development.

\[\text{See paragraph 2.118.}\]
The Regional Partnerships application

2.5 On 30 March 2004, the Shire of Serpentine-Jarrahdale applied to DOTARS for $760 800 (plus GST) in Regional Partnerships funding for the Jarrahdale Heritage Park project. The project had an expected project duration of 24 months (1 July 2004 to 30 June 2006) and was described as follows:

The Jarrahdale Heritage Park concept has been developed to showcase the natural beauty and heritage of this unique eco area. Jarrahdale played a key role in Australia’s history as one of the first major timber milling operations. Jarrahdale Jarrah has been exported around the world. Jarrahdale is the only whole town in WA that has been declared as a complete heritage town. The finished Park will be a spectacular visitor destination of state and national significance which incorporates many sought after tourist attractions and activities.

This first active implementation stage phase aims to provide the momentum for the Park to become fully operational as a major tourism icon for the state and the region. All project activities will maximise local employment and economic development opportunities during construction activities and in tourism development.

This phase includes construction of an elevated canopy walk over the picturesque brook, in the site of the old conveyor belt that was once part of the mill operations. Viewing towers, modelled on the water tower structures, will provide views across the valley, working historic timber mill and the town.

Walkways and cycle ways are a major part of the park and consist of a series of short loops, connected by bridges in the site of real historical crossings where timber was dragged from the forest to the mill.

Local and state funding has already allowed commencement of an amphitheatre project for staging a wide range of events. Refurbishment of an existing historical rotunda will become a focal point for the park. Picnic decks will be used to identify the location of old buildings on the site. All features will provide interpretative information and activities that aim to bring history alive.

As part of the local government contribution, executive support will be provided.

2.6 In addition to the requested Regional Partnerships funding, the application advised that other contributions to the project were to be made as set out Table 2.1.
### Table 2.1

Partner contributions identified in the Regional Partnerships application

<table>
<thead>
<tr>
<th>Partner</th>
<th>Cash $</th>
<th>Value $</th>
<th>In kind</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shire of Serpentine-Jarrahdale</td>
<td>566 587</td>
<td>151 500</td>
<td>Onsite cottages to be leased as backpacker accommodation and staff time in managing the project and the cost of Council technical officers.</td>
</tr>
<tr>
<td>National Trust of Australia (WA)</td>
<td>80 000</td>
<td>1 400 000</td>
<td>Value of land on which Park would be constructed</td>
</tr>
<tr>
<td>Peel Development Commission</td>
<td>46 000</td>
<td>5 400</td>
<td></td>
</tr>
<tr>
<td>Serpentine Jarrahdale Tourism Association</td>
<td>Nil</td>
<td>6 000</td>
<td>Management time as part of the Jarrahdale Heritage Park Management Committee</td>
</tr>
<tr>
<td>WA Department of Conservation and Land Management</td>
<td>Nil</td>
<td>5 400</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>692 587</strong></td>
<td><strong>1 568 300</strong></td>
<td></td>
</tr>
</tbody>
</table>


2.7 Regional Partnerships funding of $760 800 was to be used for:

- detailed planning and commencement of initial projects—$60 000;
- foundation works—$89 000;
- improving access comprising bridge construction, upgrading of trails and clearing and safety works for major projects—$68 500;
- improved facilities comprising construction of picnic decks and completion of signage and promotion—$92 500;
- preparation for major construction—$35 000;
- major construction involving viewing towers, the aerial walkway and the rotunda—$365 000;
- the site works major launch—$40 000; and
- promotion—$10 800.

### Project eligibility

2.8 At the time the Shire submitted its application, the Regional Partnerships Programme operated under the original Guidelines. Among other
things, the Guidelines stipulated that projects not eligible for funding included those:

projects that can not obtain or that are in the process of obtaining the relevant approvals or licences to progress;

2.9 Revised Guidelines were promulgated on 31 May 2004. On the issue of approvals, the Revised Guidelines stated that:

Project proposals that can not obtain or have not yet obtained the relevant approvals or licences to progress will not generally be considered.

2.10 This change to the Guidelines was approved by the acting Minister for Transport and Regional Services on 15 April 2004. In recommending the revision, DOTARS had advised the acting Minister that:

The current wording [that is, in the original Guidelines] is aimed at ensuring that proponents bear a fair share of the risk associated with projects. Any change to the guidelines needs to preserve this basic approach and not result in a significant shift in risk from the proponent to the Government.

We consider that it is possible to amend the guidelines to introduce some additional flexibility while continuing to signal strongly that projects without the necessary approvals/licenses will not be eligible for funding.

...The main change is the inclusion of the word “generally” which allows for the possibility of exceptions. We envisage that exceptions will only be made in a limited range of circumstances, predominantly where:

- the applicant is a community-based organisation;
- the cost of applying for an approval/license is a high proportion of the project cost.

2.11 DOTARS further advised the acting Minister that:

The proposed change would result in a small degree of additional risk to the Government in that such projects may ultimately fail to gain the necessary approvals/licenses. We propose to manage this risk as follows:

- by including a provision in the funding agreement to ensure that the first payment cannot be made until the necessary approvals/licenses have been obtained, and possibly a timeframe for obtaining the approval as well; and
- by including advice about the change in the Regional Partnerships programme manual used by departmental assessors and providing examples of the limited sorts of circumstances in which exceptions would be made.
2.12 At the time of applying for Regional Partnerships funding, the Shire had not obtained development approvals or building licenses for any of the construction projects to be undertaken as part of establishing the Park. Indeed, development approvals were not obtained until at least a year after the Regional Partnerships application was submitted on 30 March 2004 and, for all but one element, at least a year after being approved for funding on 7 June 2004.\(^{712}\) Relevant approvals were obtained as follows for various elements of the project:

- 8 March 2005, for the boardwalk and viewing platform;
- 13 June 2005, for the two temporary information signs;
- 18 August 2005, for the amphitheatre;
- 20 March 2006, for the picnic shelters, barbeques, toilet facilities and gas bottle enclosure; and
- 24 July 2006, for the aerial walkway, footbridge and car park.

2.13 In respect to development approval for restoration of the rotunda, a key aspect of the project being funded by Regional Partnerships, in November 2007 the Shire advised ANAO that:

> The Shire has not progressed the development application for the rotunda as the recently completed business plan has identified the sale of the land on which the rotunda currently stands is essential to fund the ongoing operation and maintenance of the Park. The rotunda’s development may be achieved through the private sector and caveats on the sale of the land or alternatively through relocation to a new site in the Park.

2.14 The project proposal did not satisfy either of the criteria identified to the acting Minister by DOTARS for being eligible for an exception to the requirement under the Guidelines to have all necessary approvals and licences in place in order to be considered for funding. Accordingly, had the Programme Guidelines and exception criteria advised to the acting Minister been applied to the assessment of this project, it would not have been eligible for funding.

2.15 Further, the obtaining of necessary approvals and licences was not made a pre-condition to be satisfied before the Shire would receive the first

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\(^{712}\) In November 2007, the Shire advised ANAO that, as the applicant, it was also the approval authority which, in terms of risk, significantly reduced the likelihood that approvals would not be granted. However, the Shire’s advice in relation to the construction of the aerial walkway and amphitheatre was that the project timeframes could not have predicted that development approval would be subject to the development of a business plan.
payment of Regional Partnerships funds. The first Regional Partnerships payment of $149 000 (plus GST) was made on 8 October 2004, six months prior to the Shire obtaining relevant approvals for the first of the project elements.

**ANAO conclusion**

2.16 The project did not satisfy the Programme’s eligibility requirements as it did not have the necessary statutory approvals in place at that time of applying, and did not satisfy the exception criteria advised to the acting Minister by DOTARS. The absence of the necessary development approvals and building licences was not raised by DOTARS at any stage of its assessment of the project. Nor was it drawn to the then Parliamentary Secretary’s attention when DOTARS sought approval of the spending proposal.

**Approval of funding**

2.17 DOTARS’ assessment of this project was provided to the then Parliamentary Secretary on 31 May 2004. This was as part of an assessment package of 14 projects. Of these, 12 were recommended for approval and two were assessed as not meeting the Regional Partnerships Programme Guidelines. The recommended projects included the application relating to the Jarrahdale Heritage Park. DOTARS summarised the project and the reasons for its recommendation as follows:

This project will activate the first implementation stage of the Jarrahdale Heritage Park. It will create employment during the construction and result in 30 direct jobs once the park is operational. There will also be social benefits for a community that has experienced a general downturn in recent times. Strong partnerships with all 3 levels of government involved.

It is a multi-year grant project.

2.18 DOTARS’ assessment advised the then Parliamentary Secretary that the project duration was 24 months with a recommended funding profile involving payment of $217 500 in 2003–04, $317 500 in 2004–05 and $225 800 in 2005–06.

2.19 DOTARS assessed the project as meeting the Regional Partnerships Programme Guidelines and satisfying all assessment criteria. DOTARS also advised the then Parliamentary Secretary that the Peel ACC had recommended the project and rated it as a high priority for its region. DOTARS recommended that the then Parliamentary Secretary approve funding of $760 800 (plus GST) for the project, subject to two conditions.
2.20 The department’s assessment rated both applicant and project viability risk as being low. However, DOTARS recommended, on a procedural basis\textsuperscript{713}, that independent assessments be undertaken of applicant and project viability.

2.21 The project was approved for funding by the then Parliamentary Secretary on 7 June 2004. Consistent with DOTARS’ recommendation, the then Parliamentary Secretary approved funding subject to:

- satisfactory independent financial viability and project viability assessments; and
- multi-year grant approval from the Minister for Finance and Administration.\textsuperscript{714}

2.22 After receiving multi-year grant approval from the then Parliamentary Secretary to the Minister for Finance and Administration on 2 June 2004, on 7 June 2004, the then Parliamentary Secretary annotated as ‘approved’ the project summary and reasons for recommendation submitted by DOTARS on 31 May 2004 and annotated as ‘Agreed’ DOTARS’ recommendation in its project assessment.

2.23 Also on 7 June 2004, the then Parliamentary Secretary advised the Member for Canning of her funding approval and issued a Media Release announcing her funding approval the next day. Letters from the then Parliamentary Secretary providing similar advice to the 7 June 2004 letter to both the Shire and the Peel ACC were dated 22 June 2004.

**Conduct of the external viability assessment**

2.24 On 15 June 2004, the signed Ministerial Brief approving funding for this project was sent to DOTARS’ Western Australia Regional Office by National Office.

2.25 On 16 June 2004, the Regional Office wrote to the Shire requesting that it authorise DOTARS to undertake steps to assess the financial viability of the Shire and the Jarrahdale Heritage Park project. This authorisation was provided to the Regional Office on 22 June 2004.

\textsuperscript{713} DOTARS advised the then Parliamentary Secretary that: ‘It is the department’s process to conduct a financial risk assessment of any entity seeking funds of this value’ and ‘it is the department’s process that an independent project viability assessment is undertaken for projects of this value’ and advised that any funding approval should be conditional on these assessments being satisfactory.

\textsuperscript{714} This relates to the Government’s policy requirement that the Finance Minister’s approval be obtained prior to awarding and announcing a multi-year grant, which originally applied to grants that involved commitments for more than twelve months. This requirement now applies to grants involving more than $2 million over a period longer than 36 months.
2.26 A draft external viability assessment report was received by DOTARS on 12 July 2004. Following examination of the draft report, the Regional Office advised National Office on 15 July 2004 that:

I confirm that we are happy with the report and will take its recommendations into account when drafting the funding agreement. It is noted that the report is generally positive in its comments. We will proceed with preparing the funding agreement.

2.27 DOTARS provided the Shire with a draft of Schedule 1 to the Standardised Funding Agreement on 20 August 2004. A full version of the Funding Agreement was provided to the Shire for execution on 7 September 2004.

**Identification and management of viability risks**

**DOTARS’ assessment and advice**

2.28 DOTARS assessed both the applicant and the project as low risk. Figure 2.1 outlines the assessment provided by DOTARS to the then Parliamentary Secretary in support of the departmental recommendation that the spending proposal be approved.

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715 The Regional Partnerships Programme has adopted Standardised Funding Agreements for use in respect to projects funded through the Programme. DOTARS’ Regional Partnerships website advises potential applicants that: ‘The Funding Agreement is a legally enforceable document, which sets out the terms and conditions governing Commonwealth funding. The terms and conditions of the funding are generally not open to negotiation.’ [sic] As a result, the only aspect of the Standardised Funding Agreement that is usually subject to discussion with successful applicants is the project specific information set out in the Schedule to each Agreement, relating to the proposed amount and timing of grant instalments, expected completion dates for project milestones and due dates for progress and final reports.
### Figure 2.1

**DOTARS’ assessment of applicant and project viability risks**

<table>
<thead>
<tr>
<th>Item</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Applicant Viability</strong></td>
<td>The Shire of Serpentine-Jarrahdale is a local government authority and is well experienced in managing grant funding. It is considered that there is minimal risk concerning the applicant’s viability.  It is the department’s process to conduct a financial risk assessment of any entity seeking funds of this value. Any funding approval should be conditional on this assessment being satisfactory. The application satisfies this criterion.</td>
</tr>
<tr>
<td><strong>Project Viability</strong></td>
<td>The project is assessed as a low risk. Comprehensive development and management plans are in place to guide the establishment of the JHP by a Management Committee with members from the main project partners, including the Shire of Serpentine-Jarrahdale, the Peel Development Commission and the National Trust of Australia (WA). The Shire of Serpentine-Jarrahdale has allocated $2.34m from its budget (6.9 per cent of total revenue) for maintenance purposes and other small developments during the next five years. Funds will be raised from council rates and from the sale of council property. Additional external funding will be required to bring the JHP to full fruition, ultimately a $4 million project. Whilst this will require substantial investment over the next few years, in view of the JHP’s important economic, social, environmental, heritage, indigenous and tourism aspects, numerous potential sources of funds have been identified. For instance, partners involved in the project are currently applying to the Australian Government’s recently announced Tourism and Forestry Assistance programmes. The PDC has also indicated that their support will increase as development of the JHP continues during the next few years. It is the Department’s process that an independent project viability assessment is undertaken for projects of this value. Any funding approval should be conditional on this assessment being satisfactory. The application satisfies this criterion.</td>
</tr>
</tbody>
</table>

Source: DOTARS project assessment submitted to the then Parliamentary Secretary on 31 May 2004.

2.29 Significantly, DOTARS’ assessment did not examine the following key project viability issues:

- the major elements of the Jarrahdale Heritage Park would be located on land that is owned by the National Trust of Australia (WA) (National Trust), but DOTARS did not examine the tenure arrangements that would apply to the Park;
- the application did not identify the assumptions underpinning the revenue projections for the project;
the sustainability of the Jarrahdale Heritage Park was not linked to direct revenue generation from the Park. Instead, viability was dependent on the Shire of Serpentine-Jarrahdale funding ongoing maintenance and operating costs;\textsuperscript{716} and 

- the Management Plan submitted with the application included indicative cost estimates only. 

2.30 The external viability assessment conducted after funding was approved by the then Parliamentary Secretary identified concerns in relation to a number of these risks. For example, concerns were raised in relation to the absence of revenue assumptions for the project, only anecdotal evidence was provided attesting to market interest in the project and the application had qualified itself in relation to the accuracy of project costing.

**Land tenure**

2.31 Land tenure is an important issue to be addressed when assessing applications for grant funding that involve the construction of assets. For the Regional Partnerships Programme, project viability is defined as evidence that the project outcomes are sustainable beyond the funding period, that the project has been appropriately costed and that there is sufficient funding to achieve the outcomes.\textsuperscript{717} Accordingly, insecure tenure over the land on which a tourist park is to be constructed was relevant to DOTARS in its assessment of this application.

2.32 In its project assessment, DOTARS advised the then Parliamentary Secretary that the National Trust was contributing the 32 hectares of land that would largely comprise the Park. As indicated in Table 2.1, the $1.4 million valuation of the land was included as an in-kind contribution to the project from the National Trust, with DOTARS advising the then Parliamentary Secretary that all partnership funding had been confirmed. However, despite the land valuation representing 46 per cent of total project costs, DOTARS had not actually undertaken any due diligence to establish and confirm the land tenure arrangements. As a result, DOTARS’ assessment of the Jarrahdale Heritage Park application did not address the fact that the land was not being

\textsuperscript{716} In November 2007, the Shire advised ANAO that it has always accepted that it would be required to fund the operating and maintenance deficit of the Park as the revenue generation capacity of the Park would not fully meet these costs. 

donated to the Shire, but rather that the National Trust had only consented to the construction of the Park on its land.

**Partnership Agreement**

2.33 In this context, the Jarrahdale Heritage Park is to be constructed on 35 hectares of land. In May 2006, the Shire of Serpentine-Jarrahdale advised ANAO of the following land ownership in relation to the Heritage Park:

- three sections of land totalling 32.4 hectares (91 per cent) are owned by the National Trust; and
- two sections of land totalling 3.1 hectares (nine per cent) are owned by the Shire of Serpentine-Jarrahdale.

2.34 The major elements of the Heritage Park development will be located on the land owned by the National Trust.

2.35 Council Meeting Minutes state that, in the original negotiations, National Trust representatives were prepared to cede the land to the Shire once they were satisfied conservation objectives had been achieved. As an interim measure, the land was to be leased to the Shire.

2.36 A proposed lease and partnership agreement between Council and the National Trust was agreed at a Heritage Park Management Committee meeting held in November 2001. Council requested some amendments to the drafts. Amended documents were presented to Council in December 2002. At this time, Council agreed to sign the partnership and lease agreements that had been negotiated with the National Trust. However, the agreements were not signed.

2.37 In January 2004, the National Trust informed the Shire that the Trust no longer wished to lease the land to it and proposed an amended Partnership Agreement. On 28 February 2004, Council resolved to enter into the revised Partnership Agreement. In its resolution, Council also stated that it intended to pursue, in the long-term, joint ownership of the land owned by the National Trust.

2.38 On 26 March 2004 the Shire of Serpentine-Jarrahdale and the National Trust of Australia (WA) entered into a Partnership Agreement. A copy of the Partnership Agreement was not examined by DOTARS when assessing the Regional Partnerships application submitted on 30 March 2004. Key terms of the Partnership Agreement relevant to assessing the viability of the project include:
• a term of three years commencing on 26 March 2004, unless the Agreement is terminated or extended;
• formation and operation of a Joint Management Committee; and
• in the event the National Trust seeks to dispose of the land, the Shire will be given an option to acquire. In exercising this option, the Agreement requires that consideration be given to any improvements as a result of works undertaken or funded by the Shire.\textsuperscript{718}

2.39 The terms of the Partnership Agreement do not provide a high degree of security to the Shire in terms of ongoing tenure over the land on which the Heritage Park is to be constructed. However, DOTARS’ assessment of the application did not explicitly address the fact that the project involves the expenditure of Regional Partnerships funds on land that is not owned by the funding recipient, and over which the funding recipient has limited rights of tenure. This fact was also not communicated to the decision maker (the then Parliamentary Secretary).

2.40 In November 2007, the Shire advised ANAO that it was in negotiations with the National Trust to establish secure tenure over the land and, when this is agreed, the arrangement will replace the Partnership Agreement.

\textit{In-kind contribution overstated}

2.41 DOTARS’ assessment relied on the statement in the application that the National Trust was making an in-kind contribution to the project involving the land, as follows:

• the Regional Partnerships application described the in-kind contribution as:
  
  \$0.95 million donation of land from Bunnings. Valued at \$1,400,000 in 2001, presented to NTWA in trust.

• DOTARS’ assessment of the application provided to the then Parliamentary Secretary on 31 May 2004 stated that:
  
  As well as \$80,000 cash, the National Trust of Australia (WA) is contributing the 32 hectares of land that will largely comprise the park, which in turn was originally donated by Wesfarmers/Bunnings and is valued at \$1.4 million.

\textsuperscript{718} This clause does not explicitly address works funded by the Regional Partnerships Programme.
2.42 The Regional Partnerships Programme Internal Procedures Manual in place at the time this project was submitted and assessed (July 2003 version) provided as follows in relation to in-kind contributions:

In-kind support to a project is products or services provided to the project that have an intrinsic value, but are not provided as direct cash support (e.g. the use of an office at no charge which would normally be rented out – the value of the rent not charged would be an in-kind contribution).

2.43 This same definition is included in the current version of the Regional Partnerships Programme Guidelines.

2.44 DOTARS’ records state that, as part of the project assessment it had been advised by the applicant (on 18 May 2004) that both the Shire and the National Trust owned/controlled sections of the site and that a ‘development of site’ agreement had been entered into. The next day, DOTARS was provided with a copy of the Management Plan for the site (which confirmed that the majority of the land for the Park was not owned by the Shire) but a copy of the disposition of property plan was not provided until June 2004 and DOTARS did not at any stage obtain a copy of the partnership agreement between the Shire and the National Trust.

2.45 DOTARS’ February 2007 advice to ANAO was that it relied on the applicant to identify relevant matters and that it was unaware of the changed land tenure arrangements because it had finalised its project assessment before it had obtained all relevant information. In particular, the department advised ANAO that:

The first documentary evidence that a different arrangement applied to the land held by the National Trust is contained within the ‘Jarrahdale Heritage Park – Development and Disposition of Property Business Plan’ – dated March 2004 but only delivered to the department on 27 June 2004 – after the project had been considered and approved by the then Parliamentary Secretary.

2.46 This advice demonstrates the importance of the department obtaining and examining\(^\text{719}\) requested documentation before recommending (in this case, substantial) funds be approved. The department’s advice to ANAO did not address why the receipt of this information, on 27 June 2004, did not lead to further inquiries being made, noting that the Funding Agreement was not signed for a further three months (the Funding Agreement was signed by the Shire on 24 September 2004 and by DOTARS on 1 October 2004), and advice

\(^{719}\) The Management Plan for the Park provided to DOTARS on 19 May 2004 explicitly identified that most of the land for the Park was owned by the National Trust of Australia (WA).
provided to the Ministerial decision-maker concerning this issue. In this context, despite the information received by DOTARS on 27 June 2004 regarding the arrangements relating to the land, the executed Funding Agreement continued to identify an in-kind contribution to the project from the National Trust of $1.4 million for the value of the land (representing 62 per cent of nominated partnership contributions to the project). In this respect, it is relevant to note that in its programme evaluations, DOTARS relies upon data from Funding Agreements to identify the contributions ‘made’ by partners rather than acquitted financial information of actual partner contributions.

**ANAO conclusion**

2.47 DOTARS’ assessment of the Jarrahdale Heritage Park application did not address the fact that the land was not being donated to the Shire, but that the National Trust had only consented to the construction of the Park on its land. The Shire has insecure tenure over the land where Regional Partnerships funds are being used to construct key elements of the Heritage Park. In this context, there was not a sound basis for including the value of the land as an in-kind contribution to the project. In the absence of this in-kind contribution, the Regional Partnerships funding represents 47 per cent of total project costs, rather than the 25 per cent advised to the then Parliamentary Secretary by DOTARS.

**Revenue projections**

2.48 In terms of economic potential, the Shire stated as follows in its March 2004 application:

The Jarrahdale Heritage Park is recognised as a project with major regional potential. It has been specifically identified as a critical project in the Regional Strategy of the Peel Area Consultative Committee, the Peel Sustainable Development Strategy 2020, the Serpentine-Jarrahdale Economic Development Plan and the Shire Strategic Plan.

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720 See, for example, Department of Transport and Regional Services, *Stage Two Mid-Term Evaluation of the Regional Partnerships Programme*, November 2006, p. 2.

721 In November 2007, the Shire advised ANAO that:

‘The independent viability assessment was received by DOTARS on 12 July 2004 after receipt of the Jarrahdale Heritage Park Development and Disposition of Property Business Plan delivered to the department on 27 June 2004. It is important to note that approval by the Parliamentary Secretary was subject to satisfactory independent financial viability of the Shire and project viability assessments. The Funding Agreement was then signed by the Shire on 24 September 2004 and by DOTARS on 21 October 2004.’
The JHP project is directly linked to national policy directions, particularly the Tourism White Paper (2004). It is a major project with international appeal, boosting the national built and natural heritage tourism assets. It can capitalise on multiple niche market opportunities, such as the backpacker, eco-tourism, cultural tourism, industry heritage and events market segments.

Jarrahdale is located near the major tourist centres of Perth, Fremantle and Mandurah, making it ideally located to attract a great number of day trippers, interstate and overseas visitors. The expected increase in visitor numbers will boost economic confidence and encourage businesses to invest in the region.

2.49 A core determinant of project viability is the set of assumptions underlying forecast project revenue. The primary assumptions are the size of the overall market and the percentage of the market that the project will capture. The accuracy of these estimates is dependent on the quality and depth of market research and, ultimately, the ability of those managing the business to delivery quality services into that market.

2.50 However, in applying for Regional Partnerships funding, the Shire did not provide any data on the assumptions that underpinned its revenue projections. DOTARS did not seek such data from the Shire when preparing its assessment of the project for consideration by the then Parliamentary Secretary. The absence of such data was commented upon as follows by the external viability assessment undertaken after the spending proposal had been approved by the then Parliamentary Secretary:

The financial information provided did not identify revenue assumptions supporting either project projections or projections for Jarrahdale.

Accordingly, due to the limited information provided, it has not been possible to make any analysis on revenue assumptions.

2.51 More broadly, the external viability assessment commented that:

The proposal itself does not contain projected results supported by clear evidence based assumptions.

The purpose of the project is to stimulate economic activity in the region. However, we note that no formal Economic Impact Assessment has been undertaken (noting that in our experience this is not unusual for smaller projects such as this).

2.52 In this respect, the external viability assessment examined the project as a $1.5 million project. It did not reflect the fact that Jarrahdale Heritage Park is estimated to cost approximately $12.5 million when fully developed, with approximately half of this is intended to be provided by the private sector.
**ANAO conclusion**

2.53 There was insufficient evidence available to DOTARS at the time of its assessment to be satisfied that the revenue projections for the project were robust and reliable in order to support its conclusion that the project represented a low viability risk.

**The Shire’s financial performance and position**

2.54 The sustainability of the Jarrahdale Heritage Park was not linked to direct revenue generation from the Park. Instead, viability was dependent on the Shire of Serpentine-Jarrahdale funding ongoing maintenance and operating costs. These costs were estimated at the time of the application at $365 000 per annum. This figure only included landscape maintenance costs and excluded a range of other ongoing costs.722 Accordingly, a key issue in assessing the viability of the project ought to have been the financial performance and position of the Shire of Serpentine-Jarrahdale.

2.55 In relation to the applicant viability criterion, DOTARS advised the then Parliamentary Secretary that:

> The Shire of Serpentine-Jarrahdale is a local government authority and is well experienced in managing grant funding. It is considered that there is minimal risk concerning the applicant’s viability.

2.56 However, DOTARS undertook no analysis of the financial performance and position of the Shire of Serpentine-Jarrahdale to inform its assessment against the applicant viability criterion. In comparison to the absence of pre-approval analysis by DOTARS, post-approval analysis undertaken as part of the external viability assessment considered:

- the Shire’s financial position, including the net asset position and the composition of the assets. It was concluded that the financial position was strong, despite deteriorating over the previous four years due to sustained losses that had reduced the net asset position;
- the liquidity ratio to provide an indicator of the Shire’s ability to meet short term creditor obligations. The conclusion was that, whilst the

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722 The Jarrahdale Heritage Park Management Plan that underpinned the Regional Partnerships application included an estimate of $365 000 per annum for the cost of general landscape maintenance. It also included ongoing park management costs of $15 000 per annum for weed removal and $5 000 per annum for brook management. The Plan also indicated that there would be ongoing costs for traffic management (which was to be the subject of a road study), environmental management and repair (which was to be assessed following finalisation of an Environmental Management Plan) and heritage management (which was to be assessed based on individual programs identified).
ratio had deteriorated, significant cash holdings as at 30 June 2003 would be sufficient to meet all short term creditor obligations;

- the level of gearing (borrowing). The conclusion was that the gearing ratio was low, reflecting the relatively small levels of debt;

- earnings analysis examining trends in profitability over the four year period to 30 June 2003. This analysis found that earnings had deteriorated over the last three years (with losses recorded in each of these years), reflecting an underlying increase in operating expenditure, principally on road infrastructure. The conclusion was that, given the deterioration in earnings, future financial performance of the Shire should be monitored by DOTARS to ensure that, should short term liquidity issues arise, they do not impact on co-funding arrangements for the construction of the Heritage Park; and

- the fact that the Shire is to fund ongoing maintenance and operation for the Heritage Park and that this additional funding pressure was likely to impact the Shire’s earnings in the short term, however, this may be offset in the future by increased taxation revenue from regional economic activity.

2.57 In terms of gearing, in September 1999, the Shire produced a Business Plan related to its proposal to borrow $605 000 for the original acquisition of land for part of the Jarrahdale Heritage Park. The debt of $605 000 was retired in 2003–04 through the subdivision and sale of six cottages in Millars Road, Jarrahdale and the subdivision and sale of seven lots of vacant land on the corner of Kingsbury Drive and Jarrahdale Road, Jarrahdale. The September 1999 Business Plan also highlighted the intention of Council to develop the remaining land in the Park. The sale of assets in order to reduce debt levels was not considered in the external viability assessment’s discussion of the Shire’s gearing levels.

2.58 In addition, neither DOTARS’ assessment (completed on 31 May 2004) nor the post-approval external viability assessment (accepted by DOTARS on 15 July 2004) examined the March 2004 Jarrahdale Heritage Park Development and Disposition of Property Business Plan. The Business Plan outlined that the Shire proposed to borrow $1 million to assist in the development of the Park, with the intention of disposing of Shire-owned land to meet interest payments and the retirement of the $1 million debt. At its meeting in April 2004, Council

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723 As noted in Minutes of Ordinary Council Meeting of 28 August 2006, p. 45.
agreed to commence implementing the land transactions as described in the March 2004 Jarrahdale Heritage Park Development and Disposition of Property Business Plan.\textsuperscript{724}

2.59 At its 28 August 2006 Ordinary Meeting, Council adopted its budget for 2006–07. The budget included an interest only loan of $1 280 000 for the Jarrahdale Heritage Park project as per Council’s forward financial plan. In adopting the 2006–07 budget, Council noted that the Jarrahdale Heritage Park Business Plan provides for this loan to be repaid in 2009–2010.

\textit{Managing risk through the Funding Agreement}

2.60 To address its findings, the external viability assessment recommended that DOTARS annually monitor the Shire’s earnings performance. It further recommended that the Shire be required to provide DOTARS with a copy of its annual accounts so that DOTARS could regularly monitor (at least annually) the financial performance of the Shire over the term of the Funding Agreement.

2.61 However, these recommendations were not addressed in the Funding Agreement. Nor has DOTARS otherwise obtained and analysed data on the Shire’s financial performance. ANAO notes that the Shire continued to report substantial operating losses in 2003–04, 2004–05 and 2005–06. In this respect, in November 2007, the Shire advised ANAO that:

\begin{quote}
The reason why the Shire’s financial performance has had operating losses in the mentioned periods is mainly due to the Shire’s infrastructure assets which form a large component of total assets. The depreciation costs (a non-cash expense) for our infrastructure assets for each year is estimated at around $2.7 million which has a significant impact on our financial performance. This is a common occurrence amongst other Local Governments as we all have a large infrastructure asset base and the need to account for this, is a regular topic of discussion at Local Government forums.
\end{quote}

\textit{ANAO conclusion}

2.62 Applicant viability risks were not addressed by DOTARS before recommending to the then Parliamentary Secretary that she approve the spending proposal.

\textsuperscript{724} ibid.
Cost under-estimations

2.63 The Internal Procedures Manual in place at the time this application was assessed defined project viability as evidence that the project outcomes are sustainable beyond the funding period, and that the project has been appropriately costed. In this respect, the internal procedures required that assessors analyse whether quotes had been obtained for the cost items and whether the costs were reasonable for the region.

2.64 Most of the Regional Partnerships funds were to be used for construction of important elements of the Park. In this respect, Annexure B to the signed Funding Agreement provides as follows:

- $9 000 in Regional Partnerships funds relating to the second milestone (Foundation works) would be used to complete the amphitheatre. The initial Regional Partnerships payment of $149 000 (plus GST) made on 8 October 2004 covered works under this milestone;
- $30 000 in Regional Partnerships funds relating to the third milestone (Improved access) was for footbridge construction across Gooralong Brook to link walking trails. The second Regional Partnerships payment of $160 500 (plus GST) made on 25 January 2006 covered works under this milestone;
- $80 000 in Regional Partnerships funds relating to the fourth milestone (Improved facilities) was for construction of picnic decks. The second Regional Partnerships payment also covered works under this milestone;
- $35 000 in Regional Partnerships funds relating to the fifth milestone (Preparation for major construction) is for completion of previous projects;
- $265 000 in Regional Partnerships funds relating to the sixth and seventh milestones (Major construction) is for the construction of viewing towers and the aerial walkway; and
- $100 000 in Regional Partnerships funds relating to the seventh milestone (Major construction) is for the repair and renovation of an existing wooden rotunda.

2.65 The external viability assessment obtained by DOTARS after the then Parliamentary Secretary’s funding approval stated that:

Given that cost assumptions are key to ensuring the project is adequately funded, we would recommend that review by appropriate experts is undertaken to minimise the risks of cost over or understatement.

2.66 DOTARS has not addressed this risk in the way recommended. In this respect, the 2004 project Implementation Plan prepared by the Shire (after Regional Partnerships funding had been approved) highlighted the deficiency of detailed planning for the project. This included significant cost underestimations, as summarised in Table 2.2, which were advised to DOTARS in September 2005.

Table 2.2
Cost increases

<table>
<thead>
<tr>
<th>Cost element</th>
<th>Regional Partnerships Application</th>
<th>September 2005 Advice to DOTARS from Council</th>
<th>ANAO comment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aerial Walkway</td>
<td>$350 000</td>
<td>$600 000</td>
<td>71 per cent increase in cost. Development application approved in July 2006 but construction is not to proceed until a Park business plan is completed that confirms this aspect.</td>
</tr>
<tr>
<td>Amphitheatre</td>
<td>$80 000</td>
<td>$350 000</td>
<td>340 per cent increase in cost. Amphitheatre was to have been completed with the first Regional Partnerships payment made in October 2004 – it is now not expected to be finished until 2007.</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS and Shire documentation.

Amphitheatre

2.67 The Park is to include an amphitheatre, described as follows by the Shire on its website:

An amphitheatre for festival and performance events is planned to be one of the highlights of the Park. Lawned terraces will allow the space to accommodate up to 500 patrons. With the backdrop of trees, a black steel stage structure will be set back within the leaves, so as to not be an intrusive element when not in use. The amphitheatre will be stunning, comfortable and practical.
2.68 The Management Plan submitted with the Shire’s Regional Partnerships application on 30 March 2004 estimated that it would cost $80 000 to construct the amphitheatre. The application stated:

Local and state funding has already allowed commencement of an amphitheatre project for staging a wide range of events.\footnote{In November 2007, the Shire advised ANAO that initial Shire and Regional Development Scheme funding allowed for preliminary concept designs.}

2.69 The first Regional Partnerships payment of $149 000 (plus GST) made on 8 October 2004 was to cover the following two milestones:

i) Detailed planning and commencement of initial projects: Architectural and management plans, safety checks on existing buildings, urgent minor works and continuation of current projects, planning permission. (Expected completion date – 3 months from commencement (January 2005))

ii) Foundation works: site clearing (including Work-for-the-Dole), contractors appointed, purchase of initial materials, completion of amphitheatre. (Expected completion date – 6 months from commencement (April 2005)) [\textit{ANAO emphasis}]

2.70 The first project progress report was provided to DOTARS in May 2005 (it was due on 1 April 2005). The Shire advised DOTARS that it had:

only expended $125,000 (GST included) of $163,900 provided as the first payment by DOTARS for this project.\footnote{The Shire advised ANAO in November 2007 that it had only ever expended funds on legitimate items related to the milestones and where it was not appropriate or possible to expend funds the Shire reported this under expenditure to DOTARS.}

2.71 In terms of the amphitheatre, which was to have been completed using funds provided in the first payment, the Shire advised DOTARS that:

[\textit{we} employed consultants to provide a detailed design of the amphitheatre. There was no initial interest received from developing the facility recommended in the development plan. Responses indicated that what was suggested was grossly under-funded. Consultants recommended repositioning the amphitheatre from the south side to the north side of the Gooralong Brook and presented an attractive and functional facility. This facility however is significantly more costly than originally envisaged.}

2.72 In September 2005, the Shire asked DOTARS to agree to a redistribution of project funds from restoration of the timber rotunda to the aerial walkway. At this time, the Shire also provided the following advice in relation to the amphitheatre:
The proposed amphitheatre project has increased in budget from $80,000 to $350,000. This budget increase is the result of detailed planning and community consultation which demonstrated that the desired result was to create a regionally significant outdoor arts venue. Planning approval has been achieved for the amphitheatre and construction tender documents completed.

2.73 The Shire advised DOTARS that the amphitheatre (and the aerial walkway) should be completed in 2006. Accordingly, the Funding Agreement was formally varied on 27 October 2005, with construction of the amphitheatre to commence in March 2006 and be completed in September 2006.

2.74 However, at the time of ANAO’s May 2006 site visit, construction work had yet to commence (as shown in Figure 2.2). Subsequently, at its August 2006 Ordinary Meeting, Council was advised that the amphitheatre would not be completed in time to be used for the January 2007 Australia Day celebrations. In February 2007, DOTARS advised ANAO that:

The information provided by the applicant indicated that the initial intention had been to site the amphitheatre on the south side of the ‘Gooralong Brook’ and any work that had commenced would have been focused on this site. The detailed planning resulted in the site moving to the north end of the ‘Gooralong Brook’ – and so any earlier work that had been undertaken would need to commence at the ‘new site’. This does not make the initial statement in the application inaccurate – just that as the project progressed the situation changed.

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728 In November 2007, the Shire advised ANAO that the timeframes could not have predicted the overheated building market or that development approval would be subject to the preparation of a business plan. The Shire further advised that construction had not commenced in May 2006 as development approval was not granted until July 2006 and was subject to the preparation of a business plan which only received the endorsement of Council in September 2007.
Figure 2.2
Site cleared for construction of amphitheatre

Source: ANAO site inspection May 2006.

Rotunda

2.75 The rotunda was located on lot 814, which was identified in the 30 March 2004 Regional Partnerships application as being part of the site of the Heritage Park project.

2.76 The Park Business Plan, as revised in March 2004, included the following estimated income from land sales:

<table>
<thead>
<tr>
<th>Year</th>
<th>Estimated Income</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004–2005</td>
<td>$140 000 (1 cottage, vacant lot)</td>
</tr>
<tr>
<td>2005–2006</td>
<td>$90 000 (1 cottage)</td>
</tr>
<tr>
<td>2006–2007</td>
<td>Nil</td>
</tr>
<tr>
<td>2007–2008</td>
<td>$765 000 (Lot 814)</td>
</tr>
</tbody>
</table>

2.77 In June 2005, the Shire was approached by representatives of Little Creatures Brewing Pty Ltd (Little Green Steps Pty Ltd is the subsidiary company) who expressed an interest in establishing a boutique brewery in Jarrahdale. Following investigation of an alternative privately owned site, which turned out to be unsuitable, Little Green Steps Pty Ltd identified a five hectare site in the northwest corner of Lot 814 as the most appropriate site for their development.
2.78 The land in question was held in freehold by the Shire. It incorporated the single men’s quarters, the rotunda and a skateboard facility.

2.79 On 13 September 2005, the Shire wrote to DOTARS seeking agreement to the redistribution of $140 000 in Regional Partnerships funding that was to be used on restoration of the timber rotunda.\textsuperscript{729} The Shire proposed to instead use these funds toward the cost of constructing the aerial walkway. In support of its request, the Shire advised DOTARS that:

As stated in the first acquittal, funds of the first payment were not fully expended due to the need for substantial detailed planning to be undertaken. This need became apparent once the Project team tried to commence the project works Implementation Plan and found that this work had not been undertaken. This detailed planning has not only attended vital considerations such as Native Title clearance but has uncovered considerable cost under-estimations of various park elements.

The outcomes of the detailed planning is the basis for this request for a redistribution of the Regional Partnerships funds which is in keeping with the original funding intent while identifying the key park projects and defining achievable goals.

2.80 In making this request, the Shire did not advise DOTARS that it was negotiating to sell the land on which the rotunda was located. In this respect, in November 2007, the Shire advised ANAO that the sale of the land was consistent with the Development and Disposition of Property Business Plan of April 2004 which had been provided to DOTARS in June 2004.

2.81 The sale was finalised in August 2006. The sale contract involved a purchase price of $550 000. The contract requires Little Green Steps Pty Ltd to renovate and maintain the single men’s quarters and the rotunda. Little Green Steps Pty Ltd was also required to relocate the Skate Board facility to a location acceptable to the Jarrahdale community and the Shire of Serpentine-Jarrahdale.

2.82 According to Shire documents held by DOTARS, the sale of this land was consistent with the Jarrahdale Heritage Park Development and Disposition of Property Business Plan approved by Council in April 2004. This land sale will also reduce the level of Council debt for the Heritage Park project. More broadly, the Minutes of Council’s August 2006 Ordinary Meeting state that:

\textsuperscript{729} Annexure B to the Funding Agreement specifically identifies $100 000 in Regional Partnerships funds to be used for the rotunda, not the $140 000 amount stated by the Shire in its request to DOTARS.
The establishment of Little Creatures in Jarrahdale will fulfil a range of objectives in progressing the Jarrahdale Heritage Park development. It will act as a major catalyst for people to visit Jarrahdale and therefore stimulate the town and the economy whilst providing much needed employment for locals. This in essence is why the Council has supported the development of the Jarrahdale Heritage Park.

2.83 Nevertheless, this land transaction would have resulted in some elements of the Heritage Park being owned by the private sector rather than the Shire or the National Trust.

2.84 However, the progress report provided by the Shire to DOTARS in January 2007 stated that, in October 2006, the Shire had been formally advised by the Directors of Little Green Steps that they would not be proceeding with the purchase of five hectares of land at the Park site. The Shire further advised DOTARS that it was actively attempting to attract other commercial interests to the Park site, and was seeking to engage a consultant to prepare a Business Plan for the Park so as to set the foundation on which future decision making by the Shire would be made. In November 2007, the Shire advised ANAO that:

It was becoming apparent that project costs for the main attractions of the amphitheatre and aerial walkway were increasing. The Shire needed to look at how these costs could be covered within the constraints of existing funding arrangements as well as by the utilisation of its own assets. As a result the Shire sought a contract variation of its Regional Partnerships funding. In terms of asset utilisation, the Shire was open to more effective ways of being able to satisfy its short and long term financial commitments to the Park. The rotunda was not likely to be a profit generating restoration, but more an act of heritage preservation. Therefore, the request to reallocate the funds from the rotunda to the amphitheatre and aerial walkway was based primarily on covering the increase in costs for these main attractions. However, the attempt to require the private enterprise financing of the rotunda restoration in the proposed Contract of Sale was an attempt to ensure the overall Park objectives were still met. It is important to note that the Contract of Sale was subject to multiple provisions being met prior to the contract being implemented. As was the case, these multiple provisions could not be met and the contract was never realised. The Shire had to make the request for the distribution of the rotunda funds regardless, as any outcome from the Contract of Sale could not be guaranteed.
Aerial walkway

2.85 As mentioned, in September 2005, the Shire asked DOTARS to agree to a redistribution of project funds from restoration of the timber rotunda to the aerial walkway. The Shire advised DOTARS that:

The initial budget for the aerial walkway, as stated in the JHP Management Plan, was $350,000. This amount was funded by the $250,000 from Regional Partnerships\(^{730}\) and $100,000 from the Shire and other contributors. While this estimate may be adequate for the 35m suspension bridge it would not include the connecting walk-bridges required to connect from the car-park to the Old Post Office ‘allowing access for all’ use. That the bridge achieves this connection is vital to the park plan as outlined in the Interpretation Plan. Based on a similar pedestrian bridge project in Donnybrook, completed in 2005, the budget estimate is $600,000.

2.86 The Shire advised DOTARS that the aerial walkway should be completed in 2006. The variation to the Funding Agreement signed on 27 October 2005 stated that construction of the aerial walkway would commence in March 2006 and be completed in September 2006.

2.87 However, at the time of ANAO’s May 2006 site visit, construction work had yet to commence. In fact, it was not until Council’s Ordinary Meeting of 24 July 2006 that the application for development of an aerial walkway, footbridge and car park was approved, subject to conditions. Key among these conditions is that:

Construction not proceed on an aerial walkway until completion of a business plan for the Jarrahdale Heritage Park which confirms construction of the aerial walkway.\(^{731}\)

ANAO conclusion

2.88 As recognised by the Regional Partnerships Programme Guidelines, the appropriate costing of projects is an important issue to be addressed by DOTARS when assessing project viability. However, in assessing the Jarrahdale Heritage Park Project, the documented procedures for scrutinising

\(^{730}\) In actual fact, Annexure B to the signed Funding Agreement discloses that $265 000 in Regional Partnerships funds relating to the sixth and seventh milestones (Major construction) is for the construction of viewing towers and the aerial walkway.

\(^{731}\) Similar to the amphitheatre (see footnote 728), in November 2007, the Shire advised ANAO that the timeframes could not have predicted the overheated building market or that development approval for the aerial walkway would be subject to the preparation of a business plan. The Shire further advised that construction had not commenced in May 2006 as development approval was not granted until July 2006 and was subject to the preparation of a business plan which only received the endorsement of Council in September 2007.
the cost of the project were not implemented by DOTARS. As a result, the risk of delays and cost increases was not addressed by DOTARS prior to recommending that the project be approved for funding by the then Parliamentary Secretary.

2.89 There have been significant delays and increases in the cost of the project. In this respect, in May 2007 the Shire of Serpentine-Jarrahdale advised DOTARS that one reason for the extensive delays in the project was the inadequate planning and design (including of costs) undertaken at the time the application was submitted (see paragraph 2.120).

**Payment arrangements**

2.90 The Regional Partnerships application form completed by the Shire advised that:

Regional Partnerships payments are linked to the achievement of milestones.

2.91 In its application, the Shire indicated that it was seeking Regional Partnerships funds as a contribution to each of the eight milestones. The relevant milestones, expected timing and cost item for which the Shire proposed to use Regional Partnerships funds are outlined in Table 2.3.
Table 2.3
Milestones and nominated payments included in the Shire’s application

<table>
<thead>
<tr>
<th>Milestone</th>
<th>Month Due</th>
<th>Cost item</th>
<th>Payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Detailed planning &amp; commencement of initial projects</td>
<td>Sep 04 (2 months after commencement)</td>
<td>Architectural and management plans</td>
<td>$60 000</td>
</tr>
<tr>
<td>2. Foundation works</td>
<td>Dec 04 (5 months after commencement)</td>
<td>Site Clearing (including Work-for-the-Dole)</td>
<td>$20 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Purchase of initial materials</td>
<td>$60 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Completion of amphitheatre</td>
<td>$9 000</td>
</tr>
<tr>
<td>3. Improved access</td>
<td>Mar 05 (8 months after commencement)</td>
<td>Installation of initial signage</td>
<td>$20 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Bridge construction</td>
<td>$30 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Upgrading of trails</td>
<td>$7 500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Clearing and safety works for major projects</td>
<td>$11 000</td>
</tr>
<tr>
<td>4. Improved facilities</td>
<td>June 05 (11 months after commencement)</td>
<td>Construction of Picnic Decks</td>
<td>$80 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Completion of signage &amp; promotion</td>
<td>$12 500</td>
</tr>
<tr>
<td>5. Preparation for major construction</td>
<td>Sept 05 (14 months after commencement)</td>
<td>Completion of previous projects</td>
<td>$35 000</td>
</tr>
<tr>
<td>6. Major construction</td>
<td>Dec 05 (17 months after commencement)</td>
<td>Viewing towers</td>
<td>$90 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Aerial Walkway</td>
<td>$100 000</td>
</tr>
<tr>
<td>7. Major construction</td>
<td>Jan 06 (18 months after commencement)</td>
<td>Rotunda</td>
<td>$100 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Continuation of Towers &amp; Walkway</td>
<td>$75 000</td>
</tr>
<tr>
<td>8. Site works major launch</td>
<td>Mar 06 (20 months after commencement)</td>
<td>Completion of projects</td>
<td>$40 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Promotion</td>
<td>$10 800</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td><strong>$760 800</strong></td>
</tr>
</tbody>
</table>


2.92 However, the staged payment approach suggested by the Shire in its application would not have accorded with DOTARS’ usual approach to structuring Regional Partnerships project payments. DOTARS’ preferred
approach has involved a smaller number of payments, with a substantial first payment being made upon signing of the Funding Agreement.\footnote{732 Where Ministerial funding approval was obtained late in the relevant financial year, ANAO observed a number of instances in which DOTARS paid an even larger proportion of the grant amount upon signing the Funding Agreement in order to increase Programme expenditure for that financial year. For this project, as the external viability assessment was not completed before the end of the financial year, the incentive to ‘front-load’ payments to the same extent did not exist. See further discussion of ANAO’s analysis of this issue in Chapter 2 in Part 5 of the main audit report on Managing for Outcomes.}

2.93 Accordingly, the draft Funding Agreement Schedule provided to the Shire by DOTARS on 20 August 2004 proposed fewer payments (five rather than the eight proposed by the Shire), with payments scheduled to be made in advance of the timing requested by the Shire. This is illustrated in Figure 2.3.

**Figure 2.3**

Proposed payment profile – Application vs Funding Agreement

![Proposed payment profile – Application vs Funding Agreement](image)

Source: ANAO analysis of the terms of the Shire of Serpentine-Jarrahdale’s application, draft Funding Agreement Schedule prepared by DOTARS and final signed Funding Agreement.

2.94 There was no negotiation between the Shire and DOTARS concerning the payment profile included by DOTARS in the draft Funding Agreement Schedule. This is unsurprising given DOTARS was proposing earlier and
larger payments than the Shire had sought in its application. In November 2007, the Shire advised ANAO that:

It was not for the Shire to direct DOTARS to alter its Funding Agreement schedule given the Shire’s proposed payment profile had formed part of the original application and therefore, it would be assumed, had been given due consideration.

2.95 A recommendation of the external viability assessment that was addressed by DOTARS in preparing the Funding Agreement involved the payment of Commonwealth funds being linked to identifiable milestones that include the provision of funds by the applicant. In this respect, the Funding Agreement included a pre-condition that the second and subsequent milestone payments would not be made until the Shire had provided satisfactory confirmation that all other funds linked to the milestones covered in the payment had been or would shortly be received. However, in its administration of the Funding Agreement, DOTARS did not require the Shire to provide such confirmation before making payments.

2.96 The second payment of Regional Partnerships funds of $160 500 was made by DOTARS on 25 January 2006. It was to cover the third and fourth milestones. These milestones and the related amounts the Shire sought in its application to be contributed by the Regional Partnerships Programme and other partners are outlined in Table 2.4.

**Table 2.4**

**Second Regional Partnerships payment: funding shares**

<table>
<thead>
<tr>
<th>Milestone</th>
<th>Regional Partnerships funds</th>
<th>Partner co-funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Improved access: installation of initial signage; improved road access, traffic calming and intersection safety; bridge construction; upgrading of trails; clearing and safety works for major projects</td>
<td>$68 500</td>
<td>$56 500</td>
</tr>
<tr>
<td>Improved facilities: construction of picnic decks, completion of signage and promotion</td>
<td>$92 500</td>
<td>$82 500</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$161 000</strong></td>
<td><strong>$139 000</strong></td>
</tr>
</tbody>
</table>

Note A: The second Regional Partnerships payment specified in the Funding Agreement was $160 500 rather than the $161 000 sought by the Shire in its application. The additional $500 was added to the final payment (the Funding Agreement specified $51 300 for completion of projects and launch and promotion whereas the Shire sought $50 800 for this part of the project in its application).

2.97 However, the second Regional Partnerships payment was made without DOTARS having obtained any confirmation that $139,000 in partner funds for the relevant milestones had been received or would shortly be received from the Shire, the National Trust and/or the Peel Development Commission, as required under the Funding Agreement. In November 2007, the Shire advised ANAO that this confirmation could have been provided, had it been sought.

2.98 DOTARS also sought to manage the risks regarding cost assumptions identified by the external viability assessment by making the payment of second and subsequent Regional Partnerships instalments contingent on the Shire providing satisfactory confirmation of all cost assumptions associated with the milestones covered in the payment. However, this provision was also not effectively administered by DOTARS.

2.99 For example, the second Regional Partnerships instalment payment was specified in the Funding Agreement to cover the third and fourth project milestones. In this respect, $80,000 of the Regional Partnerships funds identified against the fourth milestone (improved facilities) was for construction of picnic decks. Rather than providing confirmation of the cost of the picnic decks, the Shire advised DOTARS that schematic designs had been completed by architects, with final construction documents being prepared. No advice was provided to DOTARS on the estimated cost of the picnic decks. DOTARS did not seek such advice prior to making the second payment in January 2006.

2.100 The Shire advised ANAO in May 2006 that construction of the picnic shelters was, at that time, out to tender. The development approval obtained by the Shire on 20 March 2006 included shelters in three locations within the Park, but the Shire advised ANAO that the number of picnic shelters that would be constructed would depend on the costs that resulted from the tender. The Shire further advised ANAO in November 2007 that ‘true’ costs would not be known until tenders had been received.

2.101 In July 2006, the Shire provided its third progress report to DOTARS. The Shire advised DOTARS that:

During the months of May and June 2006, quotations were sought from local builders to construct the shelters, toilets, and other infrastructure however no submissions were received. Western Australia is currently experiencing significant and unprecedented growth in the building and development sectors which is making it extremely difficult to source qualified and skilled
contractors to construct infrastructure within the park. Hence, quotations will be called again in August 2006 to source local builders to implement this key component of the JHP project.

**ANAO conclusion**

2.102 Payments were made by DOTARS in advance of need. Having regard to the viability risks evident for this project, this approach placed Commonwealth funds at increased risk.

2.103 Further, Funding Agreement requirements designed to link the payment of Regional Partnerships funds to the receipt of partner contributions and the confirmation of cost assumptions were not administered effectively by the department such that DOTARS did not require the Shire to satisfy either of the pre-conditions identified in the Funding Agreement prior to making the second payment.

**Project monitoring**

2.104 According to budget included in the Regional Partnerships Funding Agreement,\(^{733}\) the Regional Partnerships Programme was to be the single largest provider of cash to the Jarrahdale Heritage Park project, with the Funding Agreement providing that the Programme would provide 52 per cent of the cash costs of $1 453 387. Other funds were to come from the Shire (39 per cent), the National Trust (six per cent) and the Peel Development Commission (three per cent). In this context, as of February 2007, the Shire had:

- submitted four progress reports;
- entered into two variations to the Funding Agreement; and
- received $309 500 in Regional Partnerships funds.

**Contract variations**

2.105 In October 2005, DOTARS and the Shire finalised the first variation to the Funding Agreement. Although the Funding Agreement still specified an Activity Period of two years, the final milestone was not expected to be completed until September 2006 (an Activity duration of 27 months). Variations were made to the expected completion dates for the various

\(^{733}\) In November 2007, the Shire advised ANAO that it will be the single largest provider of cash to the project with $1.2 million provided to date, which the Shire stated was double the cash contribution outlined in the original Regional Partnerships application.
milestones, the proposed payment due date for the remaining Regional Partnerships payments and the due date for remaining progress reports.

2.106 A second variation to the Funding Agreement was apparently agreed in July 2006, extending the completion date for the project to 31 October 2007 (an Activity duration of 40 months). Consequential changes were also to be made to vary project milestones, grant payment release dates, report dates and allocation of amounts to project components. In providing this proposed variation to the Shire, DOTARS stated that:

As this project is already well behind schedule, no further extensions will be approved beyond 31 October 2007.

2.107 DOTARS records include correspondence from the Shire stating that a contract variation had been signed and sent back to DOTARS. However, the Regional Office files made available to ANAO did not include this completed variation.

2.108 On 10 November 2006, ANAO requested that DOTARS provide a signed copy of the second variation. DOTARS provided ANAO with a copy of a Funding Agreement variation signed by the Shire on 2 February 2007, and received by the department on 6 February 2007. In November 2007, the Shire advised ANAO that it would appear that the contract variation signed in February 2007 was the July 2006 agreement that was reflective of the anticipated schedule as at July 2006.

Project progress

2.109 The varied Funding Agreement finalised on 2 February 2007 stated that significant parts of construction activities should have commenced or been completed by January 2007. Specifically:

- construction should have commenced on the aerial walkway, amphitheatre and roadworks, head works and infrastructure services; and

- construction should have been completed in respect to the shelters and toilets, pedestrian bridges, walk trails and signage.

2.110 The only element of the project that was not required to be under construction or completed as of January 2007 was the viewing tower. The varied Funding Agreement finalised on 2 February 2007 stated that construction of the tower was expected to commence in February 2007.
However, the most recent (January 2007) progress report submitted by the Shire had advised the department that:

- detailed design and preparation of tender documentation had been prepared for the higher profile infrastructure works, with the exception of the viewing tower which had not been finalised due to delays in the adoption of the concept design;
- planning and building approvals had been obtained for the higher profile works;
- some of the walking trails had been constructed and car parking and other road infrastructure had also been constructed;
- tenders for the construction of shelters, toilets and some infrastructure had been called but no submissions were received. As a result, re-tendering was required; and
- construction of the high profile aspects would not commence until a business plan for the Park had been completed and endorsed by Council, and this was expected to take some months.

2.111 Subsequently, on 18 May 2007, the Shire advised DOTARS that:

This application for a contract variation relates to a reduced scope of works to reflect the increased costs stemming from the finalisation of the detailed design of project elements and market increases in construction costs. A variation is also sought in respect to the project timeline that is necessary to accommodate the likely availability of contractors in the current building climate. Principally the impetus for change arises from the preliminary report from the Business Plan consultants which is recommending that after establishing the basis facilities in the Park in Stage II, only then should the Shire proceed with Stage II and build the key attractions which would include the viewing tower, amphitheatre and aerial walkway.

*Site inspections*

2.112 In this context, the various versions of DOTARS’ Regional Partnerships Internal Procedures Manual have included risk-based criteria for the conduct of site inspections as part of DOTARS’ management of Regional Partnership grants. The Manual current at the time of audit fieldwork (September 2005 version) stated as follows in relation to site visits:

The purpose of a site visit is to obtain some level of confidence that Australian Government funding is being spent appropriately and the project is proceeding satisfactorily.
A risk management approach to site visits is recommended. Site visits should be undertaken by Regional Office staff depending on their respective work schedules (i.e. they may coincide with an ACC meeting). Where there is a Steering Committee with ACC representation, site visits may not be necessary. ACC’s may be able to assist in remote regions.

…A project Monitoring matrix has been developed by National Office to assist Regional Offices to determine the appropriate number and timing of site visits according to the nature and size of a project.

2.113 The Internal Procedures Manuals applicable between June 2004 and 2 May 2007 included a table of project risk thresholds intended to guide the conduct of site visits and other project monitoring activities. Specifically, except for projects with a Regional Partnerships funded value of less that $50 000 payable to Local Government Authorities or non-profit organisations, there was to be at least one site visit to all funded projects during their life. For projects with Local Government Authorities receiving greater than $250 000 in Regional Partnerships fund, the Internal Procedures Manual required that Regional Offices develop a monitoring plan to co-ordinate a site visit schedule with the milestone schedule, and that random visit be undertaken by the Regional Office and National Office.\textsuperscript{734}

2.114 Notwithstanding the delays and difficulties experienced with respect to this project, it was not until 5 April 2007 that DOTARS undertook a site inspection, over 2½ years after the first Regional Partnerships payment was made in October 2004 and four months after the ANAO had provided the department with a case study on this project. This visit confirmed that little infrastructure construction activity had occurred.\textsuperscript{735}

Status of project

2.115 As at September 2007, $309 500 (plus GST) in Regional Partnership funds had been paid to the Shire, representing 41 per cent of the total approved funding.

2.116 Under the Long Form Standardised Funding Agreement used for this project (and most of the projects in the audit sample), funding recipients are

\textsuperscript{734} The original (July 2003) version of the Internal Procedures Manual did not include this table, but also advised that each project should have at least one site visit. This version of the Manual had been replaced prior to the Funding Agreement for the Jarrahdale Heritage Park project being executed.

\textsuperscript{735} The audit report on Outcomes and Financial Management discusses revised procedures for the conduct of site visits set out in a revised Chapter of the Internal Procedures Manual relating to ‘Funding Agreement Management and Completion’ issued on 3 May 2007.
required to provide acquittals of the receipt and expenditure of Regional Partnerships and other funding received in respect to the project. Due to the Shire not providing an acquittal, and delays in project progress, in March 2007, DOTARS decided that it should commence action to terminate the project and have the unacquitted funds returned.

2.117 As noted, on 5 April 2007, DOTARS conducted a site visit to the site of the proposed Park.

2.118 On 12 April 2007, the National Trust wrote to DOTARS proposing a variation to the Funding Agreement to allow some of the Regional Partnerships funds to be used to prepare a master plan for the timber mill located on the same National Trust land on which the Park was to be constructed. On 24 April 2007, DOTARS advised the National Trust that such requests would need to be made by the Shire, as the party to the Funding Agreement. In these discussions, the National Trust advised DOTARS that it was concerned about the lack of progress with the Park project, and that it was considering whether it should seek to take over the management of the project.

2.119 On 4 May 2007, DOTARS wrote to the Shire requiring it to provide the outstanding acquittal by 18 May 2007 (see Figure 2.4).
The Shire responded to the department on 18 May 2007, advising that $58,885.30 of the $160,500 second instalment paid by DOTARS on 25 January 2006 had been spent. The Shire advised that it would be seeking a Funding Agreement variation for the remaining funds relating to the remaining six project milestones. In respect to the continuing delays with the project, the Shire advised DOTARS that:

It also needs to be acknowledged that the extent of detailed planning, design and tender documentation required and the infrastructure services needed to facilitate full implementation of the project were not appreciated at the time of lodging the initial grant application. True costs for construction will not be known until tenders are called. Furthermore, this project was not underpinned by a comprehensive and detailed Business Plan that evaluated and ensured the long term sustainability of the Park. As responsible custodians of the Commonwealth’s funding and the Shire’s capital, it was incumbent on the

736 In this respect, see paragraph 2.106 where DOTARS advised the Shire of Serpentine-Jarrahdale on 25 May 2006 that no further extensions would be approved.
Shire’s Executive to complete the detailed planning, install essential services and undertake the Business Plan prior to proceeding with calling tenders and the further expenditure of grant and other monies.

I find it understandable that the department may have perceived that there has been a lack of progress on this project, as much of this necessary preparatory work has not resulted in the built structures outlined in the Agreement being constructed within the Park. I am confident that a thorough review of the information provided will lead the department to conclude that considerable progress has been made and that those items that have been completed form the essential building blocks for the successful development of the Park. To have built these project elements in the absence of this preparatory work would not only have been irresponsible but actually impossible in many respects.

2.121 On 28 August 2007, DOTARS advised the Ministerial Committee that:

A Funding Agreement was executed on 1 October 2004 and payments totalling $340,450 (GST inclusive) have been made. Work on the project has been slow and has now stalled, and following a round of consultation with parties involved in the project, the Department has concluded that the original project scope is no longer achievable, without further funding.

The funding recipient has produced a draft business plan for a revised project, however this business plan is underdeveloped and contains budget, partner and project viability issues.

Accordingly, the Department considers that a new application should be developed, underpinned by a comprehensive business plan that addresses issues relating to costs, partner funding and viability issues.

To date Regional Partnerships has contributed to one pedestrian bridge, extensive walking trails and one section of road. This work represents discrete elements of the project and can be considered to be infrastructure improvements in their own right.737

2.122 The department recommended that:

- the Ministerial Committee agree to reducing the scope of the project to the work already completed, obtaining a full acquittal of Regional Partnerships funds for the components completed to date and terminating the Funding Agreement; and

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737 In this respect, as noted, the department did not have an acquittal identifying what, if any, funding had been contributed to those activities by the Shire or other parties.
• the department write to the Shire advising it of the Committee’s decision and inviting it to submit a new application for the remaining activities.

2.123 The members of the Ministerial Committee agreed to the department’s recommendation on 19 September 2007. On 8 October 2007, DOTARS advised ANAO that a letter advising of the decision had yet to be provided to the Shire. The Shire advised ANAO that, as at 5 November 2007, it had yet to receive advice from DOTARS of the Ministerial Committee’s decision.

*ANAO conclusion*

2.124 This project was approved for funding in June 2004 with an estimated project duration of 24 months. By September 2007, more than three years after funding was approved, construction had yet to be commenced on the major elements of the project for which Regional Partnerships funding was approved and the department had concluded that the original project scope was no longer achievable, without further funding. The Ministerial Committee had agreed to reduce the scope of the project to the work already committed, obtain an acquittal for the $309,500 (plus GST) in Regional Partnerships funds already paid and terminate the Funding Agreement.

2.125 The May 2007 advice from the funding recipient in relation to project progress underscored the under-developed nature of the project at the time of the department’s May 2004 assessment, which concluded that the project satisfied each of the Regional Partnerships assessment criteria and represented low viability risks. The nature of that advice and the department’s September 2007 advice to the Ministerial Committee also emphasises the value that would have been obtained from greater attention having been paid to the findings and recommendations of the external viability assessment conducted in relation to a commercial project being undertaken by a Local Government Authority.
3. Redevelopment of Geraldton Surf Life Saving Club

This case study examines RP00769 Redevelopment of Geraldton Surf Life Saving Club. This project involved a small non-profit organisation of limited financial means obtaining significant funds from a range of different sources in order to undertake a major building redevelopment. The project was expected to be completed over a period of at least two years in an environment of escalating construction costs. At the time Regional Partnerships funding was approved, the Programme was the largest single contributor of cash to the project costs. Costs have increased substantially, with a 20 per cent increase in Regional Partnership funding being approved in May 2007 to assist the funding recipient meeting these costs.

Introduction

3.1 The Geraldton Surf Life Saving Club (GSLSC) was established in 1930. The GSLSC patrols Back Beach in Geraldton, Western Australia and in 2004–05, undertook 26 rescues.738

3.2 The GSLSC is a small non-profit organisation. In 2004–05, it had 319 members739, with total assets of $390 840, liabilities of $29 013 and made a net profit of $9 893 on total income of $134 708.740 The GSLSC’s premises are located in Willcock Drive, Geraldton. The existing building was constructed in 1967741, and, as of 30 April 2005, the GSLSC’s premises were valued at $129 306.742

3.3 On 19 December 2003, the GSLSC provided information to the Mid West Gascoyne ACC (MWGACC) on a project to redevelop the club’s premises and upgrade the Mahomet’s Recreation Precinct. The project was to occur in two stages across 2004–05 and 2005–06, at a total cost of $1 450 000 comprising:


739 ibid.

740 Geraldton Surf Life Saving Club (Inc.), *Special Purpose Financial Statements for the Year Ended 30th April 2005*.

741 In addition to the GSLSC, the building is used by the Geraldton Board Riders Club, Geraldton Harriers Winter Running Club, Geraldton Fitness and Aerobics Club and the Orchid Society as well as by other groups for meetings, functions and storage.

742 Geraldton Surf Life Saving Club (Inc.), *Special Purpose Financial Statements for the Year Ended 30th April 2005*. 


• redevelopment of the existing building—$1 200 000;
• construction of a caravan lay-by (subject to approval by the City of Geraldton)—$150 000; and
• precinct upgrade and tourist amenities—$100 000.

3.4 The GSLSC proposed to seek $500 000 from the Regional Partnerships Programme towards the cost of the project.

3.5 An application for Regional Partnerships funding was received by DOTARS on 13 April 2004. The amount sought was $500 000 to assist with project costs, which were stated to be $1 250 000.

3.6 The images in Figure 3.1, provided to ANAO by the GSLSC, are architect impressions of the proposed finished full redevelopment.
Figure 3.1
Architect impressions of finished redevelopment

Southward view with Stage 1 on the right and Stage 2 on the left (architect impression)

Eastward view with Stage 1 in the centre and Stage 2 on the left (architect impression)


Project assessment and approval

3.7 DOTARS’ clarification and assessment of the application for funding was undertaken between 13 April 2004 (when the application was received) and 24 June 2004 (the date on which the department finalised its assessment
and recommended to the then Parliamentary Secretary that funding be approved).

**Outcomes**

3.8 In its application, the GSLSC stated that the expected outcomes of the redevelopment were:

- provision of additional opportunities for youth within the region to participate in physical activity and lead active healthy lifestyles;
- a multi-use facility providing additional opportunities for seven organisations to work together in the provision of facilities specifically for youth and in so doing reduce infrastructure and capital costs for community organisations and government; and
- through the caravan lay-by, encourage tourists and visitors to stay and/or return thereby increasing the economic benefits to local businesses.

3.9 Figure 3.2 sets out DOTARS’ assessment of this application against the Outcomes assessment criterion, as advised to the then Parliamentary Secretary on 24 June 2004.

**Figure 3.2**

**Assessment against the outcomes criterion**

```
- Outcomes

The project will strengthen growth and opportunities through improved social, training and other facilities for current and potential users of the building and provide a community focal point within the Mahomet's Beach sporting, tourism and recreational precinct. The project also has potential for increasing employment and growth to local businesses through the provision of the caravan lay-by which will encourage tourists to visit local attractions in Geraldton.

The locality is isolated from other sporting and recreation infrastructure so there are unlikely to be competition issues.
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**Partnerships and viability risks**

3.10 The feasibility study attached to the GSLSC’s Regional Partnerships application outlined the expected operating expenditure and income from the redeveloped premises in the first year of operation, with a breakeven result being forecast. For the second and third years, the feasibility study predicted
that increases in expenses would be met through increased use and a minor restructure of fees. Accordingly, the project involved commercial activities.

3.11 At the time the assessment of this application for funding was undertaken, a minimum required level of co-funding for projects involving commercial activities was 50 per cent. This test was satisfied in that the Regional Partnerships funding of $500 000 represented 41 per cent of the proposed cash contributions to the project and 41 per cent of expected total project costs (cash and in-kind).

3.12 The Regional Partnerships Programme was expected to be the single largest provider of cash funds to the project. As outlined below at paragraph 3.125 further funding has been obtained from the Regional Partnerships Programme in February 2007 to fund increases in project costs with the GSLSC advising DOTARS that it was totally reliant on the Programme for additional funding.

3.13 There were six other parties nominated to provide cash to the project. Table 3.1 identifies the other funding partners and their proposed contributions as advised by DOTARS to the then Parliamentary Secretary, however most of this funding had not been confirmed at the time DOTARS completed its project assessment.

Table 3.1
Partners and their proposed contributions: June 2004

<table>
<thead>
<tr>
<th>Partner</th>
<th>Cash contribution ($)</th>
<th>Status as per application</th>
</tr>
</thead>
<tbody>
<tr>
<td>GSLSC</td>
<td>60 000</td>
<td>In negotiation.</td>
</tr>
<tr>
<td>State Department of Sport and Recreation</td>
<td>390 000</td>
<td>$195 000 committed but yet to be received. Remainder not yet applied for.</td>
</tr>
<tr>
<td>Lotterywest/Surf Lifesaving WA</td>
<td>100 000</td>
<td>Committed but yet to be received.</td>
</tr>
<tr>
<td>City of Geraldton</td>
<td>100 000</td>
<td>In negotiation.</td>
</tr>
<tr>
<td>Shire of Greenough</td>
<td>50 000</td>
<td>Contribution requested.</td>
</tr>
<tr>
<td>Mid West Variety Club</td>
<td>25 000</td>
<td>In negotiation</td>
</tr>
<tr>
<td><strong>Total Proposed Partner Funding</strong></td>
<td><strong>725 000</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: Departmental project assessment dated 24 June 2004 and GSLSC Regional Partnerships application received by DOTARS on 13 April 2004.

3.14 Notwithstanding that the minimum expected collective partner co-funding had only been satisfied by a relatively small margin, Regional
Partnerships was the single largest provider of funding and most of the partner funding had yet to be confirmed, DOTARS assessed partnership commitment as ‘excellent’.

3.15 In terms of applicant viability, DOTARS advised the then Parliamentary Secretary that it had assessed the GSLSC as representing a low applicant risk. DOTARS also assessed that the project satisfied the project viability risk criterion, although the level of risk was assessed as being ‘medium’. Figure 3.3 outlines the stated rationale for theses assessments.

Figure 3.3

DOTARS’ assessment against the applicant and project viability criteria

- Applicant Viability
  The applicant is assessed as a low risk.
  While the applicant has no previous funding history, the club has been established for 74 years and has supported itself for this period. The Club's Board of Management includes a Managing Director, Director and Partner, Accountant and Bookkeeper, and a State Government Department Manager.
  The applicant proposes to establish a management committee which will be responsible for the project, including maintenance, repairs, and future alterations and additions following completion. This committee includes local builders, engineer, surveyor, architect, electrician, user group representatives and Mahomet’s Beach Improvement Group delegates. Given the size of Regional Partnerships contribution and the organisation’s lack of previous experience in managing government grants, it is considered that a member of the Mid West Gascoyne ACC would be a valuable addition to this committee.
  It is the Department’s process to conduct a financial risk assessment of any commercial entity seeking funds of this value. Any funding approval should be conditional on this assessment being satisfactory.
  The applicant satisfies this criterion.

- Project Viability
  The project is assessed as a medium risk.
  The club has a proven record of sustainability and has successfully managed their previous facility without needing government assistance. A feasibility study undertaken by the applicant suggests operating expenditure will be balanced by income and the new building has the potential of even greater levels of use which will further increase viability.
  The City of Geraldton provides an amount of $2,500 annually for maintenance costs.
  The application satisfies this criterion.

Funding approval and announcement

3.16 DOTARS’ assessment of this project was provided to the then Parliamentary Secretary on 24 June 2004. This was as part of an assessment package of 19 projects. Of these, 17 were recommended for approval with two assessed as not meeting the Regional Partnerships Programme Guidelines. The recommended projects included the application from GSLSC.743

3.17 DOTARS’ assessment advised the then Parliamentary Secretary that the project duration was 24 months with a recommended funding profile involving payment of $290 000 in 2004–05 and $210 000 in 2005–06.

3.18 DOTARS assessed the project for the redevelopment of the GSLSC as meeting the Regional Partnerships Programme Guidelines and satisfying all assessment criteria. DOTARS also advised the then Parliamentary Secretary that the MWGACC had recommended the project and rated it as a high priority for its region. DOTARS recommended that the then Parliamentary Secretary approve funding of $500 000 (plus GST) for the project, subject to three conditions.

3.19 The project was approved for funding on 28 June 2004. Consistent with DOTARS’ recommendation, the then Parliamentary Secretary approved funding subject to three conditions:

- a satisfactory independent financial risk assessment being undertaken;
- partnership funding being confirmed; and
- multi-year grant approval from the Minister for Finance and Administration.744

3.20 Advice of funding approval was provided to the local member (The Hon Wilson Tuckey MP) on 21 July 2004 and the local member issued a Media Release in relation to the funding approval, with coverage in the local press on 23 July 2004. Letters from the then Parliamentary Secretary to the applicant and the MWGACC advising of her funding approval were dated 27 July 2004.

743 In the 24 June 2004 covering Minute to this package of assessments, DOTARS advised the then Parliamentary Secretary: ‘At our meeting on Wednesday, 16 June 2004, you asked us to put forward 100 projects for your consideration by cob next Friday, 25 June 2004. This is the sixth package of the 100 projects that we are aiming to delivery [sic] to you by that time. This package contains 19 projects and brings the total number of projects delivered to you and Mr Anderson to 94.’ This issue is discussed further in Part 3 of the main audit report relating to Application Assessment and Approval Processes.

744 This relates to the Government’s policy requirement that the Finance Minister’s approval be obtained prior to awarding and announcing a multi-year grant, which originally applied to grants that involved commitments for more than twelve months. This requirement now applies to grants involving more than $2 million over a period longer than 36 months.
3.21 The Funding Agreement signed on 28 January 2005 provided for three Regional Partnerships instalments, as follows:

- $250,000 (plus GST), the stated purpose of which was for ‘Commencement of Project and Agreement signed and conditions met’;
- $125,000 (plus GST), the stated purpose of which was for ‘Commencement of second storey development’; and
- $125,000 (plus GST), the stated purpose of which was for ‘Construction of lay-by commenced and second storey completed’.

3.22 At the time of audit fieldwork, the first two payments had been made. Payment of the first instalment of $250,000 (plus GST) was processed by DOTARS on 13 May 2005. Payment of the second instalment of $125,000 (plus GST) was processed by DOTARS on 13 June 2006.

3.23 Under the terms of the Funding Agreement, the project was to be completed by 30 October 2006, with the Post Activity Report (including audited statement of receipts and expenditure) due by 31 December 2006. These milestones were not been achieved but, as of May 2007, the Funding Agreement had not been varied to reflect the delays.

**Project eligibility**

3.24 At the time GSLSC applied for funding, final architect’s drawings had yet to be completed and, as a result, approval from the City of Geraldton for the redevelopment had not yet been sought. In this respect, in terms of the Programme administrative arrangements approved by Ministers:

- as a community-based organisation, the GSLSC satisfied the ‘exception’ test for applications that would not be required to have approvals in place prior to funding being approved; and
- accordingly, the Funding Agreement should have included a provision to ensure that the first payment would not be made until all necessary approvals/licenses had been obtained.

3.25 Approval from the City of Geraldton had still not been obtained at the time the Funding Agreement was signed on 28 January 2005. However, the Funding Agreement did not include any provision requiring all necessary approvals and licenses to be obtained before the first instalment (or any later instalments) would be paid.
3.26 On 3 February 2005, the GSLSC advised DOTARS that:

Final sketch plans have been completed and will be presented to our members next week. From there we will be finalising full working drawings and going to the City of Geraldton for our building approval.

3.27 As noted, DOTARS processed payment of the first instalment of $250,000 (plus GST) on 13 May 2005. On 17 June 2005, the GSLSC advised DOTARS that planning approval from the City of Geraldton was expected following Council’s 29 June 2005 meeting and that the GSLSC would then apply for a building permit and advertise for tenders. In this respect, on 28 June 2005, Council delegated authority to its Chief Executive Officer to approve the redevelopment project, subject to advice from the Department of Planning and Infrastructure that coastal setback requirement objectives could be met. There is no evidence of DOTARS having obtained documentation confirming the provision of development approval for this project.

**ANAO conclusion**

3.28 The absence of development approval was not raised by DOTARS at any stage of its assessment of the project. It was also not drawn to the then Parliamentary Secretary’s attention when DOTARS sought approval of the spending proposal. Changes to the Programme Guidelines were made to enable community-based organisations, such as the GSLSC, to be approved for funding prior to obtaining development approval. However, increased risks to the Commonwealth arising from providing this additional flexibility to applicants were to be managed by ensuring that the payment of Regional Partnerships funds would not occur until necessary approvals and licenses had been obtained. DOTARS did not address this issue in the Funding Agreement for this project, such that $250,000 (plus GST) or 50 per cent of the grant funds were paid prior to development approval having been obtained.

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745 The delay between execution of the Funding Agreement and processing of the first payment related to the requirement under the Agreement that the first payment would not be made until the funding recipient had satisfied two pre-conditions—confirmation of all co-funding and entering into a contract that ensured that the total cost of the project did not exceed the budget as supplied in the application for funding. Neither of those conditions were satisfied prior to DOTARS making the first payment—see further at paragraphs 3.39 to 3.52 and 3.100 to 3.110.

746 The June 2005 Council meeting was actually held on 28 June 2005.
Findings and recommendations of the external viability assessment

3.29 DOTARS’ assessment of this project was finalised without the benefit of an external viability assessment. Instead, as noted, consistent with DOTARS’ recommendation, the then Parliamentary Secretary approved funding for the project on 28 June 2004 subject to a satisfactory independent financial risk assessment being undertaken.

3.30 A ‘satisfactory’ external viability assessment can be achieved in one of two ways:

• the assessment identifies no significant findings and makes no recommendations for action by DOTARS; or

• the findings of the assessment are adequately actioned through DOTARS explicitly considering each recommendation directed at addressing or mitigating identified project and applicant risks and:

  – where a decision is made not to take action, the reasons for this decision are documented together with any alternative risk management action that the department had decided to take in order to address the concerns raised by the external assessor; and

  – otherwise, implementing the recommendations of the assessment.

3.31 On 6 August 2004, DOTARS wrote to the GSLSC requesting that it authorise the department to undertake steps to assess the financial and project viability of both the GSLSC and the project. This authorisation was provided to DOTARS on 9 August 2004. A report was received by DOTARS during September 2004. Its conclusions were as follows:

GSLSC’s total assets at 30 April 2003 were $363,788 but projected expenditure for this project is $1.25 million. In our experience, small community based organisations often have weak procedures and controls. The establishment of adequate controls around the management and expenditures of funds should be required.

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For example, this could include resolving concerns raised with the applicant, such as by obtaining further information for analysis in order to address any scope limitations or adverse findings identified by the independent assessor.
Funding is to come from at least seven separate sources, over varying time frames. Some of this funding has been committed, yet to be received, some has only been applied for, and some is under negotiation.

Project funding exactly equals projected expenditure.

No material issues were identified in our financial analysis of GSLSC (financial statements for 1999, 2000, 2001, 2002 and 2003 as well as 2004 unaudited draft profit and loss statement).

Support for cost estimates have not yet been obtained by the department.

3.32 On 10 September 2004, DOTARS National Office advised the West Australian Regional Office that it had met with the external assessors and that:

some issues were raised but, in general, [the assessors] are comfortable that risks can be adequately managed through appropriate management of funding agreement milestones.

3.33 Notwithstanding DOTARS’ records of its discussions with the external assessors, the written report did not provide the necessary ‘satisfactory’ assessment. Of significance is that the report concluded that ‘the risk of cost overruns is high’. To address this and other concerns, the report made a number of recommendations. As outlined in the remainder of this case study, none of these recommendations were effectively implemented by DOTARS.

3.34 In this respect, in March 2007, DOTARS advised ANAO that, following discussions with the firm that conducted the external viability assessment, it chose to address the issue of possible cost overruns by imposing a Funding Agreement requirement that contracts entered into for the building limit the funding recipient to no more than the total cost of the project as per the budget in the application. However, as outlined further below, such clauses are of limited value in circumstances, such as this project, where the department does not take any steps to assure itself that the clause has been adhered to. It was not in this instance. This emphasises that effective management of Funding Agreements requires attention during implementation of the project, not just in the drafting of the Funding Agreement.

**ANAO conclusion**

3.35 Funding was approved by the then Parliamentary Secretary subject to a satisfactory external viability assessment being undertaken. The assessment report obtained by DOTARS identified a number of significant risks and made recommendations for DOTARS to consider in managing these risks. However, none of these recommendations were effectively implemented by DOTARS.
Partner funding

3.36 The GSLSC’s application proposed that project funding would be provided by seven parties, including the Commonwealth through the Regional Partnerships Programme. In terms of the Partnership and Support assessment criterion, DOTARS’ assessment provided to the then Parliamentary Secretary was that:

Partnership commitment for this project is excellent, although most of the funding has yet to be confirmed.

3.37 DOTARS did not address the uncommitted nature of most of the partnership contributions in its assessments of applicant and project viability risks. In comparison, the external viability assessment saw the partnership arrangements as presenting viability risks that required explicit management. Specifically, the external assessment report included the following finding:

Funding is to come from at least seven separate sources, over varying time frames. Some of this funding has been committed, yet to be received, some has only been applied for, and some is under negotiation.

3.38 To manage the risks associated with the number of proposed funding partners and the uncommitted nature of most of the contributions, the report recommended that DOTARS:

- before entering into a funding agreement, require commitments from all funding sources to be evidenced; and
- establish payment milestones under the funding agreement that aligned with, or were triggered by, receipt of co-funding.

Confirmation and evidencing of partner contributions

3.39 As noted, one of the conditions of the then Parliamentary Secretary’s funding approval was that partnership funding be confirmed. In her 27 July 2004 letter advising that she had approved Regional Partnerships funding, the then Parliamentary Secretary advised the GSLSC of this condition, as follows:

Funding for the project has been approved, subject to a satisfactory financial risk assessment being undertaken and partnership funding for the project being confirmed.

3.40 In March 2007, DOTARS advised ANAO that it received communication from the GSLSC on 29 June 2004 indicating that $430 000 of the $740 000 partnership funding had been confirmed. However, DOTARS’ records did not include any further communications with the GSLSC on the
confirmation of partner contributions until 31 January 2005. This was three
days after the Funding Agreement was signed on 28 January 2005. The
Funding Agreement identified partner funding as per the advice provided to
the then Parliamentary Secretary by DOTARS on 24 June 2004.

3.41 Instead of requiring partner contributions to be confirmed prior to
signing the Funding Agreement, DOTARS included the following pre-
condition on the first payment of Regional Partnerships funds:

All co-funding has been approved.

3.42 On 31 January 2005, following a telephone discussion the previous
week with DOTARS, the GSLSC provided written advice on the status of
partner contributions, advising that:

All funding is in place and apart from final approval on the excising of
additional land the project is still on schedule. The final approval on land is
expected on the resumption of Parliament, however this will not interfere with
the redevelopment, as it is our intention to proceed with the first stage on the
existing land.

3.43 The GSLSC further advised that partner contributions (including
Regional Partnerships) of $1 045 000 had been approved. A further $150 000
had not yet been confirmed, with the GSLSC advising that this amount would
become part of a GSLSC loan if the funding application was unsuccessful.

3.44 DOTARS correctly identified that, in total, the cash contributions now
advised by GSLSC were $45 000 less than the $1 240 000 required by the
Funding Agreement. In addition, DOTARS also raised concerns about the
unapproved contribution of $150 000. In response to questions about the
identity and quantum of partner contributions, GSLSC informed DOTARS
that:

- the State Department of Sport and Recreation would not be
  contributing the $390 000 identified in the Regional Partnerships
  application. Whilst the first application for $195 000 had been
  successful in the 2004–05 application round, GSLSC had been advised
  not to pursue a second grant for a further $195 000 in the 2005–06
  application round;

- Lotterywest had increased its contribution from $100 000 to $200 000; and

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an application for $150 000 in funding had been submitted to the State Department of Local Government and Regional Development’s Regional Investment Fund.

3.45 The GSLSC further advised that:

We are confident these funds will be forthcoming with the support and advice received. This will take us over the $1 240 000 and the extra funds will be utilised to provide additional shade areas, outdoor paving and better beach access through the dune areas.

The worst case scenario, as indicated, is we would increase the Back Beach Improvement Group and GSLSC loan.

3.46 On 4 February 2005, DOTARS advised the GSLSC that, due to the change in partner contributions, a contract variation would need to be processed. However, DOTARS did not prepare a variation to the Funding Agreement. As a result, the Agreement was not varied to reflect the changed partner contributions. This meant that it was not possible for the GSLSC to satisfy the payment pre-condition that the partner contributions specified in the Funding Agreement be confirmed prior to the first payment being made.

3.47 The next correspondence from the GSLSC on the issue of partner contributions was on 13 May 2005, which advised DOTARS that:

Further to our telephone discussion yesterday, I wish to confirm arrangements we have in place for the remaining $150 000 of our budget.

As indicated previously, we submitted an expression of interest through the WA Department of Local Government and Regional Development earlier this year. This received a favourable hearing and we have been invited to apply for funding through the next round of the Regional Infrastructure Funding Program due to be announced in August this year.

Details of the application are being finalised this weekend and will be submitted early next week.

We are confident these funds will be forthcoming; however in the event we are not successful the loan by the Back Beach Improvement Group and the GSLSC will be increased to cover the shortfall. With additional groups now wanting to utilise the facility, increased gym patronage and opportunities to lease the kiosk/coffee shop and function area, we do not see servicing a larger loan being too difficult. The gym alone will return over $20 000 annually.

3.48 As a result of this correspondence, DOTARS processed the first payment of Regional Partnerships funds, also on 13 May 2005 (as mentioned in paragraph 3.22). This involved payment of 50 per cent of the approved grant,
being $250 000 (plus GST). This payment was made notwithstanding that the pre-condition on the first payment stipulated in the funding approval and Funding Agreement had not been met as a result of:

- the Funding Agreement not being varied to reflect changes in the partner contributions advised to DOTARS by the GSLSC; and
- a shortfall in approved funding as follows:
  - funding of $150 000 from the State Department of Local Government and Regional Development’s Regional Investment Fund had not yet been approved; and
  - the GSLSC had advised DOTARS that, in the event this funding was not forthcoming, the GSLSC would increase its borrowings although no evidence was provided as to whether facilities for such a significant increase in borrowings by a non-profit organisation had been approved.

**ANAO conclusion**

3.49 The project was approved for funding by the then Parliamentary Secretary subject to partnership funding as advised by the department being confirmed. In this respect, rather than confirming partnership funding prior to signing the Funding Agreement, DOTARS drafted the Agreement to include a pre-condition that required all partnership contributions be confirmed prior to the first payment of Regional Partnerships funds being made.

3.50 In its administration of the Regional Partnerships grant for this project, DOTARS obtained advice from the applicant that most partner funding contributions had been confirmed. However, DOTARS did not:

- require the GSLSC to provide evidence\(^\text{748}\) of the commitments from funding sources, as had been recommended by the external viability assessment. Instead, DOTARS relied solely on unsubstantiated advice from the applicant that most funds had been approved; or
- obtain documentary evidence from GSLSC to support its advice that any shortfall was able to be made up through increased borrowings.

\(^\text{748}\) For example, in some other projects included in ANAO’s sample, this involved the applicant providing DOTARS with correspondence from the funding partner that confirmed its financial contribution to the project. In this respect, the then applicable Internal Procedures Manual stated that examples of evidence to confirm partner contributions include copies of local government meeting minutes, letters of funding commitments and copies of letters advising the outcome of funding applications.
3.51 In October 2006, when seeking additional funds from the Regional Partnerships Programme to assist it in meeting increased building costs, the GSLSC advised DOTARS that the partner funding of $25,000 from the Mid West Variety Club (see Table 3.1) did not eventuate because the contract offered by the Variety Club had required that the funding be for equipment to be used only by people with disabilities (a condition the GSLSC could not meet). DOTARS had not earlier been aware of this, notwithstanding that clauses 6.1 and 6.2 of the Funding Agreement stated that:

6.1 It is a condition precedent to the payment of Funds under this Agreement that You must get people (other than Us), as identified in Item 2 of the Schedule, to provide Us with satisfactory written evidence that they will provide the Other Contributions to You, including the amounts to be provided, their due dates and the terms and conditions of the provision of the Other Contributions. The terms and conditions on which these Other Contributions are to be provided must be satisfactory to Us.

6.2 The written confirmation referred to in subclause 6.1 must be provided to Us within 20 Business Days of the Date of this Agreement, failing which this Agreement will be treated as void and as never having been entered into.

3.52 Despite the terms of the Funding Agreement, DOTARS did not obtain from the GSLSC written evidence of the various partner contributions or their terms and conditions.

Aligning payments with receipt of partner contributions

3.53 The external viability assessment report recommended that DOTARS:

Establish milestone payments triggered by receipt of co-funding.

3.54 As mentioned, the first payment of Regional Partnerships funds was subject to a pre-condition that all co-funding be confirmed. However, none of the milestone payments were structured such that they were triggered by receipt of co-funding by the funding recipient. Having regard to the number and quantum of partner contributions to this project, this meant there was a significant risk that the GSLSC would be receiving funds from a number of partners at the same time, irrespective of the project’s cash flow needs. In addition to not developing payment arrangements that reduced the likelihood of this occurring, the Funding Agreement did not enable DOTARS to effectively monitor and manage the associated risks to the Commonwealth.
**Internal controls**

3.55 The external viability assessment commented that:

In our experience, small community based organisations often have weak procedures and controls. The establishment of adequate controls around the management and expenditure of funds should be required.

3.56 The external viability assessment recommended that DOTARS have auditors review the GSLSC’s procedures and controls, and make recommendations to ensure adequate procedures existed to manage the $1.25 million project. DOTARS did not implement this recommendation.

3.57 In this respect, the GSLSC’s Special Purpose Financial Statements for the year ended 30 April 2005 included the following qualification of the audit opinion:

The Geraldton Surf Lifesaving Club has a lack of internal controls which creates a high audit risk as per the following examples:

- No stock take conducted on a regular basis.
- Receipts were not issued for all the income received and not all the income was banked.
- Lack of supporting documentation for all the income received and expenses.
- The Treasurer’s Report provided at the committee meetings was inadequate.
- No regular payments of GST were made during the year.
- The Geraldton Surf Lifesaving Club’s constitution needs to be followed more strictly.

3.58 In relation to the 30 April 2005 financial statements, DOTARS commented to ANAO that:

This is a Financial Statement which was produced after the decision to fund the project. The Financial Viability Assessment undertaken on behalf of the department was based on GSLSC’s financial statements for the years ending 2001–02 through 2003–04—none of which included any such qualification.

3.59 This post-funding decision nature of the report is recognised. However, the audit qualification serves to underline the benefit that would have been obtained from DOTARS implementing the recommendation it had received from the external viability assessment to have auditors review the GSLSC’s procedures and internal controls, and make recommendations to ensure
adequate procedures existed to manage the $1.25 million project. As noted, this was not done.

**Separate bank accounts**

3.60 The Standardised Funding Agreement developed by the Australian Government Solicitor for use in Commonwealth grant programmes, on which the Funding Agreement used in the Regional Partnerships Programme is based, requires funding recipients to:

- ensure that the Funds are held in an account in Your name, and which You solely control, with an authorised deposit-taking institution authorised under the Banking Act 1959 (Cth) to carry on banking business in Australia.\(^{749}\)

3.61 The emphasis in the Standardised Funding Agreement is on identifying the receipt and expenditure of Commonwealth funds separately within the recipient’s accounting records so that, all times, the funds are identifiable and ascertainable.\(^{750}\) However, in developing the Standardised Funding Agreement, it was recognised that there would be circumstances in which risks would be best managed by including a requirement for Commonwealth funds to be placed in a separate bank account established solely for the purpose of the project being funded, and separate from other bank accounts held by the funding recipient.

3.62 Consistent with these principles, the Long Form Standardised Regional Partnerships Funding Agreement includes the following optional item:

- This must be an account that is:
  - (i) established solely for the purposes of accounting for, and administering, any Funding provided by Us to You under this Agreement; and
  - (ii) separate from Your other operational accounts.

3.63 In preparing the Funding Agreement for this project, DOTARS did not explicitly assess the merits of requiring the GSLSC to hold the Commonwealth’s funds in a separate bank account.

3.64 As at May 2007, two instalments of Regional Partnerships funds had been paid to the GSLSC, totalling $375 000 (plus GST) or 75 per cent of the approved grant. Each payment was made into the GSLSC’s operating account.

\(^{749}\) The Banking Act 1959 provides the legislative framework for the prudential supervision of authorised deposit-taking institutions. Authorised deposit-taking institutions are corporations granted a license under the Banking Act to carry on banking business in Australia. They comprise banks, building societies and credit unions.

However, these funds were later transferred by the GSLSC into a separate bank account it had established for the redevelopment project. The account was opened in June 2005, shortly after the first Regional Partnerships instalment was received. Following identification of this issue in the ANAO’s January 2007 case study of this project, in March 2007, DOTARS advised ANAO that it had requested that the GSLSC advise it of the building account in order that all future payments are made to this account.

3.65 Following ANAO’s 6 May 2006 site inspection of this project, the GSLSC provided ANAO with copies of the bank statements for the building account for the period up to the end of March 2006.

3.66 The first instalment of Regional Partnerships funds of $275 000 (GST inclusive) was deposited into the GSLSC’s operating account on 20 May 2005. On 3 August 2005, $281 000 (including the $275 000 in Regional Partnerships funds) was transferred into the building account. Between this date and 27 March 2006:

- there was a further $14 715 deposited into the building account; and
- debits amounting to $38 230 were made, leaving a balance of $257 485.

3.67 Accordingly, there was no evidence of substantial contributions from other project partners having been deposited into the building account up to March 2006. In addition, this data demonstrated that the first instalment of Regional Partnerships funds was in excess of, and in advance of, project requirements. In this respect, DOTARS has not ensured that the most efficient and effective use was made of the public money paid to the GSLSC, having regard to the interest foregone by the Commonwealth when payments are made earlier than necessary. In relation to these issues, DOTARS advised ANAO in March 2007 that:

The department has also requested that a copy of the GSLSC building account be included with each subsequent progress report and acquittal.

**Progress reporting and acquittals**

3.68 The Regional Partnerships Long Form Standardised Funding Agreement, including the standard progress reporting and acquittal arrangements, was used for this project. As mentioned, the first payment was processed by DOTARS on 13 May 2005, the same day that DOTARS received written advice that the GSLSC would increase its borrowings if its application for funding under the State’s Regional Investment Fund was unsuccessful.
First progress report

3.69 The first progress report was due on 31 March 2005. A report was received on 26 April 2005.

Second progress report

3.70 The second progress report was due on 30 June 2005, with the second payment of $137 500 (plus GST) also proposed to be made on 30 June 2005. A DOTARS record of 3 June 2005 states that, in a telephone discussion, the GSLSC had advised that:

Building permits have not yet been finalised and [we] are hoping to start the redevelopment in July 2005. The first payment has not been expended at all, but it should happen quickly once the builders have started.

[The GSLSC] requested that the second payment be delayed until the end of September.

3.71 A progress report was provided to DOTARS on 17 June 2005. Among other things, this report stated that planning approval from the City of Geraldton was expected following the next Council meeting on 29 June 2005 and that a building permit would then be submitted and tenders advertised immediately following receipt of planning approval. No information was required, or provided, in relation to the receipt of other partner contributions, or the expenditure of the first Regional Partnerships instalment.

Third progress report

3.72 The next progress report was due on 30 September 2005.

3.73 DOTARS’ records state that, in a telephone conversation on 7 September 2005, the GSLSC advised that it had paid the engineer and architects for drawings and designs and paid for planning and building licenses. Total expenditure to date was said to be approximately $50 000. This record further states that:

[The GSLSC] is meeting with builder tomorrow to negotiate his quote. [The GSLSC] will call to provide an update. If all goes well, expect building to begin in 3-4 weeks, and 1st payment will be quickly spent. Will wait for update estimated start time from [GSLSC] before shifting payment in SAP.

3.74 DOTARS’ record of a further telephone conversation with the GSLSC on 22 September 2005 state that the department was advised that the first Regional Partnerships instalment still had not been spent and that the GSLSC would:
send through reports of plan to stage project, current expenditure and expected time frame for expenditure.

3.75 A progress report for the period 18 June 2005 to 23 September 2005 provided to DOTARS on 23 September 2005 included copies of building plans indicating the staging of the redevelopment. The report focused on cost increases and steps being taken to manage those increases. In respect to expenditure, it stated that total expenditure to date was $26,995. No information was required, or provided, in relation to the receipt of other partner contributions. The action taken by DOTARS in relation to this report was to contact the GSLSC to clarify timelines. DOTARS’ record of the telephone conversation was as follows:

Stage 1 to finish June/July 2006 but Stage 2 will go beyond that. I informed [the GSLSC contact] that he will need to request a contract variation. With building commencing by December 2005, [the GSLSC] expects 1st payment to be spent by February 2006, when he will make a claim for the 2nd payment.

Fourth progress report

3.76 A progress report was due on 31 December 2005. It was not obtained by DOTARS. In this respect, in March 2007, DOTARS advised ANAO that an update of the project was provided via fax from the GSLSC to DOTARS on 19 January 2006. Specifically, following a telephone call from DOTARS, on 19 January 2006 the GSLSC wrote to the department advising as follows:

It was hoped our builder...would commence in December 2005. They did not commence as scheduled and with their normal close down period Dec-Jan have not been back on site, so progress has been slow.

They have however completed the demolition of part of the old structure and we anticipate work will begin again within the next month.

This may delay our next payment request to April, with the finishing date now being delayed to as late as August.

The building industry is extremely busy in this region but just as soon as the builder gives us an indication of his revised time limes I will advise you accordingly.

3.77 In response, on the same date, DOTARS requested that the GSLSC submit a progress report once the club had met with the builders and there was a better indication of timelines.
Fifth progress report

3.78 A progress report was due on 31 March 2006. On 20 April 2006, DOTARS emailed the GSLSC seeking the progress report. In March 2007, DOTARS advised ANAO that a report was received on 20 April 2006. This ‘report’ was a one page letter from GSLSC dated 19 April 2006 advising that:

After a number of major hold ups we have now moved to the construction stage of our redevelopment.

The first stage of demolition has been completed and after many months of negotiations to remove a secondary dune immediately West of the new facility we have final [sic] been granted permission to proceed with its removal.

This will be moved prior to the end of April and will provide 1 metre of fill across the site to raise the proposed building.

The builder…will commence laying the slab the first week in May and anticipates completion in early December 2006.

This is a wonderful outcome for the club and the community and we look forward to its completion.

We anticipate claims will be submitted as follows;

August 2006   Second claim of $125 000
October 2006  Final claim of $125 000

3.79 In this respect, Figure 3.4 shows the project site at the time of ANAO’s 6 May 2006 site inspection, almost one year after DOTARS paid 50 per cent of Regional Partnerships funds ($250 000 plus GST).
Sixth progress report

3.80 A progress report was due on 30 June 2006.

3.81 On 24, 25 and 26 May 2006, with the end of the financial year approaching, DOTARS attempted to contact the GSLSC regarding project progress. DOTARS’ records state that, on 26 May 2006, it was advised that:

The builders have commenced with the pad down, the building sides have been completed, albeit not in place and this may well construe the opportunity for payment 2 that requires the commencement of the second storey development.

[The GSLSC] is to discuss with the builder and if possible will progress payment 2 early. He is to advise me of the situation on Monday.

3.82 On 30 May 2006, DOTARS was advised by the GSLSC that an invoice from the builder for $412,000 had been received. The GSLSC further advised that it would acquit the first payment, complete a report and produce a tax invoice for $125,000 (plus GST) for the second Regional Partnerships instalment.

3.83 On 13 June 2006, the GSLSC provided DOTARS with:

- a progress report for the period 18 June 2005 to 13 June 2006;

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751 In March 2007, DOTARS advised ANAO that it is not unusual for the Department to contact funding recipients prior to the end of the financial year, if they have payments pending, to determine the status of the forthcoming payments.
• a copy of an invoice from its builder dated 29 May 2006 in the amount of $375 000 (plus GST);

• an acquittal of the first Regional Partnerships instalment. This acquittal showed the first Regional Partnerships instalment of $250 000 together with total expenditure relating to the Regional Partnerships grant of $375 000 resulting in a shortfall of $125 000 (all amounts GST exclusive). The acquittal included no amounts for any partner contributions that may have been received and no project expenditure other than that attributed to the Regional Partnerships grant; and

• a tax invoice for $125 000 (plus GST). The stated purpose of the invoice was ‘First grant instalment (Commencement of Project and Agreement signed and conditions met)’.

3.84 DOTARS processed the second instalment payment on 13 June 2006. This payment was made notwithstanding that insufficient evidence had been received by DOTARS that further funds were required from the Commonwealth at that time, including that:

• the 19 April 2006 advice from the GSLSC noted above had advised that the second instalment would not be required until August 2006; and

• the financial acquittal received did not address the extent to which other partner contributions had been received (it included no details of the receipt of funds from other partners or of any expenditure relating to partner contributions).

3.85 In March 2007, DOTARS advised ANAO that there was no evidence on file to suggest that the GSLSC only obtained an invoice from the builder and invoiced DOTARS for the second instalment at the department’s request. DOTARS further advised ANAO that:

Separate to this fact, the second payment was made on the basis of the Milestone being met as evidenced in the invoice, progress report and acquittal of the first payment in accordance with the Funding Agreement.

3.86 The stated purpose for the second payment was for commencement of the second storey development. In this respect, having regard to the substantial delays that had already occurred in progressing this project, the absence of any evidence of the receipt and expenditure of contributions from

\[752\] This amount was the same as the $375 000 invoiced by the builder and so did not include the $26 995 that the 23 September 2005 Progress Report had said had been spent on engineers, architects and fees and charges. DOTARS did not raise this anomaly with the GSLSC.
other funding partners and the 19 April 2006 advice from the GSLSC that the
second payment would not be required until August 2006, ANAO considers it
would have been prudent for DOTARS to conduct a site visit of this project
before further expenditure of public money was made. Conducting a site visit
would also have been consistent with DOTARS’ then applicable Internal
Procedures Manual which required that, in respect of projects involving more
than $250 000 in Regional Partnerships funding payable to non-profit
organisations, that:

Regional Offices to develop Monitoring plan to co-ordinate visit schedule with
milestone schedule. Random visits by Regional Office and National Office.

3.87 As of September 2006, DOTARS had not conducted a site inspection in
relation to this project.

Seventh progress report

3.88 A progress report was due on 30 September 2006.

3.89 Correspondence was received from the GSLSC dated 16 October 2006
advising of a 30 per cent increase in project costs since original quotations were
received. The GSLSC advised that additional costs outside the Stage 1 building
contract totalled $279 263 and that it was seeking additional funding from:

- the State Government Regional Headworks Program—$49 984;
- Lotterywest—$48 000;
- State Government—$50 000; and
- Mid West Development Commission—$30 000.

3.90 If all of those applications were successful, this would leave a shortfall
of $101 315 (36 per cent). The GSLSC further advised DOTARS that it had
unsuccessfully sought additional funding from the Western Australian
Department of Local Government and Regional Development under the
Regional Infrastructure Fund and increased funds from the Department of
Sport and Recreation. In respect of the Regional Partnerships Programme, the
GSLSC requested:

- early release of $75 000 of the final instalment of $125 000 to assist the
  GSLSC to meet payments to its builder; and
- Regional Partnerships funding be increased by $101 315 to assist it in
  meeting the cost increases.

3.91 This issue is discussed further below.
3.92 Project viability is defined in the Programme Guidelines as evidence that the project outcomes are sustainable beyond the funding period, that the project has been appropriately costed and that there is sufficient funding to achieve the outcomes.\(^{753}\) In this latter respect, the Regional Partnerships Funding Agreement for this project was not drafted, and has not been managed, by DOTARS so as to address risks associated with the project being primarily funded by contributions from a large number of parties external to the funding recipient, with the Regional Partnerships Programme being the single largest contributor of cash funding.

3.93 Of note is that the Funding Agreement did not link the payment of Regional Partnerships funds to the receipt of amounts from other project partners, and DOTARS has not otherwise monitored the receipt or expenditure of contributions by other partners. Such an approach would not involve the department imposing requirements on the timing of partnership funds, but would involve the department obtaining a sufficient understanding of the nature and timing of partnership contributions such that it would be able to structure Regional Partnerships payments in a way that made efficient use of the Commonwealth funds and ensured that the Commonwealth did not bear an undue share of project risks.

### Project cost increases

3.94 There has been a high level of construction activity in Western Australia for a number of years. The high demand has led to significant increases in the cost of construction projects. This has been the case in Geraldton since the commencement of the Regional Partnerships Programme on 1 July 2003. Figure 3.5 illustrates the increases in the Rawlinsons Building Price Indices for Perth over the past 10 years, highlighting the indices for the period since the commencement of the Regional Partnerships Programme. In 2006, Rawlinsons also noted that the construction prices in the Geraldton region were expected to be in the order of seven per cent higher than in Perth. Figure 3.5 shows that the cost of undertaking major construction projects in the region has risen by almost 40 per cent since June 2003. Accordingly, in a risk management context, it is important that DOTARS’ assessment and management of construction projects in States such as Western Australia addresses viability risks associated with cost increases.

Applicant’s cost estimates

3.95 In its April 2004 Regional Partnerships application, GSLSC estimated that the cost of the building redevelopment was $1,100,000 made up as follows:

- $40,000 for design and preliminary work comprising working drawings, permits, sewer connection, structural design, workshop drawings and surveyors design and setout. These costs were expected to be incurred in the first month of the project (programmed to be July 2004);

- $520,000 for demolition of the existing building commencing in the fourth month (programmed to be October 2004). This would involve earthworks, demolition of sections of the existing building and new additions to the ground floor; and

- $540,000 for alterations and refurbishment to the ground floor and construction of a second floor extension. This was programmed to commence in the ninth month (March 2005), with the project being
completed over a period of two years (completion programmed for June 2006).

3.96 In addition, the application included an estimated cost of $150 000 for the proposed caravan lay-by. This brought the total project estimated cost to $1 250 000.

3.97 During the assessment process, the project start and completion dates were revised (on 4 May 2004) to January 2005 and December 2006 respectively.

3.98 In terms of the cost of the project, on 17 May 2004, DOTARS requested that GSLSC provide a ‘fully detailed budget including breakdown of costs and supporting documentation (e.g. quotes) if available’. In response, on 26 May 2004, GSLSC advised DOTARS that:

Draft sketch plans have been completed (copy on your file). Final architect drawings have not been finalised at present. However, two local building companies have provided quotations and on advice from Crothers Constructions we advise you of estimated costs as follows:

- Design and documentation: $40 000
- Demolition, refurbish existing building and construction of new additions to ground floor: $650 000
- Construction of first floor area and development of caravan lay by: $550 000
- Landscaping and minor parking and access construction/repairs: $10 000

3.99 No documentation of the quotes from the two local builders was provided. DOTARS did not pursue this documentation before finalising its project assessment and advice to the then Parliamentary Secretary. DOTARS also did not address as part of its assessment whether the risk of cost escalations had been adequately addressed by the applicant. This was important, given that the cost estimate of $1 250 000 was included in the April 2004 Regional Partnerships funding application but the project was expected to be undertaken over two years between January 2005 and December 2006.

**Findings and recommendations of the external viability assessment**

3.100 The external viability assessment conducted after Regional Partnerships funding was approved raised concerns about the cost of the project. This included the fact that projected income for the project of $1 250 000 was exactly equal to projected expenditure of $1 250 000, leaving no
funds in the event of cost overruns. In respect to the risk of cost overruns and the management of this risk, the report stated that:

The projected cost of the project is $1 250 000. This comprises: design and documentation of $40 000; demolition, refurbishment and ground floor construction of $650 000; caravan layby development and first floor construction of $550 000; and landscaping, parking and access of $10 000.

This is based on builder’s quotes, however, final architects drawings have not been completed. Thus, the risk of cost overruns is high. Furthermore, it is unclear from our review whether these builders’ quotes have been sighted by the department. The department should manage this risk by requiring:

- GSLSC to provide copies of all builders’ quotes obtained;
- GSLSC to obtain cost quotes with guaranteed maximum expenditure from builders, and then demonstrate funding is adequate to meet maximum expenditure; and/or
- GSLSC to obtain funding for working capital, beyond projected funding. This should be at least $125 000, representing 10% of total projected costs. We note that there is no reason to assume cost overruns would be limited to only 10%.

3.101 DOTARS did not implement any of these recommendations. The only step taken by DOTARS in developing the Funding Agreement to manage the risk of cost overruns was to include the following pre-condition on the first instalment payment:

You will enter into contracts to ensure that the total cost of the project does not exceed the budget as supplied in your application for Regional Partnerships funding.

3.102 As noted above, the first instalment payment was processed by DOTARS on 13 May 2005. That payment was made without the department seeking to establish whether the payment pre-condition had been satisfied. In this respect, the only assurance obtained by the department was 31 January 2005 correspondence wherein the GSLSC stated that:

We fully understand the reporting and payment methods and milestones agreed and guarantee budgets will not exceed the contract and budget details provided.
Results of the tender process

3.103 The initial tender from the ultimately successful construction company was dated 8 September 2005. It included a tender price of $2 033 760 (plus GST) for the full redevelopment. This comprised:

- $1 439 860 (plus GST) for the first building which was to be a two storey building. The plans for the first floor comprised a gymnasium, ablutions, training room, kitchen, office, store room and entry area. The plans for the second floor comprised two balconies, a function area, kitchen, bar, store room and ablutions; and

- a further $593 900 (plus GST) for the second building. This was to be a single storey construction comprising an equipment store area, rooms for the Geraldton Board Riders, a youth room, caretaker’s accommodation, first aid room, kiosk and courtyard.

3.104 The image on Figure 3.6 is a further architect impression of the redevelopment, this time of Stage 1 only.

Figure 3.6
Architect impression of Stage 1 (westward view)


3.105 The progress report submitted by the GSLSC to DOTARS on 23 September 2005 advised the department that:
We have experienced delays with the commencement of the project due to the extremely high increase in building costs in the area.

Original costs of some 18 months ago have seen in excess of a 30% increase in some trades. This has necessitated going back to the builder and all the trades to investigate cost cutting opportunities.

Following various meetings with the Builder, Trades, Architect and Engineer, we have resolved to construct the building in two stages. This will avoid cutting back floor space and some of the important areas such as youth space, equipment, storage and training areas and will allow us to proceed with no changes to our original outcomes.

The only area that does have a question mark is the proposed lay-by facility as we are still waiting for council to make a decision on location.

There will only be minor changes to the plans and these are currently being updated.

To reduce costs members with assistance from local businesses completed the demolition of the first section of the existing building to allow the first stage to [be] commenced. This was a saving of $10,000 on budget.

Expenditure to date is as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engineers</td>
<td>$7,559</td>
</tr>
<tr>
<td>Architect</td>
<td>$18,000</td>
</tr>
<tr>
<td>Fees and Charges</td>
<td>$1,436</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$26,995</strong></td>
</tr>
</tbody>
</table>

The builder has advised once a final price is agreed on he will require 6 weeks lead time with the construction expected to take 30 weeks.

This would see the following revised time lines:

- Commencement of stage 1 building construction: December 2005
- Completion of first stage: June/July 2006

**3.106** A revised price for the first stage was submitted by the builder to the GSLSC on 17 October 2005. This involved a price of $1,290,830 (plus GST).

**3.107** A further revised price was submitted on 31 March 2006. This involved a price of $1,337,620 (plus GST). On 7 April 2006, the GSLSC advised the successful tenderer that, at a meeting of its Board of Management on 4 April 2006, it had resolved to accept the revised tender of 31 March 2006 for the construction of the first stage of the redevelopment.
Breach of payment pre-condition

3.108 The budget for the full redevelopment project included in the GSLSC’s Regional Partnerships application was $1 250 000.

3.109 The contract with the successful tenderer involved a contract sum of $1 337 620. Accordingly, leaving aside other costs of the project (such as design and documentation), and the cost of Stage 2, the GSLSC entered into contracts for building works that exceeded by $87 620 the budget in the Regional Partnerships application. This breached the pre-condition on the first Regional Partnerships instalment payment which required that:

You will enter into contracts to ensure that the total cost of the project does not exceed the budget as supplied in your application for Regional Partnerships funding.

3.110 DOTARS was unaware of this prior to the January 2007 ANAO case study and so did not address this issue in its administration of the Regional Partnerships funding.

Effect of cost increases on financial viability

3.111 Based on the available information, ANAO estimated in January 2007 that the total cost of the redevelopment was likely to have exceeded $2.2 million. Table 3.2 provides details of this estimate.

Table 3.2
Updated estimated cost of the project

<table>
<thead>
<tr>
<th>Cost element</th>
<th>$</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Engineers, architects etc</td>
<td>26 995</td>
<td>GSLSC advice to DOTARS of 23 September 2005</td>
</tr>
<tr>
<td>Stage 1</td>
<td>1 337 620</td>
<td>Construction contract price</td>
</tr>
<tr>
<td>Stage 2</td>
<td>685 198</td>
<td>Tender price of 8 September 2005 updated using Rawlinsons Construction Cost Guide</td>
</tr>
<tr>
<td>Caravan lay-by</td>
<td>203 204</td>
<td>GSLSC estimate from December 2003 updated using Rawlinsons Construction Cost Guide</td>
</tr>
<tr>
<td>Landscaping and minor parking and access construction/repairs</td>
<td>13 347</td>
<td>GSLSC estimate from April 2004 updated using Rawlinsons Construction Cost Guide</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>2 266 364</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: ANAO analysis of available information from DOTARS, GSLSC and publicly available information.
Applicant borrowings

3.112 The only liabilities included in the GSLSC financial statements attached to its April 2004 Regional Partnerships funding application were trade creditors. Accordingly, at the time the application was submitted, the GSLSC did not have a recent history of servicing borrowings.

3.113 In its funding application, the GSLSC proposed to contribute $100 000 to the cost of the project. This was to include a $60 000 loan. In respect to servicing this loan, the GSLSC advised DOTARS on 26 May 2004 that:

The club has now been operating for 75 years and has never received Federal, State or Local government grants. GSLSC has been entirely self-sufficient. All building development, renovations, additions and maintenance have been carried out through club fundraisings and servicing of loans. The club has a sound track record of meeting these obligations.

Loan repayments will be met through the hiring of the function area, education and training opportunities and through fees from members and user groups.

3.114 In terms of borrowings, the external viability assessment noted that gearing had grown from nil in 2000 to 1.2 per cent in 2001 and 2002, and to 6.9 per cent in 2003. The report concluded that a gearing ratio of 6.9 per cent represented a very low level of debt, but it did raise a concern that:

In our experience, small not-for-profit organisations can experience significant financial distress in delivering large capital expenditure projects.

3.115 During the process of clarifying partner contributions, the GSLSC advised DOTARS on 3 February 2005 that, in the event its application for $150 000 in funding from the State Regional Investment Fund was unsuccessful, its loan would be increased. In terms of servicing a large loan, DOTARS was advised that:

With additional groups now wanting to come on board i.e. Bridge Club, $500 per month, interest in leasing of kiosk/coffee shop, registration of interest in Gym membership from 35 to 70 members (over $12 000 additional funds annually) and the training facilities income, we do not see servicing a larger loan being too difficult. Naturally we would prefer not to have this commitment and will be working closely with our local Members of Parliament from both political parties to guarantee the funding is made available.
With the function area and our successful bingo income we will still be in a position to manage ongoing maintenance costs and set aside funds to cover any recurrent costs.

3.116 In December 2006, the State Government announced\textsuperscript{754} that $50 000 in funding was to be contributed to the cost of fixtures and fittings for the new GSLSC rooms. Combined with the grant from the Community Sporting and Recreation Facilities Fund of $195 000, and the $200 000 from Lotterywest, this brought the total State Government contribution to the project to $445 000.\textsuperscript{755} However, the amount announced was $100 000 less than the $150 000 the GSLSC had told DOTARS it had applied for.

3.117 As noted above, in May 2005, the GSLSC advised DOTARS that any shortfall in grant funding from the State Government would be addressed by increased borrowings.

3.118 The 2006–07 Budget adopted by the City of Geraldton included provision for a self supporting loan or loans to the GSLSC in relation to the redevelopment project.\textsuperscript{756} At its 22 August 2006 meeting, the City resolved to enter into a loan of up to $250 000 over 10 years for the GSLSC to assist with the redevelopment project.\textsuperscript{757}

3.119 However, clause 6.5 of the Regional Partnerships Funding Agreement requires that the GSLSC must:

\begin{quote}
inform Us in writing within 10 Business Days of entering into any arrangement (whether contractual or statutory) under which You are entitled to receive any Other Contributions not identified in the Schedule.
\end{quote}

3.120 As at September 2006, DOTARS’ records did not include any advice from the GSLSC of the borrowing arrangement that had been agreed to with the City of Geraldton.

3.121 Council Minutes state that Council staff had met with representatives of the GSLSC and were provided with income and expenditure estimates for 2006–07 and 2007–08, which included provision of $41 250 per annum to service the loan.\textsuperscript{758} Council Minutes also state that there was a risk of the

\textsuperscript{754} Mid West Development Commission, \textit{Mid West Developer}, December 2006, pp. 1 and 4.

\textsuperscript{755} ibid., p. 1.

\textsuperscript{756} City of Geraldton, \textit{Council Minutes}, 22 August 2006, p. 199.

\textsuperscript{757} ibid., p. 200.

\textsuperscript{758} ibid., p. 199.
GSLSC not being able to meet its repayments. Councillors were advised that, to manage this risk:

In line with Council’s procedures in respect to self supporting loans the City will obtain a legal agreement over the organisation’s assets that ensures that in default the building becomes City property.

3.122 However, clause 7.5(a) of the Regional Partnerships Funding Agreement requires that the GSLSC must:

not encumber or dispose of any Asset ... without our prior written approval.

3.123 As at September 2006, DOTARS’ records did not include any advice from the GSLSC in relation to the proposed encumbering of the assets being constructed in whole or part with Regional Partnerships funds. In its April 2007 comments on ANAO’s case study of this project, which had identified this issue, DOTARS advised ANAO that:

DOTARS had not been advised by GSLSC that their borrowings involve an encumbrance on the property. DOTARS has now confirmed this and is pursuing the matter with the funding recipient in association with the request for a contract variation.

3.124 However, legal advice obtained by DOTARS on this issue was that, due to the concept of an asset under the Standardised Funding Agreement not being tailored to deal with property that constitutes the project or activity under the Agreement, there was not a strong argument that the proponent was required by the Funding Agreement to not encumber the asset without the department’s written approval. In light of this legal advice, in April 2007, DOTARS advised the Ministerial Committee that it did not intend to pursue the perceived breach of the Funding Agreement.

Consideration of request for additional Regional Partnerships funding

3.125 As noted at paragraph 3.90, on 16 October 2006, the GSLSC wrote to DOTARS requesting:

- early release of $75,000 of the final instalment of $125,000 to assist the GSLSC to meet payments to its builder; and

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759 ibid.
760 ibid.
761 The Regional Partnerships Funding Agreement defined ‘asset’ as any item of tangible property, purchased, leased, created or otherwise brought into existence either wholly or in part with use of Regional Partnerships funds which has a value over $5,000 inclusive of GST.
Regional Partnerships funding be increased by $101,315 to assist it in meeting the cost increases.

3.126 The GSLSC advised that the builder was on track to finish Stage 1 by December 2006 and, accordingly, sought a response from DOTARS by December 2006.

3.127 The GSLSC wrote to DOTARS a second time on 1 February 2007 concerning its request for additional funding. The GSLSC advised of completion of Stage 1 of the redevelopment, increased building costs, the loan funding from the City of Geraldton and again requested additional Regional Partnerships funding. The GSLSC correspondence stated that:

Handover
The builder will effect handover of the project to GSLSC upon the final progress payment of $50,000 (+GST) being made.
GSLSC will be able to make the final payment upon receipt of $50,000 (+GST) grant funds already approved by DOTARS.

Loan Funding
In order to avoid short term penalty interest being charged by the builder, GSLSC has secured a loan of $250,000 from the City of Geraldton.

The loan is comprised of a bridging component of $100,000 (interest free) to be repaid in full by 31st April 2007, and $150,000 to be repaid in full by principal and interest (at 6.32%) payments over the next ten years.

GSLSC is totally reliant on the application to DOTARS to assist with higher construction costs of $101,315 (+GST). Receipt of such funds will allow GSLSC to meet the repayment schedule for the bridging loan. Default on either loan will cause ownership of the building to pass to the City of Geraldton.

3.128 In April 2007, DOTARS advised ANAO that the cost overrun issues were being dealt with through a formal request for a Variation to the Funding Agreement. Specifically, on 13 April 2007, nearly six months after GSLSC first sought additional funding, a brief was given to the Ministerial Committee recommending that the Committee:

- give in principle approval for arrangements to be negotiated for the provision of funding of up to $101,315 (plus GST) for the project, which had been assessed by DOTARS as meeting all of the Programme’s assessment criteria;
• give in principle approval for arrangements to be negotiated for variation of the scope of the project to remove the caravan lay-by and reallocate the remaining instalment of $50,000 (plus GST) to other budget items in the project;762 and
• agree that DOTARS would contact the applicant and ACC Chair and advise them of the Committee’s decision.

3.129 The members of the Ministerial Committee agreed to these recommendations between 19 April and 11 May 2007.

ANAO conclusion

3.130 The external viability assessment assessed the risk of cost overruns on this project as being high and raised concerns about how any such increases would be funded. However, in its development and administration of the Regional Partnerships Funding Agreement for the project, DOTARS did not effectively address this risk from the Commonwealth’s perspective.

3.131 The cost of this project has risen substantially from that considered in the department’s assessment of the application. This raises significant risks to the project’s viability given the funding recipient’s limited financial assets and heavy reliance on partner funding, particularly through government grants, the largest of which is being provided by the Regional Partnerships Programme. In this context, the funding recipient sought a 20 per cent increase in the amount of Regional Partnerships funding, advising DOTARS that it was totally reliant on increased Regional Partnerships Programme funding to assist meet increased construction costs. The extra funding was approved in May 2007.

762 This advice indicated that DOTARS had agreed to, and processed payment for, the GSLSC’s request that some of the final Regional Partnerships instalment of $125,000 (plus GST) be advanced (see paragraph 3.90). However, the DOTARS records of this project made available to the ANAO did not include any evidence of this payment being made.
4. Lakes Creek Upgrade

This case study examines the assessment, approval and contract management processes undertaken in respect to RP00908 Lakes Creek Upgrade project. It highlights shortcomings in the departmental assessment of the application together with the flexibilities in the Programme that enable funding to be approved in circumstances where assessment criteria have not been demonstrably satisfied, with attendant risks requiring management. In this latter respect, the then Parliamentary Secretary’s approval of Regional Partnerships funding was subject to an important condition, which was not adhered to by DOTARS in its administration of the grant.

Background

4.1 Established in 1946, the Teys group of companies (commonly known as Teys Bros) is the largest Australian-owned beef processor and exporter in the country. The Teys group has an annual turnover in excess of $1 billion, of which $850 million is export dollars and $150 million domestic sales. Beef is distributed to wholesalers, importers and supermarkets in Australia and exported to some 40 countries around the world, with major international markets in Japan, Korea, the UK and the USA.

4.2 The Teys group of companies owns six plants across Australia, producing some 270 000 tonnes of beef per annum. As illustrated by Figure 4.1, four of the plants are located in Queensland (at Beenleigh, Biloela, Innisfail and Rockhampton), with the remaining two plants being in Naracoorte (South Australia) and Katherine (Northern Territory). The Teys group also owns a feedlot in Condamine, Queensland, with a capacity in excess of 28 000 cattle.

764 ibid.
765 ibid.
766 ibid.
Figure 4.1
Teys Group location map


4.3 The abattoir at Rockhampton was previously operated by the Consolidated Meat Group. Although at one time the second largest abattoir in Australia, the Lakes Creek plant closed in July 2002, following a long-running industrial dispute and a history of unprofitable operations.

4.4 At around the same time as the announcement of the imminent closure, a proposed joint venture between the Consolidated Meat Group and the Teys group of companies was also announced. On 20 August 2002, the then Executive Chairman and Joint Chief Executive of Consolidated Meat Group advised the Senate Rural and Regional Affairs and Transport Legislation Committee that:

...We, with Teys, recognise the importance of the Lakes Creek abattoir in the processing industry, it being the second largest abattoir in Australia, and recognise the impact that this has had on the Rockhampton community and the Central Queensland grazing area in general.

While we are concentrating efforts currently on the due diligence process of trying to get an amalgamation between two organisations, we are committed to reviewing all options to re-open that abattoir. It needs to be said that you could only contemplate re-opening that abattoir if an appropriate allocation of US quota was forthcoming...
Through a variety of owners, the Lakes Creek plant has generally been unprofitable over the last decade. We are looking at forming a joint venture to change the cost structure of the business in total, so that would give us a fighting chance in its own right. At a business level, appropriate macro-action is being contemplated and, at a micro-level, we need quota to facilitate a flow of cash to the business.\textsuperscript{767}

4.5 Shortly after the plant closed, the Consolidated Meat Group and the Teys group of companies reportedly entered into a joint venture arrangement to which each was to contribute their abattoirs and related meat processing assets.\textsuperscript{768} Media reports of 2 December 2002 reported the Chairman of the Teys Group as having announced that the plant would re-open, the timing of which was largely dependent on the drought, with the Chairman quoted as saying:

We always said, when we were negotiating the joint venture with [Consolidated Meat Group], that we would look at the plant and see whether we felt it was a viable proposition, and we said if it was a viable proposition, the plant will open.

At this point in time we believe the plant is a viable proposition for us. If we opened it and found it wasn’t well, then, obviously we’d have to make another decision.\textsuperscript{769}

**Application for Regional Partnerships funding**

4.6 According to the records of DOTARS’ North Queensland Regional Office, the Regional Manager met with the Chair of the Central Queensland ACC (CQACC) and the General Manager of the Teys Bros Rockhampton Plant on 10 February 2004. At that meeting, Teys Bros outlined a plan to modernise/upgrade water usage, upgrade the kill floor and hopefully re-open the plant and were seeking Regional Partnerships assistance to upgrade the computer systems, water control and restructure the kill floor to allow smaller ‘runs’ of cattle to be slaughtered. Teys Bros were going to work closely with the CQACC to develop a Regional Partnerships application which, subject to review of some costings/plans, was likely to be submitted at the end of February or early March 2004.

\textsuperscript{767} Senate Rural and Regional Affairs and Transport Legislation Committee, Reference: Australian meat industry consultative structure and quota allocation, Official Committee Hansard, 20 August 2002, RRA&T84-93.

\textsuperscript{768} Australian Competition and Consumer Commission, Informal merger clearances register at <www.accc.gov.au> [accessed 5 November 2007].

\textsuperscript{769} ABC Rural Homepage, Rural News, Lakes Creek meatworks to re-open, 2 December 2002 at <www.abc.net.au/rural/news/stories/s738912.htm> [accessed 5 November 2007].
4.7 The records of the CQACC include an Expression of Interest dated March 2004 for a project titled ‘Teys Bros—Lakes Creek Meat Processing Plant—Upgrade’. The project had a proposed start date of 1 May 2004 and proposed finish date of 31 August 2004. The proposed works were to involve upgrading the two boilers, upgrading the rendering department of the plant, introduction of a system to regulate the amount of water that the plant used and upgrading the computer system.

4.8 The Expression of Interest sought Regional Partnerships funding of $600 000 as part of a total project cost of $1 320 221 for the last stage of works for the re-opening of the Lakes Creek complex. The only other party nominated as contributing any funds to the project was the applicant, with a proposed cash contribution of $720 221. According to the Expression of Interest, an internal cost analysis had been completed by the applicant for the upgrade and re-opening of the plant as part of the company’s business planning strategies.

4.9 As part of this performance audit, ANAO sought from the CQACC all records relating to this and all other Regional Partnerships projects considered by the ACC to the time of ANAO’s fieldwork in June 2006. The records provided to ANAO did not include any documentation concerning the CQACC’s assessment and/or consideration of the Expression of Interest.

4.10 On 17 March 2004, a copy of the Expression of Interest was provided to the Regional Office by an affiliate member of the Callide-Dawson sub-committee of the CQACC. The Regional Office was advised that the Chair of the CQACC was seeking in-principle approval of the application by the then Parliamentary Secretary. The seeking and/or provision of ‘in-principle’ approval of Regional Partnerships funding is not contemplated in the documented assessment and approval procedures for the Programme. Also on 17 March 2004, this email was forwarded to DOTARS’ National Office and the Departmental Liaison Officer to the Office of the then Parliamentary Secretary. The Regional Manager expressed concerns that:

- all Regional Partnerships applications needed to be rigorously assessed;
- Teys Bros would need to provide further justification before the department could consider seeking in-principle approval or fast-tracking of the assessment; and
- the plant was likely to re-open irrespective of whether any funding was provided through the Regional Partnerships Programme.
4.11 An application for $600,000 (plus GST) in Regional Partnerships funding for the Lakes Creek Upgrade project was received by the North Queensland Regional Office on 25 March 2004. The following day, a brief was sent to the then Parliamentary Secretary so as to inform her of a number of issues relating to the application. Specifically, the then Parliamentary Secretary was advised that a preliminary assessment had identified significant issues to be resolved, including:

- insufficient budget details;
- no business plan had yet been provided;
- insufficient evidence that the plant would be primarily aimed for the export market and not impact adversely on the Australian Meat Holdings plant located within 20 kilometres of the Lakes Creek plant; and
- evidence that insufficient cattle would be available following drought conditions.

4.12 DOTARS further advised the then Parliamentary Secretary that, notwithstanding these issues, the project was likely to provide excellent outcomes based on 360 jobs being created and broader community benefits of the plant reopening. The department’s proposed strategy was that:

- it continue to work with the applicant and the CQACC to ‘fast track’ assessment of the project; and
- the applicant and the CQACC be advised that it was unnecessary to seek the then Parliamentary Secretary’s in-principle approval.

4.13 Neither National Office nor Regional Office records of this project included a signed copy of this briefing, or a record of any response from the then Parliamentary Secretary.

4.14 At DOTARS’ request, the applicant provided further information in respect to the application on 15 April 2004. On 4 May 2004, the Regional Office provided National Office with the application for entry into TRAX. On 7 May 2004, National Office advised the applicant that this process had been completed, and a copy of the electronic record was emailed to the applicant.
Identifying and appropriately scrutinising the actual applicant and its corporate group

4.15 The Regional Partnerships application form advised that certain additional information would be required from a private sector entity seeking more than $250,000 from Regional Partnerships funding. This additional information was requested by DOTARS on 1 April 2004 as part of its assessment of the Lakes Creek Upgrade project application, including:

An outline of the organisation’s/sponsor’s ownership and management structure, including details of partners and/or directors. Include their full name, date of birth, current residential address and where possible, driver’s licence number.

4.16 An organisation and ownership chart was provided to DOTARS on 15 April 2004. This chart is shown at Figure 4.2.

Figure 4.2
Organisation and ownership chart provided to DOTARS by the applicant

Source: DOTARS’ records.

Consolidated Meat Group Pty Ltd

4.17 The Regional Partnerships application form requires the provision of the applicant entity’s legal name, trading name, Australian Business Number
(ABN) and, for companies, Australian Company Number (ACN).\textsuperscript{770} The entity identified as the legal applicant in the application received by DOTARS on 25 March 2004 was ‘Teys Bros (Lakes Creek)’, with a trading name ‘Teys Bros (Lakes Creek)’ and ACN 065 093 709.

4.18 However, that ACN relates to the Australian proprietary company, Consolidated Meat Group Pty Limited. This was identified by DOTARS on 6 April 2004, with the legal name of the applicant on the application form being annotated accordingly. There is no record of any clarification being sought from the applicant.

4.19 As of 11 April 2007, the last financial report lodged with ASIC by Consolidated Meat Group Pty Limited was that relating to the 2001–02 financial year. This report was lodged with ASIC on 28 October 2002, and so was available to be accessed by DOTARS at the time it was assessing the Regional Partnerships application for funding. The Directors’ Report included within the financial report stated that:

The principal activities of the economic entity during the course of the financial year were as a trustee company.

…The company during the year continued its trusteeship of the Consolidated Meat Processors Unit Trust operations.

4.20 The financial report also indicated that the Lakes Creek operations were being undertaken by Consolidated Meat Group Pty Limited. Specifically, the Directors’ Report stated that:

The operations at Lakes Creek, Rockhampton and Innisfail are required to comply with the Queensland Environmental Act and are covered by Environmental Authority No. CR0041 and 5010000046 respectively. Rockhampton did not consistently comply with the licence conditions. During the year there were a number of breaches of the licence. Some of these occurred as a result of the plant being shutdown for five months.

4.21 The financial report further stated that the ultimate controlling entity of Consolidated Meat Group Pty Limited was:

Consolidated Press International Holdings Limited, a company controlled by Mr K F B Packer.

\textsuperscript{770} Under the Corporations Act 2001, every company in Australia has been issued with a unique, nine-digit number, an Australian Company Number (ACN), which must be shown on a range of documents. The purpose of the ACN is to ensure adequate identification of companies when transacting business. New companies are issued with numbers by the Australian Securities & Investments Commission (ASIC) upon registration.
4.22 Further, in terms of events subsequent to balance date, the Directors’ Report reported on:

a proposed merger between the Consolidated Meat Group Pty Ltd group of companies and the Teys Bros (Holdings) Pty Ltd group of companies. The CMG Group will hold 51% of the newly merged group.

**Teys Bros (Rockhampton) Pty Ltd**

4.23 As noted above, the entity identified as the legal applicant in the application received by DOTARS on 25 March 2004 was ‘Teys Bros (Lakes Creek)’, with a trading name ‘Teys Bros (Lakes Creek)’ and ACN 065 093 709.

4.24 In addition, on 15 April 2004, DOTARS received financial information in support of the application that related to ‘Consolidated Meat Group Pty Ltd Trading As Teys Bros (Lakes Creek)’. This data comprised a statement of financial performance, statement of financial position and statement of cash flows for 2002–03 (actual data, excluding cash flows) and forecasts for 2003–04, 2004–05 and 2005–06. It was not identified whether the 2002–03 actual statements had been audited.

4.25 There was no documented analysis of this financial data by DOTARS. Nor was there documented evidence of any questions being raised with the applicant by DOTARS regarding the financial information that was provided. In this respect, ANAO notes that:

- the financial data included internal transactions with a parent entity. However, DOTARS did not analyse that data or seek any further information from the applicant in order to identify which entity or entities within the overall corporate structure those transactions related to or to assess the effect of the related party transactions;

- the financial data provided to DOTARS indicated that the entity was not borrowing any capital to invest in the re-opening of the Lakes Creek plant, but it was forecast that the Teys group of companies would receive cash inflows of $18.484 million between 2003–04 and 2006–07 in relation to capital expenditure at the plant, paid for by Group companies. In this context, a Regional Partnerships contribution of $600 000 (plus GST) was not significant (relative to the total proposed capital expenditure) and it is unclear whether those funds added to the project outcomes, such that it would represent value for money to the Commonwealth;
• apart from a negligible amount of work in progress as at June 2003, the actual statement of financial position for 2002–03 and the forecasts for 2003–04, 2004–05 and 2005–06 did not include any non-current assets (such as the asset value of the plant itself and the capitalised value of capital expenditure, including the upgrade to which Regional Partnerships funds were requested); and

• the plant was forecast to be operating at a profit by the second year of operation (2005–06), raising further questions about whether Regional Partnerships funds were necessary for the project to proceed in the manner and timeframe indicated.

4.26 No company with the name ‘Teys Bros (Lakes Creek)’ has been registered with ASIC.

4.27 On 16 July 2003, Shelf Company Services Pty Ltd lodged with ASIC an application for registration as a proprietary company for an entity with the proposed name ‘Teys Bros (Rockhampton) Pty Ltd’ (Teys Bros (Rockhampton)). The application identified that the ultimate holding company for the proposed company was ‘Consolidated Press International Holdings Limited’, a company incorporated in the Bahamas. The application stated that one ordinary share had been issued, with an amount of $1.00 paid in respect of this share, which had been taken up by Teys Bros (Holdings) Pty Ltd, ACN 009 872 600 (Teys Bros (Holdings)). The registered office for the proposed company Teys Bros (Rockhampton) was the same as the address listed for Teys Bros (Holdings).771

4.28 Teys Bros (Holdings) lodged a copy of its financial statements and reports with ASIC on 17 March 2004. Accordingly, this data was publicly available at the time DOTARS was assessing the Regional Partnerships application for funding. The Director’s Report as at 30 June 2003 stated that Teys Bros (Rockhampton) was a 100 per cent owned and controlled entity of Teys Bros (Holdings).

4.29 Similarly, separate subsidiary companies have been established to operate the plants located at Biloela, Beenleigh, Innisfail and Naracoorte and the feedlot lot at Condamine, being:

• Teys Bros (Biloela) Pty Ltd ACN 009 669 265;

771 On 21 May 2004, ASIC received notification that Teys Bros (Rockhampton) Pty Ltd had passed a Special Resolution to change the company’s name to ‘Teys Bros (Central Queensland) Pty Ltd’. 

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• Teys Bros (Beenleigh) Pty Ltd ACN 009 672 459;
• Teys Bros (Innisfail) Pty Ltd ACN 105 563 282;
• Teys Bros (Naracoorte) Pty Ltd ACN 010 807 986; and
• Teys Feedlots Pty Ltd ACN 010 835 533.

4.30 This indicates that it is likely that the financial data received by DOTARS related to the proposed operation of the Lakes Creek plant by Teys Bros (Rockhampton). However, as DOTARS made no inquiries to clarify the precise applicant identity, despite the readily identifiable anomalies (as discussed above and further below), this was also not clarified.

**Teys Bros (Holdings) Pty Ltd**

4.31 At the same time as the organisation chart was provided to DOTARS on 15 April 2004, a revised Regional Partnerships application form was submitted. This time, the applicant entity was identified as ‘Consolidated Meat Holdings – Teys Bros (Lakes Creek) Pty Ltd’ trading as ‘Teys Bros (Lakes Creek)’. The ACN provided, 065 093 709, again related to Consolidated Meat Group Pty Limited. The information provided to DOTARS on 15 April 2004 also included a register of directors for Consolidated Meat Group Pty Limited, ACN 065 093 709.

4.32 However, the amended application and other additional information was provided to DOTARS under cover of a letter carrying the letterhead of Teys Bros (Holdings) Pty Ltd, with ACN 009 872 600 and ABN 38 009 872 600. On 27 April 2004, DOTARS did a search of that ABN, which confirmed that it related to Teys Bros (Holdings). The applicant name on the updated application was then amended by DOTARS to be Teys Bros (Holdings), with the annotation: ‘From ABN check.’ There is no evidence of DOTARS seeking any clarification from the applicant.

4.33 This was the entity that DOTARS advised the then Parliamentary Secretary was the applicant and with whom DOTARS subsequently executed the Funding Agreement. However, DOTARS did not seek any financial information relating to that entity or its parent entities.

4.34 As noted, at the time the Regional Partnerships application was received, the most recently available financial report for Teys Bros (Holdings) was for the 2002–03 financial year, which had been lodged with ASIC on

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772 Consolidated Meat Holdings Pty Limited is a separate company with ACN 065 092 775.
17 March 2004. This financial report, and subsequent financial reports, disclosed that the principal activities of Teys Bros (Holdings) are the production, wholesaling and exporting of meat products, feedloting and pastoral activities.\footnote{Teys Bros (Holdings) Pty Ltd, Directors’ Report 30 June 2003, Directors’ Report 30 June 2004, and Directors’ Report 30 June 2005, all available from the Australian Securities and Investments Commission’s public database.}

4.35 The financial reports also identify Teys Bros (Holdings) as a large proprietary company. The Review of Operations included in the Directors’ Report as at 30 June 2003 stated that:

The economic entity during this financial year experienced strong profits despite a difficult year and absorbing the Consolidated Meat Group trading losses.

4.36 In this respect, the Directors further reported that the profit from ordinary activities after tax and outside equity interests for the year ended 30 June 2003 was $22 496 504 and that a dividend of $22 401 990 had been declared and paid to shareholders. This level of financial performance was achieved on consolidated gross operating turnover of $821 756 421, with the consolidated gross assets of Teys Bros (Holdings) and its controlled entities being valued at $283 783 203.

4.37 Teys Bros (Holdings) is a holding company. The 2002–03 financial report that was available at the time the Regional Partnerships application was submitted stated that it fully owned 18 other companies (including 11 that it still controlled as of 11 April 2007) and majority (51 per cent) owned a further three companies (including one in which it still held shares as of 11 April 2007).\footnote{As of 11 April 2007, it was the ultimate holding company in respect to two organisations (Teys Food Services Pty Ltd ACN 116 237 757 and Murgon Leather Pty Ltd ACN 010 863 493) and held fully paid shares in 16 companies.} Reflecting its holding company nature:

- $771 223 405 (94 per cent) of the gross operating revenue reported for 2002–03 of $821 756 421 was earned by controlled entities; and
- $165 651 459 (58 per cent) of value of consolidated gross assets as at 30 June 2003 of $283 783 203 were held by controlled entities.

4.38 In this context, government grants are a valuable source of funding to for-profit organisations. This is because obtaining grant funding increases after tax cash flows to the funding recipient, but without the recipient being
required to pay a return on those funds.\textsuperscript{775} However, DOTARS did not seek to establish whether the applicant had exhausted other funding sources (including by raising either equity or debt capital or fully financing the project from within existing finances) before applying to the Regional Partnerships Programme for funding. This oversight is significant having regard to the value of the assets reported by Teys Bros (Holdings), its reported profits and the dividends paid to shareholders.

4.39 The Directors’ Report included in the Teys Bros (Holdings) financial report for 2002–03 lodged with ASIC on 17 March 2004, stated that:

The economic entity changed significantly during the financial year. The Consolidated Meat Group was merged into Teys Bros (Holdings) Pty Ltd operations. As part of this transaction, 51% of Teys Bros (Holdings) Pty Ltd was sold to the Consolidated Pastoral Company Pty Ltd. In addition to this transaction the Miamba Pastoral Coy, Sedgeford Pastoral Coy and Baratria Pastoral Coy were sold to Teys Investments from Teys Bros (Holdings) Pty Ltd.

4.40 The Teys Bros (Holdings) financial report for 2002–03 disclosed that it had acquired 100 per cent of the units and share capital of seven entities that comprised the Consolidated Meat Group and that, in addition to the shares and units, the seller issued a promissory note of $117 773 000. The financial report further disclosed that, as consideration for this acquisition, Teys Bros (Holdings):

- issued equity to the seller, Consolidated Pastoral Company Pty Ltd, which comprised 1 092 857 B Class Ordinary Shares paid in full to the amount of $91 204 516\textsuperscript{776}; and
- paid cash of $1 972 246 for acquisition costs.

4.41 The merger made Consolidated Pastoral Company Pty Ltd the majority shareholder in Teys Bros (Holdings). Specifically, it now held 51 per cent of ordinary shares on issue, with Teys Investments Pty Ltd holding the remaining 49 per cent of ordinary shares (comprising 1 050 000 A Class Ordinary

\textsuperscript{775} By obtaining Regional Partnerships funding, the recipient is able to reduce its own contribution to the project (that would have been funded either by equity or through debt) thereby reducing its outgoings, with the additional benefit of incoming cash flows (with no required rate of return) at an early stage of the project.

\textsuperscript{776} This value was reported as representing the fair value of the net assets received for the shares. This was calculated by adding the $117 773 000 promissory note received to the net liabilities of the Consolidated Meat Group at the date of acquisition of $26 568 484.
Shares\textsuperscript{777}). In its financial report for 2002–03, Consolidated Pastoral Company Pty Ltd accounted for the 51 per cent investment in Teys Bros (Holdings) at a book value of $126 617 665 at 30 June 2003.

4.42 In the course of its assessment of the application for the Lakes Creek Upgrade project, DOTARS did not obtain any information in relation to the merger so as to properly understand the corporate group that was seeking Regional Partnerships funding, including to assess whether the group had exhausted other funding sources. In this respect, according to information held by ASIC that was publicly available at the time the Regional Partnerships application was being assessed:

- as of 30 June 2003, Consolidated Pastoral Company Pty Ltd, a large proprietary company with assets of $424 518 885 and consolidated gross operating revenue of $35 511 769, was a company limited by shares incorporated and domiciled in Australia. The principal activities of the economic entity were reported as being as a pastoral company. Its ultimate parent entity was reported as being Consolidated Press International Holdings Limited, a company controlled by Mr K F B Packer;\textsuperscript{778} and

- as of 30 June 2002,\textsuperscript{779} Teys Investments Pty Ltd had issued 10 000 shares with $10 000 fully paid in relation to these shares. Of these, 9 167 shares were reported as being held by 19 different members comprising individuals and companies.\textsuperscript{780}

\textit{ANAO conclusion}

4.43 Appropriate scrutiny of relevant entities in the corporate group is an important due diligence step where incorporated entities apply for Regional Partnerships funding. This has been recognised, at least in part, in DOTARS’ assessment of some projects involving corporate entities. For example, in the case of RP01459 Sakai,CIC Business and Export Development project, involving an application for funding from the manufacturing arm of a majority Japanese-owned corporate group, DOTARS sought written confirmation that the applicant company’s Japanese and Australian parent companies agreed to

\textsuperscript{777} As at 30 June 2003, the A Class and B Class ordinary shares were reported as ranking equally.

\textsuperscript{778} As of 11 April 2007, the most recent financial report lodged with ASIC (for the 2005–06 financial year) disclosed that the ultimate parent entity of Consolidated Pastoral Company Pty Ltd remained Consolidated Press International Holdings Limited.

\textsuperscript{779} As at 11 April 2007, this was the most recent annual return lodged with ASIC by this company.

\textsuperscript{780} The identity of the member(s) in relation to the remaining 833 shares was not reported.
the applicant using its accumulated profits to fund its contribution to the project.

4.44 In the case of the Lakes Creek Upgrade application, however, DOTARS’ due diligence fell short in respect to:

- identifying the corporate entity that owned the assets that were the subject of the Regional Partnerships application for funding; and
- obtaining the information in relation to that entity and other relevant entities in the corporate group necessary to appropriately inform its assessment.

Project assessment

4.45 On 1 April 2004, the Regional Office wrote to the applicant acknowledging receipt of the application, and requesting that additional information be provided. In order to fast-track the assessment, DOTARS requested that the additional information be provided as early as possible or by 29 April 2004. Table 4.1 identifies the extent to which additional information provided by the applicant on 15 April 2004 satisfied DOTARS’ request. In addition, as outlined above, DOTARS did not adequately scrutinise this information so as to identify the entity within the corporate group that was applying for funding and, as a consequence, did not obtain the necessary financial and other data for all relevant corporate entities in the group.
Table 4.1
Provision of addition information sought by Regional Office

<table>
<thead>
<tr>
<th>Information requested</th>
<th>Information provided</th>
</tr>
</thead>
<tbody>
<tr>
<td>Clarification of the target opening, including a copy of the project plan/time line.</td>
<td>A half-page outline of the project timeline.</td>
</tr>
<tr>
<td>A business plan.</td>
<td>A copy of the strategic plan that was developed in 2003 for the Teys Group, which developed the idea of expanding the business by investing in another abattoir to increase the Group’s total cattle slaughter to 1.0 million head per year.</td>
</tr>
<tr>
<td>Any plans or studies demonstrating the need for the project.</td>
<td>A budget that was developed for the Lakes Creek plant’s re-opening comprising a three year projection of financial performance, financial position and cash flows.</td>
</tr>
<tr>
<td>An outline of Teys Bros’ ownership and management structure, including details of partners and/or directors.</td>
<td>Organisation and ownership chart provided, together with a register of directors for Consolidated Meat Group Pty Limited.</td>
</tr>
<tr>
<td>A list of pecuniary interests relevant to the project.</td>
<td>Advised that there were no pecuniary interests in the project by directors or management of the Group.</td>
</tr>
<tr>
<td>Information on funding partners.</td>
<td>Only partner funding to come from applicant: $645 640 cash and $27 000 in-kind.</td>
</tr>
<tr>
<td>Evidence of community support, co-funding and local government support.</td>
<td>Letters of support from the Mayor (elect) of the City of Rockhampton, Senator the Hon. Ron Boswell, the State Department of State Development and Innovation and the State Member of Parliament.</td>
</tr>
<tr>
<td>Clarification of the budget line items to confirm that the amounts were based on quotes received or, if estimates, how they were calculated.</td>
<td>Quotes and estimates.</td>
</tr>
<tr>
<td>Information about who will measure the nominated outcomes and the method of reporting this to the Commonwealth.</td>
<td>Restated the same outcomes and performance measures as identified in the application, with advice that the General Manager of the plant would report quarterly.</td>
</tr>
<tr>
<td>Evidence concerning the impact of the project on other businesses/organisations to address competitive neutrality issues in the region and at state and national level.</td>
<td>Extra statements made in the application form emphasising that the project involved re-establishment of competition that previously existed.</td>
</tr>
</tbody>
</table>


Outcomes

4.46 DOTARS’ assessment of the application against the outcomes criterion focused on the issue of competitive neutrality (see Figure 4.3). This issue is examined further below at paragraphs 4.90 to 4.107.
Figure 4.3
Assessment against the outcomes criterion

- Outcomes
The project is anticipated to deliver around 250 new jobs and 25 traineeships in the upgraded Lakes Creek Meatworks. However, advice from the Australian Department of Agriculture, Fisheries and Forestry is that there is excess capacity nationally in meatworks, due to limited cattle numbers and this situation is likely to exist for two to three years while the national herd is rebuilt in the wake of the drought. It is difficult to estimate the net employment outcomes, but indications are that jobs and production at the Lakes Creek plant are likely to be at the expense of work at other plants.

The application fails to address the issue of competitive neutrality, particularly in relation to the Australian Meat Holdings (AMH) plant currently operating nearby. The applicant claims that re-opening the Lakes Creek plant would be restoring competition that existed in the past. However, the industry has moved on, adapting to an environment without the Lakes Creek works.

The application does not satisfy this criterion.

Source: Project assessment provided to then Parliamentary Secretary by DOTARS on 7 June 2004.

4.47 An issue not addressed in DOTARS’ assessment against the outcomes criterion was whether the project would proceed regardless of whether Regional Partnerships funding was provided and, indeed, whether the project was already underway. This issue required attention particularly given the earlier request for in-principle approval and the observations in this regard advised to National Office by the Regional Manager. Further, as was noted by the CQACC in its representations to DOTARS in relation to the request for in-principle approval, an earlier project submitted through that ACC (RP00203 Upgrade Sawmilling Capacity to Meet Export Demand, which has also been subject to an ANAO Case Study) had not been approved for funding due to retrospective funding issues.781

4.48 In the June 2003 report of its inquiry into a funding matter under the Dairy Regional Assistance Programme, the Senate Finance and Public Administration References Committee commented that:

If, on the other hand, the program guidelines allow for a grant to be made even though a project is fully financed and is in fact already well underway, this raises questions about the guidelines themselves. It touches on the broader question of what public policy objective Dairy RAP will achieve if it has the

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781 A second application by that applicant (RP00740 AUSGUM Furniture Expansion project, which has also been subject to an ANAO case study) was being developed at the time of the CQACC’s representations. The application was subsequently submitted to DOTARS on 19 March 2004 and approved on 1 April 2004.
potential to be used simply to substitute public funding for private investment. This is a question which warrants further consideration by the department in the future administration of funding programs.782

4.49 In this respect, the ANAO Administration of Grants Better Practice Guide advises:

As a general principle, grant appraisers should be satisfied that projects would not proceed, or not in the desired manner or time scale, without assistance. Otherwise, any grant paid simply releases the applicants’ funds for other purposes that may not contribute to the objectives of the grant program. Funds paid in such circumstances provide no added value and also represent an opportunity cost to the Commonwealth...

Unless allowed under the terms of the program, one of the clearest indicators that funding assistance is not essential is if the project starts before the grant has been approved. On these occasions the applicant should be expected to prove that a good project would have collapsed without the grant.783

4.50 Under the Regional Partnerships Programme Guidelines, project proposals that are requesting funding for retrospective costs are not eligible for funding. The Regional Partnerships Internal Procedures Manual in place at the time this project was being assessed provided as follows in relation to retrospective funding:

The Commonwealth will not fund retrospective costs in relation to a project. Regional Partnerships funding cannot be used to pay any project costs incurred prior to the date of the Funding Agreement being signed by both parties (applicant and Commonwealth).

Contributions made to a project, by the applicant, prior to the signing of the Funding Agreement are not to be considered a financial contribution to the project.784

4.51 Retrospective funding is precluded under Regional Partnerships for two reasons. First, by retrospectively funding a project, the Government may be perceived as having been unduly influenced or having agreed to fund a project before due process was followed. Secondly, if an applicant has been able to secure funding to commence a project (whether this be capital or

782 Senate Finance and Public Administration References Committee, A funding matter under the Dairy Regional Assistance Program, June 2003, p. 57.

783 ANAO Better Practice Guide—Administration of Grants, May 2002, Canberra, paragraphs 3.16 and 3.20, p. 44.

borrowings), generally speaking it is unlikely that they will be able to demonstrate a sufficient level of need for Australian Government support.  

_Project start and completion dates_

4.52 There was some uncertainty regarding the date of the planned reopening of the Lakes Creek plant. In terms of the project start and completion dates:

- the March 2004 Expression of Interest stated that the project had a proposed start date of 1 May 2004 and a proposed finish date of 31 August 2004;
- the application received by DOTARS on 25 March 2004 stated that the project had an anticipated start date of April 2004 and an anticipated end date of August 2004; and
- the signed hardcopy application, dated 15 April 2004, stated that the project had an anticipated start date of April 2004 and an anticipated end date of July 2004.

4.53 The issue of the plant opening date was clarified by the Regional Office during its project assessment, but not reflected in the assessment provided to the then Parliamentary Secretary. In this respect, the supporting information attached to the hardcopy of the Regional Partnerships application form included a half-page outline of the project timelines which stated that Monday 5 July 2004 had been declared as the date for the resumption of operations at the Lakes Creek plant.

4.54 On 6 May 2004, DOTARS National Office emailed the applicant advising that, in entering the application into the TRAX database, it had discovered that the nominated start date for the project (April 2004) had already passed. The applicant was asked to confirm that April 2004 was the correct start date for the project. The applicant responded on 7 May 2004, as follows:

The proposed start date for the full scale resumption of operations on the Rockhampton plant is the 5th July 2004. Most of the work covered by that application must be completed prior to resumption. That means that we have only two months in which to complete that work.

4.55 On 28 April 2004, it was reported that the Australasian Meat Industry Employees Union and Teys Bros had agreed on wages and conditions for an

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enterprise agreement for the Lakes Creek abattoir. This provided further evidence that the plant would be re-opening irrespective of whether Regional Partnerships funding was provided.

4.56 The retrospective nature of this project was confirmed in the financial acquittal provided to DOTARS in July 2005 (see paragraphs 4.122 to 4.123). Specifically, the financial acquittal of the Regional Partnerships-funded project included expenditure incurred commencing in 8 April 2004. This was prior to:

- further information supporting the application being provided to DOTARS for assessment on 15 April 2004;
- DOTARS finalising its project assessment on 7 June 2004;
- the then Parliamentary Secretary’s approval of funding on 1 July 2004;
- announcement of the funding approval by the then Minister for Transport and Regional Services on 15 July 2004; and
- execution of a Funding Agreement on 2 September 2004.

**ANAO conclusion**

4.57 The application for funding involved retrospective funding of a project that had already commenced prior to a complete Regional Partnerships application being submitted for assessment, and well before funding was approved and a Funding Agreement signed. In this context, ANAO’s Better Practice Guide states:

> As a general principle, grant appraisers should be satisfied that projects would not proceed, or not in the desired manner or time scale, without assistance. Otherwise, any grant paid simply releases the applicants’ funds for other purposes that may not contribute to the objectives of the grant program. Funds paid in such circumstances provide no added value and also represent an opportunity cost to the Commonwealth.\(^76\)

**Partnerships**

4.58 The only parties contributing to the project were to be the Regional Partnerships Programme and the applicant. The applicant’s nominated contribution was:

- $638 630 in cash; and
- $27 000 in-kind comprising:

\(^76\) ANAO Better Practice Guide—Administration of Grants, op. cit., paragraphs 3.16 and 3.20, p. 44.
4.59 In this context, there were no third party partnership contributions to be confirmed during the assessment process.

4.60 In relation to the Lakes Creek Upgrade application for funding, the applicant was proposing to contribute 52 per cent of cash funds (with no identified borrowings) and 53 per cent of total project costs. With the Regional Partnerships funding sought for the Lakes Creek Upgrade project representing 48 per cent of cash costs, DOTARS advised the then Parliamentary Secretary that the partner contributions were insufficient for a commercial venture of this nature, but nevertheless assessed that the partnerships and support criterion was ‘partially satisfied’, as illustrated by Figure 4.4.

- $20,000 in project management (400 hours at $50 per hour);
- $5,000 for project evaluation; and
- $2,000 for audit.
**ANAO conclusion**

4.61 The project involved ‘weak’ partnership funding with the Regional Partnerships Programme being asked to contribute 48 per cent of project cash costs to a commercial project. No partnership contributions were to be made by other levels of government, with the applicant being the only other party that was nominated as making either a financial or in-kind contribution. Notwithstanding this, DOTARS assessed that the partnerships and support criterion had been partially satisfied.
Applicant and project viability

4.62 As illustrated by Figure 4.5, DOTARS assessed the applicant as representing a low viability risk, but that the project represented a high viability risk. As outlined further below, neither conclusion was supported by sufficient and appropriate due diligence inquiries, including an external viability assessment.

Figure 4.5
Assessment against the applicant and project viability criteria

- **Applicant Viability**
  The applicant is assessed as a low risk.

  Teys Brothers is an established company successfully operating other meatworks across the country. However, given the total cost of the project, a detailed risk assessment of the applicant would be required.

  The applicant satisfies this criterion.

- **Project Viability**
  The project is assessed as a high risk.

  The application fails to address critical issues such as market share, supply of cattle and competitive neutrality.

  Due to the nature and size of the project, an independent viability assessment would need to be carried out to address these issues.

  The application partially satisfies this criterion.

Source: Project assessment provided to then Parliamentary Secretary on 7 June 2004.

4.63 DOTARS also assessed the application as ‘partially satisfying’ the Project Viability assessment criterion, despite assessing the project as a high risk that had failed to address critical issues. As noted, this concept was not part of the documented assessment procedures.

*External viability assessment*

4.64 In terms of applicant financial risk and project commercial risk/sustainability, the Internal Procedures Manual applying at the time this application was assessed required that the assessment of applications from the private sector seeking more than $250,000 in Regional Partnerships funding was to include an external viability assessment. However, no such external advice was commissioned by DOTARS to inform its assessment of the project and advice to the then Parliamentary Secretary. In the context of reports that
the plant had closed in July 2002 due to unprofitable operations\footnote{See, for example, Australian Consumer and Competition Commission, \textit{ACCC not to Oppose Merger Between Consolidated Meat Group and Teys Bros}, 27 August 2002. See also comments made by the then Executive Chairman and Joint Chief Executive of Consolidated Meat Group to the Rural and Regional Affairs Legislation Committee, 20 August 2002 (see paragraph 4.4).}, it would have been prudent for DOTARS to commission an external assessment prior to finalising the funding recommendation. Instead, DOTARS intended that an external assessment would be undertaken post-approval, in the event funding was approved. In this context, on 1 July 2004, the then Parliamentary Secretary approved funding for the project:

subject to an independent viability assessment.

\textbf{4.65} As is discussed further below, this funding condition was not satisfied by the department.

\textit{Analysis of financial position and performance}

\textbf{4.66} For some projects in ANAO’s sample, the departmental assessment provided to the Ministerial decision-maker commented on the profitability of the applicant and/or the project, based on the information provided by the applicant. However, the only applications from for-profit organisations where documented analysis of historical financial results existed was in relation to applications that had been subject to an external viability assessment. In those cases, analysis was generally undertaken by the external assessor of the existing financial position, recent earnings performance and various financial ratios were often calculated and compared to benchmarks so as to inform the assessment.

\textbf{4.67} In respect to the Lakes Creek Upgrade project, as no external viability assessment was commissioned during the department’s assessment process, it was up to DOTARS officials to obtain and analyse the necessary financial and related data. However, DOTARS’ due diligence in this regard was inadequate.

\textbf{4.68} As noted in Table 4.1, the applicant provided DOTARS with a 2003 Strategic Plan for the Teys Group in lieu of a business plan for the project. DOTARS letter of 1 April 2004 had requested the business plan, which was to include, where applicable:

- feasibility study
- industry data/research
- cash flow projection for the project period + 3 years. Include assumption used and key/sensitive factors in the projections. It could
include investment analysis details such as rates of return, liquidity and debt analysis assumptions.

- marketing strategy and assumptions
- SWOT analysis.

4.69 The 2003 Strategic Plan looked at core business, goals, threats and opportunities across the Group. Embedded within that was a strategy to start up the Lakes Creek site as the first high priority opportunity. However, the Strategic Plan did not provide any financial or other analysis underpinning the viability of implementing that strategy. In providing the Strategic Plan to DOTARS on 15 April 2004, the applicant advised that:

There was no actual business plan prepared specifically for this project. We used the Strategic Plan for the Teys Group to determine our strategies for the purchase of livestock and the sale of product to the Export and Domestic Markets.

In effect the Strategic Plan became our feasibility study and business plan.

4.70 As discussed, the applicant separately provided financial information that it identified as being budgets that were developed for the Lakes Creek plant’s re-opening, but DOTARS failed to obtain any financial data relating to the entity that it understood to be the applicant (or in relation to other relevant entities in the Teys Group). However, notwithstanding the absence of the financial information necessary to inform an assessment of the applicant’s viability, DOTARS concluded that the applicant represented a low risk (see Figure 4.5 above).

Project costing

4.71 The Regional Partnerships application included a project cash budget of $1,238,680. As mentioned, on 1 April 2004, the Regional Office sought clarification of the budget line items to confirm that the amounts were based on quotes received or, if based on estimates, how they were calculated.

4.72 The requested information was provided on 15 April 2004. However, there was no documented evidence of DOTARS examining the information provided by the applicant to satisfy itself that the budget was complete and accurate and related to the project for which funding was being sought. In this respect, ANAO analysis of the information provided to DOTARS revealed that:

- although the budgeted amount for electrical works associated with the upgrade of the two boilers of $88,720 was stated to be GST exclusive,
the attached quote stated that the amount of $88 720 included GST. Accordingly, the project budget was overstated by $8 065;

- the budget included an amount of $150 000 for water conservation works. The estimate stated that this amount included a contingency of $7 000; and

- the budget included an amount of $750 000 for Information Technology integration. The quote supporting this element of the budget was for $706 394.90. This quote was annotated such that a revised quote was to be provided to include an additional $100 000. No such additional quote was obtained by DOTARS. Accordingly, the budget was either overstated by $43 605.10 (based on the original quote of $706 394.90) or understated by $56 394.90 (based on the annotation).\footnote{On this issue, in June 2007, DOTARS advised ANAO that, at the conclusion of the project, the Statement of Receipts and Expenditure in the Final Report listed expenditure for Information Technology of $902 329.20.}

4.73 None of these anomalies were identified by DOTARS and, as a result, no questions were raised with the applicant in order to clarify the position. Accordingly, the project budget was overstated by $58 670.55 (or five per cent) as compared with the documentation of expected costs. Among other things, this meant that the Regional Partnerships Programme was actually being asked to contribute more than 50 per cent of estimated project costs.

**Analysis of financial forecasts**

4.74 Also on 1 April 2004, in accordance with the requirements of the Internal Procedures Manual, the Regional Office had requested that the applicant provide cash flow forecasts for the project period plus a further three years (together with the assumptions used and key/sensitive factors in the projections). In response, on 15 April 2004, the applicant provided a budget that was developed for the Lakes Creek plant’s re-opening comprising a three year projection of financial performance, financial position and cash flows.

4.75 However, there was no documented analysis by DOTARS of this information either in TRAX or separately. For example, as illustrated by Figure 4.6, the plant was forecast to make a cash loss during 2003–04 (the year in which the plant was being readied for re-opening) and 2004–05 (the first year the plant would be back in operation). However, by the second year of operations, the plant was forecast to be generating significant positive cash flows. For example, DOTARS did not calculate an NPV for this project to
satisfy itself that the project was viable, but only with the benefit of Regional Partnerships grant funds, thereby generating economic or social outcomes of benefit to the community that might not otherwise be achieved. In June 2007, DOTARS advised ANAO that it is not a procedural requirement for assessors to calculate a project’s NPV and that:

The matter of which economic forecast calculation is best to use and under what circumstances is a matter for discussion with the department’s financial viability assessment providers.789

**Figure 4.6**

*Projected cash flows*

Source: Information provided to Regional Office by applicant, 15 April 2004.

**ANAO conclusion**

4.76 In the context of reports that the Lakes Creek plant had closed in July 2002 due to unprofitable operations, it was important that DOTARS rigorously assess applicant and project viability risks. However, the department’s assessment against the applicant and project viability criteria was deficient in terms of:

789 As noted earlier, an external viability assessment was not undertaken for this project notwithstanding that the then applicable Internal Procedures Manual required such an assessment, and the then Parliamentary Secretary had approved Regional Partnerships funding subject to an explicit condition that required an external viability assessment to be undertaken.
failing to obtain unambiguous confirmation of the entity that was the legal applicant for funding, and obtaining and scrutinising the necessary information to appropriately assess applicant viability;

an external viability assessment not being commissioned during the assessment process, notwithstanding that the then applicable Internal Procedures Manual required this to be done in every case for an application of this nature;

project costings supplied by the applicant not being rigorously scrutinised; and

there was no documented analysis of the financial forecasts for the project supplied by the applicant.

Funding approval and announcement

4.77 As illustrated by Figure 4.7, the CQACC recommended the project and rated it a high priority, but the department considered that the perceived benefits to the region did not outweigh the assessed failure to satisfy the Regional Partnerships Guidelines. Accordingly, DOTARS did not recommend the project for funding approval. The brief to the then Parliamentary Secretary covering the department’s assessment stated that:

If the application was successful there would be competitive neutrality issues in an industry that has seen a change in market share and cattle supply. In addition, the Regional Partnerships bid represents 48 per cent of the cash required for the project and is not commensurate with the estimated high level of return the applicant will receive.
Figure 4.7

ACC comments

- **Area Consultative Committee Recommendation**
  The Central Queensland ACC has recommended this project and rated it a high priority. The ACC comments note that the closure of the plant in 2002 was a shock, economically and socially, to the region and that re-opening the plant will be an excellent opportunity for some of the workers displaced by the closure. The ACC considers increased competition for cattle and market share as being positive.

- **Other Considerations**
  DOTARS recognises that the ACC considers this project important to the region. However, the project fails on one criterion, Outcomes, and only partially satisfies the criteria Partnerships and Support, and Project Viability. Therefore the project is not recommended for funding.

Source: Project assessment provided to then Parliamentary Secretary on 7 June 2004.

4.78 The assessment of the Lakes Creek Upgrade project was included in a package of 22 Regional Partnerships applications submitted to the then Parliamentary Secretary on 7 June 2004. It was one of six projects that were assessed as not meeting the Regional Partnerships Guidelines. Specifically, the then Parliamentary Secretary was advised that:

- the application did not satisfy the outcomes criterion, particularly due to competitive neutrality concerns;
- the partnerships and support criterion was only ‘partially’ satisfied; and
- the project viability criterion was also only ‘partially’ satisfied.

4.79 On 1 July 2004, the then Parliamentary Secretary annotated the project assessment stating that she disagreed with the department’s recommendation, and approving the full amount sought. The documented rationale for the decision is outlined in Figure 4.8.
As is evident from Figure 4.8, the then Parliamentary Secretary addressed two of the department’s three concerns in the documented reasons for disagreeing with the recommendation that funding not be approved. Specifically:

- the then Parliamentary Secretary indicated that she had satisfied herself that there were no competitive neutrality issues, after her Office or the Office of the then Minister for Transport and Regional Services undertook inquiries of other (unidentified) meatworks; and

- project viability issues were to be addressed through an external viability assessment as a condition of funding approval.

The then Parliamentary Secretary’s documented rationale for approving funding did not address the third concern raised by DOTARS, being that partnership contributions were insufficient given the estimated high level of returns to the for-profit applicant.

**Announcement of funding approval**

Funding for the Lakes Creek Upgrade project was approved on 1 July 2004. On 6 July 2004, the Departmental Liaison Officer to the then Parliamentary Secretary emailed DOTARS’ National Office, the Regional Office and the new media adviser in the then Parliamentary Secretary’s Office advising that funding had been approved for the project. As illustrated by Figure 4.9, this email further advised that liaison was underway with the
Office of the then Deputy Prime Minister and Minister for Transport and Regional Services regarding announcement of funding.

**Figure 4.9**

**Advice from Departmental Liaison Officer that funding had been approved**

The following advice is strictly confidential.

Mrs Kelly has not agreed with the Department’s recommendation on the above project and has approved it for the full amount of $600,000 (GST exclusive). She has disagreed on the basis of “the significant social and economic benefits of the project for the Rockhampton community”. She also does not agree that competitive neutrality is an issue as the businesses in question are largely export focussed. The Minister’s office has spoken with the other meatworks and been advised that re-opening the plant would not affect job security in the short term.

I am currently liaising with Minister Anderson’s Office re. announcement arrangements. It could be that Minister Anderson will decide to announce this project personally. As soon as I am advised, I will let you know so that you can prepare the relevant approval letters, a draft media release and project summary.

Source: DOTARS’ National Office records.

4.83 The Internal Procedures Manual in place at the time funding for the Lakes Creek Upgrade project was approved provided as follows in relation to the announcement of funding for Regional Partnerships projects:

The [coalition] MP /Patron Senator is notified a project has been funded and is invited to advise the applicants and make arrangements for announcement. Two or three days after this, advice to the successful applicants and ACCs will be despatched by the Minister’s Office. Advice to non-coalition MPs will also be despatched by the Minister’s office.790

4.84 On 14 July 2004, letters were sent to the applicant and the Chair of the CQACC providing formal advice that funding for the Lakes Creek Upgrade project had been approved. Both letters indicated that the applicant and ACC had already been advised of the funding approval. However, there are no records of when and how this earlier advice had been provided, or by whom.

4.85 In this case, a letter confirming funding approval was sent (in terms similar to the letters to the applicant and the CQACC) to the then Deputy Prime Minister and Minister for Transport and Regional Services. DOTARS records indicate that the patron Senator was provided with a copy of this

letter. On 15 July 2004, funding for this project was announced by the then Deputy Prime Minister and Minister for Transport and Regional Services (see Figure 4.10).

The Internal Procedures Manual required that the Minister’s Office also dispatch a letter advising of funding approval to the local Federal Member where that Member was not from one of the Coalition parties. In this case, a letter was required to be sent to the Member for Capricornia, who had earlier raised concerns in the Parliament about the closure of the Lakes Creek plant. However, when sending draft letters to the then Parliamentary Secretary for signature, the Departmental Liaison Officer suggested that the letter to the local Federal Member could be withheld.
4.86 Unlike many other projects that have been approved subject to a satisfactory viability assessment, the letter to Teys Bros (Holdings) from the then Parliamentary Secretary made no mention of the condition that had been placed on funding approval. This oversight was compounded by DOTARS not
taking any steps to arrange for an external viability assessment to be subsequently undertaken.

4.87 Instead, on 9 August 2004, the Regional Office provided a draft Funding Agreement for signature. The Funding Agreement was signed by Teys Bros (Holdings) on 31 August 2004, and the Regional Office on 2 September 2004. The Funding Agreement made no provision for the payment of Regional Partnerships funds to be subject to a satisfactory external viability assessment.

4.88 In the event, the funding was approved by the then Parliamentary Secretary on the explicit condition that such an assessment would be conducted. However, it is apparent that the Regional Office proceeded to execute a Funding Agreement with the applicant on the basis of the email advice of the funding approval received from the Departmental Liaison Officer (which failed to mention the conditional nature of the approval – see Figure 4.9) and without first obtaining a copy of the then Parliamentary Secretary’s actual signed approval of funding. This was not good practice.

**ANAO conclusion**

4.89 The assessment of applicant and project viability was deficient in that the documented procedures for an external viability assessment were not implemented either before the funding was approved, or subsequently. This was notwithstanding the fact that funding was approved subject to an independent viability assessment. In this respect, having not complied with the terms of the then Parliamentary Secretary’s approval of the spending proposal for this project, DOTARS did not comply with the requirements of FMA Regulation 13 in entering into the Funding Agreement.

**Competitive neutrality**

4.90 The Regional Partnerships Guidelines applicable at the time the Lakes Creek Upgrade project application was assessed and approved provided:

**What projects are not eligible for funding?**

- Where the project competes directly with existing businesses, unless it can be demonstrated that there is an unsatisfied demand for the product or service, or the product or service is to be provided in a new way.

4.91 For this project, adequate due diligence in relation to this issue necessarily required that DOTARS seek advice and information in relation to
the beef industry generally and the re-opening of the Lakes Creek plant in the context of the Central Queensland beef industry. The former aspect was addressed by DOTARS seeking advice from the Commonwealth Department of Agriculture, Fisheries and Forestry (DAFF). However, DOTARS did not undertake any inquiries of the applicant or the entity that was already operating an abattoir in the Rockhampton region. As a consequence, a more rigorous project assessment would have resulted in a better informed funding decision.

*Department of Agriculture, Fisheries and Forestry*

4.92 DOTARS contacted DAFF in relation to the Lakes Creek Upgrade project. Specifically, on 4 May 2004, DOTARS sought advice from DAFF on the likely impacts of the re-opening of the Lakes Creek plant, as follows:

They are requesting $600,000 from us, so if we approve the project, the approval will be subject to an independent assessment of the viability of the project (i.e. we won’t be making a decision based solely on any advice you can provide).

On initial reading, several issues leap out…the fundamental ones are:

- Inputs – would there be cattle available to supply the upgraded works? What are the likely impacts of increased competition for cattle?
- Markets – is there unmet demand that Lakes Creek will fill?
- The whole competition issue will need to be addressed in some detail.
- Workforce – I know this may be a bit outside your area of expertise, but you may be able to point me to someone who can advise on issues of skilled workforce availability. Also will they work at Lakes Creek given its history?

...Any advice that you can provide on the likely impacts, positive and negative, of the re-opening of the Lakes Creek works would be greatly appreciated.

4.93 DAFF provided its advice to DOTARS on 18 May 2004. DAFF advised that, in general terms, there had been a rationalisation in the processing sector as a result of excess capacity relating to the limited supply of cattle due to the drought. DAFF concluded there that there would not be significant benefits to the Australian beef processing sector arising from the project and that the project would need to be justified on social, regional or employment grounds, as follows:
Would there be cattle available?
Processors are finding it difficult to procure good quality stock as a result of the current drought. There are opportunities to take the lower end of the market at the moment and put it to the US as manufacturing beef, but industry says there are not enough of those cattle around to fill that quota either. Likewise we will (probably) not fill our EU quota this year (high quality). Projections are that this will continue for a couple of years dependent on when the drought breaks and how quickly the national herd can be rebuilt. So the short answer is, cattle will be in more limited supply than usual. State agency people would be closer to this matter.

What are the impacts of increased competition?
There is unlikely to be any significant effect on competition in the market as a result of the reopening of this works. The dominant factor at the moment is limited supply. This company is already a buyer in the market place, so their ability to immediately have an impact to increase competition is limited. One assumes that they will shift capacity from other works to get the ball rolling at Lakes Ck while they build market share in a designated market (or take the opportunity to rationalise other operations).

Is there unmet demand that Lakes Creek could meet?
There is unmet demand, but industry already has the capacity to fill this without opening Lakes Creek – the issue is limited supply.

Is there a work force?
I’m not sure who to point you to re this skilled workforce question, but you might talk to Meat and Livestock Australia (contact details removed). There is obviously a pool of talent available in the area as AMH has works there, but there is speculation that the industrial issues surrounding the Lakes Creek closure could inhibit workers desire to return to Lakes Ck. There is both skilled and unskilled labour in an abattoir, and I am unaware of the employment and unemployment profiles in the area.

I would think that the justification for providing assistance to this project would need to be on social, regional or employment grounds. It would seem from my cursory look to be difficult to justify on an industry basis, that is that there are significant benefits to the Australian beef processing sector arising from the provision of these funds. The meat processing sector has the capacity now and into the immediate future to process all the cattle that will come forward for slaughter (under normal circumstances). However, we in this part of DAFF do not have experience evaluating industry proposals for funding because we are not in that game.
4.94 This advice was reflected in the assessment and funding recommendation provided to the then Parliamentary Secretary by DOTARS on 7 June 2004 (see Figure 4.3).

**Reporting by Teys Bros (Holdings) Pty Ltd**

4.95 As noted earlier, DOTARS did not, as part of its due diligence in regard to this application, obtain and analyse the publicly available financial report for 2002–03 that Teys Bros (Holdings) had lodged with ASIC on 17 March 2004. The Directors’ Report as at 30 June 2003 included in the financial report stated as follows in relation to likely developments and expected results:

The directors foresee that the New Year’s trading conditions will be difficult due to lack of cattle availability. The results will also continue to be affected by market conditions and the Australian dollar.

4.96 This information was relevant to an assessment of competitive neutrality issues for the Regional Partnerships application for funding.

4.97 Similarly, the Directors’ Report included in the 2003–04 financial report lodged with ASIC on 17 May 2005 stated that:

Despite difficulty experienced as a result of livestock shortages due to the drought conditions, the group achieved good trading profits. This was while continuing to absorb the Consolidated Meat Group losses with Rockhampton still out of operation at that time.

4.98 Further, the Directors’ Report included in the 2004–05 financial report lodged with ASIC on 3 May 2006 stated that:

The forthcoming year is expected to bring further tightening of livestock trading. This in combination with the behaviour of the Australian dollar and its effect on export sales has profit expectations for 2006 slightly down on this last financial year.

4.99 ANAO recognises that these latter two Directors’ Reports were not available to DOTARS at the time it was assessing the Regional Partnerships application. Nevertheless, they demonstrate the continuing nature of the cattle supply shortages thereby emphasising the significance of the oversight by the department in not obtaining and analysing the 2002–03 financial report (that was available at the time of the project assessment) in order to more fully advise the Ministerial decision-maker.
**Funding decision**

4.100 In its project assessment, DOTARS concluded that the application did not satisfy the outcomes criterion due to:

- jobs and production at the Lakes Creek plant being likely to be at the expense of work at other plants due to the shortage of cattle in the wake of the drought; and

- having failed to address the issue of competitive neutrality, particularly in relation to the export beef plant operated in Rockhampton by Australian Meat Holdings Pty Limited.  

4.101 However, as illustrated by Figure 4.8 above, in approving funding for this project, the then Parliamentary Secretary annotated the brief as follows:

> Competitive neutrality is not the same issue for export focused businesses. Supply of cattle is largely dependent on seasonal factors. Ministers office has spoken with other meatworks and been advised that re opening the plant would not affect job security in the short term.

4.102 The then Parliamentary Secretary did not indicate which other meatworks had been spoken to. However, it is evident that these consultations could not have involved:

- examination of the reported cattle supply concerns of directors of Teys Bros (Holdings) Pty Ltd (as outlined above); or

- Australian Meat Holdings (as outlined below).

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792 DOTARS’ 16 December 2005 assessment of RP02026 Country Fresh project, relating to an application for Regional Partnerships funding of $1.24 million towards a project to expand the Tatura Abattoirs in the Goulbourn Valley in Victoria, similarly concluded that competitive advantage is a significant issue in the meat industry. In that case, despite the project involving the introduction of new technology to allow for the despatch of lamb product in boxes rather than as whole carcasses, DOTARS’ assessment was that the application failed to meet the Outcomes assessment criterion, as follows:

> ‘The project range is distinguishable from competitors due to cuts of meat used, specification range and packaging presentation. However these factors are insufficient to overcome potential competitive neutrality issues in a very competitive market.

> While the outcomes claimed by the applicant are substantial and likely to be achieved, assessment of the applicant’s viability indicates that the applicant in able to borrow sufficient funds to complete the project without a Regional Partnerships contribution and it is understood that the applicant is likely to complete the project even if the Regional Partnerships grant is not approved. Even though the Regional Partnerships grant will ensure the project commences immediately and is successful, this is not sufficient reason to overcome cost shifting concerns.’

On 9 February 2006, the Ministerial Committee agreed with DOTARS’ recommendation to not approve funding for this application.
Competitor’s concerns

4.103 On 26 July 2004, Australian Meat Holdings wrote to the then Deputy Prime Minister and Minister for Transport and Regional Services raising concerns that the provision of Regional Partnerships funding for the Lakes Creek Upgrade project breached the Regional Partnerships Guidelines as they pertained to competitive neutrality (see Figure 4.11).

Figure 4.11
Competitive neutrality concerns

I refer to your attached media release dated 15 July 2004, which details a grant of $6,660,000 (GST inclusive) to Teys Bros towards the up-grading of their Lakes Creek meat processing facility in Rockhampton Queensland. This export beef plant which was closed for 2 years after a major industrial disputation, re-opened for processing at the beginning of last week.

Australia Meat Holdings Pty Limited (AMH) also has an export beef plant located in Rockhampton, a few kilometres from the Teys Bros Lakes Creek operation. We employ a permanent workforce over 500 people processing around 650 head 6 days per week.

On behalf of AMH, I express our concerns over the grant to Teys Bros under the Regional Partnerships Program, administered by your Department. Of greater concern to AMH, and we believe also the Government is the assistance appears to be in contravention of the Regional Partnerships Program Guidelines. I refer you to page 4 of these guidelines which I have attached for your information. Specifically, I refer you to the section headed ‘What Projects Are Not Eligible For Funding?’ Point one of this section states:

‘Where the project competes directly with existing businesses, unless it can be demonstrated that there is an unsatisfactory demand for the product or service, or the product or service is to be provided in a new way.’

Teys Bros Lakes Creek operations compete directly with our existing business in Rockhampton for both cattle and labour within this geographical region.

The grant by the Federal Government through your Department is a clear intervention in the market place through a program which is clearly promoted on the basis of competitive neutrality. It is our strong view that the funding clearly discriminates against our viable Rockhampton operations to the advantage of Teys Bros.
Our concerns are that leading up to the election, we will see a further continuation of such grants to meat processing operators across other parts of Australia. Such grants will continue to distort the market through your Government’s direct intervention in this highly competitive industry.

We assure you that such indiscriminate grant allocations to our competitors in the Australian Meat Processing Industry will directly impact on the investment and jobs strategy, which to date has been supported by our US based shareholders.

We have expressed our concerns to The Honourable De-Anne Kelly MP, your Parliamentary Secretary for Transport and Regional Services and Mr Stuart St Clair from your Office in relation to this decision as well as several of your Federal Coalition colleagues, who represent other AMH sites in Townsville and Toowoomba. As yet we have not received a satisfactory response to our questions through these discussions.

This considerable grant allocation is to a plant, which over the past 15 years has been owned by five entities all which have spent considerable amounts of capital on the facility, but none have been able to make it viable for a sustained period. In contrast, the AMH Rockhampton plant has been a viable operation, and since 1995 has not lost one day of downtime due to industrial disputation.

In conclusion, we find it difficult to understand the basis for this ‘one off grant’ and our concern on the direct impact on our business. It is hoped that the grant provided by the Federal Government through your Department to the Teys Bros/ Kerry Packer Consolidated Meat Group owned Lakes Creek processing plant in Rockhampton will not be replicated across a host of our competitors located in rural and regional Australia.

Due to the significance of this matter we have forwarded a copy of this letter to the Prime Minister for his information. We look forward to your earliest response in relation to this correspondence.

Source: Australian Meat Holdings Pty Limited, correspondence to the then Minister for Transport and Regional Services dated 26 July 2004. Further correspondence dated 27 July 2004 corrected the amount of the grant to $660,000 (GST inclusive).

4.104 No response was provided to Australian Meat Holdings until 20 October 2004, after the 2004 General Election. On that date, the Chief of Staff of the then Deputy Prime Minister and Minister for Transport and Regional Services wrote to Australian Meat Holdings (see Figure 4.12).
Figure 4.12
Response to competitive neutrality concerns

Thank you for your letter of 26 July 2004 to the Deputy Prime Minister and Minister for Transport and Regional Services, the Hon John Anderson MP, concerning Regional Partnership funding to Teys Bros towards the up-grading of their Lakes Creek meat processing facility in Rockhampton. Mr Anderson has asked me to reply on his behalf.

I note your concern that this funding appears to be in contravention to Regional Partnerships guidelines. However, I can confirm that this is not the case, as you will note from the attached copy of the Regional Partnerships guidelines that it is a discretionary programme.

The decision to fund this project was based on advice from the Central Queensland ACC that the re-opening of the Lakes Creek operations would have significant social and economic benefits for the greater Rockhampton region and would not affect job security in the district.

Should you wish to acquire further advice, then Mr Paul Kah-Nutt, Executive Officer of the Central Queensland ACC, will be able to give you more information about Regional Partnerships, and advice as to how a project might or might not fit against the region’s priorities. He can be reached on telephone number (07) 4921 3639.

Thank you for bringing this matter to the attention of the Minister.

Source: Correspondence from the Office of the then Minister for Transport and Regional Services to Australian Meat Holdings Pty Limited dated 20 October 2004.

4.105 This response to Australian Meat Holdings differed from the basis for approval set down by the then Parliamentary Secretary. Specifically, as illustrated by Figure 4.8, in documenting her reasons for approving funding, the then Parliamentary Secretary made no reference to having received advice from the CQACC other than the ACC comments included in the departmental assessment provided on 7 June 2004 (see Figure 4.7). Instead, the Parliamentary Secretary had explicitly stated that the decision to fund the project was, in part, based on additional inquiries undertaken by either her Office or that of the then Minister for Transport and Regional Services, as follows:

Ministers office has spoken with other meatworks and been advised that re opening the plant would not affect job security in the short term.

ANAO conclusion

4.106 This project was one of a number examined by ANAO where the Regional Partnerships Programme was being asked to fund a project in an industry that is the policy responsibility of another portfolio. In this instance, DOTARS took appropriate steps to compensate for its lack of specialist knowledge of the beef cattle industry by seeking advice on competitive neutrality issues from DAFF. However, the Ministerial decision maker reached
a different view on the question of competitive neutrality, following discussions by either her Office or the Office of the then Minister for Transport and Regional Services with unidentified market competitors. It is apparent, however, that:

- DOTARS’ due diligence on this issue fell short, as it should have been aware, and advised the then Parliamentary Secretary, that Teys Bros (Holdings) was itself reporting concerns about cattle supply; and
- the other major abattoir located in Rockhampton was not consulted in terms of competitive neutrality issues.

4.107 In this case, the record of funding decision provided limited information addressing concerns about one of the criteria, but did not address the specific terms of the competitive neutrality eligibility criterion set out in the published Guidelines applicable to this application. It also did not address other issues identified by the departmental assessment.

Management of the Funding Agreement

4.108 The Funding Agreement provided for three payments of the Regional Partnerships funding, as follows:

- $300 000 (plus GST), representing 50 per cent of approved funding, was proposed to be paid on 25 August 2004 to cover project commencement;
- $245 454.55 (plus GST), representing 41 per cent of approved funding, was proposed to be paid on 30 October 2004, to cover mid-project progress; and
- the final $54 545.45 (plus GST), representing nine per cent of approved funding, was proposed to be paid on 30 December 2004 to cover project completion, final report and audit.

4.109 The invoice for the first instalment was received by the Regional Office on 2 September 2004. This and later invoices were submitted by Teys Bros (Holdings), the entity with whom the Funding Agreement was signed.793

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793 See paragraphs 4.15 to 4.43 for discussion of deficiencies in DOTARS’ identification of the corporate entity that owned the assets that were the subject of the Regional Partnerships application for funding and obtaining the information in relation to that entity and other relevant entities in the corporate group necessary to appropriately inform its assessment.
4.110 Due to some delays with its systems, DOTARS did not process the first payment until 16 September 2004.

4.111 On 25 November 2004, DOTARS received a tax invoice for the second instalment payment, together with a progress report and acquittal of the first instalment. This acquittal stated that total expenditure up to 10 November 2004 was $1 139 411. The invoice was approved for payment on the day it was received, 25 November 2004.

**Final payment made in advance of Funding Agreement requirements being fulfilled**

4.112 The Funding Agreement provided that the final payment was not to be made until:

- an acquittal had been provided to, and accepted by, DOTARS showing that the earlier payments totalling $545 454.55 (plus GST) had been fully expended, or there was evidence that the earlier payments would be fully expended in the near future;
- the Post Activity Report that was due on 1 December 2004 had been provided to, and accepted by, DOTARS; and
- a properly rendered tax invoice was received by DOTARS.

4.113 On 14 June 2005, Teys Bros (Holdings) provided the Regional Office with a tax invoice for the final Regional Partnerships instalment payment. This invoice was approved for payment on 21 June 2005 notwithstanding that the more substantive elements of the Funding Agreement had yet to be satisfied. Specifically:

- an acquittal (subsequent to the previous acquittal on 22 November 2004 that was provided to obtain the second instalment) had not been provided; and
- the Post Activity Report had not been provided.

4.114 By processing the payment on 21 June 2005 notwithstanding that the substantive elements of the Funding Agreement had not yet been satisfied, DOTARS was able to record the payment in the 2004–05 financial year.
4.115 A Post Activity Report was received by DOTARS on 4 July 2005 (dated 29 June 2005). It was provided by Teys Bros (Rockhampton). This was not the entity with whom the Funding Agreement was signed.\footnote{ibid.}

4.116 The Post Activity Report stated that one of the four project milestones had yet to be met. Specifically, the Report advised that, due to the unavailability of components, work was still being undertaken in relation to the introduction of a system to regulate the amount of water that was being used. This work was not expected to be completed for a further six months.

4.117 The Regional Partnerships funding of $600,000 (plus GST) was approved for the purposes of installing a new computer system, upgrading the electronic controls of the boilers and upgrading the plumbing to reduce water wastage. The Funding Agreement specified that the purpose for which Regional Partnerships funding would be used (the Activity) was: ‘upgrade the electronic controls of the boilers, upgrade the plumbing to reduce water wastage, and install a new computer system.’

4.118 In this context, the final instalment of Regional Partnerships funds should not have been paid until the ‘water saving’ Funding Agreement milestone had been met.

**Post Activity Report**

4.119 The Post Activity Report did not meet all the requirements of the Funding Agreement. Specifically, it did not include:

- a summary of performance against the project activity milestones. Each of the four milestones (upgrade boilers, rendering upgrade, water saving and install Uniworks information technology system) was to have been achieved by 30 November 2004. The Post Activity Report stated that, except for water saving works, each of the milestones had been achieved, but provided no information on the date by which that had occurred;

- an analysis of the planning, implementation and overall process followed to deliver the activity;

- any lessons learned throughout the activity; or

- any recommendations on improved practice that may assist in the delivery of future activities.
Financial acquittal

4.120 Included with the Post Activity Report received on 4 July 2005 was:

- a one page statement of receipts and expenditure for the project that reported total expenditure on the project as being $1 265 867.35 excluding GST; and

- an audit report in relation to the statement of receipts and expenditure, addressed to the members of Teys Bros (Holdings), the entity with whom the Funding Agreement was signed.\(^\text{795}\)

4.121 However, as illustrated by Table 4.2, this information did not satisfy the requirements of the Funding Agreement.

**Table 4.2**

**Compliance with information required under the Funding Agreement before the final payment should have been made**

<table>
<thead>
<tr>
<th>Audit Report Requirement</th>
<th>Clause</th>
<th>Information Obtained</th>
</tr>
</thead>
<tbody>
<tr>
<td>An audited detailed statement of receipts and expenditure in respect of Regional Partnerships funds and all other contributions.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Provided.</td>
</tr>
<tr>
<td>Definitive statement as to whether the financial accounts are complete and accurate.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not provided. Statement related to the financial information being presented fairly in accordance with DOTARS guidelines.</td>
</tr>
<tr>
<td>A statement of the balance of the bank account into which Regional Partnerships funds paid.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not provided.</td>
</tr>
<tr>
<td>An audited statement that the Regional Partnerships funding and other contributions were expended for the purposes of the Activity and in accordance with the Agreement.</td>
<td>9.2(d) and 3.4(c) of Schedule</td>
<td>No statement made that funds expended for the purposes of the Activity. The audit report was qualified in terms of retrospective funding issues.</td>
</tr>
<tr>
<td>A certificate that all Regional Partnerships funding other contributions were expended for the purpose of the Activity and in accordance with the Funding Agreement.</td>
<td>9.2(e)(i) and 3.4(c) of Schedule</td>
<td>No certificate provided.</td>
</tr>
<tr>
<td>A certificate that salaries and allowances paid to persons involved in the Activity are in accordance with any applicable award or agreement in force under any relevant law on industrial or workplace relations.</td>
<td>9.2(e)(ii) and 3.4(c) of Schedule</td>
<td>No certificate provided.</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS records.

\(^\text{795}\) ibid.
Retrospective funding

4.122 As noted in Table 4.2, the audit report expressed a qualified opinion in relation to the statement of receipts and expenditure. Specifically, the audit report stated that the expenditure had been incurred in the period 8 April 2004 to 31 May 2005 and that:

Clause 5.1 and 5.2 of the Regional Partnerships Funding Agreement in relation to funding for Lakes Creek Upgrade require that funding must be expended on the specified Activity during the Activity Period. Schedule 1 of the Agreement provides that the Activity Period commences on the date of the Agreement, being 2 September 2004, and ends on 30 November 2004. Certain monies included in the Statement of Receipts and Expenditure were expended outside the Activity Period.

4.123 As noted earlier in this case study, this information confirmed that funding had been approved in relation to this project in contravention of the Regional Partnerships Programme retrospective funding requirements. However, no action was taken by DOTARS to quantify the extent of expenditure that had been incurred prior to funding being approved and the Funding Agreement being signed.

Project outcomes

4.124 The Funding Agreement specified two outcomes for the project, as follows:

- increased employment, to be measured by payroll numbers; and
- export earnings, to be measured by ‘new markets’.

4.125 However, the Funding Agreement performance measures for these two outcomes did not specify any benchmarks and were not quantified in terms of targets.

4.126 The Post Activity Report stated that five outcomes had been achieved by the project, being:

- re-opening of a major industry in Rockhampton with the plant operational five days per week with one shift;
- as of 10 November 2004, employment of 336 full time equivalents including 40 trainees;
- within 10 months of opening it was envisaged that the plant would have 360 full time employees plus 25 to 30 trainees and, in this respect,
as of 31 May 2005 there were 523 full time equivalents including 30 trainees with an extra 150 jobs announced on 9 June 2005;

- total production during 2004–05 was $140 million during the re-opening process and the plant was on target to reach $350 million per annum; and

- 1,215 head of cattle were being processed each day with $200 million of cattle purchased annually.

4.127 Thus, information was provided against the first Regional Partnerships Funding Agreement outcome of increased employment.

4.128 The only data provided in relation the second Funding Agreement outcome of export sales was the production information concerning $140 million during 2004–05, with the plant being on target to reach $350 million per annum. However no information was provided on how much of that production related to exports and what, if any, new export markets had been achieved. This is of particular relevance given the focus placed on export markets in the Parliamentary Secretary’s documented reasons for disagreeing with the department’s concerns regarding competitive neutrality.

4.129 The 29 June 2005 correspondence providing the Post Activity Report stated that:

It is my understanding that Teys Bros will receive a written request within the next twelve months requesting information on regional benefits from the project and that the information supplied will complete the evaluation process.

4.130 DOTARS did not respond indicating that the funding recipient’s understanding was incorrect. However, DOTARS’ records of this project examined by ANAO also did not reveal that the department had taken any steps by June 2006 to obtain further information on project outcomes.

ANAO conclusion

4.131 Requirements set out in the Internal Procedures Manual for the conduct of site visits were not implemented; the payment of Regional Partnerships funding was finalised notwithstanding that Funding Agreement reporting and acquittal requirements had not been met; and insufficient data was obtained to assess whether the intended project outcomes had been achieved.
5. Beef Australia 2006

This case study examines RP01101 Beef Australia 2006 involving the Commonwealth contributing, for the second time, $2 200 000 towards the staging of a triennial beef cattle exposition in Rockhampton, Queensland. Important elements of the application, assessment and approval processes were bypassed for this project. Specifically, funding was approved prior to any documentation being provided to the department with respect to the application such that this decision was not informed by a departmental assessment against the Programme criteria. A truncated departmental assessment was subsequently undertaken in six days.

Introduction

5.1 Beef Expositions (Beef Expos) are held in Rockhampton every three years. The first event was staged in 1988, with the broad aim of showcasing to the nation achievements in Australia’s cattle industry. They are directed and managed by Beef Australia Inc (Beef Australia), a non-profit member-based incorporated association established for the purpose of directing and managing the planning and development of Beef Expos.

5.2 The sixth Beef Expo was conducted in 2003. It was staged at a cost of $4.4 million with funding of $2.2 million (excluding GST) provided by the Australian Government through the Department of Agriculture, Fisheries and Forestry (DAFF).\(^{796}\) Commonwealth funding for Beef Expo 2003 was first announced during the 2001 Federal Election campaign.\(^{797}\) DAFF advised ANAO in September 2006 that its records indicated that it did not provide funding for any earlier staging of this triennial event.

5.3 Beef Australia approached both the then Minister for Agriculture, Fisheries and Forestry and the then Minister for Transport and Regional Services for funding assistance for the 2006 exposition, to be called Beef Australia 2006. Significantly different approaches were taken to the invitations from Beef Australia to contribute funding to Beef Australia 2006 (see Figure 5.1).

\(^{796}\) DAFF advice to then Minister for Agriculture, Fisheries and Forestry, 17 March 2004.

\(^{797}\) The Howard Government, Election 2001, Stronger Regions, 18 October 2001, p. 10. This policy document is not to be confused with the Stronger Regions, A Stronger Australia statement launched on 29 August 2001 on which the Regional Partnerships Programme is based.
Figure 5.1
Application, assessment and approval processes

17 December 2003
Beef Australia writes to then Minister for Agriculture, Fisheries and Forestry seeking ongoing Commonwealth support.

8 January 2004
Minister responds advising that events such as Beef Australia should be largely self-funding but welcoming opportunity to discuss plans for 2006.

17 February 2004
Beef Australia writes to then Minister submitting formal invitation to Partner and Investment Program together with Business Plan, Budget 2004-2006 and Project Schedule.

17 March 2004
DAFF recommends that request for funding be declined on the grounds that one-off Commonwealth funding in 2003 was appropriate to launch a new direction for Beef Australia and continued, direct financial support is not in line with Government policy where it is preferred such events achieve sustainability through self-funding.

November 2003
Then Minister for Transport and Regional Services meets with Beef Australia.

13 February 2004
Beef Australia writes to then Minister submitting formal invitation to Partner and Investment Program together with Business Plan, Budget 2004-2006 and Project Schedule.

10 June 2004
Then Minister’s office advises DOTARS that the Minister had agreed to fund Beef Australia 2006, Provides 13 February correspondence and attachments to DOTARS National Office.

15 June 2004
Invitation to Partner sent by then Minister’s office received in DOTARS National Office. DOTARS provides Beef Australia with link to online application form.

18 June 2004
8 pages of the 76 page Invitation to Partner and associated documents provided by DOTARS National Office to Central Queensland ACC (CQACC).

21 June 2004
Beef Australia submits electronic Regional Partnerships application form and attachments.
Unsuccessful approach for funding through the Agriculture, Fisheries and Forestry portfolio

5.4 On 17 November 2003, Beef Australia wrote to the then Minister for Agriculture, Fisheries and Forestry:

looking to continue our close association and seek on-going support from the Commonwealth Government leading into 2006. We look forward to the opportunity to speak with you about the positive outcomes from Beef Australia 2003 and our plans for Beef Australia 2006.

5.5 The then Minister for Agriculture, Fisheries and Forestry responded on 8 January 2004. In relation to ongoing support from the Commonwealth, the Minister’s letter stated as follows:

Whilst I believe that events such as Beef Australia should be largely self-funding, I would welcome an opportunity to discuss your organisation’s plans for the 2006 exposition.

5.6 On 17 February 2004, Beef Australia wrote again to the then Minister for Agriculture, Fisheries and Forestry, submitting a formal ‘Invitation to Partner’. DAFF assessed this Invitation to Partner. It concluded that Beef Australia had a strong expectation that the Australian Government would contribute significantly to Beef Australia 2006, given:

- the Commonwealth provided $2.2 million for Beef Australia 2003;
- there is no indication in the business plan of a fall-back position should funding not be provided;
- earlier correspondence has indicated Government willingness to discuss the 2006 plans; and
- the stated impression, attributed to the Deputy Prime Minister during a recent visit to Central Queensland, that an application would receive favourable consideration.

5.7 Nevertheless, DAFF’s assessment was that providing funding for Beef Australia 2006:

- was not in accordance with the policies of the Commonwealth (see FMA Regulation 9(1)(a)) in that:

  …one-off Commonwealth funding in 2003 was appropriate to launch a new direction for Beef Australia and continued, direct financial support is not in line with Government policy where it is preferred such events achieve sustainability through self-funding.
would not make efficient and effective use of the public money (see FMA Regulation 9(1)(b)) in that:

Commonwealth support was sought for 2003 to help lift the event to a more professional and international level. The 2003 business plan objective was to move the event along a more sophisticated direction and develop a more business-like and commercial basis to achieve long-term sustainability. The Government saw value in helping the event to a higher profile. However, following the success of 2003, it would be reasonable to expect the trade benefits derived by participants would provide sufficient momentum for repeat or additional business sector sponsorship for 2006 without the need for continued Commonwealth support.

You indicated to Beef Australia in December 2003 that you believe events such as Beef Australia should be largely self-funding. Continued Commonwealth financial underpinning would not help the event achieve long-term viability. Additionally, the Department does not have programs that could support this type of funding request.

5.8 Accordingly, on 17 March 2004, DAFF recommended to the then Minister for Agriculture, Fisheries and Forestry that the request for funding be declined:

on the grounds that one-off Commonwealth funding in 2003 was appropriate to launch a new direction for Beef Australia and continued, direct financial support is not in line with Government policy where it is preferred such events achieve sustainability through self-funding.

5.9 DAFF advised ANAO on 4 October 2006 that:

The advice brief was returned to the Department in September 2004, during the caretaker period, but was not annotated or signed by the Minister or his office.

**Transport and Regional Services Portfolio Minister’s decision to approve funding through the Regional Partnerships Programme**

5.10 The first record held by DOTARS in relation to this project was a 10 June 2004 email from the Office of the then Deputy Prime Minister and Minister for Transport and Regional Services (see Figure 5.2).
5.11 On the same day, DOTARS advised the then Minister’s Office as follows:

Thks for this. Obviously I haven’t seen the documents so I’m not sure how they have structured their proposal in the context of Regional Partnerships, but given the multi year schedule for $2.2m, you will recall from our UNE discussion that the Minister will need to write to the Minister for Finance for his agreement to such a proposal. [sic]

I assume that their proposal outlines the other partners to the venture and their contributions. Is AFFA contributing as well?

5.12 This was the first and last reference by DOTARS to DAFF in relation to this project. No steps were taken by the department to seek advice from DAFF as to the purpose, scope and outcomes of Commonwealth funding provided to Beef Australia 2003, or to obtain any input DAFF could provide, from its perspective, on the evaluation of the merits of further Commonwealth funding to the beef cattle exposition.

5.13 On 15 June 2004, DOTARS received from the Minister’s Office a copy of a 13 February 2004 letter from Beef Australia to the then Minister (see Figure 5.3) submitting a formal Invitation to Partner and Investment Program together with a Business Plan, Budget 2004–006 and Project Schedule. As
noted, similar information was also provided to the then Minister for Agriculture, Fisheries and Forestry and informed DAFF’s advice that further funding should not be provided to Beef Australia.

**Figure 5.3**

**Funding request to the then Minister for Transport and Regional Services**

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I refer to your recent visit to Rosslyn Bay, Yeppoon and the meeting you had with Beef Australia 2003 Chairman, [name redacted] and our Executive Officer [name redacted] regarding funding for Beef Australia 2006. I can only apologise that business commitments prevented me from attending.

[Name redacted] and [Name redacted] have advised of the positive response they received and that you have indicated your support for a further $2.2m to deliver Australia’s national beef cattle exposition in 2006.

We accordingly submit our formal Invitation to Partner and Investment Program together with our Business Plan, Budget 2004-2006 and Project Schedule.

As you will appreciate to stage an event of this scope and magnitude requires significant lead time. The Investment Program is aimed at securing the funds required to progress the event according to the project schedule and meet any financial commitments that fall due.

The Investment Program involves a series of payments over time in the lead up to the staging of the Event. The preferred Investment Schedule for your Foundation Partnership is as follows:

<table>
<thead>
<tr>
<th>Month</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 2004</td>
<td>$500,000</td>
</tr>
<tr>
<td>February 2005</td>
<td>$500,000</td>
</tr>
<tr>
<td>August 2005</td>
<td>$750,000</td>
</tr>
<tr>
<td>January 2006</td>
<td>$250,000</td>
</tr>
<tr>
<td>May 2006</td>
<td>$200,000</td>
</tr>
</tbody>
</table>

The payment points will be intergrated into the marketing strategy to maximise opportunities to promote the Federal Government’s support of the event.

We thank you for your continued support and commitment to the success of Australia’s national beef cattle expositions.
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Source: Correspondence from Beef Australia Inc. to the then Minister for Transport and Regional Services, dated 13 February 2004, as held in DOTARS records.

5.14 The records held by DOTARS National Office and the North Queensland Regional Office in relation to this project did not include any
record of copies of the 13 February 2004 correspondence and attachments having been received by the department prior to 15 June 2004. In this respect:

- DOTARS directed Beef Australia to the on-line application form for Regional Partnerships grants on the department’s website on 15 June 2004, with a completed application being received electronically on 21 June 2004. This was the same day on which the department submitted its completed assessment of the project to the then Parliamentary Secretary, who endorsed the then Minister’s earlier (10 June 2004) funding decision on 22 June 2004;

- it was not until 24 June 2004 that a request to create a departmental file for this project was submitted; 798 and

- the project was approved prior to a Regional Partnerships project number being assigned. Applications for funding are assigned a Regional Partnerships identifier upon being submitted in DOTARS’ database, TRAX. On 30 June 2004, the project was assigned the identifier RP01101.

5.15 In November 2007, Beef Australia advised ANAO of its perspective of the funding approval process, as follows:

Beef Australia is an apolitical organisation with strong bi-partisan support for the Expo reflective of beef industry recognition at all levels of government. Our approaches to Governments and the business sector via deputations and in writing—Federal, State and Local—for funding support is part of our core operations. For the 2006 Beef Expo our fundraising programme coincided with the 2004 Federal election process 799 and similarly for Beef Expo 2009.

It is our practice to approach both the Government and Opposition with an Invitation to Partner. Beef Australia did meet with both the Minister for Transport and Regional Services and the Minister for Agriculture, Fisheries and Forestry in 2003-2004 in relation to our Invitation to Partner document. In 2004 following deputations and documentation, Government made the decision that if re-elected it would continue to be a Beef Expo partner. 800

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798 Specifically, on 24 June 2004, DOTARS National Office requested that a file be created with the title ‘Regional Partnerships: SONA Project – Beef Australia 2006’.

799 As noted, funding was approved in June 2004 prior to the calling of the 2004 Federal election on 31 August 2004 and the commencement of the Caretaker period.

800 Figure 5.2 and Error! Reference source not found. document the terms of funding approval, which did not state that funding was conditional on the Government being re-elected.
While it was clear that the Ministers supported Beef Australia and its aims, it was also clear that any funding we might receive was subject to review and approval through the relevant departmental channels. We were advised that the funding source would be the Regional Partnerships Programme and that we were to submit an application.

Beef Australia Ltd has no knowledge of the internal workings between the Area Consultative Committees (ACC) and the department in relation to funding of projects. Our knowledge is confined to the Central Queensland ACC servicing the many communities, local governments and industries from the Northern Territory, Queensland border to the Capricornia Coast. It is reported in terms of regional achievements and results, CQACC is a leading ACC in Australia.

At no time has Beef Australia been the subject of any political controversy and pride ourselves on bipartisanship.

**ANAO conclusion**

5.16 The Commonwealth contributed $2,200,000 to Beef Expo 2003 through administered funds appropriated to DAFF. That funding was intended to assist in launching a new direction for the triennial expositions staged by Beef Australia. In assessing whether Commonwealth funding should be provided to Beef Australia 2006, DAFF concluded that continued, direct financial support was not in line with Government policy where it is preferred such events achieve sustainability through self-funding.

5.17 Funding of $2,200,000 (excluding GST) was approved by the then Minister for Transport and Regional Services on 10 June 2004 for Beef Australia 2006 through the Regional Partnerships Programme. This approval was given prior to DOTARS receiving information that would enable it to assess the project against the assessment criteria relating to outcomes, partnerships and support, and applicant and project viability set out in the Regional Partnerships Programme Guidelines.

**Assessment against the Programme Guidelines**

**Regional Office not involved in assessment**

5.18 Until March 2006, the normal process under the Regional Partnerships Programme was for applications to be referred to the relevant Regional Office for assessment against the Programme Guidelines. The Internal Procedures Manual in place at the time the Beef Australia 2006 project was assessed stated that the Regional Offices were to:
Prepare thorough and objective analyses of applications ensuring that assessments provide sufficient and relevant information as required against programme criteria.\textsuperscript{801}

5.19 When complete, the Regional Office’s assessment and Regional Manager’s recommendation would then be allocated to National Office for quality assurance, before being submitted to the Ministerial decision maker.

5.20 This process was not followed in respect of the Beef Australia 2006 project. There is no evidence of Regional Office involvement until 8 July 2004, when National Office forwarded the relevant file to the North Queensland Regional Office, advising:

I am sending you, under cover of this minute, the file on the Beef Australia 2006 project, which was approved by the Parliamentary Secretary, Mrs Kelly on 30 June.\textsuperscript{802} In line with normal practice, this project is now best managed by the Townsville Regional Office.

**Assessment timing and criteria**

5.21 DOTARS’ records state that, at a meeting on 16 June 2004, the then Parliamentary Secretary had asked the department to put forward 100 projects for her consideration by close of business Friday 25 June 2004.

5.22 The assessment of the Beef Australia 2006 funding request was completed by National Office within six days of receiving the Invitation to Partner documentation from the then Minister’s Office on 15 June 2004 and, as noted, was completed on the same day that the department received a completed Regional Partnerships application. There was no documented evidence of any analysis of the project against the Programme criteria. There was also no documented interchange with Beef Australia questioning or clarifying any aspects of the project or the funding request. Such interactions occurred with most applications included in the audit sample.

5.23 The assessment of the Beef Australia 2006 project was provided to the then Parliamentary Secretary on 21 June 2004 as the third batch of the 100 projects the department was aiming to deliver to the then Parliamentary Secretary by 25 June 2004. It was included as part of a package of 13 projects.


\textsuperscript{802} This date is incorrect. The then Parliamentary Secretary to the Minister for Transport and Regional Services endorsed the departmental assessment on 22 June 2004. As discussed, the substantive approval of the funding had been given by the then Minister for Transport and Regional Services on or before 10 June 2004.
Of these, 11 (including Beef Australia 2006) were recommended for funding and two were assessed as not meeting the Regional Partnerships Guidelines.

5.24 The file created for this project on 24 June 2004 had been titled ‘SONA Project Beef Australia 2006’, indicating that, at least initially, the department had understood this project was being progressed outside of the published Programme Guidelines. However, the assessment submitted to the then Parliamentary Secretary by National Office assessed the project against the published assessment criteria and did not make any reference to the SONA procedures. National Office assessed that the project met the Regional Partnerships Programme Guidelines.

Outcomes assessment

5.25 The assessment against the Outcomes criterion summarised the aims of the project as set out in the Invitation to Partner sent to the then Minister by Beef Australia in February 2004. However, no quantification was included concerning these outcomes.

5.26 The assessment also did not identify which of the Regional Partnerships Programme outcomes the project would contribute to. In addition, there was also no comparative analysis of why further Commonwealth funding was warranted, having regard for the outcomes that were expected to have been achieved by funding Beef Expo 2003.

5.27 Table 5.1 compares planned outcomes and associated performance measures included in the Deed of Grant between DAFF and Beef Australia for the funding of Beef Expo 2003 with the equivalent planned outcomes identified by Beef Australia in its Invitation to Partner document for Beef Australia 2006, received by DOTARS from the then Minister’s Office on 15 June 2004.

5.28 As indicated by Table 5.1, a comparison of planned outcomes raises significant issues that DOTARS would need to have resolved in order for it to be satisfied that a further Commonwealth contribution was going to provide additional outcomes that had not already been substantively funded through the contribution to the 2003 exhibition. In this respect, in July 2007 DOTARS advised ANAO that:

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803 The Programme Guidelines current at the time of this assessment (31 May 2004 version) stated that, through Regional Partnerships, the Australian Government would partner projects that focussed on: strengthening growth and opportunities; improving access to services; supporting planning or assisting structural adjustment for communities. The normal process is for the department’s assessment of an application against the Outcomes criterion to state which of those Programme objectives the project would contribute to, and how this would be achieved.
The department notes that the reduced targets on some of the outcomes for Beef Australia 2006 were more realistic goals based on the actual results of the 2003 Expo – not on what had been set in advance in 2002. There were also six new measures introduced for 2006.

For example, the 2003 results showed overall attendance of 52,000, which included some 300 international visitors from 23 countries. Hence, the goal of 60,000 attendance and 600 international visitors for the 2006 Expo represented a realistic increase on 2003 performances.

5.29 However, this analysis was not undertaken by DOTARS as part of its project assessment. In addition, the necessary data to undertake this sort of comparison was not obtained by DOTARS from DAFF or Beef Australia.

### Table 5.1

**Comparison of planned outcomes**

<table>
<thead>
<tr>
<th>Beef Australia 2006</th>
<th>Beef Expo 2003</th>
<th>Analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase visitations to 60,000 (an increase of 9 per cent).</td>
<td>Increase visitations from 44,000 to 55,000 (a 25 per cent increase)</td>
<td>Reduced targeted increase. Beef Australia advised ANAO that visitation is limited by the amount of available accommodation.</td>
</tr>
<tr>
<td>25,000 ticketed entries to Showground activities</td>
<td>No equivalent.</td>
<td></td>
</tr>
<tr>
<td>Over 15 per cent interstate visitors.</td>
<td>20 per cent of visitations to be from outside Queensland.</td>
<td>A reduced target from that for Beef Expo 2003. Beef Australia advised ANAO that experience from 2003 showed the earlier target was unrealistic given the limited accommodation pool.</td>
</tr>
<tr>
<td>RTAM rating of 100 per cent for Fitzroy, Livingstone, Rockhampton areas for minimum five days of the event.</td>
<td>No equivalent.</td>
<td>Beef Australia advised ANAO that the target was achieved.</td>
</tr>
<tr>
<td>Secure minimum $700,000 in private sector sponsorship.</td>
<td>Sponsorship $700,000 cash and $700,000 value in-kind.</td>
<td>Same cash target as 2003, no in-kind target. No plan for increase in level of private sector sponsorship. Beef Australia advised ANAO it had a substantial increase in sponsorship between 2000 and 2003 and it was at the upper level of its likely support from private sector sponsors. ANAO was further advised that in-kind private sector sponsorship substantially increased</td>
</tr>
</tbody>
</table>
### Beef Australia 2006 | Beef Expo 2003 | Analysis
--- | --- | ---
Double international participation in the event for Beef Australia 2003 to 600 registered delegates. | Attract 3 000 international delegates from over 30 countries. | A significantly reduced target from that for 2003.
Over 85 per cent of patrons respond in market research that 2006 was best Expo to date. | No equivalent | Beef Australia advised ANAO that this measure has been found to not be a very reliable indicator of the event’s ‘true success’.
Over 2 000 participants in Conference Seminar and Education Activities over the course of the week. | No equivalent | Beef Australia advised ANAO that the target was achieved.
Over 1 800 stud cattle on display at the Rockhampton Showgrounds. | No equivalent | Beef Australia advised ANAO that the target was achieved.
Over 1 800 commercial beef cattle on display. | No equivalent | Beef Australia advised ANAO that the target was achieved.
Over 330 Trade Exhibitors. | Increase trade fair exhibitors to 900. | Reduced target from 2003. Beef Australia advised ANAO that, due to lack of space at the showground and the high infrastructure costs associated with installing significant extra tented and air conditioned space for exhibitors, it was more profitable and preferable to have less than 500 trade fair exhibitors at Beef Australia 2006.

Source: ANAO analysis of the Deed of Grant between DAFF and Beef Australia for funding Beef Expo 2003, Beef Australia’s Invitation to Partner document for Beef Australia 2006 provided to DOTARS by the Office of the then Minister for Transport and Regional Services in June 2004 and advice provided to ANAO by Beef Australia in November 2007.

#### 5.30

In respect to the value for money obtained from the Regional Partnerships funding provided towards the costs of Beef Australia 2006, in November 2007 Beef Australia advised ANAO that:

The Australian Government’s investment of $2.2 million in the 2006 Beef Exposition clearly benefits the Australian economy in [a] number of direct and indirect ways. The Queensland State Government’s commissioned study of the economic impact of Beef Australia 2006 showed spending of over $20 million across the state directly attributable to the Exposition. This figure includes spending by the event organiser and patrons to the event through travel, accommodation and discretionary spending at the Expo itself.
In addition to the event impact spending benefits, trade outcomes arising from Beef [Australia] 2006 in excess of $50 million have been reported by international export trade partners including the Queensland Department of Primary Industries and the Queensland Livestock Exporter’s Association. Many of the 625 international visitors from 26 countries who attended the event are current or potential trading partners for Australian beef cattle products and services including everything from genetics, embryos and live cattle to boxed beef, cattle panels, breeding technology and cattle management software.

Australian Bureau of Statistics figures show that since 1983-84, Australian beef exports have grown from $2 billion to $4.9 billion in 2006. We believe our Exposition has played a major role since 1988 in encouraging innovative and responsible agricultural and husbandry practices through the hundreds of property tours and seminars staged over seven Beef Expos to literally tens of thousands of industry participants.

Our industry Education programme over the past seven Expositions has focused on skilling up a generation of cattle producers and breeders in a number of vital areas...

The Beef Australia Expos unquestionably deliver clear direct and indirect benefits to both the Beef industry and the wider community and will continue to do so in future.

**Partnerships assessment**

5.31 The National Office assessment stated that there were three project partners, as follows:

- the Commonwealth—$2 200 000;
- Beef Australia (the applicant)—$2 600 000; and
- the Queensland State Government—$1 000 000.

5.32 The department’s advice to the then Parliamentary Secretary was materially inaccurate. Specifically, the project budget provided by Beef Australia did not include an applicant contribution of $2 600 000 as had been advised to the then Parliamentary Secretary by DOTARS. Instead, there were 31 project partners, including the Rockhampton City Council, from whom cash contributions totalling $900 000 would be sought. This is illustrated by Table 5.2, which is based on the Budget attached as Appendix B to the Invitation to Partner document.
Table 5.2
Budgeted partner contributions

<table>
<thead>
<tr>
<th>Partner</th>
<th>Amount (GST inclusive)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sponsorship:</strong></td>
<td></td>
</tr>
<tr>
<td>Australian Government</td>
<td>$2 200 000</td>
</tr>
<tr>
<td>State Government</td>
<td>$1 000 000</td>
</tr>
<tr>
<td>Local Government</td>
<td>$200 000</td>
</tr>
<tr>
<td>Private Sector</td>
<td>$700 000</td>
</tr>
<tr>
<td><strong>Sub-total:</strong></td>
<td>$4 100 000</td>
</tr>
<tr>
<td><strong>Exposition revenue:</strong></td>
<td></td>
</tr>
<tr>
<td>Trade Fair</td>
<td>$486 000</td>
</tr>
<tr>
<td>Cattle Activities</td>
<td>$145 000</td>
</tr>
<tr>
<td>Industry Knowledge (Conference, seminars etc)</td>
<td>$127 000</td>
</tr>
<tr>
<td>Social Activities</td>
<td>$173 750</td>
</tr>
<tr>
<td>Operations Revenue</td>
<td>$230 000</td>
</tr>
<tr>
<td>Membership Fees</td>
<td>$45 000</td>
</tr>
<tr>
<td>Interest</td>
<td>$25 000</td>
</tr>
<tr>
<td>Other</td>
<td>$530 000</td>
</tr>
<tr>
<td><strong>Sub-total:</strong></td>
<td>$1 761 750</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$5 861 750</strong></td>
</tr>
</tbody>
</table>


5.33 As is also illustrated by Table 5.2, a significant component of the budget for staging the event used in DOTARS’ assessment was to be funded from revenue generated through the event itself. DOTARS undertook no assessment of the effect on the project’s viability from the inherent risk that realised revenue may fall short of the estimates included in the budget. In November 2007, Beef Australia advised ANAO that:

While in a general sense it is correct to assume that Beef Australia can neither confirm or guarantee its revenue for a project two years in advance, it should be noted that the organisation does have a fair indication of the potential project revenue based on running seven previous events of this kind. The anticipated project revenue by Beef Australia and its non public sector partners was in fact higher than the submission estimate when budget relieving value in kind contributions are factored in. Clearly this shows that...
our estimates were submitted in good faith and based on a degree of considered experience.

When the application was submitted Beef Australia had been in existence for over fifteen years, having viably run six National Beef Expositions with a combined economic impact likely to be over $80 million.

Applicant contribution was speculative and should not have been included

5.34 Contrary to the advice included in the department’s assessment of the project provided to the then Parliamentary Secretary, the applicant was actually contributing no cash to the project, apart from $1 761 750 in estimated income to be derived through the exposition itself. There were a number of other projects examined by ANAO where the project assessment excluded such amounts as a partnership contribution on the grounds that estimated revenue is speculative in nature and therefore is not considered by DOTARS to be a genuine partnership contribution.

5.35 In July 2007, DOTARS advised ANAO that the revised Regional Partnerships Guidelines issued in July 2006 clarify that expected income is not to be considered a partnership contribution (because of its speculative nature).

Unrecognised partners

5.36 The remaining $900 000 attributed in the National Office assessment to a Beef Australia applicant contribution was actually to involve:

- local government—$200 000; and
- private sector sponsorships—$700 000.

5.37 Apart from noting in the assessment that the Queensland State Government contribution had yet to be confirmed, National Office’s assessment provided no advice on whether contributions from local government and private sector sponsors had been applied for, committed and/or received. This was notwithstanding that the electronic Regional Partnerships application submitted by Beef Australia on 21 June 2004 included this information in relation to the Rockhampton City Council contribution of $200 000 (the status of which was reported as application submitted) and amounts from 30 other partners totalling $700 000. Of this total amount:

- $570 000 was said to be in negotiation;
- $30 000 was said to be committed but yet to be received; and
- the status of the remaining $100 000 was not advised (and National Office did not seek further information on this issue).
5.38 The Business Plan also outlined that, at the time the Invitation to Partner document was provided to the then Minister in February 2004, none of the funding sources had been confirmed. The Business Plan advised that it was ‘envisaged’ that 75 percent of sponsors would be sponsors of previous beef expositions, and that sponsorship development and servicing would be undertaken in house directly by Beef Australia. Nor was the Queensland government funding confirmed. Despite the uncertainty attaching to all other funding contributions, DOTARS did not recommend that any approved funding be subject to all co-funding being confirmed, as is the usual approach taken in such circumstances.

5.39 With respect to the nominated $1 000 000 State Government contribution, there was a heightened risk that this contribution may not be forthcoming. This was recognised in DAFF’s 17 March 2004 advice to its then Minister that:

The level of Commonwealth funding for the 2003 event was agreed to on the understanding that the Queensland Government would match the Commonwealth contribution, with the remaining third coming from the private sector. In reality, the Commonwealth provided 50% of the cash flow. The State Government’s view was that it was not obliged to provide the full matching amount of its funding commitment because it had already provided $4 million to upgrade the Rockhampton Showground as the primary venue. The State Government has pledged another $3 million for on-going Showground development, thus creating a similar funding environment to 2003 and increasing the potential for the Commonwealth to again carry a significant proportion of the cash flow.

5.40 The risk foreshadowed by DAFF in its 17 March 2004 advice to the then Minister for Agriculture, Fisheries and Forestry was realised. Specifically, on 3 October 2005 (over 15 months after the Regional Partnerships funding of $2.2 million was approved, of which $1 million had been paid), the Queensland Premier and Treasurer announced that the State Government had committed $505 000 in cash and in-kind sponsorship to support Beef Australia 2006. This was to be provided through Queensland Events Corporation which would provide cash and also offer professional event advice.804

5.41 The announced State Government contribution of $505 000 in cash and in-kind support represented a considerable shortfall on the budgeted cash contribution of $1 000 000. It meant that more than eight per cent of the

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804 The Hon Peter Beattie, Premier and Treasurer, Premier Commits to $505 000 to Reaffirm Rocky is Beef Capital, Monday October 3, 2005.
budgeted income for staging the event would need to be obtained from another source, or the budget revised.

In-kind contributions not identified and assessed

5.42 The Invitation to Partner document provided to the then Minister in February 2004, and received by the department from the then Minister’s Office on 15 June 2004, did not identify any in-kind contributions to the proposed event budget. The National Office assessment, signed on 21 June 2004, stated that there were no in-kind contributions to the project. However, the electronic Regional Partnerships application, requested from Beef Australia by DOTARS on 15 June 2004 and received on 21 June 2004, identified in-kind contributions from 17 entities, which Beef Australia had valued at $1 286 900 in total. This information was not reflected by DOTARS in its abridged assessment.

5.43 In respect to in-kind contributions, in November 2007, Beef Australia advised ANAO that:

Beef Australia has a significant number of in kind contributions, the nature of which are often unconfirmed until after significant negotiation with private and public sector sponsors in the lead up to the event. Value in kind can also include a variety of contributions from budget relieving payment of equipment and services needed by Beef Australia to the provision of significantly discounted advertising from our media partners.

Value in kind contributions for Beef Australia 2006 was higher than expected, meaning that partner contributions from this key revenue source were above those stated in the application process.

No interaction with Agriculture Department

5.44 The Internal Procedures Manual in place at the time the Beef Australia 2006 assessment was undertaken by National Office stated that project assessments were to include:

whole of government consultations with other Commonwealth and State agencies to ensure non-duplication of other programmes and to encourage partnerships.805

5.45 However, despite the Commonwealth contribution to the cost of staging the 2003 event having been highlighted in the Invitation to Partner document, DOTARS undertook no such consultations with DAFF.

805 op. cit., p. 46.
Local Support not assessed

5.46 The assessment against this criterion also did not address support for the project, noting that no letters of support were attached to the Invitation to Partner and the Regional Office was not involved in the project assessment, although (as noted below) the ACC had some involvement.

Applicant viability

5.47 A concern identified by DAFF in its assessment of the invitation from Beef Australia to the then Minister for Agriculture, Fisheries and Forestry for the Commonwealth to contribute funding to Beef Australia 2006 was that:

…the SWOT analysis in the business plan does not identify an alternative major supplier or the impact on Beef Australia’s ability to deliver the event should any tier of government funding (totalling over $3.4 million) fail to eventuate.

5.48 This issue was not addressed by DOTARS National Office in its project assessment. There was also no documented analysis of the applicant’s financial performance and position or of the proposed budget for Beef Australia 2006. No consideration was documented of the merits of undertaking an external Financial Viability Assessment in relation to Beef Australia and/or Beef Australia 2006. This was notwithstanding the July 2003 Internal Procedures Manual requiring such an assessment to be commissioned.

Project viability

5.49 The July 2003 Internal Procedures Manual also stated that assessments against the project viability criterion should obtain evidence that the project outcomes are sustainable beyond the funding period, and that the project has been appropriately costed. Neither issue was addressed by National Office in its assessment of the Beef Australia 2006 project.

5.50 The electronic application received by DOTARS on 21 June 2004 stated in respect to how the project and its outcomes would be self-sustaining at the end of Regional Partnerships funding that:

Beef Australia is self-sustaining in two key ways:

The benefits in terms of direct and indirect economic impact and trade generated through the event will once again provide a return for investment to the people of Central Queensland and the Beef Industry through the staging of

\[806\] ibid., p. 66.
the event. The outcomes will also be met by the staging of the event in May 2006.

The funding provided for the 2006 Exposition will also assist in attracting greater support from other key event partners from the private and public sectors. Their support as well as the development of Beef Australia generated income streams will provide long term sustainability for the event.

5.51 DOTARS’ assessment did not address either the funding provided to the previous exposition by DAFF, or the appropriateness of DOTARS now funding a further exposition. In particular, there was no evidence of any inquiries being undertaken in respect to whether the project had demonstrated sufficient on-going sustainability arising from the earlier funding of $2 200 000 to indicate that there was value for money in providing a further $2 200 000 to stage the 2006 event. In this respect, as a consequence of not discussing the funding of the 2003 event with DAFF, DOTARS was unaware that DAFF’s view was that it would be reasonable to expect the 2006 event to be self-sustaining without the need for continued Commonwealth support, as it had advised the then Minister for Agriculture, Fisheries and Forestry on 17 March 2004 (see paragraph 5.7).

5.52 Instead of examining these issues, the National Office assessment stated that:

Beef Australia Inc will have sufficient funds on hand (including Regional Partnerships funding) to stage the exhibition plus retain sufficient funds to cover its ongoing budget requirements as it prepares successor events.

5.53 However, in forming this conclusion, no reference was made to the unconfirmed nature of the Queensland Government and industry contributions, or the reliance upon revenue projected to be generated through the event itself.

Central Queensland ACC recommendation

5.54 The July 2003 version of the Internal Procedures Manual, current at the time the Beef Australia 2006 project was approved, stated that:

After applicants have submitted applications, ACCs will be advised (via e-mail) of receipt of the application. This advice will also include the applicant’s name and reference number and a copy of the application.

ACCs will then review applications against the ACC comment template and against their regional priorities as set out in their Strategic Regional Plan. The template provides space for ACCs to advise the Department on the following:
whether or not further development of the application is required;
whether or not there are any regional issues that the ACC considers will impact (positively or negatively) on the proposal;
whether, in the ACC’s view, the project is consistent with the criteria for the programme, as outlined in the programme Guidelines. i.e.:
  - Outcomes;
  - Partnerships and support; and
  - Project and applicant viability; and
whether the project is likely to result in an unfair competitive advantage.\(^{807}\)

5.55 The Internal Procedures Manual further stated that, for those projects that were developed in consultation with the ACC, comments should be sent to the department within ten working days, but that ACCs would not be required to meet this timeframe for projects they have not been consulted on.\(^{808}\)

5.56 As was outlined in Figure 5.1, the Central Queensland ACC (CQACC) did not receive any documentation in relation to this project until 18 June 2004. DOTARS’ project assessment was provided to the then Parliamentary Secretary three days later, on 21 June 2004 (and approved on 22 June 2004). In that assessment, DOTARS advised as follows in relation to the CQACC’s recommendation:

Although the Central Queensland ACC did not forward the application, the Chair has advised that the ACC strongly supports this project and this will be confirmed in writing in the near future.

5.57 Figure 5.4 is a 13 July 2004 letter from the Chair of the CQACC confirming the support of the ACC. Among other things, it states that the CQACC carefully assessed a Beef Australia 2006 Regional Partnerships application. However, the only records the CQACC was able to provide to ANAO relating to this project were:

- a copy of the 18 June 2004 fax from DOTARS providing copies of eight of the 76 pages from the Invitation to Partner document and attachments;

\(^{807}\) op. cit., p. 34.

\(^{808}\) ibid., pp. 34–35.
a copy of the Regional Partnerships application form electronically submitted by Beef Australia on 21 June 2004 (the same day that DOTARS recommended funding be approved, including advising that the ACC strongly supported the project); and

• an unsigned copy of the letter of support from the CQACC received by DOTARS on 13 July 2004 (see Figure 5.4 for an image of the signed version of this letter held in DOTARS’ records).

Figure 5.4
Central Queensland ACC Letter of Support

Re: Beef Australia 2006

The Central Queensland Area Consultative Committee (CQACC) have carefully assessed the Beef Australia 2006 Regional Partnership application and believe such an event will contribute significantly not only to the Beef Cattle Industry within the Central Queensland region but most importantly to the Industry nationally.

As noted within the application, the beef industry in Australia continues to be at the forefront of sustainable regional development and an event such as that described will provide enormous opportunity to grow the industry by exposing it to the diverse international market.

The CQACC has a clearly defined role in encouraging and supporting initiatives which stimulate the regional economy and as an active Committee we recognise the enormous benefits of the event and therefore fully support the Beef Australia 2006 Regional Partnership application.

Source: Correspondence from the Chair of the CQACC to DOTARS dated 13 July 2004.

ANAO conclusion

5.58 The departmental assessment of the Beef Australia 2006 project was prepared by National Office with no input from the North Queensland Regional Office. This was notwithstanding the role that Regional Offices were expected to play in project assessments, in accordance with the Internal Procedures Manual.

5.59 The National Office assessment of the project did not include rigorous and objective analyses against the assessment criteria set out in the Programme
Management of the Funding Agreement

5.60 The Funding Agreement was signed by Beef Australia on 7 October 2004 and by DOTARS National Office on 15 October 2004.

Partnerships

5.61 On 17 March 2004, DAFF advised the then Minister for Agriculture, Fisheries and Forestry that Commonwealth funding of $2 200 000 (excluding GST) to Beef Australia 2003 was agreed to on the understanding that the Queensland Government would match the Commonwealth contribution, with the private sector providing the remaining one-third. The budget attached to the Invitation to Partner for Beef Australia 2006 included comparative figures for Beef Expo 2003. This showed that the total revenue for the 2003 event of $4 460 422 was not evenly contributed as had been envisaged when Commonwealth funding was agreed to, as follows:

- the Commonwealth contributed $2 200 200 (49 per cent);
- the State Government contributed $250 000 (six per cent), representing one-quarter of the contribution expected from that level of government;
- local Government contributed $150 000 (three per cent);
- private sector sponsors contributed $665 075 (15 per cent); and
- event revenues contributed the remaining $1 195 147 (27 per cent).

5.62 The 12 April 2002 Deed of Grant for Commonwealth funding through DAFF to assist in staging Beef Expo 2003 did not specify the contributions to be made by partners other than the Commonwealth. In this context, it was important that, in managing the Commonwealth contribution to the 2006 exposition, DOTARS effectively manage the risk of the State Government (and other partners) not making the budgeted financial contribution.

5.63 Clause 2.2 of the Schedule to the Regional Partnerships Funding Agreement stated that:

The Budget for the Project, identifying Regional Partnerships and Applicant/Funding partner contributions, is at Annexure A. You must provide satisfactory written evidence of the other contributions in accordance with Clause 6 of the Funding Agreement.
5.64 Clause 6 of the Funding Agreement, which is a standard clause in the Standardised Long Form Funding Agreement used for Regional Partnerships grants, placed a positive obligation on Beef Australia to confirm partner contributions.

5.65 However, the Schedule to the Funding Agreement was drafted in a manner that negated Clause 6 of the Funding Agreement. Specifically, the Schedule did not identify each partner and the amount of cash they were to contribute. Instead, based on the project budget included in the electronic version of the Regional Partnerships application, the Schedule identified the partners that were to contribute to each item of the budget, and the total amount only of each budget item. This is illustrated by Figure 5.5. Accordingly, clause 6 of the Funding Agreement and clause 2 of the Schedule to the Agreement were rendered ineffective as risk management provisions.

**Figure 5.5**

**Funding Agreement Budget**

<table>
<thead>
<tr>
<th>Applicant/Other Funding Partner Cash Contributions</th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Beef Australia, Qld Events, Primac Elders, Rockhampton Shopping Fair Wages, salary and superannuation</td>
<td>$638,000</td>
</tr>
<tr>
<td>Individuals and Small Business – Labour on-costs</td>
<td>$44,000</td>
</tr>
<tr>
<td>Moreton Hire, Qld Events, Rockhampton City Council, Meat and Livestock Aust., Coca Cola, Castlemaine Perkins, Primac Elders – Consultants/Contractors</td>
<td>$448,000</td>
</tr>
<tr>
<td>Meat and Livestock Australia – Travel</td>
<td>$65,000</td>
</tr>
<tr>
<td>Rockhampton City Council, Meat and Livestock Aust., Qld Events, Suncorp Metway – Equipment Hire/Lease</td>
<td>$757,000</td>
</tr>
<tr>
<td>Rabobank – Other Costs</td>
<td>$1,215,500</td>
</tr>
<tr>
<td><strong>Sub Total - Applicant/Other Funding Partner Cash Contribution</strong></td>
<td><strong>$3,661,750</strong></td>
</tr>
</tbody>
</table>

Source: Regional Partnerships Funding Agreement with Beef Australia, 15 October 2004.

**Progress reports and instalment payments**

5.66 The Funding Agreement required Beef Australia to submit four Progress Reports and a Post Activity Report. Each of the reports required under clause 3.1 of the Schedule to the Agreement were due after the proposed payment date for the associated payment identified in clause 2.4 of the Schedule to the Funding Agreement. As a consequence, the terms of the Agreement did not require the proponent to provide a statement of Activity
expenditure, including a summary of expenditure of cash contributions from the proponent and other funding partners, prior to receiving the second and subsequent payments.

5.67 The Funding Agreement provided for the Regional Partnerships funds of $2.2 million to be paid in five instalments, in the same amounts as those sought by Beef Australia in the ‘preferred Investment Schedule’ included in its 13 February 2004 letter to the then Minister for Transport and Regional Services (see Figure 5.3). The proposed payment due dates for the Regional Partnerships instalments were also consistent with the payment timings requested by Beef Australia on 13 February 2004. This is consistent with DOTARS relying upon the Invitation to Partner document to frame the payment schedule, rather than on analysis of Beef Australia’s actual payment needs, based on projected expenditure profiles.809

5.68 DOTARS did not seek advice from DAFF on the payments made for Beef Expo 2003 so as to assess the likely expenditure profile for the funds being contributed through Regional Partnerships. In this respect, the payment timing requested by Beef Australia was well ahead of the expected timing of the major expenditure on the event810 so as to enable Beef Australia to earn interest to help meet the costs of the event (in its project budget, Beef Australia included $25 000 in expected interest revenue).

5.69 Figure 5.6 demonstrates the actual timing of expenditure on Beef Australia 2006 as reported to DOTARS by Beef Australia in its project acquittal. It demonstrates that payments of Regional Partnerships funds were made significantly in advance of exposition cash flow requirements. There were also no steps taken to link payment of Regional Partnerships funds to receipt of contributions from other partners, including revenue from the event. As a result of the financial acquittal not identifying the amounts and dates of all contributions from the applicant (through exhibition revenue) and other partners, it was not possible to include in Figure 5.6 all project revenue, and the date on which it was received.

809 In this respect, in providing the file to the Regional Office in July 2004 (as discussed at paragraph 5.20), National Office advised: ‘You will need to finalise a Funding Agreement with Beef Australia Inc, but since Beef Australia do not want the first payment ($500 000) till this coming October (p.13 of the ‘Invitation to Partner’), there are no immediate deadlines that have to be met.’

810 On 24 August 2005, Beef Australia advised DOTARS that the major expenditure for the event would occur in November/December 2005. However, Beef Australia had requested, and received, $1 million in Regional Partnerships funds by March 2005.
In respect to the scheduling of Regional Partnerships payments, in November 2007 Beef Australia advised ANAO that:

The Investment Schedule submitted in the Invitation to Partner was adopted by Beef Australia Ltd and DOTARS. In an event such as Beef Australia there is a clear need to make forward commitments to contractors particularly with regard to infrastructure, contractor and venue costs. Without surety of funding, Beef Australia Ltd cannot in good faith enter into agreements with suppliers who put aside equipment and resources specifically for our event.

Correspondence between the parties clearly shows an understanding between Beef Australia/DOTARS that some funds were committed and still to be paid. It was our understanding that this arrangement was acceptable given that we received no advice to the contrary from DOTARS. All funds provided by DOTARS have been subject to the independent audit procedures as set out in the Agreement.  

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811 Table 5.3 outlines ANAO analysis of compliance with the audit requirements of the Funding Agreement.
First progress report

5.71 The first progress report was due on 15 October 2004, the same day that DOTARS National Office signed the Funding Agreement. It was to cover the outcomes relating to the launch of Beef Australia 2006 and formal announcements to partner.

5.72 A contract variation signed by Beef Australia on 1 February 2006 and DOTARS National Office on 9 March 2006 stated that the first progress report had been received. However, in July 2007, DOTARS advised ANAO that:

The first progress report was received from Beef Australia on 14 March 2005, noting that the official launch occurred on 2 December 2004. Previous correspondence had been received from Beef Australia notifying the department of the delay with the launch proceeding.

5.73 Further, this progress report had been provided to DOTARS after the department had contacted Beef Australia on 14 January 2005 reminding it that a progress report was due on 15 February 2005. The Funding Agreement specified that the second progress report was due on 15 February 2005. Accordingly, it is evident that the department did not obtain the first progress report for this project.

First instalment payment

5.74 The Funding Agreement provided that the first payment (of $500,000 plus GST – 23 per cent of the grant amount) was not to be made until:

- the Funding Agreement had been executed;
- a properly rendered tax invoice was received; and
- evidence of the launch of Beef Australia 2006 was received in the form of written advice or publications.

5.75 The first condition was satisfied on 15 October 2004 and a tax invoice dated 20 October 2004 was received by DOTARS on 25 October 2004. Payment of the first instalment was processed on 25 October 2004, notwithstanding that the third precondition was not met until 2 December 2004. This was the date on which the official launch of Beef Australia 2006 occurred in Rockhampton.

Second progress report and second instalment payment

5.76 The second and subsequent payments were not to be made until:
• an acquittal showing that previous payments had been fully expended, or there is evidence that the previous payments will be fully expended in the near future, was accepted by DOTARS;
• all progress reports due on or before payments are requested was accepted by DOTARS; and
• a properly rendered tax invoice was received by DOTARS.

5.77 The second progress report was due on 15 February 2005. On 14 January 2005, DOTARS’ North Queensland Regional Office emailed Beef Australia reminding it that the next instalment payment was due on 1 February 2005 and that a progress report was due on 15 February 2005.

5.78 A tax invoice and progress report was submitted by Beef Australia on 11 March 2005. The Progress Report was required to address the third and fourth milestones, but instead addressed the second and third project milestones. Beef Australia also provided a statement of expenditure against the first Regional Partnerships instalment payment of $550 000 (including GST). Beef Australia did not provide a summary of expenditure of cash contributions from its own sources and other funding partners.

5.79 In relation to the first Regional Partnerships instalment, the financial information provided to DOTARS by Beef Australia showed that $134 715.01 (24 per cent) of the first instalment had been spent.812 A further $300 000 in Regional Partnerships funds had been placed in a term deposit on 19 November 2004. This term deposit matured on 19 February 2005 and was renewed by Beef Australia on that date for a further four months.

5.80 On 22 March 2005, the North Queensland Regional Office advised Beef Australia that a further payment could not be made until the first payment was fully acquitted or a statement was provided that the remaining 76 per cent of the first payment had been committed. On 23 March 2005, Beef Australia provided DOTARS with a bill of quantities for infrastructure costs and promotion and marketing. However, while a bill of quantities can serve a number of functions,813 it does not provide evidence that payments will be made in the near future. In this respect, financial information provided to

812 In addition, the 11 March 2005 Progress Report included a statement by the Chairman of Beef Australia that $131 841.72 had been expended in accordance with the Funding Agreement. This amount included interest of $2 873.29 on funds held, thereby understating expenditure. Subsequent expenditure reports did not include any figures for the amount of interest earned on funds held at bank.

813 For example, a bill of quantities can be used as a measure of the extent of work in order to enable it to be priced.
DOTARS by Beef Australia on 24 August 2005 (seven months later) showed that the costs included in the bill of quantities remained ‘committed’ but unpaid.

5.81 In addition, the bill of quantities figure of $316 501.37 combined with expenditure of $134 715.01 still did not account for $98 783.62 (18 per cent) of the first instalment of $550 000.

5.82 Notwithstanding the non-compliance with the Funding Agreement requirement that the first payment have been spent or satisfactory evidence be produced that it would be fully expended in the near future, on 23 March 2005 DOTARS processed a further payment of $550 000 (including GST) to Beef Australia. In this respect, once the existing $300 000 term deposit matured on 19 June 2005, Beef Australia used $200 000 of this second instalment to invest in an increased term deposit in the amount of $500 000.

Third progress report and third instalment payment

5.83 On 25 July 2005, the North Queensland Regional Office wrote to Beef Australia reminding it that a progress report was due on 15 August 2005 addressing the fifth and sixth milestones and, if this was acceptable, it would generate the next payment.

5.84 On 15 August 2005, the North Queensland Regional Office telephoned Beef Australia concerning the third payment. The Regional Office record of the discussion states that:

After discussing the importance of contract management and the financial management of the project she is going to look at her upcoming commitments and tenders and see if it will be possible to received [sic] the payment and get back to us (in a reasonable time).

5.85 On 24 August 2005, Beef Australia provided a spreadsheet of expenditure on the project and a list of ‘monies committed but not paid’. This showed that, in addition to the $134 715.01 that had been reported on 11 March 2005 as having been spent between 1 November 2004 and 28 February 2005, a further $105 773.29 had been spent between 1 March 2005 and 24 August 2005. In other words, by 24 August 2005, Beef Australia had only spent $240 488.30 (22 per cent) of the $1 100 000 in Regional Partnerships funds paid by DOTARS to that date. It clearly demonstrated that the second instalment should not have been paid in March 2005 as the first instalment had not been fully spent and was not likely to be fully spent in the near future (given 56 per cent of the
first payment remained unspent five months after the second payment was made).

5.86 The financial information provided to DOTARS showed that, in addition to $240,488.30 in total cumulative expenditure, Beef Australia estimated it had $804,000 in ‘monies committed but not paid’. Beef Australia held $859,511.70 in Regional Partnerships funds ($500,000 in a term deposit and the remainder in its operating account) to meet these costs. On this basis, the North Queensland Regional Office concluded that it was unable to make the next payment of $825,000 (including GST). As the Regional Office did not propose to make the third payment at that time, on 26 August 2005 it advised Beef Australia not to submit the Progress Report that had been due on 15 August 2005.

5.87 The third Progress Report was submitted to DOTARS on 5 December 2005 (it was received by the Regional Office on 8 December 2005). It addressed the third and fourth milestones. The accompanying financial data\textsuperscript{814} showed that expenditure between 1 March 2005 and 14 November 2005 had been $389,573.40.\textsuperscript{815} Accordingly, to 14 November 2005, total expenditure from the $1,100,000 already paid to Beef Australia was $524,288.41. This meant that, $25,711.59 of the first instalment remained unspent some thirteen months after the payment was made, and none of the second instalment of $550,000 (GST inclusive), paid nearly eight months earlier, had yet been spent.

5.88 In the financial data, Beef Australia stated that there was $864,927.24 in ‘monies committed but not paid’. On this basis, on 12 January 2006, DOTARS processed for payment the invoice from Beef Australia (dated 5 December 2005) for the third instalment of $825,000 (GST inclusive).

\textit{Fourth progress report and fourth instalment payment}

5.89 Following consideration of the third Progress Report, on 12 January 2006 the Regional Office advised Beef Australia that the Funding Agreement should be varied to amend the due date for the fourth Progress Report and the proposed payment due date for the fourth instalment. A Funding Agreement Variation was sent to Beef Australia by the Regional Office on 18 January 2006. It was signed by Beef Australia on 1 February 2006 and by DOTARS National Office on 9 March 2006. The changes made were to:

\textsuperscript{814} Unlike the earlier Progress Report, the financial data was accompanied by an audit report.

\textsuperscript{815} Figure excludes $200,000 added to the term deposit on 19 June 2005 and interest on the operating account of $6,340.29.
• delay the proposed payment due date for the fourth payment of $275 000 (GST inclusive) from 2 January 2006 to 15 March 2006;
• delay the final payment of $220 000 (GST inclusive) from 30 June 2006 to 1 July 2006;
• delay the due date for the fourth Progress Report from 16 January 2006 to 1 March 2006; and
• bring forward the due date for the Post Activity Report from 1 July 2006 to 30 June 2006.

5.90 On 31 March 2006, the North Queensland Regional Office emailed Beef Australia seeking confirmation that the next Progress Report (due on 1 March 2006) and claim for payment would be forwarded by mid-April 2006.

5.91 A Progress Report dated 12 April 2006 was received by the Regional Office on 18 April 2006. It reported against the fifth and sixth milestones and was accompanied by audited financial data and a tax invoice for the fourth instalment payment. The financial data provided showed that expenditure between 15 November 2005 and 30 March 2006 had been $760 999.26. Accordingly, to 30 March 2006, total expenditure from the $1 925 000 already paid to Beef Australia was $1 285 287.67. This meant that the first two instalments paid in October 2004 and March 2005 had finally been spent by March 2006. However, only $185 287.67 (22 per cent) of the third instalment of $825 000 (GST inclusive) paid in January 2006 had been spent.

5.92 In the financial data, Beef Australia stated that there was $486 642.00 in ‘monies committed but not paid’. This meant that, as at 30 March 2006, $671 929.67 of the third instalment of $825 000 had been spent or committed. Accordingly, as the Funding Agreement required all previous payments to have been spent or there to be evidence that they would be fully spent in the near future, no further payment should have been made to Beef Australia. Notwithstanding this, on 24 April 2004, DOTARS processed for payment the fourth instalment of $275 000 (including GST).

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816 The contract variation incorrectly stated that the GST inclusive amount of the fourth instalment was $250 000. This was the GST exclusive amount.
817 The contract variation incorrectly stated that the GST inclusive amount of the final instalment was $200 000. This was the GST exclusive amount.
818 Figure excludes interest on the operating account of $3 556.79.
5.93 In July 2007, DOTARS advised ANAO that:

As of 30 March 2006, the balance of the Beef Australia account was $44,567.42. The statement as noted above indicated a commitment of $486,642.00.

5.94 As noted, the Funding Agreement required that the department make no further payments to Beef Australia unless all previous payments had been spent or there was evidence that they would be fully spent in the near future. In this respect, the commitment figure of $486,642.00 included in the progress report included amounts that had been reported to DOTARS for some period of time as being committed but not paid. For example, the committed amount of $486,642 included:

- the cost of showground hire ($80,000)—Beef Australia had been reporting this amount as ‘committed’ since 24 August 2005;
- the cost of competition schedules ($10,000)—Beef Australia had also been reporting this amount as ‘committed’ since 24 August 2005;
- on 23 March 2005, Beef Australia provided DOTARS with a copy of the bill of quantities for tentage in the amount of $320,000. The cost of tentage at the showgrounds was first reported on 24 August 2005 to DOTARS as $320,000 in ‘committed’ funds. The third progress report of 5 December 2005 reported the amount of ‘committed’ funds for tentage as being $315,000. The same amount was included in the fourth progress report of 12 April 2006.

5.95 Accordingly, in the absence of further information from the funding recipient, there was not a sound basis for the department to make a payment on the basis that $486,642 would be fully spent in the near future.

Post Activity Report and final payment

5.96 On 21 June 2006, the North Queensland Regional Office received a final report (dated 20 June 2006) from Beef Australia. This report did not meet all the requirements of the Funding Agreement. Specifically, it did not include:

- a summary of performance against the project activity milestones (some of the information required in relation to project outcomes was provided);
- details of mitigating circumstances and remedial action undertaken where milestones were not met or completed in the manner and/or by the time specified;
• an analysis of the planning, implementation and overall process Beef Australia followed to deliver the activity;
• any lessons learned throughout the activity; or
• any recommendations on improved practice that may assist in the delivery of future activities.

5.97 Similar financial data was provided to that included in earlier Progress Reports (together with an audit certificate). The financial data covered the period 31 March 2006 to 6 June 2006, with total expenditure in the period of $2 093 698.60.819

5.98 Beef Australia also provided DOTARS with an unaudited schedule showing the use of the Regional Partnerships funds against the Budget Items included in the Schedule to the Funding Agreement and an unaudited schedule showing cash contributions from other funding partners.

5.99 As illustrated by Table 5.3, this information did not satisfy the requirements of the Funding Agreement. In addition, DOTARS’ analysis of the report indicated that only some of the project outcomes were achieved. Notwithstanding this, the final payment of $220 000 (including GST) was processed on 29 June 2006.

ANAO conclusion

5.100 Key aspects of the project were not effectively managed through the Funding Agreement. In particular:

• the Funding Agreement was not drafted and administered in a way that provided assurance that budgeted partnership contributions were obtained and spent on the project;
• payments were made significantly in advance of project cash flow requirements; and
• the project was not acquitted in accordance with the requirements of the Funding Agreement.

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819 Figure excludes interest on the operating account of $1 672.08 and various deposits totalling $1 350 000.00.
Table 5.3
Compliance with information required under the Funding Agreement before the final payment should have been made

<table>
<thead>
<tr>
<th>Audit Report Requirement</th>
<th>Clause</th>
<th>Information Obtained</th>
</tr>
</thead>
<tbody>
<tr>
<td>An audited detailed statement of receipts and expenditure in respect of Regional Partnerships funds and all other contributions.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not obtained. Audited expenditure information was obtained in two of the three progress reports provided (but the information in the first progress report was unaudited) and a final report. In addition, the financial information did not include all partner contributions or, based on recent advice to ANAO from Beef Australia, all project expenditure. Accordingly, it was incomplete.</td>
</tr>
<tr>
<td>Definitive statement as to whether the financial accounts are complete and accurate.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not obtained. Statement related to the financial information being true and fair.</td>
</tr>
<tr>
<td>A statement of the balance of the separate bank account.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not obtained. Information obtained by ANAO shows the balance of the bank account into which Regional Partnerships funds were paid at 2 June 2006 was $471 521.74.</td>
</tr>
<tr>
<td>An audited statement that the Regional Partnerships funding and other contributions were expended for the purposes of the Activity and in accordance with the Agreement.</td>
<td>9.2(d) and 3.4(c) of Schedule</td>
<td>Statement provided but related to the expenditure period 31 March 2006 to 6 June 2006. Similar statements included in earlier Progress Reports (but statement in first report was not audited).</td>
</tr>
<tr>
<td>A certificate that all Regional Partnerships funding other contributions were expended for the purpose of the Activity and in accordance with the Funding Agreement.</td>
<td>9.2(e)(i) and 3.4(c) of Schedule</td>
<td>Statement provided but related to expenditure in the period (rather than Regional Partnerships funds and all other contributions). Similar statements made in earlier progress reports.</td>
</tr>
<tr>
<td>A certificate that salaries and allowances paid to persons involved in the Activity are in accordance with any applicable award or agreement in force under any relevant law on industrial or workplace relations.</td>
<td>9.2(e)(ii) and 3.4(c) of Schedule</td>
<td>Provided in each progress report.</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS records.

Potential overpayment of grant funds

5.101 Regional Partnerships funding was approved for this project on the basis of budgeted cash expenditure of $5 861 750. This was to be funded by
$2 200 000 in Regional Partnerships funding (excluding GST) and $3 661 750 from other entities and event revenue.

5.102 The Long Form Standardised Funding Agreement used for the Regional Partnerships Programme includes an effective framework for DOTARS to identify the final cost of each project, and the identity and quantum of all partnership contributions actually received. Specifically, at the conclusion of the project, funding recipients are required to provide an audited detailed statement of receipts and expenditure in respect of both the Regional Partnerships funding and all partner contributions.820

5.103 However, DOTARS did not obtain a whole–of–project acquittal of project receipts and expenditure. The only information obtained by the department in relation to project receipts was data that indicated partner cash contributions totalled $863 500 (considerably less that the $1.9 million budgeted for and included in the Regional Partnerships Funding Agreement)821 with no audited financial information obtained on exhibition revenue (budgeted at $1.76 million).

5.104 In terms of project expenditure, the information obtained by DOTARS comprised four separate audited statements of project expenditure. Three of these were provided with progress reports and the fourth with the final report received on 21 June 2006. Each report included expenditure only for the period covered by the report. There was no evidence that the department aggregated the various reports provided by Beef Australia so as to identify the total cost of the project, as had been reported to it by Beef Australia. In this respect, the information provided by Beef Australia to DOTARS in the various progress reports included total cumulative expenditure of $3 378 986.27 (see Table 5.4). This was $2 482 763.73 less than the $5 861 750 budgeted.

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820 Clause 9.2(c) of the Long Form Standardised Funding Agreement.

821 A number of envisaged partners provided no contribution, whilst others (including the State Government, Rockhampton City Council and Meat and Livestock Australia) provided a significantly reduced contribution.
Table 5.4
Project expenditure as reported to DOTARS by Beef Australia

<table>
<thead>
<tr>
<th>Source</th>
<th>Expenditure reported to DOTARS (A)</th>
<th>Term deposit purchases included in expenditure (B)</th>
<th>Interest receipts included in expenditure (C)</th>
<th>Money transfer receipts included in expenditure (D)</th>
<th>Actual expenditure (A) - (B) + (C) + (D)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Progress report for 1 Nov 04 to 28 Feb 05</td>
<td>$431 841.72</td>
<td>$300 000.00</td>
<td>$2 873.29</td>
<td>Nil</td>
<td>$134 715.01</td>
</tr>
<tr>
<td>Progress report for 1 Mar 05 to 14 Nov 05</td>
<td>$583 233.11</td>
<td>$200 000.00</td>
<td>$6 340.29</td>
<td>Nil</td>
<td>$389 573.40</td>
</tr>
<tr>
<td>Progress report for 15 Nov 05 to 30 Mar 06</td>
<td>$757 442.47</td>
<td>Nil</td>
<td>$3 556.79</td>
<td>Nil</td>
<td>$760 999.26</td>
</tr>
<tr>
<td>Post-activity report 31 Mar 06 to 6 Jun 06</td>
<td>$742 026.52</td>
<td>Nil</td>
<td>$1 672.08&lt;sup&gt;822&lt;/sup&gt;</td>
<td>$1 350 000.00</td>
<td>$2 093 698.60</td>
</tr>
</tbody>
</table>

Total $2 514 543.82 $500 000.00 $14 442.45 $1 350 000.00 $3 378 986.27

Source: ANAO analysis of progress reports and post-activity report provided to DOTARS by Beef Australia.

5.105 Based on the information provided to DOTARS by Beef Australia as part of the administration and acquittal of the Regional Partnerships grant, ANAO’s initial analysis was that project expenditure was at least $1.7 million less than actual and budgeted project revenue.<sup>823</sup> ANAO’s initial estimate (undertaken relying on the audited acquittal information held by DOTARS) explicitly recognised that the surplus of $1.7 million would be reduced to the extent that:

- there was any project expenditure that was not reported to DOTARS;

<sup>822</sup> A further $1 952.26 in interest was earned (according to the bank statements) but not included in the reports to DOTARS.

<sup>823</sup> Budgeted exhibition revenue was used in the absence of an audited acquittal of this element of the project budget having been obtained by DOTARS from Beef Australia.
• event revenue was less than budgeted; and/or
• partner contributions were less than were advised to DOTARS.

5.106 As the department had not analysed the financial information provided by Beef Australia in terms of the project budget, the department was unaware of this issue and had not raised it with Beef Australia. An ANAO case study of this project was provided to DOTARS in March 2007 drawing attention to the possible project surplus. In May 2007, DOTARS advised ANAO that it was seeking legal advice in respect to the project, including in respect to whether the department:
• had grounds to request the repayment of interest earned on the Regional Partnerships funds; and
• should be taking steps to recover the apparent overpayment.

5.107 However, as of October 2007 DOTARS records did not include any legal advice in relation to the apparent overpayment, or any correspondence with Beef Australia addressing this issue. In November 2007, Beef Australia provided ANAO with a one-page unaudited summary of actual project income (cash and in-kind) and project expenditure (cash and in-kind). This additional unaudited information indicated a project surplus of $516,829 (see Table 5.5).  

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824 In July 2007, DOTARS requested advice from the funding recipient in respect to the total amount of interest that had been earned from the Regional Partnerships funding and information as to how the interest was spent, or if it had been carried over for use in the next Beef Expo. The funding recipient advised DOTARS that a sum of $30,464 in interest had been earned in relation to the Regional Partnerships funds, which had been expended toward staging costs of the 2006 Beef Expo.

825 It was unclear from the summary information provided to ANAO by Beef Australia whether the income figures included interest earned on Regional Partnerships funds. In the event interest was not included, the project surplus would increase.
Table 5.5
Calculation of potential overpayment

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount (GST inclusive)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Project receipts:</td>
<td></td>
</tr>
<tr>
<td>Regional Partnerships</td>
<td>$2,420,000</td>
</tr>
<tr>
<td>Exhibition revenue and other contributions advised to ANAO by Beef Australia in November 2007 (unaudited)</td>
<td>$2,176,472</td>
</tr>
<tr>
<td>Total receipts</td>
<td>$4,596,472</td>
</tr>
<tr>
<td>Project expenditure:</td>
<td></td>
</tr>
<tr>
<td>Expenditure reported to ANAO by Beef Australia in November 2007 (unaudited)</td>
<td>$4,499,301</td>
</tr>
<tr>
<td>Less: Post event secretariat expenditure 2006–09 (unaudited)</td>
<td>$419,658</td>
</tr>
<tr>
<td>Total expenditure</td>
<td>$4,079,643</td>
</tr>
<tr>
<td><strong>Potential project surplus</strong></td>
<td><strong>$516,829</strong></td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS records and information from Beef Australia.

**ANAO conclusion**

5.108 Based on the information available from DOTARS’ administration of the Funding Agreement, the activity funded by the Regional Partnerships Programme cost less than the funds received from the Commonwealth grant, plus contributions from other partners and exhibition revenue. In November 2007, Beef Australia provided ANAO with a one-page unaudited summary of actual project income (cash and in-kind) and project expenditure (cash and in-kind). The unaudited information provided to ANAO by Beef Australia continued to indicate a substantial (but reduced) project surplus. In these circumstances, there would be merit in the department seeking a comprehensive audited acquittal for this $2.2 million (plus GST) Regional Partnerships grant and assessing the need for any further action that may be required.

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826 The then Parliamentary Secretary’s 30 June 2004 correspondence to Beef Australia advising that Regional Partnerships funding had been approved for Beef Australia 2006 stated that the Australian Government funding was for the planning and staging of the 2006 exposition only. This was consistent with the then applicable Regional Partnerships Programme Guidelines. In addition, the Funding Agreement signed with Beef Australia does not provide for ongoing operating costs to be part of the project costs.
6. Horse Australia 2005

This case study examines RP00936 Horse Australia 2005, involving Regional Partnerships funding being used towards the costs of a horse exposition in Rockhampton, Queensland. This case study includes comparisons to RP01101 Beef Australia 2006, involving Regional Partnerships funds being approved to assist with a beef exposition in Rockhampton. Although there were similarities between the projects, and inter-relationships between the management of the two expositions, there were significantly different approaches taken to the application, assessment, approval and announcement processes for the two grants.

Background

6.1 Horse Australia Rockhampton Association Inc (Horse Australia) was incorporated on 1 April 2004. It is a non-profit member-based association established to direct and manage the planning and development of a horse exposition in Rockhampton in Central Queensland, to be known as Horse Australia 2005. In April 2004, Horse Australia submitted an application for $500 000 (plus GST) in Regional Partnerships funding to assist with the costs of staging Horse Australia 2005.

6.2 The structure of the Business Plan and associated budget for Horse Australia 2005 was similar to that for Beef Australia 2006, the sixth triennial nation beef exposition also held in Rockhampton. This reflected the fact that Horse Australia engaged Beef Australia Inc (Beef Australia), the organising body of the national beef expositions, to assist in the development and staging of Horse Australia 2005. In addition, both the Chairman and Secretary of Horse Australia had been involved in the beef expositions. Beef Australia 2006 was also the subject of an application for funding under the Regional Partnerships Programme (RP01101 Beef Australia 2006).

6.3 Regional Partnerships funding was sought for Horse Australia 2005 and Beef Australia 2006 at around the same time. However, there were significant differences in the project application, assessment and approval processes. Specifically:

• the Horse Australia application for $500 000 (plus GST) in Regional Partnerships funds was received by the Northern Queensland Regional

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827 Due to a DOTARS error, TRAX recorded the applicant for the Horse Australia 2005 project as being Beef Australia Inc.
Office in April 2004. Assessment of the application was undertaken by the Regional Office over a 15 week period between mid-May and late August 2004, with written input from the Central Queensland ACC (CQACC). The project assessment was then finalised by DOTARS’ National Office, with a recommendation for partial funding being submitted to the then Parliamentary Secretary in late August 2004. The Parliamentary Secretary approved partial funding of $200 000 (plus GST) on 31 August 2004; whereas

• for Beef Australia 2006, an ‘Invitation to Partner’ document seeking $2 200 000 (plus GST) in funding was submitted to two Australian Government Ministers in February 2004. The then Minister for Transport and Regional Services approved funding on or about 10 June 2004, prior to the project details being provided to DOTARS for assessment or Regional Partnerships application having been submitted. A subsequent assessment of Beef Australia 2006 was undertaken by DOTARS’ National Office, with no involvement from the Regional Office and limited input from the CQACC. This assessment was undertaken over six days between 15 June 2004 and 21 June 2004.

6.4 There were also significant differences in the timeliness of the announcement of the funding decisions for the two projects. Funding for Beef Australia 2006 was announced on 2 July 2004, some 10 days after funding had been approved. However, announcement of the then Parliamentary Secretary’s 31 August 2004 decision to approve partial funding of $200 000 (plus GST) for Horse Australia 2005 was delayed at the request of the then Minister’s Office, with formal advice of funding approval not being provided to the applicant until 26 November 2004. In December 2004, the Horse Australia 2005 project was subject to debate in the House of Representatives concerning the process through which Regional Partnerships funding was approved and announced.

Application and approval processes

6.5 On 17 February 2004, the CQACC received by email an Expression of Interest for Regional Partnerships funding towards Horse Australia 2005. The project had a proposed start date of May 2004 and finish date of May 2005. Within a total project cost of $1 000 000, the Expression of Interest sought $500 000 (plus GST) in Regional Partnerships funding. Remaining funds were to come from sponsorship ($179 000) and ticket sales, nominations etc.
($321 000). In relation to the value to be added from the Regional Partnerships contribution, the Expression of Interest stated that:

To stage an event that will showcase all aspects of the Horse and attract national competitors we require Commonwealth Government support. If funding was not available the event would be downsized to a weekend competition with local participants.

6.6 The CQACC records of this project did not include documentation concerning its consideration of the Expression of Interest.

6.7 On 13 April 2004, Horse Australia submitted an application for funding to the CQACC under the Regional Partnerships Programme. Subsequently, on 7 May 2004, an application was signed and provided to the DOTARS Northern Queensland Regional Office.

6.8 On 13 May 2004, the Regional Office acknowledged receipt of the Horse Australia 2005 application, and advised Horse Australia that assessment had commenced. Also on this date, the application was referred to the CQACC for comment. Written ACC comments were received on 19 May 2004, with the ACC recommending the project as a high priority.

6.9 In its assessment of the application, the Regional Office raised a number of issues with the applicant concerning the project budget and the funding sources. As a consequence, on 20 May 2004, Horse Australia wrote to DOTARS correcting a discrepancy in the budget submitted with the original application.

6.10 The Horse Australia 2005 Regional Partnerships application included two letters of support, one from Senator the Hon Ron Boswell, Leader of The Nationals in the Senate and another from the Mayor of Rockhampton City Council. Also on 23 June 2004, the Regional Office discussed with the applicant the need to obtain further industry letters of support from people who would support the event with their attendance, as well as any other letters of support that could be obtained. A further nine letters of support were provided, as follows:

- on 6 July 2004—three letters of support from the Central Rodeo Cowboys Association, Central Queensland Zone 27 Pony Club and Central Queensland Quarter Horse Association;
- on 13 July 2004—three letters of support from the Rocky Cutting Club, Show Horse Queensland and the National Cutting Horse Association of Australia;
• on 13 August 2004—one letter of support from the Australian Pony Club Council;
• on 16 August 2004—one letter of support from the Polocrosse Association of Australia; and
• on 19 August 2004—one letter of support from the Queensland Endurance Riders Association.

6.11 The Regional Office assessment of the project was completed on 25 August 2004, at which time the draft project assessment, draft funding approval letters from the then Parliamentary Secretary and CQACC comments were emailed to National Office.

6.12 Shortly thereafter, National Office forwarded the project assessment to the then Parliamentary Secretary.\(^828\) It was included as part of a package of 15 projects. Of these, 14 (including Horse Australia 2005) were recommended for funding and one was not recommended for funding. The Horse Australia application had sought $500 000 (plus GST) in Regional Partnerships funds, however DOTARS recommended that it be approved for partial funding of $200 000 (plus GST), subject to confirmation of co-funding.

6.13 DOTARS assessed the project as meeting the Regional Partnerships Programme Guidelines, with all criteria satisfied in part or full. In addition, DOTARS advised that the CQACC recommended the project and rated it a high priority for its region. As noted, DOTARS recommended that partial funding be approved, subject to confirmation of co-funding.

6.14 In terms of FMA Regulation 9, the project was approved by the then Parliamentary Secretary at 3:37 pm on 31 August 2004. This was one of 15 projects approved by the then Parliamentary Secretary between 3:25 pm and 4:04 pm on 31 August 2004 (including a project that DOTARS had not

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\(^{828}\) The Minute to the then Parliamentary Secretary was undated, but the then Parliamentary Secretary documented her decision on 31 August 2004, indicating that the assessment was provided some time between 25 August and 31 August. The Horse Australia 2005 project was included in Package 59 provided to the Parliamentary Secretary. The preceding package of assessments, Package 58, was submitted by the Department on 29 August 2004. On that basis, the Horse Australia 2005 project seems likely to have been submitted to the Parliamentary Secretary on either 30 or 31 August 2004.
recommended for funding). A caretaker period for the 2004 election was implemented from 5.00 pm on 31 August 2004.\(^\text{829}\)

**ANAO conclusion**

6.15 Regional Partnerships funding for the Horse Australia 2005 project was applied for, assessed and approved through the established processes and procedures.

**Funding announcement**

6.16 In terms of grant announcements, ANAO’s Administration of Grants Better Practice Guide states:

The announcement of grants can be a very sensitive issue at any time but especially in the lead up to an election, be it for Commonwealth, state, territory or local governments. It is accepted that governments may choose the timing of announcements to suit their purposes having regard to other priorities. Nevertheless, from a program administration perspective and, as a matter of good practice, it is preferable for all decision on approved or unsuccessful projects to be announced together, or within a relatively short period of time. This approach enables proponents to know the outcome of their proposals as soon as possible so they can begin implementing their projects or pursue alternative sources of funding. It also has the added advantage of avoiding any perception that the timing of the announcements is being used for party-political purposes.\(^\text{830}\)

6.17 In addition, for some grants programmes (including Regional Partnerships), delays in project announcements can place projects at risk of being considered to involve retrospective funding for costs already incurred. In this respect, the Horse Australia application for funding stated that the project start date was 1 June 2004 with a completion date of 30 June 2005. Accordingly, by the time DOTARS completed its project assessment in late August 2004, there was a risk that the project had already commenced (particularly given the finite lead time available for preparing the staging of the event, planned for April 2005).

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\(^{829}\) Organisations whose Regional Partnerships applications were still being assessed or on which a decision had not been made before 5.00 pm on 31 August 2004 were advised by DOTARS that:

‘As you are aware the Prime Minister announced that a Federal Election will be held 9 October 2004. As a result of the announcement, a Caretaker Period was implemented from 5.00 pm 31 August 2004. Under the Caretaker Conventions no decisions on funding requests can be made until a new government is formed. The Caretaker Conventions do not prevent preparatory work on the assessment of your application. However, any funding decisions regarding your application will be a matter for the incoming government.’

\(^{830}\) ANAO Better Practice Guide—Administration of Grants, op. cit., p. 47.
6.18 In this respect, the then applicable Regional Partnerships Guidelines (31 May 2004 version) provided that project proposals that were requesting funding for retrospective costs were not eligible for funding. The DOTARS Internal Procedures Manual (23 June 2004 version) stated:

The Australian Government will not fund retrospective costs in relation to a project. Regional Partnerships funding cannot be used to pay any project costs incurred prior to the applicant being advised the delegate has approved the project.

Retrospective funding is defined as funding to meet any expenditure, or commitment to expenditure, prior to the applicant being advised the delegate has approved the project. Whilst the date of formal advice that a project has been approved is the test of whether a payment would be retrospective or not, the Department’s advice is that proponents not commit to expenditure on a project prior to the Funding Agreement being signed by both parties.\textsuperscript{831}

Project announcement and advice to the applicant

6.19 Included with the Horse Australia 2005 project assessment were draft letters for the then Parliamentary Secretary to sign, advising the Government Duty Senator; the applicant; the Chair of the CQACC; and the Member for Capricornia of the funding approval.

6.20 On 10 September 2004, the package containing the approved Horse Australia 2005 project was returned to DOTARS National Office from the then Parliamentary Secretary’s Office. However, no announcement was made and the letters advising of funding approval were not sent.

6.21 On 11 October 2004, following discussions with the applicant about a decision on funding the project, the Regional Office sought advice from National Office as to the status of the project. In turn, National Office sought advice from the Departmental Liaison Officer in the then Parliamentary Secretary’s Office. On 11 October 2004, the Departmental Liaison Officer provided advice to National Office and the Regional Office. This chain of correspondence, ends with advice from the Departmental Liaison Officer to the Regional Office that:

This project was approved by Mrs Kelly prior to the commencement of the caretaker period but has been put “on hold” by Minister Anderson’s Office with respect to its announcement. I have not been advised as to the reasons for the delay in its announcement. You would be aware that the Department

\textsuperscript{831} DOTARS, Regional Partnerships Internal Procedures Manual, 23 June 2004, p. 22.

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recommended (and Mrs Kelly approved) a reduced amount of funding for this project (about half of that sought by the applicant).

6.22 The applicant was still seeking advice from DOTARS in late October 2004 concerning its application for funding. The Business Plan submitted with the Regional Partnerships application stated that, by this point in time, key planning for the event was to have been well advanced including: the one-year out launch function; sponsorship development with the private sector; issue of the trade fair prospectus; development of the conference and tours programme; and availability of nominations.

6.23 On 25 October 2004, the Regional Office asked the Departmental Liaison Officer for an update so that it could respond to the request for advice from Horse Australia. The next day, the Departmental Liaison Officer\textsuperscript{832} advised the Regional Office that the then Minister for Transport and Regional Services’ office was to contact Horse Australia to provide advice on the status of the application for funding.

6.24 Nonetheless, by late November 2004, DOTARS remained unaware as to whether the project had been announced and advice provided to the applicant concerning its application for funding. These questions were resolved on 26 November 2004 when the Departmental Liaison Officer in the then Parliamentary Secretary’s Office was advised that:

\[ \text{[Minister Anderson’s Office] is calling the proponents now. She recalls that she asked Senator Boswell to announce this but it appears he hasn’t done so yet. She is going to make sure he does this soon.} \]

6.25 On the basis of that advice, it was concluded that the Regional Office could proceed with a Funding Agreement. Also on 26 November 2004 the then Parliamentary Secretary’s Departmental Liaison Officer advised DOTARS’ Regional Office and National Office that he would send out the letters to the applicant and CQACC that had been signed by the previous Parliamentary Secretary on 31 August 2004 when she had approved partial funding for the project. Both letters were date stamped 26 November 2004. The letter to the local member was date stamped 2 December 2004.\textsuperscript{833}

\textsuperscript{832} The new Government Ministry was also sworn in on 26 October 2004. At that time, the existing Parliamentary Secretary to the Minister for Transport and Regional Services (the Hon De-Anne Kelly MP) became Minister for Veteran’s Affairs, and was replaced as Parliamentary Secretary by the Hon John Cobb MP. The existing Departmental Liaison Officer continued in the role in Mr Cobb’s Office.

\textsuperscript{833} Although the Regional Office had also prepared a letter to the Government Duty Senator, DOTARS records do not include a signed copy of any letter that may have been sent.
6.26 On 10 January 2005, a draft Schedule to the Funding Agreement was provided to Horse Australia by the Regional Office. This was followed on 13 January 2005 by a full Funding Agreement for signature.

6.27 The Funding Agreement was signed by Horse Australia on 25 January 2005 and by the Regional Office on 31 January 2005. The Funding Agreement involved three instalment payments, as follows:

- $150 000 (plus GST) representing 75 per cent of approved funding was proposed to be paid on 28 February 2005. It was to cover event lead-up and preparation. This payment was made on 15 February 2005;
- $40 000 (plus GST) representing 20 per cent of approved funding was proposed to be paid on 15 April 2005 to cover further event preparation costs. This payment was made on 20 April 2005; and
- $10 000 (plus GST) representing five per cent of approved funding was proposed to be paid on 30 May 2005 to contribute towards event delivery costs. This payment was made on 28 June 2005.

6.28 The Beef Australia project assessment had not raised any project viability concerns, yet the Funding Agreement for that project required the Regional Partnerships funds to be held in a bank account separate to other operational bank accounts of Beef Australia (see the ANAO Case Study of RP01101 Beef Australia 2006). In comparison, notwithstanding that Horse Australia had only recently been incorporated and the project was assessed to represent a medium viability risk, the Funding Agreement for the Horse Australia 2005 project did not require Regional Partnerships funds to be held in a separate bank account (see Figure 6.1).  

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In this respect, under section 5.3(b), a standard provision in the Long Form Standardised Funding Agreement used in the period examined, the bank account in which the Regional Partnerships funds were to be held was only required to be a separate account if this was specified in the Schedule to the Funding Agreement. The relevant section in the Schedule to the Horse Australia Funding Agreement, ‘2.6 Bank Account’, did not specify this requirement. By way of comparison, the equivalent section of the Schedule to the Funding Agreement executed with Beef Australia did include that specification.
**Figure 6.1**

Comparison of the sections of the Horse Australia and Beef Australia Funding Agreements relating to bank account requirements

<table>
<thead>
<tr>
<th>Horse Australia Funding Agreement</th>
<th>Beef Australia Funding Agreement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Section 5.3 of Horse Australia Funding Agreement</td>
<td>Clause 5.3 of Beef Australia Funding Agreement</td>
</tr>
<tr>
<td>5.3 You must:</td>
<td>5.3 You must:</td>
</tr>
<tr>
<td>(a) ensure that the Funds are held in an account in Your name, and which You solely control, with an authorised deposit-taking institution authorised under the Banking Act 1959 (Ch) to carry on banking business in Australia;</td>
<td>(a) ensure that the Funds are held in an account in Your name, and which You solely control, with an authorised deposit-taking institution authorised under the Banking Act 1959 (Ch) to carry on banking business in Australia;</td>
</tr>
<tr>
<td>(b) if specified in the Schedule, this must be an account that is:</td>
<td>(b) if specified in the Schedule, this must be an account that is:</td>
</tr>
<tr>
<td>(i) established solely for the purposes of accounting for, and administering, any Funding provided by Us to You under this Agreement; and</td>
<td>(i) established solely for the purposes of accounting for, and administering, any Funding provided by Us to You under this Agreement; and</td>
</tr>
<tr>
<td>(ii) separate from Your other operational accounts;</td>
<td>(ii) separate from Your other operational accounts;</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Section 2.6 of Schedule to Horse Australia Funding Agreement</th>
<th>Section 2.6 of Schedule to Beef Australia Funding Agreement</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.6 Bank Account</td>
<td>2.6 Bank Account</td>
</tr>
<tr>
<td>You must ensure that the Funds are held in an account in Your name, and which You solely control, with an authorised deposit-taking institution authorised under the Banking Act 1959 (Ch) to carry on banking business in Australia.</td>
<td>You must ensure that the Funds are held in an account in Your name, and which You solely control, with an authorised deposit-taking institution authorised under the Banking Act 1959 (Ch) to carry on banking business in Australia.</td>
</tr>
<tr>
<td>3. REPORTS (SUBCLauses 1.1, 9.1 to 9.3)</td>
<td>3. REPORTS (SUBCLauses 1.1, 9.1 to 9.3)</td>
</tr>
</tbody>
</table>

Source: Funding Agreement executed with Horse Australia Rockhampton Association Inc on 31 January 2005 for Horse Australia 2005 project and Funding Agreement executed with Beef Australia Inc on 15 October 2004 for Beef Australia 2006 project [ANAO highlighting].
ANAO conclusion

6.29 Funding was approved shortly before the Caretaker Period commenced for the 2004 Federal Election. At the request of the Office of the then Minister for Transport and Regional Services, announcement of funding approval was delayed, with a consequential delay in the applicant and other relevant parties being advised that funding had been approved. The delay significantly impacted the project in that:

- formal advice that partial funding only had been approved was not provided to the applicant until November 2004, some three months after the funding had been approved and five months before the exhibition was to open, reducing the time available for the applicant to seek alternate sources of funding; and

- by the time a Funding Agreement was signed at the end of January 2005, some five months after funding was approved, the exposition was less than three months from opening, such that planning and preparation for the event was already well underway.

Partnerships

6.30 As illustrated by Figure 6.2, the partner funding arrangements proposed in the Horse Australia 2005 application were similar to those proposed for Beef Australia 2006, which had been approved for funding by the then Minister for Transport and Regional Services on or about 10 June 2004. In each case, all levels of government were expected to make a contribution; the relative contributions proposed for government, the private sector and the applicant were similar; and both applications were premised on 30 per cent of costs being funded from exhibition revenue. In addition, in both cases, none of the partner contributions had been confirmed (this was drawn to the then Parliamentary Secretary’s attention in the project assessment for Horse Australia).
Figure 6.2
Partner funding comparison

![Partner funding comparison chart]

Source: Regional Partnerships applications submitted for Beef Australia 2006 and Horse Australia 2005.

6.31 Although the proposed partner funding arrangements, and status (confirmed or otherwise) of proposed co-funding, for the two projects were similar, significantly different approaches were taken in relation to assessment of the projects against the partnerships criterion by:

- National Office in relation to Beef Australia 2006 (notwithstanding the documented roles and responsibilities, the Regional Office was not involved in the assessment of Beef Australia 2006); and
- the Northern Queensland Regional Office in relation to Horse Australia 2005.

6.32 On 23 June 2004, the Northern Queensland Regional Office contacted Horse Australia in relation to the amount of Regional Partnerships funds sought and:

queried the high Regional Partnerships bid especially in the context of the bids from other funding agencies (Sport and Recreation; Qld Events) and mentioned that this does weaken the submission against the guideline criteria. [The applicant] said she was aware of that but that they were hoping for a good outcome. We discussed the possibility of not getting the full amount and what
this would mean to the overall project. She intimated that the event would still progress as they were too far down the track and committed to it; but would maybe have to be scaled down unless more sponsors came on board.

6.33 By way of comparison, there was no evidence of National Office querying the high proportional Regional Partnerships bid for the Beef Australia 2006 project, notwithstanding the significantly lower contributions proposed to be obtained from State and local government.

6.34 Both projects also proposed an ‘applicant’ contribution that actually related to revenue expected to be generated through the staging of the event itself. The implications of this were examined in the assessment of the Horse Australia 2005 project, contributing to the recommendation that only partial funding be approved. In comparison, the issue was not addressed in the assessment of the Beef Australia 2006 application.

6.35 The differing approaches taken to the assessment against the partnerships criterion for the Beef Australia 2006 and Horse Australia 2005 projects resulted in significantly different advice being provided to the then Parliamentary Secretary in relation to the two projects (see Table 6.1).
Table 6.1
Assessment against partnerships criterion

<table>
<thead>
<tr>
<th>Beef Australia 2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Partnerships and Support</strong></td>
</tr>
<tr>
<td>The <em>Regional Partnerships</em> bid of $2.2m represents 43 per cent of total project costs. The other contributing partners are:</td>
</tr>
<tr>
<td><strong>Cash:</strong></td>
</tr>
<tr>
<td>Beef Australia Inc (Applicant)</td>
</tr>
<tr>
<td>Queensland Government</td>
</tr>
<tr>
<td><strong>Total:</strong></td>
</tr>
<tr>
<td><strong>In-Kind:</strong></td>
</tr>
<tr>
<td><strong>Total:</strong></td>
</tr>
<tr>
<td>The contribution from the Queensland State Government is yet to be confirmed.</td>
</tr>
<tr>
<td>The cost of staging the exhibition is $5,100,000. A further $700,000 is allocated to the post 2006 Beef Australia operating budget. This provides for post event planning and set up for future expositions. The <em>Regional Partnerships</em> funding is to be used for the 2006 exposition only.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Horse Australia 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Partnerships and Support</strong></td>
</tr>
<tr>
<td>The Regional Partnerships bid of $500,000 represents 34 per cent of total project costs and 46 per cent of total cash (which includes Horse Australia expected revenue from the event). The other funding partners and their contributions are:</td>
</tr>
<tr>
<td><strong>Cash:</strong></td>
</tr>
<tr>
<td>Horse Australia (Applicant)</td>
</tr>
<tr>
<td>Queensland Events Corporation (State Govt)</td>
</tr>
<tr>
<td>Rockhampton City Council</td>
</tr>
<tr>
<td>Qld Department of Sport and Recreation</td>
</tr>
<tr>
<td>Westpac Bank</td>
</tr>
<tr>
<td>Mitavite</td>
</tr>
<tr>
<td>Elders Corporation</td>
</tr>
<tr>
<td>Animal Health</td>
</tr>
<tr>
<td>Castlemaine</td>
</tr>
<tr>
<td>City Printing</td>
</tr>
<tr>
<td>Shopping Fair</td>
</tr>
<tr>
<td>Coca Cola</td>
</tr>
<tr>
<td>UDV Guinness</td>
</tr>
<tr>
<td>Other various (less than $100)</td>
</tr>
<tr>
<td>* Horse Australia contribution relates to expected revenue during the four day event from registration fees, ticket sales, merchandising revenue, workshops etc and therefore reliant on attendance numbers.</td>
</tr>
<tr>
<td><strong>Total</strong></td>
</tr>
</tbody>
</table>
6.36 In its project assessment of the Horse Australia 2005 application provided to the then Parliamentary Secretary in late August 2004 (recommending that partial funding be approved), DOTARS stated that:

Partial funding is recommended based on: the need for national consistency with similar approved projects; value for money given the high Regional...
Partnerships bid; the medium risk attached to project viability and overall outcomes likely to be some years in the future. An amount of $200 000 (GST excl) would be commensurate with the State and Local Government funding bids which total $180 000. It should be noted that the applicant has confirmed during the assessment process that total project costs are based on delivering a very high standard event. Should a reduced budget be necessary due to not all funds being secured, the project can still proceed and will operate based on the final funds secured while still meeting the overall objectives. The budget should exclude any salary costs for ongoing administrative staff thus reducing the need for Regional Partnerships funds.

6.37 Consistent with the DOTARS recommendation, on 31 August 2004, the then Parliamentary Secretary approved $200 000 in Regional Partnerships funding, subject to confirmation of co-funding. However, as late as 22 October 2004 (see paragraph 6.22 above), Horse Australia was unaware that it had not been approved for full funding.

6.38 Formal advice of partial funding was provided to Horse Australia on 26 November 2004 (via the funding approval letter) wherein it was stated that:

I am pleased to advise you that I have approved funding under Regional Partnerships of $220 000 (GST inclusive) to the Horse Australia Rockhampton Association Inc for your Horse Australia 2005 project.

This reduced amount of funding is considered an appropriate level of contribution by the Australian Government. While this project provides significant community benefits, sound justification was not provide to support the high project cost. Also, the reduction in Regional Partnerships funding results in a more equitable partner funding.

**Funding Agreement requirements**

6.39 In correspondence dated 25 January 2005 returning the signed Funding Agreement to DOTARS, Horse Australia advised as follows in relation to partnership contributions:

We note that under clause 6.1 of the Agreement we must provide details of other contributions. We are still negotiating with some of our partners but will get details of agreements which have been finalised as soon as possible. Since our original application some of the commitments have altered however we are seeking other contributions and are on budget to deliver a successful event.

6.40 The budget for the project, identifying Regional Partnerships and applicant and other funding partner contributions, was included as an annexure to the Funding Agreement (see Figure 6.3). In addition, the Funding
Agreement included the standard clause in the Long Form Standardised Funding Agreement used for most projects under the Regional Partnerships Programme which required that the applicant provide satisfactory written evidence of the other contributions in accordance with Clause 6 of the Funding Agreement. Specifically, Clauses 6.1 and 6.2 of the Funding Agreement stated that:

6.1 It is a condition precedent to the payment of Funds under this Agreement that You must get people (other than Us), as identified in Item 2 of the Schedule, to provide Us with satisfactory written evidence that they will provide the Other Contributions to You, including the amounts to be provided, their due dates and the terms and conditions of the provision of the Other Contributions. The terms and conditions on which these Other Contributions are to be provided must be satisfactory to Us.

6.2 The written confirmation referred to in subclause 6.1 must be provided to Us within 20 Business Days of the Date of this Agreement, failing which this Agreement will be treated as void and as never having been entered into.
6.41 Internal legal advice obtained by DOTARS is that Clause 6.1 of the Standardised Funding Agreement provides a positive obligation to procure
certain written evidence for the Commonwealth from a third party. In addition, as noted, the then Parliamentary Secretary’s approval of partial funding was conditional on confirmation of partner co-funding. Specifically, the applicant was advised that:

Funding for the project has been approved, subject to all partnership contributions being confirmed. [ANAO emphasis]

6.42 FMA Regulation 13 requires that the Funding Agreement entered into by DOTARS comply with the terms of the then Parliamentary Secretary’s approval of the spending proposal given under FMA Regulation 9. In this respect, DOTARS included the following precondition on the first payment of Regional Partnerships funds:

approval for partial funding subject to confirmation of co-funding

6.43 On 7 February 2005, Horse Australia provided the Regional Office with a report of progress towards the objectives of the project. In addition to providing a list of contributions received and confirmed, Horse Australia advised DOTARS that:

Partnership contributions are being finalised with some changes to the overall project sponsorship levels. We confirm that the event budget has been adjusted to reflect changes to partnership contributions.

6.44 Given the extended delays that occurred between funding approval and signing of the Funding Agreement, by the time the Agreement was signed, planning and preparation for Horse Australia was well advanced with the exposition less than three months from its opening. Accordingly, it would be reasonable for DOTARS to have expected that partnership funding arrangements would have been largely settled by the time the Agreement was signed. However, apart from the approved Regional Partnerships funding from DOTARS and prospective event revenue, the list provided by Horse Australia to DOTARS indicated that it had received and confirmed contributions totalling only $114 500. As illustrated by Figure 6.4, this meant that there was a significant shortfall in confirmed funding compared to the project budget included in the Regional Partnerships Funding Agreement.
6.45 Notwithstanding the substantial shortfall in confirmed contributions and the short time remaining before the exposition was to open, the only action taken by DOTARS was to contact Horse Australia on 8 February 2005 for further advice. DOTARS documented this discussion as follows:

I rang [Horse Australia] to clarify her initial progress report with regards to State Government funding. Seems that the original $100 000 requested from Qld Events has eventuated as $25 000. The $30 000 from Dept of Sports and Recreation has been divided up and provided to a number of equestrian codes for the specific purpose of funding portions of the Horse Australia Event 2005. (i.e. some to Horse Australia directly; some to various pony clubs, totalling approx $12 000. These submissions were detailed in the brief as not being confirmed at the time of signoff of the brief by the Parliamentary Secretary.

[Horse Australia] will provide more detail on all funds in her next progress report and will also include a section covering these funds in the final report and audit documents.

6.46 In this respect, Horse Australia had not satisfied the pre-condition on receiving the first payment, requiring that it confirm all partnership
contributions. However, on 15 February 2005, DOTARS processed the first payment of $150 000 (plus GST), representing 75 per cent of approved funding.

6.47 Further, as noted, the Funding Agreement provided (at Clause 6.1) that it would be void if Horse Australia did not provide, by 28 February 2005, confirmation that the amounts identified in the Funding Agreement would be provided by the project partners, their due dates and the terms and conditions. This obligation was also not satisfied. In this respect, in October 2007, DOTARS advised ANAO that the department made an explicit decision not to exercise this clause as Horse Australia was keeping it informed of its efforts and progress in this regard. Similarly, in November 2007, Horse Australia advised ANAO that:

As noted there were changes in partnership contributions. In submitting our application for Horse Australia we provided the best information available at the time. We notified DOTARS of the changes as they became known to us.

**Applicant contribution misstated in Funding Agreement**

6.48 Consistent with the funding approval and advice to the applicant, the draft Schedule to the Funding Agreement provided by the Regional Office to Horse Australia on 10 January 2005 identified Regional Partnerships funding of $200 000 (plus GST). The $300 000 reduction in Regional Partnerships funds (compared to what had been sought) was matched by a $300 000 increase to the applicant’s contribution specified in the draft Schedule to the Funding Agreement (to $628 500 from the $328 500 identified in the application). This approach was taken notwithstanding that the applicant’s ‘contribution’ related to expected event revenue rather than a cash contribution from the applicant’s own financial resources and DOTARS had not assessed the capacity of Horse Australia (a non-profit member-based organisation incorporated less than a year earlier on 1 April 2004) to provide $300 000 in cash to the event over and above the expected event revenue.

6.49 On 1 February 2005, one day after the Funding Agreement was executed, the Regional Office telephoned Horse Australia to confirm that it would be forwarding the tax invoice and documentation regarding confirmation of partnership and sponsorships before the end of February so that the first payment could be made on time according to the Funding Agreement (which specified a proposed payment due date of 28 February 2005). Notwithstanding that the Funding Agreement required the project budget remain at the $1 097 500 (plus GST) identified in the Regional
Partnerships application, with the applicant contributing $628,500, the Regional Office:

discussed the project and the need of the proponent organisation to “scale down” the event to some extent due to the partial funding received from the Commonwealth. I advised that as long as the intent and general outcomes did not change, then the fact that a more modest event (with not so much razzamatazz as the envisaged “Rolls Royce” version of the event) occurred this first year would still meet contractual requirements.

That is, there will still be a horse event with the activities and workshops; there will still be sponsorships from the local community; there will still be publicity for all sponsors; there will still be visitors and participants at the event and there will still be flow-on injection of cash into the city from the visitor numbers. There will still be a successful event and the solid foundation to build on for future events.

6.50 The recently signed Funding Agreement was not varied to reflect the approach that was being taken. DOTARS also did not advise the then Parliamentary Secretary that a decision had been taken to “scale down” the event. On this issue, in June 2007, DOTARS advised ANAO that:

This Funding Agreement was signed by Horse Australia. This represented a commitment to provide the funds.

The department’s assessment provided to the Parliamentary Secretary identified that should a reduced budget be necessary due to not all funds being secured, the project could still operate on the final funds secured while still meeting the overall objectives. The Parliamentary Secretary agreed to the recommendation of partial funding.

**Partnership outcomes**

6.51 Grant acquittals are an integral part of good risk management and provide a measure of assurance that public funds allocated to grant recipients have been spent for their intended purposes.835 For the Regional Partnerships Programme, effective grant acquittals, among other things, enable DOTARS to be satisfied that all project partners have contributed to the level specified in the assessment on which funding approval was based and the executed Funding Agreement.

6.52 For Horse Australia 2005, the Funding Agreement included a value for most, but not all, of the in-kind contributions. Specifically, whilst the project

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assessment provided to the then Parliamentary Secretary stated that in-kind contributions were valued at $353 000, quantified in-kind contributions in the Funding Agreement totalled only $292 000. In any event, the final report and financial acquittal did not:

- report on the extent to which the in-kind partner contributions had actually been obtained; or
- provide a value for the in-kind partner contributions that had actually been obtained.

6.53 In this context, Horse Australia 2005 is an example of a project where DOTARS approach to programme evaluations of relying on the Funding Agreement to identify partnership outcomes would give a misleading result. Specifically, the Funding Agreement (see Figure 6.3 above) suggested that the applicant and other project partners were to contribute $897 500 cash and $292 000 in-kind to the project and Regional Partnerships was to provide $200 000 cash (plus GST). Under the DOTARS approach to measuring partnership outcomes, this results in a ratio of $5.95 in partnership contributions to each $1 from the Regional Partnerships Programme. However, following a project inspection conducted by ANAO on 2 June 2006, Horse Australia advised ANAO on 14 June 2006 that:

> Whilst Horse Australia 2005 did not meet its projected financial outcomes this was mainly due to the lower than expected support from both the Commonwealth and State Governments and the private sector partners providing greater value in kind support than cash.

6.54 In this respect, the financial acquittal provided by Horse Australia to DOTARS in June 2005 revealed that cash contributed by the applicant and other partners totalled $357 903, and provided no information on the value of any in-kind contributions that were received.\(^{836}\) With the full amount of Regional Partnerships funding of $200 000 (plus GST) having been paid, this resulted in a ratio of $1.79 in acquitted partnership contributions to each $1 from the Regional Partnerships Programme.

\(^{836}\) The Funding Agreement defined ‘Other Contributions’ as comprising both financial and in-kind resources and required that the financial acquittal address whether, and to what extent, both cash and in-kind contributions are actually obtained. However, in this respect, in November 2007 Horse Australia advised ANAO that: ‘We were not asked to provide them [in-kind contributions] at the time, and we note once again that we have supplied all information requested at all times.’
ANAO conclusion

6.55 At the time the Funding Agreement was signed on 31 January 2005, the exposition opening was less than three months away. However, by 7 February 2005, Horse Australia had confirmed less than 36 per cent of the budgeted revenue of $1,097,500. Regional Partnerships funding of $200,000 (plus GST) represented some 64 per cent of the amount confirmed. Accordingly, the success of the exposition depended to a significant extent on Regional Partnerships funding, notwithstanding that partial funding had been approved partly to address what was assessed as a disproportionately high bid for Regional Partnerships funding (representing 46 per cent of project costs).

6.56 DOTARS’ management of the Funding Agreement was such that the full amount of Regional Partnerships funds was paid notwithstanding substantial reductions in contributions from other project partners. As a consequence, whilst Regional Partnerships funding was approved for 18 per cent of project costs, the Programme funded 36 per cent of the actual project costs. In addition, the first Regional Partnerships instalment payment (of 75 per cent of grant funds) was paid in breach of the requirement that all co-funding be first confirmed.

Project outcomes

6.57 In its project assessment, DOTARS advised the then Parliamentary Secretary that the application satisfied the outcomes criterion for partial funding (see Figure 6.5)
**Figure 6.5**

**Assessment against the outcomes criterion**

- **Outcomes**

  The project will **strengthen growth and opportunities** through increasing economic and indirect employment opportunities in the Central Queensland region. There is an expectation that this event will bring the same success as the nationally recognised triennial Beef Australia expositions. However, there appears to be minimal evidence to substantiate the claim to date.

  Direct economic impact on the Central Queensland region, if the anticipated 20,000 visitors eventuate, has been valued at around $2 million although there is minimal evidence to substantiate this.

  The aim of the project is to showcase the Australian equine industry; to promote local equine goods and services providers; to encourage development of export opportunities and to provide sustainable tourism, cultural and community benefits to the region. The event is to be delivered triennially from 2005 and is envisaged that the event will grow similarly to the successes experienced from the Australian beef cattle expositions.

  As there is no precedence for this event in Rockhampton, the expectation of 20,000+ visitors to the region may be overstated. It is more likely that the event will show a more modest success in the early years and grow slowly in later years, thus reducing the growth and economic impact on the region at least in the short-medium term.

  The application satisfies this criterion for partial funding.


**6.58** In its Regional Partnerships application for funding, Horse Australia included seven outcomes and related performance measures for the project. However, the Regional Partnerships Funding Agreement significantly reduced the expected project outcomes, with quantified outcomes outlined in the application being downgraded to unquantified, output measures that gave no measure of the economic or community outcomes to be achieved through the event (see Table 6.2).
### Table 6.2
Project outcomes and performance measures

<table>
<thead>
<tr>
<th>Outcome</th>
<th>Performance measure</th>
<th>Outcome</th>
<th>Performance measure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Economic impact: Direct economic impact to the Central Queensland region</td>
<td>Feedback from businesses, calculation of the number of visitors to the site and number of visitors from outside of the region</td>
<td>Strengthened economic impact to Central Queensland region</td>
<td>Local business feedback; visitor numbers to the site and number of visitors from outside the region as measured by Horse Australia records by 30 June 2005.</td>
</tr>
<tr>
<td>Attendance: overall attendance – four days Spectators – 30 000</td>
<td>Gate and ticket sales</td>
<td>Visitor attendance at the Horse Australia equestrian event</td>
<td>Gate and ticket sales; number of stall holders at Horse Australia by 30 June 2005.</td>
</tr>
<tr>
<td>Trade fair: Exhibitors – 80-100</td>
<td>Number of stall holders and their satisfaction with product sold or business transactions</td>
<td>Visitor and exhibitor satisfaction</td>
<td>Commitment from local businesses and national equestrian bodies to ongoing Horse Australia events after 2005</td>
</tr>
<tr>
<td>Seminars &amp; workshops: 10 seminars and workshops</td>
<td>Number of visitors and the satisfaction with the speakers and information gathered</td>
<td></td>
<td>Not addressed</td>
</tr>
<tr>
<td>Horses: Attract 3 000 head</td>
<td>Number horses and satisfaction with services provided</td>
<td></td>
<td>Not addressed</td>
</tr>
<tr>
<td>Volunteers: 200 registered volunteers</td>
<td>Number of volunteers and their satisfaction with the experience and organisation</td>
<td></td>
<td>Not addressed</td>
</tr>
<tr>
<td>Meet and Greet: 500 attendees</td>
<td>Visitor satisfaction and networks made</td>
<td></td>
<td>Not addressed</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of Regional Partnerships application and Funding Agreement.

6.59 Horse Australia 2005 was held between 28 April 2005 and 1 May 2005. On 29 June 2005, DOTARS received from Horse Australia a report on the project. This report included advice against each of the project outcomes set out in the Funding Agreement, as summarised in Table 6.3.
Table 6.3

**Reporting on project outcomes**

<table>
<thead>
<tr>
<th>Project Outcome</th>
<th>Performance Measure</th>
<th>ANAO analysis</th>
</tr>
</thead>
<tbody>
<tr>
<td>Visitor attendance at the Horse Australia equestrian event.</td>
<td>Gate and ticket sales; number of stall holders at Horse Aust 2005 by 30 June 2005.</td>
<td>Report stated that around 22 000 attended. No data was provided on gate and ticket sales or the number of stall holders by 30 June 2005.</td>
</tr>
<tr>
<td>Strengthened economic impact to Central Queensland region.</td>
<td>Local business feedback; visitor numbers to the site and number of visitors from outside the region as measured by Horse Australia records by 30 June 2005.</td>
<td>Qualitative information provided on local business feedback. Attendance by 22 000 people reported. However, whilst qualitative data was provided on where visitors came from, no quantitative data was provided on the number of visitors from outside the region.</td>
</tr>
<tr>
<td>Visitor and exhibitor satisfaction.</td>
<td>Commitment from local businesses and national equestrian bodies to ongoing Horse Australia events after 2005.</td>
<td>Feedback from spectators, competitors, trade exhibitors and sponsors was reported as being very positive. Report stated that many of the events will be staged annually with a larger exposition to be staged on a triennial basis.</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of Funding Agreement and final report from Horse Australia.

6.60 In terms of the project outcomes, in November 2007 Horse Australia advised ANAO that:

Horse Australia’s project outcomes did not meet the stated goals in some cases for the following reasons:

1. As funding from major partners including the State and Federal government was reduced, so was the scale of the event with a resulting impact on visitation.\(^{837}\)

2. Being the first such event, public and private awareness and support was slower to materialise than that for Beef Australia which is a much more established event in an industry with stronger private sector consolidation.

\(^{837}\) As noted in paragraph 6.36, in its project assessment recommending that partial funding be approved, DOTARS had advised the then Parliamentary Secretary that ‘should a reduced budget be necessary due to not all funds being secured, the project can still proceed and will operate based on the final funds secured while still meeting the overall objectives’.
Visitor attendance

6.61 The key outcome to be achieved by the Horse Australia was attracting an additional 20 000 visitors so as to provide an economic impact of $2 million to the region. In its assessments against the outcomes criterion and the project viability criterion, DOTARS raised concerns that the expected influx of more than 20 000 visitors may have been overstated. However, DOTARS did not address how many of the expected 20 000 visitors were likely to be attending the campdraft irrespective of whether or not Horse Australia 2005 was held. A particular issue in this regard was that, since 2003, a campdraft has been held each year at a purpose designed and constructed complex situated on Paradise Lagoons near Rockhampton, attracting in the vicinity of 10 000 visitors each year.

6.62 In addition to not being addressed in project assessment, the management and acquittal of the project also did not require that the Horse Australia 2005 outcomes be distinguished from those already being achieved from the annual campdraft. In this respect, the performance measures specified in the Funding Agreement for measuring visitor attendance involved gate and ticket sales and the number of stall holders at Horse Australia by 30 June 2005. However, no benchmark of expected performance was articulated. Subsequently, Horse Australia did not quantify gate and ticket sales or the number of stall holders in its final report to DOTARS. Instead, it advised that:

Horse Australia 2005 was staged in Rockhampton from April 28th to May 1st. Around 22 000 people attended the Rockhampton Showgrounds, The Caves, and the Paradise Lagoons Campdraft during the Expo, showing that there is much support for a new Exposition that is affordable, inclusive and expressive of the important social and commercial role of horse sport and recreation in this country.

Participants included competitors in campdraft, cutting, rodeo, pony club, showjumping, interschool teams challenge, polocrosse, hacking, dressage, farriers, team roping, rocky rush, western performance, Sponsors, and various trade fair exhibitors. Spectators and competitors came from all states in Australia with competitors from New Zealand and Dubai participating in Australia Farrier’s Championships and the FEI endurance ride.

6.63 In this context, compared to the 22 000 visitors to Horse Australia 2005 reported by Horse Australia to DOTARS, the Rockhampton Morning Bulletin has reported that:
With an expected target of 10 000 people, Rockhampton Showgrounds recorded up to 12 000 spectators from all over Australia capturing a glimpse of the horse experience.\(^{838}\)

6.64 This would indicate that, of the 22 000 attendance reported by Horse Australia, some 10 000 attended the annual campdraft. This level of attendance at the annual campdraft is consistent with the reported attendance at the 2004 event\(^{839}\) and 2006\(^{840}\), further indicating that (in the absence of the provision of the required performance data on gate and ticket sales) Horse Australia 2005 did not result in 20 000 additional visitors.

**ANAO conclusion**

6.65 The key outcome to be achieved from Horse Australia 2005 was attracting an additional 20 000 visitors so as to provide an economic impact of $2 million to the Rockhampton region. However, the application for Regional Partnerships funding, DOTARS project assessment, the Funding Agreement and reporting obtained by DOTARS on project outcomes did not differentiate between the existing economic impact and visitor numbers that was being already achieved from the annual Paradise Lagoons campdraft, and the additional outcomes that could be expected to result from Horse Australia 2005. As the Post Activity Report advised that a total of 22 000 visitors attended the various equestrian activities held in Rockhampton during the period Horse Australia 2005 was held, the available evidence is that the additional visitors that could be attributed to the staging of Horse Australia would not have been more than 12 000.

**Financial acquittal**

6.66 The Horse Australia 2005 Funding Agreement required two reports to be provided. A Progress Report was due on 15 April 2005, followed by a ‘final report and audit’ on 30 May 2005. This ‘final report and audit’ was, in other parts of the Funding Agreement, referred to by its usual title of ‘post-activity report’.

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\(^{839}\) On 14 June 2004, The Morning Bulletin reported that more than 10 000 spectators attended the 2004 campdraft, which had more than 1 000 nominations from competitors.

\(^{840}\) On 1 May 2006, the Morning Bulletin reported that more than 10 000 people had attended the campdraft. On 29 April 2006, the Morning Bulletin had reported that 2 100 nominations had been received.
6.67 An initial Progress Report was provided to DOTARS on 7 February 2005, although the Funding Agreement did not require this report. A further Progress Report was provided on 16 April 2005.

6.68 A final report dated 27 June 2005 was provided to DOTARS together with a tax invoice for the final instalment. The attached audit report was unsigned. It also did not include the various attachments. Nonetheless, in order to make the final payment before 30 June 2005, the Regional Office relied on the documentation that had been received to process the final payment on 28 June 2005. A full final report with signed audit report and all attachments was received by the Regional Office on 29 June 2005.

6.69 As illustrated by Table 6.4, the final report and acquittal did not satisfy the requirements of the Funding Agreement. Notwithstanding this, DOTARS had already made the final payment based on a draft of the final report and acquittal.
Table 6.4  
Compliance with information required under the Funding Agreement before the final payment should have been made

<table>
<thead>
<tr>
<th>Audit Report Requirement</th>
<th>Clause</th>
<th>Information Obtained</th>
</tr>
</thead>
<tbody>
<tr>
<td>An audited detailed statement of receipts and expenditure in respect of Regional</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Satisfactory audit report provided.</td>
</tr>
<tr>
<td>Partnerships funds and all other contributions.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Definitive statement as to whether the financial accounts are complete and accurate</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not obtained. Statement made that the attached financial report was an accurate</td>
</tr>
<tr>
<td></td>
<td></td>
<td>statement of the matters specified in the report. No statement made as to the</td>
</tr>
<tr>
<td></td>
<td></td>
<td>completeness of the information.</td>
</tr>
<tr>
<td>A statement of the balance of the separate bank account.</td>
<td>9.2(c) and 3.4(c) of Schedule</td>
<td>Not obtained. Information obtained by ANAO shows the bank account balance at 1 June</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2005 was $17 779.35.</td>
</tr>
<tr>
<td>An audited statement that the Regional Partnerships funding and other contributions were</td>
<td>9.2(d) and 3.4(c) of Schedule</td>
<td>Statement provided.</td>
</tr>
<tr>
<td>expended for the purposes of Activity and in accordance with the Agreement.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>A certificate that all Regional Partnerships funding other contributions were expended</td>
<td>9.2(e)(i) and 3.4(c) of</td>
<td>Statement provided.</td>
</tr>
<tr>
<td>for the purpose of the Activity and in accordance with the Funding Agreement.</td>
<td>Schedule</td>
<td></td>
</tr>
<tr>
<td>A certificate that salaries and allowances paid to persons involved in the Activity are</td>
<td>9.2(e)(ii) and 3.4(c) of</td>
<td>Not obtained.</td>
</tr>
<tr>
<td>in accordance with any applicable award or agreement in force under any relevant law</td>
<td>Schedule</td>
<td></td>
</tr>
<tr>
<td>on industrial or workplace relations.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source:  ANAO analysis of DOTARS records.

6.70 The Funding Agreement required that Regional Partnerships funds be used for plant/equipment hire or lease. The final report included a statement of receipts and expenditure. This statement, which was accompanied by an audit certificate, reported Regional Partnerships funding of $220 000, income from other contributors and event revenue totalling $357 903 and total expenditure of $538 433.841

6.71 There were unidentified, and therefore unaddressed, anomalies in the financial information provided to DOTARS in respect to a number of transactions. In particular:

841 The expenditure was apportioned between the Regional Partnerships grant ($223 876.07) and other income ($314 556.44).
Horse Australia engaged Beef Australia to assist in the development and staging of Horse Australia 2005. A total of $103,400 (over 19 per cent of the reported project costs for the Horse Australia 2005 project) was reported in the financial acquittal as having been paid to Beef Australia in two transactions (see Figure 6.6). However, as preparations for Beef Australia 2006 were occurring at the same time as preparations for Horse Australia 2005, and Regional Partnerships funding for Beef Australia 2006 was provided, in part, to cover wages, salary and superannuation expenses for Beef Australia staff, there was merit in DOTARS assuring itself that Beef Australia (as a non-profit entity) had engaged additional staff to assist in the developing and staging of Horse Australia 2005 so as to address the risk of the Commonwealth paying twice for the employment costs of the same people; and

there were various items of expenditure listed in the financial acquittal that were not similarly reflected in bank statements as an actual outgoing. The amounts totalled $143,505, including the two amounts totalling $103,400 that were reported by Horse Australia to DOTARS as having been paid to Beef Australia for event management services. In respect to these two payments, in November 2007, Beef Australia advised ANAO that:

Beef Australia did not receive payment from Horse Australia for $103,400 as noted in your report.

Figure 6.6
Audited financial acquittal: payments by Horse Australia to Beef Australia

<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>10/03/06</td>
<td>Beef Australia Inc</td>
<td>Event Management Fee</td>
</tr>
<tr>
<td>10/03/06</td>
<td>Beef Australia Inc</td>
<td>Reimbursement Costs</td>
</tr>
<tr>
<td>15/03/06</td>
<td></td>
<td>Trade Name - Horse Australia Rockhampton Association Inc</td>
</tr>
<tr>
<td>15/03/06</td>
<td></td>
<td>Advertising March 05</td>
</tr>
<tr>
<td>16/03/06</td>
<td></td>
<td>Judges Hacking</td>
</tr>
<tr>
<td>18/03/06</td>
<td></td>
<td>Rocky Rush</td>
</tr>
<tr>
<td>18/03/06</td>
<td></td>
<td>Travel - Announcer</td>
</tr>
<tr>
<td>18/03/06</td>
<td></td>
<td>Group Accident Plan - Committee</td>
</tr>
<tr>
<td>18/03/06</td>
<td></td>
<td>Group Accident Plan - Additional Volunteers</td>
</tr>
<tr>
<td>23/03/06</td>
<td></td>
<td>Purchase Sawdust at Showgrounds</td>
</tr>
<tr>
<td>23/03/06</td>
<td></td>
<td>Cokeing Coal for Farriers</td>
</tr>
<tr>
<td>31/03/06</td>
<td></td>
<td>Programme Overview Changes</td>
</tr>
<tr>
<td>31/03/06</td>
<td></td>
<td>Horse Australia Postar</td>
</tr>
<tr>
<td>31/03/06</td>
<td></td>
<td>Site Map</td>
</tr>
<tr>
<td>31/04/06</td>
<td>Beef Australia Inc</td>
<td>Event Management Fee for Service</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of final report and acquittal provided to DOTARS by Horse Australia, 27 June 2005.
6.72 Based on the financial acquittal provided to DOTARS in June 2005 (see paragraph 6.70), ANAO’s analysis was that the activity funded by the Regional Partnerships Programme cost $19 470 less than the $577 903 expected to be received from the full Commonwealth grant, plus contributions from other partners and exhibition revenue. However, as noted at paragraph 6.71, in November 2007 Beef Australia advised ANAO that $103 400 in payments by Horse Australia to Beef Australia reported to DOTARS by Horse Australia in its financial acquittal had not been received. On this basis, as outlined by Table 6.5, the final Regional Partnerships instalment of $10 000 (plus GST) should not have been paid by DOTARS and consideration should have been given to recovering some of the earlier instalments.

**Table 6.5**

<table>
<thead>
<tr>
<th>Project income and expenditure</th>
<th>$</th>
<th>$</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>INCOME</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regional Partnerships funding</td>
<td>220 000</td>
<td></td>
</tr>
<tr>
<td>Exposition revenue</td>
<td>237 194</td>
<td></td>
</tr>
<tr>
<td>Other contributions</td>
<td>120 709</td>
<td></td>
</tr>
<tr>
<td><strong>Total income</strong></td>
<td></td>
<td>577 903</td>
</tr>
<tr>
<td><strong>EXPENDITURE</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reported in the financial acquittal</td>
<td>538 433</td>
<td></td>
</tr>
<tr>
<td>Less: payments not received by Beef Australia (see paragraphs 6.71 and 6.72)</td>
<td>103 400</td>
<td></td>
</tr>
<tr>
<td><strong>Total net expenditure</strong></td>
<td></td>
<td>435 033</td>
</tr>
<tr>
<td><strong>Potential project surplus</strong></td>
<td></td>
<td>142 870</td>
</tr>
</tbody>
</table>


__ANAO conclusion__

6.73 Based on the information available from DOTARS’ administration of the Funding Agreement, the activity funded by the Regional Partnerships Programme cost less than the funds received from the Commonwealth grant, plus contributions from other partners and exhibition revenue. Initial ANAO analysis of DOTARS’ audited acquittal data that revealed a project surplus was based on audited acquittal information obtained by DOTARS. Additional information provided to ANAO by the funding recipient in November 2007...
indicated a potentially more substantial surplus than was revealed by DOTARS’ data. This case study underlines the importance of acquittal processes providing assurance that funds have been used for the purposes granted and paid in line with project cash flow needs.
7. Carnarvon Recreational Marina

This case study examines RP01133 Carnarvon Recreational Marina. It outlines the nexus that often exists for projects involving non-profit organisation applicants between the partner contributions and viability risks. This is because, for many such projects, the applicant provides little or no cash contribution. For this particular project, key issues involved identifying the scope of the project and the parties contributing cash to project costs.

Introduction

7.1 DOTARS’ assessment of the Carnarvon Recreational Marina project was provided to the then Parliamentary Secretary in October 2004. This was as part of an assessment package of 15 projects. Of those, nine were recommended for approval of funding and six were not recommended for funding. The recommended projects included the Carnarvon Recreation Marina project.

7.2 DOTARS’ October 2004 project assessment advised the then Parliamentary Secretary that the project had a duration of 12 months with a recommended funding profile involving $96 650 being paid in 2004–05 and $119 010 in 2005–06.

7.3 DOTARS assessed the project as meeting the Regional Partnerships Programme Guidelines with all criteria satisfied. In addition, DOTARS advised that the Mid West Gascoyne ACC recommended the project and rated it a medium priority for its region. On 22 October 2004, the then Parliamentary Secretary approved $215 660 (plus GST) in Regional Partnerships funding for a Carnarvon Recreational Marina project that was to involve:

constructing a two lane boat ramp with facilities for trailer boats adjacent to mooring jetties for an additional 22 deep keeled vessels.

7.4 The Regional Partnerships Funding Agreement was signed on 7 February 2005. It required the project to be completed by 31 July 2006. The total project budget was $525 600 (plus GST). In addition to the Regional Partnerships funding, the other major financial contributors were specified to be the Shire of Carnarvon ($150 000) and the Western Australia Department for Planning and Infrastructure ($150 000). The applicant, the Carnarvon Yacht Club Inc. (Carnarvon Yacht Club), and the Gascoyne Recreational Fishing Advisory Committee were each to provide $5000 in cash to the project.
7.5 On 16 March 2006, the Commodore of the Carnarvon Yacht Club advised DOTARS that:

I wish to advise that the Marina Stage 2 has been completed to the entire satisfaction of me and the committee of the Carnarvon Yacht Club, with all funds that have been received, being committed to and expended on the Stage 2 Marina Project. An audit has been carried out by [Registered Auditors].

We are pleased with the way this project was completed ahead of time, and on budget, and I understand with double the voluntary hours of our commitment.

On behalf of our committee we are proud of the voluntary workers of our Club and the amount of work that they applied to this job.

The Shire of Carnarvon has been particularly helpful with their assistance during this project, and we would like to thank you for your prompt attention to our requests at each stage of the job.

The Marina is now fully functional and an asset to Carnarvon.

Project payments and reporting

7.6 Where the financial situation of the recipient permits, a prudent agency will draft the agreement’s schedule so that funds are paid in instalments, in arrears, and on satisfactory completion of major project milestones.\(^{842}\) In this respect, the Funding Agreement signed on 7 February 2005 specified four payments, as follows:

- the first payment in the amount of $95,600 plus GST (44 per cent of the total grant) was for the commencement of the project, with a proposed payment due date of 1 February 2005;
- the second payment in the amount of $58,000 plus GST (27 per cent of the total grant) was for concrete works, with a proposed payment date of 1 June 2005;
- the third payment in the amount of $57,900 plus GST (27 per cent of the total grant amount) was for construction of facilities, with a proposed payment date of 1 September 2005; and

---

the fourth payment in the amount $4160 plus GST (two per cent of the total grant amount) was for completion of the project, with a proposed payment due date of 1 April 2006.\textsuperscript{843}

7.7 As illustrated by Figure 7.1, the Funding Agreement prepared by DOTARS proposed to make payments to the Carnarvon Yacht Club in advance of the timing that had been requested in the Regional Partnerships application.

**Figure 7.1**

Regional Partnerships instalment payment arrangements

![Graph showing cumulative payments over time with sources annotated]

Source: ANAO analysis of Regional Partnerships application submitted by the Carnarvon Yacht Club and executed Funding Agreement.

7.8 In this context, the Funding Agreement proposed that all Regional Partnerships funds would be paid to the Carnarvon Yacht Club before the project was completed (the expected completion date was 31 July 2006) and

\textsuperscript{843} The audited profit and loss statement provided to DOTARS by the Carnarvon Yacht Club to support the final instalment payment of Regional Partnerships funds identified that $612 in interest was earned on the Regional Partnerships payments. The Funding Agreement had not been varied to enable the Carnarvon Yacht Club to retain the interest earned and use it towards the project. Accordingly, on the basis of DOTARS’ 18 September 2006 advice to the ANAO, the final payment of $4160 (plus GST) should have been reduced by $612. This did not occur.
before the Post Activity Report (including financial acquittal) was due (the due date was 30 August 2006).

7.9 The Funding Agreement required the Carnarvon Yacht Club to place the Regional Partnerships funds in a bank account established solely for the purposes of accounting for, and administering, the Regional Partnerships funds that was separate from its other operational accounts. Consistent with this requirement, the Carnarvon Yacht Club advised DOTARS that Regional Partnerships funds should be deposited into a bank account titled ‘Carnarvon Yacht Club (Inc) Marina Stage 2 Account’.

ANAO conclusion

7.10 DOTARS did not structure the payment arrangements in the Funding Agreement to reflect the project timetable outlined in the Regional Partnerships application for funding. Further, payments were not appropriately aligned to the due dates for the progress reports.

Project scope

7.11 As outlined above, on 22 October 2004, the then Parliamentary Secretary approved $215 660 (plus GST) in Regional Partnerships funding for a Carnarvon Recreational Marina project that was to involve:

constructing a two lane boat ramp with facilities for trailer boats adjacent to mooring jetties for an additional 22 deep keeled vessels.

7.12 This was on the basis of DOTARS advice that:

This project will implement Stage 2 of the development of the Carnarvon Recreational Marina by constructing a two lane boat ramp and an additional 22 mooring jetties.

7.13 In addition, DOTARS advised the then Parliamentary Secretary that:

The Carnarvon Recreational Marina project will achieve five major outcomes:

- Dual recreational trailer boat ramp with facilities;
- Pens for 22 deep keeled boats;
- Increased amenity for local population;
- Increased facility for visitors to the region, hence, increase in tourist numbers; and
- Expansion in water based recreation (boating, fishing and events such as regattas and Dragon Boat Festival).
7.14 However, ANAO found that the Funding Agreement did not reflect the terms of the then Parliamentary Secretary’s funding approval in that:

- moorings were to be constructed for 12 rather than 22 keel vessels; and
- a two lane boat ramp was not to be constructed by the Carnarvon Yacht Club as part of the project for which Regional Partnerships funds were being provided.

**Number of moorings**

7.15 Although the then Parliamentary Secretary approved a project for the construction of 22 moorings, the project outcomes specified in the Funding Agreement executed by DOTARS required the Carnarvon Yacht Club to construct 12 pens for keel vessels.

7.16 The Regional Partnerships application form received by DOTARS on 22 July 2004 from the Carnarvon Yacht Club had stated that the outcomes from the project would include ‘11 pens for 22 deep keel boats’. Both the departmental assessment provided to the then Parliamentary Secretary and the draft Funding Agreement prepared by DOTARS specified the construction of 22 pens. However, on 26 January 2005, in providing comments on the draft Funding Agreement, the Carnarvon Yacht Club requested that DOTARS amend the contract outcomes to ‘12 pens for keel vessels’.

7.17 DOTARS did not raise with the Carnarvon Yacht Club the reduction in outcomes from that specified in the Regional Partnerships application (which provided the basis for DOTARS’ assessment and the subsequent approval of funding by the then Parliamentary Secretary). DOTARS also did not advise the then Parliamentary Secretary of the significant reduction in expected outcomes compared to those that had been advised in the October 2004 project assessment that formed the basis for her funding approval.

7.18 In this respect, ANAO’s 4 May 2006 site inspection confirmed that only 12 pens were constructed, as illustrated in Figure 7.2 and Figure 7.3.
**Figure 7.2**
12 new boat pens constructed at Carnarvon Yacht Club

Source: ANAO site visit May 2006.

**Figure 7.3**
Plans for Stage 2 construction of 12 new boat pens at Carnarvon Yacht Club

Source: ANAO site visit May 2006.
The two lane boat ramp

7.19 As noted, the project approved by the then Parliamentary Secretary included the construction of a two lane boat ramp. Similarly, in his 28 October 2004 announcement of funding for the project, the local Federal Member, Barry Haase MP, stated that Regional Partnerships funds would be used, in part, for construction of boat ramps, as follows:

Member for Kalgoorlie, Mr Barry Haase, today announced that Australian Government funds would go towards costs associated with the design and construction of mooring jetties and boat ramps, earthworks and dredging for boat ramps and pens.

“This project will provide much needed mooring pens and a boat ramp at the Carnarvon Yacht Club…”

7.20 In the covering letter to its Regional Partnerships application, addressed to the then Minister for Transport and Regional Services, the Carnarvon Yacht Club stated that the project:

is well outside the Yacht Club’s financial capabilities and this is the reason why we are now applying in partnership with the Shire to assist with the funds to develop the Public Boat Ramp and Boat Pens.

7.21 However, there was a significant degree of ambiguity in the application in terms of the relationship between the construction of boat pens and the public boat ramp. This is illustrated by Table 7.1.

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844 Barry Haase MP, Federal Member for Kalgoorlie, Regional Partnerships Funding for Carnarvon, Media Release, 28 October 2004.
Table 7.1

<table>
<thead>
<tr>
<th>Combined project indications</th>
<th>Separate project indications</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Shire was listed as a partner that had made a budgetary allocation of $150 000 to the project for which Regional Partnerships funds were being sought. The Department for Planning and Infrastructure was also listed as a partner, with a $150 000 contribution through the Recreational Boating Facilities Grants Scheme.</strong></td>
<td>Attached to the Regional Partnerships application was an extract of the Shire of Carnarvon’s <em>Strategic Plan 2004—2007</em>. The relevant extract included a project titled ‘Recreational Boat Ramp’. The project was described as: Design and construct a recreational boat ramp adjacent to the Carnarvon Yacht Club Marina. Working notes— $150 000 DPI funding approved. Council to endorse Fascine dredging program—March 2004. Council to endorse final design—April/May 2004. Establish Policy &amp; Reserve Fund to meet future dredging costs. The Strategic Plan extract identified that the project would be fully funded in 2004–05 with $150 000 to be contributed by the Department for Planning and Infrastructure and $150 000 from the Shire.</td>
</tr>
<tr>
<td><strong>The expected outcomes from the Regional Partnerships project included:</strong> - Dual lane recreational boat ramp with facilities; and - Pens for 22 deep keel boats completed.</td>
<td><strong>It was stated in the application that ‘the Shire of Carnarvon will own and operate the dual boat ramp as a Shire asset’.</strong></td>
</tr>
<tr>
<td><strong>The budget included $150 000 for dredging and earthworks associated with the boat ramp and a further $150 000 for concrete and breakwater for the ramp.</strong></td>
<td><strong>The plan referred to in the application and attached to it included only the marina site.</strong></td>
</tr>
<tr>
<td><strong>The Business Plan included project time lines that solely related to the marina development.</strong></td>
<td><strong>The Strengths, Weaknesses, Opportunities and Threats analysis stated that:</strong> - The Shire of Carnarvon and the Department for Planning and Infrastructure are proposing to build a double boat ramp on our Southern boundary. - Our greatest threat is that if we cannot arrange a grant to assist us with stage 2 of our Marina within the next 4 months we will miss the chance to be able to construct the Marina at the same time as the public double boat ramp, as without the assistance of the grant it would be outside our current or projected fiscal means, to complete stage 2.</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of Regional Partnerships application submitted by the Carnarvon Yacht Club.
7.22 In its assessment of the project, DOTARS did not seek to resolve this ambiguity. In addition, the department does not have a practice of undertaking site inspections as part of its assessment of projects that have applied for funding. Had it done so, as illustrated by Figure 7.4 it would have been apparent that, whilst the boat ramp site was on adjacent land to the Carnarvon Yacht Club, they are different sites with different owners. The photographs in Figure 7.4 were taken by ANAO during ANAO’s 4 May 2006 site inspection.

**Figure 7.4**

Carnarvon Yacht Club marina development and Shire of Carnarvon boat launching facility development: May 2006

Source: Concept design supplied by Carnarvon Yacht Club, photographs by ANAO.

7.23 As a result of the above shortcomings in due diligence procedures, the department’s advice to the then Parliamentary Secretary was incorrect in that it stated that:

This project will implement Stage 2 of the development of the Carnarvon Recreational Marina by constructing a two lane boat ramp and an additional 22 mooring jetties.

7.24 Upon being provided with a draft Regional Partnerships Funding Agreement, the Carnarvon Yacht Club immediately advised DOTARS that the
department had incorrectly assessed the boat ramp project as being an element of the marina development being undertaken by the Club. Specifically, on 26 January 2005, the Carnarvon Yacht Club advised DOTARS that:

The two lane boat ramp and parking area will actually be under the control of, and project managed by, the Shire of Carnarvon. The Yacht Club will be Project Managing the Marina Stage 2.

7.25 DOTARS amended the Funding Agreement description of the project to be undertaken by the Carnarvon Yacht Club to reflect the funding recipient’s 26 January 2005 advice that the Shire of Carnarvon was responsible for the boat ramp construction. Specifically, the Regional Partnerships Funding Agreement signed with the Carnarvon Yacht Club on 7 February 2005 stated that:

The Project to be undertaken by You is Stage Two of the Carnarvon Recreational Marina development, comprising 12 pens for keel vessels. An adjacent two lane boat ramp with facilities for trailer boats will be managed by the Shire of Carnarvon.

7.26 However, the Funding Agreement did not consistently reflect the advice from the Carnarvon Yacht Club that it was not undertaking the boat ramp development. Specifically:

- the project budget included as an annexure to the Funding Agreement included the $300,000 cost to the Shire of Carnarvon of the recreational boating ramp project;
- the second and third activity milestones included, respectively, earthwork and dredging for both the ramp and the pens, and construction of the boat ramp and jetty; and
- the contracted project outcomes also included the construction of a dual lane recreational boat ramp with facilities (see Figure 7.5).
**Figure 7.5**

Project outcomes and performance measures in Funding Agreement for Regional Partnerships-funded project

<table>
<thead>
<tr>
<th>Project Outcome</th>
<th>Performance Measure</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Dual lane recreational boat ramp with facilities</td>
<td>Completed on time on budget to specifications; Usage rates (vessels launching/week)</td>
</tr>
<tr>
<td>(b) 12 pens for keel vessels</td>
<td>Completed on time on budget to specifications; Usage rates (uptake of pens)</td>
</tr>
<tr>
<td>(c) Improved amenity for local population</td>
<td>User survey</td>
</tr>
<tr>
<td>(d) Improved facility for visitors to region</td>
<td>User survey</td>
</tr>
<tr>
<td>(e) Expansion in water based activities, attractions and events</td>
<td>User survey, press clippings, local government and Department of Sport &amp; Recreation records</td>
</tr>
</tbody>
</table>

Source: Funding Agreement dated 7 February 2005.

7.27 Following consideration of a January 2007 ANAO case study in relation to this project, in March 2007 DOTARS wrote to the Carnarvon Yacht Club and separately to the Shire of Carnarvon regarding the project (see Figure 7.6).

**Figure 7.6**

Request to Shire of Carnarvon for information on construction of the boat ramp and associated partner contributions

The approval for the project was given on the understanding that the marina and the boat ramp were part of one integrated project. The Shire Council’s contribution of $150,000 towards the boat ramp was a significant part of the identified partnership funding that ensured the project met the guidelines.

Given that the marina component of the project is now completed, I am writing to request an update regarding the boat ramp component as managed by the Shire of Carnarvon. Would you please provide me with:

- Updated information regarding the proposed boat ramp and its completion date; and
- Information regarding expenditure by the Shire of Carnarvon ($150,000) and the Department of Planning and Infrastructure ($150,000) on the Regional Partnerships project to construct a two lane boat ramp with facilities for trailer boats.

7.28 The Shire did not respond by the requested date of 10 April 2007. Accordingly, DOTARS wrote again on 7 May 2007, with a response being provided by the Shire on 8 May 2007 (see Figure 7.7).

**Figure 7.7**  
Response to DOTARS request to the Shire of Carnarvon for information on construction of the boat ramp and associated partner contributions

Works on the Carnarvon Boat Ramp were undertaken by the Council using its own funds and monies from the WA Government through Rounds 8 & 10 of the Recreation Facilities Boating Fund. The total budgeted expenditure on the construction of a two lane boat ramp was in the order of $710,920 of which the Council would provide $460,920. To date, the sum of about $519,000 has been spent, most of which has been provided by the Council.

The works undertaken to date involve the construction of a limestone rock retaining wall, and the installation of a sand filled hardstand area using fill from the Carnarvon Marina Project. No progress has been made on the construction of the boat ramp launching facilities at this time.

Advice has been received that the Hon Minister for Planning & Infrastructure has identified the Carnarvon Small Boat Harbour Precinct as suitable for a major tourism and residential development. Whilst this advice is preliminary in nature, indications are that the boat ramp site has been earmarked for substantial development as a tourist complex. Given that the boat ramp land is still within DPI’s area of responsibility, and Council’s inability to attract sufficient funds to complete the project, it is likely that the Council will acquiesce to any development plans as identified by the Minister for this site.

This would lead to the conclusion that it is unlikely that a boat ramp will be constructed on this site, notwithstanding the considerable capital expenditure by the Council to date.

Source: Shire of Carnarvon correspondence to DOTARS dated 8 May 2007.

**ANAO conclusion**

7.29 DOTARS’ assessment of this project did not address the ambiguities in the Regional Partnerships application concerning the scope of the project. Specifically, Regional Partnerships funding was recommended and approved by the then Parliamentary Secretary on the basis of a project that involved construction of additional moorings for 22 keel vessels and a two lane boat ramp. However, the actual project involved additional moorings for 12 keel vessels and no boat ramp.

**Assessment of partnership contributions**

7.30 DOTARS’ incorrect assessment of this project as comprising both the construction of a boat ramp and construction of an additional 22 mooring
berths also resulted in a material error in its assessment of partnership contributions. Specifically, DOTARS’ project assessment provided to the then Parliamentary Secretary in October 2004 stated that the Regional Partnerships bid of $215,660 represented 41 per cent of the cash cost of the project. Table 7.2 reflects the department’s advice on partnership cash contributions to this project.

Table 7.2

DOTARS assessment of cash contributions to the project

<table>
<thead>
<tr>
<th>Entity</th>
<th>Amount $</th>
<th>% of total cash</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regional Partnerships</td>
<td>215,660</td>
<td>41.0%</td>
</tr>
<tr>
<td>Shire of Carnarvon</td>
<td>150,000</td>
<td>28.5%</td>
</tr>
<tr>
<td>Western Australian Department for Planning and Infrastructure</td>
<td>150,000</td>
<td>28.5%</td>
</tr>
<tr>
<td>Carnarvon Yacht Club</td>
<td>5,000</td>
<td>1.0%</td>
</tr>
<tr>
<td>Gascoyne Recreational Fishing Advisory Committee</td>
<td>5,000</td>
<td>1.0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>525,660</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>

Source: DOTARS assessment of the application submitted to the then Parliamentary Secretary, October 2004.

7.31 Table 7.2 shows that the applicant was contributing a negligible amount of cash to the cost of the project. However, in terms of the applicant’s contribution, DOTARS advised the then Parliamentary Secretary that:

The applicant is a significant in-kind contributor. The applicant’s in-kind contribution is realistically costed and represents members and the local community contributing their knowledge and skills in the development of this project.

7.32 The applicant’s in-kind contribution was valued at $50,880, representing nine per cent of total project costs as identified in DOTARS’ project assessment.

7.33 More broadly, in terms of partnership support, DOTARS’ assessment was that:

The partnership support for this project is considered very sound with all three levels of government making significant cash contributions.

7.34 This advice was inaccurate. Specifically, neither the State Government nor the Shire of Carnarvon was making any financial contribution to the
Carnarvon Recreational Marina project. The funds identified in relation to these entities related to the separate project to construct a recreational boat launching facility on adjoining land to the marina.

State Department for Planning and Infrastructure

7.35 DOTARS advised the then Parliamentary Secretary that the Western Australian Department for Planning and Infrastructure was contributing $150,000 to the project. In its application, the Carnarvon Yacht Club identified that these funds were being provided through the Recreational Boating Facilities Scheme.

7.36 The Recreational Boating Facilities Scheme is a Western Australian Government grant programme providing improved boating infrastructure through joint funding of facilities that benefit recreational boat users.845 The Scheme is funded by revenue from recreational boat registration fees.846 The application process and funding rounds are aligned to the financial year.847

7.37 Under this Scheme, funding is available to Local Government Authorities, State Government departments and statutory authorities.848 In this respect, the Carnarvon Yacht Club had, in 1999–2000, unsuccessfully applied for funding under the Recreational Boating Facilities Scheme.849 The application was unsuccessful due to the Carnarvon Yacht Club not being an eligible applicant.

7.38 On 14 August 2003, the State Minister for Planning and Infrastructure, announced an allocation of $150,000 to the Shire of Carnarvon for a boat launching facility when announcing the 2003–04 round of grants.850

7.39 On 21 July 2005, the Acting State Minister for Planning and Infrastructure announced that the Shire of Carnarvon was to receive a further

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845 Department for Planning and Infrastructure, Recreational Boating Facilities Scheme (RBFS) Five Year Review: Final Report, August 2004, p. i.
846 Department for Planning and Infrastructure, Annual Report 2004–05, p. 37.
847 Department for Planning and Infrastructure, Recreational Boating Facilities Scheme (RBFS) Five Year Review: Final Report, op. cit., p. 5.
848 Department for Planning and Infrastructure, Project Information Sheet—Recreational Boating Facilities Scheme.
849 Department for Planning and Infrastructure, Recreational Boating Facilities Scheme (RBFS) Five Year Review: Final Report, op. cit., p. 4.
850 Parliament of Western Australia, Hansard, 14 August 2003, p. 9990.
$200 000 for the construction of the boat ramp, manoeuvring area, trailer park
and associated services as part of the 2005–06 round of grants.\textsuperscript{851}

\textbf{Shire of Carnarvon}

\textit{7.40} As noted above, the recreational boat ramp was included in the Shire of
Carnarvon’s \textit{Strategic Plan 2004–07}, the relevant extract of which was attached
to the Regional Partnerships application. In addition, the Shire’s \textit{Principal
Activities Plan 2004/05 to 2008/2009} (which is publicly available) includes the
recreational boat ramp project as one of the Shire’s major capital projects. This
Plan states that:

\begin{quote}
In 2002 the Department of Planning and Infrastructure (DPI) pronounced their
intent of constructing a land backed wharf in the Carnarvon Boat Harbour
Precinct. That project assumed that the current recreational boat ramp, located
at Boat Harbour, would have to be relocated. The DPI pledged 100\% funding
for the land back wharf and pledged 50\% funding for the new recreational
boat ramp with the Shire of Carnarvon costing the balance. Public consultation
was initiated with locality and logistics now finalised. Final design should be
endorsed by Council in April/May 2004. The locality will be in the near
proximity of the Carnarvon Yacht Club and construction will begin and
finalise in 2004/2005.\textsuperscript{852}
\end{quote}

\textit{7.41} The Plan states that the total cost of the project was estimated to be
$300 000. This was to be funded with $150 000 from the State Government and
$150 000 from the Shire.

\textit{7.42} In total, the Shire of Carnarvon’s boat ramp development project is
valued at $710 920. Table 7.3 summarises the components of this budget.

\begin{flushright}
\textsuperscript{851} John Bowler MLA, Acting Minister for Planning and Infrastructure, \textit{Additional funding approved for
\end{flushright}

\begin{flushright}
\end{flushright}
Table 7.3
Shire of Carnarvon boat ramp development project

<table>
<thead>
<tr>
<th>Element</th>
<th>Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>The construction of the boat ramp which was budgeted for at a total cost of $300 000.</td>
<td>$150 000 from Shire of Carnarvon funds.</td>
</tr>
<tr>
<td></td>
<td>$150 000 come from the Recreational Boating Facilities Scheme, announced on 14 August 2003.</td>
</tr>
<tr>
<td>The construction of the boat ramp manoeuvring area, trailer parking and associated services which was budgeted for at a total cost of $410 290.</td>
<td>$210 920 from Shire of Carnarvon funds.</td>
</tr>
<tr>
<td></td>
<td>$200 000 from the Recreational Boating Facilities Scheme, announced on 21 July 2005.</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$710 920</strong></td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS records, announcements by State Ministers and Minutes of Shire of Carnarvon council meetings.

7.43 DOTARS did not seek or otherwise examine the public records of Council meetings to assure itself concerning the Shire of Carnarvon’s role in the nominated project. By way of comparison, in this respect, ANAO notes that in relation to RP01390 Injune Multi Purpose Centre, when recommending funding not be approved, DOTARS advised the then Parliamentary Secretary that that:

cconcern exists that the applicant still has not put in writing their firm commitment to fund the project to the level indicated in their application. In discussions with the Department the applicant was requested to supply evidence, such as council minutes, showing the financial commitment to this project; however, this has not been supplied.

7.44 At its meeting of 20 December 2005, the Shire of Carnarvon considered the results of the tender process for the recreational boat ramp project. The Shire’s deliberations were focused on two issues:

- the tendered costs exceeded the budget allocation by a substantial sum; and
- the dredging of the Carnarvon Yacht Club marina and boat ramp access channel was to provide the fill for the boat ramp carpark and the timing of the two projects was important due to the risk of the hardstand created by the dredging spoils being undermined by various environmental factors.853

853 Shire of Carnarvon, Minutes of the Ordinary Meeting of Council Held in the Council Chambers, Francis Street, Carnarvon on Tuesday 20 December 2005, pp. 35–40.
7.45 Council resolved to not accept any of the tenders. Instead, it was decided to let a contract for construction and drainage works for the hardstand of the proposed boat ramp and defer the balance of the project works to the 2006–07 Budget to provide time to address design, timing, financial and environmental issues. The construction and drainage works for the hardstand were due to reach practical completion stage by 28 February 2006, but this was extended by Council at its July 2006 meeting.854

7.46 In finalising its project to receive the final instalment of Regional Partnerships funds, on 22 March 2006 the Carnarvon Yacht Club provided DOTARS with a signed statement from the Shire of Carnarvon concerning expenditure on its boat ramp project. As at 12 March 2006, expenditure on the Shire’s boat ramp project was reported as being $419 634. In terms of physical status, the Shire’s statement advised that:

- Project currently incomplete.
- Hardstand and armour wall protection installed.
- Project finalisation delayed and will encroach on new financial year.
- Independent audit to be conducted upon finalisation. Shire to evaluate key outcomes upon finalisation.

7.47 As noted above in Figure 7.7, the Shire of Carnarvon has confirmed the overall budget for its boat ramp development project of $710 920, but that the boat ramp project is unlikely to be completed.

**ANAO conclusion**

7.48 DOTARS advised the then Parliamentary Secretary that partnership support for this project was ‘very sound’ on the basis that all three levels of government were making significant cash contributions. However, State and local government were not, in fact, making any cash contributions to the Carnarvon Yacht Club’s Stage 2 marina development. Instead, the Regional Partnerships funds were to be the only cash contribution from any level of government.

7.49 The available evidence is that the only parties that were actually expected to contribute any cash to the project were the applicant ($5000 or two per cent) and the Regional Partnerships Programme ($215 660 or 98 per

---

cent). Accordingly, there was no basis for DOTARS’ assessment that partnership support was ‘very sound’.

Management of partnership contributions through the Funding Agreement

7.50 Because of the errors included in DOTARS’ analysis of the project scope and associated partnership contributions, the Funding Agreement specified a total project budget of $547 226 comprising $215 660 in Regional Partnerships funds (plus GST of $21 566), together with partner cash contributions aggregating to $310 000.

Confirmation of partnership contributions

7.51 Clause 6 of the Funding Agreement addressed the administration of partner contributions. Clause 6.1 stated that:

> It is a condition precedent to the payment of Funds under this Agreement that You must get people (other than Us), as identified in Item 2 of the Schedule, to provide Us with satisfactory written evidence that they will provide the Other Contributions to You, including the amounts to be provided, their due dates and the terms and conditions of the provision of the Other Contributions. The terms and conditions on which these Other Contributions are to be provided must be satisfactory to Us.

7.52 The Carnarvon Yacht Club did not provide written confirmation that the Shire of Carnarvon, the State Department for Planning and Infrastructure or the State Department of Fisheries would provide to the Club the contributions specified in the Funding Agreement. Clause 6.2 of the Funding Agreement provided that:

> The written confirmation referred to in subclause 6.1 must be provided to Us within 20 Business Days of the Date of this Agreement, failing which this Agreement will be treated as void and as never having been entered into.

7.53 Notwithstanding the Carnarvon Yacht Club’s failure to voluntarily provide written confirmation of partner contributions as required by Clause 6.1, DOTARS did not seek any information or advice from the Carnarvon Yacht Club on the partnership contributions specified in the Funding Agreement. Had it sought such information or advice, DOTARS would have become aware of the overstated partnership contributions it had included in its assessment provided to the then Parliamentary Secretary and in the Funding Agreement subsequently prepared by the DOTARS Western Australia Regional Office.
7.54 In respect of the absence of partnership contributions to the Carnarvon Recreational Marina project, the audit report submitted by the Carnarvon Yacht Club to support the final payment of Regional Partnerships funds stated as follows:

It is understood that the project undertaken was limited after the agreement was signed to “Stage 2” and then the balance of the project was made the responsibility of the Shire. This then relieved the Yacht Club of liability under paragraph 6 [of the Funding Agreement]. It is understood that the Shire have provided evidence of the extent of their involvement.

Acquittal of partnership contributions

7.55 To enable the final payment of $4160 (plus GST) in Regional Partnerships funds to be made, on 24 March 2006 the Carnarvon Yacht Club provided DOTARS with an audit report and supporting financial information for the period 1 February 2005 to 31 March 2006. Also on this date, the Carnarvon Yacht Club provided DOTARS with a letter from the Club’s Commodore concerning the completion of the project (see paragraph 7.5) and a signed statement from the Shire of Carnarvon concerning expenditure on its boat ramp project (see paragraph 7.43).

7.56 The profit and loss statement provided by the Carnarvon Yacht Club stated that total expenditure on the project was $246 174, with income of $242 112. However, the funds received (and the expenditure) included $25 840 from the Shire of Carnarvon which the audit report stated was:

a direct reimbursement for concrete work paid for by the project.

7.57 Accordingly, these amounts should not be included in the financial acquittal of the Carnarvon Yacht Club’s Recreational Marina project. Table 7.4 shows this analysis. Table 7.4 also shows that the Regional Partnerships Programme funded 98 per cent of the costs of the Carnarvon Recreational Marina project. The only other party that made any financial contribution to the project was the Carnarvon Yacht Club, with $4062 (compared to the $5000 specified in the Funding Agreement). In relation to the remaining partnership contributions specified in the Funding Agreement:

- as outlined above, the $150 000 from the Western Australian Department for Planning and Infrastructure related to the Shire of Carnarvon’s boat ramp project, not the Carnarvon Recreational Marina project;
as also outlined above, the $150 000 from the Shire of Carnarvon also related to its boat ramp project, not the Carnarvon Recreational Marina project; and

- the $5000 attributed to the Gascoyne Recreational Fisheries Advisory Committee/Department of Fisheries was not identified as having been received. In its application, the Carnarvon Yacht Club identified that these funds were to come from the Recreational Fishing Fund.855

855 The Recreational Fishing Fund was established by the Western Australian Fish Resources Management Act 1994. This Act establishes the receipts that are to be credited to the Fund and the purposes for which the amounts in the Fund may be applied.
### Table 7.4

**Adjusted financial acquittal**

<table>
<thead>
<tr>
<th></th>
<th>Audited profit and loss statement $</th>
<th>Adjusted $</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Regional Partnerships</td>
<td>215 660</td>
<td>215 660</td>
</tr>
<tr>
<td>Shire of Carnarvon reimbursement</td>
<td>25 840</td>
<td></td>
</tr>
<tr>
<td>Interest</td>
<td>612</td>
<td>612</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>242 112</td>
<td>216 272</td>
</tr>
<tr>
<td><strong>Expenditure:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accountancy fees</td>
<td>300</td>
<td>300</td>
</tr>
<tr>
<td>Bank charges</td>
<td>82</td>
<td>82</td>
</tr>
<tr>
<td>Banners</td>
<td>213</td>
<td>213</td>
</tr>
<tr>
<td>Consultancy &amp; surveying</td>
<td>6 985</td>
<td>6 985</td>
</tr>
<tr>
<td>Contract work</td>
<td>62 446</td>
<td>62 446</td>
</tr>
<tr>
<td>Electricity supply</td>
<td>5 135</td>
<td>5 135</td>
</tr>
<tr>
<td>Fees &amp; permits</td>
<td>138</td>
<td>138</td>
</tr>
<tr>
<td>Fencing</td>
<td>4 771</td>
<td>4 771</td>
</tr>
<tr>
<td>Fire protection equipment</td>
<td>137</td>
<td>137</td>
</tr>
<tr>
<td>Freight &amp; cartage</td>
<td>137</td>
<td>137</td>
</tr>
<tr>
<td>Fuel &amp; oil</td>
<td>1 972</td>
<td>1 972</td>
</tr>
<tr>
<td>Hire of plant &amp; equipment</td>
<td>9 050</td>
<td>9 050</td>
</tr>
<tr>
<td>Insurance</td>
<td>1 532</td>
<td>1 532</td>
</tr>
<tr>
<td>Landscaping expenses</td>
<td>3 410</td>
<td>3 410</td>
</tr>
<tr>
<td>Materials</td>
<td>140 804</td>
<td>114 964(^{A})</td>
</tr>
<tr>
<td>Printing &amp; stationery &amp; postage</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td>Protective clothing</td>
<td>22</td>
<td>22</td>
</tr>
<tr>
<td>Repairs &amp; maintenance plant &amp; equipment</td>
<td>1 653</td>
<td>1 653</td>
</tr>
<tr>
<td>Tools</td>
<td>1 937</td>
<td>1 937</td>
</tr>
<tr>
<td>Travelling expenses</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>Water supply</td>
<td>5 335</td>
<td>5 335</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>246 174</td>
<td>220 334</td>
</tr>
<tr>
<td><strong>Non-Regional Partnerships contribution to project costs</strong></td>
<td>4 062</td>
<td>4 062</td>
</tr>
</tbody>
</table>

**Note:**

\(^{A}\) See paragraph 7.56.

Source: ANAO analysis of DOTARS records.
ANAO conclusion

7.58 The shortcomings in DOTARS’ assessment of partnership contributions were exacerbated by the department not effectively administering the partnership contribution clauses of the Funding Agreement. In this respect, the Funding Agreement provided that it would be treated as void if written confirmation of the partnership contributions was not provided by the Carnarvon Yacht Club to DOTARS within 20 Business Days of the Funding Agreement being signed. Despite such confirmation not being provided, DOTARS did not seek any information or advice from the Carnarvon Yacht Club on the partnership contributions specified in the Funding Agreement.

7.59 In recommending that this project be approved for funding, DOTARS advised the then Parliamentary Secretary that partnership support for the project was very sound with all three levels of government making significant cash contributions. However, the Regional Partnerships Programme funded 98 per cent of the costs of the Carnarvon Recreational Marina project. The only other party that made any financial contribution to the project was the Carnarvon Yacht Club, with $4062 (compared to the $5000 specified in the Funding Agreement). This is illustrated by Figure 7.8.

Figure 7.8
Partnership contributions: DOTARS assessment versus actual as acquitted by the funding recipient

Source: ANAO analysis of DOTARS records.
8. Country Homes and Cabins

This case study examines RP01364 involving a project to construct a facility in Central Queensland for the production of relocatable houses to help address a shortage of housing. On the basis of departmental advice that the application did not meet a number of the Programme assessment criteria, funding was initially not approved. Following representations from the local Federal Member, this decision was later reversed. The review of the initial decision to not approve funding did not proceed in the manner provided for by the published Programme Guidelines and documented internal procedures.

The Regional Partnerships Programme application

8.1 On 15 December 2003, the Central Queensland ACC (CQACC) recorded receipt of an Expression of Interest for Regional Partnerships funding of $500,000 (plus GST) for a project titled ‘Country Homes and Cabins’. For a total cost of $1,572,826, the project was to involve the construction of a transportable house building factory in a production line type environment. This was to be achieved by building a shed large enough to fit 12 houses at various stages of construction, with houses to be constructed in one piece and delivered furnished (including kitchens, air conditioners, floor coverings and painted).

8.2 The CQACC records of this project did not include documentation concerning its consideration of the Expression of Interest.

8.3 A draft Regional Partnerships application for funding was provided to the CQACC on 22 July 2004, by a consultant engaged by the applicant, LTH Investments Qld Pty Ltd ATF Hawkins Family Trust (LTH Investments). The consultant provided the draft application to the CQACC so as to obtain feedback on it.

8.4 On 13 August 2004, the DOTARS North Queensland Regional Office received an electronic copy of a Regional Partnerships application for funding dated 12 August 2004. The hard copy of the application, received on 20 August 2004, included the following supporting information:

- a Business Plan dated July 2004 for Country Homes and Kitchens (sic);
- a copy of the report of the Blackwater Housing Forum;
ten letters of support including from the local Federal Member, the local State Member and the Emerald, Jericho and Bauhinia Shire Councils;

- cash flow projections for 2004–05 and 2005–06;
- a budget for the cost of the project;
- a map of the Central Highlands areas of Queensland; and
- financial reports for Lindsay’s Kitchens Pty Ltd (Lindsay’s Kitchens) for 2002–03, 2001–02 and 2000–01, an existing business whose managing director was, according to the above-mentioned Business Plan, the sole director and shareholder of LTH Investments. The Business Plan stated that Country Homes and Cabins would be managed as a separate business to Lindsay’s Kitchens.

8.5 According to the Business Plan, the house building facility would be constructed over four stages, namely:

- land development—the Business Plan stated that the total cost of the purchase and development of a two hectare block of land was $345 000 but that this was not part of the project costing as it was considered a separate property development enterprise of LTH Investments;

- building development, to take the form of a steel frame shed 25 metres wide, 156 metres long and 6 metres high at the walls, with a 9 metre skillion running the full length of the shed. It was to be located on an all weather surface yard. In addition to the house building factory, also located on site would be an administration building and an amenity building, to be produced by Country Homes and Cabins similar to the house prototypes;

- factory fit out involving dividing the shed interior into 13 12-metre long bays with each bay capable of holding one house. A mobile gantry with lifting cranes at each end would be used to lift parts of the houses during construction. The skillion would be fitted out with racks to hold the building materials with relevant material held adjacent to where it would be used. In some of the skillion bays, jigs would be set up for framing etcetera; and

- transportation/house installation equipment with houses to be transported on a specially designed trailer pulled by a prime mover with very slow gears and fitted with a generator to power welders and...
other power tools. The houses would be loaded onto transporting beams with a hydraulic power pac to be used to lift the houses onto the truck and take them off when on site. In addition, there would be a second truck fitted with a lifting crane to carry a bob cat and attachments, container for gravel and concrete mixer.

Project assessment

8.6 Departmental assessment of the application was finalised on 11 February 2005. On this date, National Office provided the then Parliamentary Secretary with a package of 12 recommended projects and 10 not recommended projects. The Country Homes and Cabins project was one of the not recommended projects. The summary advice to the then Parliamentary Secretary was that:

This project will result in the construction of a facility in Emerald where prefabricated accommodation will be built to address the shortage of housing in the region. This project is not recommended for funding as it does not meet the criteria of outcomes, competitive neutrality and project viability.

Outcomes

8.7 A key issue raised by DOTARS in its assessment against the outcomes criterion and the project viability criterion was the difficulty in recruiting and retaining skilled tradespeople in order to realise the projected employment outcomes. On this basis, DOTARS concluded that the project was unlikely to deliver the nominated employment outcomes and did not satisfy this assessment criterion.

8.8 However, an issue not addressed in the assessment and recommendation was whether the project satisfied the Programme eligibility requirements. In this respect, the project was ineligible for funding approval under the amended Guidelines approved by the acting Minister in April 2004 because Council approvals had not yet been obtained and the applicant did not satisfy the ‘exception’ tests advised to the acting Minister by DOTARS.\footnote{Even had the project been eligible for funding, the first payment of Regional Partnerships funds should not have been made until Council approvals had been obtained. However, the Funding Agreement was drafted so that the first payment was to be made for purposes that included obtaining approval of building plans. As a result, $250 000 (plus GST) in Regional Partnerships funds were paid in November 2005. Advice to DOTARS is that Council approvals were obtained in September 2006.}

\footnotemark
**Project viability**

8.9 Project viability was assessed as being a high risk based on competition and sustainability concerns. However, the project viability risk assessment did not address shortcomings in the project budget.

8.10 The project budget nominated in the application for funding was $1 571 836. The key elements of the budgeted costs of the project, and proposed sources of funds, were outlined in an attachment to the application entitled Development Budget (see Table 8.1).

**Table 8.1**

Project budget as set out in Development Budget attachment to Regional Partnerships application

<table>
<thead>
<tr>
<th>Item</th>
<th>Cost ($)</th>
<th>Cash from applicant/related parties</th>
<th>Borrowings from applicant/related party</th>
<th>Borrowings</th>
<th>Regional Partnerships</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shed</td>
<td>733 800</td>
<td>209 800</td>
<td>24 000</td>
<td>Nil</td>
<td>500 000</td>
</tr>
<tr>
<td>Fit out</td>
<td>125 690</td>
<td>99 590</td>
<td>26 100</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Yard equipment</td>
<td>61 000</td>
<td>6 500</td>
<td>54 500</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Transport equipment</td>
<td>427 646</td>
<td>19 510</td>
<td>106 330</td>
<td>301 806</td>
<td>Nil</td>
</tr>
<tr>
<td>Building plans</td>
<td>8 000</td>
<td>8 000</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Labour on costs</td>
<td>25 700</td>
<td>25 700</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Inventory</td>
<td>130 000</td>
<td>130 000</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td>Other costs</td>
<td>60 000</td>
<td>60 000</td>
<td>Nil</td>
<td>Nil</td>
<td>Nil</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1 571 836</strong></td>
<td><strong>559 100</strong></td>
<td><strong>210 930</strong></td>
<td><strong>301 806</strong></td>
<td><strong>500 000</strong></td>
</tr>
</tbody>
</table>

**Total funding**

<table>
<thead>
<tr>
<th></th>
<th>1 571 836</th>
</tr>
</thead>
</table>

**Note A** This amount was incorrectly identified as an in-kind contribution in the application and departmental assessment (see further discussion at paragraph 8.14, first dot point).

Source: ANAO analysis of Regional Partnerships application for funding, 12 August 2004.

8.11 Supporting documentation such as quotes/cost estimates were attached for $979 626 (62 per cent) of the $1 571 836 in project cash costs. However, there were a series of anomalies in the project budget that were not identified and investigated by DOTARS. Specifically:
no information was sought to support the remaining $592,210 in cost estimates included in the project budget. For example, the Business Plan stated that the administration building and amenity building were to be produced by Country Homes and Cabins similar to the house prototypes. However, the project budget attached to the Regional Partnerships application for funding stated that these two buildings would cost $46,500 in materials, $17,000 in labour and $10,000 in equipment with this to be funded by $27,000 in cash from the applicant and $46,500 from the Regional Partnerships Programme. No supporting information was provided to demonstrate how these costs were calculated, in order to address transfer pricing and other risks;

- an amount of $390,000 was included for the materials needed to construct the shed in kit form. Attached to the application was a 14 July 2004 estimate for the cost of the building of between $360,000 and $390,000 excluding GST. However, this estimate stated that a firm price was not yet available as engineering calculations on design of purlins had not yet been completed;

- the purchase of the prime mover was budgeted to cost $125,000 yet the quote attached to the application was for a purchase cost of $120,000;

- a quote was attached for the purchase of a yard fork lift at a cost of $26,500. Yet the project budget stated that this cost would be funded by a $26,500 in-kind contribution from the applicant;

- payments to the consultants employed to assist with preparing the Regional Partnerships application for funding were included in the project budget at a cost of $12,000—such costs are not eligible for funding under the Regional Partnerships Guidelines; and

- the project was to involve construction of a steel shed in an environment of rapidly increasing construction costs. The quotes attached to the application were all obtained in July 2004, but building construction was not to commence until January 2005, to be completed in March 2005 with delivery of transport equipment in April 2005. The

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857 For example, the Rawlinsons Australian Construction Handbook, the leading authority on the various aspects of construction costs in Australia, stated in relation to Queensland that the expectation at the commencement of 2004 was that, following construction cost rises of 15 per cent to 25 per cent in 2003, the level of construction activity in 2004 would sustain continued upwards pressure on building costs until at least 2005. Source: Rawlinsons Australian Construction Handbook, Edition 22. 2004, p. xiii.
project budget included no allowance for cost increases and DOTARS did not seek to establish how this risk would be managed.  

8.12 In relation to this last point, on 7 December 2004, the consultant that was assisting the applicant advised the Regional Office that:

In terms of total financial cost of the project, based on the rise in steel and other material cost, [the applicant] estimates that the construction costs would have increased at least 10%. Another 10% increase is forecast in February 2005. As another example, small tooling is now expected to reach $20 000 from $5 000.

The accommodation block is estimated to cost approximately $150 000.  

The estimate of total project cost excluded the land. In hindsight, the true cost of the project needs to include the land as with a purpose built shed on it, [the applicant] will be able to do little else with in [sic] and so it is a cost to him.

With the above points in mind, I believe the true total cost of the project would now be closer to $2.0 million.

With higher establishment cost of the project, if [Regional Partnerships] funding is reduced from the $500 000, it is inevitable that the project milestones will be delayed.

8.13 Notwithstanding this advice, the project continued to be assessed by DOTARS based on the project cost estimate of $1 571 836 set out in the August 2004 application. That is, no consideration was given to the cost increases advised to the department.

8.14 There were also various anomalies in the cash flow projections provided as an attachment to the Regional Partnerships application that were not addressed by DOTARS. For example:

- apart from revenue from house sales and GST income, the only projected receipts disclosed was $900 000 in January 2005 as ‘Loans/Rebates received’. Allowing for the fact that $500 000 in Regional Partnerships grant funding was budgeted to be received in January 2005, this was inconsistent with the $512 736 cash contributions

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858 For example, the 12 July 2004 quote of $154 406 (plus GST) for the trailer was stated to be firm for 60 days and the 12 July 2004 quote of $26 500 (plus GST) for the yard fork lift was stated to be valid for 30 days.

859 This element had been added to the project subsequent to the Regional Partnerships application being submitted, as a proposed solution to the accommodation requirements of adult apprentices.

860 The same figures were also used to develop the project budget included in the Funding Agreement that was signed in October 2005, more than 15 months after the quotes had been obtained.
that were proposed to be raised through sources other than Regional Partnerships funding and the applicant’s working capital. For example, the cash flow projections included no funds against the line ‘Transfer from Lindsay Kitchens’ notwithstanding that the detailed project budget included with the application indicated that $210,930 was to come from that source. In this respect, the completed Regional Partnerships application form was internally inconsistent in that the Project Budget table identified $210,930 as an in-kind contribution relating to materials and equipment hire/lease, whereas the table of partner contributions identified that amount as being cash borrowings from a related company. The Development Budget at Appendix V to the application showed that a significant proportion of that amount actually related to part-contributions to the cost of purchasing major items of transport equipment, including the prime mover, second truck and the bob cat, with the remaining cost proposed to be met from either commercial borrowings or the applicant’s working capital. On that basis, the contributions must actually relate to cash borrowings from Lindsay’s Kitchens. Despite this, DOTARS assessed the application on the basis that the $210,930 contribution from Lindsay’s Kitchens was to be in-kind rather than cash;

- although the Development Budget included $301,806 in equipment finance for the purchase of the prime mover, specialised trailer, bob cat and hydraulic power pac, the cash flow projections stated that the $302,000 in plant would be financed through hire/purchase or leasing. As a result, no capital outlay for these items was budgeted. Instead, monthly finance costs were budgeted to commence in January 2005. Despite this, DOTARS did not address the question of why monthly outlays on equipment leases that the cash flow projections showed would extend beyond the life of the project for which Regional Partnerships funds were being sought were included as a contribution to the project;

- in addition to including monthly finance costs on a $302,000 hire/purchase or leasing arrangement for plant, the projected cash flows included a separate line of cash outflows relating to payments of the principal and interest on a loan of $520,000 over ten years at eight per cent interest, commencing in March 2005. However, neither the Business Plan nor the Regional Partnerships application identified any borrowings in connection with the project (apart from the
the projected cash flows included expenditure of $285,000 between July 2004 and September 2004 for the purchase and development of the land. This was inconsistent with the Business Plan statement that the cost of purchasing and developing the block was $345,000 and that this would be a ‘separate enterprise of LTH Investments—property development’; and

excluding the land development costs, the remaining non-operating expenditure items identified in the cash flow projections comprised fencing ($19,000), salary and wages for fill and the yard ($24,000), emergency water supply ($8,800), truck purchase ($10,000) and building materials ($607,510). The total of these items ($669,310) fell well short of the project cash budget of $1,571,836 (inclusive of the $210,930 related party borrowings). Noticeable exclusions in the expenses identified in the projected cash flows were the cost of purchasing the major items of transport equipment, fit out costs for the factory and the costs of the office building and amenity building.

**ANAQO conclusion**

8.15 Project viability was assessed by DOTARS as being high risk due to concerns about competition and sustainability risks. However, project viability risks relating to the cost of the project and its forecast cash flows were not examined by DOTARS, notwithstanding that the documented internal procedures required that such analysis be undertaken. Based on the available documentation, there are considerable doubts about the validity of substantial elements of the project cost budget as well as the sources and application of funds for the project (including Regional Partnerships funds). In this context, significant and relevant risks were not identified in the advice provided to the then Parliamentary Secretary as the basis for making his decision.

**Partnerships**

8.16 According to the August 2004 Regional Partnerships application, the project was proposed to be financed as follows:

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861 As noted, the consultant engaged by LTH Investments advised DOTARS in December 2004 that it now considered that the land costs should now be included. However, the projected cash flows for the project submitted to DOTARS with the Regional Partnerships application in August 2004 had already included these costs at a different valuation to those identified in the Business Plan.
8.17 Following discussions between DOTARS and the applicant’s consultant, an amended application was provided to the department in December 2004 with the amount of Regional Partnerships funding sought reduced from $500 000 to $375 000. The working capital contribution from the applicant was increased from $559 100 to $684 100 so as to compensate for the $125 000 reduction in Regional Partnerships funds. The amended application stated that the applicant’s working capital contribution of $684 100 had been received.

8.18 In the project assessment provided to the then Parliamentary Secretary, DOTARS advised that the application partially satisfied the partnerships and support assessment criterion. The then Parliamentary Secretary was advised that all partner contributions were being provided by the applicant, LTH Investments. This was notwithstanding the fact that the in-kind contribution was actually cash borrowings that were to come from a related entity, the separate business of Lindsay’s Kitchens. In this respect, Applied Financial Diagnostics has advised ANAO that related party loans raise questions about the capital structure of a company and the transparency of dealings with related parties. DOTARS did not enquire into these matters as part of its assessment of the merits of public money being invested in the Country Homes and Cabins project.

8.19 In addition, the department had incorrectly added the extra $125 000 in funds that were to come from the applicant’s working capital to the $301 806 to be raised by the applicant through a finance company (to make an amount of $426 806) rather than to the amount that was to come from the applicant’s own working capital. The assessment did not advise the then Parliamentary

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To assist with analysis of this and a number of other Regional Partnerships projects, ANAO engaged treasury specialists Applied Financial Diagnostics Pty Ltd to provide advice on financial risks (including viability risks).
Secretary that these two amounts were reportedly being obtained by the applicant from different sources.

8.20 The assessment also did not address whether alternative sources of funding had been exhausted. In particular, no enquiries were documented by the Regional Office or National Office as to whether commercial funding sources (apart from equipment finance) had been exhausted. This was notwithstanding the fact that the then applicable Internal Procedures Manual required that this issue be addressed.\(^{863}\) In this context, as noted above at paragraph 8.14, the cash flow projections attached to the project indicated that the applicant was borrowing funds in the order of $520 000 in connection with this project.

8.21 In addition, DOTARS’ project assessment did not address the status of the partnership contributions. In particular:

- both the original August 2004 application and December 2004 amended application stated that equipment finance of $301 806 was in negotiation. However, during the six months the project was being assessed by DOTARS, the department did not seek to obtain information from the applicant demonstrating that these negotiations had been successful and, if so, the terms and conditions on which equipment finance would be provided (noting that the financial projections provided with the application had made assumptions about the costs of servicing a hire purchase/lease for equipment);

- $210 930 in borrowed capital was to come from Lindsay’s Kitchens. This contribution was said to be committed. However, Lindsay’s Kitchens’ 30 June 2002 balance sheet, also attached to the Regional Partnerships application, showed that its working capital at that time was $1 329, which was insufficient to support a contribution of $210 930 to the new venture Country Homes and Cabins; and

- under the original August 2004 application, $559 100 in working capital was to come from the applicant, LTH Investments. The application said that this contribution had been received. However, no balance sheet or bank statements relating to LTH Investments were obtained by DOTARS in order to demonstrate that this financial contribution had been received and was available for the project. The cash flow projections showed an opening bank balance on 1 July 2004 of $400 000,

but $285 000 was budgeted for land purchase and development costs, leaving only $115 000 available for ongoing operations and the project that was the subject of the Regional Partnerships application for funding.

**ANAO conclusion**

8.22 The departmental assessment against the partnerships and support criterion was deficient in that it did not address whether alternative sources of funding had been exhausted and did not examine and assess that status of nominated partner contributions.

**Applicant viability**

8.23 According to information received by DOTARS on 5 May 2005, LTH Investments was started in about April 2004 to undertake property development and was identified as the business entity to run the house building business.

8.24 As noted, attached to the August 2004 Regional Partnerships application were financial statements for three financial years (but not the most recently completed year, 2003–04) for the related business, Lindsay’s Kitchens. DOTARS finalised its assessment of the project on 11 February 2005 without seeking to obtain a copy of the 2003–04 financial statements. As noted, DOTARS also did not seek a copy of recent financial statements for the actual applicant (LTH Investments) or the related family trust.

**ANAO conclusion**

8.25 DOTARS’ assessment of applicant viability was also deficient. In particular, the department advised the then Parliamentary Secretary that the applicant represented a low viability risk, notwithstanding that no information had been obtained concerning the financial position and performance of the entity that had submitted the Regional Partnerships application for funding.

**ACC support**

8.26 On 8 December 2004, the Executive Officer of the CQACC advised the North Queensland Regional Office that concerns were held over issues that would impact on the overall validity of the project and its projected outcomes. Notwithstanding the 8 December 2004 advice to the Regional Office, the CQACC recommended the project and rated it as a high priority, as was advised to the then Parliamentary Secretary by DOTARS in February 2005. In July 2007, DOTARS advised ANAO that:
The Department’s assessment report, as per the brief to the Parliamentary Secretary, reflected the ACC’s comments under ‘Project Viability’, noting that the project is a high risk in regard to competition and sustainability. The assessment also noted that the ACC recommended the project and rated it as a high priority for its region.

**Initial decision not to approve funding**

8.27 On 18 February 2005, the then Parliamentary Secretary signed the DOTARS project assessment, agreeing with the department’s recommendation that funding not be approved for the Country Homes and Cabins project (see Figure 8.1).

**Figure 8.1**

Record of Parliamentary Secretary’s decision not to approve funding

![Source: DOTARS project assessment provided to the then Parliamentary Secretary on 11 February 2005.](image)

**Advice provided to the local Federal Member of the decision not to approve funding**

8.28 On 18 February 2005 the Office of the then Parliamentary Secretary advised the local Federal Member that funding had not been approved for the Country Homes and Cabins project (see Figure 8.2).
Figure 8.2
Record of advice provided to local Federal Member of decision not to approve funding

<table>
<thead>
<tr>
<th>RP No</th>
<th>Organisation Name</th>
<th>Project Title</th>
<th>Location</th>
<th>State</th>
<th>Status</th>
<th>ACC and Rating</th>
<th>Summary of Project and Justification for Recommendation</th>
<th>RP Bid (GST incl)</th>
<th>Total Project Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>RP01241</td>
<td>Nambucca Shire Council</td>
<td>Nambucca Heads Town Centre Upgrade</td>
<td>NAMBUMA</td>
<td>NSW</td>
<td>Cooper</td>
<td>Australian Holiday Coast ACC - 3 Medium Priority</td>
<td>This project will repurpose Nambucca Heads Town Centre with RP funding being used to cover the cost of survey, including court services, street furniture, drainage, lighting and electrical works. A previous application was denied, which was assessed and not recommended. The applicant has now submitted a new application, which is not recommended at the rate of cost. The rate of cost is not sufficiently addressed and the application is seen as seeking funds that are, or could be perceived as cost shifting from State and Local Government. Also, the applicant has not demonstrated value for money by providing quotations or other standard cost estimates to support the budget.</td>
<td>$0 (Adj amount: $132,108)</td>
<td>$330,250</td>
</tr>
<tr>
<td>RP01171</td>
<td>Deniliquen Council</td>
<td>Deniliquen Tourist Drive</td>
<td>DENILIQUIN</td>
<td>NSW</td>
<td>Ferrer</td>
<td>Central Murray ACC - 2 Low Priority</td>
<td>This project involves the development of a tourist drive through the town of Deniliquen. The project is assessed as not recommended due to the lack of cost justification by the applicant, and the demonstration of need or likelihood of achieving planned outcomes.</td>
<td>$0 (Adj amount: $3,950)</td>
<td>$11,850</td>
</tr>
<tr>
<td>RP01235</td>
<td>Gulargambone RRC</td>
<td>Gulargambone Community Centre – Isaacs Library</td>
<td>GULARGAMBONE</td>
<td>NSW</td>
<td>Goyder</td>
<td>Crane Development and Employment ACC - 4 High Priority</td>
<td>This project involves the development of a community centre in Gulargambone. The project is assessed as not recommended due to the lack of cost justification by the applicant, and the demonstration of need or likelihood of achieving planned outcomes.</td>
<td>$0 (Adj amount: $74,700)</td>
<td>$24,700</td>
</tr>
<tr>
<td>RP01366</td>
<td>QLD Forests Qld Pty Ltd</td>
<td>Country Homes and Cottages - Emerald</td>
<td>EMERALD</td>
<td>QLD</td>
<td>Marama</td>
<td>Central Queensland ACC - 4 High Priority</td>
<td>This project involves the development of a country homes and cottages in Emerald. The project is assessed as not recommended due to the lack of cost justification by the applicant, and the demonstration of need or likelihood of achieving planned outcomes.</td>
<td>$0 (Adj amount: $175,000)</td>
<td>$1,571,836</td>
</tr>
</tbody>
</table>

Source: DOTARS records.
8.29 Four days later, on 22 February 2005, the Departmental Liaison Officer to the then Parliamentary Secretary’s Office informed DOTARS National Office that, in accordance with the department’s recommendation, funding had not been approved for six projects, including Country Homes and Cabins (see Figure 8.3). At this time, National Office was advised that the department could now write to the unsuccessful applicants (in accordance with the documented Programme procedures).

**Figure 8.3**

Record of advice to the department that project not approved and applicant to be informed of this decision

<table>
<thead>
<tr>
<th align="center">The following <strong>not recommended</strong> projects have also <strong>not been approved</strong>. The Department can now write to the unsuccessful applicants.</th>
</tr>
</thead>
<tbody>
<tr>
<td align="center">RP01242 Nambucca Shire Council - Nambucca Heads Town Centre Upgrade</td>
</tr>
<tr>
<td align="center">RP01171 Deniliquin Council - Deniliquin Tourist Drive</td>
</tr>
<tr>
<td align="center">RP01235 Gulargambone Rural Transaction Centre - Gulargambone Community Motel Feasibility Study</td>
</tr>
<tr>
<td align="center">RP01384 LTH Investments QLD Pty Ltd - Country Homes and Cabins (Emerald)</td>
</tr>
<tr>
<td align="center">RP01149 Good Beginnings Australia Ltd - Southern Cairns Connect</td>
</tr>
<tr>
<td align="center">RP01444 The Corporation of the City of Port Augusta - Outdoor Activity Business Centre Development</td>
</tr>
</tbody>
</table>

I will fax through the signed-off assessments.

Source: DOTARS records.

**Request for a review of the decision not to approve funding**

8.30 The process for seeking a review of a decision not to approve funding and the manner in which such reviews will be undertaken has been outlined in the Internal Procedures Manual and disclosed on the DOTARS Regional Partnerships website. The July 2006 and July 2007 versions of the Regional Partnerships Programme Guidelines now also provide detail regarding the review process (previous versions of the Guidelines had included little detail in this respect, with advice of the review process being provided to applicants through Fact Sheets available from DOTARS’ website). For example, the July 2007 Guidelines state that:

Applicants who are unsuccessful or have a lower level of funding approved than that requested, can ask to have the assessment reviewed. The review will be conducted by Departmental staff who were not involved in the initial assessment of the project. To be eligible for a review, applicants must write to the Department within six weeks of receiving the letter advising them of the outcome of their application.864

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8.31 At the time the County Homes and Cabins application was assessed and funding not approved, both the Review of Ministerial Decision Fact Sheet available through the DOTARS website and the department’s Internal Procedures Manual specified three threshold criteria that were required to be met before a review would be undertaken.

8.32 The first two criteria were procedural in that they specified that the request for a review must be made in writing to DOTARS National Office and that the request must be made within 12 weeks of being advised of the Ministerial decision (by letter from the DOTARS Regional Office).

8.33 The third criterion, as set out in the Review of Ministerial Decisions Fact Sheet applicable at the time of this application, was that:

Requests for review will only be considered if the applicant considers that the information supplied in the original application has been misinterpreted or misunderstood or that proper procedures have not been followed.

8.34 This was reflected in the requirement set out the Internal Procedures Manual that:

The proponent should provide a statement of claims that the application has been misinterpreted, misunderstood or that proper procedures have not been followed. 865

8.35 The Fact Sheet and Internal Procedures Manual stipulated that:

- a review would be based only on information supplied in the original application; and
- the availability of further information relating to an application did not provide grounds for a review of the original decision. 866

8.36 On 5 October 2005, when providing the Senate Committee with information in relation to questions taken on notice at the 12 August 2005 hearing of the inquiry into the Regional Partnerships Programme, DOTARS advised the Committee that:

Only unsuccessful applicants are able to request a review of a decision not to approve a project application under the Regional Partnerships program. 867


866 In January 2006, the Ministerial Committee agreed to revised review procedures under which appellants are able to provide new information as part of the review process where the information helps rectify a misunderstanding or misinterpretation on the part of departmental officials who advised the Ministerial decision-maker on the original application.
8.37 This advice provided to the Senate Committee by DOTARS was consistent with the provisions of the Internal Procedures Manual applicable during the period examined. Specifically, the Manual stated as follows:

Unsuccessful applicants should be advised in writing within two weeks after the Ministerial announcement is made. This letter should include the specific reason(s) for non-approval. It should also include an explanation that the Department can arrange a consultation, if they wish to address reasons for non-approval, and that there may be an opportunity to re-submit an application when these issues have been addressed.\footnote{867}

8.38 However, before DOTARS had the opportunity to write to the applicant and CQACC advising that funding had not been approved for the Country Homes and Cabins application, the local Federal Member wrote to the then Parliamentary Secretary on 23 February 2005. In that correspondence, the local Federal Member requested that the decision not to approve funding be reconsidered and sought the opportunity to discuss this issue with the then Parliamentary Secretary as soon as possible. Figure 8.4 shows this correspondence.


\footnote{868}{This advice had been included in all versions of the Manual applicable during the four years to June 2007.}
Figure 8.4
Request from Federal Member for reconsideration of funding decision

Dear Parliamentary Secretary

I am writing to provide you with additional information you may not have received with Country Homes and Cabins application and which will contradict advice you have previously received.

I understand the advice has failed to recognise the significant support of local shires and businesses in the region. The provision of affordable accommodation on the Central Highlands and Mid West, within a reasonable time frame, is a problem all shire councils and businesses are currently facing, with at least a six month waiting list for current enquiries. Therefore, the suggestion of competitive neutrality effecting existing companies becomes a non-issue because of their inability to meet the demands in this area.

Furthermore, I would like to add that the applications received from ExtremeCo Pty Ltd and Country Homes and Cabins were part of a package to help address the employment issues the Emerald Shire is now facing as a result of the Citrus Canker outbreak and the long term impact this is having on the area.

I had written to Deputy Prime Minister John Anderson and Minister Warren Truss when quarantine restrictions were first imposed to the area regarding the potential loss of jobs in the citrus industry in the Emerald Shire. The quarantine restrictions, when imposed on the shire were in the nations' best interests. I would like this decision reconsidered as it is of paramount importance to support jobs in the area which are not affected by the economics of the agricultural sector.

I would appreciate the opportunity to discuss this issue with you as soon as possible in the hope of determining a favourable outcome for Country Homes and Cabins and the Emerald Shire.

Yours sincerely

Source: DOTARS record of correspondence from the Member for Maranoa to the then Parliamentary Secretary to the Minister for Transport and Regional Services, dated 23 February 2005.

8.39 As a result of this correspondence, the 18 February 2005 decision not to approve funding was reconsidered. In this respect, in July 2007, DOTARS advised ANAO that:

The draft updated Procedures Manual states:

The Assessor shall prepare a package for a ‘not recommended’ assessment that contains:

- a covering minute
- the Ministerial Committee brief
- a notification letter to the applicant, and
• a notification letter to the relevant ACC with a copy of the letter to the applicant.

The department notes that this procedure makes no reference to informing Senators and Members of Parliament of unsuccessful projects.

**ANAO conclusion**

8.40 The documented and publicised threshold criteria for review of a decision not to approve funding were not satisfied in relation to the Country Homes and Cabins application. Specifically, the applicant, LTH Investments, did not:

• request a review in writing to the department; or

• provide a statement of claims demonstrating that the application had been misinterpreted, misunderstood or that proper procedures had not been followed.

8.41 Indeed, there is no evidence that the applicant had been advised of the decision. Instead, the decision was reviewed on the basis of a request from the local Federal Member, who had been provided with advance notice that the application had not been approved for funding by the then Parliamentary Secretary’s Office.

**Review of initial decision leading to a subsequent decision to approve funding**

8.42 In terms of responsibility for conducting any such review, the Fact Sheet on the DOTARS website specified that the department would assess all requests for review. The Internal Procedures Manual specified that:

• reviews would be undertaken in DOTARS National Office by an officer other than the original assessor;

• on completion of the review, the department would brief the Minister about the outcome and that, as the Minister is the final decision-maker, the Minister must also make decisions arising from the review; and

• if the review process recommended that the original decision be overturned, the department would prepare a letter for the Minister’s signature advising the applicant of the next steps in the process. If the original decision stood, the department would prepare a letter for the
Minister to the applicant advising of the outcome of the review and, where relevant, inviting the applicant to consider re-applying.869

8.43 On 24 February 2005, the North Queensland Regional Office provided the Departmental Liaison Officer with comments in relation to the local Federal Member’s 23 February 2005 letter to the Parliamentary Secretary (see Figure 8.5). The Regional Office reiterated its earlier assessment that, in addition to competitive neutrality concerns, the long term regional housing market and the unavailability of skilled tradespeople combined to raise doubts about the sustainability of the project and whether it would deliver the outcomes claimed relating to increasing employment and contributing to the economic development of Central Queensland.

869 op. cit., p. 104.
Figure 8.5

Regional Office reiteration of recommendation not to approve funding

<table>
<thead>
<tr>
<th>In response to your query following the fax to you from Bruce Scott MP the following is provided:</th>
</tr>
</thead>
<tbody>
<tr>
<td>The problem of affordable accommodation on the Central Highlands and the Mid-West is a result of a current boom in the mining sector. This dependence on the mining sector is acknowledged in much of the supporting documentation provided with the application. Industry sources advise that there are approximately 12 companies providing demountable and relocatable buildings to the mining sector, and that it is a highly competitive business. As part of the assessment process, the industry was discussed in very general terms with representatives of AUSCO Building Systems, the largest provider of demountable/modular accommodation in Australia. Coincidentally, at the time of this discussion, these representatives where on a tour of Central Queensland to discuss the needs of the mining communities. They indicated that they anticipate current growth is expected to continue for 12-18 months, and then plateau for 3 to 5 years.</td>
</tr>
<tr>
<td>While Emerald, Jericho and Bauhinia Shire Councils and local businesses would like to believe that provision of housing would encourage families to move to the region, every statistic and demographic available indicates that our population is drifting from these inland areas to the coast. For example, in the ABS Queensland Key Statistics of 11 November 2004, the Central West and the North West Statistical Districts were the only ones to record negative population growth. Even with the growth of the mining sector, families stay in the well serviced coastal centres such as Rockhampton and Mackay, and workers commute to the mine sites. Mine shifts are structured to support this lifestyle, such as two weeks on, one week off.</td>
</tr>
<tr>
<td>Competitive neutrality is not the sole reason for not recommending funding of this project. There is a national shortage of tradespeople, especially in the building sector. It will be difficult to attract the tradesmen to Emerald to work in the facility. The applicant acknowledges this issue, and the short term solution proposed, subcontracting or redploying local tradesmen will not create new jobs. Local intelligence suggests that tradesmen in Emerald will be diverted to the facility when they are needed and available, and that, as most of the process line tasks are of a semi-skilled nature, the trainees will do the bulk of the labour.</td>
</tr>
<tr>
<td>In relation to &quot;failure to recognise the significant support of local shires etc&quot; you would note that the assessment brief did in fact reflect this fact.</td>
</tr>
<tr>
<td>The issues discussed above; the long term regional housing market and the availability of skilled tradespeople combine to raise doubts about the sustainability of the project, and whether it will deliver the outcomes detailed in the application of increasing employment and contributing to the economic development of Central Queensland.</td>
</tr>
</tbody>
</table>

Source: DOTARS Regional Office record of advice provided to the Departmental Liaison Officer to the Office of the then Parliamentary Secretary dated 24 February 2005.

8.44 There is no documentation on DOTARS' files evidencing any instruction it may have subsequently received from the then Parliamentary Secretary and/or his Office in relation to the local Federal Member's request for the decision not to approve funding to be reconsidered.

8.45 There was also little documentation in DOTARS' files evidencing what further due diligence inquiries were made by the department as a consequence of the local Federal Member seeking a review of the decision. Specifically, between 24 February 2005 (see Figure 8.5) and 17 April 2005, the only record on DOTARS' files was the results of an internet search for suppliers of portable buildings.

8.46 On 18 April 2005, the Departmental Liaison Officer to the Office of the then Parliamentary Secretary advised DOTARS that:
This project from Package 81 is still under consideration by Mr Cobb. Mr Cobb has now asked if the Department could organise external applicant and project viability assessment that would have been undertaken if the project were recommended by the Department. Mr Cobb is particularly interested in exploring this organisation’s financial position, including the financing arrangements for this particular project. It would be appreciated if these assessments could be completed as soon as possible.

8.47 The Regional Office wrote to the applicant on the same day, requesting that it authorise DOTARS to undertake steps to assess the financial viability of the applicant and the project. The requested authorisation was provided on 5 May 2005.

External viability assessment

8.48 DOTARS National Office issued a work order for the external assessment on 20 May 2005, requesting a report by 27 June 2005 with the cost of the report not to exceed $2500. The report was provided on 9 June 2005.

8.49 In requesting the applicant’s authorisation for the external assessment on 18 April 2005, DOTARS also requested that the applicant provide additional information and documents for each of the commercial entities associated with LTH Investments, namely:

- details of the business owners/directors/partners;
- three years of audited financial statements;
- balance sheet;
- profit and loss report;
- bank statements;
- proof of loan approvals;
- cash flow projections including: capital costs of establishing the project; project revenues for future years; projected ongoing costs for future years; assumptions, calculations and data underlying projections (for example, builders quotes, quantity surveyor’s reports, industry figures etcetera);
- three year historical income tax returns for entities involved in the project; and
- any other relevant information.
8.50 As noted at paragraphs 8.20 to 8.21, DOTARS’ project assessment, completed on 11 February 2005 did not address whether alternative funding sources had been exhausted or how LTH Investments was going to fund its working capital contribution (identified as $559 100 in the original application, increased to $684 100 in the amended application). In this respect, on 10 May 2005, in responding to DOTARS’ request for additional information for the purposes of the external viability assessment, the applicant’s consultant advised that:

In terms of fund approval, LTH Investments does have 2 funding facilities with Bank West (confirmation letter follows). These are partly drawn at present but proceeds from the sale of some property is expected to reduce the amount drawn in the coming months. In summary:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Bank West available funds</td>
<td>$122 457</td>
</tr>
<tr>
<td>Credit Balance CBA</td>
<td>$37 110</td>
</tr>
<tr>
<td>Sale Proceeds of 17 White St, Emerald (contract following)</td>
<td>$420 000</td>
</tr>
<tr>
<td>Proceeds from Lew Harris Transport Invoice (attached)</td>
<td>$67 727</td>
</tr>
<tr>
<td>Net proceeds from sale of 242 Borilla St, Emerald</td>
<td>$350 000</td>
</tr>
<tr>
<td>Total</td>
<td>$997 294</td>
</tr>
</tbody>
</table>

When sale proceeds are returned to the loan accounts, there will then be available funds to cover the proponents share of the projects expenditure in line with the application.

8.51 Whilst some of the information requested was provided, important information was not forthcoming from the applicant. As a result, the report of the external viability assessment was qualified due to continuing gaps in the information provided for analysis, specifically:

- financial statements for LTH Investments (the applicant) were not provided;
- financial statements for entities related to the applicant were unaudited with three years of financial statements provided in relation to Lindsay’s Kitchen’s (2000–01, 2001–02 and 2002–03 but not 2003–04) and financial statements for one year for the Howkins Family Trust (2003–04);
- cash flow projections were provided for only two years rather than the recommended ten years;
- details of the funding arrangements with the finance company for acquiring the transportation equipment had not been provided;
evidence of funds committed by LTH Investments had not been provided; and

there was an absence of evidence to substantiate the number of house sales and production.

8.52 The external viability assessment concluded that project viability risk was medium and applicant viability risk was high. The following rationale was provided:

**Project Viability**

Overall we have assessed the financial viability risk of project as medium based on our analysis and key findings listed in the table below. In assessing the viability of the project we have considered the reasonableness of projected results, proposed funding arrangements, cost and earnings assumptions, and examined as to whether the applicant has undertaken adequate market research to support the demand for houses as new industrial developments commence. Some of the key findings that influenced our risk rating included:

- Surpluses have been forecasted in the second year of operation, however, this may be considered optimistic;
- Results may be influenced by changes in market conditions in the agricultural and housing industries;
- Revenue projections are heavily dependent on the sale of three houses per month and the production of one house per week;
- Only two years of projections have been provided for review;
- There are discrepancies between the amount of funds sought and committed by the applicant. However, total funds for the project are consistent in the application form and the business plan; and
- Ongoing cost assumptions have not accounted for indexation.

The forecasted results indicate that the project may be financially viable as the project’s future operations are sustained through ongoing profits. However, the project is heavily dependent upon the financial and ongoing support of the applicant’s related entities. The success of the project may also be influenced by changes in the market conditions in the agricultural and housing industries.

**Applicant Viability**

Overall we have assessed the financial viability risk of the applicant as high based on our analysis and key findings listed in the table below. In assessing the viability of the applicant, we have reviewed the financial statements of the applicant’s related entities being Lindsay Kitchens Pty Ltd and the Howkins
Family Trust. The financial statements of LTH Investments Qld Pty Ltd were not provided. Some of the key findings that influenced our risk rating included:

**Lindsay Kitchens Pty Ltd:**
- The net profits of the company have increased over the period analysed.
- The company has a low gearing ratio. Therefore, the risk of the company not being able to service its debt is low.
- The company has a low liquidity ratio. If this ratio deteriorates further, the company may not have the ability to pay its debts as and when they fall due.

**The Hawkins Family Trust:**
- The trust has a low cash balance in proportion to its total assets.
- The trust has a negative liquidity ratio, indicating that it may not have the ability to pay its debts as and when they fall due.
- The trust’s high gearing ratio indicates a heavy reliance on external funding.
- The trust has incurred an operating loss in its first year of trading.

**Absence of a revised project assessment**

8.53 Notwithstanding the results of the external viability assessment, DOTARS did not prepare a revised project assessment for consideration by the then Parliamentary Secretary. This was despite the Departmental Liaison Officer advising National Office on 6 June 2005 that:

Mr Cobb’s Office is happy for the Department to finalise [the external viability assessment]. However, the Office would now also like some advice from the Department as to what it all means for the Department’s “not recommended” recommendation. For example, do the [external assessor’s] findings add weight to the Department’s original recommendation? What are the key reasons for this as identified in the [external viability assessment] report? Can the issues identified by the [external assessor] be addressed easily by requiring the applicant to supply more information or are they fundamental which will require the applicant to completely re-think and re-work their application? etc

The Office would like this advice as soon as possible.

8.54 If any such advice was provided to the then Parliamentary Secretary’s Office, it was not documented by DOTARS.
8.55 Accordingly, the information identifiable as having been placed before the then Parliamentary Secretary by DOTARS did not reflect that:

- the external assessment had rated applicant viability risk as high, whereas DOTARS’ February 2005 assessment had advised that this risk was low;
- the external assessment had rated project viability risk as medium, whereas DOTARS’ February 2005 assessment had advised that this risk was high; or
- DOTARS’ February 2005 assessment was that the partnerships and support criterion was partially satisfied, but that this assessment had not reflected the information subsequently obtained in May 2005 demonstrating that the applicant had not exhausted alternative funding sources and uncertainties about the funds to be obtained from a related entity (Lindsay’s Kitchens) and from equipment finance.

8.56 In this respect, there was a reasonable basis for DOTARS to conclude that, in addition to not meeting the criteria of outcomes, competitive neutrality and project viability (as had been assessed and advised to the then Parliamentary Secretary in February 2005), the application also did not meet the applicant viability and partnerships and support criteria. In other words, an updated project assessment would most likely have identified shortcomings against all Programme criteria.

8.57 On 22 June 2005, the then Parliamentary Secretary signed a ‘clean’ copy of the project assessment provided by the department on 11 February 2005, this time disagreeing with DOTARS’ 11 February 2005 recommendation that funding not be approved. Figure 8.6 illustrates the signature block on the project assessment signed on 22 June 2005. Written advice of funding approval was provided on:

- 22 June 2005 to the local Federal Member; and
- 27 June 2005 to the applicant and the CQACC.
8.58 The then Parliamentary Secretary’s record of his approval of this spending proposal stated that he was satisfied that the applicant had addressed:

- the competitive neutrality issues raised in DOTARS’ 11 February 2005 project assessment; and
- concerns raised in the 11 February 2005 assessment in relation to the partnerships and support criterion that there were no letters of support from potential customers. Specifically, the then Parliamentary Secretary stated that there was sufficient demand in the mining industry for the type of housing that would be constructed due to its expansion.

8.59 However, whilst the local Federal Member’s 23 February 2005 letter to the then Parliamentary Secretary had addressed these two issues, there was nothing to indicate that the applicant had provided any additional information to address the competitive neutrality issues or the concerns raised in relation to demand for the type of housing that would be constructed. In relation to
competitive neutrality, in the report of its inquiry, the Senate Committee recommended that competitive neutrality procedures be strengthened, including the introduction of a procedure for potential competitors to lodge objections.\textsuperscript{870}

8.60 The only evidence of any additional inquiries being made in relation to market demand relating to competitors of the proposed Country Homes and Cabins project was the 24 February 2005 email from the North Queensland Regional Office to the then Parliamentary Secretary’s Departmental Liaison Officer (see Figure 8.5 above) wherein it was stated that:

As part of the assessment process, the industry was discussed in very general terms with representatives of AUSCO Building Systems, the largest provider of demountable/modular accommodation in Australia. Coincidentally, at the time of this discussion, these representatives were on a tour of Central Queensland to discuss the needs of the mining companies. They indicated that they anticipate current growth is expected to continue for 12-18 months, and then plateau for 3 to five years.

8.61 Also in respect to market demand, ANAO notes that the external viability assessment raised concerns about the reasonableness of the revenue assumptions, and recommended that this risk be mitigated by requesting the applicant to supply evidence to substantiate the projected number of house sales and production. DOTARS’ records did not indicate that this information was requested or obtained.

**Outcomes criterion and project viability criterion**

8.62 On 11 February 2005, DOTARS had recommended that funding not be approved as the application did not meet the criteria of outcomes, competitive neutrality and project viability. However, the then Parliamentary Secretary’s 22 June 2005 recorded reasons for funding approval did not address the concerns raised by the department in relation to:

- project outcomes, specifically that the project was unlikely to deliver the outcomes outlined in the application of increasing employment and contributing to the economic development of Central Queensland; and
- project viability, noting that the external viability assessment (a draft of which had been provided to the then Parliamentary Secretary’s Office) also raised concerns against the project viability criterion.

\textsuperscript{870} Senate Committee Report, Senate Finance and Public Administration References Committee, \textit{Regional Partnerships and Sustainable Regions programs}, October 2005, Recommendation 18, p. 207.
**ANAO conclusion**

8.63 The manner in which the 18 February 2005 decision not to approve funding was reviewed, and funding subsequently approved, did not follow the documented Programme procedures, or published material on the operation of the Programme. It also did not represent sound practice in that:

- there was no documentation that outlined the inquiries made that enabled the then Parliamentary Secretary to conclude that the competitive neutrality and partnerships concerns raised by the department in its assessment had been addressed;
- in approving funding, the shortcomings identified in DOTARS’ assessment with respect to the outcomes criterion and the project viability criterion were not addressed;
- in the four months between the original decision to not approve funding and the later decision to approve funding, an external viability assessment was undertaken which concluded that the applicant represented a high viability risk, rather than the low viability risk that had been previously advised to the then Parliamentary Secretary by DOTARS. Notwithstanding this, a revised project assessment was not provided to the then Parliamentary Secretary, so as to draw attention to this issue; and
- similarly, additional information provided by the applicant revealed further shortcomings against the partnerships and support criterion which were not identified by DOTARS and were not drawn to the then Parliamentary Secretary’s attention.

8.64 As a result, an application for funding that failed to satisfy the Programme criteria was approved for funding.

**Management of the Funding Agreement**

8.65 On 30 June 2005, the North Queensland Regional Office faxed a draft Schedule to the Funding Agreement to the applicant. On 3 August 2005, the Regional Office emailed the applicant seeking urgent advice as to the acceptability of the proposed Schedule, or any proposed changes.

8.66 On 29 August 2005, following discussions on 12 August 2005, a revised draft Schedule was provided to the applicant. Compared to the draft provided on 30 June 2005, changes were made to the project milestone descriptions and to various dates for milestone completion, payments and progress reports. On
19 September 2005, a further follow-up call was made to the consultant that had assisted the applicant to prepare the application for funding. On 21 September 2005, a finalised version of the Funding Agreement was provided to the applicant for signature. The Funding Agreement was executed on 20 October 2005.

**Progress reporting and payment of Regional Partnerships funds**

8.67 The first Progress Report from LTH Investments was due on 15 November 2005, with 30 November 2005 being the proposed payment due date for the first Regional Partnerships instalment of $250 000 plus GST (67 per cent of approved funding). The purpose of this payment was to assist with the costs of the first milestone, being plans for the factory were to be finalised and approved with construction materials ordered. The Funding Agreement specified that the expected completion date for this milestone was 15 November 2005.

8.68 The Progress Report provided to the Regional Office on 16 November 2005 stated that a number of critical project activities had been completed but that the first milestone in the Regional Partnerships Funding Agreement had not yet been achieved, although building completion was still planned for March 2006. The Progress Report did not include the required statement of activity expenditure.

8.69 In relation to project progress, the Progress Report advised that, whilst building plans had been completed, they had not yet been approved by Emerald Shire Council but that this was anticipated in the following two weeks. The Progress Report further stated that, as a result of the delay in obtaining building plan approval, only some of the building materials had been ordered, with the final order to await building approval.

8.70 In July 2007, DOTARS advised ANAO that conducting a site visit to the project prior to Council planning approvals being confirmed would not have provided value for money in the expenditure of Commonwealth funds as it was evident that progress could not occur prior to receipt of those approvals. Notwithstanding the awareness that the project could not progress without the approvals, and that the applicant had specifically advised that the first milestone (which included approval of plans) had not yet been met, the first Regional Partnerships instalment payment was processed by DOTARS on 16 November 2005. In this respect, ANAO considers it would have been
prudent for DOTARS to await approval of building plans and the ordering of all building materials before processing the payment of $250 000 (plus GST).

8.71 The second Progress Report was due on 15 March 2006. A reminder email, sent to the applicant by the Regional Office on 1 March 2006, was not responded to. The Progress Report was not received by 15 March 2006. As a result, on 4 April 2006, the Regional Office wrote to the applicant in relation to the overdue Progress Report. On 20 April 2006, a response was received from the applicant’s consultant advising as follows:

As discussed today, the Country Homes and Cabins project is progressing albeit at a slow pace.

[The funding recipient] reports fabrication is 90 per cent complete of the shed. He is waiting for Building Plans and Council Approval so he can go ahead with putting the structure up.\(^871\)

He has been assured that Plans will be finished next week.

He is confident that the structure will be up in 3 months.

The demand for the transportable home is still very strong and construction is proceeding as reported previously.

The financial strength of the company is still strong and delays in the project are largely out of control of management.

8.72 DOTARS’ 4 April 2006 correspondence to the applicant had included a Progress Report proforma and acquittal of funds proforma. Neither were completed and returned to DOTARS by the applicant. The department also did not otherwise obtain the statement of activity expenditure that was required by the Funding Agreement, including acquittal of the first Regional Partnerships instalment payment.

8.73 The only action taken by DOTARS in relation to the advice of project delays was to advise the applicant and its consultant that a formal contract variation would be prepared to move the due date for the second Progress Report and payment to 30 June 2006 and the due date for the final report, audit and payment to 30 September 2006. A Funding Agreement variation was sent to the applicant by the Regional Office on 24 April 2006. On 29 May 2006, the Regional Office emailed the applicant, their consultant and the CQACC as the

\(^{871}\) This advice differed from that set out in the first Progress Report provided to DOTARS in November 2005 wherein it had been stated that building plans had been completed and that Council approval of the plans was expected within two weeks.
Funding Agreement variation had not yet been signed and returned to DOTARS.

8.74 ANAO undertook a site inspection of the project with the funding recipient on 5 June 2006. The photographs at Figure 8.7 were taken during that site visit, evidencing that, at that date, the project was well behind the Funding Agreement schedule, and the expected timetable for construction advised by the funding recipient’s consultant in April 2006.
Figure 8.7
Photographs of project site taken during ANAO’s 5 June 2006 site visit

Site for factory shed

Trusses for factory shed

Source: Photographs taken during ANAO site visit conducted on 5 June 2006.
8.75 DOTARS records state that the funding recipient telephoned the department on 8 June 2006, advising that:

…things are progressing OK. He now has finalised plans for the big shed, and has to get all of the necessary approvals. He says he will follow up with a written report “next week”.

I will follow up on 19th June if we haven’t heard anything.

8.76 A report was not received. On 5 July 2006, the Regional Office wrote to the applicant, with copies to the funding recipient’s consultant and the CQACC, regarding the non-receipt of the promised Progress Report as well as the variation to the Funding Agreement sent on 24 April 2006. The Regional Office correspondence stated that:

Due to the continuing disregard of your obligations under the Funding Agreement, consideration is being given to placing this matter in the hands of our Debt Recovery Unit. This could result in withdrawing the offer of Regional Partnerships funding, and recovering funds paid to date.

8.77 On the afternoon of 19 July 2006, the North Queensland Regional Office undertook a site inspection of the Country Homes and Cabins project accompanied by the funding recipient, the funding recipient’s consultant and a committee member of the CQACC. The record of DOTARS’ 19 July 2006 site visit stated that the department had concluded that:

The main reasons given for the project delays are that design of the shed has taken 12 months, and Council approvals are still not completed. It was apparent that [the funding recipient] is a man of vision, hard working and very good at what he does. Unfortunately, it would appear that he has limited capacity to meet the demands of the Regional Partnerships Funding Agreement in terms of meeting milestones, responding to correspondence, creating reports etc. He works on the houses from sun rise to sunset and there isn’t a site office there. He goes to his office once a week for all of the routine business issues.

Furthermore, the way that the project is progressing, it would be very difficult to establish realistic milestones that will be met. Major issues such as the internal layout of the shed, the mechanics of how the houses will be processed through the shed and the design of the specialist trailer remain unresolved at this stage.

In terms of outcomes, [the funding recipient] indicated that he had 12 employees on his books, which included 3 apprentices. Also, I think that some subcontractors such as plumbers and painters were included in this figure. There
was only one employee working with [the funding recipient] while we were there.

The Way Ahead

[The funding recipient’s consultant] has offered to take on the role of contract manager for the project. [The funding recipient] has a meeting with Council scheduled for today (21 July) to discuss what else is required for building and development approval. He will then talk to [the funding recipient’s consultant] and work out some milestones. [The funding recipient’s consultant] will then work with us. Realistically, I expect that any milestones that are negotiated will be very rubbery, given the developmental nature of so much of the project. The best we can do is to keep monitoring the project closely and make sure that SAP and TRAX records are maintained to reflect the status of the project.

8.78 Subsequent to the DOTARS site visit, on 27 July 2006, the funding recipient’s consultant advised the Regional Office that Council had lost the funding recipient’s plans. On 4 August 2006, the consultant advised the Regional Office that the fire safety requirement had been achieved but that operation works approval had not yet been obtained from Council as the size of the plans needed to be reduced.

8.79 The then applicable Internal Procedures Manual stated as follows in relation to due dates for reports and overdue reports:

There will often be some negotiation required around reporting and due dates, as in practice, dates may slip for various reasons. However these must remain within reasonable and satisfactory timeframes. The system needs to be updated to reflect any changes made to reporting dates.

Regional Office staff must remain across the circumstances of each Project and be satisfied that progress is being made and that the Project has not stalled. If there are concerns about lack of reports and progress, these need to be discussed on a case by case basis with the Regional Manager and a national program manager to determine appropriate action. A site visit would be warranted in these circumstances and discussions undertaken with the applicant and the ACC where the ACC is represented on the Steering Committee.872

8.80 However, the Regional Office’s concerns about the lack of reports and progress were not discussed with a National Office program manager. In addition, a variation to the Funding Agreement still had not been finalised and

signed. Further, due to the due dates for the remaining Progress Reports specified in the extant Funding Agreement having already passed, there was no contractual framework in place for requiring the funding recipient to provide Progress Reports that address the matters specified in the Funding Agreement, being:

- details of progress and performance against activity milestones;
- details of progress and performance to date (if any) against the specified project outcomes;
- details of mitigating circumstances and remedial action undertaken in the event a milestone had not been met or completed in the manner and/or by the time specified;
- copies of any published reports, promotional material, media publicity, pamphlets or other documentation relevant to the project;
- a register of all assets wholly or partly purchased with Regional Partnerships funds; and
- a statement of activity expenditure including:
  - a list of all budget items identified in the Funding Agreement;
  - a list of additional budget items, not identified in the Funding Agreement, that incurred expenditure from Regional Partnerships funding;
  - total expenditure of Regional Partnerships funding on the budget items listed; and
  - a summary of expenditure of cash contributions from the applicant and any other funding partners.

8.81 On 30 August 2006, the Regional Office emailed the funding recipient’s consultant seeking advice on some dates that might reflect how the applicant:

> thinks the project might go!? These dates will not be etched in stone, but will give us all something to work towards.

> We cannot just leave the Regional Partnerships funding drifting along in an open-ended fashion.

8.82 On 5 September 2006, a response was received from the consultant advising of revised expected completion dates, with the shed fit-out not expected to be completed until 30 August 2007. No action was taken by the department to arrange a variation to the Funding Agreement.
8.83 On 24 October 2006, the department sought a further update on project progress. A response was received on 26 October 2006, leading the department to conclude that:

There are some major issues with the performance of this project. The latest advice we have from the proponent’s consultant is that the shed will be erected by the end of February [2007], but the 2nd milestone of “shed completed and fitted out for house production” will not be completed until (about) 30 August 2007. As discussed, all indications are that the third milestone “Factory commissioned and operational. Specialised transporter delivered and operational” will not be achieved until at least the latter part of 2008. As we agreed, the way ahead is to write a formal letter to the proponent, indicating that the project is progressing at an unsatisfactory pace that is not in accordance with the timeframes proposed in the Regional Partnerships application and agreed to in subsequent Funding Agreement, signed on the 20 October 2005. In that letter, we will propose a Funding Agreement Variation. The applicant’s response will determine the future direction with this project. In the interim, I have moved the 2nd payment to 30 March 2007, and the third payment to September 2007.

8.84 After receiving advice on 3 November 2006 concerning revised milestone completion dates from the funding recipient’s consultant, on 22 November 2006 DOTARS wrote to the funding recipient offering it a variation to the Funding Agreement. The variation was not signed by the funding recipient until 14 February 2007 (and by DOTARS on 19 February 2007). The variation extended:

- the second milestone involving completion of shed construction and the fit-out for the house production line underway to 30 August 2007;
- the third milestone involving the factory being commissioned and operational and the specialised transporter being delivered and operational to 4 January 2008; and
- the post activity report to be submitted by 15 December 2008.

8.85 A progress report was received by DOTARS on 19 September 2007 (some information was provided on 30 August 2007). Accordingly, more than 22 months elapsed before DOTARS obtained a progress report in the manner required by the Funding Agreement, including an acquittal of the first Regional Partnerships instalment of $250 000 (plus GST) and formal advice on the delays, mitigating causes and action taken to address the situation.
**ANAO conclusion**

8.86 In a risk management context, the various shortcomings evident in the assessment of the application against the Regional Partnerships assessment criteria could reasonably have been expected to be addressed through careful structuring of the payment of Regional Partnerships funds, and regular monitoring of project progress. However:

- the first Regional Partnerships payment of $250,000 (plus GST), representing 67 per cent of approved funding, was made by DOTARS in November 2005, notwithstanding that the first project milestone had not been met and, until it was, the project was unable to proceed. Advice to DOTARS from the funding recipient is that this milestone was completed in September 2006; and

- there have been significant and ongoing delays in the project, with the department not requiring the funding recipient to meet its reporting and financial acquittal obligations under the Funding Agreement. Instead, DOTARS deferred and re-scheduled progress reports until such time as progress may be achieved and took 22 months to obtain an acquittal of the substantial up front payment that was made.
9. Undercarriage Remanufacture Facility

This case study examines RP01365 Undercarriage Remanufacture Facility involving the provision of $500 000 (plus GST) in venture capital to a private sector enterprise for the importation of specialised undercarriage remanufacture equipment. The case study illustrates the potential consequences of inadequate assessment of viability risks and partner funding arrangements, combined with the practice of making substantial grant payments in advance of need in situations where little attention is paid to monitoring the progress of the funded project. Specifically, in August 2007 an administrator was appointed to the company that received the Regional Partnerships grant and the majority of the equipment purchased in whole or part with Regional Partnerships funding has been advertised for sale.

Introduction

9.1 On 17 May 2004, ExtremeCo Pty Ltd (ExtremeCo), trading as Field MEC, submitted an Expression of Interest for funding under the Regional Partnerships Programme to the Central Queensland ACC (CQACC). The project was to:

involve the re-manufacture, service and repair of “Undercarriage” components of heavy earthmoving and mining machinery. A purpose built facility will house specialised machinery and tooling in a factory style environment. The plant will allow the remanufacture of undercarriage components to Original Equipment Manufacturer (O.E.M.) specifications. Core production equipment required is not available within Australia and would be imported from the USA.

9.2 The Expression of Interest stated that $250 000 of Regional Partnerships funds were sought, within an overall project cost of $1 320 000. Other funds were to come from the applicant ($820 000) and community and other contributions ($250 000).

9.3 The CQACC held no records of its consideration of this Expression of Interest.

Regional Partnerships application for funding

9.4 On 20 July 2004, the CQACC wrote to the Northern Queensland Regional Office of DOTARS as follows:
Included herewith is a hard copy version of the Field MEC Regional Partnerships Application.

The application is being forwarded to you prior to the [CQACC] Executive’s assessment and with the encouragement of the Parliamentary Secretary, Hon De-Anne Kelly.

9.5 However, the Regional Office did not receive the application until 12 August 2004. The total project cost identified in the application had increased significantly from that identified in the Expression of Interest, as had the amount of funds sought from Regional Partnerships. Specifically, the application sought $500 000 in Regional Partnerships funds, within a total project cost of $1 937 000.

9.6 Key aspects of the application were:

- the applicant was ExtremeCo Pty Ltd trading as Field MEC;
- it was seeking $500 000 in Regional Partnerships funds (plus GST) for the following project:

This proposed project is to develop an Undercarriage Remanufacture Facility in the community of Emerald will introduce and develop a new industrial opportunity to the Emerald region. (sic)

This project will involve the re-manufacture, service and repair of “Undercarriage” components of heavy earthmoving and mining machinery. A purpose built facility will house specialised machinery and tooling in a factory style environment. The plant will allow the remanufacture of undercarriage components to Original Equipment Manufacturer (O.E.M.) specifications. Core production equipment required is not available within Australia and will be imported from the USA.

Undercarriage components of heavy earthmoving and mining machinery consist of tracks, rollers, idlers, final drives and frames (as shown in appendix A). The demand for these components is assured as they are high-wearing, critical elements of track equipment and their life is limited. Undercarriage maintenance forms up to 50% of track equipment operating expenses. This often exceeds the operating expense associated with the mechanical components of the same machines. No facility of this kind currently exists in the Bowen Basin, and industry is required to transport equipment outside of the local region.

Mining companies and contractors will be the principal cliental, however the proposed facility will also have the capability to service rural, civil and Government activities throughout Queensland and the Northern Territory. At
this time there are 25 coal mines located within 200 kilometres of Emerald, housing no less than 23 major earthmoving contractors.

With support, this project can be commissioned in approximately 6 months, with a total project outlay of $1.937M. The funding sought from the Regional Partnerships Programme will provide the project with funding for some of the specialist imported machinery.

- the project start date was 15 August 2004 with an end date of 31 December 2005;
- Regional Partnerships funding would be used for purchase of specialised plant ($130,000 in August 2004 when the order would be placed, with the remaining $370,000 in November 2004 when the imported equipment was delivered);
- to achieve nominated outcomes in the areas of employment/social, cultural/community and economic growth;
- the only party providing cash to the project other than the Commonwealth through Regional Partnerships was the applicant, which was providing $524,706. This was despite the Expression of Interest including a proposed cash contribution from a ‘Venture Partner’ of $250,000, with the Expression of Interest stating that:
  negotiations with venture partners are well advanced.
- there were nominated in-kind contributions from:
  - the landlord of the applicant (Excelbond Pty Ltd) which was to provide a purpose-built facility valued at $500,000 to house the equipment, with the lease term to be extended to 10 years plus a 10 year option;
  - the applicant would provide $143,000 in existing plant and equipment; and
  - Toowoomba Wholesale Machinery had committed to supply on consignment inventory items to the value of $250,000.

Project assessment and approval

9.7 Departmental assessment of the application was finalised on 11 February 2005. On this date, National Office provided the then Parliamentary Secretary with a package of 12 recommended projects and
not recommended projects. The Undercarriage Remanufacture Facility project was one of the recommended projects.

9.8 DOTARS’ project assessment advised the then Parliamentary Secretary that the project had a duration of six months with a recommended funding profile involving $250 000 being paid in 2004–05 and $250 000 in 2005–06.

9.9 In terms of informing the then Parliamentary Secretary’s decision as to whether to approve Regional Partnerships funding for this project, DOTARS assessed the project as meeting the Programme Guidelines and that each assessment criterion had been satisfied. DOTARS further advised that the CQACC recommended the project and rated it as a high priority for its region.

9.10 On 18 February 2005, the then Parliamentary Secretary approved funding of $500 000 (plus GST) towards the purchase and commissioning of specialised undercarriage machinery components. Advice of this decision was provided to the local Federal Member (on 18 February 2005), the applicant (on 28 February 2005) and the CQACC (on 1 March 2005). The Funding Agreement was signed by ExtremeCo on 22 March 2005 and by DOTARS on 6 April 2005.

**DOTARS’ identification and assessment of viability risks**

9.11 DOTARS assessed both the applicant and the project as being low risk. Table 9.1 outlines the assessment provided by DOTARS to the then Parliamentary Secretary in support of the departmental recommendation that the spending proposal be approved.
Findings and limitations of the external viability assessment

9.12 On 7 December 2004, ExtremeCo signed an authorisation for DOTARS to engage an external consultant to conduct an external viability assessment. The report of the external viability assessment was finalised in January 2005. It concluded as follows in relation to applicant and project viability:

**Project Viability**

Based on the results of our analysis and the scope of the work performed, nothing has come to our attention to cause us to believe that the project will not be viable.

A positive Net Present Value and Internal Rate of Return indicate that the project will not make a loss. The Net Present Value and Internal Rate of Return have been calculated based on 2½ years of forecasted data and a cost of capital of 8.4%. This rate is equivalent to the interest on the loan to be provided by [the parents of the applicant’s Managing Director].

Table 9.1

**DOTARS’ assessment of applicant and project viability risks**

<table>
<thead>
<tr>
<th>Applicant viability</th>
<th>Project viability</th>
</tr>
</thead>
<tbody>
<tr>
<td>An independent viability assessment was undertaken for this project. The assessment provided positive recommendation with regards to the applicant and their ability to finance and manage the project. The applicant has no history of funding grants from any level of Government. However, the business has a proven track record in good management. The applicant has been servicing heavy earthmoving equipment and mining infrastructure for over 10 years. It currently employs 32 staff and turnover for 2003/4 exceeded $4.436M. A comprehensive business plan with relevant historical financial data and realistic operating budget forecasts has been supplied. All financial data suggest that the business will generate strong growth and a healthy profit. In addition, there is evidence of proprietor’s assets sufficient to minimise the margin of risk to lenders and financiers of the business. The application satisfies this criterion.</td>
<td>The project is assessed as low risk. Costs of plant and equipment are supported by quotations and operating budget appears realistic for this industry. Support from industry and related local businesses is high and project sustainability has been demonstrated. The independent project viability assessment has provided a positive result confirming that the mining and construction machinery manufacturing sector is strong with a continuing demand for re-manufacturing. There are no signs of any negative industry conditions. The assessment confirms that this business is robust and all financial data suggest that the business will generate strong growth and a healthy profit and that the project will be viable. This ensures a high level of confidence in the project sustainability. The application satisfies this criterion.</td>
</tr>
</tbody>
</table>

It should also be noted that the success of the project is dependent upon various parties meeting their commitments to provide funding and the achievement of forecasted results.

**Applicant Viability**

Based on the results of our analysis and the scope of the work performed, nothing has come to our attention to cause us to believe that ExtremeCo will not be viable.

Profits in the four years leading up to 30 June 2004 and a positive net asset position indicate that ExtremeCo is currently in a desirable financial position.

9.13 DOTARS’ assessment of the external assessment report was finalised on 19 January 2005. The Regional Office concluded that:

This looks good.

I think that some of the recommendations regarding additional info are not relevant as we already have some of these documents.

[National Office] agrees that based on this we can progress assessment as having passed external viability.

She will arrange for the “final” version to be forwarded to us. Don’t need to wait for it before progression.

9.14 As a consequence, none of the 11 recommendations made in the external viability assessment report were implemented by DOTARS. Instead, DOTARS finalised its assessment recommending funding for submission to the then Parliamentary Secretary.

9.15 Further, the advice provided by DOTARS to the then Parliamentary Secretary did not accurately reflect the findings of the external viability assessment. Medium and High risks identified by the external assessment were not drawn to the then Parliamentary Secretary’s attention. Nor was he advised that DOTARS had not implemented any of the 11 recommendations made by the external assessor to address the various risks that had been identified. Table 9.2 compares DOTARS’ advice to the then Parliamentary Secretary with the actual content of the external viability assessment.

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873 As noted, DOTARS’ records state that some of the additional information the external assessment had recommended be obtained was already held by DOTARS. However, the DOTARS records made available to ANAO did not include any of this material. In any event, the finding underpinning the relevant recommendation was not addressed either by DOTARS providing such information to the external assessor to enable the necessary additional analysis to be undertaken, or by DOTARS undertaking the necessary analysis itself.
Table 9.2

Advice to the then Parliamentary Secretary of the results of the external viability assessment

<table>
<thead>
<tr>
<th>DOTARS advice of results</th>
<th>ANAO analysis of external viability assessment</th>
</tr>
</thead>
<tbody>
<tr>
<td>The findings of the independent viability assessment corroborate the market opportunities identified by the applicant.</td>
<td>The external viability assessment ‘supports the comments made by the applicant’ rather than corroborating the opportunities identified by the applicant.</td>
</tr>
<tr>
<td>This application has been subject to an external viability assessment which has confirmed that the business is robust and the project will be viable.</td>
<td>No conclusions were made in relation to the robustness of the business. Negative assurance was provided on viability, viz: ‘nothing has come to our attention to cause us to believe that the project will not be viable.’ This is a different conclusion to one that the project ‘will be viable’ as advised by DOTARS.</td>
</tr>
<tr>
<td>An independent viability assessment was undertaken for this project. The assessment provided positive recommendation with regards to the applicant and their ability to finance and manage the project.</td>
<td>No such positive recommendation was provided. Concerns were raised in relation to aspects of the applicant’s ability to finance the project.</td>
</tr>
<tr>
<td>The independent project viability assessment has provided a positive result confirming that the mining and construction machinery sector is strong with a continuing demand for remanufacturing. There are no signs of any negative industry conditions. The assessment confirms that this business is robust and all financial data suggest that the business will generate strong growth and a healthy profit and that the project will be viable. This ensures a high level of confidence in the project sustainability.</td>
<td>Confirmation of the demand was not provided. Instead, the assurance was negative in that it supported the anecdotal evidence offered by the applicant and found no apparent indicators of any industry downturn that would compromise demand. No opinion was offered on the robustness of the business. Instead, a number of recommendations were made concerning the projected results and the reasonableness of both revenue and cost assumptions. There was no expression of a high level of confidence in the project sustainability.</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS’ assessment provided to the then Parliamentary Secretary on 11 February 2005 and the January 2005 report of the external viability assessment.

**ANAO conclusion**

9.16 An external viability assessment was obtained prior to DOTARS recommending that funding be approved for this project. This provided the opportunity for the external assessment to inform the decision about whether this spending proposal should be approved for funding. However, none of the 11 recommendations made in the external viability assessment were implemented by DOTARS before recommending that the project be approved for funding. Consequently, analysis necessary to fully informing an assessment of the financial viability of this project was not undertaken.
Analysis of financial returns and risks

9.17 In the project assessment provided to the then Parliamentary Secretary recommending funding approval, DOTARS advised that it had not addressed whether the applicant had sought loan funds for the project (see Figure 9.1).

**Figure 9.1**
Assessment against the partnerships criterion

<table>
<thead>
<tr>
<th>Partnership support for this project is considered strong with the applicant contribution of $524,708 cash and $143,000 in-kind for existing plant and equipment. There are two substantial in-kind (private enterprise) partnership contributions:</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Excelbond P/L as the landlord will provide a purpose built facility valued at $500,000 to house the equipment. In addition, the lease term will be extended to 10 years plus a 10 year option. This in-kind contribution is a significant injection of capital growth expenditure into the Emerald community and as such could be seen in the same light as a cash contribution. In these terms, the cash contribution of the Australian Government would then account for a reasonable 33% making this an even better value for money project.</td>
</tr>
<tr>
<td>- Toowoomba Wholesale Machinery has committed to supply on consignment inventory items to the value of $250,000. All partnership support has been confirmed and is considered very satisfactory.</td>
</tr>
</tbody>
</table>

*We are aware that he already has a business loan in place with the National Australia Bank.*

*He has also borrowed for part of his contribution at current financial rates from his parents. A statement to the effect that his parents have committed to this investment as a positive step to secure a retirement income stream has been provided during the assessment phase.*

*To our knowledge there is no compatible State Government funding programme available for private sector infrastructure projects.*

This application has been subject to an external viability assessment which has confirmed that the business is robust and that the project will be viable. It provides good value for money for the Commonwealth at an RP bid of 26% of total project costs. This project is expected to create up to 23 direct employment outcomes as well as flow-on employment opportunities for other regional service repair businesses. Emerald is situated approx 230km north-west of Brisbane and 260 km west of Rockhampton in Central Queensland. The development of this business will help establish a heavy industry service base adjacent to the mining areas with positive regional employment growth and wealth creation opportunities outside of the Southern capital cities and the coastal regions

Letters of support have been received from the Federal Member for Maranoa, the Hon Bruce Scott; State Member for Gregory Vaughan Johnson; Queensland Government Department of State Development and Innovation (Rockhampton office); Emerald and Bauhinia Shire Councils; local development corporations and local employment providers.

The application satisfies this criterion.

Source: DOTARS' project assessment provided to the then Parliamentary Secretary on 11 February 2005, and handwritten comment by the then Parliamentary Secretary.
9.18 In the context of DOTARS advising the then Parliamentary Secretary that due diligence inquiries had not been undertaken in relation to the availability to the commercial applicant of finance through a lending institution, Applied Financial Diagnostics\(^{874}\) advised ANAO that:

This project, as represented, offers a considerably higher return than normally required by venture capitalists. On this basis, it appears to be an extraordinarily profitable project.

There are two potential implications.

The first is that the projected cash flows are too good to be true, and the project is unlikely to be as successful as represented.

The second is that the project is fairly represented in the business plan. In this case the business owner would have no difficulty in funding the plan on a commercial basis and it is questionable as to why $500 000 of Commonwealth funds are provided as a free gift to a commercially viable enterprise.

9.19 In its January 2007 progress report following the completion of the project, ExtremeCo advised DOTARS that, whilst the project construction had been successfully completed, major financial losses had been incurred leading to termination of the services of the Business Manager. In addition, in respect to the ongoing viability of the project, ExtremeCo reported that its financial position had adversely affected its ability to secure support from financial institutions leading to a decision to sell-down up to 30 per cent of the business. As outlined further below, in August 2007 an administrator was appointed to the company and the majority of the specialised undercarriage remanufacture equipment purchased in whole or part with Regional Partnerships funding had been advertised for sale.

**Reasonableness of revenue projections**

9.20 A core determinant of project viability is the set of assumptions underlying forecast project revenue. The primary assumptions are the size of the overall market and the percentage of the market that the project will capture. The accuracy of these estimates is dependent on the quality and depth of market research and, ultimately, the ability of those managing the business to deliver quality services into that market.

\(^{874}\) To assist with analysis of this and a number of other Regional Partnerships projects, ANAO engaged treasury specialists Applied Financial Diagnostics Pty Ltd to provide advice on financial risks (including viability risks).
9.21 Revenue projections for this project were based on unaudited figures provided by the applicant. The revenue projections were for the period December 2004 to June 2007, included as part of projected cash flows for a two and a half year period attached to the Business Plan. In respect to these cash flow projections, the external viability assessment stated that:

Future cash flow projections have only been provided for 2½ years. This period of time may not be sufficient in order to correctly calculate the Net Present Value and Internal Rate of Return of the project. It is preferable that at least ten years of projections be provided. Based on our experience, a projection of ten years is commonly used.

9.22 As noted above, none of the recommendations of the external viability assessment were implemented by DOTARS before recommending that funding be approved, including the recommendation that the department obtain from ExtremeCo projected results for a 10 year period.

9.23 In this context, the external viability assessment had noted that monthly income was projected to increase by five per cent from 2005 to 2006 and by 14 per cent from 2006 to 2007. The revenue projections were predicated on the applicant gaining ‘market share’ of 25 per cent. However, the application did not include underlying data on the existing market, any assumed growth in the market or how the applicant proposed to increase its market share from nil to 25 per cent in a single year. On these issues, the external viability assessment stated that:

Achievement of the revenue projections is heavily dependent upon Field Undercarriage capturing 25% market share. As this appears to be a target, revenue for future years will fluctuate depending upon the actual market share captured.

Furthermore, the projected revenue per machine operated has not been provided. As such, we were unable to assess the reasonableness of revenue projections in this regard.

9.24 No action was taken by DOTARS to address these risks in its assessment of the project, or to draw them to the then Parliamentary Secretary’s attention so as to fully inform the decision whether or not to approve Regional Partnerships funding.

9.25 DOTARS also did not critically examine the marketing plan for the project. Nor did the department assess the veracity of the estimate that achieving 25 per cent market share would translate into $5 million in annual turnover. On this issue, in April 2007, DOTARS commented to ANAO that:
The applicant, in their Business Plan, referred to six forms of research conducted which led to their objective to obtain 25% of the total market. They further stated in their Business Plan that ‘none of the competitors have the facilities to do complete undercarriage re-manufacture’.

9.26 However, in a risk management context, statements made in an application for funding do not obviate the need for DOTARS to undertake its own due diligence inquiries on key issues affecting the viability of the project. These inquiries have been required by each version of the Internal Procedures Manual. Figure 9.2 outlines ExtremeCo’s advice to DOTARS in this respect in its January 2007 progress report following the completion of the project.

**Figure 9.2**

Difficulties encountered during the project—market share

The viability of this Project is reliant on the support of the facility by the end users, the cost of imported replacements, the demand on mineral commodities, the retention of skilled labour and the management of FIELD MEC.

Consumer Confidence of Undercarriage Remanufactured from FIELD MEC has to be earned from end users. This has a direct relationship to the rate of development that FIELD MEC will enjoy in the initial months of operation.

These issues were identified at the outset of the Project.


**ANAO conclusion**

9.27 DOTARS did not take sufficient and appropriate steps in its assessment of this application to assess the rigour of the revenue projections underpinning the viability of the applicant and the project being proposed for Regional Partnerships funding.

**Cost of imported equipment**

9.28 The Expression of Interest submitted to the CQACC on 17 May 2004 stated that the cost of the project was estimated to be $1,320,000. ExtremeCo sought $250,000 in Regional Partnerships funds, with a ‘Venture Partner’ to contribute a further $250,000 and the applicant to contribute the remaining $820,000.
9.29 The budget included with the Expression of Interest included $640 000 for ‘plant and equipment’. This was the single largest item in the budget. In terms of equipment costing, the applicant stated that:

   Equipment costing is based on supplier quotation.

9.30 No quotes were included with the Expression of Interest identifying the supplier, the equipment involved or its cost.

9.31 A Business Plan was submitted with the Regional Partnerships application. The Business Plan stated that it was to be used as an application for Regional Partnerships funding. According to the Business Plan, the key factory tool was to be a 360 tonne track press. The statement of achievements to date reported in the Business Plan included:

   Identified suitable equipment from overseas Manufacturers and finalised costing.

9.32 The Business Plan included a cost estimate of AUD560 206 for the purchase of ‘WTC Plant’. This comprised the cost of imported plant of USD350 000, converted at an exchange rate of 0.6800 to AUD514 706; freight from Brisbane to Emerald (AUD8 000); Customs duties (AUD17 500); and the cost of a foreign exchange option (AUD20 000). However, there were a number of errors in this costing, as follows:

   • the exchange rate of 0.6800 did not bear any relationship to the exchange rate prevailing at the time of the Regional Partnerships application (which was 0.7141), thereby overstating the amount required for the purchase of imported equipment;
   • the quotes for the imported machinery totalled USD328 802 rather than the USD350 000 used for the Regional Partnerships funding application, further overstating the amount required for the purchase of imported equipment;
   • Customs duties of five per cent were calculated on the USD equipment price, rather than the Australian dollar equivalent, understating these costs; and

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875 This reference would appear to relate to WTC Machinery Corporation, the United States based company from whom ExtremeCo proposed to purchase the undercarriage remanufacture equipment.

876 The customs value of imported goods into Australia must be expressed in Australian currency. If it is expressed in foreign currency, it must be converted into Australian currency at the rate of exchange prevailing on the day of export of the goods (not the day the goods arrive in Australia). This rate is specified by the Chief Executive Officer of Customs (as required by section 161J of the *Customs Act 1901*).
the amount of $20,000 included for the cost of a foreign exchange option was overstated.\textsuperscript{877}

9.33 Adjusting for these various errors, ANAO estimates that the Business Plan on which the application was based overstated the cost of the imported equipment by 14 per cent. In this respect, in April 2007 DOTARS advised ANAO that ‘noted’ the second and fourth errors outlined above. In relation to the first and third errors, DOTARS commented respectively as follows:

Noted—however the exchange rate was 0.6819 on 18 June 2004—less than 2 months prior to the date of the application submission, and despite being 0.7141 on the date of the application (12/8/04), the exchange rate fell again to 0.6886 less than a month later (10/9/04). The 0.68 rate can reasonably be regarded as a risk adverse estimate valid at the time.

Noted—this potentially cancels out the first point above.

9.34 More broadly, DOTARS commented that if the total expenditure of funds against the Regional Partnerships funded budget items\textsuperscript{878} is less than that specified in the Funding Agreement, either the final payment is reduced or unspent funds are returned.

\textit{ANAO conclusion}

9.35 DOTARS’ assessment of this project did not rigorously scrutinise the basis for the equipment cost estimate of $560,206 used to support a request for $500,000 (plus GST) in Regional Partnerships funds.

\textbf{Foreign exchange risk}

9.36 As mentioned, the project budget supporting the application for Regional Partnerships funding included an amount of $20,000 for the cost of a foreign exchange hedge to manage the foreign exchange risk on the importation of equipment. Accordingly, it would have been prudent for DOTARS to, through the Funding Agreement, require foreign exchange risk to

\textsuperscript{877} In this respect, Applied Financial Diagnostics advised ANAO that: ‘If this line referred to a foreign exchange option, they would cover their foreign exchange exposure from the time of purchasing the option. While we would regard this as a prudent action on their part, we note that the amount budgeted bears no commercial resemblance to the actual cost of obtaining full cover (forward purchase of U.S. Dollars for 1 year). This would only have cost approximately AUD6,500 and an option to buy USD500,000 at a strike rate of 0.6800 (the budgeted rate) for 1 year around AUD2,000. Therefore the financial analysis of foreign exchange rate management appears to be significantly over-estimated and not based on commercial fees and charges.’

\textsuperscript{878} The Funding Agreement for this project included only one budget item, namely: ‘Plant/Equipment purchase’.
be managed.\textsuperscript{879} This did not occur. ExtremeCo has advised ANAO that no hedge was purchased. In this respect, in April 2007, DOTARS advised ANAO that:

Hedging was identified by ExtremeCo in their Regional Partnerships application as their responsibility.

The audit required at the end of the project will identify ExtremeCo’s costs relating to the project and ExtremeCo will be required to return any unspent funds.

9.37 Exchange rate movements can both increase and decrease costs. Accordingly, the essence of the foreign exchange risk issue in relation to this project is not about the return of any unspent funds should exchange rate movements reduce costs. It relates to the effective management, by DOTARS, of the Funding Agreement so as to be satisfied that the applicant has managed identified risks. In this respect, an open foreign exchange position that results in costs increasing can have adverse impacts on the viability of the project.

\textit{ANAO conclusion}

9.38 As was identified in the external viability assessment, foreign exchange risk existed in relation to the purchase of imported specialised undercarriage remanufacturing equipment for this project. Although $20 000 of the budgeted equipment procurement costs on which the Regional Partnerships funding bid was based related to spending on foreign exchange hedging, the Funding Agreement developed by DOTARS did not require this risk to be managed.

\textbf{Extension to building and associated lease payments}

9.39 Partnerships support for the project was assessed as ‘strong’ on the basis that the applicant was contributing $524 708 cash and $143 000 in-kind together with two substantial in-kind contributions from other private sector parties totalling $750 000. This meant that, in aggregate, DOTARS assessed that the Regional Partnerships Programme was being asked to contribute 26 per cent of total project costs.

9.40 The Business Plan submitted with the Regional Partnerships application included $454 700 as a funding contribution in relation to ‘Building frame—Landlord’. In terms of the extension, the external viability assessment commented as follows:

\textsuperscript{879} Alternately, DOTARS could have deducted $20 000 from the amount being funded by the Regional Partnerships Programme.
ExtremeCo currently has a five year lease plus a five year option with Excel Bond Pty Ltd for the premises used for business operations. Excel Bond Pty Ltd has agreed to redevelop these premises used by Field Services to accommodate the undercarriage remanufacture facility.

The estimated cost for the redevelopment is $500,000. No documentation has been received to support the estimation of the costs.

Subsequent to facility expansion, the lease term will extend to ten years with a ten year option. Furthermore, a rental adjustment will be performed in order to increase the lease costs in proportion to the extra capital expenditure.

9.41 That is, Excel Bond Pty Ltd would be seeking a commercial return from ExtremeCo for any capital expenditure on expanding the facility, with the cost of such expansion being unsubstantiated. These issues were not addressed by DOTARS in its assessment of the application, or drawn to the then Parliamentary Secretary’s attention so as to properly inform the decision as to whether or not to approve funding. Instead, the only reference made to the extension to the building and associated lease payments in the assessment provided to the then Parliamentary Secretary was the following advice that the building extension represented one of two ‘substantial in-kind (private enterprise) partnership contributions’ as follows:

Excelbond P/L as the landlord will provide a purpose built facility valued at $500,000 to house the equipment. In addition, the lease term will be extended to 10 years plus a 10 year option. This in-kind contribution is a significant injection of capital growth expenditure into the Emerald community and as such could be seen in the same light as a cash contribution. In these terms, the cash contribution of the Australian Government would then account for a reasonable 33% making this an even better value for money project.

9.42 The Regional Partnerships Programme Internal Procedures Manual in place at the time this project was submitted and assessed (September 2004 version) provided as follows in relation to in-kind contributions:

In-kind support to a project is products or services provided to the project that have an intrinsic value, but are not provided as direct cash support (e.g. the use of an office at no charge which would normally be rented out—the value of the rent not charged would be an in-kind contribution).

9.43 This same definition was included in the revised July 2006 and July 2007 versions of the Regional Partnerships Guidelines.

9.44 ANAO inspected the project in the company of ExtremeCo’s Managing Director on 5 June 2006. Following the site inspection, ExtremeCo provided
ANAO with a copy of its new lease for the expanded facility. DOTARS had not obtained a copy of this key document as part of its management of the Regional Partnerships grant. The lease was made on 3 March 2006. Significantly, it provided that:

- the cost of the building extension was now estimated to be $1 million rather than the $500,000 that was included as part of the Regional Partnerships application and accepted by DOTARS without verification via quotes or estimates; and

- the annual rent for the year following completion of the new building works would be at least $295,165 (plus GST). This was 77 per cent higher than the planned rent of $166,610 included as part of the financial projections underpinning the Regional Partnerships application.

9.45 Applied Financial Diagnostics advised ANAO that the additional rental expenditure would have caused the project’s net present value to become significantly negative. ANAO was further advised that the significant increase in annual rent was not commensurate with the $1 million value of the building extension. Specifically, using a rate of return of eight per cent, the value of the building extension was more than $2.5 million, compared to a stated construction cost of $1 million.

9.46 The lease agreement was finalised after the project assessment was completed, funding approved and a Funding Agreement signed. However, notwithstanding that 90 per cent of Regional Partnerships funds had been paid for a project that included a contracted in-kind contribution of $500,000 from the landlord for ‘purpose built buildings & structures to house the remanufacture machinery’, the department had not taken any steps to monitor the change in the leasing arrangements for the building extension.

9.47 Further evidence that the expanded facility did not represent a genuine in-kind contribution was provided in the February 2007 financial acquittal of the project. Specifically, DOTARS permitted ExtremeCo to claim, as project expenditure, a total of $60,166 in increased rental due to the factory extension.

**ANAO conclusion**

9.48 The specialised undercarriage equipment was to be housed and operated in an extension to the funding recipient’s existing leased premises. The landlord was to receive a commercial return on its investment by way of increased rent on the premises, over a longer period of time. DOTARS’
assessment had reflected this commercial investment by the landlord both as an expense (in the viability assessment) and an asset (as in-kind partner funding). Such an approach overstated the level of in-kind partnership support for the project as well as incorrectly advising that that support could be taken as reducing the proportion of project cash costs being funded through Regional Partnerships.

**Partnership outcomes**

**9.49** In its project assessment (see Figure 9.1 above), DOTARS advised the then Parliamentary Secretary that partnerships support was strong with the applicant contributing both cash and in-kind support as well as two substantial in-kind private enterprise contributions. The assessment was that the Regional Partnerships Programme was being asked to contribute 26 per cent of total project costs and 49 per cent of the total cash requirement.

**9.50** The Funding Agreement reflected the assessed partnership contributions. However, as illustrated by Table 9.3, one of these in-kind contributions did not eventuate and the funding recipient did not contribute tools to the value expected (although the acquittal included a significant in-kind project management contribution from the funding recipient). Table 9.3 also indicates that the actual cost of the factory extension was greater than expected although, as outlined above, this cost does not represent a genuine in-kind partnership contribution to the project. In terms of partnerships, in its January 2007 progress report following the completion of the project, ExtremeCo stated that:

> Every project would be unique in nature; in my case I feel that the partnership needs to be more than monetary. The application process is supported exceptionally well with much valuable input readily accessible at no cost. After the monies are awarded, the support required is difficult to obtain and comes only from independent professionals at great expense. An extension of the partnership beyond the monetary component, by way of a commitment from one of the application parties to provide ongoing support to the applicant throughout the project. I believe this would prove very beneficial for all parties and ensure positive delivery of project outcomes.
Table 9.3  
**Acquittal of partnership contributions**

<table>
<thead>
<tr>
<th>Item</th>
<th>Budget</th>
<th>Acquitted</th>
</tr>
</thead>
<tbody>
<tr>
<td>ExtremeCo: Tools</td>
<td>143 000</td>
<td>18 000</td>
</tr>
<tr>
<td>ExtremeCo: Project management etc</td>
<td>Nil</td>
<td>161 729</td>
</tr>
<tr>
<td>Toowoomba Wholesale Machinery—inventory</td>
<td>250 000</td>
<td>Nil</td>
</tr>
<tr>
<td>Excelbond—Factory extension</td>
<td>500 000</td>
<td>875 804</td>
</tr>
<tr>
<td><strong>Total in-kind contributions</strong></td>
<td><strong>893 000</strong></td>
<td><strong>1 055 533</strong></td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS records.

**ANAO conclusion**

9.51 DOTARS’ management of the Funding Agreement for this project was such that it was not aware of the increase in lease payments to be paid by ExtremeCo, nor had it identified the need for further investigation concerning the veracity of the lease payment calculations and their impact on the project’s viability. In total, partnership contributions exceeded the amounts expected when funding was approved, but this was largely attributable to an increased cost of the building extension which, as noted, did not represent a genuine partner contribution to the project. The remaining (genuine) non-applicant private sector partner contribution was not obtained.

**Payments and progress reporting**

9.52 The Funding Agreement finalised in April 2005 provided that the Activity Period commenced on 6 April 2005 and ended on 31 December 2005. In this respect, the Funding Agreement identified four milestones, as follows:

- by 15 March 2005, ExtremeCo was to have placed its order for imported equipment and provided evidence of this to DOTARS;
- by 30 September 2005, construction of the factory for housing the equipment was to have been completed;
- also by 30 September 2005, the imported equipment was to have been delivered on-site, and a progress report and financial acquittal was to have been provided to DOTARS, together with tracking of co-funding expended to date; and
by 31 December 2005, the factory was to have been commissioned and opened and 15 staff recruited, with their training completed. The final audit and final evaluation report including employment records was to have been provided to DOTARS.

9.53 None of these milestones were met.

9.54 On 20 October 2005, in response to advice of delays set out in a progress report from ExtremeCo of 5 October 2005, the Funding Agreement was varied to extend the due date for the final audit and report to 31 March 2006, with the proposed date for the final payment extended to 1 April 2006.

9.55 A further progress report in April 2006 outlined that the project would not be completed until 30 June 2006. Consequently, a further variation to the Funding Agreement signed by ExtremeCo on 11 April 2006 and DOTARS on 19 April 2006 extended the contract timetable to 1 July 2006, with the final report and audit due by not later than 1 August 2006.

9.56 As mentioned above, ANAO conducted a site inspection with ExtremeCo in Emerald on 5 June 2006. ExtremeCo advised ANAO that the imported equipment would not be delivered until at least August 2006. Figure 9.3 shows the site plan for the workshop extension and includes photographs of the extension works at the time of ANAO’s site inspection. The building extension was, at the time of ANAO’s inspection, being used in connection with ExtremeCo’s existing business activities.
Figure 9.3
ANAO site visit

Source: Site plan and photographs taken at ANAO site visit June 2006.
9.57 On 8 September 2006, DOTARS’ Northern Queensland Regional Office requested that ExtremeCo provide it with an urgent status report of the overdue project. As no response was received, on 18 September 2006, DOTARS wrote to ExtremeCo advising that:

I now must advise that, as per Clause 21 of the Funding Agreement, you are in breach of your requirements under this Agreement. You now have ten (10) business days from the date of receipt of this notice to rectify the situation. After this time the Department will take steps to immediately terminate the term of this Agreement and invoke the terms of Subclause 21.2 of the Funding Agreement.880

9.58 An ‘interim’ report was provided to DOTARS by ExtremeCo on 24 September 2006. This report stated that:

- the extension of the building was completed on 31 August 2006, with commissioning due for 13 November 2006; and
- the imported equipment was expected to arrive in Brisbane on 25 October 2006 and be delivered in Emerald on 31 October 2006.

9.59 ExtremeCo sought an extension of the project to the end of November 2006, with the post activity report to be created following close of business on 30 June 2007 and provided to DOTARS before the end of July 2007.

9.60 On 4 October 2006, DOTARS offered ExtremeCo a ‘final time extension’. The variation was signed by ExtremeCo on 12 October 2006 and by DOTARS on 23 October 2006. This provided for:

- completion of the project, including all milestones, by 30 November 2006;
- final report and audit to be received by DOTARS no later than 31 December 2006; and
- the final post activity report showing the outcomes achieved to be due on 30 June 2007.

9.61 In offering this contract variation, DOTARS did not obtain an acquittal for the Regional Partnerships funds totalling $450 000 (plus GST) that had been paid in May and October 2005 (see further below).

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880 Clause 21 of the Funding Agreement relates to termination for default. Among other things, subclause 21.2 provides DOTARS with the power to recover funds (in defined circumstances).
Payments made in advance of need

9.62 The Regional Partnerships application form completed by ExtremeCo and submitted to DOTARS on 12 August 2004 required the applicant to break the project down into key milestones and associated required payments. The details required to be provided were the milestone description; the month it was due to occur; the cost items associated with each milestone and their estimated cost; and the payment (if any) required from the Regional Partnerships Programme for each milestone.

9.63 In its application, ExtremeCo had proposed that the payment of Regional Partnerships funds be made consistent with its cashflow needs in paying for the imported equipment. Specifically:

- the quotes included in the Business Plan attached to the Regional Partnerships application stated that the terms of the supplier of the imported equipment required 25 per cent of the price to be paid at the time of order. In its Regional Partnerships application form, ExtremeCo requested that DOTARS make a payment of $130 000 when the order was placed for the imported equipment. This was to cover the order deposit ($130 000); and

- the remaining $370 000 in Regional Partnerships funds were to be paid to ExtremeCo upon delivery of the imported equipment.

9.64 However, the draft Funding Agreement Schedule provided to ExtremeCo by DOTARS on 8 March 2005, and the Funding Agreement signed by DOTARS on 6 April 2005, provided for three payments, as follows:

- a first payment of $250 000 (50 per cent of the Regional Partnerships funds) to cover the first milestone, defined as:

  Contract executed. Order placed for imported equipment and evidence provided.

- a second payment of $200 000 (40 per cent of the Regional Partnerships funds) to cover the second and third milestones, defined as:

  Factory construction for housing equipment complete.

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881 This figure is consistent with the Business Plan attached to the Regional Partnerships application (putting aside the errors outlined by ANAO above). Specifically, the Business Plan included a figure of AUD514 706 for the purchase of imported equipment. 25 per cent of this amount is AUD128 677.
Imported equipment delivered on site; progress report to date plus financial acquittal of first payment provided; tracking of co-funding expended to date; and

- a final payment of $50,000 (the final 10 per cent of the Regional Partnerships funds) to cover the fourth milestone, defined as:

Factory commissioned. Factory opened. 15 staff recruited and training completed. Final audit and final evaluation report including employment records provided.

First payment

9.65 The amount of the first payment specified in the Funding Agreement ($250,000) was significantly greater than the amount requested by the applicant to cover an initial deposit upon ordering ($130,000).

9.66 On 23 March 2005, ExtremeCo provided its bank account details to DOTARS. In doing so, ExtremeCo advised DOTARS that:

We are using our normal operating account because the funds will be quickly TT’d to the American supplier.

When we submit the invoice for the first claim it will include details of the amount of the deposit to be made on the order of the equipment and that will be TT’d straight after the funds are received. The balance will then be placed on call deposit until it is used in accordance with the agreement.

9.67 On 12 May 2005, ExtremeCo provided DOTARS with an invoice for the first payment of Regional Partnerships funds of $250,000 and advised that:

Discussions have been initiated with two suppliers and negotiations are continuing with WTC (USA) and Lincoln Australia to obtain the most suitable equipment at the best landed price in Emerald.

The final order and deposit will be placed with one of the above suppliers as soon as price terms and conditions are agreed.

9.68 Despite the terms of the relevant milestone (Contract executed. Order placed for imported equipment and evidence provided), DOTARS processed the first payment of $250,000 on 12 May 2005 without seeking any further evidence that the order for the equipment had actually been placed. Nine months elapsed between the time the first payment was invoiced and paid in May 2005 and the date of orders for imported equipment actually being placed. This occurred on 14 February 2006, when two orders were placed with US suppliers, as follows:

- the first order was placed with a different company to that identified in the Business Plan accompanying the Regional Partnerships application
for equipment to a value of USD23,885 (AUD32,364.50). This equipment was different equipment to that identified at the time the Regional Partnerships application was lodged; and

- the second order was placed with the supplier identified in the Business Plan accompanying the Regional Partnerships application. This order related to three of the six items of equipment identified in the Regional Partnerships application. The order for these three items totalled USD227,031 (AUD307,630). The other three items identified in the Regional Partnerships application were not included in this order.

Second payment

9.69 The Funding Agreement provided that the second payment of $220,000 (GST inclusive) would be made for the purposes of the second and third milestones, as follows:

- Factory construction for housing equipment complete.
- Imported equipment delivered on site; progress report to date plus financial acquittal of first payment provided; tracking of co-funding expended to date.

9.70 The Funding Agreement stipulated that the second payment would not be made until:

- an acquittal was provided to, and accepted by, DOTARS showing that the first payment had been fully expended, or evidence that the previous payment would be fully expended in the near future;

- the first progress report had been provided to, and accepted by, DOTARS; and

- a properly rendered tax invoice was received by DOTARS.

9.71 On 29 August 2005, the Regional Office contacted ExtremeCo to remind it about the progress report due by the end of September and the related second payment. The Regional Office contacted ExtremeCo again on 4 October 2005 to discuss the progress report and acquittal, which had not been received.

9.72 A progress report was provided on 5 October 2005. In it, ExtremeCo advised that, since the Funding Agreement had been signed, the main focus had been on finalising the plans to the extension of the shed. ExtremeCo further advised that the landlord had, on 4 October 2005, signed a contract for the building extension and that the expected completion date for the extension...
was the end of February 2006. In terms of the imported equipment, the cost item on which the Regional Partnerships Programme funds were able to be spent, the progress report from ExtremeCo stated that:

Now that a firm date has been set for the completion of extensions a firm order can be placed to import the press etc required for use in the undercarriage factory. Despite Field MEC incurring considerable expenditure to get the project to this stage the initial payment is on call deposit with the National Australia Bank to remit to America to complete the import of the equipment.

It is now anticipated that the initial equipment will be landed and in place in the new shed in mid December 2005. The slight delays to date would mean that the end of February 2006 would be the commissioning of the factory and final audit and evaluation report including employment records would be provided.

ExtremeCo also provided DOTARS with a completed acquittal form for the first payment which stated that none of the Regional Partnerships funds had yet been spent, although they were ‘committed’.

An invoice for the second payment of $220 000 (GST inclusive), dated 5 October 2005, was also provided to the Northern Queensland Regional Office. The second payment was paid by DOTARS on 6 October 2005. This payment was made despite the evidence that the first milestone had still not been met in that the imported equipment had not yet been ordered and, consequently, expenditure of the first payment of $250 000 (plus GST) was not imminent (particularly that portion of the first payment that would not be required until delivery of the equipment). Clearly, the terms of the third milestone (which related to the imported equipment having been delivered on site) had also not yet been achieved.

In April 2007, DOTARS advised ANAO that:

The second milestone was deemed met in that:

a) the recipient had provided a signed progress report outlining delay issues and implications (i.e. machinery could not be landed without the factory expansion in place). Signed report confirmed formal contract signed between landlord and builder to supply factory extension within a designated period; new lease agreed with landlord; and recruitment of extra staff (9 to that date) had begun; and

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882 As noted above, in September 2006, ExtremeCo advised DOTARS that the workshop extension was actually completed on 31 August 2006 with commissioning due for 13 November 2006.
b) the signed acquittal showing funds committed in line with report and Funding Agreement. Funding Agreement allows for acceptance of commitment to expend funds in order that subsequent payments are made (Schedule item 2.5 states that a payment can be made on ‘evidence that the previous payments will be fully expended in the near future’).

9.76 Having regard to the circumstances of this project outlined above and the fact that Regional Partnerships funding was only approved for use towards the cost of purchase and commissioning of specialised undercarriage machinery components (and not for costs associated with the factory extension), the acquittal of funds referred to by DOTARS did not provide adequate support for a conclusion that a further payment of public money was warranted at that time. Specifically, through the acquittal, ExtremeCo:

- advised that it had not yet spent any of the first Regional Partnerships instalment;
- provided no evidence that the equipment for which Regional Partnerships funding was approved had yet been ordered883;
- stated that the only expenditure that had been undertaken to that date involved $123,250 of partner funds; and
- completed that part of the proforma inviting it to confirm whether the preceding $250,000 instalment had been expended or committed by simply deleting the word ‘expended’.

9.77 As noted above, some of the imported equipment was ordered on 14 February 2006, well after the second payment was made by DOTARS. ExtremeCo advised ANAO during the 5 June 2006 site inspection that the terms of the order actually placed were that payments were not required before despatch. Instead, the full cost of the equipment was required to be paid once it was landed in Australia, in serviceable order. ANAO was advised that this was expected to occur in September 2006.

9.78 On 19 November 2006, ExtremeCo submitted to DOTARS a ‘3rd Claim Report’ dated 18 November 2006, together with an invoice for the remaining Regional Partnerships instalment of $50,000 (plus GST). The report stated that:

- the factory extension had been completed on 31 August 2006;

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883 As noted at paragraph 9.68, despite the terms of the relevant milestone (Contract executed. Order placed for imported equipment and evidence provided), DOTARS processed the first payment of $250,000 on 12 May 2005 without seeking any evidence that the order for the equipment had actually been placed. DOTARS’ only comment on this finding was ‘Noted’.
• the imported equipment had been received and delivered on-site on 7 November 2006;
• the factory had been commissioned on 17 November 2006; and
• the final report and independent audit would be provided to DOTARS by 30 November 2006, with the Post Activity Report to be created following close of business on 30 June 2007 to be provided to DOTARS before the end of July 2007.

9.79 On 27 November 2006, DOTARS advised ExtremeCo that the final payment was to be made in arrears, based on receipt of an audited financial report. DOTARS further advised ExtremeCo that the financial acquittal would need to identify applicant and other partner contributions and that the final report would need to include evidence as required by the Funding Agreement to demonstrate that the Funding Agreement outcomes had been achieved.

9.80 On 8 February 2007, ExtremeCo submitted to DOTARS a ‘Regional Partnerships Final & Evaluation Report’ dated January 2007. The report included summary information on partner contributions and advice on the extent to which project outcomes had been achieved, other benefits to the region, the next stage of the business development, ongoing viability and sustainability of the business and difficulties encountered.

**ANAO conclusion**

9.81 The Regional Partnerships application form stated that payments would be linked to project milestones. However, the Funding Agreement prepared by DOTARS and signed with ExtremeCo departed from the payment arrangements proposed by the applicant in its application. Specifically, payments were made significantly in advance of need. Further, neither of the first two payments (90 per cent of Regional Partnerships funds) was made in accordance with the terms of the Funding Agreement.

**Financial acquittal and project outcomes**

9.82 On 13 February 2007, DOTARS received an audited statement of receipts and expenditure from ExtremeCo’s auditor. Table 9.4 outlines ANAO’s analysis of the information included in the acquittal (and information subsequently provided by ExtremeCo in response to queries from DOTARS) with the budget that formed the basis of the project approved for funding by the then Parliamentary Secretary. In this respect, DOTARS’ administration of the acquittal process was deficient in that:
the Funding Agreement stated that Regional Partnerships funding would contribute to the project by purchasing and commissioning of specialised undercarriage machinery components. The total cost of purchasing this equipment reported to DOTARS was $415 414 (including Customs duties) with ExtremeCo undertaking the receipt, installation, assembly, testing and commissioning of the equipment.\footnote{884} Accordingly, of the $500 000 (plus GST) in Regional Partnerships funding, $84 586 was not required for purchase and commissioning costs (as approved by the then Parliamentary Secretary and reflected in the Funding Agreement). DOTARS did not identify this shortfall; and

the department permitted the funding recipient to claim, as project cash expenditure, in-kind costs together with operating costs. In this latter respect, this was permitted notwithstanding that the project budget that formed the basis of the approval of Regional Partnerships funding included no operating costs but, instead, was a ‘capital development budget’.\footnote{885} Adjusting for these factors, the total project cash cost was $697 123, meaning that the funding recipient had made a cash contribution to the capital costs of the project of $197 123 with Regional Partnerships funding 72 per cent of project cash costs (compared to the 49 per cent that informed the then Parliamentary Secretary’s decision to approve Regional Partnerships funding).

\footnote{884} The acquittal included $161 729 relating to internal costs of this and related project management, planning and coordination activities undertaken by ExtremeCo. These are an in-kind contribution to the project as they did not involve any cash expenditure by ExtremeCo.

\footnote{885} The operating costs included increased rent attributable to the factory extension.
Table 9.4

Acquittal of project expenditure

<table>
<thead>
<tr>
<th>Item</th>
<th>Budget</th>
<th>Acquitted</th>
</tr>
</thead>
<tbody>
<tr>
<td>Imported specialised undercarriage</td>
<td>560 206</td>
<td>415 414</td>
</tr>
<tr>
<td>remanufacture equipment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Business Systems</td>
<td>109 000</td>
<td>43 961</td>
</tr>
<tr>
<td>Fit-out</td>
<td>127 000</td>
<td>86 276</td>
</tr>
<tr>
<td>Workshop tools</td>
<td>349 000</td>
<td>59 466</td>
</tr>
<tr>
<td>Other</td>
<td>41 794</td>
<td>Nil</td>
</tr>
<tr>
<td>Inventory</td>
<td>Nil</td>
<td>92 006</td>
</tr>
<tr>
<td><strong>Total eligible cash expenditure</strong></td>
<td>1 187 000</td>
<td>697 123</td>
</tr>
<tr>
<td>Ineligible costs included in acquittal:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>operating costs</td>
<td></td>
<td>328 518</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS records.

9.83 The Funding Agreement required that ExtremeCo not use any of the equipment acquired with Regional Partnerships funds as security for obtaining any loans or credit, and that the equipment not be encumbered or disposed of without DOTARS’ prior written approval. On 3 April 2007, ExtremeCo sought DOTARS’ written approval to use the undercarriage remanufacture equipment as security for $500 000 in bank finance that was being obtained to meet statutory obligations with the Australian Taxation Office, superannuation funds and the Office of State Revenue. DOTARS was advised that the relevant bank held a charge over the assets of the company, of which the undercarriage remanufacture equipment formed part. In this respect, on 27 August 2007, DOTARS advised the Minister for Transport and Regional Services that:

ExtremeCo Pty Ltd has breached Clauses 5.5(c) and 7.5(a) of the Funding Agreement by not seeking the Commonwealth’s prior written approval to use tooling obtained from Regional Partnerships funding as security for additional finance.

Legal advice is that the Funding Agreement does not allow the department to retrospectively approve the use of assets as security. While the department would have supported the facility, there is no practical way to remedy this breach other than to advise ExtremeCo that the Commonwealth expects applicants to comply with Funding Agreements in their entirety.

…Based on the final report and audit the project is complete. The requirements of the Funding Agreement have been met and the final payment, less the interest earned, will be provided to ExtremeCo.
This matter has been under consideration since March 2007 and the applicant is expecting final payment to assist with the ongoing viability of the business.

9.84 Shortly thereafter, on 31 August 2007, pursuant to section 436A of the Corporations Act 2001, an administrator was appointed to the company. On 4 September 2007, DOTARS advised the Minister for Transport and Regional Services that it had become aware of this appointment through informal advice on 3 September 2007 from the CQACC, and that the advice had been confirmed through discussion with the administrator on the same day. The Minister was further advised that the department was seeking legal advice to determine the implications of this development on the final Regional Partnerships payment.

9.85 The first meeting of creditors was held on 7 September 2007. At that meeting, creditors were advised that the company would not be able to continue trading and that, prior to the administrator’s appointment, the company had stood down all employees and had formed the view that it could not pay creditors. Creditors were further advised that the company was likely to be placed into liquidation and the assets would be subject to a sale agreement. In this respect, the majority of the specialised undercarriage remanufacture equipment purchased in whole or part with Regional Partnerships funding had been advertised for sale by expression of interest with a closing date of 7 September 2007.\footnote{886}

\textit{ANAO conclusion}

9.86 The project has not delivered the contracted outcomes and the public funds paid to the applicant are now reflected in assets being realised for the benefit of creditors, although the Funding Agreement may provide a means for DOTARS to recover some of these funds or, at least, to refrain from making the final instalment payment of $50,000 (plus GST). This case study illustrates the importance of viability risks and partner funding arrangements being appropriately examined, as well as the heightened risks that arise where substantial grant payments are made in advance of need, particularly in situations where little attention is paid to monitoring the progress of the funded project.

\footnote{886} The Funding Agreement provides that the funding recipient requires DOTARS’ prior written consent to dispose of any assets prior to the project completion date and that if at the time of sale the asset has not been fully depreciated, the funding recipient must pay to the department an amount equal to the proportion of the undepreciated value of the asset that is equivalent to the proportion of the purchase price of the asset that was funded by the Regional Partnerships Programme.
10. Sakai/CIC Business and Export Development

This case study examines the assessment, approval and contract management processes undertaken in respect to the application received in February 2005 for the RP01459 Sakai/CIC Business and Export Development project. This project illustrates challenges that can arise in adequately dealing with commercial projects. For this project, this is particularly the case in relation to effectively assessing applications, developing Funding Agreements that comply with the terms of the Ministerial approval, and managing the Funding Agreement in a way that adequately protects the Commonwealth’s financial interests.

Background

10.1 On 11 February 2005, Sakai,CIC (AUST) Pty Ltd (Sakai) applied for Regional Partnerships funding of $250 000 (plus GST) for the Sakai/CIC Business and Export Development project. Sakai is the manufacturing arm of a majority Japanese-owned corporate group involved in the production and sale of mould flux, an essential raw material in the manufacture of steel. The mould flux manufactured by Sakai is sold to the group’s selling agent, CI Ceramics (Aust) Pty Ltd (CI Ceramics), for on-sale to Sakai’s predominant customer, BlueScope Steel Port Kembla (BlueScope).

10.2 The project for which Regional Partnerships funds were sought involved the purchase and installation of a spray drying facility at the business’ existing site at Albion Park Rail in NSW (see Figure 10.1). This facility would enable the manufacture of spherical granule mould flux. Sakai had been supplying an extruded granule form of mould flux to BlueScope for approximately 10 years. BlueScope had advised Sakai that eligibility for any future contracts would depend upon it obtaining the capability to provide the more advanced spherical granule form.
Figure 10.1
Spray drying facility constructed with use of Regional Partnerships funds

Source: Photograph of spray drying facility taken during an ANAO site visit.
10.3 The Regional Partnerships application stated that the applicant would contribute $1 388 100 to the project, based on a total project cost of $1 638 100 and Regional Partnerships funding of $250 000. The application advised that the estimated purchase and construction costs had increased by approximately $250 000 since January 2004, due to increases in the price of stainless steel, a prime component in the spray dryer, and other construction cost increases.

10.4 Separately, the group of companies was investing a further $2 million in other infrastructure on the site, which it had identified as being necessary additions to its operations and would be used whether it produced the spherical granule product itself or imported it for on-sale to BlueScope. However, the applicant also stated that the combined cost of $3 638 100 would be over-capitalising its plant, and that the $250 000 funding from Regional Partnerships would bring its own construction costs back to a level where it could go ahead. The applicant advised that, at the higher cost, its parent company in Japan was wavering over the cost/benefit of the investment.

10.5 The application stated that BlueScope had guaranteed that, if Sakai upgraded its facilities to manufacture the product, it would be BlueScope’s sole supplier for five years, with a three year option. That contract would be worth $3 million per annum. Provision for the five year contract had been made in Sakai’s existing two year contract with BlueScope, which was due to expire on 31 October 2005. The relevant provisions stated as follows:

Clause 2.2 Section B: Subject to the successful development, trailing (sic), application and final approval of the Spherical Granular Mould Powder by the BlueScope Steel Representative – Technical, BlueScope Steel may, at its discretion, enter into negotiations with the Supplier for an extension of the Agreement as prescribed in Clause 7 of Section A.

Clause 7 Section A: Subject to the procedure described in Clause 2.2 of Section B, BlueScope Steel may, at its sole discretion, renegotiate the terms and conditions of this Agreement for a further period of up to five (5) years for the purchase of the “Spherical Granular” Mould Powder.

10.6 The Regional Partnerships application advised that, if the company group elected to import the spherical granule mould flux, Sakai would be liquidated, with a loss of four direct jobs, and possibly up to five indirect jobs in the company group.

10.7 DOTARS’ assessment of the application, submitted to the then Minister for Transport and Regional Services on 1 August 2005, recommended that it be approved on the following terms:
• total project costs were $1 638 100, of which Regional Partnerships funding of $250 000 would represent 15 per cent, with the remaining $1 388 100 being provided by the applicant;

• Regional Partnerships funding would used toward the purchase and installation of the spray drying facility; and

• approval for funding should be subject to the applicant providing evidence of its five year contract with BlueScope.

10.8 On 16 August 2005, the Minister for Transport and Regional Services approved, for the purposes of FMA Regulation 9, Regional Partnerships funding of $250 000 (plus GST) for use towards the purchase and installation of the spray drying facility, with a total project cost of $1 638 100, subject to the applicant providing evidence of its five year contract with BlueScope.

Consideration of cost and viability issues

10.9 The July 2005 external viability assessment of the application commission by DOTARS rated the financial viability risk of both the project and applicant as medium. The viability of the project was identified as being heavily reliant upon the commitment of funding, the achievement of projected results (which appeared to include projected revenue before the new facility was due to be on-line), and the extension of the existing BlueScope contract.

Basis for Ministerial approval

10.10 An important consideration in the assessment submitted to the then Minister was that:

The applicant has indicated that it is financially unviable for it to spend any more of its own funds on this project (beyond its $1.38m contribution) as it would overcapitalise its premises. This appears reasonable given the $2 million upgrade of their facilities currently underway which is financed by a bank loan.

10.11 The Minister was further advised that:

If the applicant ceases to be able to supply BlueScope Steel, the business would be immediately liquidated and the applicant’s selling agent would simply import the product for on-sale to BlueScope Steel. This would result in the unemployment of 4 staff at the applicant’s business and the likely unemployment of 4-5 staff at the applicant’s selling agent. It would also add $3m per annum to Australia’s current account deficit. Funding for this project
will ensure the applicant’s viability and set the platform for future export sales. 887

10.12 The then Minister was also advised that the Regional Partnerships funding would be used towards the purchase and installation of the spray drying facility. 888 This is the basis on which the funding was approved. The clear implication in the advice to the then Minister was that the project as a whole would not proceed in the absence of the requested Regional Partnerships funding, resulting in the liquidation of the applicant.

10.13 In March 2005, one month after the application was submitted, the applicant provided DOTARS with a more detailed list of the project budget which indicated that estimated costs had increased by a further $219 654 over the budget identified in the application, to $1 857 654 (GST exclusive). This higher estimate was used in the external viability assessment, which noted that, given the increases in estimated project costs since the applicant had started planning the project, there was a risk that construction costs may continue to increase and may be higher than anticipated. The external assessment also found that quotes had not been provided for all costs. 889

10.14 The apparent willingness of the applicant to incur additional expenditure equating to 88 per cent of the amount originally sought from Regional Partnerships was not considered by DOTARS. There is no evidence of DOTARS seeking additional information from the applicant regarding its capacity to absorb the increased costs, in light of its earlier statements that it could not commit more than $1 388 100 to the project. Instead, the departmental assessment submitted to the then Minister continued to use the original, lower project cost of $1 639 100 and applicant contribution of $1 388 100. In this respect, in December 2006, DOTARS advised ANAO that:

The original application was submitted 11 February 2005 with a total cash co-funding budget of $1 388 100 and a Regional Partnerships bid of $250 000, equalling total project costs of $1 638 100 (there is no in-kind contribution). The

887 ANAO notes that the external assessor reported that the applicant had only provided anecdotal evidence to support the potential for customers in addition to BlueScope, and that it had been unable to obtain external evidence to support the demand for spherical granular mould flux in Australia, South-East Asia and India.

888 This was despite both the February 2005 application and March 2005 advice to DOTARS from the applicant indicating that the Regional Partnerships funds would be spent on costs associated with constructing the facility to house the spray dryer.

889 The project costs appear to have remained uncertain for some time. Project quotes provided to ANAO by the applicant in April 2006 totalled $1 200 550. This included quotes that differed from those that had been provided to DOTARS and quotes were not provided for some of the items identified in the applicant’s March 2005 advice to the department.

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Department was advised on 14 March that the total costs of the project had increased to $1 873 514 to cover the cost of additional requirements for a fireproof wall and provision for improved dust collection. The company advised that they would absorb this cost and the Regional Partnerships bid amount would remain unchanged.

The Financial Viability Assessment undertaken by the Department in June 2005 used the increased total project costs of $1 873 514\textsuperscript{890} in its assessment, not the original $1 638 200. The Department commissioned the FVA to determine whether Sakai could meet the increased project costs.

10.15 This advice did not address the question of why the departmental assessment provided to the then Minister did not consider the applicant’s willingness and capacity to invest more funds in the project, having regard for the premise on which the Regional Partnerships funding had been sought. In particular, DOTARS did not address whether the applicant had clearly demonstrated a need for Regional Partnerships funding in order for the project to be viable. Nor did the department’s December 2006 advice to ANAO address its inaccurate advice to the then Minister in respect to the project costs.

10.16 The department’s advice in respect to the purpose for which the external viability assessment was commissioned also appears to be inaccurate, as there is no evidence that it was prompted by consideration of the applicant’s capacity to meet the increased project costs. Rather, the available contemporaneous evidence is that the commissioning of the external assessment was prompted by the normal considerations relating to an application from a for-profit organisation for an amount of $250 000 or more.\textsuperscript{891} Further, in seeking National Office advice in May 2005 in relation to the appropriate sort of external report to request, the Regional Office referred to the original budget and applicant contribution, as follows:

The applicant is a private concern, in quite a specialised industry sector and seeking to upgrade to an innovative process. The company is an independent Australian company but has some quite direct financial and structural links to a Japanese ‘parent’ company. The applicant has requested $250 000 from Regional Partnerships, and has committed $1.4[m] to the project.

10.17 Further, the departmental assessment provided to the then Minister on 27 July 2005 advised:

\textsuperscript{890} ANAO notes that the external viability assessment was based on total project costs of $1 857 654. The amount referred to by DOTARS incorrectly included a GST component, which the applicant corrected on 29 March 2005.

\textsuperscript{891} As per the then applicable Internal Procedures Manual – February 2005 version.
An external financial viability assessment was conducted on this project given its innovative nature, commercial basis and the amount of funds requested from Regional Partnerships.

10.18 In advising the then Minister of the findings of the external viability assessment, the department referred to the project cost increases that had occurred prior to the Regional Partnerships application being submitted, but made no reference to the additional costs of $219,654 the applicant had subsequently advised to the department. Despite this, the assessment advised:

Cost increases are particularly relevant as the applicant has stated that they would consider not proceeding if the cost increased much more due to the long period for the realisation of dividends as well as the likelihood that any increase would begin to overcapitalise their premises.

Cost of the spray dryer

10.19 The spray dryer was to be manufactured in China, and imported in about 700 component parts. The budget set out in the February 2005 application included an estimate of A$580,000 for the purchase and importation of the spray dryer. This was based on a quotation dating from August 2004 totalling US$440,486, which the applicant had converted to AUD using an exchange rate of US$0.76 to A$1. The revised budget advised to DOTARS in March 2005 maintained the estimate of A$580,000 for the purchase and importation of the spray dryer, based on the same quote and estimated exchange rate (this is discussed further below).

10.20 The external viability assessment advised that, if a forward contract for the acquisition of the spray dryer from the Chinese manufacturer had not or would not be entered into, the applicant would be exposed to foreign currency risk. The external assessor noted that this exposure may be favourable or unfavourable, and recommended that, as a risk mitigation strategy, DOTARS request that the applicant appropriately hedge this purchase. However, in the course of its assessment completed on 1 August 2005, there is no evidence of DOTARS:

- seeking to have the applicant update the quote obtained nearly a year earlier for the purchase of the spray dryer;
- obtaining current exchange rate information in order to validate the estimated Australian dollar cost of the equipment; or
- seeking advice from the applicant as to whether it had entered into a forward contract in relation to the purchase, or considering whether it
should require that the applicant to do so to protect the viability of the project.

10.21 In this respect, DOTARS advised ANAO in December 2006 that: ‘The Regional Partnerships grant was not used for the purchase of the spray drying facility.’ ANAO notes that the discussion above relates to the matters taken into account by the department as part of its assessment of the application, including the extent to which it acted on the recommendations of the external viability assessment. The departmental assessment recommending funding approval advised the then Minister that the Regional Partnerships funds would be used towards the purchase and installation of the spray drying facility.

10.22 As is discussed further below, the department did not become aware that the spray dryer had already been purchased until after funding approval. It was only at that time that it agreed that the applicant use the approved funding for the installation of the spray dryer only. Accordingly, it would have been appropriate for DOTARS to have taken the matters discussed above into account in its assessment of the viability of the project.

Retrospectivity and value for money

10.23 The Regional Partnerships Guidelines stipulate that projects are not eligible for funding where the project proposal is requesting funding for retrospective costs. The Guidelines that applied until the July 2006 version stated that DOTARS defined retrospective funding as funding to meet any expenditure, or commitment to expenditure, incurred prior to a Funding Agreement being signed by both parties.

10.24 The applicant made a number of statements throughout the assessment process to the effect that a decision on the Regional Partnerships application was required urgently, due to the long lead times involved in getting the project underway once a decision was made. As late as 15 August 2005, one day before funding was approved by the then Minister, the Regional Office advised National Office that:

The latest advice on this project is the applicant has until Wednesday to make a decision to go ahead with the project, this could result in not going ahead and closing the plant down. I understand representations are being made to the Minister along these lines.

10.25 However, there are a number of indications that the company may have been already committed to the project.
Specialist equipment already ordered and delivered

10.26 On 26 August 2005, during finalisation of the Funding Agreement for the project, the applicant advised DOTARS that a few of the activities had already commenced due to lengthy delays for equipment ordering and labour availability. On 5 September 2005, DOTARS asked for confirmation that the activities referred to were not part of the Regional Partnerships project, or had only begun after the applicant had received the letter of approval from the Minister. DOTARS advised the applicant that the Regional Partnerships Guidelines provided that no funding be expended before receiving Ministerial approval.892 On 6 September 2005, the applicant advised DOTARS that:

The timetable has been completely driven by our customer who demands that we make significant progress on this project before contract negotiations.

- The spray dryer arrived as approximately 700 pieces on 20 July 2005;
- Installation will commence next week – possibly Monday – and will continue for approximately 6 to 12 weeks, depending on labour availability;
- The deposit [on the spray dryer] was paid on 10 January 2005.893 We waited as long as possible, but the Chinese company had on two previous occasions warned us about the rapidly escalating price and availability of stainless steel. They warned that further delays in commencing manufacture could jeopardise any chance of completion before November [2005].894 I was also concerned that if this did occur, then construction would also be severely delayed due to the effect of Christmas and New Year construction company holidays. It is almost impossible to get construction work done in December & January.

I can only hope that these facts do not exclude us from the grant eligibility, as we have acted in good faith throughout this application.

10.27 The Regional Office advised National Office of this issue on 6 September 2005, advising that:

The applicant has implied they would have returned the dryer if funding wasn’t approved. The dryer was delivered in July this year, which

892 This advice is not consistent with the provisions set out in the published Guidelines relating to retrospectivity that applied at the time (see paragraph 10.23).

893 Therefore, this expenditure occurred in the 2004–05 financial year. The Budget Summary included with the application submitted by the applicant on 11 February 2005 identified all of the estimated $580 000 purchase cost of the spray dryer being expended in the 2005–06 financial year.

894 The applicant’s existing contract with BlueScope was due to expire on 31 October 2005. A subsequent contract was dependent upon it successfully developing the spherical granule capability.
demonstrates how long it takes to order and deliver such a piece of equipment. Total project costs are $1.6m, excluding the purchase cost would bring it to around $1m.

Despite the difficulties this brings, the project still represents value for money and will still deliver regional benefits to the community and beyond. While the purchasing costs should have been excluded from the project budget, it would still have been reflected in the assessment acknowledging it as a strong commitment to the project by the applicant.

I am proposing to proceed ahead with the contract negotiations on the basis we put Regional Partnerships funding towards the installation only. This still reflects what the Minister approved.

10.28 National Office advised that it was comfortable with the proposed approach and asked the Regional Office to proceed as suggested.

10.29 This approach did not have regard to whether the purchase of the equipment before the Regional Partnerships application had been submitted meant that the applicant was already committed to its installation.

10.30 In this context, in April 2006, the applicant provided ANAO with the following documentation:

(a) copies of letters dated 23 and 29 March 2005 confirming the decisions of the Boards of its Australian and Japanese parent companies respectively supporting its commitment to the development of a new production facility at Albion Park Rail. Each Board expressed the belief that the project was essential for the survival of Sakai. Both letters stated:

The board…acknowledges there is strong support for the project from customers, the community and the parties concerned, and we look forward to construction completion and successful future operations of the project.

In supplying the letters, the applicant advised ANAO that: ‘The approval does not distinguish between purchase and construction’;

and

(b) copies of:

– the August 2004 quote from Sakai’s intermediate supplier for the purchase and importation of the spray dryer components, amounting to US$440,486 (this was the quote provided to DOTARS), and
- a contract executed on 18 November 2004 with the intermediate supplier for the purchase and importation of the spray dryer components, which amounted to a cost of US$389 263. The applicant advised ANAO that:

The contract [with the intermediate supplier] was concluded much earlier than the equipment was actually ordered. This was an agreement that we would purchase the equipment through [it] and not direct from the supplier, but contains NO order/purchase date. The drawings, mentioned in the agreement, were reviewed by [the intermediate supplier] and not by Sakai/CIC. There is no mention of cancellation conditions mentioned in this agreement.

10.31 The spray dryer was ordered by the applicant in January 2005, for the purchase price of US$389 263, US$51 223 less than the cost identified to DOTARS in February and March 2005. Based on the estimated exchange rate of $0.76 used by the applicant in its application, the actual purchase cost was A$67 399 lower than the cost used in DOTARS’ assessment. Based on documentation provided to ANAO, the applicant had paid the overseas supplier a minimum of A$304 734 prior to the then Minister approving the Regional Partnerships application in August 2005 (comprising a 40 percent deposit in January 2005 and a 20 per cent payment in June 2005).

**Potential impact on Ministerial decision-making**

10.32 The primary outcome to be obtained from the Regional Partnerships funding, as advised to the then Minister by DOTARS, was the avoidance of job losses and increased importation that would result should the applicant’s group of companies elect to import the spherical granule product rather than manufacturing it. To the extent that the applicant had already committed to pursuing development of the spherical granule capability on which those jobs were dependent, their future retention or otherwise would appear to rely on the outcome of the development and normal commercial processes. There is no evidence of DOTARS undertaking any analysis to identify what, if any, additional outcome would be achieved from continuing to provide the Regional Partnerships funding after the earlier purchase of the spray dryer came to light.

10.33 DOTARS had various opportunities during the assessment process to seek updated information from the applicant in respect to validating the cost of purchasing the spray dryer, including raising the external assessor’s recommendation that the department take steps to mitigate the foreign
exchange risk. If any of those opportunities had been taken, it would have become apparent that the equipment had been ordered before the application was submitted; purchased for a lower cost than the cost advised to DOTARS; and received and largely paid for before the department’s assessment of the application was submitted to the then Minister for consideration. It is reasonable to assume that this additional information would have been an important consideration in the then Minister’s decision as to whether to approve funding for the project.

10.34 In December 2006, DOTARS advised ANAO that:

The funding recipient did not disclose to the Department that they had committed to the purchase of the spray drying facility during the assessment of the project.

10.35 As noted, the department had opportunities to seek information during its due diligence process that is likely to have elicited this information. Even if it had not, this advice does not address why, once the matter did come to the department’s attention, it did not more robustly consider the question of whether funding the project continued to represent value for money to the Commonwealth and, accordingly, whether the matter should be referred back for further Ministerial consideration.

**Ministerial approval of project scope changes not sought**

10.36 DOTARS did not seek Ministerial endorsement of its decision to proceed with executing a Funding Agreement with the applicant or of the changes from the terms of the approval given by the Minister for the purposes of FMA Regulation 9. This was despite:

- the intended definition of the Regional Partnerships-funded project changing from that approved by the then Minister (from purchase and installation to installation only)—see discussion below in this respect;

- the intended proportion of partner contribution to the Regional Partnerships funded activity changing (given the costs associated with the purchase of the equipment should not be in the project budget)—see discussion below in this respect;

- the activities included in the milestones to which payments were to be tied differing from the activities approved by the Minister; and

- the emergence of a question over whether the application represented value for money given the applicant’s prior commitment, and whether
it was ineligible under the Regional Partnerships Guidelines in respect to retrospectivity.

10.37 In those circumstances, there is doubt as to whether the Funding Agreement executed with the applicant was made in accordance with the terms of the Minister’s approval. In this respect, in December 2006, DOTARS advised ANAO that:

The Funding Agreement reflected the Minister’s decision in that it included ‘purchase and installation’...

10.38 While the Funding Agreement initially executed by DOTARS continued to reflect the original purpose of funding as approved by the then Minister, through the inclusion of the statement ‘Regional Partnerships funding will contribute to the Project by funding the purchase and installation of the spray drying facility’, this was not consistent with the arrangement agreed with the applicant by DOTARS as a means of overcoming the retrospectivity issues.

10.39 As a result, the milestones identified in the Funding Agreement, which the applicant was required to achieve in order to perform the Regional Partnerships-funded Activity, all related to the installation and commissioning of the spray drying facility. None of the contracted project milestones related to the purchase of the spray dryer.

Dealing appropriately with commercial projects

10.40 This application is an example of the tensions that can arise when dealing with applications for funding for a commercial project through a Government grant programme.

10.41 In this case, the applicant had approached the Illawarra Area Consultative Committee at least as early as July 2004, but the application was not formally submitted to DOTARS until February 2005. A decision was then not taken until August 2005, including a period of delay due to a change in Minister.

10.42 During a site visit to this project by ANAO in April 2006, the applicant advised that it had become frustrated with the time taken to progress the application, due to rising costs and pressure from its primary customer for the project to be progressed in order to meet the customer’s required timelines. The applicant advised that, ultimately, these pressures had meant that it had to proceed with the project.
10.43 This example highlights that, particularly where there are known time-critical factors involving commercial considerations, it is important that DOTARS’ assessment of applications from for-profit organisations places sufficient emphasis on examining the potential for the project to commence prior to consideration of funding approval, and that appropriate inquiries are made in that light. Applications that involve projects to which the applicant has made commercial commitments, or where it is clearly in the applicant’s commercial interests to proceed with the project regardless of whether grant funding is obtained, raise particular questions in respect to both value for money to the Commonwealth and eligibility in respect to potential retrospective funding.

Management of the Funding Agreement

10.44 The Funding Agreement executed on 27 September 2005 was based on the Short Form Standardised Agreement, normally used for Regional Partnerships projects involving funding of $50,000 or less. Under the reduced obligations imposed on such funding recipients, the short form Agreement does include any requirement for the funding recipient to provide an audited statement of receipts and expenditure in respect to the project. This is not an appropriate form of Agreement to use in relation to a grant payment of $250,000 (GST exclusive) to a commercial entity for use in relation to a commercial project. In December 2006, DOTARS advised ANAO that:

The short form Funding Agreement was used in error. On 29 September 2006 TRAX was altered to always default to the Long Form Agreement.

10.45 Further to the issues discussed above in relation to the purchase of the spray dryer, other aspects of the Funding Agreement have also not been managed in accordance with the terms of the approval provided by the then Minister. The Funding Agreement also failed to accurately reflect the approach agreed within DOTARS for addressing the post-approval discovery that the applicant had already purchased the spray dryer.

Waiving of condition of approval

10.46 The then Minister’s approval of Regional Partnerships funding was subject to the funding recipient providing evidence of its five year contract with BlueScope. This reflected the company’s economic dependence on that customer, as identified by the external viability assessment.
10.47 The then Minister’s letter of 16 August 2005 advising the funding recipient of the approval specifically identified the condition that was attached to Regional Partnerships funding being provided. This requirement was also included in the Funding Agreement as a pre-condition to it receiving the first payment of $115 000 (GST inclusive – 46 per cent of the total grant). The first payment was also contingent on DOTARS’ acceptance of the first progress report and was expected to be paid on 31 December 2005. The funding recipient signed the Funding Agreement in September 2005.

Funding recipient unable to satisfy pre-condition for funding

10.48 On 1 November 2005, the funding recipient provided DOTARS with a copy of a letter to it from BlueScope, which advised as follows:

BlueScope Steel entered into a contractual arrangement with C.I. Ceramics (Aust) Pty Limited…for the supply of extruded granular mould powder on 1st November 2003, with an initial term of 2 years expiring 31st October 2005 (the Contract).

Under the Contract, C.I. Ceramics supplies extruded granular mould powder and is also committed to developing a new and improved mould powder known as spherical granular mould powder.

Should the spherical granular mould powder prove acceptable as a substitute for extruded granular mould powder, the Contract provides that BlueScope Steel may, in its sole discretion, renegotiate the terms of the Contract for a further period of up to five (5) years. Pending development of an acceptable spherical granular mould powder, BlueScope Steel may, in its sole discretion and subject to satisfactory fulfilment of KPIs, extend the Contract for periods of six (6) months, for the continued supply of extruded granular mould powder.

10.49 The existing contract between C.I. Ceramics and BlueScope for the supply of extruded granular mould powder manufactured by the funding recipient was extended for six months on 1 November 2005, with an expiry date of 1 May 2006. As a five year contract was not likely to be signed for at least 20 months (allowing 12 months for construction of the spray drying facility and eight months for testing to produce the new product), the funding recipient was unable to satisfy the condition on the then Minister’s funding approval or the relevant clause in the Funding Agreement. There was also no guarantee that the funding recipient would successfully develop the product to BlueScope’s satisfaction.
**DOTARS’ approach**

10.50 On 6 December 2005, DOTARS decided to address the issue by:

- including the next six monthly contract renewal between the funding recipient’s parent company and BlueScope, due by 1 May 2006, as an additional milestone for the Regional Partnerships funded project; and

- making the execution of the five year contract with BlueScope for supply of the new product (expected to occur some 20 months in the future) an outcome of the Regional Partnerships funded project.

10.51 This was decided on the basis that:

I think it is an unrealistic expectation re Bluescope putting a five year contract in place with Sakai for a new product that will not be produced and tested for another 20 months. However, this condition is included in both the assessment and the Minister’s approval.

10.52 In this respect, the funding recipient had provided DOTARS with extracts from its existing contract with BlueScope on 14 March 2005 as part of the application assessment process. Those extracts had clearly identified the conditions under which BlueScope may, at its discretion, enter into a five year contract for supply of the spherical granule mould flux from the funding recipient. Further, a DOTARS note for file dated 6 July 2005 explicitly acknowledged advice from the applicant that the spherical granule mould flux would take approximately 12 months to develop once the facility was in place, as it required extensive testing and trialling.

10.53 On that basis, it should have been apparent to DOTARS that BlueScope was unlikely to enter into any long term contract with the applicant prior to the product being proven. Yet the department recommended to the then Minister in August 2005 that the project be approved on the condition that the applicant provide evidence of such a contract having been signed before any payment of Regional Partnerships funds. Accordingly, the assessment and recommendation provided to the then Minister did not present an accurate basis on which to make a determination as to whether the project represented an acceptable level of risk and value for money.

10.54 In supporting the course of action decided to address the funding recipient’s inability to satisfy the funding approval condition, the view was also expressed within the department that:

I understand the contract issue was not raised as a risk factor in the external assessment that was undertaken.
10.55 However, in concluding that both the project and applicant were of medium risk, the external viability assessment specifically identified that:

- achieving revenue projections is heavily dependent upon BlueScope Steel Port Kembla extending its contract with Sakai for the supply of mould flux for a further five years post expiry of the existing contract,
- Sakai is economically dependent upon the revenue received from BlueScope Steel. If the contract with BlueScope Steel is lost, Sakai may encounter financial difficulty; and
- per the audited financial statements, the majority of revenues earned by the company are dependent on a contract between a related party and BlueScope Steel. We assume that this related party is Sakai’s selling agent, CI Ceramics. This significant economic dependency on the revenues from BlueScope Steel creates a high risk that the company may encounter financial difficulty if this contract is lost. The applicant even indicates that Sakai will be liquidated if it is unable to produce spherical granular mould flux.

10.56 On 19 December 2005, DOTARS wrote to the funding recipient advising that:

In order to comply with the spirit of the funding precondition but also allow you to access the funding you require to develop the new facility and eventually produce the new product, I recommend that we amend the contract to make securing of a long term contract with Bluescope Steel an outcome of the funding as opposed to a precondition for the funding.

If you agree, I would simply ask that you keep the Department informed of the current status of your contractual relationships with Bluescope Steel when you submit each Progress Report. Then, when you submit your Post Activity Report in October 2006, I would ask that you comment in more detail about the progress you have made towards securing the long term contract with Bluescope Steel.

*First payment made in contravention of Funding Agreement*

10.57 DOTARS’ records indicate that the first payment of $115 000 (GST inclusive) was approved for payment on 19 December 2005, and processed on 20 December 2005. On 21 December 2005, the funding recipient wrote to DOTARS advising that it agreed with the recommended changes to the contract. As the Funding Agreement provides that it can only be varied by
written agreement, this first payment was made in contravention of the terms of the Agreement as it stood at the date of payment.\footnote{\textsuperscript{895}}

\textit{Ministerial approval of waiving the funding condition not obtained}

10.58 The course determined by DOTARS resulted in a Ministerial \textit{pre-condition} to the applicant receiving any funding being treated as an \textit{outcome} resulting from the provision of the funding. Given the evident risk that the spherical granular mould flux would not be successfully developed to BlueScope’s satisfaction, the Regional Partnerships funding essentially represented venture capital at risk.

10.59 The terms of the varied Funding Agreement agreed to by DOTARS did not comply with the terms of the approval given by the then Minister for the purposes of FMA Regulation 9. Whilst the Ministerial funding condition was initially included in the Funding Agreement as a \textit{pre-condition} to the first payment being made, the department’s subsequent actions resulted in that \textit{pre-condition} being waived, with the department agreeing to vary the Agreement to allow the first payment to be made without evidence of the five year contract with BlueScope Steel having been provided. DOTARS did not seek the Minister’s approval of this substantive change to the terms of the funding approval. In this light, the department also did not meet its obligations under FMA Regulation 13.

\textbf{Purpose of Regional Partnerships funding and project budget}

10.60 The Funding Agreement executed with the funding recipient did not accurately reflect the basis on which DOTARS had determined that it was appropriate to proceed with the Regional Partnerships funding, despite the spray dryer having already been purchased.

\footnote{\textsuperscript{895} A Regional Office evaluation, dated 24 February 2006, of the second Progress Report submitted by Sakai on 7 February 2006 noted that: ‘In discussion with the Regional Manager, it was decided that the letter sent to the grantee regarding the revision of outcomes for the project could be more appropriately captured by revising the ‘Project Outcomes’ table in the Funding Agreement. (An extra outcome would be added to reflect the achievement of the five-year contract with BlueScope Steel for of [sic] supply of spherical-granule mould flux below the existing outcomes.) I will prepare a variation to the Funding Agreement along these lines early next week.’ This did not occur. On 22 August 2006, DOTARS, via email, provided the funding recipient with a proposed change to the performance measure for the ‘Strengthened business viability of Sakai (CIC) Aust’ performance outcome in the Funding Agreement, to include ‘Specifically, a long term contract (five years or more) is put in place by the end of 2007 for Sakai CIC Pty Ltd to supply their new spherical mould flux product to Bluescope Steel.’ DOTARS requested that the funding recipient indicate its acceptance of the change to the outcomes table in its next Progress Report. It is not clear that an exchange of that nature would represent an effective variation of the Funding Agreement having regard for the requirement that the Funding Agreement can only be varied by written agreement. Regardless, in January 2007, DOTARS advised ANAO that it considered that the Funding Agreement had been varied through the December 2005 exchange of letters.}
10.61 DOTARS had decided that the Regional Partnerships funding would be applied to the installation of the spray dryer only, and that the cost of purchasing the equipment should be excluded from the project costs and the funding recipient’s partner contribution to the project. Despite this, Schedule 1 to the Funding Agreement stated that:

Regional Partnerships funding will contribute to the Project by funding the purchase and installation of the spray drying facility. The purpose for which Regional Partnerships funding will be used shall be referred to as the ‘Activity’.

The Activity Period commences on the Date of this Agreement and ends on 30 September 2006.

10.62 Consequently, both the Activity and Activity Period defined by the Funding Agreement encompassed the purchase of the equipment, which DOTARS was aware had already taken place some months earlier.

10.63 Further, the Budget stipulated in the Funding Agreement identified an applicant cash contribution of $1 388 100 and a total cash contribution budget of $1 663 100. This was the original budget submitted by the funding recipient in its February 2005 application, plus $25 000 GST on the Regional Partnerships grant payment. This is inconsistent with the revised budget submitted in March 2005 and also failed to exclude the equipment purchase costs.

10.64 As a consequence, the Activity and project Budget defined in the Agreement are inconsistent with the Milestones the funding recipient was required to complete in order to perform the Activity, which, as noted, related to the installation and product testing phases only.

Payments and acquittals

10.65 As discussed, the first payment was made on 20 December 2005, following receipt of a progress report which described the activities that had been undertaken. In order to obtain the second instalment of $115 000 (GST inclusive) (a further 46 per cent), the funding recipient was required to provide an acquittal showing that the previous Regional Partnerships payment had been fully expended, or evidence that the previous payment would be fully expended in the near future.

10.66 The funding recipient’s second progress report, provided to DOTARS on 6 February 2006, advised that the first payment had been allocated against

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896 This is the same as the purpose to which the then Minister was advised the Regional Partnerships funding would be put in DOTARS’ August 2005 assessment.
four invoices from one company, and one invoice from another company, totalling $119,266.81. All invoices were dated January 2006, indicating that the December payment was made in advance of expenditure requirements. The second payment was made on 27 February 2006.

10.67 A further consequence of the use of the short form Funding Agreement is that it did not require the funding recipient to provide any reporting on total project expenditure or the expenditure of its own contribution to the project until the Post Activity Report (which, as noted, is not required to be audited). As a result, despite the Commonwealth being a minority partner in a commercial project that the funding recipient was co-funding through accumulated reserves, DOTARS did not establish any requirements for the funding recipient to demonstrate that the payment of Regional Partnerships funds only occurred in relation to demonstrated need.

10.68 Nor did DOTARS document any consideration as to why the payment of Regional Partnerships funds should not occur in arrears upon identification of actual expenditure incurred, rather than simply upon reporting of activities undertaken. For example, there is no documented consideration as to why Regional Partnerships funding was to be paid before the construction phase of the project was complete or near completion, having regard for the interest foregone by the Commonwealth when payments of public money are made earlier than necessary.

**Final acquittal process**

10.69 ANAO provided DOTARS with a draft of the case study of this project on 4 September 2006.

10.70 The final payment of $45,000 (GST inclusive) was scheduled to be made on 30 November 2006, following acceptance by DOTARS of the Post Activity Report, due 31 October 2006, and a satisfactory site visit. DOTARS undertook a site visit in October.

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897 This company was not included in the companies that had provided the quotes submitted to DOTARS. There is no evidence of DOTARS querying this with the funding recipient. In April 2006, the funding recipient advised ANAO that the company that had provided the quote for this work were unable to supply the large number of tradesmen required for the job when the time came to commence, the second company was recommended to it and the two companies had worked together to complete the job.

898 In contrast, the Long Form Funding Agreement provides for grant recipients to include a summary of expenditure of cash contributions from the recipient and other partners in each progress report, as well as acquitting expenditure of Regional Partnerships funding received to date.
10.71 The funding recipient provided DOTARS with a final report for the project on 31 October 2006. On 15 December 2006, DOTARS wrote requesting that it provide a number of outstanding items in relation to the Post Activity Report, including a signed statement of expenditure as required under the Funding Agreement. In addition, the department requested copies of receipts for the major purchases related to the expenditure statement (including evidence of the cost of the spray drying machine). The department also advised the funding recipient that it required this statement to be certified by an Independent Auditor (although this was not a requirement of the Funding Agreement).

10.72 The Funding Agreement also required the Post Activity Report to provide a summary of the applicant’s performance against the Outcomes and Milestones set out in the Agreement. DOTARS’ 15 December 2006 request to the funding recipient also requested confirmation that the five year contract with BlueScope Steel was in place, or confirmation from BlueScope of their intention to contract for five years and from when that would occur.

10.73 DOTARS advised that payment of the final instalment of Regional Partnerships funds could not be processed until it received and was satisfied with the outstanding information.

10.74 The funding recipient provided DOTARS with an audited Statement of Expenditure for the project on 21 February 2007 which identified that, to that date, it had expended $1 990 189 on the project. This was $602 089 or 43 per cent more than the $1 388 100 proposed as the applicant’s cash contribution in the Regional Partnerships application and DOTARS’ assessment provided to the then Minister. As noted, the application had stated that, together with the $2 million upgrade of its facilities that was also being undertaken, the combined cost of $3 638 100 would be over-capitalising its plant, and that the $250 000 funding from Regional Partnerships would bring its own construction costs back to a level where it could go ahead.

10.75 In March 2007, DOTARS advised ANAO that the funding recipient had reached an in-principle agreement with BlueScope Steel in relation to the five year contract. By 21 May 2007, the date at which ANAO fieldwork for this project was completed, the contract had yet to be finalised and the final instalment of Regional Partnerships funds had yet to be paid. On 10 October 2007, DOTARS advised ANAO that:
The funding recipient is providing monthly updates to DOTARS regarding the status of the contract with BlueScope Steel. The contract has been negotiated but is awaiting final signature from BlueScope.
11. Aerox Odour Control Filters for Grape Marc Separator/Dryer

This case study examines RP01578 Aerox Odour Control Filters for Grape Marc Separator/Dryer which was to involve the purchase and installation of ‘Aerox’ odour control filters and the electrical supply and installation for a grape marc separator/drying facility to be built at Nuriootpa in South Australia. The funded project was high risk as it involved a recently established company with no track record of profitable operations implementing a new process and relying on an undeveloped market for most of its revenues. There were two assessments of this application; the first did not recommend funding. A second assessment, requested by the then Parliamentary Secretary, led to a new recommendation that funding be approved.

Introduction

11.1 On 13 December 2004, Coonawarra Gold Facilities Pty Ltd (Coonawarra Gold) submitted an application for funding under the Regional Partnerships programme for a project titled ‘Aerox Odour Control Filters for Grape marc separator/dryer’. Coonawarra Gold was seeking $598 000 (plus GST) as part of an overall project valued at $4 million.

11.2 The overall project was to involve the construction of a grape marc separator/dryer plant on the Tarac Technologies Pty Ltd site at Nuriootpa at the northern end of the Barossa Valley in South Australia. The plant would separate ‘spent marc’ into three products: grape marc meal and grape seed meal (for stockfeed) and grape seed. The grape seed would then be transferred to a Coonawarra Gold mill at Millicent in South East South Australia where it would be milled to produce grape seed oil.

11.3 Coonawarra Gold Facilities Pty Ltd was registered as a company on 25 March 2003. The ‘preliminary’ business plan budget appended to the Regional Partnerships application showed no revenues prior to September 2003. Sales of grape marc products were projected to comprise 92 per cent of company revenues. The remainder was to come from ‘toll pressing’ charges from pressing other seeds when the current year’s marc was fully processed.

899 This is the date that the South East South Australia ACC (now Limestone Coast ACC) forwarded the application to DOTARS’ South Australian Regional Office.

900 Grape marc is the product left after the grape juice has been crushed from grapes for wine (that is, marc involves grape skin and grape seeds).
11.4 In this context, Coonawarra Gold was essentially a new venture set up to implement the plan to process grape marc and sell stock feed and grape seed oil. In this respect, Applied Financial Diagnostics⁹⁰¹ advised ANAO that:

From a commercial investor’s perspective (either debt or equity), any new venture is a far riskier investment than one in an established business with a demonstrable track record.

New processes in start-up enterprises are notorious for under-delivering to expectations and costing more money and time to implement than expected, followed by more time than expected in understanding the process and to iron out bugs. In a larger, established company process development would be undertaken under a research and development budget, which is most often viewed as long term expenditure with the potential for future returns, rather than as an immediate income-producing exercise.

11.5 Construction of the grape marc separator/drying plant commenced in January 2005. In submitting its Regional Partnerships application in December 2004, Coonawarra Gold requested an immediate answer from DOTARS as the filters were said to have a critical start date around 1 February 2005. On 6 January 2005, DOTARS’ South Australian Regional Office sought clarification and additional information in relation to the application. The Regional Office also advised the applicant that:

Unfortunately I am not in a position to provide an immediate answer as the application needs to go through an assessment stage first (which will include independent advice on the financial viability of your organisation and possibly a full project viability assessment) with the final decision being made by the honourable John Cobb MP, Parliamentary Secretary.

…In view of the above, it would appear unlikely that a decision will be made in this matter before 1st of February 2005 as requested by you. If the overall project must commence (or has commenced) by this date there may be the possibility of Regional Partnerships funding being used to assist in funding a “stand alone” component of the project such as the installation of the filters.

11.6 In response, on 10 January 2005, Coonawarra Gold advised DOTARS that:

Our aim is to have the Aerox Odour Control Filters only funded under this program. These units form a discrete aspect of the project and were stipulated

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⁹⁰¹ To assist with analysis of this and a number of other Regional Partnerships projects, ANAO engaged treasury specialists Applied Financial Diagnostics Pty Ltd to provide advice on financial risks (including viability risks).
by the EPA [South Australian Environment Protection Authority] after commencement of the project as a requirement to obtain their approval.

11.7 On 28 January 2005, DOTARS advised the applicant that:

Having looked at the application and supporting documentation it is apparent that the actual project you are seeking funding for is the provision and installation of the “Aerox” filters and not the overall establishment of the plant. As the installation of the filters is to be a “stand alone” component of the establishment of the plant it is only the costs associated with this that can be taken into consideration.

As such the request for funding from Regional Partnerships of $598 000 would appear to cover the total project cost with your organisation not contributing to this “component” or stage of the larger project.

In this regard, you will need to “revise” your budget to show the total project cost being the cost of purchasing and installing the filters and amend the amount requested from Regional Partnerships to assist with this “stage”.

11.8 On 31 January 2005, the applicant advised DOTARS that:

We reiterate that the total funding initially requested was only 15 per cent of the overall Project Cost. However, in the interests of expediency, we are happy to amend our budget as follows:

Supply and Install Aerox Control Filters 30 per cent of $498 000.00 = $149 400.00
Mechanical Installation and Commissioning 30 per cent of $277 650.00 = $83 295.00
Electrical Supply and Installation 40 per cent of $402 353.00 = $160 941.00
TOTAL REQUESTED $393 636.00

First project assessment and recommendation that funding not be approved

11.9 DOTARS provided the then Parliamentary Secretary with two assessments of this application. As is discussed further below (see Figure 11.5), the second assessment was undertaken following advice to the department that the then Parliamentary Secretary was inclined to support funding for the project but had requested further information. In providing the second assessment to the then Parliamentary Secretary, which recommended funding approval, DOTARS stated that:

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902 The EPA is an independent statutory authority that is responsible for the protection and enhancement of air and water quality, and control of pollution, waste and environmental noise. Source: EPA, Annual Report 2004–05, p. 4.
This project was originally not recommended and sent to Mr Cobb for consideration in Package 90. The Department considers this Package 112 brief to replace the Package 90 brief and, therefore, requests that the latter be disregarded.

11.10 In respect to both assessments, the then Parliamentary Secretary was advised that the South East South Australia ACC had recommended the project and rated it a high priority for its region. However, the department’s own assessment against the Programme assessment criteria reached markedly different conclusions.

11.11 DOTARS’ first assessment provided to the then Parliamentary Secretary on 18 March 2005 recommended that funding not be approved. In respect to the Programme assessment criteria, the department concluded that:

- the partnerships and support criterion had been satisfied;
- the application partially satisfied both the applicant viability criterion and project viability criterion. The application was assessed as representing a ‘medium’ risk in terms of both criteria; and
- the outcomes criterion was not satisfied.

**Assessment of viability risks**

*Analysis of applicant’s financial position*

11.12 As part of its first assessment, on 10 January 2005, DOTARS requested that the applicant provide the department with financial statements for the previous three years. At the time it applied for funding, the company had been in existence for 21 months. As a result, it was not possible for the applicant to provide financial statements for the last three years.

11.13 On 18 January 2005, the applicant provided DOTARS with an unaudited profit and loss statement for the 2003–04 financial year and unaudited balance sheets as at 30 June 2004, 30 November 2004 and 31 December 2004 for Coonawarra Gold Facilities Pty Ltd. The applicant advised DOTARS that it would forward audited statements when they arrived. However, at no stage of its assessment did DOTARS obtain audited financial statements.

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903 The applicant also provided DOTARS with an unaudited profit and loss statement for 2003–04 and unaudited balance sheet as at June 2004 for Coonawarra Gold Pty Ltd, another company in the group.
11.14 The unaudited financial information provided by the applicant to DOTARS on 18 January 2005 revealed that:

- for 2003–04, the only income earned was $99 925 for ‘toll crushing’, with a gross profit of $87 569 after deducting cost of sales of $12 356. After deducting overhead expenses of $225 006 and interest and business establishment expenses of $34 545, the company made an overall net loss for the year of $171 983; and

- as of 31 December 2004, net assets of the company were $79 831. This comprised current assets of $1 063 999, non-current assets of $4 652 240, current liabilities of $685 084 and non-current liabilities of $4 951 324.

*Working capital from the applicant*

11.15 The purchase, installation and commissioning of the filters was part of the larger project of establishing the grape marc separator/dryer plant. In its December 2004 Regional Partnerships application, Coonawarra Gold stated that it had contributed $3 011 600 in working capital\(^{904}\) to the overall project. However, according to information provided by the applicant to DOTARS on 18 January 2005, Coonawarra Gold had working capital of $378 915 as of 31 December 2004. In this context, Applied Financial Diagnostics advised ANAO that:

Coonawarra was a start-up venture that raised capital to put in place infrastructure and processes from which revenue were to be generated. Very little revenue was to be earned before all the infrastructure was in place and operating. As such, the issue with the greatest potential to bring about failure was the cash ‘burn rate’. This is the amount per month that expenses and capital expenditure exceeds revenues. The ‘time to ruin’ is the available cash divided by the cash burn rate. If available cash is expended before revenues kick in, the company is forced to seek further capital or fold.

11.16 There was no analysis documented by DOTARS of the gap between the working capital that was said to have been contributed by the applicant and its working capital position at the time of its Regional Partnerships application.

*Business plan*

11.17 Appended to the Regional Partnerships application was a preliminary business plan for Coonawarra Gold. The document is undated but appears to

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\(^{904}\) Working capital is current assets less current liabilities.
have been produced in the latter half of 2003^905 (that is, at least 12 months prior to the Regional Partnerships application being submitted). It was accompanied by:

- a supply agreement with Tarac Technologies dated 21 July 2003;
- an unexecuted agreement with Mataranka Grains dated 29 April 2003;
- a Coonawarra Gold Pty Ltd balance sheet dated as of April 2003;
- budgets for the years ending June 2004, June 2005 and June 2006; and
- some background on Grape Seed Oil Australia Pty Ltd and some information from Microwave Processing Technologies Pty Ltd.

11.18 The business plan did not analyse the size of the existing market for grape seed oil nor what percentage of that market Coonawarra Gold aimed to capture. It also did not mention the existing size of the stock feed market, existing sources for stock feed or how Coonawarra Gold planned to fit into that market.

11.19 Further evidence that the business plan was no longer current is apparent from the supply contract for grape meal. Attached to the preliminary business plan was an unexecuted contract with Mataranka Grains Pty Ltd. However, according to the December 2004 Regional Partnerships application, Coonawarra Gold had an exclusive supply contract for grape marc and grape seed meal with a different company (Castlegate VGS Pty Ltd). In this respect, Applied Financial Diagnostics advised ANAO that:

This change of suppliers and the absence of evidence of the new contract both increase project risk. It would be prudent for financiers to determine why the original agreement was terminated and the actual terms of the new agreement (rather than to rely on the outdated agreement provided by the applicant).

11.20 DOTARS did not undertake these inquiries.

*Cash flow and sensitivity analyses*

11.21 In terms of cash flow and sensitivity analyses in the business plan, Applied Financial Diagnostics advised ANAO that:

It is normal in a business plan to calculate the internal rate of return and/or net present value of the project, and to include profit sensitivities to key

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^905 This is on the basis that the first budget year included is for the year ended June 2004 and the agreements included were dated April and July 2003.
assumptions. In this case, sensitivities to oil extraction rates and meal sales, for instance, would have been useful.

Sources and uses of cash over the life of the project (cash burn) would be essential in the case of Coonawarra as it is highly reliant on receiving $300 000 from Zero Waste SA as well as the Regional Partnerships Programme grant. Failure to get either would appear to threaten the viability of the project. The Coonawarra business plan had none of these analyses.

11.22 DOTARS did not request such analyses from the applicant, or undertake the analyses itself. In this respect, DOTARS advised ANAO in March 2007 that:

At the time this project was assessed, when a project was not recommended to the then Parliamentary Secretary for approval on the grounds of failing to meet an eligibility criterion, an independent financial viability assessment was not necessarily undertaken.

11.23 Notwithstanding this, having regard to the fact that Ministers have retained the discretion to approve projects that the department assessed as not satisfying one or more criterion, it is appropriate and necessary for DOTARS to undertake a comprehensive and rigorous assessment of all applications for funding. This is just as important for projects not recommended for funding so as to fully inform the Ministerial decision, including identifying areas where, should the Minister decide to approve funding notwithstanding the department’s assessment, it would be prudent to include conditions on the funding approval.

**ANAO conclusion**

11.24 DOTARS’ assessment was deficient in terms of the financial analysis undertaken on the applicant and the project as presented in the Regional Partnerships application and the business plan included with the application. Given that the project involved a recently established company with no track record of profitable operations implementing a new process and relying on an undeveloped market for most of its revenues, more rigorous analysis of the available information would have been appropriate.

**Outcomes criteria and project eligibility**

11.25 The Regional Partnerships Programme Guidelines in place at the time the application was submitted and assessed (November 2004 version) stated that project proposals requesting funds for retrospective costs are not eligible for funding. The Internal Procedures Manuals in place at the time the
application from Coonawarra Gold was received (September 2004 version) and the assessment was completed (February 2005 version), both advised as follows in relation to retrospective costs:

Retrospective funding is defined as funding to meet any expenditure, or commitment to expenditure, prior to the applicant being advised in writing the Minister has approved the project. Whilst the date of formal advice that a project has been approved is the test of whether a payment would be retrospective or not, the department’s advice is that proponents not commit to expenditure on a project prior to the Funding Agreement being signed by both parties.

...Retrospective funding is precluded under Regional Partnerships for two reasons. First, by retrospectively funding a project, the Government may be perceived as having been unduly influenced or having agreed to fund a project before due process was followed. Secondly, if an applicant has been able to secure funding to commence a project (whether this be capital or borrowings), generally speaking it is unlikely that it will be able to demonstrate a sufficient level of need for Australian Government support.

11.26 Construction of the grape marc separation/dryer plant commenced in January 2005, shortly after the Regional Partnerships application was submitted in December 2004. Accordingly, to be eligible for funding under the Regional Partnerships Programme Guidelines, the project to install Aer ox odour control filters had to be able to be seen as a stand-alone project from the project to which the applicant had already committed and commenced.

11.27 The key to satisfying this requirement was the advice from the applicant that the EPA requirement for the installation of the filters came after planning and budgeting for the overarching project had been completed. This was an important element in DOTARS’ assessment processes. For example, advice to the South Australian Regional Office from National Office on 10 May 2005 was that:

It certainly looks as if the outcomes are worthy of our support and it has been a matter of timing that the requirement for the filters was not identified by the Environmental Protection Agency (sic) until well after the project was initiated. [DOTARS emphasis]

11.28 Similarly, comments from the South East South Australia ACC included in both of DOTARS’ project assessments provided to the then Parliamentary Secretary included the advice that:
The request to the Regional Partnerships Programme is to fund a portion of two Aerox Odour Control Filters which were a last minute stipulation by the EPA.

11.29 There was no questioning by DOTARS of this key aspect of the application, notwithstanding that documentation attached to the application indicated that the EPA odour control requirements should already have been factored into the project as a necessary element or, at a minimum, could have been reasonably foreseen, as follows:

- performance of the July 2003 agreement (which was appended to the Regional Partnerships application) between Coonawarra Gold and Tarac Technologies for the supply and subsequent treatment of spent marc was subject to four conditions being met, including:

  • the obtainment by Coonawarra Gold or, where appropriate, Tarac, and at all times at Coonawarra Gold own cost, of all necessary consents and approvals that may be required with respect to the drying equipment, including any consents or approvals by the Environmental Protection Authority or the local government by no later than 31 December 2003 or such other time as may be agreed between the parties in writing;

  and

  • the Provisional Development Plan Consent (which was also appended to the Regional Partnerships application received from Coonawarra Gold) granted by Light Regional Council on 22 September 2004 for alterations and additions to Tarac Technologies’ existing operations for a spent marc drying and pelleting facility required Tarac Technologies to contact the EPA before acting on the development approval so as to ascertain licensing requirements. It was stated that additional conditions of licence would include, but not be restricted to, compliance with specified odour emission rates. Given the applicant had commenced construction well before any funding decision had been taken in relation to Regional Partnerships funding, it is reasonable for DOTARS to have taken the position that the company had done so in the knowledge of the odour control standards it would be required to satisfy in order to construct and operate the plant. As no funding from Regional Partnerships could be assumed, the commencement of construction essentially represented a commitment by the applicant to the necessary expenditure on odour control.
11.30 DOTARS also did not seek or obtain any documentation from the applicant to substantiate the advice that the requirement for the installation of the filters was ‘stipulated’ by the EPA after the project had commenced. In this respect, the EPA advised ANAO in December 2006 that:

The EPA does not have any direct communication with Coonawarra Gold. All potential environmental issues were addressed through the Tarac Technologies Pty Ltd licence issued by the EPA in relation to activities involving its marc drying and pelleting facilities. It is the understanding of the EPA that Coonawarra Gold will have ownership of equipment and Tarac will operate the facility.

The EPA has not placed any specific requirements within the Tarac licence in relation to use of equipment. An EPA licence specifies expected standards that are to be met and does not specify how those standards must be met.

Therefore, in response to your query, the EPA has not provided any direct advice to Coonawarra Gold or Tarac requiring the installation of two Aerox odour control filters. However, the EPA strongly encourages companies to use best available technology to meet licence conditions and also encourages actions to be taken that contribute to “beyond compliance” where appropriate.

11.31 In terms of the Tarac Technologies licence, the EPA further advised ANAO in January 2007 that:

An amended EPA licence was issued to Tarac Technologies Pty Ltd on 13 September 2005. The Licence contains a condition requiring the company to meet specified air emission standards and submit verified stack test results to the EPA by 31 March 2006.

However, these requirements have been communicated to the company earlier in a response (dated 10 September 2004) to the development application for the grape marc drier and pelletising facility that was lodged in 2004.

11.32 Shortly after the EPA correspondence of 10 September 2004 communicating the air emission standards that the grape marc separator/dryer plant would be required to meet, provisional development plan consent was granted by Light Regional Council (on 22 September 2004). As noted above, this consent (which referenced the odour control standards to be required) was attached to the Regional Partnerships application.

**ANAO conclusion**

11.33 As a result of insufficient rigour in the assessment process, this project was approved on the basis of unsound advice that the EPA had stipulated the installation of Aerox odour control filters well after the overall project had
been initiated. Specifically, advice provided to the then Parliamentary Secretary by DOTARS was incorrect in two important respects:

- Aerolodour control filters had not been specified as a requirement by the EPA. Whilst the EPA licence specifies air emission standards, it does not stipulate how these standards are to be met; and

- the EPA’s emission standards had been advised to the licence holder on 10 September 2004, shortly before Council issued its provisional development plan consent (which was the first attachment to the Regional Partnerships application submitted by Coonawarra Gold). This advice was provided by the EPA three months prior to the Regional Partnerships funding application being submitted and four months prior to construction commencing.

11.34 As a result, the project was ineligible for funding under the terms of the Regional Partnerships Programme Guidelines. DOTARS’ first assessment of this project did not address these issues.

Departmental recommendation to not approve funding

11.35 On 18 March 2005, the first assessment of this project was provided to the then Parliamentary Secretary as part of an assessment package of 15 projects. Of these, six were recommended for approval of funding and nine were not recommended for funding. The projects not recommended included the application from Coonawarra Gold. DOTARS’ summary of the project and the reasons for its recommendation against funding being approved is illustrated by Figure 11.1.

Figure 11.1

First project assessment: recommendation to not approve funding

This project will result in the installation of special air filters in a new grape marc separator and dryer facility which once completed will enable the applicant to take grape marc waste from wineries and separate it into 3 products. The filters are an Environment Protection Authority requirement. Regional Partnerships funding would be used towards the purchase and installation of two ‘Aerolodour’ odour control filters, electrical supply and installation and commissioning of the plant. This project is not recommended on the basis that the outcomes from Regional Partnership funding are not clear given that the installation of the filters is an intrinsic part of the larger project and the project has already commenced.

On 10 May 2005, the applicant contacted DOTARS’ South Australian Regional Office noting that the application had been submitted five months earlier and seeking advice on what stage the application was up to. On this date, DOTARS National Office advised the Regional Office that the assessment was with the then Parliamentary Secretary and that a decision on funding was expected that week.

Also on 10 May 2005, after considering DOTARS’ assessment recommending that funding not be approved, the then Parliamentary Secretary requested further information on the project. Figure 11.2 illustrates DOTARS’ records of the request for further information.

**Figure 11.2**

**Further advice requested by then Parliamentary Secretary**

Mr Cobb is inclined to support funding for this project. However, he has asked for further information before making a final decision on funding. Mr Cobb has asked for the following:

1. external financial and project viability assessments to be undertaken;
2. advice on whether the applicant has secured commercial borrowings to fund the overall project; and
3. advice as to whether there are any competitive neutrality issues with the project.

I will fax through the signed-off assessment.

Source: Email correspondence between the Departmental Liaison Officer to the Office of the then Parliamentary Secretary and DOTARS dated 11 May 2005.

**Second project assessment and recommendation that funding be approved**

The second assessment of this project, undertaken by DOTARS between 11 May 2005 and 20 June 2005, recommended that funding be approved. This assessment was focused on addressing the three issues raised by the then Parliamentary Secretary in May 2005 following his consideration of DOTARS’ first assessment.

**External applicant and project viability assessments**

The various versions of the Regional Partnerships Internal Procedures Manual that have existed throughout the course of the Programme have included criteria for when external advice on viability issues should be sought in relation to individual applications. In particular, relatively clear criteria were included in the Manual that applied between 1 July 2003 and 22 June 2004. The threshold matrix included in that Manual required a sliding scale of applicant and project viability checks based on consideration of applicant type, project type and amount of funding being sought. An external assessment of the
The project’s commercial risk/sustainability was required for all projects requesting funding of $250,000 or more, regardless of the type of applicant.

11.40 The Manual that applied between 23 June 2004 and February 2005 had less stringent and clear criteria, but still required that all applications for funding of $50,000 or more from either non-profit organisations for commercial activities or from for-profit organisations be subject to at least an external assessment of the applicant’s financial risk status. The requirement for an assessment of a project’s commercial risk/viability was to be determined on a case by case basis, regardless of the applicant type, project type or amount of funding being sought.

11.41 The Internal Procedures Manuals that have applied since February 2005 have still set out criteria for determining when an external viability assessment should be commissioned in respect of individual applications. However, those criteria are less clear than those included previously, being based on the departmental assessor’s judgement regarding the perceived project risk. In particular, a risk-based matrix is no longer included. Instead, the Manual has required that external viability assessments should be undertaken when the assessor considers the project viability to be a medium to high risk (with no distinction being made in the Manual with regard to applicant or project type). Such judgements are, necessarily, being exercised in the absence of the viability analysis that would result from an external assessment. Applicant Credentials Verifications are identified as being mandatory for all private enterprise applicants.

11.42 In this context, on 6 January 2005, DOTARS advised the applicant that independent financial advice on the applicant’s viability would be undertaken as part of the department’s assessment of the application. The applicant was also advised on this date that a project viability assessment may also be undertaken. However, in undertaking its first assessment of the project, DOTARS did not commission independent advice on either the applicant’s viability or the viability of the project.

11.43 As noted, on 10 May 2005, the then Parliamentary Secretary requested that DOTARS undertake external financial and project viability assessments in respect to this application.

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906 The Internal Procedures Manual states that an Applicant Credentials Verification is conducted by an external consultant to confirm the ownership and structure of private enterprise applicant organisations. Applicant Credentials Verifications examine only applicant viability risks.
Applicant viability assessment

11.44 On 11 April 2005, the Office of Regional Affairs within the South Australian Department of Trade and Economic Development had obtained a financial capability assessment and feasibility study review of Coonawarra Gold Pty Ltd and Coonawarra Gold Facilities Pty Ltd. This was in the context of assessing Coonawarra Gold’s application under the Regional Development Infrastructure Fund for $78 500 to cover 50 per cent of the cost of providing a gas supply to the company’s Millicent plant.\(^{907}\)

11.45 On 17 May 2005, the applicant contacted the then Parliamentary Secretary’s Office and suggested that the assessment undertaken on behalf of the State Government be used to expedite the Regional Partnerships assessment process.\(^{908}\)

11.46 Rather than commission its own external viability assessment of the project for which $393 636 in Regional Partnerships funding was being sought (being the establishment of a grape marc separator/dryer plant, using new technology, on the Tarac Technologies Pty Ltd site at Nuriootpa), DOTARS obtained a copy of the assessment of the applicant’s viability by an accounting firm commissioned by the State Government in relation to the separate application for State Government funding. In relation to the department not obtaining its own external viability assessment of this project, DOTARS advised the Senate Rural and Regional Affairs and Transport Legislation Committee that:

That is not unusual in cases where we consider that a reputable financial viability assessment has been done by another party.\(^{909}\)

11.47 In this respect, ANAO notes that reference to the use of viability assessments undertaken by other parties was first included in the February 2005 version of the Internal Procedures Manual, which was the version applicable at the time of this assessment. A risk criteria checklist included in this version to assist assessors to make a decision about when an external

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\(^{907}\) In March 2007, DOTARS advised ANAO that: ‘Information from the SA Govt website (http://dataserver.planning.sa.gov.au/publications/1094p.pdf) indicates (p25) that the funds approved were for “Coonawarra Gold at Nuriootpa – $78,500 to assist with the upgrade of the Nuriootpa town gas regulator and a gas meter”—not for the Millicent plant as indicated in the Financial Viability report undertaken on behalf of the SA Govt.’

\(^{908}\) A DOTARS file note made on or about 8 June 2005 states that: ‘the viability report has been passed to the Minister and is being considered.’

\(^{909}\) Senate Rural and Regional Affairs and Transport Legislation Committee, Hansard, 17 February 2006, p. RRA&T12.
viability assessment should be carried out advised that if the answer to the question ‘Is a pre-existing FVA\textsuperscript{910} for the project already available that demonstrates the viability of the project from an independent source, for example from State Governments or from financial institutions?’ was yes, there was no need to proceed with an FVA. In this case, the viability assessment commissioned by the State Government related only to applicant viability and did not demonstrate the viability of the project for which Regional Partnerships funding was being sought (this issue is discussed further at paragraphs 11.52 to 11.61).

11.48 The report of the assessment commissioned by the State Government stated that the financial capability analysis undertaken on the applicant and Coonawarra Gold Pty Ltd as at 30 June 2004 had found that:

both companies had a poor solvency, liquidity and profitability position.

11.49 The report also drew attention to gaps in business plan information compared to the assessor’s expectations, particularly with respect to financial analysis. A specific concern was that very little detail had been provided in terms of the assumptions used in the financial estimates and the absence of sensitivity analysis for different scenarios. The overall recommendation was that:

Based on the information available and the procedures undertaken we found little comfort/support of the ongoing financial viability of the organisations and consider that little analysis/consideration has been given to the project risks and financial impact.

We note however, that the proposed financial returns could be significant should the business plan be achieved. The projected growth in turnover of the company ($2.5 million in 2005, $15 million in 2006 and $17 million in 2007) is significant compared to the company’s combined annual sales revenue for 2004 of $100 000.

We understand separate analysis is being undertaken to review the cost of the grant versus the associated benefits to South Australia.

11.50 However, the concerns regarding the financial viability of the applicant identified in the report were not emphasised by DOTARS in its second assessment of the Regional Partnerships application. Specifically, on 27 May 2005, the Regional Office advised National Office that:

\textsuperscript{910} The Internal Procedures Manual defines the term Financial Viability Assessment (FVA). Financial Viability Assessments can assess applicant viability risks, project viability risks, or both. Accordingly, ANAO has used the term external viability assessment.
It should be noted that, whereas the applicant is Coonawarra Gold Facilities Pty Ltd the assessment was based on both that organisation and Coonawarra Gold Pty Ltd. The applicant’s covering letter\textsuperscript{911} makes comments on this.

As can be seen from the PKF report, they consider that little analysis/consideration appeared to have been given to the project risks and financial impact but that the proposed financial returns could be significant.

Whilst the State Government has taken this information into account when awarding a grant of $78,500.00 it should be noted that their level of risk is lower than the Commonwealth’s, however both the Australian Government and State Government have significantly lower levels of risk than the applicant.

It is my view that the likely job outcomes and other benefits, such as a cheap source of animal feed (which may well be of increased benefit during the drought), make the risk to the Commonwealth reasonable in this case. To further reduce the risk we could make smaller but more frequent payments to the applicant with a higher than normal final payment of say 15 per cent.

\textbf{11.51} Consistent with this approach, DOTARS’ second assessment of the project, provided to the then Parliamentary Secretary on 20 June 2005, did not reflect the applicant viability risks identified in the report. In particular, no reference was made to the poor solvency, liquidity and profitability position of the applicant and a related company identified in the report (see Figure 11.3).

\textbf{Figure 11.3}

\textbf{DOTARS’ assessment of applicant viability}

\begin{itemize}
  \item \textbf{Applicant Viability}
  The applicant is assessed as a medium risk.

  The applicant is considered medium risk in that the State Government has undertaken an external viability assessment through PKF Chartered Accountants and has approved funding for part of the overall project based on this assessment.

  The applicant has no record in the successful management of Government grant funds but is a part of a successful group of companies and has been approved for State Government and Bank finance. The applicant has no history of funding grants from Commonwealth, State or Local Government.

  The application satisfies this criterion.
\end{itemize}

Source: DOTARS project assessment dated June 2005.

\textsuperscript{911} No covering letter from the applicant was held on the DOTARS records made available to ANAO, or provided subsequently to ANAO by DOTARS.
Project viability assessment

11.52 In its Regional Partnerships application, Coonawarra Gold stated that:

The project is the construction of an innovative $4 million Grape Marc Dryer and Separator plant (patent pending) in the Nuriootpa and Millicent regions of South Australia. This plant utilises state-of-the-art technology, and will accept waste grape marc from 70 per cent of the Australian wine industry, and produce three saleable produces from this waste material, namely grape marc meal and grape seed meal (which are both exported as stock feed across Australia), and grape seed oil (which will be exported internationally and sold throughout Australia as an import substitution product).

...The unique dry separation process (patent pending) utilizes latest technology...

11.53 One of the appendices to the application was a 17 January 2001 consultancy report provided to the EPA. The application drew on this report as evidence that the project would not duplicate or compete with existing businesses but would transform waste grape marc in a new and different way (that is, waste grape marc would be transformed into stock feed and grape seed oil for export).

11.54 The January 2001 consultancy report was titled ‘Opportunities for the re-use of winery industry solid wastes’. It had been supported by the South Australian Waste Management Committee, through its Rural Grants Waste Management Grants Scheme, ‘on the potential options for the future treatment and re-use of winery solid waste’. The stated objectives of the research were to:

- evaluate the quantities, types and regional distribution of winery solid wastes in South Australia;
- evaluate the effectiveness and sustainability of current waste treatment practices;
- examine the opportunities for the re-use of these wastes as value-adding products for existing composts and mulches; and
- provide a preliminary appraisal of infrastructure impediments and opportunities for enhanced solid waste recovery and re-use.

11.55 On 17 February 2006, DOTARS advised the Senate Rural and Regional Affairs and Transport Legislation Committee that its assessment of the application:

...did include an assessment of the process in addition to the viability of the company. The assessment of the company was, as we said, undertaken on
behalf of the South Australian government. There was additional information, and the advice we received was that manufacturing grape waste into stockfeed and grape seed were both commercially viable.\footnote{912}

11.56 DOTARS subsequently advised the Senate Rural and Regional Affairs and Transport Legislation Committee that the source of the additional information on project viability was PPK Environment and Infrastructure Pty Ltd and the applicant.\footnote{913} The report referred to by DOTARS was the January 2001 consultancy report attached by Coonawarra Gold to its application.

11.57 In this context, the consultancy report was not undertaken to assess whether manufacturing grape waste into stockfeed and grape seed was commercially viable.\footnote{914} In fact, the report made no comments on the use of waste for manufacturing into stockfeed. In terms of the potential for grape seed oil production, the report commented as follows:

If stalks are stripped from grapes prior to crushing, winery marc consists of approximately 30 per cent seeds and 70 per cent skin and pulp. Currently there is no commercial grape seed oil production within Australia and grape seed oil is imported from Europe.

Research on the feasibility of establishing a grape seed oil production industry in Australia is currently being undertaken. This was initiated through a partnership of EcoRecycle Victoria, the Cooperative Research Centre for Food Manufacturing and Packaging Science and the Australian Centre for Oil Seed Research. This feasibility study has a national focus and has involved estimating market opportunities, and the logistics of manufacturing grape seed oil.

Unfortunately the price of imported grape seed oil from the EU is very low because of tax incentives provided to these producers.


\footnote{913} Senate Rural and Regional Affairs and Transport Legislation Committee, \textit{Answers to Questions on Notice: Additional Budget Estimates February 2006}, Question no. REGS 10.

\footnote{914} ANAO's case study of this project was provided to DOTARS on 29 January 2007. On 14 March 2007, DOTARS advised the Senate Standing Committee on Rural and Regional Affairs and Transport of the following in relation to the advice provided to the Senate Rural and Regional Affairs and Transport Legislation Committee hearing on 17 February 2006:

'It has now been brought to my attention that while the assessment undertaken by PKF Chartered Accountants and the Environment Protection Agency study undertaken by PPK Environment and Infrastructure Pty Ltd considered viability aspects of the processing of grape marc, neither specifically concluded the process by which Coonawarra Gold planned to manufacture grape waste into stockfeed and grape seed to be 'commercially viable.'
11.58 In this context, in its advice to ANAO, Applied Financial Diagnostics stated that:

In the business plan, Coonawarra lists the following issues under ‘Business Risks’: the relationship with Tarac as they control the grape marc supply; the potential for Tarac to break the agreement to supply Coonawarra with spent marc through Coonawarra’s contractual non-performance; competing companies taking market share; and mechanical breakdown of manufacturing processes.

However, they do not mention the three risks that are, in our opinion, much more significant, namely: start-up company; reliance on an untried process; and targeting undeveloped local and/or export markets.

11.59 In terms of DOTARS’ assessment, Applied Financial Diagnostics advised ANAO that:

There does not appear to have been any questioning of or investigation into the nature, degree of complexity and risk of failure of the new process to dry and separate grape marc and extract grape seed oil by cold pressing, as designed and patented by Coonawarra.

There does not appear to have been any questioning of or investigation into the assumptions made by Coonawarra as to the size of the markets for grape seed oil and grape marc stock feed, nor for the anticipated market share that Coonawarra would capture.

11.60 These deficiencies are reflected in the department’s assessment of project viability advised to the then Parliamentary Secretary on 20 June 2005. The department’s conclusion that the application satisfied the project viability criterion was based solely on high level comments made in the report about the proposed financial returns and the employment outcomes proposed by the applicant. These considerations were assessed as satisfying any risk the Commonwealth may have (see Figure 11.4).
Figure 11.4
DOTARS’ assessment of project viability

- Project Viability
  
The project is assessed as a medium risk.

  The cost of the filters has been supported by quotes and is considered realistic. The State Government has undertaken an external viability assessment through PKF Chartered Accountants and whilst this shows that little consideration appears to have been given to the project risks the proposed financial returns could be significant. This and the proposed employment outcomes would appear to satisfy any risk the Commonwealth may have. The Department considers it possible to manage this risk through the Funding Agreement.

  The application satisfies this criterion.

Source: DOTARS project assessment dated June 2005.

11.61 As shown in Figure 11.4, DOTARS advised the then Parliamentary Secretary that any viability risks could be managed through the Funding Agreement. However, the Funding Agreement prepared and executed by DOTARS following approval of funding by the then Parliamentary Secretary on 20 June 2005 included no specific measures to address viability risks associated with this project.915 In particular:

- the payment arrangements specified in the Funding Agreement did not involve ‘smaller but more frequent payments to the applicant with a higher than normal final payment’ as the Regional Office had proposed (see paragraph 11.50). The Funding Agreement provided for the approved Regional Partnerships funding to be paid in four instalments, with a significant proportion (40 per cent) to be paid in advance upon signing of the Agreement. The final payment of 10 per cent was to be paid on acquittal; and

- no other changes were made to the Long Form Standardised Funding Agreement used for Regional Partnerships projects in order to address or manage the financial and project viability concerns identified in relation to this project. For example, DOTARS did not include extra pre-conditions on payments or exercise the option set out in the Standardised Funding Agreement to require that Regional Partnerships funds be held in a bank account separate from other operational accounts maintained by the applicant.

915 As such steps were not taken either before the Funding Agreement was signed or through the terms of the Funding Agreement, the department did not comply with FMA Regulation 13.
Commercial borrowings

11.62 On 17 May 2005, the Departmental Liaison Officer to the then Parliamentary Secretary’s Office advised DOTARS that the applicant had advised him that it had secured commercial borrowings for the project from a bank and that details were available if required. DOTARS did not obtain any details in relation to the commercial borrowings. There was also no documented analysis by DOTARS of the borrowing terms and conditions, if such details were obtained, or of the potential implications for applicant and/or project viability that may arise from the applicant’s contribution to the overall project being funded from commercial borrowings rather than any working capital or accumulated reserves. Prior to this advice from the applicant to the then Parliamentary Secretary’s Office, there is no evidence of DOTARS having sought to confirm the source of the applicant’s contribution to the project.

11.63 In March 2007, DOTARS advised ANAO that its updated Internal Procedures Manual now requires the department to sight documentary evidence of such claims.

Competitive neutrality

11.64 No additional research was undertaken by DOTARS in relation to competitive neutrality issues. Based on the information it held at the time of its first assessment, DOTARS advised the then Parliamentary Secretary in its second assessment that:

The department considers that there are no competitive neutrality issues involved with this project as no other business currently undertake (sic) this activity.

11.65 However, the assessment did not address a number of issues that the then applicable Internal Procedures Manual (February 2005 version) advocated as relevant in assessing competitive neutrality issues. This would have involved examining the size of the stock feed market, existing sources for stock feed or the impact on existing suppliers of stock feed should the project be successful in gaining a share of the stock feed market. The assessment also did not address the suggestion in the Internal Procedures Manual that applicants be asked to provide letters of support from existing businesses that could be disadvantaged if the project were to go ahead.

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916 See also paragraph 11.59 for advice to ANAO from Applied Financial Diagnostics on these issues.
Departmental recommendation to approve funding

11.66 On 20 June 2005, DOTARS submitted a revised funding recommendation to the then Parliamentary Secretary. The revised recommendation is reflected in Figure 11.5.

Figure 11.5
Second project assessment: recommendation to approve funding

This project was originally not recommended and sent to Mr Cobb for consideration in Package 90. The Department considers this Package 112 brief to replace the Package 90 brief and, therefore, requests that the latter be disregarded.

The project was not recommended as it was considered that the outcomes did not relate specifically to this project that Regional Partnerships were being asked to fund. However, subsequent discussions within the Department concerning the interpretation of the guidelines on this issue have led to a shift thinking on this issue. The Department now believes that the assessment of the outcomes should take into consideration the project as a whole rather than just the project activity being funded.

Regional Partnerships funding was initially sought to purchase and install the Aerox odour filters which were stipulated by the EPA and as such form part of a legislative requirement. Whilst the overall project has already commenced the stage for which Regional Partnership funding is being sought “the Activity” has not yet commenced and as such retrospectivity is not an issue in this case. The stage for which funding is being sought is an intrinsic part of the larger project with the project outcomes dependant on the installation of the filters.

Source: DOTARS project assessment dated June 2005.

11.67 Whilst DOTARS’ advice to the then Parliamentary Secretary was that the project as a whole should be considered in assessing the extent to which the application satisfies the Outcomes assessment criterion, a different approach was taken to the issue of retrospectivity. In terms of whether the project involved retrospective funding, DOTARS advised the then Parliamentary Secretary on 20 June 2005 that:

Whilst the overall project has already commenced the stage for which Regional Partnerships funding is being sought “the Activity” has not yet commenced and as such retrospectivity is not an issue in this case.917

11.68 This approach to the question of retrospectivity (or prior commitment) appears inconsistent with the argument presented by DOTARS to support its revised assessment that the project did satisfy the Programme Guidelines requiring that it deliver value for money outcomes for the Regional Partnerships funds, being that the installation of the odour filters was ‘an intrinsic part of the larger project with the project outcomes dependent on the

917 This approach to assessing retrospectivity was also inconsistent with other projects included in ANAO’s audit sample.
installation of the filters’ (see Figure 11.5). The department’s approach to retrospectivity for this project also does not address:

- the fact that the commencement of construction of a plant to which the odour filters were intrinsic essentially represented a commitment by the applicant to the necessary expenditure on odour control; or
- whether the filters had already been ordered.918

11.69 On 20 June 2005, the then Parliamentary Secretary approved funding of $393 636 (plus GST) for the project. DOTARS’ assessment advised the then Parliamentary Secretary that the project duration was two months with a recommended funding profile involving payment of all funds in 2005–06.

**ANAO conclusion**

11.70 Departments have a responsibility to be responsive to the requests of Ministers for further and better advice, as was requested in respect to this project. However, the department’s due diligence inquiries were such that they did not provide a sound basis for the revised advice to the then Parliamentary Secretary that funding should be approved.

**Project outcomes**

11.71 Funds were approved for the purchase and installation of two Aer ox odour control filters and the electrical supply and installation for a grape marc separator/dryer facility to be built at Nuriootpa in South East South Australia. A Regional Partnerships Funding Agreement was signed by Coonawarra Gold and DOTARS on 23 June 2005. Under the terms of the Funding Agreement, the electrical supply was to be installed, filters connected and commissioned and operations begun at the plant by 30 September 2005.

11.72 This project was to deliver the following outcomes:

- a new process for grape seed oil fusioning, measured by the plant being operational and grape seed oil being produced;
- 30 new full time employment positions created;

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918 Specifically, the quote for filters attached to the Regional Partnerships application specified that the filters were to come from the Netherlands with delivery to occur from the factory approximately 13 weeks after the order was placed. A progress report submitted to DOTARS by Coonawarra Gold on 13 July 2005 stated that the filters had been purchased and had arrived on site. A 13 week delivery timeframe indicates that the filters would need to have been ordered on or before 13 April 2005, more than two months prior to the then Parliamentary Secretary’s approval of Regional Partnerships funding. The actual date the filters were ordered was not established by DOTARS as part of its administration of the Funding Agreement.
• a new export industry for grape seed oil was to be created, as measured by AusIndustry data; and

• 70 per cent of wine industry marc was to be removed, measured by Tarac Technologies weigh bridge figures.

The Funding Agreement did not link payments to need

11.73 The Regional Partnerships application submitted by Coonawarra Gold stated that funds for the filters would be required once the filters were delivered. However, the Funding Agreement proforma completed by DOTARS did not link payments to the cash flows associated with the purchase of filters, electrical supply installation and commissioning of the plant. Instead, the Funding Agreement proposed that payments be made as follows:

• an ‘advance’ payment of $157 454.40 plus GST (40 per cent of Regional Partnerships funds) on 24 June 2005 (the day after the Funding Agreement was signed);

• a further 25 per cent ($98 409.00 plus GST) of Regional Partnerships funds to be paid on 15 July 2005 following receipt of a second Progress Report (although, according to the Funding Agreement, no project milestones were expected to have been completed by that date);

• a further 25 per cent to be paid on 15 August 2005 (the first milestone – purchase and installation of the filters – was expected to be completed on 12 August 2005); and

• the remaining 10 per cent of funds ($39 363.60 plus GST) to be paid upon acceptance by DOTARS of the Post Activity Report and financial acquittal (due on 30 September 2005).

11.74 Payments were made broadly in line with the Funding Agreement. Specifically, a total of $393 636 (plus GST) in Regional Partnerships funds was paid to Coonawarra Gold in four instalments between 23 June 2005 and 5 October 2005, as follows:

• the first instalment (an advance payment) of $157 454.40 (40 per cent) was paid on 23 June 2005, following execution of the Funding Agreement;
• the second instalment of $98 409 (25 per cent) was approved for payment and paid on 15 July 2005, following receipt of Progress Report 2;919
• the third instalment of $98 409 (25 per cent) was approved for payment on 12 August 2005, following receipt of Progress Report 3; and
• the final instalment of $39 363.60 (10 per cent) was paid on 5 October 2005.

Project acquittal

11.75 The final payment was made on 5 October 2005 on the basis of:
• a Post Activity Report (the third project report received from Coonawarra Gold) that reported that all three project milestones had been achieved, including that the filters were working and the plant had begun operations on 8 September 2005. The report was dated 5 September 2005 (that is, three days prior to the date on which it stated that the plant had commenced operations);
• an invoice from Coonawarra Gold for the final payment dated 8 September 2005;
• a statement of acquittal from Coonawarra Gold dated 30 September 2005 certifying that the project had been completed, funds had been spent according to the project budget and that the Post Activity Report and Financial Report had been endorsed by the Project Manager/Project Management Committee;
• a project income and expenditure statement to 30 September 2005 that identified income from DOTARS ($354 272.40 plus GST received and $39 363.60 plus GST still to be received) as well as from the applicant ($784 367.00 received) and total expenditure of $1 224 410.34; and
• an audit report dated 30 September 2005 attesting that the project income and expenditure statement was complete and accurate and that the expenditure was expended for the purpose of the activity in accordance with the Funding Agreement.

919 The Funding Agreement provided for a first progress report to be provided on 23 June 2005, the same date that the Agreement was executed. There is no evidence of such a report having been sought or obtained by DOTARS.
11.76 DOTARS did not inspect the plant before making the final payment to assure itself that the plant was, in fact, operating with the filters installed and working.\textsuperscript{920} It is now clear that the plant had not commenced operations at the time DOTARS made the final payment of Regional Partnerships funds (and did not commence operations – see paragraphs 11.80 to 11.84). In addition, the acquittal was finalised and the final payment made notwithstanding a number of anomalies in the project income and expenditure statement received from Coonawarra Gold. Specifically:

- the statement of income and expenditure included a mix of GST-inclusive and GST-exclusive line items;
- there was no interest allocated as having been earned on the Regional Partnerships funds;
- the inclusion of expenditure with no apparent connection to the purpose for which Regional Partnerships funding was approved, being ‘the purchase and installation of two ‘Aerox’ odour control filters, electrical supply and installation and commissioning of the plant’.\textsuperscript{921} Specifically, amounts were included for planning and supervision, travel and Tarac Technologies charges for odour modelling; and
- a number of the income and expenditure line items included in the statement were identical to the amounts included in the revised Regional Partnerships application. It is unclear whether these amounts reflected the actual costs incurred given, for example, the quote for the supply and installation of the two imported filters was dated 23 December 2004 and was valid for 3 months. Unless the quote had been accepted prior to the Minister’s 20 June 2005 funding approval (which occurred nearly six months after the date of the quote), the cost of purchase, importation and installation can be expected to have changed. Acceptance of the quote prior to the Minister’s approval would also have raised further issues about retrospective funding.

11.77 Correcting for those anomalies that can be quantified, ANAO has recalculated project income and expenditure on a GST-exclusive basis as

\textsuperscript{920} The February 2005 and September 2005 versions of the Internal Procedures Manual both required that at least one site visit be conducted to projects involving more than $250 000 in Regional Partnerships funding being undertaken by for-profit entities.

\textsuperscript{921} Whilst expenditure relating to the broader project was included in the acquittal of the Regional Partnerships-funded activity, revenue relating to the broader project, including the grant received from the South Australian Government, was not included.
outlined in Table 11.1. It needs to be emphasised that this statement has not been audited by the ANAO, but has been prepared on the basis of the limited financial information that was available from DOTARS’ records. There is no evidence of DOTARS having scrutinised the financial acquittal received from Coonawarra Gold in order to identify and resolve any apparent anomalies.

11.78 In this respect, DOTARS advised ANAO in March 2007 that:

While we accept that we have an obligation to verify that the acquittal is accurate, there is difficulty in questioning an acquittal that is accompanied by a signed statement from an auditor as above.

The department is following up with the auditor to clarify the apparent anomalies.

Table 11.1

<table>
<thead>
<tr>
<th>ANAO adjusted project income and expenditure statement</th>
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<tbody>
<tr>
<td><strong>INCOME</strong></td>
</tr>
<tr>
<td>Regional Partnerships funding</td>
</tr>
<tr>
<td>Other contributions</td>
</tr>
<tr>
<td><strong>Total income</strong></td>
</tr>
<tr>
<td><strong>EXPENDITURE</strong></td>
</tr>
<tr>
<td>Purchase and installation of Aerox odour control filters</td>
</tr>
<tr>
<td>Connect electrical supply</td>
</tr>
<tr>
<td>Supply and install main board</td>
</tr>
<tr>
<td>GPM electrical supply and installation</td>
</tr>
<tr>
<td><strong>Total expenditure</strong></td>
</tr>
<tr>
<td><strong>Project surplus</strong></td>
</tr>
</tbody>
</table>

Source: ANAO analysis of DOTARS data.

11.79 Table 11.1 indicates that, based on the information available, the activity funded by the Regional Partnerships Programme cost $103,221 less than the $1,178,003 received from the Commonwealth and contributed by the
applicant. On the basis of the reporting accepted by DOTARS, the final Regional Partnerships instalment of $39 363.60 (plus GST) should not have been paid by the department and consideration should have been given to recovering some or all of the third instalment.

**Liquidation of the company**

11.80 On 17 November 2005, a meeting of the directors resolved that the company was insolvent or likely to become insolvent at some future time and a Joint and Several Administrator of the company should be appointed, in accordance with section 436A of the *Corporations Act 2001*. On 14 December 2005, the creditors of the company resolved that the company be wound up (liquidated). In terms of the liquidation, DOTARS advised the then Senate Rural and Regional Affairs and Transport Legislation Committee on 17 February 2006 that:

...there are no funds owed to us and we do not have equity in that project.

11.81 In March 2007, DOTARS advised ANAO that:

Both plants of Coonawarra Gold have now been sold. The Millicent plant was sold as a going concern in early 2006 to Gardiner Smith Pty Ltd a subsidiary of Riverland Oil Processors and continues to operate. The Nuriootpa plant has been purchased by Tarac Technologies Pty Ltd and is expected to be operational towards the end of March 2007. The processes you referred to would therefore appear to be viable.

11.82 DOTARS records stated that, on 18 April 2007, the owners of the former Coonawarra Gold plant at Nuriootpa had advised that the plant was not yet open, but that it may be open by the end of April 2007.

11.83 On 10 October 2007, DOTARS advised ANAO that:

DOTARS has been advised that the facility is partially operational and is currently sorting out technical difficulties before becoming fully commercially operational.

**ANAO conclusion**

11.84 As of October 2007, the project had not achieved any of the contracted outcomes and the public money paid to the applicant was reflected in assets

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922 The statement of income and expenditure provided by the applicant stated that it had contributed $784 367 to the project, being the amount stipulated in the assessment approved by the then Parliamentary Secretary and the executed Funding Agreement.
liquidated for the benefit of creditors. Deficiencies in DOTARS’ assessment and contract management procedures contributed to this result. Specifically:

- key risks relating to applicant and project viability were not identified and rigorously assessed so as to inform the then Parliamentary Secretary’s funding decision;
- deficiencies in risk assessments were compounded by the Funding Agreement not being drafted so as to effectively manage applicant and project viability risks. For example, although the project was a high risk commercial venture, funds were paid in advance rather than arrears (including a significant advance payment following signing of the Funding Agreement);
- the acquittal was finalised and the final payment made despite the department having not undertaken a site inspection to confirm that the filters had been purchased and installed and that the plant was operating; and
- the acquittal was finalised and the final payment made notwithstanding a number of identifiable anomalies in the project income and expenditure statement. These anomalies were such that, based on the reporting accepted by DOTARS, the final payment should not have been made, and consideration should have been given to recovering some of the third instalment.
12. Expansion of Seed and Grain Breeding, Marketing, Processing and Fractionation at Keith

This case study examines the assessment, approval and contract management processes undertaken in respect to RP02074 Expansion of Seed and Grain Breeding, Marketing, Processing and Fractionation at Keith project. It highlights departures from the usual processes for assessing applications under the Programme Guidelines, as well as deficiencies in DOTARS’ assessment, and subsequent administration, of various aspects of the application relating to project viability and partnership funding risks.

Background

12.1 Keith Seeds Pty Ltd (Keith Seeds), a private company with 27 shareholders, is a vertically integrated breeder, producer, seed processing and marketing company which was operating over two sites at Keith, 250 kilometres south east of Adelaide. In order to expand the business and improve logistics access, the company planned to relocate to a larger facility on a single site. A February 2002 application to the Dairy Regional Assistance Programme (Dairy RAP) for funding of $180 000 was unsuccessful because of an unsatisfactory financial viability assessment conducted on the applicant.

12.2 The company first inquired with the South East South Australia ACC (now the Limestone Coast ACC) about possible Regional Partnerships funding in August 2004 and subsequently lodged an Expression of Interest. In June 2005, the company requested that the ACC review its proposal as early as possible, advising that one of its existing sites had been rezoned as residential and it believed that Council may move to force it from the site. In that context, the company also provided a letter of explanation in respect to issues raised in the viability assessment undertaken in relation to the Dairy RAP application.

12.3 The ACC Board subsequently supported the proposal and the ACC assisted the company in preparing a Regional Partnerships application for the project, which was submitted on 12 August 2005. The application sought funding of $571 500 (plus GST) towards RP02074 Expansion of Seed and Grain Breeding, Marketing, Processing and Fractionation at Keith project. This was part of a three stage project. The Regional Partnerships funding was sought for Stage 1 (relocate to a single leased site and allow for expanding the existing...
business) and Stage 2 (build a pulse splitting plant as a new business), to be undertaken concurrently.923

12.4 The total project cost identified in the application was $3 460 402. The other funding partners proposed were the applicant—$2 802 902 cash (to be funded through a bank loan) and $6 000 in-kind; and Tatiara District Council—$15 000 cash and $65 000 in-kind. The application identified a project start date of 1 December 2005 and completion date of 30 June 2006.

12.5 The anticipated project outcomes identified in the application included 10 direct Full-Time Equivalent jobs. At a Regional Partnerships funding bid of $571 500, this represented $57 150 per direct job.924 Other anticipated outcomes were a projected 57 indirect jobs (based on a 1998 report for the Industrial Supplies Office) and new grower, transport and market opportunities.

Assessment process

12.6 On 1 November 2005, the Office of the then Minister for Transport and Regional Services requested advice from the department in respect to progress on two Regional Partnerships applications for projects located in Keith, including the Keith Seeds application. This request had arisen from a query from the Office of Mr Patrick Secker MP, Federal Member for Barker, who had provided a letter of support for Keith Seeds’ application.

12.7 In providing a response to the query to National Office on 2 November 2005, the South Australian Regional Office advised that there may be a potential conflict of interest issue associated with the Keith Seeds application as it had just discovered that Mr Secker was a shareholder in the company.925

12.8 On 7 November 2005, Mr Secker wrote to the then Minister for Transport and Regional Services declaring an interest (see Figure 12.1).

923 Stage 3 (build a pea fractionation plant for the separation of peas into fibre, starch and protein) was planned to be undertaken some 12 months after relocation.

924 DOTARS considers that, for projects where job creation is a focus, a good value-for-money outcome is for each ongoing full-time equivalent job to have been supported by less than $25 000 in grant funds (see Regional Partnerships Guidelines, July 2006, p. 11).

925 The 2001 Dairy RAP application form had required the applicant to identify details of any relevant pecuniary interests of members/employees. The application had noted: ‘Local Member of Parliament (Patrick Secker) is a minor shareholder of the company. He is not a current member of the Board.’
**Figure 12.1**

**Declaration of interest by the Federal Member for Barker**

Dear Minister,

In previous correspondence I wrote in support of a Regional Partnerships application for Keith Seeds Pty Ltd.

Keith Seeds Pty Ltd is now owned by what was a grower's co-operative that I belonged to as a prerequisite to growing certain PBR varieties of Lucerne seed.

I have now been informed that I was a minority shareholder (241 shares out of a 20,000 share issue) and that technically I need to declare an interest.

I have subsequently sold these shares (at a loss) to avoid any conflict of interest.

I am informed that my name may remain on the share registry until the Annual General Meeting of that company, even though I no longer own shares in the company.

Since being elected to Parliament seven years ago I have not served in any capacity with this company or the previous co-operative, nor have I attended any meetings or sent a representative.

I trust that this clarifies the matter.

Source: Correspondence from the Member for Barker to the then Minister for Transport and Regional Services, 7 November 2005.

12.9 As part of its assessment of the Keith Seeds application, DOTARS commissioned an external viability assessment. The November 2005 report of the external assessment identified issues in relation to the applicant viability criterion and concluded that the project was medium to high risk.

12.10 This conclusion was based on the detailed findings of the assessment, which included:

- The industry, in our opinion, is one that carries significant risk due to the seasonal fluctuations and competitiveness of the global industry.

- The Company is not in a strong liquid position with limited working capital funds. This increases the risks associated with adverse market and climatic conditions to the Company in the future.

- Overall we have some concerns about the accuracy and achievability of the projections based on prior trading results and industry risks.

12.11 DOTARS’ recommendation that funding not be approved was provided to the Ministerial Committee on 13 January 2006. Based on the
findings of the external viability assessment, DOTARS advised that this project failed to meet the program’s assessment criteria for applicant viability and only partially satisfied the assessment criteria for project viability. DOTARS advised:

...The level of risk associated with this project is medium. The new and expanded business venture holds a level of risk in itself, and the applicant’s plan to borrow a large sum of funds totalling $2.8 million for the relocation and expansion of business adds considerably to this risk.

**12.12** On 31 January 2006, Minister Lloyd returned the assessment to the department for further information. On 7 February 2006, DOTARS advised the external consultant that had undertaken the external viability assessment that:

We have had a number of questions from the Minister’s office concerning this project and the *financial viability* assessments undertaken. Can you please let me know if the assessment of this application contemplated/analysed the context of this organisation in the environment it operates and the constraints that are generally faced by primary industry/export companies.

**12.13** On 8 February 2006, the external assessor advised DOTARS that:

The financial viability report for Keith Seeds did look closely at the commercial risks associated with the agricultural industry and the financial risks associated with commodities trading for primary industry export companies.

The main risks included:

1. Seasonal fluctuations resulting in a significant loss of sales revenue.
2. Bulk commodity trading risks with regard to exchange rates and penalties associated with non-delivery or down graded seed; and
3. A highly competitive global market.

These factors were taken into account when assessing Keith Seeds and are reflected in our findings.

**12.14** DOTARS’ records indicate that the application was due to be reconsidered by the Ministerial Committee at its 15 February 2006 meeting.

**Formal withdrawal of application**

**12.15** It is the usual process under the Regional Partnerships Programme that, apart from the necessary interactions in respect to clarifying questions and/or requests for missing or required documentation, the department is not to discuss its assessment or funding recommendation with an applicant once
assessment has begun. In this respect, the Internal Procedures Manual in place at the time this application was assessed stated:

Within 10 working days, the applicant must be contacted by Regional Office staff to advise:

... 

- that assessment of the application has commenced (where the application passed the pre-eligibility check). This advice will emphasise that no commitment to funding should be assumed and that the program is a discretionary grant program.

Once the applicant has been sent this last letter advising them that an assessment has commenced, there should be no further indication given on the likely timing or progress of the assessment.

The Department has been specifically requested NOT to advise applicants that their projects are with the Minister or with National Office.926

12.16 Once an application has been either formally withdrawn by the applicant or not approved by the Minister, the applicant may seek feedback in respect to aspects of the proposal that could be revised to strengthen the chances of any fresh application being successful. In this respect, DOTARS’ Internal Procedures Manual stated:

Unsuccessful applicants should be advised in writing within two weeks after the RO is notified of the Ministerial decision. This letter should include the specific reason(s) for non-approval...It should also include an explanation that if they wish to address reasons for non-approval, the Department can arrange a consultation, and that there may be an opportunity to re-submit an application when these issues have been addressed.927

12.17 The Internal Procedures Manual did not provide specific guidance regarding providing feedback to applicants that had formally withdrawn their application.

12.18 In accordance with sound and transparent management practices, it is also the usual process for any new proposal submitted by an applicant following the withdrawal or non-approval of an earlier application to be treated as a fresh application that is given its own unique identifier and subjected to the normal assessment process.

926 The last two paragraphs of this advice were added to the second version of the Internal Procedures Manual, issued in June 2004 and appeared in all subsequent versions issued to 30 June 2007.

927 DOTARS Regional Partnerships Programme Internal Procedures Manual, September 2005, p. 120.
**Formal withdrawal of application by Keith Seeds**

12.19 On 13 February 2006, the Office of the then Minister indicated to DOTARS that Keith Seeds intended to withdraw its application. The Minister’s Office requested that DOTARS provide feedback to the applicant as to how its application might be strengthened should the company wish to submit a revised application (see Figure 12.2).

**Figure 12.2**
Minister’s Office request for DOTARS to provide feedback to the applicant

| Can you please ask the Adelaide Regional Office to provide feedback to the applicants of the following RP - why the dept did not recommend it and what would need to be strengthened in the application should they wish to resubmit? |
|---|---|---|---|
| MO | 12/08/2005 | 2074 | Keith Seeds Pty Ltd |
| Expansion of Seed and Grain Breeding, Marketing, Processing and Fractionation at Keith | KEITH | SA | Limestone Coast A |

Source: Email correspondence from the Office of the then Minister for Transport and Regional Services to DOTARS National Office, 13 February 2006.

12.20 On the same day, National Office advised the Regional Office that it had been informed that Keith Seeds intended to withdraw, with a view to submitting a new application that addressed the financial viability issues. National Office also noted that it had advised the Minister’s Office that DOTARS was unable to enter into discussions with the applicant prior to the application either being not approved or formally withdrawn (see Figure 12.3).

**Figure 12.3**
National Office advice to Regional Office and Minister’s Office regarding discussions with applicant prior to formal withdrawal

I have been advised that the applicant intends to withdraw this application in order to address the concerns that were identified and submit a new application that covers the financial viability issues. I would appreciate you advising us ASAP when you receive this request to withdraw as RP2074 is due to be considered by the Ministerial Committee this Wednesday.

I advised the Minister’s Office that we cannot engage in discussions with the ACC/applicant until the Ministerial Committee have either made a decision or the applicant has formally withdrawn the current application.

Please contact me if you have any concerns.

Thanks.

Source: Email advice from National Office to South Australian Regional Office, 13 February 2006.
12.21 A 13 February 2006 email from the Chairman of Keith Seeds advised the Executive Officer of the Limestone Coast ACC that the company wished to formally withdraw its Regional Partnerships application (see Figure 12.4).

**Figure 12.4**

Formal withdrawal of Keith Seeds application by the applicant

![Email](source: Email from Chairman of Keith Seeds to Limestone Coast ACC Executive Officer, 13 February 2006 [Names and contact details removed].)

12.22 There is no record of how the applicant had become aware that the department had financial concerns with the application. In this respect, on 22 August 2007, DOTARS advised ANAO that:

The information was not provided by the Department prior to the withdrawal of the application.928

12.23 On the same day, the ACC forwarded the email to DOTARS with a request that it be actioned and the Regional Manager instructed internally:

Please action this matter by withdrawing the application.

12.24 The Regional Office provided a copy of the Chairman’s email and a full copy of the assessment to National Office on 13 February 2006, and also requested that National Office allocate the application back to it so that it could take action to record the withdrawal in TRAX. National Office instructed that the application be removed from the information scheduled to be provided to the Ministerial Committee at its 15 February 2006 meeting.

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928 In providing advice to National Office in relation to this question, the South Australian Regional Office advised: ‘It is our understanding that this advice came from either the Ministers Office or from their local MP but we are unsure. This office did NOT provide the advice.’
Continued assessment of withdrawn application

12.25 A Regional Office file note dated 14 February 2006 recorded a telephone discussion with National Office regarding the request from the Minister’s Office to provide feed-back to Keith Seeds in relation to its withdrawn application, as follows:

[National Office] advised that he had received a call from [a consultant] who Keith Seeds are using to “re-write” their application stating that it had been withdrawn and as such we (the Department) could now discuss the issues and give them some “guidance”.

We discussed what steps the applicant could make to strengthen the application but agreed that the Financial Viability Assessment was the primary reason for non-recommendation and were not sure how this could be addressed. [National Office] queried whether providing the Grant would assist overcome these concerns raised in the FVA but it was considered that this would not be the case as why (sic) it may improve their cash holdings temporarily it would not address the issue re delays in collecting and paying debts.

It was agreed that the best course of action would be to obtain [the external assessor’s] permission to release the FVA to Keith Seeds and then write to Keith Seeds asking them to demonstrate as to why the risks are no longer an issue or how they can be addressed.

12.26 The Regional Partnerships Programme Guidelines have been published as the basis on which applications will be assessed and funding decisions made. In that context, potential applicants and other stakeholders may reasonably expect that the Programme funding decisions will be made in a manner, and on a basis, that is consistent with the published guidance. The approach adopted by the department in this case represented a decision to undertake further assessment of a withdrawn application, which is contrary to the Programme procedures outlined in the Guidelines and internal procedures manual, and applied in relation to many other applicants that were required to submit new applications in order to be considered for funding.

12.27 In this context, it is not the normal practice for applicants to be given the opportunity to comment on the findings of either the departmental assessment or any independent assessment the department may have commissioned in relation to their application. DOTARS did not record the rationale for choosing to provide the applicant with a copy of the actual assessment, rather than providing feedback in relation to the main areas of
concern, as is the normal course followed in advising of the reasons for applications being unsuccessful.

12.28 That the department was resuming its assessment of the withdrawn application was also evident in DOTARS’ advice to the applicant in providing it with a copy of the external viability assessment on 23 February 2006, as follows:

I refer to previous discussions between yourself and this Department concerning the Regional Partnerships application submitted by Keith Seeds Pty Ltd for funding for your Expansion of Seed and Grain Marketing Production and Fractionation at Keith project and how the application may be “strengthened”.

Enclosed for your information is a copy of the Financial Viability Assessment conducted by [external assessor], which was completed as part of the assessment process for this application.

The assessment by [external assessor] raised a number of concerns regarding the overall viability of the project. To address these concerns you will need to provide evidence that they are no longer issues or provide evidence that processes have been put in place to overcome them...

...It should be noted that any further evidence supplied on behalf of Keith Seeds Pty Ltd will need to be address (sic) the above issues and show clearly that they have been resolved or are in the process of being resolved. The Department will then assess that information and advise the Minister accordingly.

It is also important to note that there is no guarantee that if the evidence and information is supplied that funding for the project will be approved.

[ANAO emphasis]

12.29 The department’s advice clearly indicated that the assessment process in respect to the applicant’s original application was on-going and represented an invitation to the applicant for it to provide further information for assessment.

12.30 The applicant provided written comments to the department on the findings of the external viability assessment, as well as additional information regarding revised financing arrangements for the project, in a letter dated 1 March 2006. The applicant requested that its application receive favourable attention as soon as possible. The applicant made no reference to its formal withdrawal of the application on 13 February 2006.
12.31 The applicant also provided DOTARS with a copy of a further letter from its bank dated 3 March 2006 regarding possible financing for the project (an earlier expression of interest from the bank had been provided with the application). The 3 March 2006 letter from the bank identified a different proposed financial arrangement for the project than had been set out in the Regional Partnerships application. This involved the possible bank loan being reduced from $2.9 million to $2 188 467, and a new $500 000 contribution from the applicant to be funded through a share issue.

12.32 The total project funding identified in the bank’s letter represented a shortfall in project funding of some $130 000 compared to the project costs identified in the Regional Partnerships application. However, there was no information provided, or sought by DOTARS, in respect to how cost savings would be achieved to meet this funding shortfall (as discussed further below).

Supplementary external viability assessment

12.33 Both the applicant’s letter and attached letter from its bank were provided to the external assessor by DOTARS on 10 March 2006. At that time, the external assessor was also provided with other material that had been included as attachments to Keith Seed’s August 2005 application, but which had not previously been provided to it by the department, including:

- the construction and equipment purchase quotes on which the project budget had been based; and
- the applicant’s lease agreement over the site of the proposed facility.

12.34 DOTARS requested that the external assessor peruse the documents and advise whether the information contained in them would in any way change the assessment previously given and, if so, how. The March 2006 supplementary external viability assessment concluded that its opinion of the applicant against the applicant viability criterion remained, but that:

However we believe that the project risk should be revised from high to medium based on the additional information provided by Keith Seeds in relation to the project including detailed quotes, funding and trading arrangements.

[See ANAO comments at paragraphs 12.66 to 12.67 regarding the funding question.]

Revised Departmental assessment

12.35 The supplementary external viability report was also provided to the applicant by DOTARS. In agreeing that this occur on 24 March 2006, National
Office also advised that it was expecting the Regional Office to complete the assessment based on the new information.

12.36 On 28 March 2006, the Regional Office advised the external assessor that the applicant had not raised any issues with the supplementary report. On 29 March 2006, the Regional Office advised National Office that:

This project has been referred back for QA following its withdrawal and further financial viability assessment.\(^\text{929}\)

12.37 The department’s revised assessment submitted to the Ministerial Committee on 6 April 2006\(^\text{930}\) continued to recommend that funding not be approved, with DOTARS advising the Ministerial Committee that:

The revised financial viability assessment changed the project viability assessment from high risk to medium risk as a result of further information provided by the applicant (including details of quotes, funding and trading arrangements). The Department and independent assessor still have concerns regarding the ability of the applicant to ensure sustainability and profitability post-project implementation. In particular, the suggestion that profitability will rise from about 1% to 21% seems very ambitious.

...While the revised viability assessment is more optimistic than the earlier analysis, there remain concerns about the project and applicant viability. The assessment suggests that there is still a moderate risk that the company will not be sustainable in the longer term.

**ANAO conclusion**

12.38 The department’s treatment of this withdrawn application departed from the approach usually applied in other such cases. Had the department adopted an approach consistent with the published Guidelines and documented assessment procedures, it would have advised the applicant that the issues identified in respect to its application would need to be addressed in any fresh application, should the applicant choose to submit one.

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\(^{929}\) The National Office copy of this email was marked: ‘Project re-opened in TRAX 29/3/06 following its earlier withdrawal.’

\(^{930}\) The assessment did not advise the Ministerial Committee that the application had been withdrawn by the applicant subsequent to the Committee’s 31 January 2006 request for further information.
Ministerial decision-making processes

Ministerial consideration of revised departmental assessment

12.39 As noted, the department signed its revised assessment for provision to the Office of the then Minister for Transport and Regional Services on 6 April 2006. On 19 April 2006, the then Minister’s Office requested that the department provide it with a copy of the documentation used by the external assessor in forming its conclusion that the applicant had forecast an average net profit margin of 21 per cent, which was significantly higher than the historical financial results reviewed of approximately one per cent. The external assessor had expressed concerns regarding the achievability of those results. Although this issue had been identified in the original November 2005 external viability assessment, it was only highlighted to the Ministerial Committee by DOTARS in its April 2006 revised advice.

12.40 A letter dated 26 April 2006 from the Member for Barker provided the then Minister with a letter from the applicant, dated 21 April 2006, with the Member’s covering letter noting:

I request your response on their comments of some of the issues in respect to their funding application.

12.41 The applicant’s letter was marked to the attention of an Advisor to the then Minister, with reference ‘Telephone conversations with [the applicant’s consultant]’. The letter stated: ‘We have been asked to comment on a couple of issues with respect to our application.’

12.42 The applicant’s 21 April 2006 letter provided comment in respect to two of the areas of risk identified by the external assessor in both its original (November 2005) and supplementary (March 2006) viability assessments, relating to business risk in the agriculture industry and analysis of the profit projections included in the supporting documentation provided with the application. In particular, the applicant suggested that the profit projections had been misinterpreted by the external assessor. The applicant had not raised this issue in its 1 March 2006 comments on the original external viability assessment, which it had been provided with on 23 February 2006.

12.43 There is no evidence of the external assessor being asked to comment on the applicant’s position as set out in its 21 April 2006 letter.\footnote{The Member advised that the applicant had also forwarded a copy of the letter to the department, but the only copy addressees to the applicant’s letter were the Member and the applicant’s consultant. A copy of the letter was faxed to the Regional Office, apparently from National Office, on 12 May 2006.}
12.44 The 6 April 2006 Minute covering the department’s revised assessment included a signature block in which each member of the Ministerial Committee could indicate whether he approved funding, did not approve funding, or the application was returned for further information. All three Ministers signed the Minute, but there was not initial agreement on the outcome.

12.45 On 28 April 2006, Minister Lloyd signed under the department’s recommendation that funding not be approved, but it is unclear whether the Minister was approving or not approving funding at that time. The ‘Approve Funding’ option in the signature block was circled at some stage, but, as is discussed below, the application was approved for funding at the Committee’s 31 May 2006 meeting. Minister Truss’ signature to the Minute is dated 31 May 2006, at which time the ‘Approve Funding’ option may have been circled.933

12.46 More clearly, Minister Nairn signed the signature block on 7 May 2006, annotating that his decision was to ‘Not approve’ (see Figure 12.5).

932 In this respect, in August 2007, DOTARS advised ANAO that: ‘The supplementary External Viability Assessment was received by the Department in March 2006, prior to the applicant’s 21 April 2006 correspondence. The consultant, in describing the approach used in preparing the Financial Viability Assessment, noted that the report was based on additional information made available, including a copy of the applicant’s 1 March 2006 letter to the Department regarding the issues of business risks and projected returns.’ In this respect, ANAO notes that, as discussed, the 21 April 2006 letter from the applicant had arisen from telephone conversations between the applicant and an Adviser to the then Minister subsequent to the department completing its revised assessment, rather than as part of the department’s re-instituted assessment process. In those circumstances, it is reasonable to expect that inquiries in relation to the issues raised would have included providing the independent assessor with the opportunity to comment on the applicant’s comments suggesting that its assessment had been in error.

933 In August 2007, DOTARS advised ANAO that its perspective on this issue is that: ‘The ‘Approve Funding’ option was circled, with Minister Lloyd providing no additional comment with his signature block, clearly demonstrating his recommendation was to approve funding.’
Ministerial meeting with the applicant

12.47 DOTARS’ records in relation to this application include an unsigned document titled ‘Meeting Minutes Draft’. The draft minutes record that the meeting, held on 24 May 2006 in Minister Truss’ Office, was attended by:

- Minister Truss;
- Minister Nairn;
- the Member for Barker;
- the Chairman of Keith Seeds; and
- advisers to Ministers Truss and Nairn.934

12.48 ANAO is aware of a number of occasions over the course of the Regional Partnerships Programme on which delegations from potential applicants have met with the responsible Minister(s) in order to present

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934 The draft minutes also recorded that the meeting was attended by an officer identified as being from DOTARS. In August 2007, DOTARS advised ANAO that the officer was a Graduate Administrative Assistant on a placement within the Minister’s office, observing the role of the Minister’s adviser. DOTARS advised that: ‘As such, he had no representative status or role in this meeting. The Department was not informed of the meeting nor officially invited to attend in a representative capacity.’
information in support of their intended application. However, based on the
documentation held by DOTARS, such meetings typically occur prior to an
application being submitted for assessment. Accordingly, it is unusual for an
applicant to meet directly with the Ministerial decision-maker during the
Ministerial consideration of the department’s assessment and funding
recommendation in relation to their application.

12.49 The draft meeting Minutes record that the Ministers discussed various
aspects of the application and the applicant’s business with the applicant and
the Member for Barker.935 The draft Minutes also recorded:

Minister Truss voiced concern over the sustainability of the company. He said
that projected profit turnarounds of 20% were unrealistic.

[The Chairman of Keith Seeds] said that the profit assessment completed by the
Department was wrong. He said that despite shutting down grain trading,
relocation would allow the company to move into processing grains for
human consumption and access niche markets, resulting in a projected 2% return.

Minister Truss said that the assessment had been undertaken by [an external
consulting firm], not the Department, and it was unlikely this firm was
mistaken.

12.50 The draft Minutes also record that the Chairman advised the Ministers
of the shareholders’ decision to contribute $500 000 in capital to the project,
and further recorded:

Action:

The Ministerial Committee will consider Keith Seed’s application according to
the Regional Partnerships Guidelines.

12.51 Where there is not consensus between the members of the Ministerial
Committee in relation to an application, the normal process is for the
application to be referred to a formal meeting of the Committee. The Keith
Seeds application was included in the agenda for the Committee’s 31 May 2006
meeting. The Minute confirming the decisions taken at that meeting records
that funding of $571 500 (plus GST) was approved for the Keith Seeds
application subject to confirmation of a capital contribution of $500 000 by the
shareholders. A fresh version of the signature block to the 6 April 2006 Minute,
generated by DOTARS using a revised template that had been adopted

935 Reference was made to a $47 000 partner contribution from the State Government to relocate electricity
infrastructure. However, this was not identified in the application.
subsequent to the original Minute being submitted to the Ministers, was signed by all three Ministers, dated 31 May 2006, with the ‘Approve Funding’ option being circled by each Minister (see Figure 12.6).

**Figure 12.6**
Second set of signatures on 6 April 2006 Minute to Ministerial Committee

![Recommended Action](image)

Source: DOTARS records.

12.52 The Ministerial Committee’s reasons for approving funding for the Keith Seeds application were not recorded on either the signed project Minute or the Minute confirming the decisions taken at the 31 May 2006 meeting. Nor is there any record of what information was communicated to the third member of the Committee not present at the meeting with the applicant regarding the matters discussed with the applicant.

**ANAO conclusion**

12.53 The published Programme Guidelines applicable to this application did not advise of any capacity for applicants to provide information to the Minister in support of their project other than through the application and other information submitted to DOTARS. The Guidelines also did not contemplate
local Members lobbying the Minister in support of a project through means other than providing letters of support for inclusion with the application submitted to DOTARS, or any capacity for applicants or Members to meet with the Minister during the Ministerial consideration of an application. While Ministers may find access to such information useful to inform their decisions, it is important that there be a clear understanding on the arrangements that would apply generally given the assessment process is still active.

12.54 The Ministerial Committee has agreed a process for considering applications in respect of which there is not consensus between the members of the Committee, under which such applications are referred to a formal meeting of the Committee for decision. In considering the revised departmental assessment of the Keith Seeds application, it is apparent that there was disagreement among the members of the Committee as to whether the application should be approved for funding. However, the processes applied in resolving that question were not recorded in a manner that articulated the reason for departures from the usual decision-making process.

**Confirmation of applicant’s finance approval**

12.55 The August 2005 application identified the applicant’s cash contribution of $2,802,902 as being sourced from borrowed capital, and was described as ‘Contribution committed’. However, at the time of submitting its application, the applicant did not have confirmed financing in place. This was explicitly identified in a letter from its bank that was included in the supporting documentation accompanying the application. The letter, dated 12 August 2005, stated that the bank wished to express interest in providing finance of up to $2.9 million to assist in the relocation and identified a number of matters that would need to be considered when making formal application for finance to that level. The letter further stated:

> This letter is not intended to convey or indicate approval of any facility whatsoever, it is solely intended to provide sufficient information for the company’s board to assess whether they wish to make a formal application to [the bank] for the finance. [ANAO emphasis]

12.56 During the assessment process, on 9 September 2005, the applicant confirmed to DOTARS that it did not yet have any approved finance, advising that it was working with the bank on a formal proposal and would provide the department with proof of a formal letter of offer when it had been received.
Consideration of co-funding in DOTARS’ original assessment

12.57 The original departmental assessment provided to the Ministerial Committee on 13 January 2006 did not include any advice that the applicant did not have approved finance in respect to its proposed contribution (which represented 83 per cent of the project cash funding proposed in the application submitted on 12 August 2005). It also did not advise the Committee that any funding approval should be subject to confirmation of the bank finance.

12.58 In this respect, DOTARS advised ANAO in November 2006 that:

The recommendation was that the application not be approved. Consequently, the need for a condition concerning confirmation of co-funding was redundant. [emphasis as per DOTARS’ advice]

12.59 ANAO notes that this advice takes a narrow view of the department’s role in the Regional Partnerships Programme assessment and approval process. While the department may recommend that funding not be approved in respect to a particular application, it is the Ministerial Committee that decides whether funding will be approved. Accordingly, it is prudent for the department to provide the Ministers with all information necessary to enable them to make an informed decision as to whether funding will be approved and, if so, the conditions that should appropriately be placed on any such approval to manage risks to the Commonwealth.

Additional information obtained during re-instituted assessment process

12.60 As noted, after being provided with the external viability assessment commissioned by DOTARS, the applicant provided additional information to the department in a letter dated 1 March 2006. In respect to the applicant’s financing, the external viability assessment had reported:

Project Capital Cost Requirements

We have not seen any documentation relating to the above financing of the project and therefore cannot confirm the accuracy of the proposed funding.

The reasonableness and accuracy of the costing provided to relocate, construct and fit out the Keith facility cannot be confirmed as no documents relating to the construction or subsequent funding were provided.

12.61 As also noted, the application provided to DOTARS had included a document from the bank relating to possible finance for the project, albeit that the document confirmed that no funding approval had been either given or yet
sought. DOTARS had not provided the external assessor with this documentation. Regardless, the external assessment had recommended that:

the Department request a copy of funding approval from the Company’s lending institution to confirm it has the necessary funds to finance the Expansion Project.

12.62 The Regional Office did not action that recommendation as part of its original assessment. This was confirmed in its 23 February 2006 advice to the applicant in providing a copy of the external viability assessment, which advised:

Whilst it was suggested at the time that the Department seek a copy of the funding approval from the company’s lending institution confirming it had the funds this was not done due to further issues of concern. However, to address this issue such documentation may need to be provided.

12.63 The applicant’s 1 March 2006 letter to DOTARS advised:

We again kindly draw you (sic) attention to Appendix 2 [of the application] which includes a letter of support from our Financial Institution. The letter gives general funding support to the project however the Board chose not to apply for a formal letter of offer until we had received approval of our grant application. Please find following a further letter of support from our Bankers.

As a Board on the 10/10/2005 it was agreed that Keith Seeds Pty Ltd would raise $500,000.00 in extra capital by further issuing 400,000 shares at a $1.25 per share. The Board who control 72.6% of the shares are prepared to underwrite the share issue and make them available to all existing shareholders on a prorata basis.

After several meetings with our Bank, they expressed general comfort and opinion that funding would available (sic) once the grant had been approved and the capital raised, it was mutually agreed that we should leave a formal application until we had grant approval.

12.64 Similarly to its earlier letter, the further letter of support from the applicant’s bank, dated 3 March 2006, again specifically stated:

This letter is not intended to convey approval of any facility, and it does not form a binding agreement between the Bank and yourselves, it is solely intended to provide sufficient information for you to assess whether you wish to proceed to making a formal application for finance to [the bank]. [ANAO emphasis]
12.65 Despite receiving this advice, DOTARS did not identify the question of confirmation of co-funding as being an outstanding issue in relation to the application.

Supplementary external viability assessment

12.66 As noted, the March 2006 supplementary external viability assessment concluded that the project risk should be revised from high to medium based on the additional information provided by Keith Seeds, including in relation to project funding. However, one of the premises on which this conclusion was based was in error. The external assessment stated:

A letter from [the applicant’s bank] dated the 3 March 2006 states that the Bank will provide funding support to the value of $2 190 000 to assist in the relocation of the Company. This is conditional on the approval of the regional assistance grant and additional shareholder funds of $500 000. Further, the Bank require an additional commitment from shareholders to support a contingency fund of $250,000 during construction…

The letter from the [the bank] confirms funding support to the value of $2.19 million, which is approximately $612 902 less than stated on the application. However it appears that the majority of the shortfall of funding will be made up with additional shareholder funds of $500 000 and a reduction in costs of approximately $130 000.

12.67 However, as noted, the bank’s 3 March 2006 letter specifically stated that it was not a letter of approval or commitment and the 1 March 2006 letter from the applicant had specifically stated that it would not be applying for bank finance until after the Regional Partnerships application had been approved.

Likely conditions on any bank finance

12.68 The bank’s 3 March 2006 letter indicated that any approved funding for the project would be subject to a number of conditions, including that:

Shareholders funds and Government/Council Grants are to be expended prior to utilising the Bank facility. Evidence of the availability of the grants is to be provided to the Bank. Contributions from all other sources are required to ensure the Bank facility following sale of existing premises does not exceed $1,990,000. [ANAO emphasis]

12.69 Despite having received a copy of the bank’s letter, DOTARS did not identify this likely condition on any bank finance for the project or consider
whether such arrangements would be satisfactory from the Commonwealth’s perspective.

12.70 The bank’s letter also identified that, should finance for the project be applied for and approved, it would require:

an additional commitment from the shareholders to support a contingency fund of $250,000.00 during construction...Any cost overruns or cost of variations are to be met by the Shareholders. Refer our comments in respect to contingency fund...

12.71 Again, DOTARS did not identify this likely condition on any bank finance. Nor did it assess any potential impact on the assessed level of applicant or project viability risk should the shareholders be required to support the contingency fund, in light of the concerns already identified in relation to the company’s financial position. In November 2006, DOTARS advised ANAO that:

No action was taken to confirm that the shareholders would contribute $250 000 to a contingency fund. This occurred because this amount was a requirement of the shareholders by the bank, not of the Department.

Revised departmental assessment

12.72 The department’s revised assessment of the application did not accurately reflect the revised funding arrangements or project costs that had been proposed by the applicant and reflected in the bank’s 3 March 2006 letter, as follows:

- the department’s revised assessment identified the project budget as being $3 460 402, as per the original application. There was no adjustment made for either the reduced project costs or reduced potential bank finance that had been proposed by the applicant;
- the applicant’s contribution was identified as being $2 802 902 as per the original application, rather than the lower contribution of $2 688 467 identified in the bank’s 3 March 2006 letter and referred to in the supplementary external viability assessment; and
- the revised assessment did not refer to $500 000 of the applicant’s contribution now being sourced from a share issue rather than bank finance.
12.73 These incorrect amounts were subsequently also included in the Funding Agreement executed with the applicant. In November 2006, DOTARS advised ANAO that:

The amounts of $3 460 402 (total project budget) and $2 688 467 (cash contribution from Keith Seeds Pty Ltd) were not changed in TRAX and, as a consequence, were not changed in the brief to the Minister or the Funding Agreement. The amount requested for funding under the Regional Partnerships program did not alter as the reduction in costs ($130,000) reduced the applicant’s contribution. The reason for the amount not being changed is unknown.  

12.74 However, the Minute to the Ministerial Committee covering the revised departmental assessment did advise: ‘The previous shortfall in funds will be made up from reduced costs and a $500 000 share issue.’ As noted, the Committee approved funding of $571 500 at its 31 May 2006 meeting, with Minister Truss annotating that the funding approval was subject to confirmation of cash capital contribution of $500 000 from shareholders.

12.75 Again, the Committee was not advised that the applicant did not have approved finance. As a consequence, the funding approval was not made conditional on it providing evidence confirming approval of the bank finance.

**Payments made before bank finance is approved**

12.76 The Funding Agreement for this project was executed on 3 August 2006. The first payment of Regional Partnerships funds of $285 750 (plus GST) (50 per cent of approved funds) was approved on 7 August 2006.

12.77 The funds to be contributed by the applicant by way of a bank loan represented 66 per cent of the revised cash cost of the project, as identified in the bank’s letter of 3 March 2006. DOTARS’ 7 November 2006 response to an ANAO inquiry as to whether the department had obtained evidence confirming approval of the bank finance prior to the first payment being made confirmed that no such evidence had been obtained. DOTARS advised that:

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936 In August 2007, DOTARS advised ANAO that: ‘The Department notes the budget errors made in the Funding Agreement budget were against the Applicant/Other Partner Cash Contributions – not against the funding provided under Regional Partnerships Cash Contributions, which remained unchanged. The $130 000 project cost reduction raised Regional Partnerships funding, as a percentage of total project costs, from approximately 16.5 per cent to approximately 17 per cent. The applicant reducing project costs is, therefore, unlikely to have any material impact on the decision to approve project funding.’ In this respect, as discussed at paragraphs 12.126 to 12.127, the departmental assessment did not take any account of the time that had elapsed since the quotes had been provided, the potential for construction and/or equipment costs to have changed over that time; or what aspects of the project the apparent reduction in costs related to and how they were proposed to be achieved.

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The letter from [the applicant’s bank] dated 3 June 2006 and the Financial Viability Assessments were interpreted to indicate that the loan had been approved. [sic – It appears that the reference to the bank’s letter refers to the bank’s letter of 3 March 2006. A letter from the bank dated 3 June 2006 was not held in DOTARS’ records]

12.78 On 9 November 2006, ANAO requested advice from the funding recipient as to the status of its bank loan. On 29 November 2006, the funding recipient advised ANAO that:

We should receive the formal accepted letter of offer from the bank in the next two weeks, we to date have been funding the building out of our current facilities secured by the shareholders.

12.79 A formal letter of offer for a financing facility of $1.9 million for the construction costs was provided to the funding recipient by its bank on 27 December 2006 and accepted on 14 January 2007, five months after the first payment of Regional Partnerships funds of $285,750 (plus GST) and over one month after the second Regional Partnerships payment of $228,600 (plus GST) was made on 8 December 2006 (totalling 90 per cent of approved funds).

Risks realised through actual conditions on bank finance

12.80 To protect the bank’s interests, the letter of offer from the bank identified a number of conditions precedent. These included a requirement that, before the first drawing from the construction facility, the funding recipient was required to provide satisfactory evidence to the bank that shareholders’ equity in the project (identified by the bank as including the Regional Partnerships grant) had been fully expended. Accordingly, the risk that was apparent from the terms of the bank’s 3 March 2006 letter, but which DOTARS failed to adequately examine, was realised. As a consequence, combined with DOTARS agreeing to a payment schedule that involved the advance payment of 50 per cent of Regional Partnerships funds, the Commonwealth was placed in the position of accepting financing costs and other risks that it would be reasonable to expect a commercial applicant to carry, through its commercial finance arrangements.

12.81 The Funding Agreement provided that the funding recipient would not receive the final instalment of $57,150 (plus GST) until it had completed the final milestone, including ‘production commenced’. As this is inconsistent with the terms of the bank finance, it is apparent that the funding recipient would need to self-bridge some component of the Regional Partnerships contribution.
This contributes to the elevated cash-flow risk exposure which had been identified in the assessment process.

12.82 The bank’s 27 December 2006 letter of offer also stipulated that it would require a First Registered Mortgage over the leasehold property and a Deed of Consent in relation to the mortgage over the lease from the lessor and lessee. The funding recipient accepted the financing offer, including this term, on 14 January 2007. In this respect, clause 7.5(a) of the Regional Partnerships Funding Agreement stipulates that the funding recipient must not encumber or dispose of any Asset, or deal with or use any Asset other than in accordance with clause 7, without DOTARS’ prior written approval.937

12.83 The ANAO case study on this project was provided to DOTARS on 30 March 2007. In July 2007, the department wrote to the funding recipient advising:

It has been brought to our attention that on the 14 January 2007 a financing arrangement with [your bank] was accepted by you encumbering Assets acquired wholly or in part out of Funding from the Regional Partnerships programme. We have not provided prior written approval for this arrangement as required under subclause 5.5 and paragraph 7.5(a) of the Agreement...

Without waiving or otherwise diminishing any of our future accrued rights under the Agreement, we are willing to consider a request from you to encumber the Asset. This request must be received from you by the Department by the 6 August 2007...938

937 ‘Asset’ is defined as any item of tangible property, purchased, leased, created or otherwise brought into existence either wholly or in part with use of the Regional Partnerships funds, which has a value of over $5 000 inclusive of GST, but does not include Activity Material. In this respect, the first progress report provided to DOTARS by the funding recipient in November 2006 stated: ‘To date the first payment from DOTARS has been allocated to the building and construction inclusive of all contractors and consultants.’ A final report provided on 23 April 2007 further advised that: ‘All the DOTARS funding has been acquitted in the building and construction inclusive of all contractors and consultants.’

938 The approach of seeking to provide a retrospective approval of the funding recipient encumbering assets acquired wholly or in part out of funding from the Regional Partnerships Programme is contrary to advice the department provided to the Minister for Transport and Regional Services one month later, on 27 August 2007, in relation to RP01365 Undercarriage Remanufacture Facility (which has also been the subject of an ANAO case study – see Chapter 9 of this volume) that:

‘ExtremeCo Pty Ltd has breached Clauses 5.5(c) and 7.5(a) of the Funding Agreement by not seeking the Commonwealth’s prior written approval to use tooling obtained from Regional Partnerships funding as security for additional finance.

Legal advice is that the Funding Agreement does not allow the department to retrospectively approve the use of assets as security. While the department would have supported the facility, there is no practical way to remedy this breach other than to advise ExtremeCo that the Commonwealth expects applicants to comply with Funding Agreements in their entirety.’
DOTARS will consider your request once all documents have been received and reviewed and will inform you of its decision within a reasonable time from receiving your request. Nothing in this letter should be interpreted as providing written approval of the encumbrance under the Agreement or as committing to provide written approval under the Agreement.

If you do not agree that you have encumbered an Asset acquired out of Funding from the Regional Partnerships programme you should explain your reasons in writing including any supporting documents.

12.84 In providing comments on the case study to ANAO on 22 August 2007, DOTARS did not advise as to whether the funding recipient had responded by the due date.

Implementation of Ministerial funding condition

12.85 DOTARS provided a Funding Agreement to the funding recipient for signature on 21 June 2006. The Agreement stipulated that confirmation of the cash capital contribution of $500 000 from shareholders was a pre-condition to the first Regional Partnerships payment being made, as per the terms of the Ministerial Committee’s funding approval. In providing the Funding Agreement, DOTARS advised the funding recipient that:

Since our discussion over the phone, I have confirmed that the Department will require confirmation of the shareholders contribution of $500,000, as opposed to a minute from the Board of Directors to underwrite this amount. This requirement is to comply with the specific condition set by the Minister.

12.86 On 23 June 2006, the funding recipient provided DOTARS with a draft letter from shareholders for its approval, advising:

Shareholders are willing to make commitments, we just need to ensure that the confirmation is in a format that is satisfactory to you.

12.87 On 27 June 2006, DOTARS advised the funding recipient that the format of the proposed letter met its requirements. On 31 July 2006, the funding recipient provided DOTARS with five letters from shareholders, each of which stated:

Please be advised that we have undertaken to invest up to $(nominated amount) in the share issue to be made by Keith Seeds to facilitate their relocation. [ANAO emphasis]
12.88 The maximum investment amounts nominated in the five letters totalled $525,000\textsuperscript{939}, exceeding the $500,000 identified in the Ministerial Committee's funding condition. However, the form of letter agreed to by DOTARS did not represent a guarantee that the investment actually made by each shareholder would be at least the amount nominated. Instead, each shareholder had only undertaken to invest up to the nominated amount. Consequently, there was also no undertaking by the shareholders that the cumulative amount invested would total at least the $500,000 required or, indeed, any funds.

12.89 The relevant Regional Office identified this shortcoming internally on 1 August 2006, but the Regional Manager was advised:

With regards to the letters confirming the shareholders contributions...these only state what they are willing to contribute up to it which exceeds the amount the Minister has set. Unfortunately [Regional Office] accepted the format of the letter and I feel that we are now bound to accept the letters.

12.90 ANAO considers that, even had the letters obtained from the shareholders been in a more appropriate form so as to provide an undertaking to invest at least the required amount, the approach taken by DOTARS to confirming that the Ministerial Committee's condition on funding approval had been satisfied would still have been deficient.

12.91 In the context of other ANAO performance audits, DOTARS has commented that instruments such as letters of comfort are not intended to give rise to a legally binding contract or agreement and are not an arrangement that would give rise to any legal consequences.\textsuperscript{940} Accordingly, DOTARS' approach in this instance meant that there was a risk that the letters of undertaking, in the form provided, did not provide the necessary confirmation of cash capital contribution that the Ministerial funding approval required. In August 2007, DOTARS advised ANAO that:

The financial support letters from shareholders were intended to provide an investment guarantee for the project, binding the shareholders to their nominated investment. The letters sought confirmation of the $500,000 cash contribution to meet the funding condition imposed by the Ministerial Committee – the Department was not seeking letters of comfort.

\textsuperscript{939} The individual maximum amounts were up to $300,000, $75,000 and three amounts of $50,000.

...the financial letters of support from shareholders were intended to meet the
funding conditions stipulated by the Ministerial Committee.

12.92 In this respect, ANAO notes that, in agreeing to the letter of
undertaking approach, there is no evidence of DOTARS examining whether
the form of letter proposed by the funding recipient would provide a binding
investment guarantee from the relevant shareholder, or the department’s
capacity under the Funding Agreement to recover any funding provided
should the investment from shareholders not be realised to the necessary
amount. Nor did DOTARS obtain any details from the funding recipient in
relation to the proposed timing of the capital raising.

12.93 Risks to the Commonwealth would have been more effectively
managed by requiring the funding recipient to provide evidence that the
required amount of $500 000 had been physically invested by the shareholders.
Evidence of the capital raised could be provided by way of bank statements,
share certificates, shareholder agreements and/or other appropriate
documents. This would also have enhanced DOTARS’ ability to ensure that it
did not pay public money outside the terms of the Ministerial approval.

**ANAO conclusion**

12.94 DOTARS did not undertake adequate due diligence in respect to
confirming the financing arrangements for the applicant’s proposed cash
contribution, a key issue for this application. The department did not
adequately scrutinise documents that were provided to it by the applicant,
both with the original application and subsequently. Had it done so, it would
have realised that both the original and supplementary external viability
report were in error in respect to this aspect of the project.941

12.95 It would also have realised that the Ministerial Committee should have
been advised that, should it choose to disagree with the department’s
recommendation and approve funding, it would be appropriate to make such
approval subject to the applicant providing evidence of finance approval. This
would have addressed the risk of Regional Partnerships funds being paid prior
to the funding necessary to complete the project having been secured.

12.96 Nor did DOTARS examine the relative assignment of risk and
financing costs to the Commonwealth that would arise under the conditions
likely to be attached to any approved bank finance for the project. The

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941 The first in regard to whether the applicant had provided any documentation regarding the bank finance
and the second in regard to whether the bank had confirmed the funding.
associated risks have subsequently been realised under the terms of the financing facility offered by the bank and accepted by the applicant.

12.97 DOTARS also did not implement the funding condition stipulated by the Ministerial Committee in respect to confirmation of the cash capital contribution of $500 000 from shareholders in a manner that ensured that risk to the Commonwealth was minimised.

**Confirmation of development approval**

12.98 The letter of offer provided to the funding recipient by its bank identified a number of other conditions precedent that were designed to ensure there was no draw down on the construction facility prior to all necessary risk-management requirements being in place, including requirements that:

- the building contract be perused by the bank’s technical consultant, and found satisfactory to the bank as to content and counter-party; and
- all approvals and/or building consents be in place.

12.99 However, no such conditions were attached to the funding recipient receiving the first payment of Regional Partnerships funds. In this respect, Keith Seeds is not a community organisation. Nor had it identified a need to delay obtaining Development Approval pending approval of the Regional Partnerships grant due to the costs involved. Indeed, it had set the approval process in train prior to applying for Regional Partnerships funding. Consequently, it did not satisfy the criteria that the then acting Minister had agreed in April 2004 were to be applied in determining the limited range of circumstances in which there would be an exception to the requirement that:

> Project proposals that can not obtain or have not yet obtained the relevant approvals or licences to progress will not generally be considered. [ANAO emphasis]\(^{942}\)

12.100 The supporting documentation provided to DOTARS by the applicant with its August 2005 application included a letter of support dated 19 July 2005 from Tatiara District Council. The letter clearly identified that the applicant did not yet have all necessary approvals, advising:

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\(^{942}\) Those criteria had been advised to the acting Minister for Transport and Regional Services in seeking the Minister’s agreement to a revision to the Programme Guidelines to allow for the possibility of some limited exceptions to the provision that projects that had not yet obtaining relevant approvals and licences were not eligible for funding. These limited criteria were also set out in the Internal Procedures Manual.

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Although Development Approval has not been granted as yet, as we are part way through the public consultation process, this should be straight forward.

12.101 In the assessment process, the applicant advised DOTARS on 9 September 2005 that:

Building approvals are under way and we have been granted Provisional Development Plan consent. I will forward a copy of the letter from council shortly.

12.102 However, DOTARS did not obtain a copy of the Provisional Development Plan consent during its assessment. Nor was any further scrutiny applied to the question of eligibility under the Guidelines before the project was submitted to the Ministerial Committee for its consideration in January 2006. Had DOTARS obtained a copy of the Provisional Development Plan consent, it would have been in a position to identify that the notification form clearly stated that Development Approval was still required and that the project could not proceed until that Approval had been given.

12.103 On 19 September 2006 ANAO requested DOTARS’ advice as to why it had not included advice to this effect in either the original or revised assessments provided to the Ministerial Committee or advised the Committee that any funding approval should be subject to the applicant obtaining all necessary approvals. On 7 November 2006, DOTARS advised ANAO that:

The recommendation was that the application not be approved. Consequently, the need for a condition concerning confirmation of development approval was redundant. [Emphasis as per DOTARS’ advice]

12.104 However, as noted, it is prudent for the department to take a wider view of its role in the assessment and approval process.

**ANAO conclusion**

12.105 The applicant did not have the necessary development approvals in place at the time of application and assessment. In this respect, the Programme Guidelines in place at the time this project was assessed stipulated that: ‘Project proposals that can not obtain or **have not yet obtained** the relevant approvals or licences to progress will not generally be considered.’ The project did not satisfy the criteria for an exception to this eligibility requirement that had been advised to the acting Minister by DOTARS in seeking his agreement to a relaxation of the original eligibility requirement in relation to projects having obtained necessary approvals, and set out in the Internal Procedures Manual. Further, the department’s assessment did not provide the Ministerial...
Committee with relevant information to ensure appropriate risk mitigation conditions were imposed on its funding approval.

**First payment made before all relevant approvals were obtained**

12.106 Consistent with the department’s 2004 advice to the acting Minister for Transport and Regional Services in obtaining the Minister’s approval for exceptions to be made to the requirement for statutory approvals, the Internal Procedures Manual applicable at the time this application was assessed and approved stipulated that:

> To cover off the risk associated with these exceptions a provision must be included in the Funding Agreement to ensure that the first payment cannot be made until the necessary approvals/licences have been obtained, and possibly a timeframe for obtaining the approval as well.943 *[Emphasis as per Manual]*

12.107 Contrary to both the April 2004 departmental advice to the acting Minister and the requirements of the Internal Procedures Manual, the Funding Agreement provided to Keith Seeds for signature on 21 June 2006 did not stipulate that obtaining all necessary approvals was a pre-condition of the first payment being made. Instead, the first milestone description, which had an expected completion date of 21 July 2006, included ‘Building plans and approvals finalised’. The first Progress Report was also due on 21 July 2006. The first payment of $285 750 was proposed to be made on 28 July 2006.

12.108 In providing the Funding Agreement, DOTARS advised the funding recipient that:

> To allow time for the necessary process of consulting the shareholders I have set a due date for the first report as 21 July 2006. This report should cover the activities of the first milestone (listed in the Schedule to the Agreement) and include evidence of the shareholders approval, details of the successful tenderer and confirmation of the building approval. On receipt of this report we can then allow for the first payment to be made.

12.109 On 31 July 2006, the funding recipient returned the signed Funding Agreement, advising that also enclosed was ‘Copy of development approval from the Tatiara District Council.’ However, the document provided was a copy of the Provisional Development Plan consent of 12 August 2005 referred to during the assessment process, but not previously obtained by DOTARS (see paragraphs 12.101 to 12.102). As noted, the provisional approval clearly

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943 DOTARS Regional Partnerships Programme Internal Procedures Manual, September 2005, p. 34.

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stated that a Provisional Building Rules consent and Development Approval were both still required. It further stated:

No work can commence on this development unless a Development Approval has been obtained. If one or more consents have been granted on this Notification Form, you must not start any site works or building work or change the use of the land until you have also received notification of a Development Approval.

12.110 This document clearly did not satisfy the terms of the Funding Agreement, in that the applicant had not provided a Progress Report that confirmed building plans and approvals were finalised. Despite this, the first instalment was approved for payment by DOTARS on 7 August 2006.944

12.111 In response to ANAO queries on this issue, on 7 November 2006 DOTARS advised ANAO that Development Approval was obtained by the applicant on 11 August 2006.945 DOTARS had obtained a copy of the Development Approval from Tatiara District Council on 3 November 2006, some three months after the first payment of Regional Partnerships funds of $285 750 (plus GST) was made. It is apparent that the department made inquiries in this respect only in response to ANAO’s queries.

ANAO conclusion

12.112 DOTARS did not adequately scrutinise the documentation provided to it by the funding recipient, both with its original application and subsequently, in relation to the status of necessary development approvals. Nor did it seek necessary documentation, so as to ensure that:

- the Ministerial Committee was adequately advised as to the eligibility of the application under the Regional Partnerships Guidelines;
- the Funding Agreement, and any payments made pursuant to it, properly reflected the basis on which the acting Minister had approved

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944 From July 2006, the Programme Guidelines no longer stipulated a requirement that statutory approvals are required for project eligibility. In August 2007, DOTARS advised ANAO that: ‘This revision recognises that gaining the required approvals can take considerable time and that certain projects can not adequately progress should they be required to suspend progress until statutory approvals are received.’ However, DOTARS advised that, as a risk mitigation measure, the Guidelines now state that: ‘If a project is approved without all required statutory approvals, it will be necessary to obtain the approvals before a first payment can be made.’

945 In this respect, ANAO notes that the applicant’s first Progress Report to DOTARS on 29 November 2006 reported that: ‘Construction began on the 24/07/2006 with the formation of the earthworks on the site.’ On that basis, it appears that construction commenced prior to the applicant obtaining Development Approval.
the change to the Guidelines in relation to approvals and licences and appropriately managed any risks to the Commonwealth; and

- no payments of Regional Partnerships funds were made until the department had received evidence of all necessary approvals for the project to proceed.

**Conditions precedent in lease agreement**

**12.113** Also included in the supporting documentation provided to DOTARS with the August 2005 application was a copy of the 50 year lease the applicant had entered into for the site on which it proposed to construct the new facility. The lease commenced on 1 January 2005 and expires on 31 December 2054. Clause 7.4 of the lease agreement stipulated as follows:

**Construction of Lessee’s Facility**

The Lessee must at the Lessee’s expense:

(a) commence construction of the Lessee’s Facility by no later than 30 December 2005;

(b) construct the Lessee’s Facility strictly in accordance with the approved plans and specifications and planning approval, obtained prior to commencing construction of the Lessee’s Facility; and

(c) bring the Lessee’s Facility to Practical Completion by no later than 31 December 2006.

**12.114** Clause 8 of the lease agreement stipulated conditions precedent, as follows:

**8. CONDITIONS PRECEDENT**

8.1 This Lease and the obligations of the parties under it (apart from this clause) are subject to the Lessee:

(a) obtaining all necessary building and development approvals for construction of the Lessee’s Facility prior to 1 July 2005; and

(b) commencing to construct the Lessee’s Facility prior to 30 December 2005.

8.2 The Lessee must use its best endeavours to satisfy the conditions set out in clause 8.1.

8.3 If the conditions set out in Clause 8.1 are not satisfied by the dates specified in clause 8.1 the Lease may be rescinded by:

(a) the Lessor; or
(b) the Lessee, if there is no default by the Lessee under Clause 8.2.

12.115 As discussed, it was apparent from the 19 July 2005 letter of support from Tatiara District Council that all necessary building and development approvals had not been obtained prior to 1 July 2005 (see clause 8.1(a) above). Further, construction of the facility did not commence prior to 30 December 2005 (see clause 8.1(b) above).

12.116 In those circumstances, there was an identifiable risk that the lease over the land on which the applicant proposed to construct the new facility could be rescinded. DOTARS did not seek any information from the applicant to confirm the arrangements it had in place with the lessee in regard to any extension of time to obtain building and development approval and commence construction. On 7 November 2006, DOTARS confirmed to ANAO that this was not identified as an issue during the assessment process.

ANAO conclusion

12.117 Similar to the financing issue discussed above, DOTARS did not adequately scrutinise the documentation provided to it in order to determine the conditions and associated risks attaching to the applicant’s tenure over the land on which the new facility was proposed to be constructed.

Project costs

12.118 The total project cash costs identified in the August 2005 application were $3 389 402 (GST exclusive). This was comprised of:

- $2 349 991 (69 per cent) for construction of the facility, as identified in a quote from a construction company dated 12 May 2005; and
- $1 039 411 (31 per cent) for the purchase of imported specialised processing equipment, as identified in three quotes from two firms, one dated 27 July 2005 and two dated 8 August 2005.

12.119 In its 12 August 2005 application, the applicant proposed to fund up to 83 per cent of cash costs by way of a bank loan. The external viability assessment had identified concerns in respect to the applicant’s liquidity position. In those circumstances, the accuracy of the project budget, and the

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946 The application, as submitted, proposed that the applicant would contribute $2 802 902 toward project cash costs of $3 389 402. A letter to the applicant from its bank, included in the supporting documentation attached to the application, expressed an interest in providing the applicant with finance of up to $2.9 million for the project. Accordingly, the application as originally submitted by the applicant and reflected in the department’s original assessment provided to the Ministerial Committee in January 2006, was that it would borrow $2.8 million towards the project cash costs of $3.389 million.
means by which the applicant intended to fund any potential cost increases, were important considerations in respect to the viability of the project. However, the assessment undertaken by DOTARS did not adequately scrutinise this aspect of the application.

Construction costs

12.120 The May 2005 quote for construction of the facility included with the August 2005 Regional Partnerships application stated:

[The] pricing is based on special quotations from Suppliers. In order for us to secure the prices we would appreciate an early decision by the Board. Also if a prompt decision is reached and the Board awards [its] the contract it would allow us to prepare plans, computations and all the documents required during June 2005 so that we can commence onsite the 1st week in July 2005.

12.121 Despite the pricing qualification included in the construction company’s quote, there is no evidence of DOTARS applying any scrutiny to this element of the project costs. Nor did DOTARS provide the quotes included with the application to the external assessor to consider as part of its original viability assessment. The October 2005 draft report of the external assessor had stated that:

The reasonableness and accuracy of the costing provided to construct and fit out the Keith facility cannot be confirmed given no documents relating to the construction or the subsequent funding were sighted.

12.122 Despite having the relevant quotes in its possession, DOTARS instructed the external assessor to finalise its report on 8 November 2005 without providing any further advice regarding that aspect of the report. The references to the absence of quotes remained in the final version of the report.

12.123 The applicant’s 1 March 2006 letter commenting on the external viability assessment referred DOTARS to the appendices to its application containing the construction quote and two equipment quotes, advising:

This in our opinion covers the full cost of the project in an in-depth format. The Board has accepted these quotes and are firm and binding once the grant has been approved.

12.124 As noted, however, the May 2005 quote advised that the pricing was dependent on a quick decision to allow the contractor to secure ‘special quotations’.
12.125 DOTARS provided the construction and equipment quotes to the external assessor on 3 March 2006, for its consideration in undertaking the supplementary external viability assessment. As noted, the March 2006 supplementary external assessment revised its assessment of the project viability from high to medium, advising:

The reasonableness and accuracy of the costing provided to construct and fit out the Keith facility is confirmed. The letter from [the applicant’s bank] confirms funding support to the value of $2.19 million, which is approximately $612,902 less than stated on the application. However it appears that the majority of the shortfall of funding will be made up with additional shareholder funds of $500,000 and a reduction in costs of approximately $130,000.

12.126 However, this assessment did not take any account of the time that had elapsed since the quotes had been provided, the potential for construction and/or equipment costs to have changed over that time; or what aspects of the project the apparent reduction in costs related to and how they were proposed to be achieved.

12.127 The department’s April 2006 revised assessment similarly failed to apply any scrutiny to those factors. DOTARS did not seek any further clarification from the applicant in regard to the ‘firm and binding’ nature of the project costs prior to advising the Ministerial Committee on 6 April 2006 (over ten months after the date of the construction quote) that:

The reasonableness of the costings was confirmed in the revised viability assessment. The previous shortfall of funds will be made up from reduced costs and a $500 000 share issue.

12.128 In August 2007, DOTARS advised ANAO that the applicant’s statement that the quotes were firm and binding was seen as reconfirmation of the validity of the quotes, and that the advice set out in the supplementary financial viability assessment was interpreted as confirmation that the costs were accurate and firm. However, given DOTARS had the quotes referred to by the applicant in its possession, which clearly identified that the validity periods had elapsed, a more prudent approach would have been for the department to have obtained unambiguous confirmation of the status of the quotes from the applicant, including documentation provided by the relevant suppliers confirming their quoted prices. This was not done.

12.129 Rawlinsons produces building indices applicable to projects worth in excess of $500 000 as a guide to the effect on building costs brought about by
periodic variations in the rates of labour and materials, together with the effect of building activity and resource availability (that is, market competition).\footnote{Rawlinsons, Construction Cost Guide 2006 For Housing, Small Commercial and Industrial Buildings, Edition 14, p. 3.} Table 12.1 outlines the estimated effect on the cost of the project that would have been identifiable to DOTARS at the time of its assessment by applying the available Rawlinsons’ building price indices to the May 2005 construction quote. It also includes the price ultimately struck in the construction contract for the project executed on 2 August 2006.

**Table 12.1**

<table>
<thead>
<tr>
<th>Cost projection point in time</th>
<th>Total Cost $(GST exc.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>May 2005 quote</td>
<td>2 349 991</td>
</tr>
<tr>
<td>January 2006: Original assessment completed (31 December 2005 index)</td>
<td>2 603 446</td>
</tr>
<tr>
<td>April 2006: Revised assessment completed (31 March 2006 index)</td>
<td>2 655 515</td>
</tr>
<tr>
<td>August 2006: Regional Partnerships Funding Agreement signed (30 June 2006 index)</td>
<td>2 681 550</td>
</tr>
<tr>
<td>August 2006: Contracted price</td>
<td>2 723 199</td>
</tr>
</tbody>
</table>

Source: ANAO analysis of documentation provided to DOTARS and ANAO by Keith Seeds and Rawlinsons building price indices.

12.130 Table 12.1 shows that by January 2006, when DOTARS provided its original assessment to the Ministerial Committee, the use of Rawlinsons’ indices by the department would have indicated that the cash cost of the project was likely to have risen to $3 642 857 (GST exclusive) (having regard only to likely construction cost increases). That is an increase of $253 455 or 7.5 per cent higher than the cost used in the assessment. The use of Rawlinsons’ indices further indicates that by April 2006, when DOTARS provided its revised assessment to the Ministerial Committee, the cost of the project was likely to have increased by a further $52 069 to $3 694 926, 8.3 per cent higher than the project cash costs identified in DOTARS’ assessment.

12.131 Likely cost increases of this nature are significant, particularly in cases, such as this application, where there are already financial viability concerns. Although the department was not recommending the project for funding
approval, advice in relation to likely cost increases, and analysis as to how the applicant was proposing to fund such increases, could be expected to be of value to the Ministerial Committee to inform its decision regarding the appropriateness of approving funding for the application.

12.132 Table 12.1 further illustrates that Rawlinsons’ indices indicated that by August 2006, when DOTARS executed the Funding Agreement, the May 2005 quote of $2,349,991 (GST exclusive) could have been expected to have increased to $2,681,550, or $331,559 (14 per cent) higher than the costs included in the Funding Agreement. Table 12.1 also shows that the projected rate of increase was borne out in the actual price of $2,723,199 (GST exclusive) specified in the contract executed between Keith Seeds and the construction company on 2 August 2006.

**Imported specialised processing equipment costs**

12.133 The remaining $1,039,411 of cash costs identified in the application and DOTARS’ assessments related to equipment that would be imported from overseas, as set out in three quotes attached to the application. All quotes were time limited. Two were valid until 31 October 2005. The third, dated 27 July 2005, was subject to a confirmed order acceptance within 30 days of the quotation. Consequently, all of the equipment quotes were no longer valid at the time DOTARS submitted its assessment of the project to the Ministerial Committee on 13 January 2006. Each quote was also based on a specified foreign exchange rate that was subject to variation. As a result, unless the applicant had entered into forward contracts, it would have a foreign exchange exposure that could impact on project costs.

12.134 Despite the resulting uncertainty in relation to the cost of a significant component of the project, neither DOTARS nor the external assessor addressed these issues in either their original or revised assessments of the application.

12.135 The first progress report provided to DOTARS by the funding recipient in November 2006 advised that:

Machinery quotes will be accepted at a board meeting on 14/12/06 and formal orders placed for machinery soon after that. It is expected that the machinery will arrive in Australia in late February for installation late Feb early March.

12.136 In August 2007, DOTARS advised ANAO that the final payment of Regional Partnerships funds of $57,150 (plus GST), originally scheduled for March 2007, had yet to be made, pending receipt and acceptance of a final report and audited financial acquittal of project costs. DOTARS advised that:
The audit report will not be available until 28 September 2007 as equipment to be purchased with Regional Partnerships funds is yet to be delivered. As a consequence the final audited statement will not be available until after purchases are finalised with the final payment being delayed accordingly. A variation to the due date for the final report was executed in May 2007 to accommodate the anticipated delay in the provision of the audit report. The variation has moved the final report due date to 28 September 2007.

A site visit is planned post equipment delivery, prior to approving any final payment.

12.137 On 10 October 2007, the South Australian Regional Office advised National Office that:

I understand that a further short extension of time has been given for the provision of the final report and audit. There has been a delay with the delivery of a final bit of equipment from overseas but the funding recipient anticipates he can provide the report by the end of October.

ANAO conclusion

12.138 DOTARS’ project assessment and January and April 2006 advices to the Ministerial Committee did not identify and evaluate the risk of the project costing more than the amount budgeted for, despite an environment of increasing construction costs and the outdated nature of the quotes on which the project budget was based. As a result, DOTARS also did not examine how the applicant would manage any cost increases. Construction cost increases have occurred. The assessment similarly did not address foreign exchange risks relating to over $1 million in imported specialised processing equipment.
13. Projects approved without a departmental assessment

On some occasions, a Minister has taken the decision to approve Regional Partnerships funding for a project prior to the department undertaking an assessment of the project against the Programme Guidelines. Nine such instances were noted by ANAO. Two of these projects examined below are illustrative of the difficulties that can arise where the decision-making processes for the Programme depart from those set out in the published Programme Guidelines and complementary departmental procedures. This includes an elevated risk of funding being approved for projects that either do not proceed as planned or which do not result in the anticipated outcomes and associated community benefits. A third instance is examined in the ANAO case study of RP01101 Beef Australia 2006 set out earlier in this volume.

Peel Region Tourist Railway

13.1 On 2 February 2004, the Prime Minister announced that the Australian Government would commit $845,000 to the Peel Region Tourist Railway project, subject to matching funding being provided by the State Government. At that time, there had not been any application made to the Regional Partnerships Programme in relation to the project, which involved the upgrading of the Pinjarra heritage rail precinct and the Pinjarra to Boddington railway. The tourist railway is operated by Hotham Valley Tourist Railway.

13.2 The Prime Minister’s announcement was based upon a December 2003 document which the Peel Development Commission advised DOTARS (on 1 April 2004) had been forwarded to the office of the Federal Member for Canning and, subsequently, to the Prime Minister’s office. This document outlined the project and proposed that the Federal Government partner with the Rail Heritage Foundation of WA and Western Australian State Government to undertake the project. The paper sought a commitment of $845,000 from the Federal Government over the period 2003–04 to 2007–08. In terms of this process, in November 2007, the Rail Heritage Foundation of WA advised ANAO that:

The Peel Region Tourist Railway proposal was put to the Federal Government through the Peel Development Commission (PDC) by way of which I believe

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948 As ANAO undertook detailed examination of a sample only of the projects approved for funding to 30 June 2006, it is possible that other projects were approved in a similar manner over the course of the Programme.
was the result of a request, suggestion or recommendation by Federal Member Ian McFarlane (and perhaps Don Randall, Member for Canning) whilst he was visiting the Peel Region in 2003. The RHFWA and I as Chairman did not know of nor were invited to be part of those discussions. Never-the-less, Mr. Howard’s announcement was welcomed by the RHFWA as a major step forward. I did not at that time know how or when the funds were to be delivered. It was not until later it was revealed that the funds would be administered via a Regional Partnerships Program application through DOTARS. It has remained a mystery to me and the RHFWA Board that the funds were publicly committed prior to the application process being completed. The application was prepared with the assistance of the PDC and lodged directly with DOTARS in 2004.

13.3 On 12 March 2004, the Office of the then Deputy Prime Minister and Minister for Transport and Regional Services advised DOTARS:

As you are aware the Prime Minister has committed the government to the Pinjarra railway restoration project. The Deputy Prime Minister supports this initiative. Could you please initiate a funding platform for the project.

13.4 On the same day, the Regional Services Division within DOTARS, which has responsibility for Regional Partnerships, was internally advised:

I understand that the PM announced funding of $875 000 [manually corrected to $845 000 on file copy] over 5 years for the project on 2 February 2004. There is an expectation that $150k will be spent this FY and that the total funding would come from RP...

13.5 It was, therefore, accepted that the Prime Minister had provided the substantive approval for this funding and that it would come from Regional Partnerships. DOTARS did not obtain any documentation from the Prime Minister’s Office in relation to the decision to approve the funding.

13.6 Also on 12 March 2004, DOTARS’ National Office requested that the Western Australia Regional Office follow-up with the project proponent, the Rail Heritage Foundation of WA, to get a Regional Partnerships application started. DOTARS also advised the Peel ACC of the funding announcement.949

13.7 On 7 April 2004, in response to a request from the Office of the then Minister for an update on the project, the Regional Office advised National Office that:

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949 The Chair of the Rail Heritage Foundation is a member of the Peel ACC. In this respect, in November 2007, the Rail Heritage Foundation advised ANAO that the Peel Region Tourist Railway Regional Partnerships application was submitted directly to DOTARS Perth and that this process was as requested by DOTARS Perth such that at no time did a conflict of interest arise.
We have been able to get a copy of the project summary outline from the Peel Development Commission which we understand was the one provided to the PM’s office. We have been trying to contact the principals of the proponent organisation however the key individuals are unavailable on leave. They are expected to return soon after Easter and we will progress the application process then.

13.8 In response, National Office advised:

This project assessment will need to be fast-tracked as soon as you receive the application!

13.9 On 20 April 2004, the State Government announced that it would provide the Peel Tourist Railway with $845 000 towards the establishment of a rail museum and other works at Pinjarra and Boddington stations.

13.10 DOTARS received a completed Regional Partnerships application form on 19 May 2004 and submitted it into TRAX on 20 May 2004. The project scope, and budget items listed in the application for which Regional Partnerships funding was being sought, were the same as those that had been identified in the December 2003 proposal on which the Prime Minister’s approval had been based. The department then undertook a truncated assessment process and submitted its assessment recommending that funding be approved on 7 June 2004 (19 days after receipt of the application).

13.11 During the assessment, the department obtained a copy of the December 2003 proposal on which the Prime Minister’s announcement was based and a December 2003 Business Plan. There was no documented analysis of the information by the department, with much of the information presented in the 7 June 2004 departmental assessment having been transcribed directly from the proposal and business plan. In assessing the application as satisfying the project viability criterion, DOTARS advised the then Parliamentary Secretary that:

The recently updated business plan for the project, which includes a SWOT analysis, tourism market analysis and estimated revenue projections, demonstrates its sustainability through a responsible development programme, including the works to be completed during this project.

13.12 While assessing the project as a low risk, the department advised the then Parliamentary Secretary that it was the department’s process that an independent project viability assessment be undertaken for projects of this value and that the funding should be conditional on that assessment being satisfactory.
13.13 The Parliamentary Secretary agreed to the department’s recommendation on 15 June 2004 and, following receipt of approval to award the multi-year grant from the then Parliamentary Secretary to the Minister for Finance and Administration, advised the Member for Canning of the funding approval in a letter dated 22 June 2004. Letters dated 25 June 2004 advised the funding recipient and Peel ACC Chair of the funding.

13.14 However, the nature of inquiries subsequently undertaken by DOTARS indicates that, at the time the department completed its truncated assessment, there was inadequate understanding of important aspects of the project. For example, in November 2004, DOTARS advised the Peel ACC that it was seeking the following advice from the proponent:

Basically, DOTARS asked for confirmation that the proposed venture is based on a sound current business plan, and that the project has been fully funded and is sustainable long-term; also that the roles and responsibilities of the various entities involved have been agreed and appropriately documented, particularly concerning ownership, control of and responsibility for assets.

Project status

13.15 A Funding Agreement for this project was not able to be executed until 24 January 2007, nearly three years after the Prime Minister’s announcement and 2½ years after the then Parliamentary Secretary endorsed the departmental recommendation that funding be approved. An internal review of the project and development of a business plan by the proponent had failed to demonstrate the viability of the project in its existing form.950 On 8 November 2006, DOTARS advised the Ministerial Committee that:

An internal review951 of the project and development of a business plan by the proponent failed to satisfy the Australian Government funding approval

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950 In November 2007, the Rail Heritage Foundation advised ANAO that the review ‘did not fail to demonstrate viability in all areas of the project.’

951 In November 2007, the Rail Heritage Foundation advised ANAO that:

‘A Business Plan was developed for the Peel Region Tourist Railway project by Indec Consulting on behalf of the Peel Development Commission (PDC) in October 2003. That Plan considered the project viable and sustainable. I suspect the “internal review” referred to is the review of the Indec Business Plan, also developed for the PDC by Parsons Brinckerhoff in mid 2006. The second Review identified strengths and weaknesses and made recommendations accordingly and did indeed provide for forward planning and sustainability.

As my location minimizes my electronic capability I relied upon others to forward copies of this report to DOTARS Perth and have recently discovered this did not occur. I am currently rectifying this as I believe the Linkage Report will offer satisfaction. I mention this because in some small it way demonstrates some of the difficulties the RHFWA has had to contend with over time. It is interesting to note that the PDC held a position on the RHFWA Board from its inception until August 2006. Upon resignation from the Board and a long awaited shift in roles, the project began to progress.’
condition of project viability. In addition, the Peel Development Commission had similar concerns about some of the project activities it was to fund…the applicant has now submitted a revised budget, containing items agreed to be viable and sustainable, which will enable the condition of funding approval to be met.

13.16 The revised budget omitted a number of elements of the original project, including the construction of a railway station and boardwalk at Boddington. On 5 December 2006, the Ministerial Committee agreed to vary the scope and budget for the project. Although the activities to be completed under the project were substantially varied, the total Regional Partnerships funding remained at $845 000 (plus GST), as announced by the Prime Minister in February 2004. Table 13.1 compares the budget items in the original project scope approved for funding with the revised scope of items advised to the Ministerial Committee in late 2006 as being viable and sustainable.

### Table 13.1

**Original and revised scope for Peel Region Tourist Railway project**

<table>
<thead>
<tr>
<th>Approved Budget Items</th>
<th>Approved funding</th>
<th>Revised Budget Items</th>
<th>Revised funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pinjarra Station construction</td>
<td>$165 000</td>
<td>Pinjarra Station construction</td>
<td>$272 000</td>
</tr>
<tr>
<td>Boddington Railway Station and Boardwalk</td>
<td>$100 000</td>
<td>Pinjarra – Safe pedestrian crossing</td>
<td>$260 000</td>
</tr>
<tr>
<td>Carriage Storage Shed</td>
<td>$130 000</td>
<td>Pinjarra – Turntable construction</td>
<td>$50 000</td>
</tr>
<tr>
<td>Loco running shed and conservation works</td>
<td>$250 000</td>
<td>Alumina Junction (Pinjarra)—Signalling</td>
<td>$153 000</td>
</tr>
<tr>
<td>Rail Museum</td>
<td>$200 000</td>
<td>Dwellingup – Inspection Pit construction</td>
<td>$10 000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Boddington – Tullis Bridge restoration</td>
<td>$100 000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$845 000</strong></td>
<td><strong>Total</strong></td>
<td><strong>$845 000</strong></td>
</tr>
</tbody>
</table>

Source: DOTARS advice to Ministerial Committee dated 8 November 2006.

13.17 In November 2007, the Rail Heritage Foundation advised ANAO that:

The variation came about by a previously unforeseen escalation of costs for the planned construction of the Pinjarra Station. This variation was done in complete and open consultation including the Rail Heritage Foundation, the Peel Development Commission, the Shires of Boddington and Murray, DOTARS Perth and others.
13.18 The first payment of Regional Partnerships fund of $517,000 (plus GST) (61 per cent of approved funds) was made on 2 February 2007. On 6 February 2007, bushfires destroyed large elements of the railway line on which the tourist railway operated. Media reports indicated that the Hotham Valley Tourist Railway’s main revenue source, the steam engine trips from Pinjarra to Dwellington, would stop for up to a year, putting the financial future of the railway in doubt.

Gunnedah Grains to Ethanol

13.19 As was discussed by the Senate Committee in the report of its inquiry into the Regional Partnerships Programme, an instance in which it is evident that a Ministerial Adviser played a significant role in the approval process for a particular application related to RP01207 Gunnedah Grains to Ethanol project submitted by Primary Energy Pty Ltd (Primary Energy). Based on the information that was available to it, the Senate Committee stated that it had:

...concerns about three aspects of the assessment of the Primary Energy application: the intervention in the department’s assessment and advice on the application by ministers and their staff; conflicting evidence to the Committee from departmental officers; and the use of the SONA guidelines to bypass the eligibility criteria of the Regional Partnerships program.

13.20 The proposal relating to that project had originally been submitted by Primary Energy under the Namoi Valley Structural Adjustment Package (NVSAP). That programme was subsumed into Regional Partnerships from 1 July 2003.

13.21 The proposal had sought Commonwealth funding of $1.5 million to undertake financial planning work for the construction of an ethanol bio

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952 DOTARS records indicate that the substantial up front payment was necessary in order to provide a guarantee to the Shire of Murray (a sub contractor to the funding recipient) that funds were available to enable tenders to be called and work to commence on the initial activities to be undertaken by the Shire.

953 The West Australian, 6 February 2007.


955 ibid., p. 127.

956 Under the NVSAP, announced on 22 August 2002, the government had agreed that up to $20 million would be provided over ten years for community adjustment through proposals which promoted future growth of the Namoi Valley region, diversity industry and generate long term employment. The geographical scope of the NVSAP was defined as the Local Government Areas of Gunnedah, Narrabri, Quirindi and Walgett. On 20 February 2003, the Prime Minister agreed that funding be provided for the NVSAP from the Regional Assistance Programme ($13 million over eight years) and the remaining funds of up to $7 million ($1 million per year for seven years) be met from the Natural Heritage Trust. The Regional Assistance Programme, including the NVSAP, was subsumed into the single regional assistance programme, Regional Partnerships, from July 2003.
refinery plant in Gunnedah. On 27 June 2003, the Namoi Valley Advisory Committee (NVAC) advised the then Minister for Regional Services, Territories and Local Government that it had recommended that the Minister agree to provide $1.1 million (GST inclusive) to the project, contingent on the applicant meeting performance measures based on the confirmation of financiers and a positive financial due diligence exercise.

13.22 The purpose of the NVSAP was to address the economic impact on the community from production losses expected to arise from the implementation of the NSW government’s Water Sharing Plans (WSP), which proposed a reduction in water licences for users in the Namoi Valley. The WSP was to be implemented from July 2003, later postponed to 1 January 2004. On 28 October 2003, the WSP was further deferred until 30 June 2004 ‘to give the Commonwealth more space to develop its National Plan for Water.‘

13.23 On 17 December 2003, DOTARS recommended to the then Minister for Transport and Regional Services that, given the NVSAP was predicated on the introduction of the Namoi WSP, it should be held in abeyance until the position was clearer. DOTARS advised that, until the Package was reactivated, applications from the region could still be considered under Regional Partnerships.

13.24 The department further advised that, at that time, there were four outstanding NVSAP applications that had been recommended for funding by the NVAC (including the Primary Energy application), which it advised should still be considered for funding and that a separate minute would be submitted to the Minister for his consideration.

13.25 Projects submitted under the NVSAP were located within the electorate of the then Minister for Transport and Regional Services, the Hon. John Anderson MP. On 7 January 2004, DOTARS advised the then Minister for Local Government, Territories and Roads (Minister Campbell) that:

On 22 December, Minister Anderson’s Office asked that the four outstanding projects be brought forward for consideration. Minister Anderson has asked that you be the decision maker for these matters. These projects are summarised for consideration in this brief.

13.26 DOTARS’ January 2004 advice to Minister Campbell in respect to the Primary Energy NVSAP application is set out in Figure 13.1.

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Figure 13.1

DOTARS’ advice to Minister for Local Government, Territories and Roads on Primary Energy NVSAP application: 7 January 2004

Primary Energy Pty Ltd sought funding of $1.5 million for financial planning work including finalisation of contracts and partner funding for a major Ethanol Plant in Gunnedah. They will contribute $7.5m to this phase of the project. The NVAC recommended funding of $1.1 million (GST inclusive) subject to financial viability assessment and the applicant meeting performance measures based on the confirmation of financiers. It will be important to gain assurance from Primary Energy that they consider the project is economically viable and commercially self-sustaining in the longer term given the Government’s mid-December decision to phase in excise tax on ethanol ramping up effectively from 2008-10 to a full rate of 12.5 c per litre in 2012. Primary Energy’s original business plan may have been on the basis of no excise tax of any kind.

Proponents for new Australian biofuels plants have run a very strong line that they need an excise-tax free regime for a considerable period of time - they would prefer indefinitely - in order to make a commercial profit. In the course of the BTRE/ABARE/CSIRO report on the viability of reaching a 350 million litre biofuels production target by 2012, [redacted] Primary Energy, along with the proponents for a similar plant proposed for Dalby in Queensland, made claims to the research partners along the lines that they did not believe their plants were viable with an excise tax (at whatever level) for at least 15 years.

It is crucial that Primary Energy establish whether they can indeed construct, repay any loans and make a commercially viable concern happen before the 2012 excise regime commences and reduces their per litre profit.

The claims of 50 direct jobs and 350 indirect jobs flowing from the proposed Gunnedah ethanol plant are difficult to substantiate. In addition, many of the jobs will require expertise not available in the local area, so they will be sourcing professionals and technicians from outside the region.

The Department also has some concerns from a number of other perspectives reflected in the project assessment criteria (see Attachment H) including:

- whether there are any potential retrospective funding elements, and
- the ability of the project to generate new and sustainable forms of economic activity in the region.

The NVAC has imposed significant conditions on the project and these should be fully explored before a final decision is made especially in light of the Government’s recent excise decisions (see Attachment D for details). This approach would also provide the Department with an opportunity to clarify the retrospectivity question. The use of the requested funding for consultancy purposes is also a matter of concern. The approach would also allow the Department to explore other elements of the project which may be suitable for the Australian Government to fund.

Following the financial viability assessment which will allow an examination of the issues outlined above, confirmation of financiers and the clarification of any possible retrospectivity concerns, the Department will be in a position to provide further advice.

Source: DOTARS records [name deleted by ANAO].
13.27 On 15 January 2004, Minister Campbell advised the NVAC that:

In respect to the Primary Energy proposal I note your advice regarding the need for financial viability assessment and for the applicant to meet performance measures based on the confirmation of financiers. My department has also advised that there are other issues that need clarification, so I would like these to be fully explored before a final decision is made.

13.28 No further due diligence was undertaken by DOTARS in respect to this application.958 At this time, the department had not completed an assessment of the application against the NVSAP criteria or provided any funding recommendation for Ministerial consideration.959

Consideration under Regional Partnerships

13.29 The department did not prepare an assessment of the project against the Regional Partnerships Guidelines until after it had received a letter from Minister Campbell on 5 July 2004, which the Minister had signed following receipt of written advice from Minister Anderson’s Office. Specifically, a note dated 30 June 2004 from Minister Anderson’s Chief of Staff, which was copied to Minister Anderson and included a draft letter to the department for Minister Campbell’s signature, advised Minister Campbell that:

Following concerns expressed by a number of parties about delays in progressing the application by Primary Energy for a grant under the Namoi Valley structural adjustment package I have made a number of enquiries and have concerns about the situation.

Discussions with [the applicant, its bankers and solicitors] have led me to the conclusion that there is no reason why this grant cannot be progressed now.

958 In response to questions from the Senate Committee as to the extent of due diligence undertaken on the project by the department, DOTARS advised the Committee in August 2005 that: ‘We did the backgrounds of the applicant and its codevelopers. Our checking found that they had extensive experience in developing greenfields infrastructure assets and operating and maintaining renewable fuel facilities.’ (Official Hansard, Senate Finance and Public Administration References Committee, Reference: Regional Partnerships Program, Wednesday, 17 August 2005, F&PA20). In this respect, the June 2003 Namoi Valley Structural Adjustment Package application submitted by Primary Energy stated: ‘Primary Energy and its co-developers and partners have extensive experience in developing green fields infrastructure assets and operating and maintaining renewable fuel facilities.’

959 In February 2004, Minister Anderson agreed to the recommendation to hold the NVSAP in abeyance and suspended the activities of the NVAC. However, it is unclear from departmental records as to whether, despite its earlier advice to the contrary, the department considered this extant application to also be in abeyance.
13.30 The Chief of Staff advised the Minister Campbell that:

- because the bankers and solicitors were working on a success fee basis, it was highly unlikely that they would be continuing if they did not believe that the plant had anything but an odds-on chance of success;
- export markets showed real promise;
- the main objective of getting the grant seemed to have become obscured, with the requirement being to get a sound financial package developed to bring closure, not to have a sound financial package in place with offtake arrangements before the grant was paid; and
- in his view, there was no doubt the plant would be built. In this regard, the Chief of Staff advised the Minister that:

  But if we do not keep [Primary Energy] in the game then it will be built by a consortium led by [the applicant’s bankers] in Newcastle to take advantage of the ease of access to the port and the import of raw material for processing without the hassle of “up county” quarantine requirements.

13.31 The Chief of Staff advised Minister Campbell that:

Under these circumstances my view is that there are strong grounds for the application to be quickly approved...

It is my view that Primary Energy Limited now has the expertise in place and has done more than enough preliminary work to satisfy the conditions. There is no question of retroversity being involved.

I would strongly recommend that you sign the attached letter to the Acting Deputy Secretary asking the Department to fast track this before the opportunity is lost to regional Australia.

13.32 The activities for which funding was sought, being the development of a funding prospectus and the attraction of funding partners, are not eligible for funding under the published Regional Partnerships Guidelines. However, in advising the then Minister that funding should be progressed, the Chief of Staff did not make any reference to the Programme Guidelines. Nor was any reference made to the use of the SONA procedures as a means of approving Regional Partnerships funding for an otherwise ineligible project.

13.33 It has been the practice within the Regional Partnerships Programme that a Minister will not participate in the consideration of applications for projects located in his or her electorate. It is reasonable that this principle be extended to apply not only to Ministers personally, but also to exclude the
involvement of a Minister’s staff in any processes relating to such applications after they have been submitted.

13.34 Minister Campbell’s 5 July 2004 letter to the department advised:

I have reviewed the circumstances under which the application for a grant under the Namoi Valley structural adjustment package by Primary Energy Limited has been considered.

There appears to have been some confusion over the prime purpose of the application. This has resulted in the application, which was approved for the amount of $1.1 million by the Namoi Valley Advisory Committee, being put on hold. There is now a distinct possibility that the plant will be moved from a regional location to a metropolitan centre with the subsequent loss of the social and economic benefits to regional Australia.

Both…the company’s solicitors and bankers, have confirmed that the funds are being sought for the purpose of bringing the project to financial closure. While financial modelling work has been done much is still required to finalise the financing package. Amongst other things this involves detailed engineering design and quantity surveying and legal work including agreements for ethanol and gluten offtake arrangements. The estimated cost of this work is between $1.6 million and $2.0 million. No retrospectivity is involved in processing this application now.

The conditions set down by the Namoi Valley Advisory Committee were that the funding was to be for the purpose of financial planning work for a major ethanol plant in Gunnedah. I am concerned that the matter appears to be caught up in a “Catch 22” situation. The funds were sought for major financial planning work to bring the project to “prospectus” stage and give it the best change of success. It is not contingent on firm offtake arrangements or successful financial closure as these cannot occur until the work for which the grant is being sought is completed.

[The company’s banker] is an international investment banking firm recognised as a world leader in the fields of corporate finance, infrastructure development, project financing and development and structured finance. An important consideration when considering the level of risk involved in this project is that [the company’s solicitors and bankers] are not charging upfront fees for their work. Rather the work is being done on a success fee basis which, given the reputation of these companies, suggests that there is a high level of likelihood of success in raising the equity and debt capital require to bring the plant on stream.

Offtake is not and should not be a major consideration in deciding on the provision of these funds. Nevertheless I am advised by the parties that a
number of Heads of Agreement are in train for the purchase of product by companies in the US, Europe and Japan, with negotiations continuing with the major oil companies and trading houses in Australia.

I am now satisfied that sufficient work has been done by Primary Energy Limited and their bankers to warrant progressing the application and would ask that this be done so that the funds can be provided to the company within the next two weeks.

13.35 Despite confirming that ‘the funds were sought for major financial planning work to bring the project to “prospectus” stage’, an ineligible activity under the Regional Partnerships Programme, the Minister did not refer to the Programme Guidelines, or the criteria that applied to the discontinued NVSAP. Nor did the Minister refer to having applied the SONA procedures as the basis for determining that funding should be approved for an otherwise ineligible project.

13.36 On 9 July 2004, Primary Energy’s solicitors provided a letter to DOTARS, which confirmed that it had been in discussions with the Office of the then Minister for Transport and Regional Services, advising:

We act for Primary Energy Limited in relation to its Ethanol Bio-Refinery Project. On behalf of our client and further to the formal application and confirming our oral briefing to…the Deputy Prime Minister’s Chief of Staff, I am writing to confirm that the purpose of the grant from the Namoi Valley Structural Adjustment Package is to take the Ethanol Bio-Refinery Project through to financial close.

The tasks to be funded and service providers together with an estimated timeline for payment and the distribution of costs between the Australian Government and other parties is set out in the attached table.

Your urgent attention to this matter would be appreciated, please.

13.37 A new Minister for Local Government, Territories and Roads, Minister Lloyd, was sworn in on 18 July 2004. On 23 July 2004, DOTARS provided a Minute recommending that funding not be approved for this project to Minister Lloyd’s Office. The department’s recommendation was based on its subsequent assessment of the application against the Regional Partnerships (and NVSAP) Guidelines. Attached to the Minute were:

• the 30 June 2004 note from Minister Anderson’s Chief of Staff to Minister Campbell (Attachment A);

• Minister Campbell’s 5 July 2004 letter to the department (Attachment B);
• the 9 July 2004 letter to the department from Primary Energy’s solicitors (Attachment C); and
• a copy of the SONA guidelines (Attachment D).960

13.38 The departmental assessment of 23 July 2004 assessed the project as not satisfying the partnerships or project viability criteria, as well as being ineligible under the Guidelines. In relation to partnership funding, the department advised that the $470 000 (30 per cent) co-funding proposed by the applicant did not satisfy the normal minimum requirement for commercial ventures of this type.961 In relation to project viability, the department assessed the project as a high risk, with significant issues surrounding the viability of such ethanol plants, and that the application had not demonstrated how the project would be sustained beyond the Regional Partnerships funding.

13.39 The department’s covering Minute identified three options ranging from no funding, partial funding or full funding.962 The department recommended that the Minister agree with the option of not approving any funding on the basis that the project did not satisfy the Regional Partnerships Guidelines and:

the national benefit of the project has not been sufficiently demonstrated to invoke the waiving of guidelines and assessment criteria under SONA guidelines.

13.40 The Minute and assessment were returned from Minister Lloyd’s Office, without annotation from the Minister, with the covering sheet being noted by the Minister’s Office:

Returned as discussed. Replacement minute to be provided.

13.41 DOTARS’ records in relation to this project did not document the reason for the original Minute being withdrawn. In this respect, in the course of the Senate Committee’s inquiry, DOTARS advised that this had occurred following review of the Minute by the then Acting Secretary. The Senate

960 The Minute was copied to: the Minister for Transport and Regional Services; the Parliamentary Secretary to the Deputy Prime Minister and Minister for Transport and Regional Services; Secretary of DOTARS; Acting Deputy Secretary; and Acting First Assistant Secretary, Regional Programmes and Territories.

961 This was the co-funding set out in the 9 July 2004 letter obtained by the department from Primary Energy’s solicitors. In this respect, as identified in Figure 13.1, the applicant had originally proposed to contribute $7.5 million to this phase of the project in its NVSAP proposal. This was not discussed in DOTARS’ Regional Partnerships assessment.

962 In preparing this Minute (and a subsequent Minute), DOTARS identified the funding bid as $1.1 million GST exclusive. As noted, the 27 June 2003 advice from the NVAC to the then Minister for Regional Services, Territories and Local Government was that it had recommended that the Minister agree to provide $1.1 million GST inclusive.
Committee was further advised that this review had been prompted by a telephone call from Minister Anderson’s Chief of Staff who had advised that he did not think the Minute had accurately reflected Minister Campbell’s letter. However, DOTARS did not document the communication it had received from the Chief of Staff or the subsequent deliberations within the department that led to it changing its funding recommendation.

13.42 A replacement departmental Minute provided to Minister Lloyd on 28 July 2004 advised that the department had taken Minister Campbell’s letter to mean that the former Minister had decided to fund the project. The option of not providing any funding to the project was omitted from the replacement Minute. On that basis, Minister Campbell had approved the spending proposal on 5 July 2004 in the absence of a departmental assessment of the project. Although the Minister appears to have based his approval on the advice received from Minister Anderson’s Chief of Staff, the Chief of Staff’s 30 June 2004 note to Minister Campbell was omitted from the attachments to the replacement Minute.

13.43 Despite acknowledging that Ministerial approval to fund the project had already been received, the replacement Minute sought further approval from the new Minister for the now recommended option of partial funding of $525 000 (plus GST). The reason for this is unclear. For example, advice provided to the Senate Committee by the official who had, as Acting Secretary of DOTARS, requested that the original Minute be withdrawn was that:

I read the correspondence from Senator Campbell and the minute that had gone across to the office. I formed the view, in doing so, that the minute was inadequate. It did not give due regard to Minister Campbell’s correspondence and it may therefore have misled the new minister, Minister Lloyd, about the chain of events and the circumstances at that stage.

When I met with the officials concerned, I said to them that that was my view and that I thought that the department’s brief did not responsibly and rigorously deal with a request that Minister Campbell had made in that letter. For that reason, I thought the minute was inadequate; that is probably the description I would use. When a minister makes a request of his department—and it is very rare that a minister does that in writing—then it is my professional view that it is the department’s responsibility to see that that request is implemented. That was, in effect, what I said to the staff. I then

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964 As noted, Minister Campbell’s letter to the department, together with the Chief of Staff’s note to the Minister, had been attached to the original Minute provided for Minister Lloyd’s consideration.
asked that the minute be withdrawn. In doing so, I think I said to them, ‘Be careful. I want to know whether the minute has gone to Minister Anderson or Minister Lloyd,’ because it is not good practice to attempt to withdraw something after it has already been read by its intended recipients. I received the clarification that it had not been seen by the ministers some time after that. In any event, I said to the staff that I thought the minute should be redrafted to better reflect the content of Minister Campbell’s letter. Subsequently, the revised minute was restructured to deal properly with the terms of Minister Campbell’s letter, including an outstanding issue.

13.44 The department’s original assessment of the project against the Programme criteria, recommending that funding not be approved, was again attached to the replacement Minute. However, the second departmental Minute recommended partial funding of $525 000 (plus GST) for project elements that were consistent with activities previously funded under the Regional Partnerships Programme for eligible applicants. In contrast to its earlier advice, DOTARS’ replacement Minute now concluded that the application was eligible for consideration under SONA, advising:

In the circumstances, this is our preferred option and could be justified on the basis that the national benefit of the project has been sufficiently demonstrated to invoke the waiving of guidelines and assessment criteria under SONA guidelines.

13.45 The other option identified in the Minute (option 2) was to ‘exercise Ministerial discretion’ and approve full funding of $1.1 million (plus GST) for the application. DOTARS advised:

This would be entirely consistent with the decision by Minister Campbell to fund the project.

It would, however, set a precedent that could be difficult to justify, as many projects of this nature have been rejected in the past and many more are likely to be submitted in the future. In other words, it may be difficult to reject other such projects in future, if this one is funded unconditionally.

13.46 On 2 August 2004, the Minister disagreed with the department’s recommendation of its preferred option and advised:

I approve of option 2. Pls prepare recommendation as appropriate.

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966 On 13 August 2004, DOTARS sought confirmation from the Departmental Liaison Officer to the Minister’s Office that it was correct in its ‘interpretation of Minister Lloyd’s request (in the signed brief), is that the Department proceed with Option 2, as per the normal process for approved RP projects’ was correct. This was confirmed.
13.47 The Minister did not record any reasons for the approval.

Project status

13.48 The Funding Agreement with Primary Energy was executed on 28 September 2004. It identified the project being undertaken as ‘the construction of a 120 Megalitre ethanol bio-refinery in Gunnedah, NSW, Australia.’ The Activity for which Regional Partnerships funding was to be used was finalising of the financial package, which was to be concluded on 31 December 2005. The Funding Agreement was varied in June 2005 to allow for an extended Activity completion date of 28 February 2006.

13.49 As at May 2007, $1.054 million (plus GST) of the $1.1 million in approved funding had been paid to Primary Energy. DOTARS advised the Senate Standing Committee on Rural and Regional Affairs and Transport that the final payment of $46 000 (plus GST) was still dependent upon approval of a state government environmental impact statement, the receipt of a final report and an auditable payment, with that report being expected in early September 2007.967 Depicted in Figure 13.2 is the site of the planned bio-refinery as at the time of a July 2007 ANAO site visit.

Figure 13.2

Site of proposed bio-refinery at Gunnedah as at July 2007

Source: Photograph taken during July 2007 ANAO site visit.

967 Official Committee Hansard, Senate Standing Committee on Rural and Regional Affairs and Transport, Estimates, Budget Estimates, 22 May 2007, RRA&T54.