Submission to Independent Review of the PGPA Act and Rule

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Overview

The objectives of the Independent Review of the *Public Governance, Performance and Accountability Act 2013* and Rule (the review) are to examine if the PGPA Act and Rule are achieving the objects of the PGPA Act, to identify options to enhance public sector productivity, governance and accountability and to consider the nature and extent of Department of Finance (Finance) support to Commonwealth entities (entities).

The review focuses on the need for good governance to improve risk management and public service outcomes overall, and considers improved governance drives enormous value for organisations. The review notes that:

> *.. The key to success is leadership. Leadership at all levels must be actively involved. Ministers, secretaries and all accountable authorities need to set the tone at the top. A values-led culture of transparency, trust and aligned purpose underpins, and is essential for driving sustained improvement in governance, performance and accountability… (p. 1 – Executive Summary)*

The review's 46 recommendations address a number of themes, but this submission only deals with the following recommendations:

- audit committees (Recommendations 4 – 8, 15 – 22)
- managing and engaging with risk (Recommendations 10 – 14)
- the Comcover Benchmarking survey Tool (Recommendation 39)
- Clarifying reporting requirements and reducing the reporting burden (Recommendations 23 to 28), and
- Finance support (Recommendation 38).

Overall, I agree with the review that good governance is tied to strong culture and the need to engage with risk, and that APS leaders must actually 'lead' on these issues. It also requires robust structural and behavioural norms which are consistently and transparently applied. I also agree with the intent of many of the recommendations addressing structural and system improvements, however too many recommendations rely on process driven solutions likely to increase the reporting and compliance burden and not deliver the cultural and behavioural changes required.

Improving governance and performance requires a sustained, dedicated and increased resource investment (time, people and money). This will not get any easier in a resource constrained APS where many remain to be convinced of either the merit of such an investment or that it is also their responsibility.

Audit Committees: Recommendations 4 – 8, 15 – 22.

Recommendations 4-8 to improve the skills, capability and focus of audit committees are welcome, as are the suggestions to support them with learning programs. A key element, as noted by the Joint Committee of Public Accounts and Audit (JCPAA), remains the need to set clear governance parameters – what is the committee's role, what are their powers, what outputs are expected from them (quality, timing and value), how do they interact with other committees and the Executive Board and who is accountable for the committee's outcomes and findings.

Recommendations 15 to 22 suggest increasing the independence of audit committees, increasing accountable authority and senior management involvement, broadening the skills and qualifications of audit committee members, regularly refreshing committee membership, ensuring regular briefing and training, and improving transparency of the audit committee's membership, attendance, remuneration and operations.

Audit committees do not tend to be exemplars of diversity, so widening the pool of potential audit committee candidates, consistent with the changes occurring in the private sector, is long overdue. Organisational capture and 'group think' are obvious risks in committees that are not regularly refreshed with 'new blood', with newer members likely to be more willing to ask difficult questions or seek more information when they are not satisfied with the information put before them.

The Prudential Inquiry into the Commonwealth Bank of Australia Final Report (John Laker AO, Jillian Broadbent AO and Graeme Samuel AC) (CBA Inquiry) also considered that continuity of membership can lead to other organisational risks. In the case of CBA committees and the Board, the lack of change, when combined with a collegiate style of senior management interaction, meant that the Board and various committees put too much faith in trusting their colleagues, and not enough on interrogating the material put before them.

Increasing senior management involvement is necessary to ensure the right 'tone from the top' and to clarify committee governance arrangements. This requires a greater commitment to improve the quality of information put before the committee and to build relationships with the chair and committee members which are robust enough to deal with the 'hard questions' that should be asked at committee meetings. Constructive and challenging committee discussion is critical.

Whether all committee members should be independent of not just the entity, but the APS, is an interesting suggestion. This recommendation is likely to be resisted by entities based on confidentiality concerns, that members may have little understanding of government or the entity's business drivers (and therefore add no value) and that it would significantly increase the reporting burden.

Rather than a zero-tolerance position, I suggest that one or two members of the committee could be employed by the entity (obviously not the Chair), and always on the basis that such members would be in the minority. This would enable a stronger link into the entity to facilitate movement of information and outcomes, improve organisational understanding of audit committee roles and functions, yet maintain the committee's independence.

Managing and engaging with risk: Recommendations 10 to 14

These recommendations represent an area of interest given my role in implementing the Commonwealth Risk Management Policy while managing Comcover between 2014 to 2016.

Relevant review findings were that the Commonwealth Risk Management Policy has improved government risk management practices, but the pace of reform is patchy across entities and/or too slow. Further, that the APS remains too risk averse.

Recommendations 10 to 14 suggest that Accountable Authorities should:

- do more to embed risk management into policies and programs, and incentivise officials to manage risk
- engage with ministers and other key stakeholders on risk appetite and risk management
- consider appointing a Chief Risk Officer, and
- consider establishing a separate risk committee or improving the risk review of existing audit committees.

While a greater focus on risk management is welcomed, I am not sure the real answer lies in enhancing existing risk processes or building new ones. Doing so could in fact be counterproductive and may maintain risk management inertia.

Almost inevitably, any review of government activity overemphasises the value of process. While the PGPA Act has been a valuable and important public sector governance reform, more process is not necessarily going to 'embed' improved risk management behaviour.

In relation to Recommendation 10, the types of processes suggested already exist – they are just not always adhered to. For example, Cabinet processes (including past templates for New Policy Proposals) have tried a variety of different and potentially worthy approaches to identify project/risk management in policy and program proposals. However, often this process is sometimes derailed by extraordinarily short timeframes, policy outcomes pushed through to meet external deadlines (i.e. Budget deadlines) or for a variety of other reasons.

The Royal Commission into the Home Insulation Program (HIP) is but one example of this. Reasons for the program going the way it tragically did included the ridiculously short timeframes to implement the final version of the scheme, which led to poor program design which incentivised market rorting and shoddy practices.

The policy/program process for developing the HIP did not lack for committees, departments, Deputy Secretaries, senior ministers, junior ministers, briefings, minutes, private sector risk managers, lawyers and other hangers-on. Many of the process boxes were ticked, but in the end, no-one wanted to own responsibility for the decisions taken (or not taken).

- For example, early on during this process, the risk of electrocution during installation was raised, based on similar risks eventualising in New Zealand. However, this risk was dismissed as the New Zealand program involved floor installation and not ceiling installation. Other risks, such as how to apply WHS regulations effectively to the flood of newly established insulation fitting businesses, were simply considered a state regulation problem and ignored.

Nor did process and committees assist the CBA, which also suffered from overly complex and bureaucratic decision making processes, unclear accountabilities and a lack of ownership of key risks at the Executive Committee level.

The suggestions that Accountable Authorities find ways to incentivise officials to become better risk managers and that they hold conversations with key stakeholders about risk appetite are both valuable and useful.

However, it would be even more useful if these activities are embraced right throughout the organisation and the chain of command. That not only ministers, but all officials, understand the organisation's risk appetite, and that ministers also understand the need for risk management processes to be hardwired into policy development and program management and not avoided.

In terms of how risk management could be improved at organisational level, key elements include the need to:

1. **Explain**, in the simplest terms possible, what the aim of the behaviour is, what is expected, why it is important and how people can achieve it
2. **Set up a relatively simple and useable framework**, preferably focused on principles, with supporting information and training to aid understanding for users
3. **Live it** – at every level of the organisation. Set an appetite for risk. Talk about it, disagree about it, challenge it, review it. Deal with the good and bad of it – reward/incentivise good behaviours and take very transparent steps about not so good ones. Become comfortable with the idea of risk and the reality it is always there.
4. **Make decisions**.
5. **Own those decisions**.

Risk is about making decisions. The legal concept of negligence includes the act of not making a decision, yet too often public servants somehow think that this is safer than making one. Risk is always there, whether you do something or not.

Making risk 'special' does little to break down the cultural silos around risk. Risk is a part of daily business, and should be treated as such, and discussed at branch meetings, division meetings etc, and form part of the agenda like everything else. Too often, the APS hides behind an endless cycle of risk process through Minutes/Briefs/Submissions/emails to avoid responsibility for policy development or program delivery. You do need a paper trail – but you don't need a paper super-highway with endless 'accountability toll booths'.

Give people real authority to make decisions, and real accountability for the consequences of those decisions. This enables 'buy-in', builds trust and incentivises staff to manage risk.

Risk discussions should also become more general to encourage a wider and more mature perspective on risk, not just for policies and programs, but for all phases of enterprise planning (corporate plans, business plans, annual reports, performance reports). The more risk is 'specialised' the more it becomes 'too difficult' to do.

Recommendation 11 deals with increased leadership on risk, risk appetite and the need for an improved dialogue with ministers and Parliament about risk management.

The review noted that:

> *The risk appetite of accountable authorities is strongly influenced by that of ministers and the Parliament. To effectively instil a more positive risk culture within entities, accountable authorities need support from their ministers, and the Parliament. Put another way, they need to be given some leeway to fail. However, there is no evidence the risk appetite of ministers, or the Parliament, has shifted in recent years…*
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> *…Entities' approach to risk could be enhanced if the Parliament acknowledged the complex environment in which government operates….*

This issue influences many interactions at senior levels of the APS. Heightened concerns about the risks of failure, how it will be reported and potential career impacts, are hardwired into the APS. This is not aided by the combative nature of politics and the 24/7 news cycle.

Changing this dynamic will require robust relationships and conversations between accountable authorities and ministers, a willingness 'to ride out' the media storm when it occurs, and an ability to maintain a focus on the 'big picture'.

There is no shortage of cross portfolio policies and programs requiring significant and complex interactions across entities, APS staff and external stakeholders. The fact of complexity is likely to already be acknowledged by Parliament. Part of the issue may lie in the limited information provided to Parliament, which feeds the suspicion that the APS is hiding something. What may be required is a more fulsome explanation to Parliament from ministers or the APS about how a policy or program was implemented and whether it is being adequately managed in meeting its publicly intended goals.

The CBA Inquiry noted that the complexity of some program risks across the CBA's business lines was used as an excuse for complacent behaviour in addressing those risks. Similar arguments can also be made across the APS. Clarifying responsibility and accountability, especially identifying a program owner, shifts the onus on to that person to not only deal with risk, but explain it to stakeholders, including Parliament.

In relation to Recommendations 12, 13 and 14, there is nothing intrinsically wrong with setting up specific committees to deal with risk issues or identifying a risk guru called the Chief Risk Officer (CRO). Such initiatives are useful signals of cultural change and identify risk as something that must be addressed. As the review noted, Professor Peter Shergold's 2015 report arising from the HIP (*Learning from failure*) also suggested that CROs be seriously considered.[1]

Around the time of the Shergold report, some Commonwealth agencies began to employ CROs. In my discussions with them at the time, some of them observed that businesses in line areas thought the role of the CRO was to own the risks of the line areas, and not to 'pass them on' to those undertaking the activity.

[1] Professor Peter Shergold AC, *Learning from Failure*, 12 August 2015 Chapter C pp. 36 – 44.

The CROs at the time were mostly SES already within the organisation, who were given a shiny new title, variable senior executive time and support, little or no training and very limited resources. Often, they had to undertake the CRO job as part of a suite of other corporate roles.

While well intentioned initial steps, it compares poorly with the expectations surrounding CFOs, where it is well understood that CFOs require specific training and skills to oversee the finances of organisations responsible for billions of dollars of public expenditure. The same mindset does not apply to CROs, or to risk management more generally.

Another concern with elevating consideration of risk to CROs or committees is that it moves risk further away from those who are actively dealing with the risk, stretching lines of communication and accountability.

Committees are often attended by busy senior people who do not have the time or capacity to dig down into the issues before them. Increasing senior management engagement on processes doesn't improve them per se. As stated above in relation to audit committees, unless the governance arrangements for risk committees (and CROs) are very clear about what their roles and responsibilities are, not only will it continue to waste time and effort, no-one will want to own the risk and it will difficult to identify actual responsibility.

Page 40 of the Shergold report noted that:

> *In organisations that have achieved positive risk cultures, individuals are expected to identify and respond to risks <u>in their own sphere of influence, rather than assuming that responsibility sits with senior managers or risk committees</u> (my emphasis). They know who to approach in their agency if they need help, they receive support to identify and treat risks as early as possible, and they know that when they identify problems their concerns will be appropriately addressed by management. Knowledge of risk needs is widely shared.*
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> *… The APS too often places exclusive responsibility for risk management too high up the bureaucracy, away from the people who may be best placed to identify and act on it. This unwittingly creates two problems: it overcrowds senior leaders' agendas; and it removes management of implementation risk from those who may be most informed about how to manage it.*

Similarly, in CBA's case, the committee and reporting processes meant that line areas passed risk issues further up the line rather than feeling responsible for them or empowered to deal with them.

The relationships, responsibilities and accountabilities of the respective audit and risk committees must be clearly set out and understood by committee members, the senior executive and across the organisation. As part of setting the 'tone from the top' senior leaders must embrace the importance of accountability and transparency in attending these committees and accept the consequences of failing to meet organisational and/or committee expectations.

While recommendations 4 to 8 and 15 to 22 identify a range of new requirements for audit committees, no similar recommendations have been made in relation to risk committees, even though they are equally applicable.

Risk maturity will not occur without an increased organisational investment to assist business areas to become risk owners. This requires time, effort and resources (i.e. ASL, training budgets, networking with other CROs, senior management support). The Shergold report (at page 42) suggested that the APS should adopt the private sector approach of spending around 1 per cent of resources on risk management activities. Whatever method is used to determine the 1%, it is unlikely that entities spend that much now.

The CBA Inquiry also highlighted CBA's failure to invest appropriately in risk management capability, and recommended that the CBA increase capacity, subject matter expertise, staffing and training.

You can't 'fake it till you make it' with risk management.

Comcover Benchmarking Survey Tool - Recommendation 39

Under the heading 'Technical and other matters', recommendation 39 suggests that Finance should review the interaction between the Commonwealth Risk Management Policy and the Comcover Benchmarking Survey Tool. This is a useful suggestion as the Survey Tool has an important role in triggering risk culture discussions within organisations.

The Survey Tool is a self-assessment tool, used for many years voluntarily by entities, and provides useful information about an entity's risk maturity. When the Commonwealth Risk Management Policy was implemented as part of the PGPA Act, the Survey Tool was substantially revised to reflect the Policy, providing a new baseline for measuring risk maturity. As part of those reforms, and to drive behavioural change in relation to risk management, the Survey Tool became a mandatory part of Comcover's insurance arrangements with entities.

An entity's engagement with the Survey Tool varies significantly, depending on their willingness to invest time and effort into the survey, to test risk issues with their line areas, and engage with senior management.

Often, as an organisation learns more about its risk practices, there is a realisation that more could and should be done to improve risk culture. Yet, if previous surveys have shown that the organisation has a high risk maturity (4 out of 5) there is sometimes a reluctance to accept this reality and suffer a drop in the ratings from a 4 to a 3. Put another way: "*What, we are getting worse at managing risk? But we are doing <u>more</u>*.." Risk maturity means accepting this and communicating this message to key stakeholders such as the minister, peers and staff.

Clarifying reporting requirements and reducing the reporting burden - Recommendations 23 to 28

These recommendations seek to clarify and simplify the reporting burden and provide a stronger line of sight between an entity's portfolio budget statements (PBS), corporate plans and annual reports, thereby further improving transparency and accountability.

While a worthy aim, doing so will require a significantly improved understanding and appreciation of the purpose of each document, their key stakeholders and owners, and how these documents interact with each other. Such knowledge usually falls within the rather narrow domain of ministers' offices, the ANAO, Finance department officers, CFO areas and budget teams in central and line agencies.

As a starting point, this cohort of stakeholders should have an agreed understanding of the purpose and content of these documents. This understanding should then be communicated across the APS, to small and large entities alike, so that those undertaking the work also understand the linkages and start tailoring their reporting and accountability to match public expectations.

Again, this requires investing time and effort in communicating between the various APS layers, from top to bottom. In the absence of such efforts, irrelevant data will continue to be painstakingly collected, passed up the line and inserted into reports based on a strongly held belief that this is what is needed for accountability, and corporate documentation like the PBS, corporate plans and annual reports will remain poorly understood and prone to minimalist compliance based box ticking.

Standardised corporate plans and other templates may assist some initial thinking around the structure of reports, provided they remain flexible and optional, rather than mandated. This should hopefully also avoid the perceived need to focus on content and presentation (e.g. the 'coffee table' corporate report) and instead deliver a concise, relevant report on activities and outcomes. Sometimes less is more, and sometimes transparency means that there is not much to report during one quarter or year, Budget or MYEFO.

Recommendation 26 proposes amending the PGPA Rule on corporate plans to require entities to outline how they will achieve their purpose(s) over four years, how they will coordinate with others and how key risks will be identified and managed.

If the review's goals include improving transparency and lessening the reporting burden on entities, then Recommendation 26 will achieve neither outcome. Further, it will lead to a proliferation of wishful thinking, crystal ball gazing and weasel words. Given that agencies are struggling with the current reporting framework, quadrupling the extent of reporting, guesswork and forward planning will not improve the quality of information provided in the public domain.

Recommendations 32 and 33 appear to be based on the premise that there is limited evidence that the PGPA Act has enhanced cooperation between Commonwealth entities, and that further, more formal, steps should be used by the Government and the Secretaries Board to improve cooperation. It is just not clear what the issue is and what is being recommended. Neither will it reduce the reporting burden.

An initial question is the basis for the assumption. Is there data or performance metrics supporting this view? Is it anecdotal, personal? I suspect the answer is no, given the option in Recommendation 33 to develop and report on whole of government performance information.

A deeper analysis of the incentives, drivers and rationale is required, rather than setting up another process involving more written priorities and objectives for leaders. Cooperation, particularly on complex issues, requires discussion, clarification, negotiation, acceptance of responsibility and accountability. This requires a change of culture, not process. As the review noted earlier, the key to improved culture is leadership.

Finance support – Recommendation 38

Finance has an important role in supporting and enhancing the resource management framework. The activities suggested, of communities of practice, one on one interactions with entities, providing up to date guidance material and increasing Finance's web presence, are all useful initiatives.

To support such activity, and consistent with my comments above, I suggest that all entities, including Finance, significantly increase their commitment and resourcing to improving public sector governance and transparency.