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Public Sector Governance Conference

Different Perspectives of Public Sector Governance
Asia and Australia

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Background

The Australian Government public sector is in the midst of a very interesting period:

- the significant expansion of government outlays to respond to global economic events;
- a new approach to federalism to improve the way the Federal and State Governments interact;
- a move to more centralisation after many years of devolution; and
- the prospect of further changes in the light of the recently announced reform of Australian Government administration to build “the world’s best public service.”

The public sector world is increasingly challenging, complex and interconnected, involving relations between government agencies, different levels of government, and the private sector and not-for-profit sector.

The rate of change is also noticeable, putting pressure on the management of the new measures as well as existing programs.

Public Sector Governance

In such an environment there is a premium on sound governance to oversight changes and ensure outcomes are delivered in accordance with expectations. We should continue to be eclectic in drawing from global experience in the public and private sectors, and to build on the successes and the lessons of the past.

Further we should actively lend support to those values that encourage an apolitical, performance orientated public service.

As complexity and challenges increase, the more important values and culture are to performance.

- I was interested to read an interview recently with Dr Saad Al-Barrak, the CEO of the Kuwait based Telco, Zain, who said that '(we) *conduct our business with values and principles as our only guide.'*[1]

Now, that will never happen in the public sector, but the message nevertheless should not be lost:

- as important as policies, procedures and controls are for sustained long term performance, there is a point where layers of rules can stifle performance;
- and it is a prudent investment for organisations to obtain leverage from values and culture; and it is empowering for staff to operate in such an environment.

Nevertheless, we understand government is different. James Molison, the 4th President of the USA (1809-17) commented on the nature of government, and why controls are important, in the following way:

> *"If men were angels no government would be necessary. If angels were to govern men, neither external nor internal controls on government would be necessary. In framing a government which is to be administered by men over men, the great difficulty lies in this: You must first enable the government to control the governed; and in the next place oblige it to control itself."*[2]

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[1] Tiefel John, An interview with Saad Al Barrak, McKinsey Quarterly, 2009, Number 3, p18.
[2] Madison, James, The Federalist No 51, *The Structure of the Government Must Furnish the Proper Checks and Balances between the Different Departments*, Independent Journal, Wednesday, February 6, 1788, cited in Milton Friedman.

Because we are not governed by angels, our system of government is based on a range of checks and balances, where governments are expected to act in accordance with wide considerations of public interest, be focused on the short-term and long-term wellbeing of the nation, and be accountable to the Parliament. Despite the recent focus on market failure, and its effects, most would agree that when it comes to expectations of government '*there is far less tolerance for government failure than tolerance for market failure.*'[3]

This is why sound governance arrangements are so important in the public sector.

- and in the last 10-15 years we have seen significant improvements in frameworks for public sector governance with the establishment of advisory boards, audit committees and improved scorekeeping and reporting regimes.

The issue in the public sector that we all need to focus on most is not so much the frameworks, but their effective implementation.

Audit coverage by the ANAO continues to highlight this, and that:

- program implementation can be a poor cousin to policy development in terms of having the involvement of the senior leadership group and the necessary horsepower (right people) to deliver the measure or program;
- risks to successful implementation increase if a project involves significant elements of integration or IT components;
- there is a tendency for initial estimates of cost and schedule for major projects to be optimistic and contingencies to be set too low;
- where departments have a key role in sensitive areas of public administration, such as assessing the merits of proposals as in grants administration or determining the need for a government advertising

[3] Funnell W, Jupe R & Andrew J, *In Government We Trust*, p14. Referred to in The Times, 30 August 2007, p33.

campaign, it is important to ensure arrangements in place are rigorous, and subject to periodic review; and

- SES officers have a key role in providing objective advice (including viable options) to ministers having regard to the APS values, and showing the way for less-senior staff.

I don’t think we in the public sector are any different to the private sector when it comes to implementation being the challenge in governance regimes, rather than the governance frameworks.

When the ASX released Revised Corporate Governance Principles and Recommendations in August 2007, a key change introduced was an emphasis on the disclosure of an entity’s <u>actual</u> practice when reporting on corporate governance (emphasis added). Entities are required to ‘disclose or provide a summary’ in the annual report of the practices or specific policies that govern the practices;

- it is no longer sufficient for a company to report it has certain practices in place.[4]

Also of interest here, the Walker Review[5] of corporate governance in UK banks and other financial industry entities (BOFI), observed that the principal deficiencies in BOFI boards related much more to patterns of behavior than to organisation.

[4] Elsing Luise, ASX review of governance reporting, *Keeping Good Companies*, Chartered Secretaries Australia, October 2009.
[5] Walker, Sir David, *A Review of Corporate Governance in UK Banks and Other Financial industry entities,* HM Treasury, 16 July 2009.

Sir David Walker observed the fact that similar financial institutions in essentially similar regulatory regimes weathered the market storm materially better than others as indicative of differing qualities and capabilities of governance as major contributory explanatory variables. He referred to the pressure sustained by BOFIs during this crisis as an *"over-reliance on an inappropriate business model; insufficient management and control processes; and defective diligence and judgement on acquisitions shortly before or during the crisis phase".*[6]

However, one potential framework issue raised by Walker concerned the need for enhanced governance of risk, and he has suggested that best practice in a bank or life assurance company is for the establishment of a board risk committee separate from the audit committee.[7]

- his argument is that in practice the audit committee has clear responsibility for oversight and reporting to the board on the financial accounts and adoption of appropriate accounting policies, internal control, compliance and other matters. This vital responsibility is essentially, though not exclusively, backward looking.

- closely related, but separate, responsibilities are the critically important oversight of current risk in real-time in the sense of approving and monitoring appropriate limits on exposures and concentrations; and determination by the board of its risk tolerance and risk appetite through the cycle in the context of future strategy. This is largely a forward-looking focus designed to address past failures in risk assessments by boards.

Walker's essential point is that a clear differentiation is needed in ensuring that appropriate and separate focus is given to backward and forward-looking risk

[6] Ibid, p28
[7] Ibid, p81.

factors. Further, in support of board-level risk governance, a BOFI board should be served by a Chief Risk Officer who should participate in the risk input and oversight process at the highest level and should have a status of total independence from individual business units.

The value of such a committee with a focus on current risk and future strategy for some public sector entities is well worth consideration. For departments, in particular, it would be best orientated to the risks and uncertainties in, and options for, delivering government outcomes that are the administrative responsibility of the portfolio;

- such an approach recognises earlier comments to the effect that the consequences of poor choices and poor program implementation in the public sector are severe, and deserve high level and focused consideration.

Mark Matthews[8] of the Australian National University makes the point that public sector decision making can appear cumbersome, risk averse and time consuming because the unintended consequences of getting it wrong are far too severe.

- he makes the point that it is dangerous to react to such criticism defensively; and
- the reality is that governments handle uncertainties and risks that markets can't cope with.

[8] Matthews, Mark, *Fostering creativity and innovation in cooperative federalism – the uncertainty and risk dimensions; Critical Reflections on Australian Public Policy* – selected essays. Edited by John Wanna. Grahame Cook, PSM, Director of Grahame Cook Consulting Pty Ltd and Mark Matthews are working with the ANAO in developing an Innovation Better Practice Guide, *Innovation in the Public Sector: Enabling Better Performance, Driving New Directions*.

So the message here is to set the organisational risk appetites to reflect the circumstances,

- and that public sector organisations need effective methods for evaluating uncertainty and risk; and
- in some circumstances, such as implementing an IT system or acquiring a major item of plant, our risks appetite might be comparable with the private sector, but in advising on, and implementing a new policy measure, greater caution is understandable (because of the consequences of misqueuing).

Conclusion

The rate of change in the public sector continues apace, most agencies have noticed the budgetary constraints, and there is a substantial reform agenda on the way.

Such an environment places a premium on the governance arrangements of public sector entities to manage the new priorities, existing programs, and the uncertainties required to be dealt with by government.

The work of the ANAO shows that, by and large, governance frameworks are suitable, but we can continue to learn from experience elsewhere;

- the forward-looking arrangements to focus on risk and uncertainty being a case in point.

However, it is implementing existing governance frameworks effectively that requires on-going emphasis. Key considerations to bear in mind include:

- the importance of 'tone at the top' and senior leadership oversight of key projects;
- the different skill sets required for policy development and implementation (while recognising the benefit of overlap between these main elements);
- the value of effective risk management and monitoring;
- the long term benefits of investing in the values and culture of the organisation; and
- the role of the SES in setting the standard.

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