

The Auditor-General
Audit Report No.9 2009–10
Performance Audit

**Airservices Australia's Upper Airspace
Management Contracts with the Solomon
Islands Government**

Airservices Australia
**Department of Infrastructure, Transport, Regional
Development and Local Government**

Australian National Audit Office

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of Australia 2009

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Canberra ACT
5 November 2009

Dear Mr President
Dear Mr Speaker

The Australian National Audit Office has undertaken a performance audit in Airservices Australia and the Department of Infrastructure, Transport, Regional Development and Local Government in accordance with the authority contained in the *Auditor-General Act 1997*. Pursuant to Senate Standing Order 166 relating to the presentation of documents when the Senate is not sitting, I present the report of this audit and the accompanying brochure. The report is titled *Airservices Australia's Upper Airspace Management Contracts with the Solomon Islands Government*.

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office's Homepage—<http://www.anao.gov.au>.

Yours sincerely

Ian McPhee
Auditor-General

The Honourable the President of the Senate
The Honourable the Speaker of the House of Representatives
Parliament House
Canberra ACT

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Abbreviations

2006-07 Audit Report	ANAO Audit Report No.8 2006-07, <i>Airservices Australia's Upper Airspace Management Contracts with the Solomon Islands Government</i>
Air navigation fee revenue	The air navigation fee payable by owners / operators of aircraft flying through the upper airspace of the Solomon Islands
Air Services Act	<i>Air Services Act 1995</i>
ANAO	Australian National Audit Office
Auditor-General Act	<i>Auditor-General Act 1997</i>
CAC Act	<i>Commonwealth Authorities and Companies Act 1997</i>
CASA	Civil Aviation Safety Authority
CDM Guidelines	Contract Development and Management Guidelines
Chicago Convention	The Convention on International Civil Aviation concluded at Chicago on 7 December 1944
Civil Aviation Act	Solomon Islands' <i>Civil Aviation (Amendment) Act 2005</i>
DOTARS	Department of Transport and Regional Services
DITRDLG	Department of Transport, Infrastructure, Regional Development and Local Government
ERMF	Enterprise Risk Management Framework
Flight Information Region (FIR)	An airspace of defined dimensions allocated by the International Civil Aviation Organisation.

Summary and Recommendations

Summary

Introduction

1. Airservices Australia is the Commonwealth statutory authority responsible for managing Australia's airspace in accordance with the Chicago Convention on International Civil Aviation.¹ Airservices Australia also has a role of promoting and fostering civil aviation in Australia and overseas.²
2. As part of the above roles, and in pursuit of increased commercial opportunities, Airservices Australia expanded its airspace management services in 1998 by contracting to manage the Solomon Islands and Nauru upper airspace.³ There have been two upper airspace management contracts with the Solomon Islands Government since 1998, with the current contract to conclude in 2013.⁴
3. Under the upper airspace management contracts, Airservices Australia manages the Honiara Flight Information Region (FIR) and acts as a collection agent of statutory air navigation fee revenue for the Solomon Islands Government (for which it receives a management fee).

Previous reviews of the Solomon Islands Government's upper airspace management contracts

4. On 5 May 2006, the then Minister for Transport and Regional Services requested that the Australian National Audit Office (ANAO) undertake a performance audit of Airservices Australia's administration of its upper airspace management contract with the Solomon Islands Government. This request arose from findings of a broader civil aviation audit conducted by the Solomon Islands Auditor-General, who had identified irregularities in the

¹ Australia is a contract state of the Chicago Convention on International Civil Aviation.

² Airservices Australia Annual Report 2007–08 p. 6.

³ Upper airspace is defined as that space above a specific flight level, dedicated to over flight. The Solomon Islands upper airspace applies to airspace above 28 500 feet. Conversely, lower airspace is the space below that flight level, dedicated to airport approaches.

⁴ The first contract was made on 27 April 1998 (the original contract) and ran for a period of five years. The current contract commenced on 21 May 2003 (the current contract), and runs for 10 years.

administration of air navigation fee revenue collected by Airservices Australia on behalf of the Solomon Islands Government.

5. ANAO Audit Report No.8 2006–07, *Airservices Australia's Upper Airspace Management Contracts with the Solomon Islands Government* (the 2006–07 Audit Report) was tabled in the Parliament on 18 October 2006. ANAO found that Airservices Australia's commercial interests overshadowed its responsibilities as a Commonwealth statutory authority, incorporated by an Act of the Australian Parliament for a public purpose.⁵

6. Of particular note was that Airservices Australia's administration of the Solomon Islands Government's air navigation fee revenue departed significantly from the approach specified in the upper airspace management contracts. More than \$2.1 million (20 per cent of all payments) were paid outside the terms of the upper airspace management contracts. This amount comprised:

- 305 payments made to third parties between February 1999 and September 2003, totalling \$2.1 million; and
- 17 cash advances and payments, totalling \$28 558, made using Airservices Australia corporate credit cards.

7. ANAO made four recommendations relating to the development, administration and management of the upper airspace management contracts with the Solomon Islands Government and to provide greater clarity over its ability to enter into future, similar commercial arrangements with other countries.

Audit objective

8. The objective of the follow-up audit was to assess the extent to which Airservices Australia, and where relevant, the Department of Infrastructure, Transport, Regional Development and Local Government (DITRD⁶), have

⁵ ANAO Audit Report No.8 2006-07, *Airservices Australia's Upper Airspace Management Contracts with the Solomon Islands Government*, Canberra, 18 October 2006, para. 17.

⁶ Throughout this report, ANAO refers to the Department of Infrastructure, Transport, Regional Development and Local Government as DITRD⁶. At the time the previous ANAO audit was undertaken, the transport function was included in the Department known as the Department of Transport and Regional Services (DOTARS). ANAO refers to the former department as DOTARS throughout this report.

implemented the four ANAO recommendations contained in the previous audit report.

Overall audit conclusions

9. Airservices Australia has recently changed its strategic direction to focus on its core business activities and no longer aims to pursue new commercial revenue opportunities similar to the Solomon Islands upper airspace management contract. As a consequence, Airservices Australia has not entered, and advised it is not currently seeking to enter, into new commercial contracts with other countries of a similar nature to its Solomon Islands contract. In these circumstances, the likelihood of administrative irregularities reoccurring is reduced.

10. Airservices Australia has also significantly improved its processes and procedures for the management of the financial aspects of the existing upper airspace management contract with the Solomon Islands Government. As a result, in the period from 1 September 2006 to 31 March 2009 Airservices Australia had:

- remitted all air navigation fee revenue to the account specified in the current contract;
- not made any third party or cash payments in respect of air navigation fee revenue it collected on behalf of the Solomon Islands Government; and
- received payment for managing the Solomon Islands Government's upper airspace in accordance with the contract.

11. In summary, Airservices Australia and DITRD LG, where relevant, have substantially implemented the four recommendations of the 2006–07 Audit Report.

Key findings

Legislative compliance and strategic direction (Chapter 2)

12. Following a change in strategic direction, Airservices Australia has not entered into any commercial revenue contracts similar to the current contract since the 2006–07 Audit Report was tabled in Parliament. In addition, Airservices Australia advised ANAO that it is unlikely to pursue commercial revenue opportunities of this type in the future.

13. Airservices Australia has documented policies and procedures to provide itself, the Minister and DITRDLG with increased assurance that new proposed business opportunities comply with Airservices Australia's strategic direction and its Minister's Statement of Expectations, the *Air Services Act 1995* (Air Services Act) and Australian Government policy. These policies and procedures provide a systematic approach for Airservices Australia to promote compliance with its operational, strategic, financial and legislative obligations.

14. The 2006–07 Audit Report concluded that the absence of a shared understanding between Airservices Australia and the then Department of Transport and Regional Services (DOTARS) regarding Airservices Australia's ability to enter into commercial contracts to manage the upper airspace of other countries was not conducive to a sound governance framework for Airservices Australia's international operations. Airservices Australia and DITRDLG have discussed and resolved these inconsistencies such that the first recommendation of the 2006–07 Audit Report has been substantially implemented. However, there would be benefits in the shared understanding being more formally documented by senior officials in both entities (at present, the understanding is documented through an exchange of emails, with a relatively junior DITRDLG officer indicating that the department was 'happy with the approach' suggested by Airservices Australia). In October 2009, DITRDLG advised ANAO that the department would be seeking an exchange of letters with Airservices Australia at the chief executive officer level on this matter.

Contract development, management and administration (Chapter 3)

15. Airservices Australia has sought to address many of the contract development and management issues identified in the 2006–07 Audit Report. Specifically, Airservices Australia has:

- introduced a revised corporate structure to develop and manage international contracts, which clearly specifies the roles and responsibilities of relevant contract management staff;
- improved the communication between those Airservices Australia areas responsible for various aspects of contract management including legal, finance and administration;

- developed documented practices, procedures and controls which address the findings of the 2006–07 Audit Report and subsequent internal reviews of the current contract⁷; and
- introduced a systemic approach to monitoring and reporting on completed international contracts.

16. Airservices Australia has also taken measures to improve the current contract. Specifically, Airservices Australia has amended the contract and the related Contract Management Plan to recognise the nature of the relationship between the Solomon Islands Government and Airservices Australia and its role as a collection agent on behalf of the Solomon Islands Government. There would be benefit in Airservices Australia improving the rigor of the Contract Risk Management Plan, in the manner advocated by its recently adopted Enterprise Risk Management Framework.

Accounting for collections, payments and the receipt of management fees (Chapter 4)

17. Following the development and execution of the 2007 amendment to the current contract, Airservices Australia has increased its awareness of its obligations and responsibilities under the Solomon Islands Constitution and the current contract. Specifically, Airservices Australia has:

- obtained assurance that the manner in which it is paid for the administration of the upper airspace of the Solomon Islands is compliant with the Solomon Islands Constitution;
- remitted all air navigation fee revenue collected on behalf of the Solomon Islands Government to the Aviation Special Fund, although this could be more timely⁸;
- not made any third party payments in respect of air navigation fee revenue collected on behalf of the Solomon Islands Government; and

⁷ Subsequent reviews include an internal audit (conducted by Airservices Australia's Audit and Assurance Division in April 2008) and external review (conducted by an independent consultant in August 2008) of Airservices Australia's implementation of the findings arising from the 2006-07 Audit Report.

⁸ Under the terms and warranties of the current contract, Airservices Australia must remit air navigation fee revenue to the Solomon Islands Government's Aviation Special Fund no later than 60 days after the air navigation fee revenue has been collected for the relevant month, in order to comply with the Solomon Islands Constitution (rather than remitting fees within 90 days as is the current practice).

- not made any cash advances or credit card transactions in respect of air navigation fee revenue collected on behalf of the Solomon Islands Government.

18. This is a positive response to the earlier issues arising from the management of the upper airspace management contracts with the Solomon Islands Government.

Agency responses

19. DITRDLG advised ANAO that it was pleased that the performance audit found that Airservices Australia and the department have substantially implemented the four recommendations of the 2006–07 Audit Report. Airservices Australia commented as follows:

Airservices Australia agrees with the outcome of the audit and is pleased, in particular, with the overall conclusion that recognises the significant efforts that have been made to improve processes and procedures that govern these types of contracts. Airservices Australia notes that there are no new recommendations arising from this report.

Audit Findings and Conclusions

1. Introduction

This chapter provides background information on Airservices Australia and its upper airspace management contract with the Solomon Islands Government. It also explains the audit approach and structure of the audit report.

Background

1.1 The world's airspace is divided into a series of contiguous Flight Information Regions (FIRs) within which air traffic services are provided. Australia has two FIRs, which collectively cover more than 11 per cent of the world's surface. This includes Australia's sovereign airspace (comprising the Melbourne and Brisbane FIRs) as well as international airspace over the Pacific, Indian and Southern Oceans.

1.2 Airservices Australia is the Commonwealth statutory authority responsible for managing Australia's airspace in accordance with the Chicago Convention on International Civil Aviation.⁹ One of Airservices Australia's principal roles is to provide for the safe navigation of aircraft within Australian-administered airspace.¹⁰

1.3 Airservices Australia also has a role of promoting and fostering civil aviation in Australia and overseas.¹¹ As part of this role, and in pursuit of increased commercial opportunities, in 1998 Airservices Australia started to expand its airspace management services by contracting to manage the Solomon Islands and Nauru upper airspace.¹² Figure 1.1 shows Australia's sovereign airspace, as well as the FIRs of Solomon Islands (Honiara) and Nauru.

⁹ Australia is a contract state of the Chicago Convention on International Civil Aviation.

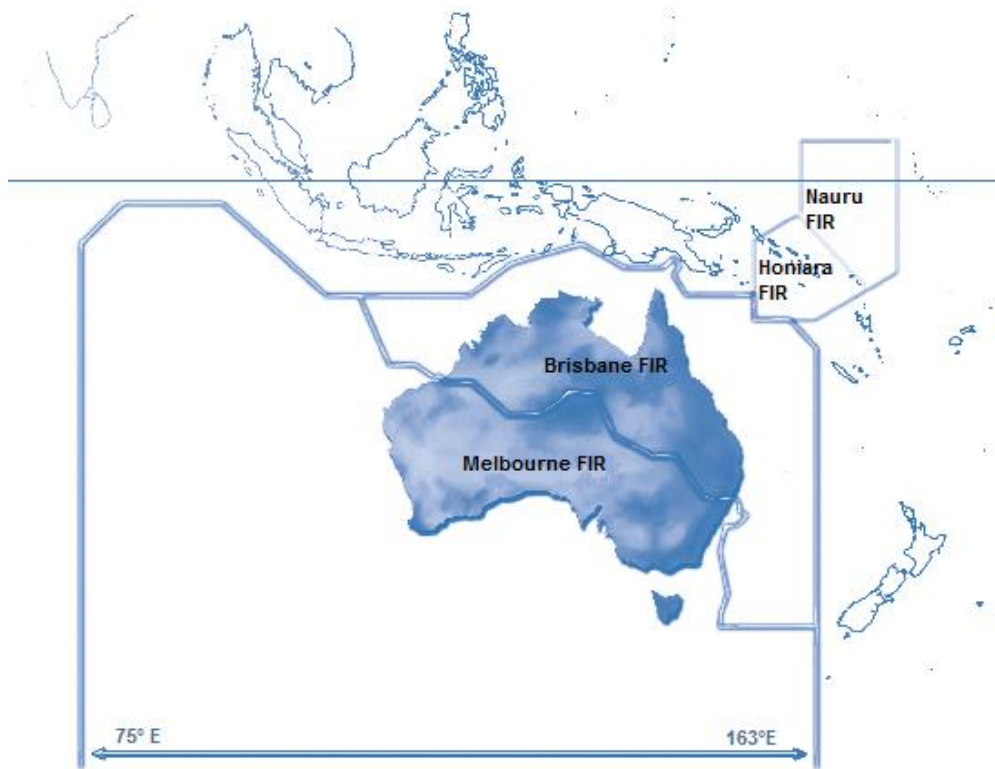
¹⁰ Airservices Australia Annual Report 2007-08 p. 6.

¹¹ *ibid.*

¹² Upper airspace is defined as that space above a specific flight level, dedicated to overflight. The Solomon Islands upper airspace applies to airspace above 28 500 feet. Conversely, lower airspace is the space below that flight level, dedicated to airport approaches.

Figure 1.1

Upper airspace controlled by Airservices Australia



Source: Airservices Australia.

Overview of Airservices Australia's contracts to manage the Solomon Islands upper airspace

1.4 There have been two upper airspace management contracts with the Solomon Islands Government. The first contract was made on 27 April 1998 (the original contract) and ran for a period of five years. The current contract commenced on 21 May 2003, and runs for a further 10 years.¹³ The terms of this contract were similar to the original contract. Both contracts have comprised two distinct but related services:

¹³ In order to strengthen the corporate governance arrangements between Airservices Australia and the Solomon Islands Government, two variations were made to the current contract. Separate amendments to this contract were made on 17 August 2004 and 3 August 2007. The variation made on 3 August 2007 was made in part to address the issues identified in the 2006-07 Audit Report. This is discussed further in Chapter 4.

- management of the upper airspace in the Honiara FIR; and
- collection of air navigation fee revenue from aircraft/airlines that pass through the Honiara FIR upper airspace on behalf of the Solomon Islands Government, and the remittance of such revenue to a designated Solomon Islands Government bank account in accordance with the contract.

1.5 For the year ended 30 June 2009, there were a total of 4 489 flights through Solomon Islands upper airspace. Air navigation fee revenue attributable to those flights totalled \$1.48 million. Airservices Australia received approximately \$594 000 for the management of the Solomon Islands upper airspace for that time period.

The 2006–07 Audit Report

1.6 On 5 May 2006, the then Minister for Transport and Regional Services requested that the Australian National Audit Office (ANAO) undertake a performance audit of Airservices Australia's administration of its upper airspace management contract with the Solomon Islands Government. The then Minister for Transport and Regional Services' request arose following findings of a broader civil aviation audit conducted by the Solomon Islands Auditor-General.

1.7 On 31 May 2006, the Auditor-General designated a performance audit under section 18 of the *Auditor-General Act 1997* (Auditor-General Act). The objectives of that audit were to:

- examine the development and administration by Airservices Australia of its contracts with the Solomon Islands Government for upper airspace management;
- assess the regularity of payments made under the contracts and steps taken by Airservices Australia in respect of any irregularities; and
- make recommendations for any improvements in processes employed by Airservices Australia in developing and administering these and similar contractual arrangements.

Findings and recommendations

1.8 ANAO Audit Report No.8 2006–07, *Airservices Australia's Upper Airspace Management Contracts with the Solomon Islands Government* (the 2006–07 Audit Report) was tabled in the Parliament on 18 October 2006.

1.9 ANAO found that Airservices Australia's administration of air navigation fee revenue for the Solomon Islands Government departed significantly from the approach specified in its written contracts. Specifically, more than \$2.1 million (20 per cent of all payments) was paid outside the terms of the upper airspace management contracts. This amount comprised:

- a total of 305 payments to third parties between February 1999 and September 2003 amounting to \$2.1 million. The main categories comprised fees and expenses of an aviation adviser contracted to the Solomon Islands Government, education expenses for Solomon Islanders studying at academic institutions in a number of countries, and travel expenses; and
- a total of 17 cash advances and payments totalling \$28 558 made using Airservices Australia corporate credit cards. This amount principally related to travel allowances and travel expenses.

1.10 Airservices Australia relied upon authorisation from Solomon Islands Government Ministers and officials as sufficient basis to depart from the terms of the written contract. However, the audit concluded that this approach was not consistent with sound contract management practices, and was not prudent given the number and variety of payment transactions. Further, the manner in which these transactions were processed as deductions from air navigation fee revenue may also have contributed to any irregularities in the use of this revenue by Solomon Islands Government Ministers and/or officials.¹⁴

1.11 ANAO concluded that, in developing and managing the Solomon Islands upper airspace management contracts, Airservices Australia was primarily concerned with managing its commercial interests and related risks. Further, the prioritisation of its commercial interests overshadowed

¹⁴ The Solomon Islands Auditor-General's report identified irregularities in the administration of the contract, with particular reference to payments made by Airservices Australia to third parties. See Solomon Islands Auditor-General Report, 4 October 2006, *Special Audit into the Financial Affairs of the Civil Aviation Division of the Ministry of Infrastructure and Development*.

Airservices Australia's responsibilities as a Commonwealth statutory authority, incorporated by an Act of the Australian Parliament for a public purpose.

1.12 ANAO made four recommendations relating to the development, administration and management of the upper airspace management contracts with the Solomon Islands Government and to provide greater clarity over its ability to enter into future, similar commercial arrangements with other countries.

Internal reviews

1.13 On 4 December 2007, Airservices Australia's Board requested that the organisation's Audit and Assurance Division undertake a review of the implementation of the ANAO's recommendations. Overall, Airservices Australia's Audit and Assurance Division concluded that:

...subject to the implementation of the agreed business improvements¹⁵, Airservices has successfully implemented all of ANAO's recommendations and the internal control process improvements advised to the Minister.

1.14 Further, in response to a request by the then Minister for Transport and Regional Services on 29 June 2007, a consultant was appointed by Airservices Australia's Board in April 2008 to assess whether the ANAO's recommendations had been fully implemented. The consultant's report was finalised on 26 August 2008 and concluded that:

Airservices, in consultation with the Department and the Minister, has taken action to meet each of the four ANAO recommendations, with Recommendations 1 and 4 being fully implemented. Airservices' response to Recommendations 2 and 3 were immediate with the release of new management instructions and the re-structure of the business development, contract management and administration to achieve separation.¹⁶

¹⁵ The areas for improvement identified in the Audit and Assurance Division's report related to Airservices Australia's record keeping obligations, documentation of Airservices Australia's Business Development operational procedures, implementation of contract management systems and the implementation of a performance management system across relevant members of the Business Development team.

¹⁶ Independent consultant, 2007-2008, *Follow-up of ANAO Recommendations relating to the Solomon Islands Contract*. p. 3.

Follow-up audit approach

1.15 On 13 March 2009, the Auditor-General designated a follow-up audit under section 18 of the Auditor-General Act. The objective of this follow-up audit was to assess the extent to which Airservices Australia, and where relevant, the Department of Infrastructure, Transport, Regional Development and Local Government (DITRD LG¹⁷), have implemented the four ANAO recommendations contained in the 2006–07 Audit Report.

1.16 The follow-up audit focused on the actions of Airservices Australia and DITRD LG to implement the recommendations of the 2006–07 Audit Report. The audit did not examine the administration, by Solomon Islands Government agencies or Ministers, of the upper airspace management contracts with Airservices Australia. The audit methodology included:

- an examination of all upper airspace management contracts between Airservices Australia and the Solomon Islands Government, including amendments to the contract from 1 September 2006 to 31 May 2009;
- an examination of legal documents (including legal advice provided to Airservices Australia and DITRD LG) relating to Airservices Australia's management of Solomon Islands upper airspace;
- an examination of internal documents and correspondence between Airservices Australia and DITRD LG regarding the management of Solomon Islands upper airspace;
- an examination and reconciliation of financial transactions (for the collection and payment of air navigation fee revenue and receipt of management fees) regarding Airservices Australia's management of Solomon Islands upper airspace from 1 September 2006 to 31 March 2009. This also included documents (including electronic records) supporting or associated with these transactions;
- a review of correspondence between Airservices Australia and the Solomon Islands Government;

¹⁷ Throughout this report, ANAO refers to the Department of Infrastructure, Transport, Regional Development and Local Government as DITRD LG. At the time the previous ANAO audit was undertaken, the transport function was included in the Department known as the Department of Transport and Regional Services (DOTARS). The ANAO refers to the former department as DOTARS throughout this report.

- a review of internal board and board audit committee papers and minutes from 1 September 2006 to 31 May 2009;
- an assessment of Airservices Australia's policies and procedures documentation relating to the management of international business contracts; and
- interviews with key Airservices Australia staff with responsibility for developing, administering and managing the Solomon Islands upper airspace management contract, key DITRDLG staff and relevant Department of Foreign Affairs and Trade staff.¹⁸

1.17 Audit fieldwork was conducted between April 2009 and June 2009. Audit fieldwork was undertaken by McGrathNicol, for the ANAO. The audit was conducted in accordance with the ANAO Auditing Standards and at a cost to the ANAO of \$265 000.

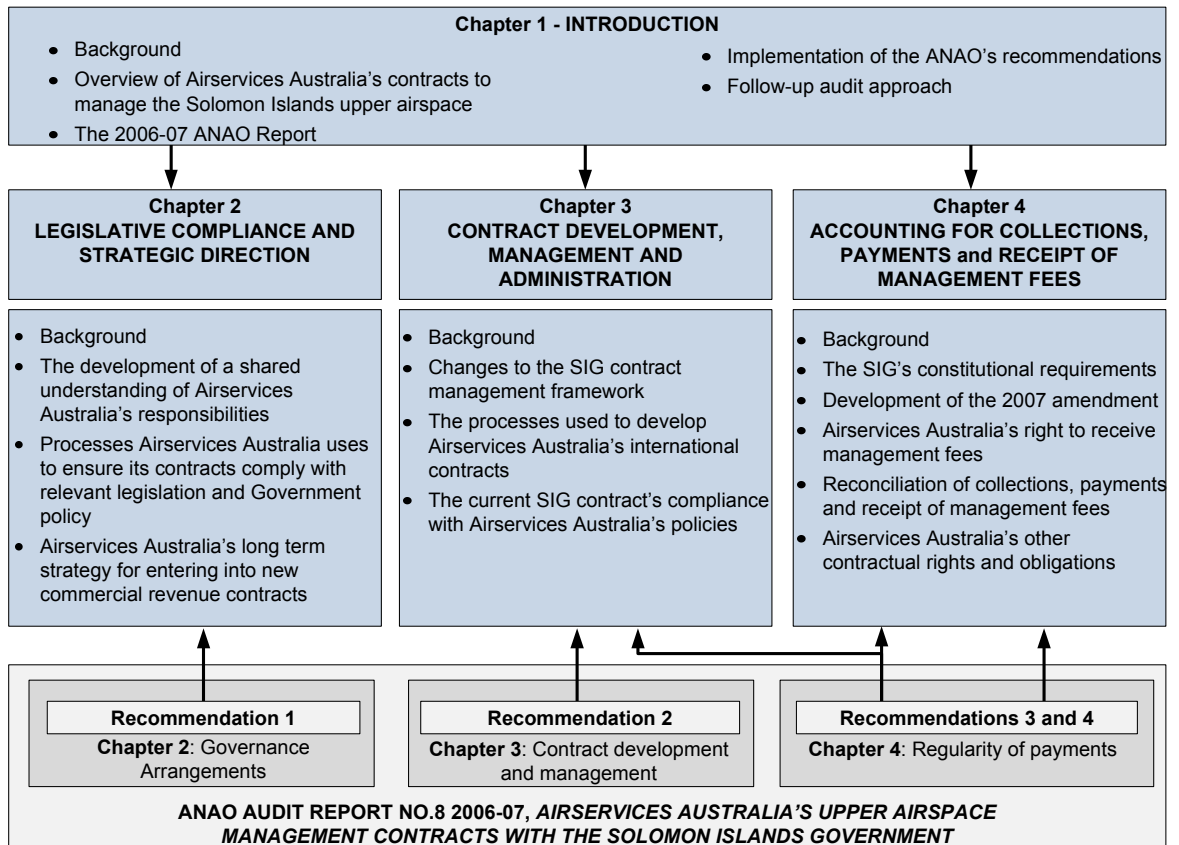
Report structure

1.18 Figure 1.2 provides the structure of the follow-up audit report and the links to the recommendations of the 2006–07 Audit Report.

¹⁸ Discussions with DFAT staff were held in order to gain an understanding of the processes and procedures used by Australian Government agencies when pursuing potential business opportunities with foreign governments.

Figure 1.2

Audit report structure



Source: ANAO.

2. Legislative compliance and strategic direction

This chapter addresses the issues and recommendation made in Chapter 2 of the 2006–07 Audit Report. The chapter also examines developments in Airservices Australia’s long term strategy for entering into upper airspace management contracts with other countries.

Background

2.1 Airservices Australia is a statutory authority under the *Commonwealth Authorities and Companies Act 1997* (CAC Act) having been established under its enabling legislation—the *Air Services Act 1995* (Air Services Act). As a statutory authority, it relies on the powers conferred upon it by its enabling legislation to earn commercial revenue. Airservices Australia’s statutory roles and functions are specified in sections 8 and 9 of the Air Services Act. Section 8(1)(b) of the Air Services Act specifies that Airservices Australia has a role in ‘promoting and fostering civil aviation whether in or outside Australia’.

2.2 The 2006–07 Audit Report examined whether Airservices Australia’s enabling legislation allowed it to enter into commercial contracts to manage the Solomon Islands upper airspace. ANAO analysis of legal advice obtained by Airservices Australia in March 2002 against the upper airspace management contracts with the Solomon Islands Government raised issues about whether Airservices Australia was empowered by its enabling legislation to enter into the contracts at the time. Subsequent legal advice obtained by Airservices Australia in September 2006¹⁹ concluded that the Air Services Act²⁰ provides the authority for Airservices Australia to enter into commercial contracts of this type.

2.3 The 2006–07 Audit Report also raised questions about whether Airservices Australia had developed appropriate processes to enter into contracts to administer other countries’ upper airspace. This included an assessment of whether key stakeholders had a common understanding of, and

¹⁹ This legal advice was obtained from the Australian Government Solicitor.

²⁰ Section 8(1)(b) of the Air Services Act.

had agreed to, the processes Airservices Australia used to enter into international commercial contracts.

2.4 The audit concluded that Airservices Australia and one of its key stakeholders (the then DOTARS) did not have a shared understanding of the process Airservices Australia needed to follow to enter into commercial contracts with other countries. This finding led to Recommendation 1 of the 2006–07 Audit Report (see Table 2.1).

Table 2.1

ANAO Audit Report No.8 2006–07: Recommendation No.1

ANAO recommends that the [then] Department of Transport and Regional Services and Airservices Australia develop and implement a shared understanding of:

- a) the extent to, and processes by, which Airservices Australia is able to agree to requests from other countries that it administer airspace allocated to those countries under the Chicago Convention on International Civil Aviation; and
- b) whether agreeing to requests to manage airspace under contract makes that airspace “Australian-administered airspace” for the purposes of the Air Services Act.

Source: ANAO Audit Report No.8 2006–07, p. 51.

The development of a shared understanding of Airservices Australia’s responsibilities

2.5 During the 2006–07 audit, Airservices Australia and the then DOTARS each obtained legal advice on whether the Air Services Act empowered Airservices Australia to enter into upper airspace management contracts. In the 2006–07 Audit Report, ANAO identified differences in the legal opinions obtained by each party. Table 2.2 summarises the differences in the legal advices obtained by Airservices Australia and the then DOTARS.

Table 2.2**DOTARS' and Airservices Australia's respective understanding of 'Australian administered airspace'**

View	DOTARS	Airservices Australia
Whether the Australian Government authorised Airservices Australia to enter into the contracts	The Government has not authorised Airservices Australia to enter into the upper airspace management contracts with the Solomon Islands Government. It was, however, not necessary for this to have occurred in order for Airservices Australia to enter into these contracts and provide services under these contracts.	On the basis that the then Minister responsible for Airservices Australia had not instructed Airservices Australia to refrain from entering into the first upper airspace management contract, it was reasonable for Airservices Australia to infer that: <ul style="list-style-type: none"> it had been authorised by the Australian Government to enter into contracts such as the Solomon Islands contract; and for that purpose, it was further authorised to accede to requests by other countries for their airspace to become 'Australian-administered airspace'.
Whether the Honiara FIR is 'Australian-administered airspace'	This airspace is not 'Australian administered airspace'. The provision of services by Airservices Australia does not require that the relevant airspace is 'Australian-administered airspace'.	

Source: ANAO Audit Report No.8 2006–07, p 51.

2.6 The absence of a shared understanding (at the time of the 2006–07 Audit Report) between Airservices Australia and DOTARS was not conducive to a sound governance framework for Airservices Australia's international operations. Not having a shared understanding of Airservices Australia's legislative responsibilities also increased the risk that Airservices Australia would:

- enter into a contract that was outside its legislative remit or was not consistent with Australian Government policy; or
- be incorrectly advised not to enter into a contract that it was entitled to enter.

2.7 In its response to Recommendation 1 of the 2006–07 Audit Report, DOTARS indicated that it and Airservices Australia had reached a shared understanding on the issues specified in Table 2.2 above.

2.8 During an internal audit follow-up of the ANAO's recommendations²¹, Airservices Australia sent an e-mail to DITRDLG on 18 March 2008 to seek clarification and ratification of the shared position, outlined as follows²²:

Issue 1

Airservices Australia is able to consider requests from other countries to administer airspace allocated to those other countries under the Chicago Convention subject to Airservices Australia complying with all applicable laws and:

1. complying with the ministerial notification provisions under section 15 (1)(e) of the Commonwealth Authorities and Companies Act 1997;
2. complying with the Statement of Expectations dated 12 May 2007 (or any subsequent variations, amendments or replacement of same); and
3. otherwise informing itself of relevant risks associated with the activity.

Issue 2

Airservices Australia and the Department agree that airspace administered by Airservices Australia under a commercial contract with another country (and not a request by that country to the Commonwealth) will generally not be 'Australian administered airspace' for the purpose of the Air Services Act 1995.

2.9 In response to the email, a relatively junior DITRDLG officer indicated that the department was 'happy with the approach' suggested. There would be benefits in the agreed approach being more formally documented by senior officials in both entities. In October 2009, DITRDLG advised ANAO that it agreed with this suggestion and that the department would be seeking an exchange of letters with Airservices Australia at the chief executive officer level on this matter.

2.10 Against this background, it is clear that through discussions and exchanges of correspondence DITRDLG and Airservices Australia have discussed and agreed a shared position in relation to the need for Airservices Australia to seek Australian Government authorisation to enter into contracts, and whether the Honiara FIR is 'Australian administered airspace'. Also Airservices Australia, DITRDLG and the Minister have put in place processes which, if followed, provide increased assurance that the Minister and

²¹ See paragraph 1.13 for the conclusion of the Airservices Australia Internal Audit report.

²² Note that Issue 1 and Issue 2 correspond to the views specified in Table 2.2.

DITRDLG are aware of the potential business opportunities²³ Airservices Australia is seeking to enter into. These processes are specified in or are guided by:

- section 15 of the CAC Act;
- *Minister's Guidelines to Airservices Australia for Engaging in Significant Non-Regulated Business Opportunities* (the Minister's Guidelines); and
- the Minister's Statement of Expectations (SOE).²⁴

Processes Airservices Australia uses to ensure its contracts comply with relevant legislation and Government policy

2.11 In establishing whether Airservices Australia had the appropriate authorisation to enter into commercial contracts with other countries, the 2006–07 Audit Report examined whether the content of the Solomon Islands contracts was consistent with Australian Government policy, and whether those contracts complied with relevant legislation.

2.12 Providing the Minister and DITRDLG with adequate visibility of, and the ability to comment on, significant proposed business opportunities reduces the risk that contracts will not comply with relevant legislation and Government policy. Ideally, DITRDLG, the Minister and Airservices Australia should also have a shared understanding of the extent to, and processes by, which Airservices Australia enters into these contracts.

2.13 To assess what Airservices Australia has done to provide itself, the Minister and DITRDLG with adequate assurance that its proposed business opportunities comply with relevant legislation and are consistent with Government policy, the ANAO examined:

- the Minister's Guidelines; and
- meeting minutes and records of Airservices Australia's Investment and Review Committee (IRC).

²³ Potential business opportunities may include airspace contracts and other commercial revenue opportunities.

²⁴ The current SOE for the period 1 November 2008 to 30 June 2010 was received by Airservices Australia on 28 October 2008.

2.14 These control mechanisms are discussed below.

Minister's Guidelines

2.15 Under section 15(3) of the CAC Act, a Minister may give written guidelines to an agency to assist it to determine under what circumstances it needs to inform the Minister of a proposed business opportunity. A failure to comply with the Minister's Guidelines can potentially lead to breaches of the CAC Act.

2.16 On 12 March 2007, the then Minister for Transport and Regional Services issued an update to the Minister's Guidelines.²⁵ These guidelines outline the Minister's information requirements regarding Airservices Australia's proposed business opportunities. This information can be used by the Minister and DITRDLG to determine whether Airservices Australia's proposed business opportunities are consistent with:

- Airservices Australia's legal framework; and
- Australian Government policy.

2.17 The Minister's Guidelines were not established prior to Airservices Australia entering into the upper airspace management contracts with the Solomon Islands Government. These guidelines were in part established as a control to minimise the risk that the issues applicable to the contracts (identified in the 2006–07 Audit Report) would reoccur.

2.18 When a particular proposal meets criteria specified in the Minister's Guidelines (for example when the value of a proposed business opportunity exceeds \$15 million²⁶), Airservices Australia must compile a business case for the Minister and DITRDLG that:

- specifies the expected financial and other benefits the business opportunity will deliver;
- identifies the risks associated with pursuing the activity or arrangement together with appropriate risk mitigation strategies;

²⁵ The original Minister's Guidelines were issued on 1 April 2004.

²⁶ Section 15(1)(e) of the CAC Act specifies that a Commonwealth Authority must immediately give the responsible Minister written comments of a proposal when it commences or ceases a significant business activity. The Minister's Guidelines identify one characteristic of a significant business activity as one that is greater than \$15 million.

- provides assurance that the proposed business opportunity complies with Airservices Australia's enabling legislation; and
- provides assurance that the proposed business opportunity is not likely to bring the Australian Government into disrepute or expose Airservices Australia to a loss of public confidence.

2.19 Since the ANAO last examined Airservices Australia's upper airspace management contracts in 2006, Airservices Australia has provided the Minister and DITRD LG with two proposed business opportunities. ANAO examined these two business cases to assess whether the Minister's Guidelines (if used) will provide increased assurance that potential proposed business opportunities (which may include upper airspace management work) comply with Airservices Australia's legal framework and are consistent with Australian Government policy. In this respect, the information contained in these proposals:

- clearly articulated the proposed business opportunity;
- specified the expected financial and other benefits of the proposed business opportunity at a high level;
- assessed the risks associated with pursuing the proposed business opportunity together with appropriate risk mitigation strategies at a high level; and
- provided assurance that the proposed business opportunity complied with Airservices Australia's enabling legislation.

2.20 Business cases of this type provide the Minister and DITRD LG with the opportunity to question, or comment on, Airservices Australia's proposed business opportunity in order to reduce the risk that Airservices Australia will enter into significant commercial contracts with other nations that do not have Ministerial support.

Airservices Australia's Investment and Review Committee (IRC)

2.21 On 17 December 2007, the IRC was formed to improve Airservices Australia's organisational decision making through the informed consideration and integrated coordination of activities. It replaced a number of pre-existing Airservices Australia committees. The IRC, through its Chair, reports to the Airservices Australia Board and Executive Committee on relevant IRC activities and decisions.

2.22 The objective of the IRC includes, but is not limited to, assisting the Airservices Australia Executive Committee by:

- monitoring planning and delivering all expenditure and revenue projects;
- monitoring planning and delivering all off-shore contracts;
- monitoring work programs of international operations;
- oversighting contract management and procurement programs; and
- monitoring alignment of the Airservices Australia's investment program with its strategic direction.

Airservices Australia's long term strategy for entering into new commercial revenue contracts

2.23 The 2006–07 Audit Report identified Airservices Australia's pursuit of other commercial revenue opportunities as a key strategic focus for the organisation. As part of the strategy detailed in its Corporate Plan July 2005-June 2010, Airservices Australia aimed to:

- expand its customer and product/service base to grow and diversify revenues; and
- be the preferred regional supplier of air traffic management and related services, jointly servicing with its partners the southern hemisphere airspace over the long term.²⁷

2.24 The focus at that time was on pursuing international business opportunities in the Gulf States, China and India. Airservices Australia's push into the international commercial market was demonstrated through the establishment of dedicated regional offices in Dubai, United Arab Emirates and New Delhi, India.

Reducing the number of commercial revenue contracts

2.25 In February and March 2008, Airservices Australia closed its Dubai and New Delhi offices following the Board of Airservices Australia's decision to revise the organisation's strategic focus from 'winning' new other commercial

²⁷ Airservices Australia, *Corporate Plan July 2005-June 2010*, p. 1.

revenue to focusing on its 'core' activities. This was to be achieved through its three strategic objectives:

- **delivering excellent core performance**—meeting regulatory and legislated obligations and improving the quality and cost-effectiveness of Airservices Australia's core services;
- **building a high achieving organisation**—developing Airservices Australia's people, leadership and capabilities; and
- **delivering the future**—meeting the challenges of the future and positioning Airservices Australia for the next generation of innovation and technology.²⁸

2.26 This strategic approach is consistent with the Government's vision for Airservices Australia, which is articulated through the Minister's SOE. The current SOE requires Airservices Australia to focus on delivering core air traffic and aviation rescue and fire fighting services, not only within Australia, but in the Asia Pacific region.²⁹ In addition, a transition plan has been developed to rationalise other commercial revenue activity including gradual termination of contracts as they expire.

2.27 A result of Airservices Australia's change in strategic focus is seen in its projected revenue figures for other commercial revenues. Figure 2.1 shows that:

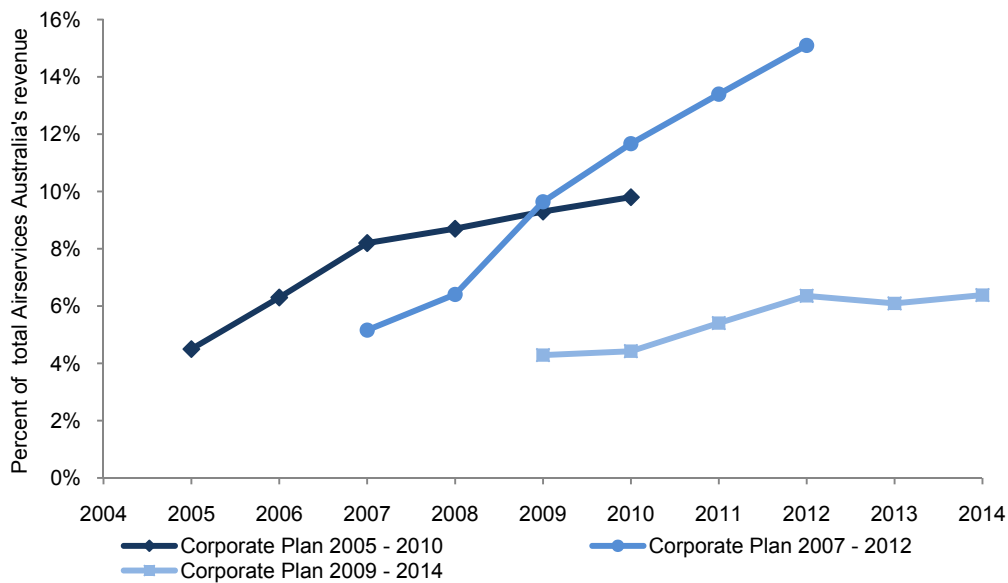
- projected other commercial revenues are expected to decrease by over eight per cent of total revenues (or \$73.95 million) in 2012 between Airservices Australia's Corporate Plan 2007–2012 and Corporate Plan 2009–2014 based on Airservices Australia's new strategic direction; and
- the five year other commercial revenue compound annual growth rate is expected to decrease by over 16 per cent (from 24 per cent to eight per cent) between Airservices Australia's Corporate Plan 2007–2012 and Corporate Plan 2009–2014.

²⁸ Airservices Australia, *Corporate Plan 2008 – 2013*, p. 6.

²⁹ *National Aviation Policy Green Paper*, pp. 62-63.

Figure 2.1

Projected other commercial revenue as identified in Airservices Australia's corporate plans



Source: Airservices Australia's Corporate Plan July 2005-June 2010, Airservices Australia's Corporate Plan July 2007-2012 and Airservices Australia's draft Corporate Plan 2009-2014.

2.28 Together with the processes and controls discussed earlier in this chapter, the significant change in Airservices Australia's strategic direction reduces the risk that issues similar to those surrounding the Solomon Islands Government contracts will reoccur.

3. Contract development, management and administration

This chapter addresses Recommendations 2 and 3 of the 2006–07 Audit Report by examining the implementation of the recent changes to Airservices Australia's contract development and management procedures.

Background

3.1 As at April 2009, Airservices Australia was managing 35 international contracts³⁰, including the current contract. As discussed in Chapter 2, Airservices Australia changed its focus from pursuing new business opportunities earning other commercial revenue to focusing on core business activity. As a result, Airservices Australia has not developed or managed any new international contracts of a similar nature³¹ to the current contract since the 2006–07 Audit Report was tabled in Parliament on 18 October 2006.

3.2 In the 2006–07 Audit Report, it was noted that Airservices Australia had not undertaken the necessary preparatory work to develop its contract in accordance with Australian law and the Solomon Islands Constitution. That is, Airservices Australia had not established the nature of the relationship between itself and the Solomon Islands Government before the contract was originally signed. The nature of the relationship between the Solomon Islands Government and Airservices Australia involved a determination of whether it was:

- able to hold air navigation fee revenue in trust on behalf of the Solomon Islands Government as a trustee; or
- acting as a 'collection agent' for the Solomon Islands Government which carries with it a range of fiduciary duties and duty of care responsibilities.³²

³⁰ As at 7 April 2009.

³¹ That is, where Airservices Australia acts as a collection agent on behalf of another country.

³² In the 2006–07 Audit Report, ANAO found that, based on Airservices Australia's legal advice, Airservices Australia could not act as a trustee for Solomon Islands funds and that it was a collection agent for the Solomon Islands Government.

3.3 The 2006–07 Audit Report also found that, in developing the contract with the Solomon Islands Government, Airservices Australia had not undertaken the necessary preparatory work to determine whether its method of collecting and remitting air navigation fee revenue was consistent with the Solomon Islands Constitution and better practice. These findings resulted in the two recommendations set out in Table 3.1.

Table 3.1

ANAO Audit Report No.8 2006–07: Recommendations 2 and 3

ANAO Recommendation No.2

ANAO recommends that, prior to entering into future international business contracts, Airservices Australia clearly identify the nature of the relationship that is being established by the contract and any resulting fiduciary and other duties, and ensure its practices and procedures satisfy these requirements.

ANAO Recommendation No.3

ANAO recommends that, prior to entering into future contracts that involve it acting as the collection agent of other governments, Airservices Australia take the necessary steps to identify the requirements and/or conditions that need to be satisfied when collecting and remitting statutory revenue.

Source: ANAO Audit Report No.8 2006–07 pp. 63 and 83.

Changes to the Solomon Islands Government contract management framework

3.4 Amendments to the contract were made in 2004 and 2007 to address the nature of Airservices Australia’s relationship with the Solomon Islands Government regarding the management of upper airspace. These amendments were supported by legal advice.

3.5 In addition, changes to administrative practice, and the current contract (based on Airservices Australia’s and the Solomon Islands Government’s legal advice) have clarified and finalised issues regarding the collection and remittance of statutory revenue by Airservices Australia.

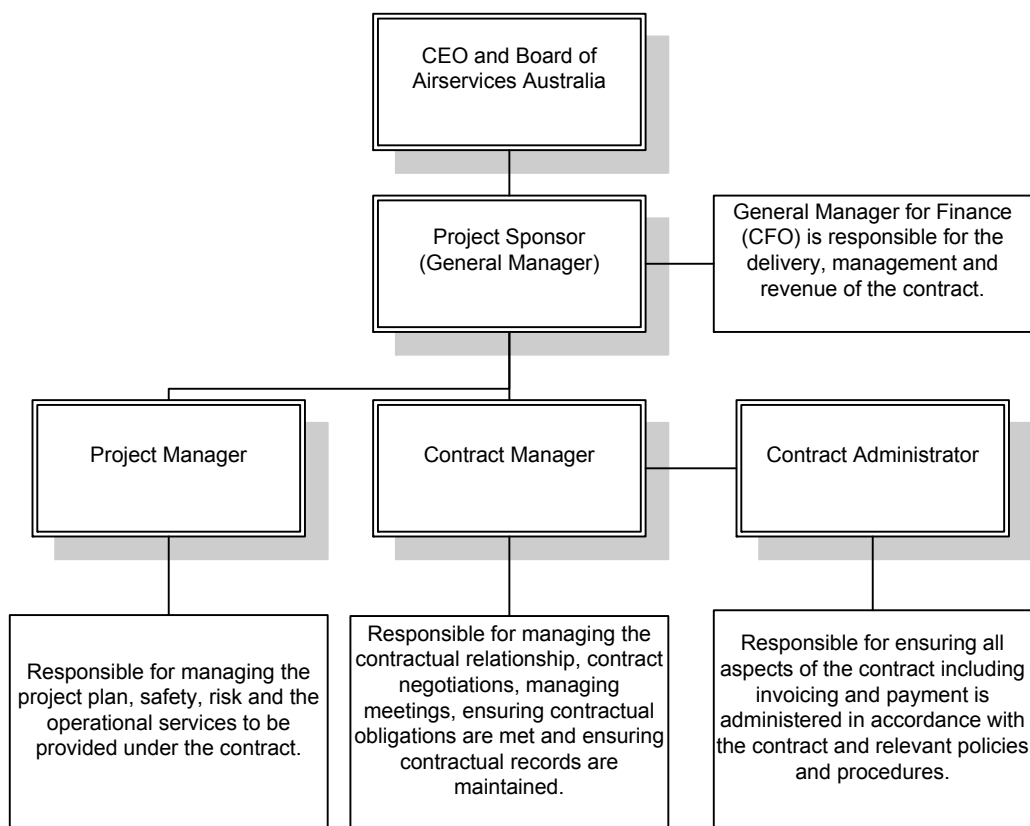
3.6 Airservices Australia has also made a number of changes to the governance of its international contracts since the 2006–07 Audit Report. Figure 3.1 details the responsibilities of the current key personnel assigned to manage the current contract. In this respect:

- the roles and responsibilities of key contract development and management staff have been clearly defined and documented;
- there are clear lines of accountability for each staff member;

- the Airservices Australia Executive has visibility of contracts either directly or through relevant committee processes; and
- there is improved coordination between the relevant areas of Airservices Australia. For example, Airservices Australia's Office of Legal Counsel, contract management and financial management.

Figure 3.1

Roles and responsibilities of key Airservices Australia personnel responsible for administering the Solomon Islands upper airspace contract



Source: Amended Airservices Australia Contract Management Plan for Solomon Islands Upper Airspace Contract.

Contract Development and Management (CDM) Guidelines

3.7 Airservices Australia's Contract Development and Management Guidelines (CDM Guidelines) were released by the Office of Legal Counsel on 19 May 2008.

3.8 As Airservices Australia has not entered into any upper airspace management contracts since the 2006–07 Audit Report, the ANAO was not able to assess how these guidelines have been applied in practice. However, the CDM Guidelines address aspects of Recommendations 2 and 3 of the 2006–07 Audit Report, and are consistent with better practice. Specifically, the CDM Guidelines address:

- establishing the nature of a contract (including fiduciary and other duties). This is covered through specific processes covering stakeholder consultation, risk identification³³ and specifying contract deliverables; and
- taking the necessary steps to identify the requirements that need to be satisfied when collecting and remitting statutory revenue. This is covered (at a high level) through processes covering stakeholder consultation.³⁴

3.9 The CDM Guidelines also reference additional internal and external documentation that should be considered when applying the guidelines. This additional documentation includes the 2006–07 Audit Report.

3.10 In 2008, Airservices Australia developed a Contract Management Plan for the Solomon Islands Upper Airspace Contract (Contract Management Plan). The Contract Management Plan has been developed in accordance with Airservices Australia's CDM Guidelines.

3.11 The Contract Management Plan is sound and addresses the major concerns raised in Recommendations 2 and 3 of the 2006–07 Audit Report. Namely, it:

- specifies precisely the nature of the relationship between the Solomon Islands Government and Airservices Australia;
- specifies the duties associated with collecting air navigation fee revenue on behalf of the Solomon Islands Government and remitting air navigation fee revenue to the Solomon Islands Government;

³³ The identification and assessment of contract risks are discussed further in paragraphs 3.16 to 3.21.

³⁴ Airservices Australia's approach to addressing this aspect of Recommendation 3 is discussed further at paragraphs 3.16 to 3.17

- specifies the responsibilities of the collection agent (Airservices Australia), namely duty of care and fiduciary duties; and
- identifies Airservices Australia's obligation to comply with the Solomon Islands Constitution.³⁵

3.12 However, the Contract Management Plan has not been signed and dated by an approved Airservices Australia delegate.

Contract reviews

3.13 Under its CDM Guidelines, Airservices Australia is required to develop a Contract Management Plan for all high risk or high value contracts during the planning phase of the contract. The Contract Management Plan was prepared in 2008 and is subject to review at least every six months during the term of the contract. Airservices Australia conducts monthly, quarterly, half-yearly and annual reviews of the Solomon Islands contract, as follows:

- **Monthly reviews**—conducted at a meeting with key personnel. Minutes and relevant action items are documented. A monthly report on the Solomon Islands contract is also presented at the monthly Airservices Australia Board meetings;
- **Quarterly and half-yearly reviews**—conducted in a similar manner to monthly reviews, but include a broader cross-section of internal stakeholders. ANAO noted that these meetings were additional to the monthly and annual reviews required under the contract; and
- **Annual contract review**—this review takes place with face-to-face discussions with stakeholders in Solomon Islands on issues such as contract amendments, including price increases and changes in legislative requirements.

3.14 The processes Airservices Australia has in place to review its current Solomon Islands Government contract and other contracts are generally sound. These processes provide assurance that issues identified with the contract will be discussed at the appropriate levels within Airservices Australia, and that

³⁵ Airservices Australia's compliance with section 100 of the Solomon Islands Constitution is specified in the Contract Management Plan. This section relates to the receipt of monies by the Solomon Islands Government.

there is a continuing dialogue regarding contract performance with the Solomon Islands Government.

3.15 Airservices Australia prepares a minuted record of all meetings and sends a copy of the annual review to the Solomon Islands Government. However, approval or endorsement of these meetings is not sought from the Solomon Islands Government. Better practice³⁶ prescribes that stakeholders should be involved on an ongoing basis through meetings and/or other forms of communication where minutes are taken and distributed amongst all parties for agreement. Obtaining confirmation of the minutes from all parties would provide added assurance that all parties are aware of current contract developments and have agreed on future actions that will occur.

Management instructions for international contracts

3.16 In July 2008, Airservices Australia released its International Management Instructions. These instructions:

- specify the roles and responsibilities of those individuals who are charged with administering contracts with international clients and stakeholders³⁷;
- identify the training requirements for all employees travelling overseas or who are otherwise involved in the administration or management of off-shore activities;
- identify the key contract management records that need to be maintained; and
- identify other key Airservices Australia policies and references relevant to the development and maintenance of international contracts. This includes a link to the 2006–07 Audit Report containing Recommendations 2 and 3.

3.17 The International Management Instructions provide additional contract management procedural information relevant to international contracts that were not available to staff who developed the original contract. This document goes some way to addressing the issue raised in Recommendation 3 of the

³⁶ See section 5.5 of the ANAO and Department of Finance and Administration Better Practice Guide on Developing and Managing Contracts.

³⁷ See Figure 3.1.

2006–07 Audit Report.³⁸ More specific instructions regarding the importance of obtaining a sound understanding of other countries' laws prior to entering into a commercial contract would improve the comprehensiveness of this document, and would provide additional assurance that Recommendation 3 has been fully implemented. Nevertheless, the attendant risks have been reduced by Airservices Australia's decreased strategic focus on pursuing these types of contracts.

Enterprise Risk Management Framework (ERMF)

3.18 An independent consultant's review of the Solomon Islands contract undertaken in August 2008³⁹ identified the need for Airservices Australia to develop a risk management plan based on a suitable risk management framework.⁴⁰ This review identified that:

An adequate risk management plan did not form part of the current Solomon Islands contract management plan....Given that the contract has already resulted in reputational impact for Airservices Australia, a risk management plan needs to be developed urgently.

3.19 In December 2008, following this review, Airservices Australia released a revised Enterprise Risk Management Framework (ERMF) to strengthen its risk management approach. This document articulates the approach for identifying, assessing and monitoring risks facing Airservices Australia. Under the ERMF, formal risk assessments must be completed for all contracts where:

- expenditure is more than \$50 000;
- the transaction could have an adverse impact on the operational systems;
- the transaction could have an adverse impact on safety;
- the transaction could have an adverse impact on the environment; or

³⁸ This recommendation was made with reference to Airservices Australia obtaining an adequate understanding of the Constitution of the Solomon Islands regarding the collection and remittance of statutory revenue.

³⁹ See Chapter 1 of this report for further information on this review.

⁴⁰ The inadequate identification of risks was a key finding of the report of the external follow-up of the ANAO's recommendations of the Solomon Islands contract issued on 26 August 2007.

- the transaction could have an adverse impact on Airservices Australia's reputation.

3.20 As discussed in Chapter 2, Airservices Australia has not entered into new contracts similar to the current Solomon Islands Government contract. ANAO has therefore not been able to assess how the ERMF has been used in the development of a new contract. However, a risk assessment under the ERMF has been completed for the current contract. Specifically, during 2008, Airservices Australia developed a Risk Management Plan for the Management of the Upper Airspace Agreement for the Solomon Islands Government. However, this document:

- does not clearly identify the risks applicable to the contract;
- has a facility for, but does not clearly identify, controls or mitigation strategies for risks;
- does not address core elements of the ERMF, which require the following details for each risk strategy:
 - what is to be done;
 - who is responsible for its implementation; and
 - when it is expected to be completed; and
- has not been signed and dated by an approved delegate.

3.21 Accordingly, there would be benefit in Airservices Australia improving the rigour of the Contract Risk Management Plan, in the manner advocated by its recently revised ERMF.

4. Accounting for collections, payments and the receipt of management fees

This chapter examines the administration of air navigation fee revenue, which was a key issue that arose in the 2006–07 Audit Report. In this respect, the chapter includes the results of a reconciliation exercise conducted by ANAO in respect of the payments made by Airservices Australia and the receipt of its management fees between September 2006 and March 2009.

Background

4.1 The original and current contracts provide for air navigation fee revenue collected on behalf of the Solomon Islands Government by Airservices Australia to be paid to:

- the Solomon Islands Government bank account specified in the contract; and
- Airservices Australia for its management fees (as an ‘off-set’) under the upper airspace management contract, and fees under any other contracts with the Solomon Islands Government.

4.2 In the 2006–07 Audit Report, it was noted that Airservices Australia had made third party payments and credit card transactions that were not in accordance with the original or current contracts. In addition, Airservices Australia had not established an understanding of the Solomon Islands’ constitutional requirements governing the collection and remittance of air navigation fee revenue, and the manner in which Airservices Australia was paid for managing the upper airspace of the Honiara FIR. These findings resulted in recommendations relating to the collection and payment of air navigation fee revenue, and the receipt of its management fees (see Table 4.1).

Table 4.1

ANAO Audit Report No.8 2006–07: Recommendations No.3 and 4

ANAO Recommendation No.3

ANAO recommends that, prior to entering into future contracts that involve it acting as the collection agent of other governments, Airservices Australia take the necessary steps to identify the requirements and/or conditions that need to be satisfied when collecting and remitting statutory revenue.

ANAO Recommendation No.4

ANAO recommends that Airservices Australia consult with the Solomon Islands Government so as to ensure that the manner in which it is paid for managing the upper airspace in the Honiara FIR fully complies with the requirements of the Solomons Island Constitution.

Source: ANAO Audit Report No.8 2006–07 pp. 83 and 85.

The Solomon Island Government's constitutional requirements

4.3 To allow an external entity to collect its statutory revenue, the Solomon Islands Government amended the *Air Navigation (Air Traffic Control) Regulation of the Civil Aviation Act*. As a result of the amendments, Airservices Australia is authorised to collect air navigation fee revenue as a collection agent of the Solomon Islands Government.

4.4 The Solomon Islands Constitution⁴¹ requires that 'all revenues or other monies raised or received by or for the purposes of the Government be paid into and form one Consolidated Fund'.⁴² The only exceptions provided to this, which require a relevant law to be passed by the Solomon Islands Parliament, relate to:

⁴¹ The United Kingdom established a protectorate over the Solomon Islands in the 1890s. The Solomon Islands achieved self-government in 1976 and declared its independence two years later, with the Solomon Islands Constitution coming into effect on 7 July 1978.

⁴² The relevant provision is:

Consolidated Fund and Special Funds

100(1) All revenue or other monies raised or received by or for the purpose of the Government (not being revenues or other monies that are payable by or under any law into some other fund established for any specific purpose or that may, by or under any law, be retained by the authority that received them for the purpose of defraying the expenses of that authority) shall be paid into and form one Consolidated Fund.

100(2) Parliament may make provision for the establishment of Special Funds, which shall not form part of the Consolidated Fund.

100(3) The receipts, earning and accruals of Special Funds established under this section and the balance of such funds at the close of each financial year shall not be paid into the Consolidated Fund but shall be retained for the purposes of those funds.

- revenues or monies that may, by or under any law, be retained by the authority that received them for the purposes of defraying the expenses of that authority; or
- revenues or monies that are payable by, or under, a law into a Special Fund (separate from the Consolidated Fund) established by the Solomon Islands Parliament.

4.5 The 2006–07 Audit Report identified that the first exception could not apply to the collection of air navigation fee revenue collected by Airservices Australia given the nature of the contract. Moreover, the second exception did not apply until 31 October 2005. On this date, the Solomon Islands' *Civil Aviation (Amendment) Act 2005* (Civil Aviation Act) established the Aviation Special Fund, into which all air navigation fee revenues are paid. Until this date, all air navigation fee revenue collected by Airservices Australia on behalf of the Solomon Islands Government was required to have been paid into the Consolidated Fund.

4.6 Key features of the Aviation Special Fund include that:

- its primary source of revenue is air navigation fee revenue;
- monies from the Aviation Special Fund can only be expended for purposes directly related to civil aviation infrastructure and facilities in Solomon Islands;
- there is a separate bank account for the Aviation Special Fund; and
- the relevant Solomon Islands Government Permanent Secretary is charged with the control and management of the Aviation Special Fund.

4.7 In early 2007, Airservices Australia obtained legal advice confirming that it was legal to deposit air navigation fee revenue into the Aviation Special Fund.

Development of the 2007 contract amendment

4.8 In October 2006, Airservices Australia consulted with the Solomon Islands Government Accountant-General to address the issues raised in Recommendations 3 and 4 of the 2006–07 Audit Report. As part of these discussions, it was proposed that a resolution to the air navigation fee revenue collection and payment issues raised in 2006–07 Audit Report could be addressed through an amendment to the current contract. The proposed

amendment involved ensuring that the following complied with the Solomon Islands Constitution:

- Airservices Australia's remittance of air navigation fee revenue to the Solomon Islands Government; and
- the manner in which Airservices Australia is paid for managing the upper airspace of the Honiara FIR.

4.9 In developing the 2007 amendment, Airservices Australia identified a number of issues relating to the current contract's compliance with the Solomon Islands Constitution. These issues related to the:

- remittance of all the air navigation fee revenue to the Aviation Special Fund;
- establishment of an arrangement whereby Airservices Australia's management fees would be direct debited from an Australian bank account established by the Solomon Islands Government, to which Airservices Australia would deposit 100 per cent of all air navigation fee revenue collected from airlines passing through the upper airspace of the Honiara FIR; and
- any right to 'off-set' debts due to Airservices Australia from air navigation fee revenue payable to the Solomon Islands Government.

4.10 To obtain assurance that the proposed approach complied fully with the Solomon Islands Constitution, Airservices Australia sought external legal advice. Overall, this advice indicated that Airservices Australia and the Solomon Islands Government's existing administrative arrangements complied with the Solomon Islands Constitution.

4.11 The then Legal Draftsman for the Solomon Islands Attorney General's Department also sought to confirm the legality of the 2007 amendment regarding the remittance of air navigation fee revenue to the Solomon Islands Government and the off-set provision. In advice to Airservices Australia, the then Legal Draftsman noted that:

The provision relating to the withholding payment may cause some concern. In terms of section 100 of the Constitution, all revenue or other monies raised or received by or for the purposes of the Government must be paid into the Consolidated Fund, unless payable to some other fund established for any specific purpose. The funds collected under the Airservices Australia agreement in terms of the Civil Aviation (Amendment) Act, which created the

special funds are to be appropriated from the Consolidated Fund into the Aviation Special Fund. The question that may arise is as to whether Airservices Australia could withhold monies due to Solomon Islands revenue for certain services rendered.

It could be argued that this provision does not breach section 100 of Constitution, as the monies raised or received for the purposes of Government may be subject to certain legal or legitimate deductions being made, i.e. charges or fees payable as administration costs with collection of fees. The amount due or payable to the Government will, therefore, be the amount receivable subject to certain contractual liabilities.⁴³

4.12 Following both sets of legal advice, and input from the then DOTARS and the Solomon Islands Government, an amending agreement was entered into by Airservices Australia and the Solomon Islands Government on 3 August 2007. The agreement was signed by Airservices Australia's Chief Executive Officer and the Permanent Secretary of the Solomon Island's Ministry of Communication, Aviation and Meteorology.

The current Solomon Islands Government contract's compliance with the Solomon Islands Government Constitution

4.13 In addressing the current contract's compliance with the Solomon Islands Constitution, the 2007 amendment included specific representations and warranties, on a continuing basis, from the Solomon Islands Government that:

- the account specified in Schedule 5 of the 2007 amendment constitutes the, or part of the, Aviation Special Fund for the purposes of the Solomon Islands Constitution;
- by remitting air navigation fee revenue to the nominated account in the manner and time specified in the 2007 amendment, Airservices Australia is not breaching any legal or other obligations or requirements for the remittance of funds which exist under Solomon Islands Law;
- the right to withhold payment, contained in the 2007 amendment, will not breach any legal or other obligations or requirements which exist under Solomon Islands law; and

⁴³ Memorandum to the Director of Civil Aviation, 11 June 2007, p. 2.

- the right to deduct or off-set any payment or debt owed by the Solomon Islands Government to Airservices Australia from monies payable to the Solomon Islands Government, specified in the current contract, will not breach any legal or other obligations or requirements which exist under Solomon Islands law.

4.14 The 2007 amendment also incorporates the following clause to ensure compliance with the Civil Aviation Act:

Airservices will, for payment and other consideration required under the Agreement, collect the Charges from the Aircraft on behalf of the Solomon Islands Government and remit the Charges to the Aviation Special Fund Account specified at Schedule 5 in accordance with, and subject to, the Agreement.

4.15 Based on the external legal advice sought by Airservices Australia and Airservices Australia's consultation with the Solomon Islands Government's representatives, there is sufficient evidence that the 2007 amendment complies with the requirements of the Solomon Islands Constitution.

Airservices Australia's right to offset its management fees against revenue collected

4.16 In accordance with clause 3.1(a) of the current contract, the Solomon Islands Government must pay to Airservices Australia the Contract Price⁴⁴ in the manner and form provided for in the current contract in exchange for the provision of the agreed services⁴⁵.

4.17 Until the 2007 amendment, Airservices Australia was entitled to deduct its management fees from the air navigation fee revenue collected on behalf of the Solomon Islands Government prior to the remittance of such funds to the Solomon Islands Government. The 2006–07 Audit Report identified that Airservices Australia's ability to deduct its management fees may be contrary to section 100(1) of the Solomon Islands Constitution, which requires that all funds be remitted to the account specified in the contract.

⁴⁴ The amount of \$45 000 per month or as varied in accordance with clause 3.1(b) of the current contract. This amount increased to \$49 500 in June 2008 in accordance with clause 3.1(b) of the current contract.

⁴⁵ Services to be provided and performed by Airservices Australia pursuant to Schedule 1 of the current contract.

4.18 To clarify whether it was able to off-set its management fees in this way, Airservices Australia obtained legal advice from the Solomon Islands Attorney General's Department (see paragraph 4.11) and representations and warranties received from the Solomon Islands Government (see paragraph 4.13). This legal advice provided that Airservices Australia's ability to off-set its management fees will not breach any legal or other obligations or requirements which exist under Solomon Islands law.

Reconciliation of collections, payments and receipt of management fees

4.19 To assess Airservices Australia's compliance with the current contract, ANAO examined all financial transactions from 1 September 2006 to 31 March 2009⁴⁶ relating to the:

- collection of air navigation fee revenue by Airservices Australia;
- payment of air navigation fee revenue to the Solomon Islands Government; and
- receipt of management fees by Airservices Australia.

Collection of air navigation fee revenue

4.20 Under the contract, a key role for Airservices Australia is to collect air navigation fee revenue from aircraft/airlines that pass through the Honiara FIR upper airspace, and then remit this revenue to a designated Solomon Islands Government bank account in accordance with the contract. During the period examined by ANAO, Airservices Australia collected \$3 684 352 in flight charges.

4.21 The 2007 contract amendment required, amongst other things, that air navigation fee revenue be paid to the Aviation Special Fund no later than 60 days after the revenue had been collected. However, Airservices Australia

⁴⁶ This represents the time period following the 2006-07 ANAO Report up to 31 March 2009.

has adopted the practice of remitting air navigation fee revenue to Solomon Islands Government no later than 90 days after it has been collected.⁴⁷

Payment of air navigation fee revenue

4.22 During the period examined, a total of \$4 194 042 was paid from Airservices Australia's dedicated Solomon Islands bank account. This amount comprised:

- \$3 773 022 paid to the Solomon Islands Government's Aviation Special Fund in accordance with the current contract; and
- \$421 020 off-set by Airservices Australia to account for its management fees, also in accordance with the current contract.⁴⁸

4.23 These payments are in accordance with the contract. In addition, there was evidence of Airservices Australia declining to make payments that did not accord with the written contract such that, during the period between 1 September 2006 and 31 March 2009, there were no:

- payments made to any third parties; or
 - cash payments or credit card transactions processed.
-

Ian McPhee
Auditor-General

Canberra ACT
5 November 2009

⁴⁷ In correspondence sent to the Solomon Islands Government on 10 May 2007, Airservices Australia had proposed to remit air navigation fee revenue no later than 90 days after collection for the relevant month. Although this proposal was intended to be captured in the 2007 amendment, it was not included. This was an administrative oversight by Airservices Australia. As a result, Airservices Australia remains required under the current contract to remit air navigation fee revenue to the Solomon Islands Government's Aviation Special Fund no later than 60 days after the charges have been collected for the relevant month.

⁴⁸ During the period examined, the Solomon Islands Government directly paid 57 per cent (\$827 480) of total management fees invoiced by Airservices Australia. Airservices Australia off-set 29 per cent (\$421 020) of its fees against the revenue it collected (in accordance with the current contract). Airservices Australia advised ANAO that the outstanding balance of 14 per cent (\$202 000) as at 31 March 2009 was subsequently off-set in May and June 2009.

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