

# **Governance and Integrity of the Northern Australia Infrastructure Facility**

Northern Australia Infrastructure Facility

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Canberra ACT

10 April 2019

Dear Mr President

Dear Mr Speaker

In accordance with the authority contained in the *Auditor-General Act 1997*, I have undertaken an independent performance audit in the Northern Australia Infrastructure Facility. The report is titled *Governance and Integrity of the Northern Australia Infrastructure Facility*. 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 to the Parliament.

Following its presentation and receipt, the report will be placed on the Australian National Audit Office's website — <http://www.anao.gov.au>.

Yours sincerely



Grant Hehir  
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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# Summary and recommendations

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## Background

1. The Northern Australia Infrastructure Facility (NAIF) is a corporate Commonwealth entity under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), established from 1 July 2016 under the *Northern Australia Infrastructure Facility Act 2016* (NAIF Act).
2. The objective of the NAIF is ‘to provide grants of financial assistance to the States and Territories for the construction of Northern Australia economic infrastructure’, which is defined in the NAIF Act as infrastructure that provides a basis for economic growth in Northern Australia and stimulates population growth in Northern Australia.<sup>1</sup> It can include infrastructure located outside Northern Australia that satisfies the statutory definition. The NAIF Act provided for \$5 billion to be appropriated from the Consolidated Revenue Fund for this purpose. The NAIF Board has until 30 June 2021 to make decisions to provide financial assistance.

## Rationale for undertaking the audit

3. On 14 June 2017, the Senate referred an inquiry into the governance and operation of the NAIF to the Senate Economics References Committee, which tabled its Final Report on the results of the inquiry on 6 July 2018.<sup>2</sup> The Final Report stated that a significant number of submissions to the Committee related to a ‘proposal for NAIF funding to build a railway line from the Carmichael coal mine to the Abbot Point port’.<sup>3</sup> The report included 12 recommendations covering:
  - governance changes with the addition of a second responsible minister, structured engagement with the Clean Energy Finance Corporation, publication of Indigenous Engagement Strategies and Indigenous representation on the Board;
  - publication of conflicts of interest, publication of more detail about investment decisions, prioritisation of projects with high local content, and allocating funds to the tourism industry; and
  - a review of NAIF transparency, a more transparent transaction pipeline, more resources in Darwin, and more transparency in senior staff remuneration.
4. The NAIF Act provides for a statutory review of the operation of the Act to be undertaken as soon as possible after the period of three years beginning when the Act commenced (as soon as possible after 1 July 2019). The statutory review must consider whether the time limit of 30 June 2021 for making decisions should be extended, and the appropriate governance arrangements after that date.<sup>4</sup>

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1 *Northern Australia Infrastructure Facility Act 2016*, section 3.

2 Senate Economics References Committee, *Governance and operations of the Northern Australia Infrastructure Facility (NAIF)*, Canberra, 6 July 2018, available from [www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Economics/NAIF/Final\\_Report](http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/NAIF/Final_Report) [accessed 9 November 2018]. The report included a minority report by Government members. The NAIF made a submission to the Senate Inquiry (available as submission 43).

3 *Ibid*, paragraphs 1.5 and 1.6.

4 *Northern Australia Infrastructure Facility Act 2016*, section 43.

## **Audit objective and criteria**

5. The objective of the audit was to examine the effectiveness of governance and integrity arrangements for the NAIF.
6. To form a conclusion against the audit objective, the ANAO adopted the audit criteria:
  - Does the NAIF have in place a sound governance framework that is fit-for-purpose?
  - Has the NAIF implemented arrangements that support effective integrity and transparency in relation to its operations?
7. The audit scope did not address the merits of Northern Australia infrastructure policy, ministerial appointments to the Board, or particular decisions to grant financial assistance.

## **Conclusions**

8. The NAIF's arrangements to support the integrity of decision making were not fully effective. While NAIF has established appropriate governance and policy frameworks, decision support processes were not sufficiently transparent or evidenced to demonstrate projects have been treated in a consistent manner.
9. The NAIF has an appropriate governance framework, including systems of risk management and internal control, and effective arrangements with the Export Finance and Insurance Corporation (Efic) as its key service provider. Appropriate oversight is provided to the Minister for Resources and Northern Australia through reporting and regular meetings. While the Board adopted a flexible approach to strategy, only a small number of projects were assessed as addressing an identified infrastructure need, and amendments to the Investment Mandate changed the scale and scope of projects that the NAIF Board was considering beyond its original purpose. Remuneration policies and practices were not consistent with public sector governance standards, and information governance requires attention to meet National Archives standards and improve transparency.
10. The NAIF did not implement effective arrangements to support integrity and transparency throughout all elements of its operations. The NAIF had an appropriate integrity policy framework and the management of conflicts of interest was effective, however the NAIF adopted but did not adequately implement the Protective Security Policy Framework. Arrangements for engaging with stakeholders were generally effective. Arrangements for ensuring the integrity of decision support processes were not effective, with insufficient evidence that all applicants were evaluated in a consistent manner throughout the assessment stages. The Board placed reliance on the CEO to present projects for Board consideration, and the Board has not made any Investment Decisions to refuse financial assistance for the applications presented.

## **Supporting findings**

### **Governance**

11. The NAIF's governance framework is in accordance with relevant legislative and policy requirements. The NAIF has an appropriate statutory framework, Board processes and suite of governance policies. The NAIF provides the Minister for Resources and Northern Australia with oversight of its governance and decision-making through transaction pipeline reports and weekly



meetings with the Minister's office, but did not keep minutes of these meetings. The NAIF Board has oversight of the Chief Executive Officer and staff, however remuneration policies and practices were not consistent with public sector governance standards.

12. While NAIF origination strategies promoted the achievement of its purpose: NAIF facilitated origination has not generated a significant or sustained increase in either the annual number of new projects or the annual number of successful applications; and only a small number of projects considered by the NAIF Board were assessed as addressing an infrastructure need identified through a Commonwealth, State or Territory assessment process, pipeline, or priority list. The eligibility criteria for financial assistance were substantially broadened in order to increase the number of Investment Decisions.

13. The NAIF has developed an appropriate system of risk oversight and management that is consistent with the requirements of the *Commonwealth Risk Management Policy* and relevant Australian Prudential Regulation Authority (APRA) and Australian Stock Exchange (ASX) governance standards.

14. The NAIF has developed a system of internal control which is appropriate for its requirements. The NAIF Board adopted a blended system that relied primarily on service providers' policies and practices to provide coverage broadly equivalent to the *model accountable authority instructions*. The blended system has an inherent risk of insufficient clarity in relevant roles and responsibilities which should be monitored.

15. The Service Agreement and preceding inter-entity arrangement between the department and Efic were effective in supporting the establishment and operation of the NAIF, and had benefits for Efic in relation to demand management and the development of staff capability. Aspects of the NAIF's contract management of the Service Agreement could be improved to ensure ongoing value for money is maintained and evidenced.

16. The NAIF's information governance requires improvement to meet National Archives of Australia standards. The NAIF has implemented Freedom of Information and Information Publication Scheme processes. The NAIF published information about decisions to grant financial assistance as required by the Investment Mandate, but did not publish information about decisions not to grant financial assistance. The NAIF did not always disclose assessment criteria and processes, or non-confidential information about decisions.

## **Integrity and transparency**

17. The NAIF had an appropriate integrity policy framework. The integrity compliance program was largely reliant on induction training and self-reporting, which could be supplemented by ongoing training, pro-active compliance reviews and internal audit coverage.

18. The management of conflicts of interest was effective. The NAIF Board approved a conflicts of interest policy that applied to Board members and staff. The NAIF Board implemented sound declaration practices at Board meetings, and sound recusal practices at Board meetings and in Board papers. Declarations were more likely to be made after conflict checks were conducted or when an application reached the due diligence stage, indicating that there would be value in conducting conflict checks for all proposals from the earliest stage.

19. The NAIF adopted but did not adequately implement the Protective Security Policy Framework. The NAIF relied on service providers' security risk management policies and practices, and more recently approved policies specific to its own circumstances in areas such as business continuity. The NAIF did not use security classification and dissemination limiting markers on official documents. Some NAIF Board members used non-official email accounts to conduct official business and make decisions on projects with commercial and political sensitivities.

20. The NAIF implemented arrangements for engaging with stakeholders which were generally effective. The Board exercised regular oversight of stakeholder engagement. While the NAIF conducted regular consultation with government stakeholders with assistance from the department, providing more complete information to these stakeholders would help to identify and manage shared risks. The NAIF has draft bilateral protocols for statutory consultation with State and Territory jurisdictions under the Master Facility Agreements, and with Infrastructure Australia.

21. The arrangements for ensuring the integrity of decision support processes were not effective. The NAIF Board placed reliance on the CEO to determine whether a project progressed to the strategic assessment stage in circumstances where it is unclear why certain projects were presented to the Board and not others, and the Board has not made any Investment Decisions to refuse financial assistance for the applications presented to it. There was insufficient evidence that all projects were evaluated in a consistent manner throughout the assessment stages, and the NAIF sent letters of support or term sheets before applicants provided appropriate supporting documentation. There was no apparent consistency in how site visits were planned, conducted, documented or reported to the NAIF Board.

22. The NAIF Board met minimum external reporting obligations, but did not set measures that provided clear accountability and transparency in relation to its performance, did not measure the realisation of public benefit, and did not meet key performance targets in 2017–18.

## Recommendations

**Recommendation no.1** The NAIF publish criteria and all information necessary for applicants to submit complete applications for grants of financial assistance.

**Paragraph 2.34**

**The Northern Australia Infrastructure Facility response:** *Agree.*

**Recommendation no.2** The NAIF develop an information governance framework, electronic data and records management system, and appropriate records disposal authorities in line with National Archives of Australia requirements.

**Paragraph 2.72**

**The Northern Australia Infrastructure Facility response:** *Agree.*

**Recommendation no.3** The NAIF publish more information about decisions, public benefit assessments, environmental assessments and Indigenous engagement strategies.

**Paragraph 2.79**

**The Northern Australia Infrastructure Facility response:** *Agree.*

**Recommendation no.4** The NAIF cease the use of all non-official email accounts and servers to conduct official business.

**Paragraph 3.24**

**The Northern Australia Infrastructure Facility response:** *Agree.*

**Recommendation no.5** The NAIF select projects at each assessment stage on a consistent and transparent basis in accordance with published criteria, and retain adequate documentation to record the rationale for decisions made and actions undertaken.

**Paragraph 3.60**

**The Northern Australia Infrastructure Facility response:** *Agree in principle.*

**Recommendation no.6** The NAIF revise its performance measures and targets to provide clearer accountability and transparency in the measurement of its performance, and measure and report on the realisation of public benefit.

**Paragraph 3.70**

**The Northern Australia Infrastructure Facility response:** *Agree.*

## Entity response

23. The proposed audit report was provided to the Northern Australia Infrastructure Facility. The full response, including ANAO rejoinders to that response, are reproduced at Appendix 1. The summary response is reproduced below.

NAIF agrees to ANAO Recommendations 1-4 and 6 agrees in principle to Recommendation 5. NAIF's full response is at Appendix 1 and in responses to those Recommendations provided in the report.

NAIF agrees with the ANAO that principles of accountability and transparency are essential to maintaining public confidence in the quality of public administration.

NAIF disagrees with the ANAO finding that NAIF's arrangements to support the integrity of NAIF decision making were not fully effective in terms of either transparency or evidence of consistent treatment of projects.

NAIF's decision making criteria are transparent being comprehensively set out in a list of five mandatory criterion and at least 27 requirements in the NAIF Act and Investment Mandate that the Board must consider in making an Investment Decision.

NAIF publishes information, at all times balancing transparency with its best practice statutory obligations to maintain commercial in confidence information, in order to deliver on its mandate.

Documentary evidence exists for all NAIF decisions to progress projects through NAIF's various stages. NAIF does not accept that the examples provided at paragraphs 3.45–3.51 are evidence of a lack of clarity as to why particular projects were presented to the Board and not others.

The NAIF process has been designed to deliver on its objective of accelerating infrastructure development. It involves a test (applied at the strategic assessment stage) requiring that a project demonstrates potential to meet all criteria. There is a separate test which requires the NAIF CEO to have formed a view that a project if it were presented to the Board, the Board would be likely to exercise its discretion to decline an Investment Proposal.

NAIF also disputes the ANAO's statements at paragraph 3.50. There were no instances where a project that did not have the potential to meet the criteria was recommended to be moved to due diligence.

All decisions have been made against consistent and correct criteria. NAIF accepts and has acted to ensure there is more consistency in documentation by different executives for the strategic assessment stage (in being clear the analysis at that stage relates to a potential to meet criteria). A lack of decisions by the NAIF Board to refuse financial assistance for the applications presented to it is also not reflective of any issue with NAIF's process.

The ANAO analysis (at paragraphs 3.40-3.41) focussing on the time projects are in the NAIF system is not evidence of any inconsistency or lack of integrity of NAIF's decision making process and is not determinative of an outcome. As a result of both the unique project and proponent characteristics and the overlay of commercial judgement, projects progress at different rates which creates variability in timing to progress. That is not evidence of a lack of consistency of approach or process. NAIF applies the same process consistently to the differing parameters of each project to assess against the NAIF requirements.

ANAO (at paragraph 3.42) asserts that NAIF should ensure it makes a decision to grant or refuse all projects expeditiously and to a 30 June 2021 deadline. NAIF's response is that projects may not be ready to be managed by NAIF to such an outcome. NAIF is actively seeking to progress projects quickly where feasible but it does not discount any opportunity peremptorily and it does not control project timelines.

24. The Department of Industry, Innovation and Science (the department) was provided with extracts of the report containing those sections where the department was specifically mentioned. The department did not provide comment.

## Key messages from this audit

### Accountability and transparency

Principles of accountability and transparency are essential to maintaining public confidence in the quality of public administration. The Australian Parliament and the Australian Government give these principles specific expression in legislative and policy standards that apply to the powers, functions and duties of public sector bodies, including corporate Commonwealth entities such as the Northern Australia Infrastructure Facility (NAIF).

This audit concluded that the NAIF's arrangements to support the integrity of decision making were not fully effective. While the NAIF established appropriate governance and policy frameworks, decision support processes were not sufficiently transparent or evidenced to demonstrate that projects had been treated in a consistent manner.

It is concerning that the NAIF's response reflects a view that these findings are unjustified on the basis that they fail to consider the application of 'expert commercial judgement' in the decision making process.

The general duty imposed on officials in all Commonwealth entities to act honestly, in good faith and for a proper purpose<sup>5</sup> necessitates the demonstration of matters taken into consideration in arriving at a decision. While the use of expert judgement may be appropriate, this does not reduce the expectation that the use of this judgement is transparent and clearly documented. This audit found insufficient evidence of the specific circumstances considered in moving some projects forward in the decision making process in preference to other projects — whether these considerations took the form of expert judgement or otherwise.

The accountable authority of a Commonwealth entity must govern the entity in a way which demonstrates to the Parliament, and the Australian Public, that it is promoting the proper use and management of public resources.<sup>6</sup> It is incumbent on the NAIF Board, which has responsibilities with respect to the allocation of \$5 billion of public funds, to understand its accountabilities and responsibilities in this regard.

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5 *Public Governance, Performance and Accountability Act 2013*, section 26.

6 *Public Governance, Performance and Accountability Act 2013*, section 15.



## **Audit findings**

# 1. Background

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## Introduction

1.1 The Australian Government has established a policy focus on developing Northern Australia — comprising the Northern Territory and those parts of Western Australia and Queensland above the Tropic of Capricorn.<sup>7</sup>

1.2 In June 2014, the Department of the Prime Minister and Cabinet released the *Green Paper on Developing Northern Australia*.<sup>8</sup> Inviting comment for the development of a White Paper, it proposed six broad policy directions for Northern Australia: infrastructure; land; water; business, trade and investment; education, research and innovation; and governance.

1.3 On 4 September 2014, the Joint Parliamentary Select Committee on Northern Australia tabled the *Pivot North* report.<sup>9</sup> The report included 14 recommendations on the provision of new or existing infrastructure in Northern Australia, and the establishment of a rural investment fund to provide opportunities for investors to participate in rural infrastructure development projects.

1.4 In January 2015, Infrastructure Australia<sup>10</sup> released the *Northern Australia Audit — Infrastructure for a Developing North* report. The report assessed critical gaps in Northern Australian economic infrastructure — the transport (airports, ports, rail and road), energy (generation and transmission), water and communications sectors. The report concluded that processes and policy frameworks for the evaluation of major projects need to improve to avoid unwanted or stranded infrastructure investment; there may be merit in considering multi-user investment with some social amenity; Government investment should only proceed where there is a clearly defined value to the taxpayer; and strengthened infrastructure network planning and coordination merits consideration.<sup>11</sup>

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7 This definition of ‘Northern Australia’ comes from the Australian Government, *Our North, Our Future: White Paper on Developing Northern Australia*, Canberra, June 2015. Section 5 of the *Northern Australia Infrastructure Facility Act 2016* contains a more precise definition of the term ‘Northern Australia’ specific to that Act.

8 Department of the Prime Minister and Cabinet, *Green Paper on Developing Northern Australia*, Canberra, June 2014.

9 Joint Select Committee on Northern Australia, *Pivot North — Inquiry into the Development of Northern Australia Final Report*, Australian Parliament, Canberra, 4 September 2014, available from [www.aph.gov.au/Parliamentary\\_Business/Committees/Joint/Former\\_Committees/Northern\\_Australia/Inquiry\\_into\\_the\\_Development\\_of\\_Northern\\_Australia/Tabled\\_Reports](http://www.aph.gov.au/Parliamentary_Business/Committees/Joint/Former_Committees/Northern_Australia/Inquiry_into_the_Development_of_Northern_Australia/Tabled_Reports) [accessed 9 November 2018].

10 Infrastructure Australia is an independent statutory body with a mandate to prioritise and progress nationally significant infrastructure. It was established in July 2008 to provide advice to the Australian Government under the *Infrastructure Australia Act 2008*.

11 Infrastructure Australia, *Northern Australia Audit — Infrastructure for a Developing North Report*, Canberra, January 2015, available from <http://infrastructureaustralia.gov.au/policy-publications/publications/Northern-Australia-Infrastructure-Audit.aspx> [accessed 9 November 2018]. The report’s conclusions are at pages 4–5.



1.5 On 12 May 2015, the Australian Government announced the establishment of the Northern Australia Infrastructure Facility (NAIF) under the Department of the Treasury, stating that ‘the loan facility will be open for applications from 1 July 2015’.<sup>12</sup>

1.6 This was followed in June 2015 by the release of the *Our North, Our Future: White Paper on Developing Northern Australia*.<sup>13</sup> In line with the preceding Green Paper, the White Paper contained a range of measures including ‘infrastructure to support growth’ and outlined the Government’s infrastructure investment strategy. It provided further detail on the NAIF, linking it to the Northern Australia infrastructure projects pipeline with the statement that ‘projects wanting funding from the Northern Australia Infrastructure Facility will benefit from being on the pipeline’.<sup>14</sup> In October 2015, the Treasury informed the Senate that Treasury officials had met with ‘over 100 individuals across 40 or so different companies’.<sup>15</sup>

1.7 Following machinery of government changes on 30 September 2015, responsibility for the NAIF moved to the Minister for Resources, Energy and Northern Australia<sup>16</sup>, and the Government commenced consultation on draft legislation to establish the NAIF as a separate entity.<sup>17</sup> The Minister stated in the second reading speech on 17 March 2016 that over 200 stakeholders were consulted on the bill and ‘through the consultation process, 40 projects with an indicative capital value of \$21 billion have been identified as potential NAIF projects...around half have been identified in Infrastructure Australia’s *Northern Australia audit*’.<sup>18</sup>

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12 Australian Government, ‘Developing Northern Australia—Northern Australia Infrastructure Facility’, *Budget Measures 2015–16—Part 2: Expense Measures*, Canberra, 12 May 2015, page 174.

13 Department of the Prime Minister and Cabinet, *Our North, Our Future: White Paper on Developing Northern Australia*, Canberra, June 2015, available from [www.industry.gov.au/strategies-for-the-future/northern-australia-agenda](http://www.industry.gov.au/strategies-for-the-future/northern-australia-agenda) [accessed 9 November 2018].

14 White Paper, page 9. The pipeline was established under the Department of Infrastructure and Regional Development: Australian Government, ‘Developing Northern Australia—northern Australia infrastructure projects pipeline’, *Budget Measures 2015–16—Part 2: Expense Measures*, Canberra, 12 May 2015, page 134.

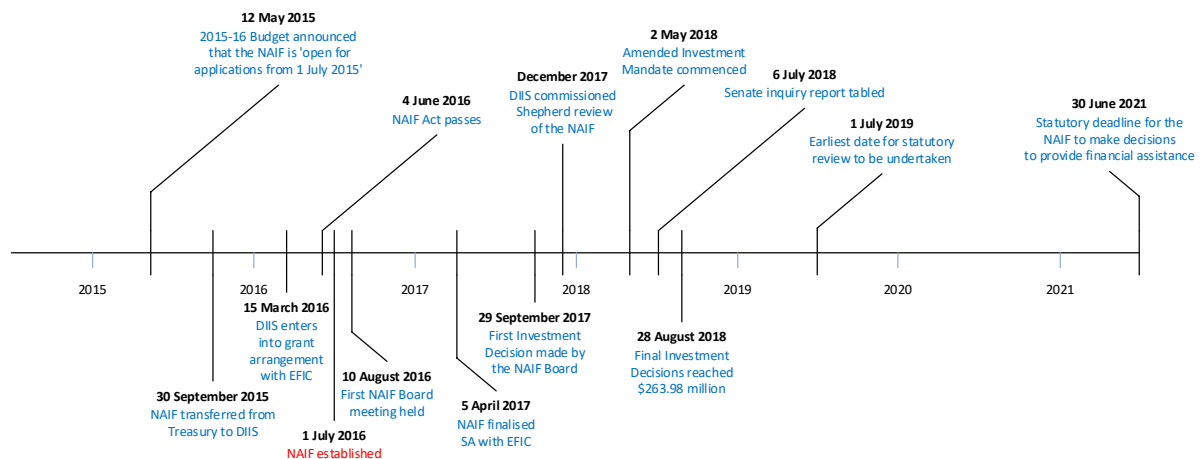
15 Senate Economics Legislation Committee, *Official Committee Hansard*, 21 October 2015, pages 124–126.

16 Senate Economics Legislation Committee, *Official Committee Hansard*, 21 October 2015, page 121; reflected in *Administrative Arrangements Order—30/9/2015*, C2016Q00008; Part 13. Departmental responsibility also moved from the Department of the Treasury to the Department of Industry, Innovation and Science.

17 The consultation process included a paper to seek feedback on the proposed design and operation of the NAIF released on 9 November 2015, exposure draft legislation on 28 January 2016, and a draft Investment Mandate on 17 March 2016. The Northern Australia Infrastructure Facility Bill 2016 was introduced into the House of Representatives on 17 March 2016, the Senate on 19 April 2016, and passed both Houses on 3 May 2016. On 17 March 2016, the Bill was referred to the Joint Select Committee on Northern Australia, which reported on 14 April 2016.

18 House of Representatives, *Official Hansard No. 5, 2016*, 17 March 2016, page 3443.

**Figure 1.1: NAIF timeline**



Source: ANAO analysis.

## The Northern Australia Infrastructure Facility

### Structure and governance

1.8 The NAIF is a corporate Commonwealth entity under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), established from 1 July 2016 under the *Northern Australia Infrastructure Facility Act 2016* (NAIF Act) with a Chair, a Board and a Chief Executive Officer (CEO).<sup>19</sup>

1.9 The NAIF Board is responsible to the Minister for Resources and Northern Australia (the Minister), who is advised by the Office of Northern Australia within the Department of Industry, Innovation and Science (the department).<sup>20</sup> The Minister appoints and provides direction to the NAIF Board, the NAIF Board appoints and provides direction to the CEO, and the CEO engages and provides direction to staff as required.<sup>21</sup>

1.10 The Minister provides statutory direction to the NAIF through an Investment Mandate.<sup>22</sup> The purpose of the Investment Mandate is to direct the NAIF in relation to the performance of the functions of the NAIF as set out in section 10 of the NAIF Act. The Investment Mandate requires that the NAIF must have regard to Australian best practice government governance principles, and

19 The *Northern Australia Infrastructure Facility Act 2016* (C2016A00041) received royal assent on 4 May 2016 and commenced on 1 July 2016. Board members were appointed on 19 July 2016, an interim CEO in July and an ongoing CEO on 24 October 2016.

20 *Administrative Arrangements Order*, 19 April 2018, C2018Q00017; Part 12.

21 *Northern Australia Infrastructure Facility Act 2016*, sections 15, 29, 30, 38 and 39.

22 The *Northern Australia Infrastructure Facility Investment Mandate Direction 2018* commenced on 2 May 2018, repealing the Investment Mandate made on 4 May 2016. The Investment Mandate is a non-disallowable legislative instrument and is exempt from sunset.

Australian best practice corporate governance for Commercial Financiers, when performing its functions.<sup>23</sup>

1.11 As at 3 December 2018, the NAIF directly employed 25.6 full-time equivalent staff members with an operating budget of \$9.535 million for the 2018–19 financial year<sup>24</sup>, and had offices in Cairns, Sydney, Brisbane and Perth.

1.12 Corporate services, and services for grants of financial assistance, have been provided by a mixture of NAIF staff, staff seconded from the Export Finance and Insurance Corporation (Efic) to the NAIF, and fee-based services provided by Efic to the NAIF under a Service Agreement.<sup>25</sup> Efic is a corporate Commonwealth entity, established and operating under the *Export Finance and Insurance Corporation Act 1991*, as amended to empower Efic to provide and charge for these services.<sup>26</sup> Efic's purpose is to facilitate and encourage Australian export trade by the provision of insurance and financial services and products.

## Investment framework

1.13 The objective of the NAIF is to provide grants of financial assistance to the States and Territories for the construction of Northern Australia economic infrastructure<sup>27</sup>, which is defined in the NAIF Act as infrastructure that provides a basis for economic growth in Northern Australia and stimulates population growth in Northern Australia. It can include infrastructure located outside Northern Australia that satisfies the statutory definition.<sup>28</sup> The NAIF Act provided for \$5 billion to be appropriated from the Consolidated Revenue Fund for this purpose.<sup>29</sup> The NAIF Board has until 30 June 2021 to make decisions to provide financial assistance.<sup>30</sup>

1.14 The NAIF Board is responsible for considering applications by Project Proponents<sup>31</sup> against the eligibility criteria set out in the NAIF Act and the Investment Mandate, and the assessment

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23 Subsection 17(1) of both versions of the Investment Mandate. The term 'Commercial Financier' is defined in section 4 of the Investment Mandate to mean 'a private sector body that provides finance or investment into infrastructure projects'.

24 NAIF Annual Report 2017–18, page 39. Australian Government, *Budget 2018–19—Budget Paper No. 4 Agency Resourcing 2018–2019 Part 1: Australia's Federal Relations*, Canberra, 8 May 2018, page 105.

25 Service Agreement between the Northern Australia Infrastructure Facility and the Export Finance and Insurance Corporation of 5 April 2017.

26 The *Export Finance and Insurance Corporation Act 1991* was amended by the *Northern Australia Infrastructure Facility (Consequential Amendments) Act 2016* from 1 July 2016 and further amended by the *Export Finance and Insurance Corporation Amendment (Support for Commonwealth Entities) Act 2017* from 15 September 2017.

27 *Northern Australia Infrastructure Facility Act 2016*, subsection 3(1).

28 *Northern Australia Infrastructure Facility Act 2016*, subsection 3(2) and drafter's note. Such proposals would also need to satisfy mandatory criterion 3 of the 2018 Investment Mandate (The Project is located in, or will have a significant benefit for, Northern Australia).

29 *Northern Australia Infrastructure Facility Act 2016*, section 41.

30 *Northern Australia Infrastructure Facility Act 2016*, section 8. This statutory deadline applies to decisions to provide financial assistance, and financial assistance can continue to be provided after this date.

31 Section 4 of the Investment Mandate defines the term 'Project Proponent' to mean the entity responsible for a Project.

criteria developed by the Board, and making Investment Decisions.<sup>32</sup> The NAIF Board established a four stage framework for assessing proposals in the ‘transaction pipeline’, as set out in Figure 1.2.<sup>33</sup>

**Figure 1.2: The NAIF four stage assessment framework**



Source: NAIF, *Application and Approval Procedure*, Annexure 2.

1.15 The Investment Mandate permits the NAIF to have a high risk tolerance in relation to factors that are unique to investing in Northern Australia economic infrastructure, including but not limited to, Northern Australia’s distance and remoteness and climate.<sup>34</sup> The NAIF must commence consultation with the relevant State or Territory jurisdiction as soon as practicable after receiving an Investment Proposal, must consult Infrastructure Australia on decisions greater than \$100 million, and can consult with relevant government stakeholders as appropriate.<sup>35</sup> The NAIF Board must make decisions, and does so based on advice from the CEO and staff.<sup>36</sup>

32 While the NAIF Board makes many decisions about applications made by Project Proponents, section 4 of the Investment Mandate defines the term ‘Investment Decision’ to mean ‘a decision by the Board to offer, or not to offer, a Financing Mechanism’, and the Explanatory Statement to the 2018 Investment Mandate (F2018L00567) clarifies that ‘Final Investment Decisions can only be made after the Ministerial consideration period as required by section 11 of the *Northern Australia Infrastructure Facility Act 2016* has elapsed’.

33 NAIF, *Application and Approval Procedure*, Annexure 2.

34 Investment Mandate, section 12.

35 Investment Mandate, sections 13 and 14.

36 Investment Mandate, subsection 6(1). While the Mandate describes these as ‘investment decisions’, these are not investments within the meaning of the *Public Governance, Performance and Accountability Act 2013*: see section 58 or section 59, and the Department of Finance Resource Management Guide 411 *Grants, Procurements and other financial arrangements* at paragraph 35.

1.16 If the NAIF Board decides to grant financial assistance, it must provide the Minister with a written proposal notice.<sup>37</sup> The Minister considers the proposal<sup>38</sup> and receives advice from the department, which in turn consults other Australian Government agencies relevant to the proposal. Neither the Minister nor the relevant State or Territory jurisdiction can direct the NAIF to grant financial assistance to specific projects; however, each can determine that financial assistance should not be provided.<sup>39</sup> If the Minister does not provide a rejection notice within the consideration period, which can be between 21 and 60 days, the NAIF Board can make an Investment Decision.<sup>40</sup> When the NAIF Board makes an Investment Decision, it must notify the Project Proponent as soon as practicable, and within 30 business days must publish information regarding the Investment Decision on its website.<sup>41</sup>

1.17 The department and the NAIF have established Master Facility Agreements (MFA) with Queensland, the Northern Territory and Western Australia that cover the origination, assessment, execution and administration of financial assistance to, and concessional loans to Project Proponents by, the relevant State or Territory jurisdiction.<sup>42</sup>

1.18 Unlike commercial financiers, the NAIF is not a party to the loan contract, does not recognise loans as assets in its balance sheet, and does not carry financial risk or reward. The financial assistance arrangements (illustrated at Figure 1.3) operate as follows:

Concessional financial assistance, in the form concessional loans, will be funded by a special appropriation, attributable to the Department of Industry, Innovation and Science (Industry) as the Accountable Authority.

A Master Facility Agreement (MFA) will provide a contractual arrangement between the Commonwealth (represented by Industry), NAIF corporate Commonwealth entity and the States, for the provision of the concessional financial assistance. This will enable each of the States to provide concessional finance to the project proponents as a pass-through arrangement. Further, MFA absolves the States of any exposure to variability in cash flows, including those arising from credit risk and market risk.

The Commonwealth will not be a direct party to the loan contract with the project proponent. The MFA provides for the financial assistance to be made via the States to the project proponents and repayment of funds to the Commonwealth.<sup>43</sup>

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37 *Northern Australia Infrastructure Facility Act 2016*, subsection 11(2).

38 *Northern Australia Infrastructure Facility Act 2016*, parts 3, 4 and 5.

39 The Minister under Part 4 of the *Northern Australia Infrastructure Facility Act 2016* on statutory grounds; relevant jurisdictions under the Investment Mandate subsection 13(4). The Minister, Finance Minister and Treasurer must approve alternative financing mechanisms under section 11 of the Investment Mandate. In December 2017, Queensland provided the NAIF with a subsection 13(4) notification in respect of a proposal.

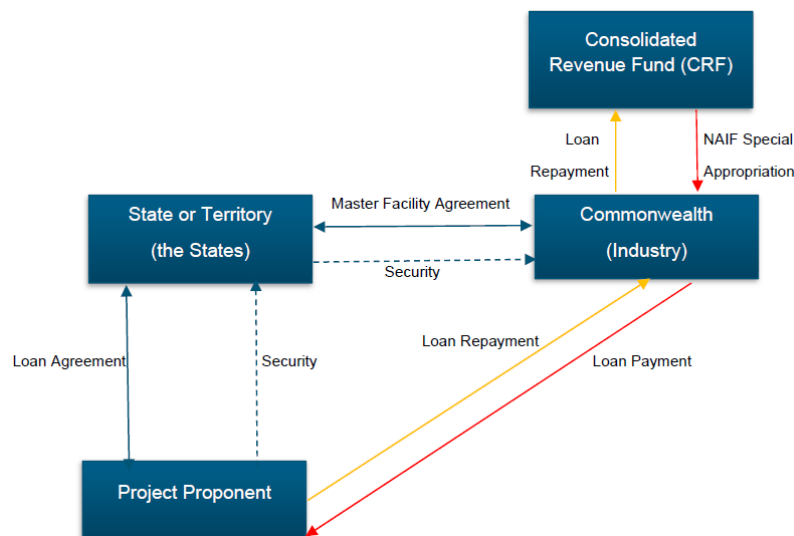
40 Final Investment Decisions can only be made after the Ministerial consideration period as required by section 11 of the *Northern Australia Infrastructure Facility Act 2016* has elapsed: Explanatory Statement to the 2018 Investment Mandate (F2018L00567) at Attachment A under section 17.

41 Investment Mandate, subsections 6(2) and 17(2).

42 Each MFA defines the term 'Project Proponent' to mean 'a borrower under a Finance Contract'. Section 4 of the Investment Mandate defines the term 'Project Proponent' to mean 'the entity responsible for a Project'.

43 Department of Industry, Innovation and Science, *Accounting Policy for Concessional Loans Provided by the Northern Australia Infrastructure Facility 2017–18*, pages 3–4 and Figure 1.

**Figure 1.3: Financial assistance arrangement for concessional loans**



Source: Department of Industry, Innovation and Science, *Accounting Policy for Concessional Loans Provided by the Northern Australia Infrastructure Facility 2017–18*.

1.19 The department’s accounting policy further states that ‘the risk of default will be borne by the Commonwealth and not the States’, the department ‘will recognise these loans as assets in its administered balance sheet’ with the Secretary as the accountable authority, and loans ‘will be assessed at each reporting date to assess whether there is any objective evidence that they are impaired’.<sup>44</sup>

1.20 Concessional loans are those loans provided on terms that are more favourable than the proponent could obtain from other financing sources on a commercial basis. The concessional elements provided by the NAIF can include longer loan tenor, lower interest rates and fee structures, extended periods of capitalisation of interest beyond construction completion, deferral of loan repayments, ranking lower than commercial financiers (subordinate rather than senior or *pari passu* debt), limited or no recourse loans, or alternative financing mechanisms such as financial guarantees to commercial financiers.<sup>45</sup> The Investment Mandate requires that the Board ‘must limit the concessions offered to the minimum concessions the Board considers necessary for the Investment Proposal to proceed’.<sup>46</sup>

1.21 After establishment on 1 July 2016, the NAIF Board made its first decision to grant financial assistance in September 2017. In December 2017, the department commissioned Mr Anthony Shepherd AO to conduct a review (the Shepherd review) to ‘recommend ways to accelerate project development and ensure the NAIF can best meet its legislated objective’.<sup>47</sup> The Shepherd review recommended specific changes to NAIF and government practices and broadening the Investment Mandate in order to increase the volume of decisions. The Minister

44 Department of Industry, Innovation and Science, *Accounting Policy for Concessional Loans Provided by the Northern Australia Infrastructure Facility 2017–18*, pages 4 and 5.

45 Investment Mandate, sections 10 and 11.

46 Investment Mandate, subsection 9(2).

47 Anthony Shepherd AO, *Northern Australia Infrastructure Facility (NAIF) Expert Review Report*, January 2018, page 13.

subsequently amended the Investment Mandate, which took effect from 2 May 2018. By 31 December 2018, the NAIF had made six final Investment Decisions totalling \$263.98 million (see Table 1.1), of which \$13.57 million had been drawn down by 30 January 2019.

**Table 1.1: Final Investment Decisions (1 July 2016–31 December 2018)<sup>48</sup>**

Decision date	Proponent	Goods/services involved	Loan Amount (up to)	Location
29 September 2017	Onslow Marine Support Base Pty Ltd	Development of a marine supply facility including wharf and harbour expansion	\$16.8 million	WA
3 May 2018	Humpty Doo Barramundi Pty Ltd	Development of a solar farm, a medium fish nursery, processing equipment and adult fish feeding systems	\$7.18 million	NT
14 May 2018	Voyages Indigenous Tourism Australia Pty Ltd	Airport runway, taxiway and apron upgrade, runway lighting and provision of contractor accommodation	\$27.5 million	NT
15 June 2018	James Cook University	Building of a Technology Innovation Complex, a 10,000m <sup>2</sup> centre for students, industry partners and researchers	\$98.0 million	QLD
2 August 2018	Pilbara Minerals Limited	Upgrading the public Pippingarra Road	\$19.5 million	WA
28 August 2018	Sheffield Resources Limited	Construction of infrastructure including LNG power station and reticulation, site accommodation village and processing facility and also upgrading of existing local road and port infrastructure all to support the Thunderbird Mineral Sands Project	\$95.0 million	WA
<b>Total</b>			<b>\$263.98 million</b>	

Source: NAIF website (<https://naif.gov.au/corporate-reporting/naif-investment-decision-notifications>), 1 February 2019.

## Audit approach

1.22 The objective of the audit was to examine the effectiveness of governance and integrity arrangements for the Northern Australia Infrastructure Facility.

1.23 To form a conclusion against this objective, the ANAO adopted the following high level criteria:

- Does the NAIF have in place a sound governance framework that is fit-for-purpose?

<sup>48</sup> Prior to publication, the NAIF stated to the ANAO that the NAIF Board had made ten Investment Decisions as at 1 March 2019. The four decisions made since 1 January 2019 did not form part of the audit evidence.

- Has the NAIF implemented arrangements that support effective integrity and transparency in relation to its operations?

1.24 In undertaking the audit, the audit team:

- examined relevant NAIF documents, including Board papers, management reports, policies, procedures, frameworks, external reviews and internal audits;
- interviewed NAIF and service provider staff; and
- sought written and verbal feedback from government stakeholders with statutory roles under the NAIF Act and Investment Mandate.

1.25 The audit was open for citizen contributions, including from NAIF applicants and Project Proponents, non-governmental stakeholders and the general public — no contributions were received. The ANAO did not approach individual applicants for NAIF financial assistance, Project Proponents or non-government stakeholders for comment.

1.26 The audit was conducted in accordance with ANAO Auditing Standards<sup>49</sup> at a cost to the ANAO of approximately \$564,445. Audit team members were Christopher Swain, Chirag Pathak, Anne Kent and Paul Bryant.

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49 *Australian National Audit Office Auditing Standards (28/02/2018)*, C2018G00152, available from [www.legislation.gov.au](http://www.legislation.gov.au).



## 2. Governance

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### Areas examined

The ANAO examined whether the Northern Australia Infrastructure Facility (NAIF) has in place a sound governance framework that is fit-for-purpose.

### Conclusion

The NAIF has an appropriate governance framework, including systems of risk management and internal control, and effective arrangements with the Export Finance and Insurance Corporation (Efic) as its key service provider. Appropriate oversight is provided to the Minister for Resources and Northern Australia through reporting and regular meetings. While the Board adopted a flexible approach to strategy, only a small number of projects were assessed as addressing an identified infrastructure need, and amendments to the Investment Mandate changed the scale and scope of projects that the NAIF Board was considering beyond its original purpose. Remuneration policies and practices were not consistent with public sector governance standards, and information governance requires attention to meet National Archives standards and improve transparency.

### Recommendations

The ANAO made two recommendations to improve transparency by publishing criteria and more information about Investment Decisions.

### Is the NAIF's governance framework in accordance with relevant legislative and policy requirements?

The NAIF's governance framework is in accordance with relevant legislative and policy requirements. The NAIF has an appropriate statutory framework, Board processes and suite of governance policies. The NAIF provides the Minister for Resources and Northern Australia with oversight of its governance and decision-making through transaction pipeline reports and weekly meetings with the Minister's office, but did not keep minutes of these meetings. The NAIF Board has oversight of the Chief Executive Officer and staff, however remuneration policies and practices were not consistent with public sector governance standards.

### Legislative framework

2.1 The NAIF's legislative framework, as set out in the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), the *Northern Australia Infrastructure Facility Act 2016* (NAIF Act) and the Investment Mandate, requires that the NAIF Board must:

- govern the NAIF in a way that promotes the proper use and management of public resources for which the Board is responsible, the achievement of the purposes of the NAIF, and the financial sustainability of the NAIF;
- not act in a way that is likely to cause damage to the Commonwealth Government's reputation, or that of a relevant State or Territory government; and

- have regard to Australian best practice government governance principles, and Australian best practice corporate governance for Commercial Financiers, when performing its functions.

## Ministerial oversight

2.2 The Minister appoints the Chair and other Board members<sup>50</sup> and is accountable to the Parliament for the governance of the NAIF. In turn, the NAIF Board must keep the Minister informed of the activities of the NAIF; give the Minister any reports, documents and information in relation to those activities as the Minister requires; and otherwise keep the Minister informed.<sup>51</sup>

2.3 The Minister must give directions to the NAIF about the performance of the NAIF's functions by legislative instrument — the Investment Mandate — and the NAIF must take all reasonable steps to comply with the Investment Mandate.<sup>52</sup>

2.4 The Investment Mandate provides a statutory framework for ministerial oversight of NAIF governance, and the ministerial consideration process set out in the NAIF Act provides a framework for ministerial oversight of decisions to grant financial assistance:

- there are safeguards in the NAIF Act intended to prevent ministers from using the Investment Mandate mechanism to direct, or have the effect of directing, the NAIF to provide financial assistance to a particular project or person<sup>53</sup>;
- the Explanatory Statement to the 2016 Investment Mandate states that 'Subject to the Minister's limited powers of direction with respect to Investment Decisions...the Facility will make investment decisions independently of the Commonwealth'<sup>54</sup>; and
- the Explanatory Statement to the 2018 Investment Mandate similarly states that 'Within the scope of the Investment Mandate, the Facility will make individual investment decisions independently of the Commonwealth. Those decisions are subject only to the Minister's limited powers of rejection set out in section 11 of the NAIF Act'.<sup>55</sup>

2.5 In addition to the statutory oversight mechanisms:

- the Minister provided the NAIF with a Statement of Expectations<sup>56</sup> that outlined the Minister's 'expectations on the operation and performance of the NAIF, beyond that considered by the legislative framework', and on 3 January 2019, the NAIF responded with a Statement of Intent 'outlining how NAIF will direct its operations'; and
- the NAIF provided the Minister with information about projects in the transaction pipeline through monthly transaction pipeline reports to the Minister and the Department of

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50 *Northern Australia Infrastructure Facility Act 2016*, sections 15 and 16.

51 *Public Governance, Performance and Accountability Act 2013*, section 19.

52 *Northern Australia Infrastructure Facility Act 2016*, section 9.

53 *Northern Australia Infrastructure Facility Act 2016*, subsection 9(4).

54 Explanatory Statement to the *Northern Australia Infrastructure Facility Investment Mandate Direction 2016*, F2016L00654.

55 Explanatory Statement to the *Northern Australia Infrastructure Facility Investment Mandate Direction 2018*, F2018L00567.

56 The Statement of Expectations is not a legislative instrument.

Industry, Innovation and Science (the department), and weekly meetings with the Minister's office and departmental staff about applications for financial assistance progressing through due diligence or other significant developments. While the NAIF circulated in advance of each meeting a list of projects to be discussed, no minutes were kept.<sup>57</sup>

2.6 If the NAIF Board proposes to provide financial assistance, the NAIF must give the Minister written notice of the proposal to do so (a proposal notice).<sup>58</sup> Between 1 July 2016 and 30 September 2018, the NAIF gave six proposal notices to the Minister.

2.7 The Minister has a statutory 21 day consideration period for proposal notices, and can extend this to a total of 60 days, before which time the department cannot provide the proposed financial assistance.<sup>59</sup> Under the NAIF Act, the Minister does not give formal approval of a proposal, but at any time during the consideration period may notify the NAIF in writing that the financial assistance should not be provided (a rejection notice).<sup>60</sup>

2.8 The Minister may issue a rejection notice only if satisfied that providing the proposed financial assistance would:

- be inconsistent with the objectives and policies of the Commonwealth Government;
- have adverse implications for Australia's national or domestic security; or
- have an adverse impact on Australia's international reputation or foreign relations.<sup>61</sup>

2.9 A ministerial rejection notice must be accompanied by the Minister's written reasons for the notice, and within 20 sitting days after the rejection notice is given, the Minister must table the notice in each House of the Parliament.<sup>62</sup> To date, the Minister has not rejected any proposals.

## The NAIF Board

2.10 The NAIF Board was established and operates under Part 5 of the NAIF Act. It consists of the Chair and between four and six other members. The Minister appoints the Chair and members in writing on a part-time basis for a period not exceeding three years. There is no statutory bar to reappointment. Remuneration is set by the Australian Government Remuneration Tribunal. The Minister may terminate appointments on statutory grounds such as misbehaviour, incapacity or bankruptcy. The inaugural Chair occupied the position from July 2016 to April 2018. The appointment of the next Chair, who had served as acting Chair since May 2018, occurred on 1 August 2018.

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57 Attendees from the department compile a summary from the meeting for internal use only. The NAIF stated that it has commenced keeping records of these weekly meetings from January 2019.

58 *Northern Australia Infrastructure Facility Act 2016*, section 11.

59 The NAIF stated that 'in practice the funds also cannot flow to a proponent (via the relevant jurisdiction) until the facility agreement is signed by relevant jurisdiction and proponent and all conditions precedent met. This would include all regulatory, environmental and Native Title approvals as required in s15(2) of the Investment Mandate. NAIF though its portfolio management function is responsible for providing this assurance and confirming to the Department drawdowns to action'. The Export Finance and Insurance Corporation (Efic) provides the portfolio management function on behalf of the NAIF.

60 *Northern Australia Infrastructure Facility Act 2016*, subsections 11(3) and (4).

61 *Northern Australia Infrastructure Facility Act 2016*, subsection 11(5).

62 *Northern Australia Infrastructure Facility Act 2016*, section 12.

2.11 The NAIF Board operates under the NAIF Board Charter. The NAIF Board created one subcommittee, the Board Audit and Risk Committee (BARC), which operates under the NAIF Board Audit and Risk Committee Charter. Both Charters were approved by the NAIF Board at its first meeting on 10 August 2016, revised following legal review on 20 June 2017, updated on 14 June 2018, and are publicly available on the NAIF website.

2.12 The Chair must convene at least two Board meetings each financial year, and Board procedure is set out in the NAIF Act and the NAIF Board Charter. In the two and a half years between establishment on 1 July 2016 and 31 December 2018, the NAIF Board held 29 meetings. This frequency of meetings reflected the volume of work associated with the governance requirements for a newly established entity, together with the transaction pipeline of proposals requiring consideration. The NAIF Board has a forward work program, regular standing items on its agenda, and its papers were prepared to a consistent and transparent standard.

2.13 The NAIF Board commissioned a review of its effectiveness by an external corporate governance consultant. The resulting March 2017 report noted that the Board ‘has applied itself with great effect to the governance challenges of a start-up board’ and ‘has produced effective, plain English Board documentation that encapsulates good practice in a modern Australia boardroom’ (*sic*). It also recommended areas for further development in Board planning and practices. The NAIF Board should continue to seek ongoing review of its performance where appropriate.

### **Chief Executive Officer (CEO) and staff**

2.14 The NAIF Board appoints the CEO by written instrument on a full-time or part-time basis for a period of up to five years. CEO remuneration is set by the Australian Government Remuneration Tribunal. The CEO may resign, and the Board may terminate the appointment on statutory grounds such as misbehaviour, incapacity, unsatisfactory performance or bankruptcy.

2.15 The NAIF Board appointed an interim CEO from 18 August 2016 until an executive search was completed, and an ongoing CEO on 24 October 2016 for a fixed period ending on 31 October 2019. The CEO is responsible for the day-to-day administration of the NAIF, and must act in accordance with policies determined by the NAIF Board. The responsibilities and duties of the CEO are outlined in the NAIF Board Charter. The NAIF Board has provided regular policy and other direction to the CEO, and the CEO has provided regular reports to the NAIF Board on the ongoing operations of the NAIF.

2.16 The employment and remuneration of NAIF staff is governed by section 38 of the NAIF Act, the PGPA Act requirement for the proper use and management of public resources, and the Investment Mandate requirement to have regard to best practice governance principles, such as:

- the Workplace Bargaining Policy — which directly applies to the NAIF as a corporate Commonwealth entity;
- job families, work level standards and other remuneration-related policies developed by the Australian Public Service Commission (APSC);
- Prudential Standard CPS 510 *Governance* and *Prudential Practice Guide PPG 511 Remuneration* developed by the Australian Prudential Regulation Authority (APRA); and

- the Australian Stock Exchange (ASX) *Corporate Governance Principles and Recommendations* (used by the NAIF in its Senate Inquiry submission).

2.17 The NAIF Board's functions under the NAIF Board Charter include to 'review and approve the executive remuneration policy framework'.

2.18 The NAIF Board approved a remuneration policy on 20 June 2017, almost one year after the establishment of the NAIF and after the engagement of four senior staff members. The NAIF stated that prior to the adoption of the NAIF remuneration policy, it operated with reference to the Efic remuneration policy. The NAIF reported aggregate information on executive salaries under the Executive Remuneration Reporting framework, but did not publish the NAIF remuneration policy.

2.19 The NAIF remuneration policy states that 'Market salary will be determined by comparing each employee's salary, to salary data from the financial services sector'. The NAIF did not assess proposed job roles against the APSC Job Family Model and work level standards to determine whether the financial services sector was an appropriate benchmark for each of these roles.<sup>63</sup>

2.20 The NAIF used financial services sector salary data obtained from the Financial Institutions Remuneration Group<sup>64</sup>, and paid average total remuneration to six executives equivalent to Australian Public Service departmental deputy secretaries.<sup>65</sup>

2.21 The NAIF submitted an *Assessment of Remuneration Proposal* and *CEO Declaration* to the Australian Public Service Commissioner to contain non-promotion salary increases over a three-year period to an average of 2 per cent per annum.<sup>66</sup> On 23 August 2017, the Board approved salary increases for three employees of 25 per cent (from \$200,000 to \$250,000), 15.6 per cent (from \$216,300 to \$250,000) and 7.7 per cent (from \$325,000 to \$350,000) respectively. These were described as salary increases 'in line with promotions'. The three employees receiving the salary increases remained in the same roles before and after the increases.<sup>67</sup>

2.22 The NAIF remuneration policy stated that 'The provision of annual performance awards is discretionary. Bonuses are considered, where set objectives are met and the organisations values

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63 The NAIF stated that in some individual cases, the 'NAIF did consider existing salaries and role descriptions of candidates sourced from the APS in the consideration of salaries for NAIF specific role descriptions'.

64 The Financial Institutions Remuneration Group is a member-based not-for-profit organisation that provides remuneration and benefits data to the financial services industry ([www.firg.com.au](http://www.firg.com.au)).

65 The *NAIF Executive Remuneration 2017–18* report stated that NAIF executives received average total remuneration—including base salary, superannuation and bonuses—in 2017–18 of between \$342,781 and \$414,985. The *Australian Public Service Remuneration Report 2017* stated that the Total Reward—including base salary, superannuation and bonuses—paid to deputy secretaries (Senior Executive Service Band 3 employees) in 2017 was between \$369,158 (P5) and \$481,555 (P95).

66 *Assessment of Remuneration Proposal* dated 15 September 2017 and *CEO Declaration* dated 13 September 2017.

67 The NAIF stated that these were for employees who were performing at a more senior level and with significant expansion of responsibility than anticipated at the outset; the salary increases were made to reflect alignment to market and to address disparity with peers; and the NAIF's non-promotion salary increases since establishment total \$35,000 or 0.8 per cent compared to the 6 per cent approved by the Australian Public Service Commission for the three year period of September 2017 to August 2020. The ANAO notes that an internal audit in August 2018 found that the majority of NAIF staff had been at NAIF for less than twelve months. Under the NAIF Remuneration Policy, remuneration is reviewed annually, and the majority of NAIF staff would therefore not be eligible for non-promotion salary increases.

have been demonstrated over the course of the year' (*sic*), but did not explicitly link the calculation of performance-based remuneration to the achievement of measured performance outcomes or risk, which is inconsistent with relevant APRA and ASX standards.<sup>68</sup>

2.23 The NAIF Board approved bonus payments for four employees of 25–30 per cent of their total salary packages (between \$200,000 and \$350,000) for the period 1 July 2016–30 June 2017.<sup>69</sup> While the NAIF had not made any Investment Decisions during this period, the bonus payments were based on meeting performance targets relating to the NAIF 'governance framework [being] established' and 'development of [a] potential investment proposal pipeline'.<sup>70</sup> Internal documents<sup>71</sup> demonstrated that these bonus payments were also partly intended to have the effect of topping up base salaries.

2.24 The NAIF Board considered and approved remuneration policies and practices on advice from the CEO, but did not establish a remuneration subcommittee as recommended by relevant APRA and ASX standards.<sup>72</sup>

### **Governance policies and practices**

2.25 The department provided Efic \$2.301 million in 2016–17 to support the establishment and initial operation of the NAIF as a corporate Commonwealth entity. As a result, the NAIF Board was provided at its first meeting with a number of draft governance policies, based on existing Efic policies. The Board modified these draft policies to meet the needs of the NAIF, approved a number of these policies within its first six months, and regularly reviewed the majority of these policies, including obtaining legal review.

2.26 For activities and functions where there was no specific NAIF policy, procedure or framework, the NAIF Board adopted a number of its service provider's internal governance policies, including fraud control, information security, and human resources policies.<sup>73</sup> The Board was provided with copies of some but not all of the adopted policies. On 16 November 2017, the NAIF appointed a Manager Compliance and Risk function whose role included reviewing the adopted policies, and included these policies in a compliance plan.

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68 APRA CPS 510 *Governance* at paragraphs 54–56 and PPG 511; and commentary to Recommendation 8.2 of the ASX *Corporate Governance Principles and Recommendations*.

69 On 23 August 2017, the NAIF Board resolved to defer any decision regarding performance bonuses for NAIF staff (and Efic seconded staff) until December 2017, on the basis that Board members did not believe performance bonuses should be paid prior to completion of a project transaction. Nonetheless, the Board resolved to take into account in their bonus calculation the period of service for each applicable staff members from their start date until the bonus recommendation. On 14 February 2018, the NAIF Board agreed 'in principle to the provision of bonuses to eligible NAIF staff for the period of 1 July 2016 to 30 June 2017'.

70 These performance targets are set out in the NAIF Annual Report 2016–2017, pages 14–15.

71 These documents were not presented to the NAIF Board as part of the proposal for approval of the relevant bonuses.

72 APRA CPS 510 *Governance* at paragraphs 65–72 and PPG 511; Principle 8 and Recommendation 8.1 of the ASX *Corporate Governance Principles and Recommendations*. The latter states at page 31 that 'no...senior executive should be involved in deciding his or her own remuneration'.

73 These policies were formally adopted by the NAIF Board through Circular Resolution 3 of 2017 (1 August 2017).

## Did the NAIF's strategy promote the achievement of its purposes?

While NAIF origination strategies promoted the achievement of its purpose: NAIF facilitated origination has not generated a significant or sustained increase in either the annual number of new projects or the annual number of successful applications; and only a small number of projects considered by the NAIF Board were assessed as addressing an infrastructure need identified through a Commonwealth, State or Territory assessment process, pipeline, or priority list. The eligibility criteria for financial assistance were substantially broadened in order to increase the number of Investment Decisions.

2.27 The NAIF Board's selection and implementation of strategies that promote the achievement of its purposes is an important component of its duty to govern the NAIF.<sup>74</sup>

2.28 In the second reading speech to the NAIF Bill in 2016, the Minister for Resources, Energy and Northern Australia stated that 'Northern Australia has great potential for economic and population growth, but it needs the right backbone economic infrastructure to drive that growth' and that the NAIF 'will support the private sector to construct transformative economic infrastructure for northern Australia'.<sup>75</sup> The Minister further stated that 'these major projects may include airports, ports, roads, rail, energy, water, and communications infrastructure. These are the types of economic infrastructure needed to further open the North for business, and to deliver wider public benefits for the rest of Australia'.

2.29 As set out in the second reading speech, *Green Paper*, *Pivot North* report, *Northern Australia Audit* and *White Paper*:

- the **scale** of infrastructure is described in terms such as 'fundamentally enabling', 'backbone', 'transformative' and 'major project';
- the **scope** of economic infrastructure is defined to include infrastructure in the transport (airports, ports, rail and road), energy (generation and transmission), water and communications sectors; and
- the **purpose** is identified as delivering public benefit by addressing the drivers of market failure in economic infrastructure investment, including short loan tenor available to applicants and higher investment risk caused by distance, remoteness and climate and other factors unique to investing in Northern Australia economic infrastructure.<sup>76</sup>

### Origination strategies

#### *Proponent-led origination*

2.30 The 2015–16 Budget papers stated that 'the loan facility will be open for applications from 1 July 2015'. This opening date was almost one year before eligibility criteria were set out in the

74 *Public Governance, Performance and Accountability Act 2013*, section 15.

75 House of Representatives, *Official Hansard No. 5, 2016*, 17 March 2016, page 3441–2.

76 This purpose is also reflected in the Investment Mandate, for example, Schedule 1 item 2 in requiring public benefit, section 10 in determining loan conditions including tenor, and section 12 in permitting a high risk tolerance for factors unique to investing in Northern Australia economic infrastructure such as distance, remoteness and climate.

NAIF Act and Investment Mandate, and before the NAIF was established and thus could develop or publish assessment criteria.

2.31 The NAIF Board was provided at its first meeting on 10 August 2016 with a transaction pipeline of 60 projects. Two years later, in August 2018, and after changes to the Investment Mandate, three of these 60 projects had progressed to either the due diligence or execution stages. By November 2018, this had increased to four projects, and the NAIF had assessed 47 of these 60 projects as not proceeding.

2.32 Following its establishment, the NAIF:

- took 16 months to finalise assessment criteria, during which time it continued to invite, accept and assess project proposals; and
- did not make seven of ten documents outlining assessment criteria, including the Applications and Approvals Procedure, publicly available.<sup>77</sup>

2.33 While publicising the NAIF as soon as possible may have raised interest amongst potential proponents, inviting proposals before developing and publishing the criteria for financial assistance reduced the opportunity for potential proponents and investors to consider whether their projects would meet these criteria, and increased the risk that the NAIF would receive proposals that would not meet these criteria.

### Recommendation no.1

2.34 The NAIF publish criteria and all information necessary for applicants to submit complete applications for grants of financial assistance.

**The Northern Australia Infrastructure Facility response: Agree.**

2.35 *The NAIF Act and published Investment Mandate provide a comprehensive list of five mandatory criteria and at least an additional 27 requirements that the NAIF Board must either consider, have regard to or be satisfied with in making an Investment Decision. In addition the NAIF website publishes a detailed outline containing other information required as a project is assessed. Notwithstanding this existing transparency NAIF undertakes to assist proponents by publishing case studies and further guidance.*

### NAIF-facilitated origination

2.36 In April and June 2017, the NAIF Board considered and endorsed a strategic plan including both proponent-led and NAIF-facilitated origination strategies. NAIF-facilitated origination involved the NAIF working with governments, industry and other stakeholders to identify projects that were unlikely to be brought forward solely through the existing proponent-led process. The strategic plan described this approach as ‘actively identifying and facilitating transformative opportunities’.

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77 The NAIF stated in December 2018 that some of these documents were ‘internal policies, procedures and guidelines’ or other ‘internal documents never intended for publication’; for example, the Risk Appetite Statement, the NAIF Credit Approval Guidelines and the Investment Decision Considerations framework. The NAIF did publish the *Environmental and Social Review of Transactions Policy*, the *Indigenous Engagement Strategy Guideline* and the *Public Benefit Guideline*.



2.37 The 2017–18 Corporate Plan reported that as at 30 June 2017, the NAIF Board, CEO and staff had collectively met with more than 1500 interested stakeholders and presented at 15 events, reaching audiences of over 2000 people. This included travel at the invitation of Austrade to the People's Republic of China, the United States of America and Canada to present to potential institutional investors.

2.38 Since the implementation of the NAIF-facilitated origination strategy:

- the annual number of new projects in the transaction pipeline remained relatively steady in 2016 (94), 2017 (91) and 2018 (81, to 22 August 2018); and
- the annual number of successful applications (projects at the due diligence stage or beyond, by origination date) — remained relatively steady in 2016 (seven), 2017 (eight) and 2018 (seven, to 22 August 2018).<sup>78</sup>

The data does not demonstrate a clear relationship between the NAIF-facilitated origination strategy and a significant or sustained increase in either the annual number of new projects or the annual number of successful applications.

2.39 In January 2018, the Shepherd Report noted 'The resource intensity of monitoring and supporting projects in the pipeline, despite a low number being potentially viable and eligible projects, may not be the best use of resources'.<sup>79</sup> The Shepherd Report also noted:

Many projects on the NAIF long list are unlikely to ever reach investment stage. It is a truism in development that your success varies inversely with the size of the list you are working on.

...

It may be sensitive from a public relations perspective, it would be more productive for NAIF to concentrate its limited resources on less projects. For example, those projects that are investment ready or are closer to investment readiness and are assured of support from the relevant State or Territory.

2.40 While advice was qualified as to the risks to pipeline projections in reports, and subsequent reports provided updated information, pipeline reporting consistently overestimated the health and maturity of the transaction pipeline compared to the Investment Decisions actually made by the NAIF Board. For example:

- on 15 November 2017, the CEO reported to the NAIF Board proposals for approximately \$1.6 billion in finance were in due diligence for 'potential close by June 2018';
- the CEO noted in the report that 'There is a degree of uncertainty around potential financial close dates given the NAIF mandate requirements (including issues around whether a gap will be established) and the timing of when potential proponents will provide due diligence material to NAIF for assessment'; and

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78 As at 22 August 2018.

79 Anthony Shepherd AO, *Northern Australia Infrastructure Facility (NAIF) Expert Review Report*, January 2018.

- by 30 June 2018, the NAIF Board had made Investment Decisions to provide \$149.48 million in financial assistance (9.3 per cent of the predicted amount).<sup>80</sup>

#### *Jurisdiction-led project selection model*

2.41 In August 2017, prior to any grants of financial assistance being made, and amongst attempts at accelerating known projects, the NAIF Board also agreed to consider the merits of a jurisdiction-led project selection model. This recognised that the Board, in making a decision, must consider a preference for projects that address an infrastructure need identified through a Commonwealth, State or Territory assessment process, pipeline, or priority list such as the *Northern Australia Infrastructure Audit*.<sup>81</sup> The NAIF met regularly with jurisdictions at ministerial and senior executive levels to discuss its origination efforts. Six of 27 projects considered by the NAIF Board at the strategic assessment stage were assessed by the NAIF as addressing an infrastructure need identified through a Commonwealth, State or Territory assessment process, pipeline, or priority list.<sup>82</sup>

#### **Changing the criteria for financial assistance**

2.42 From April 2017 to April 2018, the NAIF made a number of requests to the Minister to modify the Investment Mandate in order to make more projects eligible for financing, including existing applications under consideration.

2.43 In December 2017, the department commissioned the Shepherd review ‘to recommend ways to accelerate project development and ensure the NAIF can best meet its legislated objective’. Following the Shepherd review, the Minister revised the Investment Mandate with effect from 2 May 2018.<sup>83</sup> All but one Investment Decision by the NAIF Board has post-dated this change.

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80 The NAIF stated that each report provides qualifications to ensure that the Board is on notice as to the risk to the projections in the reports, including the factors that are outside the control of NAIF which impact the projections but which are clearly noted on various public statements; in order to control this risk, the NAIF regularly updates the Board on the transaction pipeline and reviews the pipeline with the Board; since August 2018, this included a Dashboard that identifies applications having a 50 per cent likelihood of reaching an Investment Decision by the close of the Financial Year; and the Board also questions the executive as to likely timing and risks to projects in the pipeline. The NAIF further stated that its reporting was not overestimated as it was a forecast at a point in time based on proponent information and NAIF’s Executives’ assessment of facts at the time.

81 This was a non-mandatory criterion in Schedule 2 of the previous 2016 Investment Mandate, and was retained as a matter to be considered when making Investment Decisions in paragraph 7(3)(b) of the 2018 Investment Mandate. The *Northern Australia Infrastructure Audit* was conducted by Infrastructure Australia in 2016 and identified a number of priority infrastructure projects in northern Australia: see paragraph 1.4.

82 The 27 projects were considered by the NAIF Board at the strategic assessment stage over the period 1 July 2016–20 April 2018—before amendments to the Investment Mandate took effect in May 2018.

83 The revised Investment Mandate implemented four of the 15 recommendations in the Shepherd Report: recommendation 4 relating to the interpretation of the term ‘Northern Australia economic infrastructure’ and relaxation of the multi user test; recommendation 5 in removal of the ‘crowding out test’ in subsection 7(1) and mandatory criterion 3 of the original Mandate; recommendation 6 in removal of the ‘debt cap’ in mandatory criterion 5 of the original Mandate; and recommendation 7 to fully exploit flexibility in providing concessional finance.

### *Small-scale projects and removal of the debt cap*

2.44 The original 2016 Investment Mandate included as a non-mandatory criterion that the proposed project be seeking financing from the NAIF for an amount of \$50 million or more.<sup>84</sup> This non-mandatory criterion was consistent with the *White Paper*, which observed that ‘Governments’ role is to create successful business environments, not successful businesses’.<sup>85</sup> On 28 August 2017, the NAIF Board requested the Minister review this non-mandatory criterion, on the basis that ‘the Executive continued to report confusion from stakeholders about this requirement’.

2.45 The 2016 Investment Mandate also required as a mandatory criterion that NAIF loan monies were not the majority source of debt funding, and that the proponent needed to show that NAIF finance would not exceed 50 per cent of total debt for the proposed project. This requirement was ‘in keeping with the principle that the Facility will work in partnership with Commercial Financiers and any other financiers, who should provide an equal or majority source of finance’<sup>86</sup> and was consistent with the *White Paper’s* observation that ‘It is not the Commonwealth Government’s role to direct, or be the principal financier of, development’.<sup>87</sup> It was also consistent with the intended role of the NAIF as a market gap financier — ‘The Facility will fill the gaps in the infrastructure financing market for Northern Australia by supplementing private financing for Projects that produce benefits to the region’.<sup>88</sup>

2.46 Both criteria were removed from the revised 2018 Investment Mandate, increasing risks that:

- the NAIF would attract and be required to assess and manage a large number of small projects — by August 2018, the pipeline of 266 projects included 44 projects seeking \$50 million or less in finance, and 41 projects seeking more than \$50 million (181 projects had no amount listed). Around half of the projects with a known financing amount were therefore small-scale projects, an increase from 27 per cent the previous year;
- the NAIF would predominantly finance small-scale projects — between 1 July 2016 and 31 December 2018, all six Investment Decisions related to small-scale projects, four of which fell within the former non-mandatory criterion threshold of \$50 million, and none of which exceeded the \$100 million minimum threshold for consultation with Infrastructure Australia; and

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84 Investment Mandate 2016, Schedule 2 Item 1.

85 White Paper, page 2.

86 Investment Mandate 2016, Schedule 1 Item 5.

87 White Paper, page 2.

88 Explanatory Statement, *Northern Australia Infrastructure Facility Investment Mandate Direction 2016*, 4 May 2016.

- the Australian Government would in effect carry the majority of the risk of non-repayment of debt in projects that were below investment grade.<sup>89</sup>

### *The interpretation of Northern Australia economic infrastructure*

2.47 The object of the NAIF Act is ‘to provide grants of financial assistance to the States and Territories for the construction of Northern Australia economic infrastructure’, and defines Northern Australia economic infrastructure as ‘infrastructure that: (a) provides a basis for economic growth in Northern Australia; and (b) stimulates population growth in Northern Australia’.<sup>90</sup>

2.48 In May 2016, the Explanatory Statement to the 2016 Investment Mandate stated that ‘The Board will preference multiple user infrastructure that benefits the broader economy. It is not intended that the Facility fund a project’s operating assets (such as plant and equipment)’. The Explanatory Statement to the 2018 Investment Mandate did not include this statement.

2.49 Mandatory criterion 1 in the 2016 Investment Mandate required that ‘The proposed Project involves construction or enhancement of economic infrastructure’ and provided that economic infrastructure ‘includes, but is not limited to, rail, water, energy and communications networks, ports and airports’. In the Senate debate on the NAIF Bill, the Minister for Northern Australia stated ‘I want to make clear that we are talking about infrastructure investment, not mines, not hotel rooms and not individual businesses...As the government has always said, for infrastructure like rail lines, airports, water infrastructure et cetera’.<sup>91</sup>

2.50 The 2018 Investment Mandate amended mandatory criterion 1 to read ‘Northern Australia economic infrastructure’, and the Explanatory Statement included a significantly expanded list of potential projects: ‘ports, airports, rail, roads, water, energy and communications networks, social infrastructure (including health facilities, education facilities, research facilities, training and related accommodation facilities), processing facilities (including abattoirs and agricultural processing plants) and transshipment vessels’.

2.51 This interpretation of the term ‘Northern Australia economic infrastructure’ to include non-economic infrastructure such as social infrastructure, processing facilities and transshipment vessels reflected the interpretation adopted by the NAIF Board as early as February 2017.

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89 In relation to debt funding, the revised 2018 Investment Mandate inserted at section 12 a requirement that the NAIF is not the sole holder of financial risk, allowing equity to be taken into account. The Mandate also required that the Board consider ‘the potential of the investment to encourage private sector participation in financing a Project’ at paragraph 7(2)(d), and that ‘The Board must limit the concessions offered to the minimum concessions the Board considers necessary for the Investment Proposal to proceed’ at subsection 9(2).

90 *Northern Australia Infrastructure Facility Act 2016*, section 3.

91 Senate, *Official Hansard No. 6, 2016*, 2 May 2016, page 3250.

## Is there an appropriate system of risk oversight and management?

The NAIF has developed an appropriate system of risk oversight and management that is consistent with the requirements of the Commonwealth Risk Management Policy and relevant Australian Prudential Regulation Authority (APRA) and Australian Stock Exchange (ASX) governance standards.

2.52 The NAIF Board is subject to legislative and policy requirements that it establish and maintain an appropriate system of risk oversight and management.<sup>92</sup>

2.53 The NAIF Board approved a risk management policy on 20 September 2016. The Board Audit and Risk Committee (BARC) endorsed a revised version of this policy on 13 February 2018, which the NAIF Board approved on 14 February 2018.

2.54 The BARC endorsed, and the NAIF Board approved, a risk management framework on 10 February 2017 which was subject to regular review and revision from April 2017 to August 2018, and an extract of the framework was published on the NAIF website. The framework included a statement on the NAIF's risk appetite and risk tolerances, and sets out four broad categories of risk:

- strategic — risks related to meeting strategic objectives and expectations of key stakeholders;
- investment decisions — project assessment and credit related risks;
- governance, legal and regulatory — compliance with relevant obligations such as confidentiality, conduct and anti-money laundering and counter-terrorism financing; and
- operational — risks associated with running a viable and efficient business including resourcing, business continuity, outsourcing and health and safety.

2.55 The risk management policy and framework are consistent with the requirements of the Commonwealth Risk Management Policy and relevant APRA and ASX governance standards. The NAIF adopted the Three Lines of Defence (3LOD) risk management and assurance model. The risk management policy and framework set out roles and responsibilities for the Board, the BARC and executive management, and the BARC considered risk-related issues at regular meetings.

2.56 In July 2017, the NAIF engaged a consultant to review its risk management framework, and the Board approved and implemented the resulting recommendations. On 16 November 2017, the NAIF appointed an executive specifically responsible for risk (other than assessment of credit risk on individual transactions). The NAIF Board appointed an internal audit provider on 20 December 2017 and subsequently developed an internal audit plan through to 2020. From March 2018, the NAIF provided the Board with quarterly risk management and compliance reports. These measures should assist the NAIF to continue to develop its system of risk oversight and management.

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92 *Public Governance, Performance and Accountability Act 2013*, section 16. Relevant Australian best practice government governance principles include the Commonwealth Risk Management Policy, and the Department of Finance Resource Management Guide 211 *Implementing the Commonwealth Risk Management Policy—Guidance*. Relevant Australian best practice corporate governance for Commercial Financiers includes the APRA prudential standards and practice guides for risk management, and the ASX *Corporate Governance Principles and Recommendations*.

2.57 The NAIF worked closely with Efic to assess credit risk in investment decision-making. The Efic chief credit officer approved risk ratings and oversight. While the NAIF did not verify risk ratings, the NAIF verified that assigned rating numbers were within the NAIF's risk tolerance.

### Is there an appropriate system of internal control?

The NAIF has developed a system of internal control which is appropriate for its requirements. The NAIF Board adopted a blended system that relied primarily on service providers' policies and practices to provide coverage broadly equivalent to the *model accountable authority instructions*. The blended system has an inherent risk of insufficient clarity in relevant roles and responsibilities which should be monitored.

2.58 The NAIF Board is responsible for establishing and maintaining an appropriate system of internal control.<sup>93</sup> The NAIF Board delegated responsibility for monitoring the system to the BARC in August 2016, and issued instructions to the CEO. The BARC provided assurance and review through the risk management framework, which identified a number of key enterprise risks relating to internal control. Information about the establishment of components of the internal control system was provided to the NAIF Board through CEO reporting, and specific reporting on the monitoring of internal controls was provided to the Board from March 2018.<sup>94</sup>

2.59 The NAIF's system of internal control is documented in a suite of policies, procedures and inter-entity agreements including:

- NAIF governance policies (as approved over time);
- Efic governance policies (in the absence of NAIF policies);
- the Service Agreement, which required Efic to comply with its own policies unless a NAIF policy applied;
- the NAIF CEO Instruments of Delegation; and
- arrangements with the department and Efic for the portfolio management of loans, including the accounting entries and financial information the department requires from the NAIF and Efic.

2.60 Together, these arrangements provide coverage broadly equivalent to the six core topics in the Department of Finance's *model accountable authority instructions*.<sup>95</sup> The NAIF's internal control documents are authored by separate entities<sup>96</sup> and the framework to manage the suite of

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93 *Public Governance, Performance and Accountability Act 2013*, section 16.

94 Information included in the NAIF Risk Management and Compliance Reports provided to the Board and the BARC included updates on: policy development and review; compliance training; reporting incidences; and changes compared to the previous reported period.

95 Department of Finance, Resource Management Guide 206 *Model accountable authority instructions Corporate Commonwealth entities*, available at <https://www.finance.gov.au/resource-management/accountability/accountable-authority-instructions/> [accessed 9 November 2018].

96 For example, elements of the NAIF internal control framework are authored by Efic and the Department. On 1 August 2017, the NAIF Board formally adopted a number of its service provider's internal governance policies for activities and functions where there was no specific NAIF policy, procedure or framework. Under the Service Agreement, in the absence of a NAIF policy, Efic staff rely on the Efic policy: see paragraph 2.26. The Department is responsible for the Financial Information Protocol and the *Accounting Policy for Concessional Loans Provided by the Northern Australia Infrastructure Facility 2017–18*.

documents has not always been clear. In February 2018, an issue with policy document version control highlighted the importance of having a centralised accessible location for internal control documents, supported by a management process to safeguard against the NAIF and relevant Efic staff not having access to the current documents, or lacking awareness of where these documents are located. In September 2018, the NAIF created an Intranet site with relevant policies.

2.61 Although the NAIF Board remains responsible for the system, significant elements are managed by Efic staff providing corporate services under the Service Agreement in the key areas of financial controls, security controls and credit risk assessments. Whilst the Board determined that reliance on its service provider in these areas was appropriate, the blended system also increased the risk of insufficient clarity in relevant roles and responsibilities, for example:

- the delivery of agency security adviser services only covered physical security in one location, despite the NAIF's presence across four offices; and
- the blended system created inherent potential conflicts of duties for Efic staff providing services to the NAIF analogous to key executive roles — for example, when providing financial advice, negotiating annual payment schedules under the Service Agreement, providing legal advice, or in the management and consequences of Efic staff recusals from NAIF executive and Board processes.

2.62 The NAIF should consider using its internal audit and compliance programs to test the system of internal control in light of these risks.<sup>97</sup>

## Is the Service Agreement mechanism effective?

The Service Agreement and preceding inter-entity arrangement between the department and Efic were effective in supporting the establishment and operation of the NAIF, and had benefits for Efic in relation to demand management and the development of staff capability. Aspects of the NAIF's contract management of the Service Agreement could be improved to ensure ongoing value for money is maintained and evidenced.

2.63 From an early stage it was intended that Efic would provide corporate and grant services to support the establishment and operation of the NAIF. Engagement between the Treasury and Efic commenced from May 2015.

2.64 In the second reading speech introducing the Northern Australia Infrastructure Facility (Consequential Amendments) Bill 2016, the Minister for Resources, Energy and Northern Australia stated that the legislation 'does not mean that Efic will have to be used as a service provider for the NAIF, but amending the EFIC Act to allow Efic to undertake these services will ensure this is an option that is available to the NAIF. I am keen to utilise existing Commonwealth capabilities, achieve

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<sup>97</sup> Given the absence of a fully functional internal control system and a financial governance framework, the ANAO adopted a mainly substantive approach to audit testing for the 2017–18 financial statements, and recommended that the NAIF consider how best to obtain assurance from their service provider so as to provide assurance to the Board that appropriate systems of internal controls are in place. The NAIF stated that an internal audit covering the Service Agreement will be conducted in early 2019.

cost-effectiveness and provide for flexibility in the delivery of this important policy'.<sup>98</sup> This statement summarised the benefits of the arrangement for the NAIF.

2.65 On 15 March 2016, the department entered into a grant agreement with Efic to support the establishment and operation of the NAIF. The grant term was extended and amount increased from \$0.800 million by 31 August 2016 to \$1.280 million by 30 November 2016, and to a total of \$2.301 million by 31 March 2017.<sup>99</sup> Efic's governing legislation was also amended to allow Efic to provide and charge for services to the NAIF and similar entities.

2.66 On 5 April 2017, the NAIF entered into a Service Agreement with Efic for a range of corporate and grant services.<sup>100</sup> The Service Agreement is not published in full on the NAIF website, but a high level summary, including the types of services offered by Efic, was published on the NAIF and Efic websites.<sup>101</sup>

2.67 The Service Agreement provided that the parties must annually negotiate a payment schedule of charges, and that charges included under a payment schedule must be calculated and claimed on a cost recovery basis only. Invoices were presented on a monthly basis, substantiated with detailed extracts of expenses by line item, and approved for payment by the NAIF CEO on recommendation of the NAIF Chief of Staff.

2.68 The Service Agreement and preceding inter-entity arrangement was effective in supporting the establishment and operation of the NAIF and avoided some duplication of corporate and grant services capabilities. The Service Agreement also had benefits for Efic in relation to demand management and the development of staff capability.

2.69 The Service Agreement complied with most of the mandatory inclusions for an inter-entity agreement set out in the *model accountable authority instructions*<sup>102</sup>. The following gaps were noted:

- the agreement did not have a fixed term<sup>103</sup> — the usual mechanism for triggering periodic reassessment of value for money — but lasts indefinitely until terminated;<sup>104</sup>

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98 House of Representatives, *Official Hansard No. 5, 2016*, 17 March 2016, page 3444.

99 In August 2016, the NAIF Board agreed that the Service Agreement would be finalised following the appointment of an ongoing CEO, to ensure that the CEO was able to contribute to the negotiations on the NAIF's behalf on how the arrangement would be implemented.

100 Service Agreement between the Northern Australia Infrastructure Facility and the Export Finance and Insurance Corporation, dated 5 April 2017. Efic has subsequently entered into similar arrangements with the National Housing Finance and Insurance Corporation.

101 In April 2017, the NAIF and Efic discussed potential publication of the Service Agreement, but the parties agreed not to publish it due to concerns raised by Efic that publication could prejudice their future business negotiations for service provision to other entities.

102 Department of Finance, Resource Management Guide 206 *Model accountable authority instructions Corporate Commonwealth entities* (14 January 2019), available at <https://www.finance.gov.au/resource-management/accountability/accountable-authority-instructions>.

103 The NAIF stated that 'The NAIF and Efic did not set a fixed term for the SLA as one of the core services to be provided and leveraged through the SLA is the Portfolio Management Department services. This is the ongoing monitoring of obligations under the facility agreements including repayment of loans. It is noted that NAIF loans are expected to be long term potentially up to 30 years'.

104 The NAIF stated that value for money can potentially be tested through the statutory review of the operation of the Act and the annual budget negotiation process.



- the agreement required the parties to ‘use their best endeavours to develop, as soon as practicable, Key Performance Indicators (KPIs) relating to the availability of ICT and the performance of the Services’ — however, KPIs were not developed relating to the performance of corporate and grant services, meaning that there is no benchmark against which to objectively measure and assess the quality of service delivery; and
- the agreement provided for quarterly service management meetings with specific topics to be discussed — however, aside from ongoing operational contact, there was no evidence that quarterly service management meetings occurred or were documented.

## How are information governance requirements managed?

The NAIF’s information governance requires improvement to meet National Archives of Australia standards. The NAIF has implemented Freedom of Information and Information Publication Scheme processes. The NAIF published information about decisions to grant financial assistance as required by the Investment Mandate, but did not publish information about decisions not to grant financial assistance. The NAIF did not always disclose assessment criteria and processes, or non-confidential information about decisions.

2.70 The NAIF must exercise effective governance of information resources in accordance with section 15 of the PGPA Act, in line with specific legislation such as the *Archives Act 1983*, the *Freedom of Information Act 1982* (FOI Act) and the *Privacy Act 1988*, the *Information Management Standard* and principles issued by the National Archives of Australia (NAA), and Australian best practice government governance principles such as the non-binding *Principles on open public sector information* published by the Office of the Australian Information Commissioner (OAIC).

2.71 The NAIF did not implement a NAA-compliant information governance framework and did not use a NAA-compliant electronic data and records management system.<sup>105</sup>

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105 The NAIF stated in December 2018 that it has commenced implementation of an internal governance framework and electronic data and records management system as well as the records disposal authorities in order to meet the requirements of the Australian Government’s *Digital Continuity 2020* policy.

## Recommendation no.2

2.72 The NAIF develop an information governance framework, electronic data and records management system, and appropriate records disposal authorities in line with National Archives of Australia requirements.

**The Northern Australia Infrastructure Facility response: Agree.**

2.73 *NAIF has commenced engagement with the National Archives of Australia (NAA) on the implementation of an information governance framework, including data and records management, in line with NAA requirements. NAIF will progress this work over 2019 to meet the requirements of the Australian Government's Digital Continuity 2020 Policy.*

2.74 The NAIF Board approved an FOI policy on 10 August 2016, and regularly reviewed this policy in conjunction with legal advice. Reports provided by the NAIF to the OAIC indicated that FOI requests were processed in a timely manner.<sup>106</sup>

2.75 The NAIF published corporate information on its website as required by the Information Publication Scheme, but did not publish a proportion of its operational material relating to applications and assessments (refer to paragraph 2.32).<sup>107</sup> Instead, proponents needed to contact the NAIF directly in order to obtain the necessary information to make an application.

2.76 The NAIF must publish certain information within 30 business days of an Investment Decision.<sup>108</sup> The NAIF published information within statutory timeframes for all decisions to offer a Financing Mechanism made between 1 July 2016 and 1 December 2018. No information was published about decisions not to offer a Financing Mechanism during the same period, which

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106 The NAIF reported to the OAIC that the NAIF received 1,367 requests in 2016–17, and 12 requests in 2017–18. Over 1,300 of these requests were received over a two-week period in May and June 2017 and attributed by the NAIF to an automated FOI request generation programme hosted on a non-government organisation's website. The NAIF reports to the OAIC indicated 27 requests were withdrawn, and the NAIF refused 1,335 applications on the basis that a 'practical refusal reason' existed under the FOI Act, refused four applications for other reasons, granted access in part to 12 applications and granted access in full to one application.

107 Section 8A of the FOI Act states that 'An agency's operational information is information held by the agency to assist the agency to perform or exercise the agency's functions or powers in making decisions or recommendations affecting members of the public (or any particular person or entity, or class of persons or entities)'. The FOI Act provides by way of example 'The agency's rules, guidelines, practices and precedents relating to those decisions and recommendations'.

108 Subsection 17(2) of the Investment Mandate. Section 4 of the Investment Mandate defines the term 'Investment Decision' to mean 'a decision by the Board to offer, or not to offer, a Financing Mechanism'.

reduced the opportunity for potential applicants, the public and the Parliament to understand the assessment process and the NAIF's interpretation of the criteria for financial assistance.<sup>109</sup>

2.77 The NAIF did not always disclose:

- many of its assessment criteria and processes;
- transaction pipelines and project summaries, even when applicants consented or themselves lawfully disclosed this information to the market and media; or
- non-confidential information about decisions, public benefit assessments, environmental assessments and Indigenous engagement strategies.

2.78 Whilst the NAIF took the view that a default confidentiality position was appropriate, this approach to disclosure limited the opportunities for public scrutiny of decision-making. In July 2018, the Senate Economics References Committee made four recommendations relating to transparency and publication of information in the final report of its inquiry into the governance and operation of the NAIF.<sup>110</sup> In December 2018, the NAIF stated it has made an active policy change towards greater disclosure of information about proposals that have progressed to the due diligence phase of the NAIF assessment process.

### Recommendation no.3

2.79 The NAIF publish more information about decisions, public benefit assessments, environmental assessments and Indigenous engagement strategies.

**The Northern Australia Infrastructure Facility response: Agree.**

2.80 *Taking into account the requirements of NAIF's legislative framework to uphold both public accountability and appropriately maintain commercial in confidence information NAIF commits to, at a project or portfolio level as appropriate, continue to publish more information, by way of case studies, about its Investment Decisions together with examples of expected public benefit, Indigenous engagement strategies and environmental outcomes from NAIF investments.*

109 During the period 1 July 2016 to 1 December 2018, the NAIF Board made final Investment Decisions about six formal Investment Proposals—in each case to offer a Financing Mechanism. In the same timeframe, the ANAO identified 24 projects where the NAIF Board was informed of a decision by NAIF staff acting under an authorisation from the NAIF Board contained in Annexure 4 of the NAIF Board-approved Application and Approval Procedure to 'notify the relevant Project Proponent that the NAIF Board would likely exercise its discretion to decline an Investment Proposal' and mark the proposal as 'not proceeding' on the transaction pipeline. The ANAO took the view that these were in effect decisions not to offer a Financing Mechanism. The NAIF stated 'The Board were never asked to make any decision on the papers which outlined this feedback. The Board was only provided these papers for information purposes' and also stated 'NAIF maintains its position that no Investment Decisions to not offer financial assistance have been made and accordingly the requirement to publish information on an Investment Decision, to not offer finance, has not been triggered'.

110 Recommendations 3, 6, 9 and 10 of the Senate Economics References Committee, *Governance and operations of the Northern Australia Infrastructure Facility (NAIF)*, Canberra, 6 July 2018, available from [www.aph.gov.au/Parliamentary\\_Business/Committees/Senate/Economics/NAIF/Final\\_Report](http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/NAIF/Final_Report) [accessed 9 November 2018]. The report included a minority report by Government members. The NAIF made a submission to the Senate Inquiry (available as submission 43).

### 3. Integrity and transparency

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#### Areas examined

This chapter examines whether the NAIF implemented arrangements that support effective integrity and transparency in relation to its operations.

#### Conclusions

The NAIF did not implement effective arrangements to support integrity and transparency throughout all elements of its operations. The NAIF had an appropriate integrity policy framework and the management of conflicts of interest was effective, however the NAIF adopted but did not adequately implement the Protective Security Policy Framework. Arrangements for engaging with stakeholders were generally effective. Arrangements for ensuring the integrity of decision support processes were not effective, with insufficient evidence that all applicants were evaluated in a consistent manner throughout the assessment stages. The Board placed reliance on the CEO to present projects for Board consideration, and the Board has not made any Investment Decisions to refuse financial assistance for the applications presented.

#### Recommendations

The ANAO has recommended that the NAIF:

- cease the use of all non-official email accounts and servers to conduct official business;
- implement a more rigorous and transparent decision-making process; and
- revise its performance measures and targets to provide clearer accountability.

#### Does the NAIF have in place a sound integrity framework?

The NAIF had an appropriate integrity policy framework. The integrity compliance program was largely reliant on induction training and self-reporting, which could be supplemented by ongoing training, pro-active compliance reviews and internal audit coverage.

3.1 The *Public Governance, Performance and Accountability Act 2013* (PGPA Act) imposes governance, risk oversight and management obligations on the NAIF, and NAIF Board members and staff are subject to the general duties of officials under the PGPA Act.<sup>111</sup> The NAIF Board must take all reasonable measures to prevent, detect and deal with fraud relating to the entity.<sup>112</sup>

3.2 The NAIF Board Charter and BARC Charter contain appropriate governance provisions in relation to integrity, with assigned roles, responsibilities and oversight mechanisms. The Board

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111 These include a duty of care and diligence (section 25); a duty to act honestly, in good faith and for a proper purpose (section 26); a duty in relation to use of position (section 27); a duty in relation to use of information (section 28); and a duty to disclose interests (section 29).

112 *Public Governance, Performance and Accountability Rule 2014*, section 10. Relevant Australian best practice government governance principles include the Commonwealth Fraud Control Policy, and Resource Management Guide 201 *Preventing, detecting and dealing with fraud*, published by the Attorney-General's Department. Relevant Australian best practice corporate governance for commercial financiers includes Prudential Standard CPS 520 *Fit and Proper* and Principle 3 of the *ASX Corporate Governance Principles and Recommendations*.

Charter requires the NAIF Board to ‘maintain corporate governance practices for NAIF’s responsible and ethical compliance with relevant regulatory requirements and governance standards’. In June 2017, the Board Charter was amended to include in the Chief Executive Officer’s (CEO) responsibilities the need to ‘instil in NAIF a culture of trust, honesty and integrity in relationships with those stakeholders both internal and external to NAIF’.<sup>113</sup>

3.3 As part of its suite of governance policies, the NAIF Board was provided at its first meeting on 10 August 2016 with a number of draft integrity-related policies based on existing Efic policies. The Board adapted these policies to the needs of the NAIF, approved them by 30 June 2017, and then regularly reviewed these policies, including obtaining legal advice. In February 2018, the NAIF Board approved a Fraud Control Policy, consistent with the requirements of section 10 of the *Public Governance, Performance and Accountability Rule 2014*.

3.4 Other NAIF integrity policies have been established to cover anti-corruption, code of conduct, staff security trading, public interest disclosure and incident reporting. The NAIF maintains a regularly updated list of trading-embargoed securities (the Embargo List)<sup>114</sup> and an issues register,<sup>115</sup> together with guidance about the recording of transaction entities on the Embargo List. From March 2018, incidents were reported to the Board and the BARC in a quarterly NAIF Risk Management and Compliance (RMAC) Report. The March and September 2018 RMAC Reports included reporting (and nil reports) against each of the 12 NAIF Key Enterprise Risks, and a NAIF Incident Register Table was added to the September 2018 report consolidating this information. The Enterprise Risk Management Forum, established in September 2018 and attended by the executives responsible for each of the key enterprise risks, is required to review incident reports to ensure appropriate resolution.

3.5 The NAIF’s compliance training program consists of a combination of induction, online and face-to-face training. For the 2017–18 financial year, the NAIF relied on Efic to provide training for NAIF employees. With the commencement of the NAIF Risk and Compliance Manager, this was supplemented by a tailored NAIF compliance program. Evidence of monitoring staff completion of training in the 2017–18 financial year was limited. Since September 2018, additional monitoring has been established including through annual staff declarations reflecting completion of integrity policy training by 28 NAIF staff.

3.6 The NAIF’s integrity compliance program is reliant on staff training and self-reporting. The NAIF also uses the compliance plan to monitor NAIF policy compliance with legislative requirements. As the NAIF compliance program develops, the NAIF should supplement training and declarations with compliance checks of trading in securities on the Embargo List and internal audit coverage.

3.7 The *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML-CTF Act) imposes identity verification and reporting obligations on designated financial services entities, and

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113 The NAIF stated that this was one of several changes made to the Charter as part of the annual review, which had initially been drafted based on the Efic Charter.

114 Transaction entities in which the NAIF is in possession of insider information and therefore where NAIF staff are subject to restrictions regarding associated securities trading.

115 The NAIF stated that this register is used to record reported instances of all issues within the organisation, including non-compliance with integrity policies.

since 18 December 2017 these obligations applied to the NAIF.<sup>116</sup> On 24 January 2018, the NAIF Board considered draft AML-CTF procedures which were based on the Efic policy and developed following consultation with the department, State and Territory jurisdictions and the Australian Transaction Reports and Analysis Centre.<sup>117</sup> The NAIF Board should consider including testing on the effectiveness of AML-CTF controls in its internal audit plan.

## Does the NAIF manage conflicts of interest effectively?

The management of conflicts of interest was effective. The NAIF Board approved a conflicts of interest policy that applied to Board members and staff. The NAIF Board implemented sound declaration practices at Board meetings, and sound recusal practices at Board meetings and in Board papers. Declarations were more likely to be made after conflict checks were conducted or when an application reached the due diligence stage, indicating that there would be value in conducting conflict checks for all proposals from the earliest stage.

3.8 The NAIF Board, CEO and staff are subject to various rules about their use of information and duty to disclose material personal interests that relate to the affairs of the NAIF.<sup>118</sup>

3.9 While the appointment of individuals with relevant backgrounds to a government board will always have potential for conflicts of interest, the Minister for Resources and Northern Australia has publicly stated that ‘the potential for conflicts of interest was live here given that northern Australia is a relatively small economy’.<sup>119</sup>

3.10 There has been significant and sustained public and Parliamentary interest in conflicts of interest management by the NAIF Board, with Senate Questions on Notice as early as August 2016,

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116 As a result of Declaration 2 of 2017 under section 248 of the AML-CTF Act (dated 18 December 2017), available from [www.austrac.gov.au/businesses/exemptions-and-modifications/exemptions-granted](http://www.austrac.gov.au/businesses/exemptions-and-modifications/exemptions-granted).

117 The approval of the draft AML-CTF procedures was not recorded in the NAIF Board or BARC papers, but subsequent Board decisions and NAIF practices appear to have taken AML-CTF compliance into account. The NAIF provided the ANAO with written confirmation from current Board members who were present at the meeting that the resolution discussed at that meeting was passed.

118 *Public Governance, Performance and Accountability Act 2013*, section 29. Other disclosure and recusal requirements around material personal interests are contained in Division 2 of the *Public Governance, Performance and Accountability Rule 2014*, with interpretive guidance in the Department of Finance Resource Management Guide 203 *General duties of officials*. Similar requirements are best practice for Commercial Financiers, such as directorial independence rules in Prudential Standard CPS 510 *Governance*, recommendation 1.3 of the *ASX Corporate Governance Principles and Recommendations*, and disclosure and recusal requirements in the *Corporations Act 2001*.

119 Senate Economics Legislation Committee, *Official Committee Hansard – Estimates*, 1 June 2017, testimony of Senator Canavan, page 166–7, available from [https://www.aph.gov.au/Parliamentary\\_Business/Senate\\_Estimates/economicsctte/estimates/bud1718/index](https://www.aph.gov.au/Parliamentary_Business/Senate_Estimates/economicsctte/estimates/bud1718/index) [accessed 9 November 2018]. Senator Canavan went on to add ‘I know from talking to the NAIF from the very early days that there was always a lot of effort to make sure that their conflict of interest policies were very robust, and I have full confidence that they have put them in place in compliance with the law and in compliance with the general expectation that is on boards and directors to comply with conflict of interest policies’.

at least one Freedom of Information request for relevant Board minutes, discussion during Senate Estimates in 2017<sup>120</sup>, submissions to the Senate Inquiry<sup>121</sup>, and in the 2018 Senate Report.

3.11 On 30 November 2016, the NAIF Board approved a conflicts of interest policy that applied to Board members and staff. The Board sought legal review of this policy in June 2017, approved revised policies on 20 June 2017 and 14 June 2018, and commissioned an internal audit that reported in August 2018 on conflicts of interest policy and practice. Directors were asked to complete a Personal Interest Disclosure at the commencement of each financial year, and to review and check their disclosures.

3.12 The NAIF Board adopted a definition of ‘material personal interest’ that required declarations of potential and apparent as well as actual conflicts, conflicts of duty, immaterial interests, and non-personal interests.

3.13 The NAIF Board implemented sound declaration practices at Board meetings, with no apparent contravention of PGPA Act or Rule requirements, and sound recusal practices at Board meetings and in Board papers.

3.14 The Board Secretary conducted conflict checks for particular projects by writing to all Board members to invite declarations and recusals for that project. While information about proposals was presented to the Board throughout the assessment process, for example through regular transaction pipeline reports, declarations were more likely to be made after conflict checks were conducted or when a proposal reached the due diligence stage:

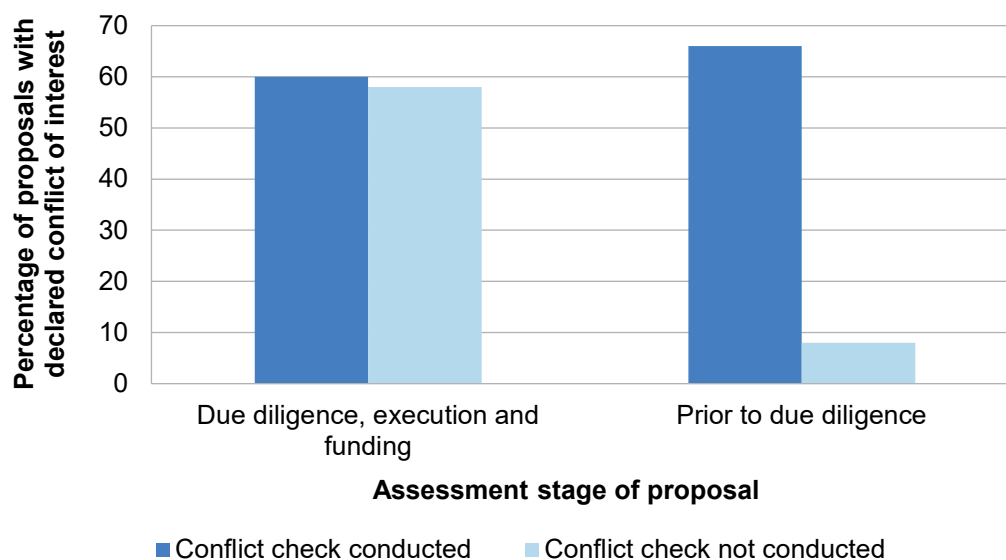
- conflict checks conducted for 45 per cent of proposals at the due diligence, execution, or funding stages resulted in declarations in 60 per cent of these checks;
- where no checks were conducted for the remaining 55 per cent of proposals at these stages, declarations were made for 58 per cent of these proposals;
- conflict checks conducted for 4 per cent of proposals at stages prior to due diligence resulted in declarations in 66 per cent of these checks; and
- where no checks were conducted for the remaining 96 per cent of proposals at stages prior to due diligence, there were only declarations for 8 per cent of those proposals.

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120 Senate Economics Legislation Committee, *Official Committee Hansard – Estimates*, 1 June 2017, from page 161, available from [https://www.aph.gov.au/Parliamentary\\_Business/Senate\\_Estimates/economicsctte/estimates/bud1718/index](https://www.aph.gov.au/Parliamentary_Business/Senate_Estimates/economicsctte/estimates/bud1718/index) [accessed 9 November 2018].

121 For example, submissions 42, 55, 60 and 102 to the Senate Inquiry, available from [www.aph.gov.au](http://www.aph.gov.au). The NAIF submission at submission 43 contains details of its conflict of interest management.

**Figure 3.1: Effectiveness of conflict checks**



Source: Analysis of NAIF Board papers, NAIF Register of Conflicts and transaction pipeline reports to 22 August 2018.

3.15 Conflict checks were an effective means of prompting declarations before the due diligence stage, with an eightfold increase in declarations following a conflict check. The NAIF should consider conducting conflict checks for all proposals from the earliest stage, and these conflict checks should cover proponents and their equity partners and advisers.

3.16 Staff induction training included conflict of interest training that directed staff to relevant policies. An internal audit found in August 2018 that there was no refresher or reinforcement training ('due to the majority of NAIF staff having been at NAIF for less than 12 months') and no requirement for attestations or annual compliance declarations. The audit report recommended 'compulsory annual conflicts of interest reinforcement training for all NAIF Officers' and annual declarations, to which management agreed and scheduled face-to-face training in October 2018.

## Are effective security controls in place?

The NAIF adopted but did not adequately implement the Protective Security Policy Framework. The NAIF relied on service providers' security risk management policies and practices, and more recently approved policies specific to its own circumstances in areas such as business continuity. The NAIF did not use security classification and dissemination limiting markers on official documents. Some NAIF Board members used non-official email accounts to conduct official business and make decisions on projects with commercial and political sensitivities.

3.17 The NAIF recruits and manages executives and other staff with access to market sensitive information. As an assessor of potential government financing to major infrastructure projects, the NAIF manages high value information assets of commercial and political sensitivity. The NAIF also faces potential risks to the physical security of people and property across a number of locations arising from its actual or perceived involvement with controversial projects and proponents.

3.18 The NAIF Board adopted but did not adequately implement the Protective Security Policy Framework (PSPF), which represents a better practice standard for a corporate Commonwealth



entity.<sup>122</sup> The PSPF provided the NAIF with an effective framework for security risk management and controls around security governance, personnel security, information security and physical security.

3.19 The NAIF Board relied on its service providers' security risk management policies and practices, and approved a NAIF-specific Business Continuity Management Policy and Recovery Plan on 14 June 2018, and a Corporate Information Security Policy in October 2018. The service provider provided some but not all agency security adviser and information technology security adviser functions. Since March 2018, the NAIF provided the Board with regular updates on security risk management in quarterly Risk Management and Compliance reports, and prior to this updated the Board through the CEO report and specific update papers.

3.20 The NAIF sub-leased each of its Sydney, Brisbane, Cairns and Perth offices from separate Commonwealth entities and relied on existing physical security arrangements provided by each of these entities, combined with ad hoc arrangements for off-site meetings.

3.21 The NAIF relied on its service provider for personnel security, including employment screening. In areas that were not covered by the service provider, the NAIF did not maintain separate policies or practices, for example informing the Australian Government Security Vetting Agency of personnel security clearance maintenance or employee departure. The NAIF stated in relation to maintaining security clearances that 'the NAIF leverages and adopts Efic's policies and practices where a NAIF specific policy is not in place'. The NAIF also relied on its service provider to deliver a secure electronic information environment, including information technology services and regular vulnerability testing.

3.22 The NAIF did not use security classification and dissemination limiting markers on official documents as required by the PSPF, which can increase the risk that information is handled inappropriately.<sup>123</sup>

3.23 NAIF Board members used non-official email accounts to conduct official business, including sharing commercially sensitive information and making Investment Decisions, with records stored on private servers or consumer-grade email services. The NAIF Board decided to cease this practice at its 22 August 2017 meeting; however, some Board members continued to use non-official email accounts to conduct official business as recently as June 2018.<sup>124</sup> By October 2018, the three most

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122 The PSPF represents better practice for corporate Commonwealth entities and wholly-owned Commonwealth companies: see <https://www.protectivesecurity.gov.au/Pages/default.aspx>. In addition, the NAIF is separately required by subsection 17(1) of the Investment Mandate to have regard to Australian government best practice governance principles, and this includes the PSPF.

123 Australian Cyber Security Centre, *Australian Government Information Security Manual*, February 2019 (ISM): see <https://acsc.gov.au/infosec/ism/index.htm>. The ISM states that 'All electronic information needs to be marked with an appropriate protective marking. This ensures that appropriate security controls are applied to the information and helps prevent unauthorised information being released into the public domain': security control 0273, page 112. The NAIF stated that 'the PSPF represents better practice for corporate Commonwealth entities such as NAIF. As a better practice NAIF has regard to its framework and principles but is not required to legally comply with it'.

124 The NAIF stated that 'Information provided by proponents is regarded as commercial in confidence and NAIF has in place systems in which to control the dissemination and management of this information'. However, the use of non-official emails compromised the integrity of these control systems and placed commercially sensitive information on non-government servers potentially accessible to non-government IT personnel.

active Board members sending emails to the NAIF from their non-official accounts had respectively sent around 7100, 1600 and 1500 emails.<sup>125</sup> Guidance from the Australian Signals Directorate states that ‘given the uncertainty around the security provided by consumer-grade email services, particular care should be taken when choosing to use such services, especially when using the services for sensitive business transactions’.<sup>126</sup> The deletion of Commonwealth records from non-official email accounts could also contravene the record keeping requirements of the *Archives Act 1983*.

#### Recommendation no.4

3.24 The NAIF cease the use of all non-official email accounts and servers to conduct official business.

**The Northern Australia Infrastructure Facility response:** *Agree.*

3.25 *NAIF has ceased the use of non-official email accounts, for any NAIF business. This does not extend to stakeholder or proponent engagement via the email accounts provided by those parties.*

#### Are effective arrangements in place to engage with stakeholders?

The NAIF implemented arrangements for engaging with stakeholders which were generally effective. The Board exercised regular oversight of stakeholder engagement. While the NAIF conducted regular consultation with government stakeholders with assistance from the department, providing more complete information to these stakeholders would help to identify and manage shared risks. The NAIF has draft bilateral protocols for statutory consultation with State and Territory jurisdictions under the Master Facility Agreements, and with Infrastructure Australia.

3.26 The NAIF’s stakeholder engagement requirements are set out in the PGPA Act, the NAIF Act and the Investment Mandate, including with State and Territory jurisdictions, Infrastructure Australia, and other relevant government stakeholders.<sup>127</sup>

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125 In response to concerns raised by the ANAO, on 19 December 2018 the NAIF stated that the NAIF Board had resolved at its Board meeting on 29 November 2018 for ‘Board members to arrange the closure of all personal email accounts being used by them for NAIF business’.

126 Australian Cyber Security Centre, *Using Consumer-Grade Email Services*, January 2019: see [https://acsc.gov.au/publications/protect/Consumer\\_Grade\\_Email.pdf](https://acsc.gov.au/publications/protect/Consumer_Grade_Email.pdf).

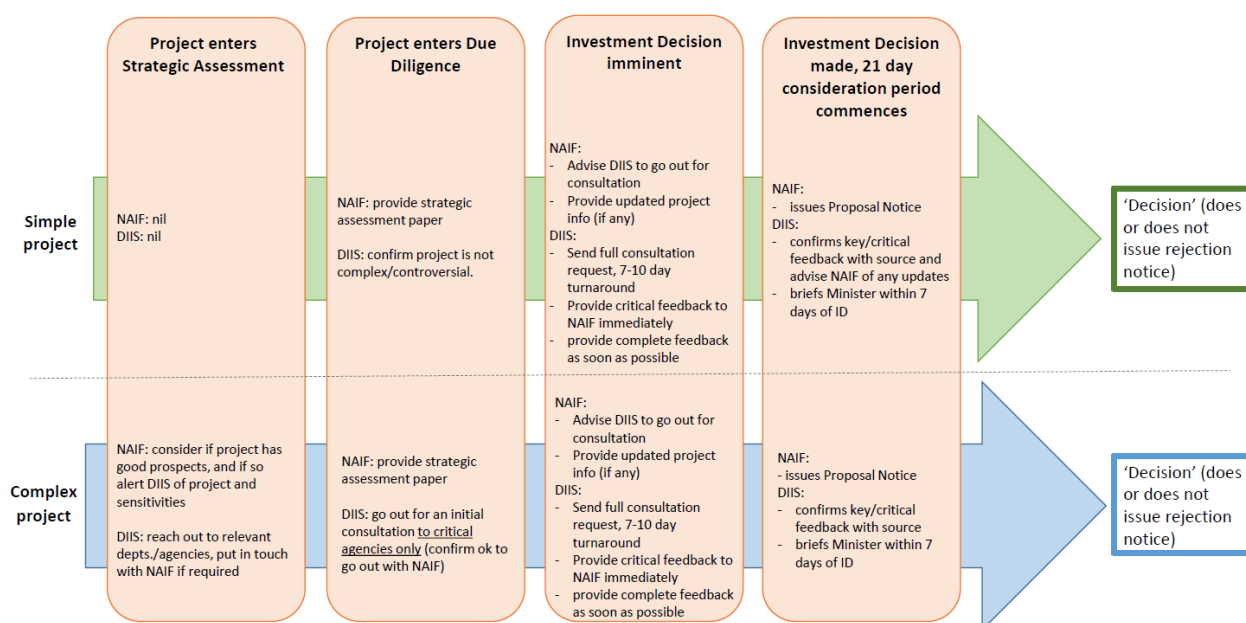
127 The requirements for stakeholder engagement are found in: sections 17 and 18 of the *Public Governance, Performance and Accountability Act 2013*; sections 7, 9 and 11 of the *Northern Australia Infrastructure Facility Act 2016*; and the Investment Mandate. The Investment Mandate requires that the NAIF Board must: have regard to the potential effect of projects on other infrastructure and the Australian infrastructure financing market (subsection 7(2)); prevent the Commonwealth overall having the majority financial risk in a project (subsection 12(1)); consult relevant State and Territory jurisdictions (section 13); consult Infrastructure Australia and relevant government stakeholders (section 14); not provide financial assistance to projects that have not received all relevant regulatory, environmental and Native Title approvals (section 15); and not act in a way that is likely to cause damage to the Commonwealth Government’s reputation, or that of a relevant State or Territory government (section 16).

3.27 The NAIF Board exercised regular oversight of stakeholder engagement activities.<sup>128</sup> The NAIF conducted regular consultation with Australian, State and Territory government stakeholders, including early engagement on applications. The NAIF held monthly meetings with State and Territory jurisdictions on the transaction pipeline.

3.28 The department assisted the NAIF to identify and consult other Australian Government departments to meet its stakeholder engagement requirements from the strategic assessment stage through to the ministerial consideration period, as illustrated in Figure 3.2.

**Figure 3.2: Stakeholder consultation process by the NAIF and the department**

### NAIF consultation – process map



Source: Department of Industry, Innovation and Science, October 2018.

3.29 The consultation process provided government stakeholders with high-level pipeline reports and abbreviated project summaries. While summaries may be helpful in providing an overview, more complete information could assist other agencies to identify and manage shared risks in a proposed grant of financial assistance, particularly for projects with commercial and political sensitivities.

<sup>128</sup> The Board identified key stakeholders through a market engagement plan in September 2016, and in June 2017 in a stakeholder engagement plan. By November 2017, the NAIF began to address concerns about their approach to communication with key stakeholders by developing a government engagement strategy including short, medium and long-term deliverables. In February 2018, the Board considered an update to this strategy including advice on measurement against goals, objectives and immediate deliverables. The Board considered this strategy again in April 2018, and emphasised the importance of announcements—and announcements of decisions in particular—to NAIF's communications narrative and stakeholder engagement in the near-to-medium term.

3.30 The NAIF should develop a bilateral protocol with the department to clarify respective roles and responsibilities and information requirements to support statutory consultation and shared risk management with Australian Government stakeholders.

3.31 The NAIF prepared draft bilateral protocols for statutory consultation with State and Territory jurisdictions<sup>129</sup> under the Master Facility Agreements — covering the origination, assessment, execution and administration of grants of financial assistance — and with Infrastructure Australia.

3.32 The NAIF Board should put in place mechanisms to seek and act on stakeholder feedback and review the effectiveness of stakeholder engagement. While there was broad support for the NAIF's statutory purpose and general satisfaction with the frequency of engagement among stakeholders, common themes from stakeholder consultations during the audit identified that the NAIF could improve coordination and collaboration with government stakeholders through:

- seeking input from government stakeholders to better assist with project prioritisation by the NAIF within each jurisdiction;
- continuous disclosure and better information sharing with government stakeholders; and
- greater willingness to understand the perspectives and needs of government stakeholders including approval processes and timeframes, and the potential consequences of NAIF decisions on those stakeholders.<sup>130</sup>

## Are arrangements effective in ensuring the integrity of decision support processes underpinning investment decisions?

The arrangements for ensuring the integrity of decision support processes were not effective. The NAIF Board placed reliance on the CEO to determine whether a project progressed to the strategic assessment stage in circumstances where it is unclear why certain projects were presented to the Board and not others, and the Board has not made any Investment Decisions to refuse financial assistance for the applications presented to it. There was insufficient evidence that all projects were evaluated in a consistent manner throughout the assessment stages, and the NAIF sent letters of support or term sheets before applicants provided

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129 The NAIF stated in December 2018 that it held workshops with the Department and each of the State and Territory jurisdictions, and the latest drafts of the State and Territory jurisdictions protocols were provided to each of the jurisdictions on the following respective dates: Western Australia in January 2018, Queensland in February 2018 and the Northern Territory in April 2018. The NAIF stated that 'draft written protocols are being tested against practical examples by way of continuous improvement' and 'None of the Jurisdictions has been ready to finalise the protocols yet as they and NAIF want to work through live examples before they do that. Not having them finalised at this stage has not in any way hindered progress of projects or created uncertainty for the jurisdictions or other key stakeholders. The jurisdictions have raised no particular issues with NAIF as a consequence of the protocols not being in final form'.

130 The NAIF stated that 'NAIF maintains its position that it extensively consults with, seeks priorities of and shared significant information with its jurisdictions and other stakeholders' and referred to 'the challenging circumstances, including the stakeholder environment in which the NAIF operates. Examples, operating in environments where matters are outside the control of the NAIF'. The NAIF further stated that 'NAIF has gained a fuller understanding of these matters as we work through live examples particularly of Investment Decisions and the process through to financial close'.

appropriate supporting documentation. There was no apparent consistency in how site visits were planned, conducted, documented or reported to the NAIF Board.

3.33 The NAIF has an obligation to utilise public resources appropriately, and therefore the integrity of decision support processes is critical in enabling the NAIF Board to demonstrate that it is making Investment Decisions that achieve the objectives of the NAIF and maintain the reputation of the Australian Government. Decisions, or the absence of decisions, at every stage of the process are judicially reviewable as decisions under an enactment.<sup>131</sup>

3.34 On 7 October 2016, the NAIF Board approved an Application and Approval Procedure, which set out 'how applications for NAIF funding will be managed' through the assessment stages, and revised this procedure on 6 April 2017. The NAIF did not publish the full procedure, but did publish the high-level summary information contained at Annexure 2 to the procedure.

3.35 The NAIF assessed proposals and applications for financial assistance through the decision-making stages in the transaction pipeline as illustrated at Figure 1.2. As of 22 August 2018, the NAIF transaction pipeline contained 266 projects at various stages of assessment, and was diverse in terms of geography and industry sector.

3.36 The 2016 Investment Mandate, which applied between May 2016 and April 2018, stated that to be eligible for financial assistance, project proponents needed to meet all seven mandatory criteria:

- (a) the proposed Project involves construction or enhancement of economic infrastructure;
- (b) the proposed Project will be of public benefit;
- (c) the proposed Project is unlikely to proceed, or will only proceed at a much later date, or with a limited scope, without financial assistance;
- (d) the Project is located in, or will have a significant benefit for, Northern Australia;
- (e) Facility's loan monies are not the majority source of debt funding;
- (f) the loan will be able to be repaid, or refinanced; and
- (g) the Project Proponent must provide an Indigenous engagement strategy.

3.37 The 2016 Investment Mandate further stated that preference would be given to projects that met one or both of the non-mandatory criteria:

- (a) the proposed Project is seeking financing from the Facility for an amount of \$50 million or more; and
- (b) there is an identified need for the Project.

3.38 The 2018 Investment Mandate, which has applied since May 2018, states that to be eligible for financial assistance, the Board must be satisfied that the Investment Proposal meets all of the following five mandatory criteria:

- (a) the proposed Project involves construction or enhancement of Northern Australia economic infrastructure;

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<sup>131</sup> *Administrative Decisions (Judicial Review) Act 1977*. The relevant enactments are the *Northern Australia Infrastructure Facility Act 2016* and the Investment Mandate.

- (b) the proposed Project will be of public benefit;
- (c) the Project is located in, or will have a significant benefit for, Northern Australia;
- (d) the loan will be able to be repaid, or refinanced; and
- (e) the Project Proponent must provide an Indigenous engagement strategy.

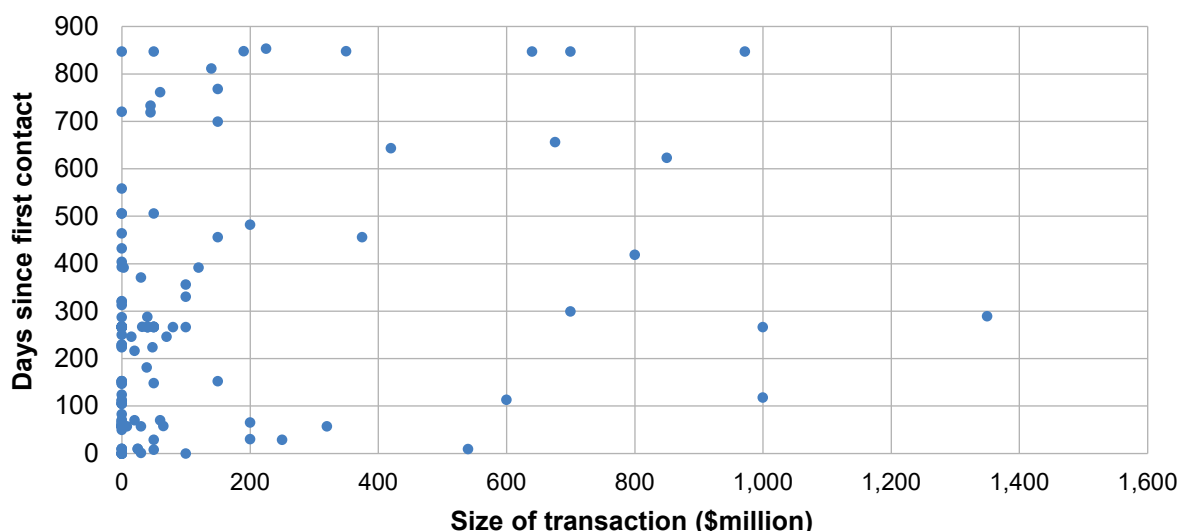
### Enquiry and preliminary assessment stages

3.39 On its website, the NAIF encouraged prospective applicants to contact the NAIF ‘to discuss any potential projects prior to commencing, or submitting, any formal information’, and provided an investment proposal template.<sup>132</sup>

3.40 The Application and Approval Procedure states that ‘The Transaction Team will review and undertake a preliminary assessment of the Enquiry Information provided by the Project Proponent. The Transaction Team will consult with the NAIF CEO on the potential suitability of the Project for NAIF financial assistance and provide nonbinding feedback to the Project Proponent’. The CEO consultation process determined whether a project progressed to the strategic assessment stage for presentation to the NAIF Board.

3.41 The NAIF did not always actively manage projects at the enquiry and preliminary assessment stages to an outcome — either presentation to the Board for strategic assessment, or a refusal to grant financial assistance. As a result, projects remained at the enquiry and preliminary assessment stages for up to 850 days after first contact, as illustrated in Figure 3.3, while others were selected for strategic assessment relatively quickly.

**Figure 3.3: Wait time and size of projects awaiting strategic assessment**



Source: NAIF, Pipeline as at 22 August 2018. For visual clarity, three outliers have been removed. The figure does not illustrate the wait time and size of applications that progressed to strategic assessment or beyond.

3.42 Analysis obtained by the NAIF suggested that it takes between two and three years for a project to reach financial close and potentially longer for proponent-led or higher risk projects. As at 22 August 2018, the NAIF transaction pipeline included 139 projects at the enquiry and

<sup>132</sup> NAIF website, <https://naif.gov.au/project-assessment-process/assessment-process/> [accessed 9 November 2018]. The template is a requirement of section 17(3) of the Investment Mandate.

preliminary assessment stage. The NAIF Board should establish planning to ensure that a decision to grant or refuse financial assistance can be made in relation to all projects in the pipeline more expeditiously, and in particular before the 30 June 2021 statutory decision-making deadline.

### Strategic assessment stage

3.43 At the strategic assessment stage, proponents were asked to submit further information including a detailed business plan, project financial analysis and other supporting evidence that the application meets the assessment criteria.<sup>133</sup> At the conclusion of this stage, the NAIF CEO presented the NAIF Board with a Strategic Assessment Paper (SAP) and requested the Board agree that the project has the potential to meet all the mandatory criteria in the Investment Mandate and agree for the NAIF to commit resources to due diligence. At this stage, a project may meet some but not all criteria.

3.44 The NAIF CEO selected applications for strategic assessment by the NAIF Board under the NAIF Board's Application and Approval Procedure.

3.45 Alternatively, in circumstances defined in Annexure 4 to the Application and Approval Procedure, the NAIF CEO should notify the proponent that the Board would 'likely exercise its discretion to decline an Investment Proposal'.<sup>134</sup> These circumstances included if the project:

- 'does not involve the construction or enhancement of Northern Australia economic infrastructure' (mandatory criterion 1);
- 'does not have sufficient public benefit to Northern Australia' (mandatory criterion 2); or
- 'lacks an Indigenous Engagement Strategy' (mandatory criterion 7, later 5).

3.46 Annexure 4 operated as a 'soft refusal' process by inviting an applicant to revise or withdraw their application, and an applicant so notified would be marked as 'not proceeding' or 'inactive' in the transaction pipeline. The procedure required that the NAIF Board must be notified and given the opportunity to endorse the CEO's actions at the next Board meeting — in practice, this notification occurred through updates to the transaction pipeline.

3.47 A review of projects in the transaction pipeline during the first two years of the NAIF's operations before the Investment Mandate was amended (1 July 2016 to 20 April 2018)<sup>135</sup> identified:

- 24 projects notified under the Annexure 4 process and marked as not proceeding; and
- 27 projects selected for presentation to the NAIF Board for strategic assessment.

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133 The NAIF stated that in practice this level of detail is not always available from the proponent at this stage.

134 Annexure 4 to the NAIF Application and Approval Procedure states that 'This policy outlines the circumstances where the NAIF CEO in administering the Northern Australia Infrastructure Facility should notify the relevant Project Proponent that the NAIF Board (the Board) would likely exercise its discretion to decline an Investment Proposal'.

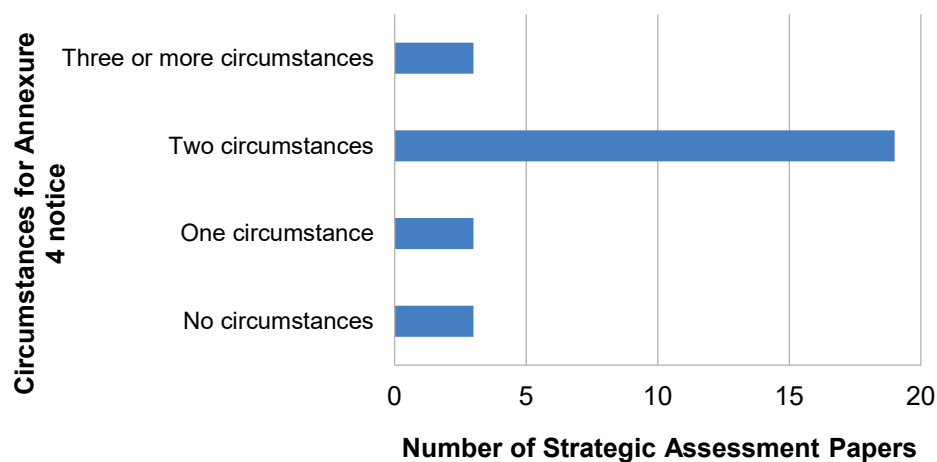
135 The NAIF Board adopted a broader definition of economic infrastructure in February 2017; this was later reflected in the Explanatory Statement to the revised Investment Mandate in April 2018.

3.48 A review of 28 SAP for the 27 projects selected for presentation to the Board<sup>136</sup> found that the NAIF had assessed that 13 projects met no more than one or two of the seven mandatory criteria applicable at the time of Board presentation (including being located in northern Australia).

3.49 It was not clear from the SAP why projects that met one or two mandatory criteria were presented to the NAIF Board to move forward to due diligence in preference to projects in the transaction pipeline not presented to the NAIF Board that also appeared to meet one or two criteria, including the 24 projects that were notified under the Annexure 4 process and marked as not proceeding.

3.50 For 25 of 28 SAP presented to the NAIF Board, the material contained in the NAIF's assessments of projects in the SAPs indicated that the project met the circumstances for an Annexure 4 notification that the Board would 'likely exercise its discretion to decline an Investment Proposal' (e.g. not assessed as economic infrastructure; no public benefit assessment; no Indigenous engagement strategy, etc). The CEO recommended to the NAIF Board that these projects move forward to due diligence (see Figure 3.4).

**Figure 3.4: Number of Annexure 4 circumstances in SAP**



Source: NAIF Board papers between 1 July 2016 and 20 April 2018

3.51 The NAIF stated in December 2018 that the 'decision will always be a matter of expert judgement by the NAIF Executive', but that 'NAIF has undertaken to develop a framework protocol for procedure to select a project for SAP'.

3.52 A review of SAPs and corresponding Board decisions identified that SAPs:

- were presented to the Board in a consistent format;

136 Two separate SAP documents were presented to the Board at different phases for one specific project.



- provided summaries of the project but did not usually present to the Board the complete application and supporting evidence provided by the proponent in support of their project;<sup>137</sup> and
- recommended the Board agree to projects moving to due diligence on the basis that certain criteria were met, even where the detail of the SAPs indicated that the criteria were either not met or not yet assessed.<sup>138</sup>

3.53 From the NAIF Board papers between 1 July 2016 and 30 September 2018, nine examples were identified where the NAIF Board agreed to send letters of support and indicative term sheets to assist applicants to solicit potential investors and financiers. In all nine cases, letters of support or term sheets were issued before the applicant provided the NAIF with a final application and supporting evidence, before the application was assessed as meeting the criteria for a grant of financial assistance, and before the NAIF completed due diligence checks. While non-binding, there is a risk that Australian and international investors and commercial financiers could act in reliance on letters of support and indicative term sheets from an Australian Government entity, and a corresponding risk of reputational damage to the Australian Government.<sup>139</sup>

## Due diligence

3.54 At the due diligence stage, the NAIF undertook due diligence checks and prepared a NAIF Credit Approval Paper (NCAP) or Conditional Credit Approval Paper (CCAP) as the basis for the NAIF Board to give the Minister a proposal notice. This included assessment of the application against mandatory criteria such as the ability to repay or refinance, public benefit and Indigenous engagement, and other Investment Mandate requirements such as loan concessions, investment risk, regulatory and environmental approvals and other matters.

3.55 A review of NCAPs, CCAPs and the corresponding Board decisions identified that:<sup>140</sup>

- NCAPs were presented to the Board in a consistent format;
- on four occasions, the NAIF Board agreed for projects to move to the next stage despite the projects not meeting specific criteria in relation to the loan repayment, the project involving construction or enhancement of economic infrastructure, public benefit, and provision of an Indigenous engagement strategy — the reasons provided were that either the assessment is to be confirmed or the approval is predicated on legislative change;

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137 The NAIF stated in December 2018 that ‘these can be extremely voluminous (in excess of 800 pages of extremely technical material). The role of the Board is not to review that but rather to rely on the expertise of the NAIF executive, experts advising them and the Chief Credit Officer and his team to determine what information is appropriate to be provided to the Board within the NAIF credit guidelines’.

138 In one instance where a SAP stated that the Indigenous engagement strategy mandatory criterion was met despite no Indigenous engagement strategy being provided, the NAIF later stated this ‘meant the team had determined their view it will be able to be met given the nature of proponent being Indigenous’.

139 The NAIF stated in December 2018 that ‘This risk is noted but considered appropriate in order to achieve the objectives of the legislation. NAIF has had the template letter drafted and reviewed by legal counsel in order to ensure it is not misleading’.

140 Where applicable, the ANAO reviewed the Conditional Credit Approval Paper (CCAP).

- due diligence processes and financial analysis of applications appeared robust, with the NAIF undertaking risk assessment with a credit risk recommendation by the Efic Chief Credit Officer under the Service Agreement;
- projects were approved by the NAIF Board with a NAIF credit risk grade as per the guidance outlined in the NAIF Risk Appetite Statement and Credit Assessment Paper Guidelines. It was unclear from documentation whether this credit risk was related to factors that are unique to investing in Northern Australia economic infrastructure, as required by the Investment Mandate;
- whereas Efic publishes the weighted average risk grade of its commercial account exposures, the NAIF does not publish the weighted average risk grade of the NAIF portfolio; and
- in two cases, the NAIF Board made decisions contingent on changes to the Investment Mandate, including not assessing applications against criteria the Board expected would be amended.

3.56 On some occasions, the NAIF would conduct a site visit as part of the strategic assessment or due diligence process. There was no apparent consistency in how site visits were planned, conducted, documented or reported to the NAIF Board. A review of the NAIF Board papers identified that:

- the NAIF Board approved policies covering travel and expenses for Board members and the CEO, and a Due Diligence Costs Policy in August 2018, and the attribution of these costs to applicants under cost indemnity letters;
- the NAIF did not have a policy covering when, why or how site visits would be conducted, and it was not possible to provide assurance that site visit decisions — whether or not to conduct a site visit, who would attend, how many site visits to conduct, and for what purpose — were made in a consistent manner in accordance with documented policy; and
- while SAP and NCAP documents occasionally referred to site visits being conducted, there was no evidence that site visit reports were prepared for the NAIF Board to function as direct supporting evidence for their decisions.

3.57 The NAIF should develop and implement a policy for the planning, conduct, documentation and reporting of site visits.<sup>141</sup>

## Investment decision

3.58 Once the Board provided a proposal notice to the Minister, if the Minister did not give the NAIF a refusal notice within the consideration period, the project could proceed to Investment Decision and financial close subject to the satisfaction of any conditions precedent to the decision.

3.59 As noted in paragraph 2.76, the Investment Mandate requires the NAIF to publish certain information about decisions within a statutory timeframe. The NAIF Board generally did not publish

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141 The NAIF stated in December 2018 that it did not have a specific policy covering site visits. However, travel expenses incurred during site visits were covered by the general travel expenses policy approval regime and attribution of costs associated with site visits was covered under NAIF's Due Diligence Costs Policy.

any other information about decisions — for example, key supporting evidence such as public benefit assessments, environmental assessments and Indigenous engagement strategies, or reasons for its decisions.<sup>142</sup>

### Recommendation no.5

3.60 The NAIF select projects at each assessment stage on a consistent and transparent basis in accordance with published criteria, and retain adequate documentation to record the rationale for decisions made and actions undertaken.

**The Northern Australia Infrastructure Facility response:** *Agree in principle.*

3.61 *NAIF has and will continue to consistently select projects by assessment against the published NAIF requirements which will include at the strategic assessment stage whether mandatory criteria have potential to be satisfied and at the Investment Decision stage whether the requirements have been satisfied. NAIF will refine its published guidance material to elaborate on the type of information and factors that may be taken into account at each stage noting projects vary on their facts and that expert commercial judgement is always applied. In addition, while NAIF strenuously rejects any assertion that its decisions have not been based on robust and consistently applied processes, NAIF will strengthen its internal protocols around documenting its rationale for early stage assessments.*

### Are appropriate monitoring and reporting arrangements in place to provide clear accountability in relation to the NAIF's performance?

The NAIF Board met minimum external reporting obligations, but did not set measures that provided clear accountability and transparency in relation to its performance, did not measure the realisation of public benefit, and did not meet key performance targets in 2017–18.

3.62 The enhanced Commonwealth performance framework states that ‘the public and the parliament — like the shareholders of a company and financial supporters of charitable institutions — have a right to know what results are being achieved with the money they have provided. A balanced and complete performance framework should provide both financial and non-financial information that allows judgements to be made on the public benefit generated by public expenditure’.<sup>143</sup>

142 On one occasion when the NAIF included information about public benefit in its annual report, the calculation of the public benefit claims was inconsistent with the NAIF's Public Benefit Guideline. The NAIF stated that ‘NAIF's Annual Report is produced for a broad public audience’.

143 Department of Finance, *Enhanced Commonwealth Performance Framework*, available from <https://www.finance.gov.au/resource-management/pmra/performance/> [accessed 9 November 2018].

3.63 In addition to the reporting requirements in the NAIF Act, as a corporate Commonwealth entity, the NAIF must meet statutory performance monitoring and reporting requirements for corporate plans, annual reports and annual performance statements.<sup>144</sup>

3.64 The NAIF Board published corporate plans, annual reports and annual performance statements, and compliance with statutory content requirements has improved over time. The PGPA Rule requires the NAIF to publish its corporate plan by the last day of the second month of the reporting period, and include in the corporate plan ‘any measures, targets and assessments that will be used to measure and assess the entity’s performance’.

3.65 The first 2016–17 corporate plan, published in June 2017, did not cover the required four reporting periods, and did not contain any measures, targets or assessments.

3.66 The 2017–18 corporate plan identified eight performance criteria, with associated measures and targets, in the areas of:

- generating public benefit;
- Indigenous engagement;
- decisions by the NAIF Board;
- effective risk management;
- encouraging private sector contribution to financing projects;
- raising awareness of NAIF value through dissemination of information to industry stakeholders;
- building a diverse pipeline of potential infrastructure projects; and
- achieving sound financial performance.

3.67 The 2018–19 corporate plan used the same performance criteria, measures and targets, but revised the target for total capital value of projects supported per annum downwards from a \$1.25 billion–\$3.75 billion target to \$750 million–\$2.5 billion.<sup>145</sup>

3.68 The measures and targets set by the NAIF Board in relation to the eight performance criteria did not provide clear accountability in relation to the NAIF’s performance, with:

- no quantitative measures or targets for claimed public benefit and no measures for realised public benefit beyond each project having a ‘Net public benefit for Northern Australia’ — which is a mandatory statutory criteria that must be met for projects to be financed; and
- input or activity measures substituting for performance measures in relation to stakeholder engagement.

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144 These requirements are set out in the *Public Governance, Performance and Accountability Act 2013*, the *Public Governance, Performance and Accountability Rule 2014*, the enhanced Commonwealth performance framework, relevant Resource Management Guides published by the Department of Finance, and the Requirements for Performance Information included in Portfolio Budget Statements Finance Secretary Direction under subsection 36(3) of the PGPA Act.

145 The NAIF stated that its Executive and Board conducted a review of the forward key performance indicators and decided that it would be appropriate to lower the targets.

3.69 The NAIF did not meet its target for 2017–18 of providing grants of financial assistance between \$300 million to \$1 billion for projects with a total capital value of between \$750 million to \$2.5 billion (less than \$200 million in investment decisions were made in 2017–18).

### Recommendation no.6

3.70 The NAIF revise its performance measures and targets to provide clearer accountability and transparency in the measurement of its performance, and measure and report on the realisation of public benefit.

**The Northern Australia Infrastructure Facility response:** *Agree.*

3.71 *NAIF's performance measures have been subject to review by its internal audit function, which has found the existing performance measures are considered relevant, reliable, complete and meaningful. The NAIF Board reviews all performance measures annually in a manner consistent with guidance provided through materials including the Public Governance, Performance and Accountability Act 2013 and Department of Finance Resource Management Guides. Within its capacity NAIF will monitor and publish information on public benefit realised through NAIF investments.*



Grant Hehir  
Auditor-General

Canberra ACT  
10 April 2019



## **Appendices**

## Appendix 1 Entity response

Mr Grant Hehir  
Auditor-General  
Australian National Audit Office  
PO Box 707  
CANBERRA ACT 26001

19 March 2019

Dear Auditor-General

Thank you for the opportunity to respond to the Australian National Audit Office's (ANAO) proposed audit report of the Northern Australia Infrastructure Facility (NAIF) under Section 19 of the *Auditor-General Act 1997* (the Report). This letter summarises NAIF's response to the main issues raised in the audit.

NAIF has already or will in the near term, adopt all recommendations in the Report as outlined in NAIF's responses (refer the respective recommendation paragraphs within the detail of the Report).

### Context of Report

The ANAO has approached this audit with an interest in overseeing the governance and transparency of a defined group of financing investment-focused entities that have been established by the Commonwealth in recent years. In addition to NAIF, these include Clean Energy Finance Corporation (CEFC) and the Regional Investment Corporation.

The ANAO's preference is to see these entities adhere to 'template' governance policies and frameworks. NAIF accepts there are some instances where there may be merit in this and indeed had the benefit of that approach in its arrangements with Export Finance and Insurance Corporation (Efic). However, ANAO also would seek to have those agencies which have been established to operate in a commercial context to conform to modes of organisational set up, decision-making and function execution that are aligned to the ANAO's preferences.

This point of view is evident from the ANAO's engagement with NAIF, from the fact that the Report's remit broadened to include these matters subsequent to referral<sup>a</sup>, and from the ANAO's position that the entities should default to an established public sector governance framework without an overlay of peer (whether public or private sector) lending institutions' best practice.<sup>b</sup>

NAIF simply notes these observations regarding the ANAO's preferences to provide context for those considering this Report.

### Integrity of processes

The integrity of NAIF's processes is of utmost importance to the organisation and in its view they are effective.

NAIF assesses each project according to a consistent process. Each project has unique characteristics that determine whether and how rapidly it can progress through NAIF processes



and when it is capable of satisfying NAIF's requirements. Also NAIF's management of its pipeline will always call for the exercise of commercial judgement. That creates variability, as projects progress at different rates, enter periods of inaction or hiatus, or are modified (sometimes materially). It may be clear early that a project will meet criteria, for others they may be established as only having potential in that regard but allow an expert view that NAIF's conditions will subsequently be met. That is not evidence of a lack of consistency of policy or approach, but rather the natural outcome of consistently applying a single process to the differing parameters of each project to assess against the NAIF requirements. If NAIF had no regard to each project's specific circumstances, or failed to exercise commercial judgement, it would almost certainly risk causing detriment to the Commonwealth and proponents alike.<sup>c</sup>

NAIF is satisfied that it has had adequate oversight of the NAIF project pipeline of proposals and the management of individual projects. The fact that it has not rejected a proposal presented for formal consideration is evidence that the filtering and management process is effective, rather than the reverse. It has not been demonstrated that any project has been advantaged, disadvantaged or delayed as a result of any failure on the part of the NAIF organisation.<sup>c</sup>

Since its establishment NAIF has ensured that appropriate frameworks and policies have been in place for all decisions taken.

NAIF's process is disciplined and its decisions are thoroughly documented.<sup>d</sup> NAIF nonetheless will strengthen its internal protocols around documenting its rationale for early stage assessments.

### **Transparency**

NAIF is keenly aware of its responsibility as a steward of public resources to be as transparent as reasonably practicable.

The organisation's disposition is to publish information where doing so does not compromise the interests of the Commonwealth or risk breaching NAIF's legislated obligation to have regard to industry best practice. This obligation, which is in the nature of a two way consent, includes the obligation to protect commercially sensitive information, and arises from an understanding that the Commonwealth's own interests (including the protection of its reputation) are best served by the protection of confidential information. Confidentiality helps avoid disclosures that might deter proponents, or that might lead private financiers to conclude they can lessen their exposure to a project, in turn increasing demands on the public purse or lessening the achievement of NAIF's objectives.<sup>e</sup>

In striking a balance between transparency and commercial confidentiality, NAIF regularly benchmarks its practices against public peers and equivalent private sector organisations. NAIF's practices are in conformance with these norms.

NAIF protects its information sources through an appropriate Corporate Information Security Policy which in line with its obligations as a corporate Commonwealth entity<sup>f</sup>, has regard to better practice such as the Commonwealth's Protective Security Policy Framework.

### **Speed of decisions**

NAIF is aware that many Australians are eager to see investment decisions that expedite the development of Northern Australia. The organisation is comprised of individuals who themselves are committed to the same outcome.

NAIF is agile and responsive. It moves at the same or a faster pace relative to other market participants in both the private and public sector but has been, and (by reason of its legislative design) will continue to be limited by the capacity and willingness of proponents to progress their proposals. Where possible, NAIF has endeavoured to accelerate proposals by adopting an innovative and flexible approach consistent with proper standards of governance. The NAIF record shows that its approach is working. As one comparison, the US Transport Infrastructure and Innovation program, created in 1998 to perform a function similar to NAIF, invested in just two projects in its first six years, despite the size of the US market and the poor state of its transport infrastructure. In the past 10 months to 1 March 2019 NAIF has made nine Investment Decisions and three current conditional approvals totalling ~\$1.3 billion of dollar value of NAIF investment.

NAIF seeks to make decisions on projects as early as possible. The NAIF Act specifies the current last date for investment decisions (being 30 June 2021), but this does not create a statutory requirement for NAIF to make decisions on all projects in its pipeline by that date. Projects may not be ready to be managed by NAIF to an outcome of granting or refusing NAIF financial assistance by a deadline. The pace of movement of a project through NAIF's processes is largely governed by the project proponents themselves. It is based on the complex interplay of bespoke factors, for instance industry type or geography. The time a project spends within the NAIF system is not determinative of its outcome.

NAIF does not discount any opportunity peremptorily. To do so may damage the commercial value of the proponent (making it explicit that it was unsuccessful in obtaining 'gap' finance). It is not possible for NAIF to accelerate all projects at the same pace. The rate of approval or rejection of a project in no way is informative of the failure of integrity in NAIF's process.<sup>8</sup>

### **Text Changes requested**

Attached is a list of factual text corrections that NAIF suggests might be made in the final Report (Attachment 2).

### **Concluding remarks**

NAIF acknowledges the professionalism of ANAO officers and thanks the Office for this Report.

Yours sincerely

Khory McCormick

Chair

### ***ANAO comments on NAIF's response***

- (a) As an independent officer of the Parliament, the Auditor-General has complete discretion in determining the objective, criteria and scope of ANAO performance audits. Whilst the Auditor-General receives audit requests from members of Parliament from time to time, the Auditor-General is not subject to direction from anyone in relation to whether or not a particular audit is conducted, or the way in which a particular audit is conducted.

- (b) The audit assessed the NAIF against legislative and policy requirements that applied to the NAIF as a corporate Commonwealth entity, and these requirements are set out in each of the relevant sections of the report. This included subsection 17(1) of the Investment Mandate, which required that 'The Facility must have regard to Australian best practice government governance principles, and Australian best practice corporate governance for Commercial Financiers, when performing its functions'. The application of these requirements to the NAIF is a matter of law and Australian Government policy, and not ANAO preference.
- (c) Paragraphs 3.33 to 3.57 set out the ANAO's analysis of the integrity of decision support processes in the NAIF. Decisions, or the absence of decisions, at every stage of the process are judicially reviewable as decisions under an enactment. The ANAO found that the arrangements for ensuring the integrity of decision support processes were not effective, in particular as it is unclear why certain projects were presented to the Board and not others and there was insufficient evidence that all projects were evaluated in a consistent manner throughout the assessment stages.
- (d) Paragraphs 3.33 to 3.57 set out the ANAO's analysis of the integrity of decision support processes in the NAIF. The ANAO found that the NAIF sent letters of support or term sheets before applicants provided appropriate supporting documentation (paragraph 3.53); there was no consistency in how site visits were planned, conducted, documented or reported (paragraph 3.56); the NAIF Board agreed for projects to move to the next stage of assessment despite documentation not reflecting the basis for these projects to move forward in preference to other projects (paragraph 3.52 and paragraph 3.55); and projects were approved by the NAIF Board with a NAIF credit risk grade below investment grade in circumstances where it was unclear from documentation whether this credit risk was related to factors that are unique to investing in Northern Australia economic infrastructure (paragraph 3.55).
- (e) Paragraphs 2.76 to 2.78 examined the NAIF's approach to information governance and transparency. Whilst the NAIF took the view that a default confidentiality position was appropriate, its approach to disclosure limited the opportunities for public scrutiny of decision-making. Paragraphs 3.62 to 3.69 examined accountability in relation to the NAIF's performance, and found that the NAIF did not monitor the realisation of public benefit.
- (f) Paragraphs 3.17 to 3.23 considered whether the NAIF had effective security controls in place, including information security. The ANAO found that the NAIF adopted but did not adequately implement the Protective Security Policy Framework.
- (g) Paragraphs 2.36 to 2.40 examined origination and case management, and found that the data did not demonstrate a clear relationship between the NAIF-facilitated origination strategy and a significant or sustained increase in either the annual number of new projects or the annual number of successful applications. Paragraphs 3.40 to 3.42 examined the management of projects at the enquiry and preliminary assessment stages, and found that the NAIF did not always actively manage projects at these stages to an outcome — either presentation to the Board for strategic assessment, or a refusal to grant financial assistance. As a result, projects remained at the enquiry and preliminary assessment stages for up to 850 days after first contact.