

The Auditor-General
ANAO Report No. 16 2016–17
Performance Audit

Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services

Department of Immigration and Border Protection

© Commonwealth of Australia 2016

ISSN 1036–7632 (Print)

ISSN 2203–0352 (Online)

ISBN 978-1-76033-179-5 (Print)

ISBN 978-1-76033-180-1 (Online)

Except for the content in this document supplied by third parties, the Australian National Audit Office logo, the Commonwealth Coat of Arms, and any material protected by a trade mark, this document is licensed by the Australian National Audit Office for use under the terms of a Creative Commons Attribution-NonCommercial-NoDerivatives 3.0 Australia licence. To view a copy of this licence, visit

<http://creativecommons.org/licenses/by-nc-nd/3.0/au/>.

You are free to copy and communicate the document in its current form for non commercial purposes, as long as you attribute the document to the Australian National Audit Office and abide by the other licence terms. You may not alter or adapt the work in any way.

Permission to use material for which the copyright is owned by a third party must be sought from the relevant copyright owner. As far as practicable, such material will be clearly labelled.

For terms of use of the Commonwealth Coat of Arms, visit the It's an Honour website at

<http://www.itsanhonour.gov.au/>.

Requests and inquiries concerning reproduction and rights should be addressed to:

Senior Executive Director
Corporate Management Branch
Australian National Audit Office
19 National Circuit
BARTON ACT 2600

Or via email:

communication@anao.gov.au.



Canberra ACT
13 September 2016

Dear President and Speaker

The Australian National Audit Office has undertaken an independent performance audit in the Department of Immigration and Border Protection titled *Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services*. The audit was conducted in accordance with the authority contained in the *Auditor General Act 1997*. 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

AUDITING FOR AUSTRALIA

The Auditor-General is head of the Australian National Audit Office (ANAO). The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits, financial statement audits and assurance reviews of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Australian Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

For further information contact:

**Australian National Audit Office
GPO Box 707
Canberra ACT 2601**

**Phone: (02) 6203 7300
Fax: (02) 6203 7777
Email: ag1@anao.gov.au**

ANAO audit reports and information about the ANAO are available on our website:
<http://www.anao.gov.au>

Audit Team

Grace Guilfoyle	Jess Scully
Tracey Martin	Renee Hall
Tony Varnes	Anne Molloy
Rowena Hayman	Gillian Meek
Nicole George	Joyce Knight
Hannah Climas	Edel Kairouz

Contents

Summary and recommendations.....	7
Background	7
Conclusion.....	8
Supporting findings.....	9
Recommendations	14
Summary of entity responses.....	15
Audit Findings	19
1. Background	21
Introduction.....	21
Audit approach	31
2. Establishing the offshore processing centres in 2012	32
Introduction.....	32
In adopting limited tender processes, did the department have regard to the mandatory requirements of the <i>Commonwealth Procurement Rules</i> ?.....	33
Did the department demonstrate value for money through the procurement and negotiation processes?.....	36
Did the department establish processes to manage probity risks?	44
Were relevant approvals by the Chief Financial Officer obtained prior to commencing the procurement process?.....	45
3. Consolidation of contracts in Nauru and on Manus Island in 2013–14	47
Was the adoption of a limited tender process on the grounds of urgent and unforeseen circumstances appropriately documented and defensible?	49
Did the process applied to contract consolidation support the achievement of planned savings, innovations and efficiency in service delivery?.....	57
4. Open Tender Process from 2014 to 2016	71
Introduction.....	72
Did the department adopt tender planning and probity arrangements consistent with <i>Commonwealth Procurement Rules</i> requirements?.....	74
Did the department adopt tender evaluation processes consistent with the requirements of the <i>Commonwealth Procurement Rules</i> ?.....	80
Did the department’s negotiation processes facilitate value for money?	84
Did the department establish effective oversight controls?	87
Recommendations	91
Appendices	93
Appendix 1 Entity responses	94

Summary and recommendations

Background

1. In 2012 the Australian Government established offshore processing centres¹ in the Republic of Nauru (Nauru) and Papua New Guinea (PNG) with the agreement of the Nauruan and PNG Governments.² Under the agreements, the Australian Government was to bear all costs associated with the construction and operation of the centres. Transfers of asylum seekers to Nauru commenced on 14 September 2012 and to PNG on Manus Island³ on 21 November 2012.⁴

2. To underpin operations at the centres, the Department of Immigration and Border Protection (DIBP or the department)⁵ entered into contracts for the delivery of garrison support and/or welfare services with a number of providers. Garrison support includes security, cleaning and catering services. Welfare services include individualised care to maintain health and wellbeing such as recreational and educational activities.

3. The department has undertaken a series of procurements relating to the garrison support and welfare services functions. The department applied limited tender procurement methods to acquire the services initially in 2012 and then again in late 2013. In 2015–2016, the department conducted an open tender procurement process for the services (for a single contract across both islands).

4. In October 2015, Transfield⁶ became the sole provider of all garrison support and welfare services to asylum seekers at the offshore processing centres⁷ in Nauru and on Manus Island. In February 2016 these arrangements were extended through to 28 February 2017 and in August 2016 the contract with Transfield was further extended until 31 October 2017. The contracts for garrison support and welfare services are set out in Table 1.1. The total combined contract value as at the end of March 2016, as reported on AusTender, was \$3 045 million.

5. The Australian Government is a significant purchaser of goods and services and has in place resource management legislation and related policies that establish a framework for Government procurement and contracting. The *Commonwealth Procurement Rules* (CPRs) establish procurement

1 Offshore processing centres are also referred to as regional processing centres (RPCs).

2 To give effect to the arrangements legislation was required to provide for the processing of arrivals in locations outside Australia.

3 On Manus Island asylum seekers are referred to as transferees.

4 Department of Immigration and Citizenship, *Department of Immigration and Citizenship Annual Report 20122013* p.9. [Internet], available from <<https://www.border.gov.au/ReportsandPublications/Documents/annual-reports/2012-13-diac-annual-report.pdf>> [accessed June 2016].

5 At the time the initial procurements examined in this audit were undertaken the department was known as the Department of Immigration and Citizenship.

6 Transfield Services Group was rebranded on 30 October 2015 and Transfield Services (Australia) Pty Ltd's name changed to Broadspectrum (Australia) Pty Ltd on 30 November 2015. For consistency, the ANAO will use the name Transfield throughout this report for Broadspectrum (Australia) Pty Ltd. As at 13 May 2016 a Spanish company Ferrovia was in the process of taking over Transfield. [Internet], available from <<http://www.transfieldservices.com/news/ferrovial-today-announced-that-it-has-received-acceptances-for-92-05-of-broadspectrum-shares>> [accessed May 2016].

7 Transfield also provides limited services to resident refugees at the centres.

principles that apply to all Australian Government procurement processes. The CPRs combine both Australia's international obligations⁸ and good practice, and enable Government entities to design processes that are robust, transparent and instil confidence in the Australian Government's procurement activities. The CPRs are issued under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act)⁹ and articulate the requirements for officials performing duties in relation to procurement.

Audit objective, scope and criteria

6. The objective of the audit was to assess whether the Department of Immigration and Border Protection (DIBP) had appropriately managed the procurement of garrison support and welfare services at offshore processing centres in Nauru and Papua New Guinea (Manus Island); and whether the processes adopted met the requirements of the *Commonwealth Procurement Rules* (CPRs) including consideration and achievement of value for money.

7. The audit examined procurements conducted since 2012, when the arrangements were first put into place, through to the open tender process which commenced in 2015. The ANAO reviewed DIBP and service provider records; and interviewed relevant DIBP officials (past and present) and stakeholders including service providers, tenderers and Government officials from Nauru and Papua New Guinea. The audit team also visited Manus Island and Nauru during August and September 2015. Due to shortcomings in DIBP's record keeping system, DIBP was not able to provide the ANAO with assurance that it provided all departmental records relevant to the audit.¹⁰

Conclusion

8. The Department of Immigration and Border Protection's (DIBP) management of procurement activity for garrison support and welfare services at the offshore processing centres in Nauru and Papua New Guinea (Manus Island) has fallen well short of effective procurement practice. This audit has identified serious and persistent deficiencies in the three phases of procurement activity undertaken since 2012 to: establish the centres; consolidate contracts; and achieve savings through an open tender process.

9. Of most concern is the department's management of processes for contract consolidation and the open tender. The Australian Government intended that these procurement processes would rein in the growing expense associated with managing the centres. In both cases, the approach adopted by the department did not facilitate such an outcome. The department used approaches which reduced competitive pressure and significantly increased the price of the services without Government authority to do so. The open tender process was cancelled by the department on 29 July 2016 and consequently had no outcome.

8 Including a range of free trade agreements.

9 The PGPA Act came into effect from 1 July 2014. Prior to this the use of public resources by Government departments was governed by the *Financial Management and Accountability Act 1997* and the *Financial Management and Accountability Regulations 1997*.

10 The department acknowledged these issues in its comments on the proposed audit report. See Appendix 1.

10. The conduct and outcomes of the tender processes reviewed highlight procurement skill and capability gaps amongst departmental personnel at all levels. Procurement is core business for Commonwealth entities and the deficiencies have resulted in higher than necessary expense for taxpayers and significant reputational risks for the Australian Government and DIBP. The audit's two recommendations are intended to address:

- the significant skill and capability gaps identified amongst personnel at all levels in the department, including within the central procurement and budget units; and
- persistent shortcomings in the planning and conduct of the procurements, including in relation to record keeping, consistency and fairness in the treatment of suppliers, and the assessment of value for money.

Supporting findings

Establishing the offshore processing centres in 2012

11. For each of the procurements involved in this establishment phase, the department adopted limited tender arrangements. The department relied on the conditions for limited tender in the *Commonwealth Procurement Rules*, relating to urgent and unforeseen circumstances.¹¹ Given the circumstances which existed—the department was expected to establish operations for the offshore processing centres in Nauru and on Manus Island immediately—the use of limited tender was justified. However, there was limited specification of the type of services to be delivered, and no estimation of the expected value of individual procurements, as required by the *Commonwealth Procurement Rules*.

12. The department was unable to demonstrate the achievement of value for money in three of the four procurement processes.

- In engaging Transfield the department set aside an earlier approach to Serco.¹² The department did not require Transfield to provide a proposal specifying services to be delivered and a price. As a result it was very difficult for the department to demonstrate that it had conducted a robust value for money assessment which considered the financial and non-financial benefits of the proposal. Transfield was instead assessed on its ability to respond in a short timeframe.
- The Salvation Army¹³ was also assessed as providing value for money on the basis of availability, without any specification of the services to be delivered or price.
- The department could not make available any records of how Save the Children¹⁴ was assessed as providing value for money.
- G4S¹⁵ was engaged following a limited tender procurement that involved a request for expressions of interest from five potential suppliers. This approach introduced competition in an otherwise limited tender procurement.

11 See Footnote 16.

12 Serco Group Pty Ltd is referred to as Serco in this report.

13 The Salvation Army (New South Wales) Property Trust is referred to as The Salvation Army in this report.

14 Save the Children Australia is referred to as Save the Children in this report.

15 G4S Australia and New Zealand is referred to as G4S in this report.

13. Contracts with service providers took between 16 and 43 weeks to negotiate, and the department relied on letters of intent or heads of agreement pending contract signature. Service requirements and prices were not settled until contracts were entered into. The approach adopted by the department introduced additional risk for the Commonwealth.

14. The department was not able to provide the ANAO with evidence that it implemented mechanisms to manage probity risk. The ANAO's review, based on available evidence, of the conduct of these initial procurements indicates that suppliers were not always treated fairly or equally. In particular, Serco's proposal was set aside without an opportunity to negotiate. The available records indicate that the department did not seek probity advice on this proposed course of action or document its decision-making. There are no available records of specific conflict of interest declarations having been made by departmental officers responsible for the initial procurements.

15. The department's central procurement unit had limited effective oversight of the initial limited tender procurements. Available records indicate that program areas with responsibility for conducting the initial procurements obtained the necessary approvals to conduct limited tender procurements from the Chief Financial Officer, but not prior to commencing the procurement process as required by DIBP's financial delegations.

Consolidation of contracts in Nauru and on Manus Island in 2013–14

16. The department again relied on paragraph 10.3(b) of the CPRs¹⁶ to conduct a limited tender, on the basis of urgent and unforeseen circumstances, to engage Transfield in Nauru and on Manus Island as part of a contract consolidation process. At the time, consolidation was considered an interim measure pending an open tender process in 2014. The available record does not indicate that urgent or unforeseen circumstances existed but suggests that the department first selected the provider and then commenced a process to determine the exact nature, scope and price of the services to be delivered.

- The department decided not to continue with the existing provider (G4S), but did not clearly document its reasons.
- Advice prepared by the department's Central Procurement Unit was not consistent with the CPRs and the Department of Finance (Finance) guidance on key issues. In seeking advice from Finance, the Unit made written statements implying underperformance by service providers which was not supported by the evidence. The department subsequently referenced Finance's support in briefings for its Minister.

17. DIBP's approach to engaging Transfield through limited tender procurement removed competition from the outset. The services to be provided and related costs were not agreed with Transfield prior to G4S and The Salvation Army being advised that they would exit from

16 Paragraph 10.3 of the 2012 and 2014 CPRs sets out the conditions for limited tender above the relevant procurement threshold. Paragraph 10.3(b) allows limited tender to be conducted when, for reasons of extreme urgency brought about by events unforeseen by the relevant entity, the goods and services could not be obtained in time under open tender or prequalified tender.

service delivery on Manus Island. The proposed costs submitted by Transfield were higher than the department had anticipated and exceeded those charged by G4S and The Salvation Army for service provision on Manus Island.

18. Ministers expected the consolidation of contracts to achieve innovation and savings. Savings were not realised and the basis which the department relied upon to demonstrate savings was unreliable. In particular:

- The department applied a benchmark model to demonstrate the achievement of value for money. Overall the benchmark was adjusted above historical costs to account for changes to the department's service requirements and contractual approach, upwards to \$372 million, to accommodate a number of service enhancements. The Government had directed the department to reduce per-head costs. The department had no authority to increase the funding value of the contract above historic costs.¹⁷
- Separate benchmarks were developed for Nauru and Manus Island, but the department determined 'value for money' and claimed savings (against the benchmarks) on a combined basis. This allowed the department to demonstrate 'savings' by offsetting higher costs for Manus Island against lower costs for Nauru. While Transfield's bid for Nauru was lower than historical costs, the bid for Manus Island exceeded historical costs by between \$200 million and \$300 million.

19. While the department based the negotiated contract price on a high capacity scenario, there was a steady drop off in new asylum seeker arrivals from a high of 1 647 in August 2013 to zero in March 2014. On this basis it was increasingly unlikely that the high capacity levels would eventuate. The resulting contract was volume driven, with significant economies of scale expected at high capacity levels. This contract exposed the Commonwealth to the risk of locking-in a high price for services delivered at lower capacity levels.

20. There is no available record of specific conflict of interest declarations having been made by departmental officers who were responsible for the procurement. There is also no available documentation to indicate whether the department performed due diligence checks on the successful tenderer (Transfield) or its subcontractors as part of the contract consolidation.

21. The Prime Minister had requested that per head costs be lower as a result of retendering the contracts, but the department did not calculate a per person cost. Finance advised the ANAO that under the consolidated contract, the per person per annum cost of holding a person in the offshore processing centres in Nauru and on Manus Island, was estimated at \$573 111, at the time of the Mid-Year Economic and Fiscal Outlook 2015-16.¹⁸ Prior to consolidation Finance estimated the cost at \$201 000.

Open Tender Process from 2014 to 2016

22. While aspects of the department's open tender planning addressed the requirements of the CPRs, insufficient consideration was given to:

¹⁷ The ANAO reviewed the records of the Department of the Prime Minister and Cabinet, the Department of Finance and DIBP relating to the Government decisions and Ministerial approvals.

¹⁸ Released in December 2015.

- The use of benchmarking to determine overall value for money. The department’s approach involved comparing only the preferred tenderer’s negotiated final costs with a benchmark, and was incompatible with the CPRs. The CPRs require each eligible¹⁹ tenderer’s financial and nonfinancial benefit to be compared on a like for like basis with other eligible tenders.
- The scope of services set out in the statement of requirement. In particular, whether the department had policy authority to expand the services or increase the value of the contract beyond the contracts which were in place. The value of expanded services was estimated by an external adviser (KPMG) at between \$594 million to \$835 million above historical costs. The Government had not provided policy authority to expand the services or increase the funding value of the contract to accommodate service enhancements or adjustments.

23. The department’s tender evaluation processes were not sufficiently robust to meet a range of applicable CPR requirements. In particular:

- the department was unable to demonstrate that the original tender documents lodged through AusTender were used by evaluation team members for the tender evaluation;
- individual assessor records were incomplete and there were missing documents in relation to various aspects of the process;
- using compact disks rather than TRIM²⁰ files did not provide sufficient control over the security of the tender documentation and the commercial material contained within those documents; and
- there were significant unquantified pricing risks related to most of the tender bids, which the department did not clarify prior to selecting a preferred tenderer and forming an opinion on value for money of the preferred and reserve tenderers.

24. The assessment of value for money focused on provider claims and referee reports and did not take into account the department’s own contract management experience with suppliers.

25. The department determined to only enter into negotiations with the preferred tenderer (Transfield). During the course of negotiations the department amended its requirements and accepted enhancements and adjustments to services which flowed through to a \$1.1 billion increase in Transfield’s overall price. The department did not seek clarification or repricing from any other tenderers and instead set out to determine value for money by comparing the negotiated price with a benchmark. The benchmark was the cost of services provided in Nauru and on Manus Island, which had been procured via a non-competitive limited tender process in 2013–14. The approach adopted was not consistent with an open tender which requires that eligible tender bids are compared on a like for like basis.

26. The delegate had determined to finalise the procurement process and sign the contract. There are no available records to demonstrate that the delegate: considered if sufficient funds were available to enter into the commitment; considered if additional policy authority was required to accommodate the service enhancements negotiated; or questioned the increased cost of the bid.

19 The CPRs require that consideration must be given only to submissions that meet the minimum content and format requirements. On this basis an eligible tender would be one that met these requirements.

20 TRIM is the department’s official electronic document and records management system.

27. A steering committee and independent probity adviser were key oversight mechanisms for the open tender process. Both were consulted after the negotiation team had reached agreement on a final negotiated outcome with Transfield and prior to the anticipated contract signing. The probity adviser identified that the department's negotiation report appeared to include substantial modifications to the statement of requirement from that released to the market and that Transfield appeared to have been permitted to make material changes to its original tender, including significant overall price increases. The probity adviser considered that these developments raised significant probity and process risks, including the risk that the department was not in a position to determine whether the changes continued to represent best overall value for money compared with other tenderers.

28. After considering this advice the steering committee decided it was unable to determine whether the final negotiated outcome with Transfield demonstrated best value for money. The effective operation of these oversight mechanisms contributed to the department initiating an amended tender process. The Minister was advised of the amended tender process prior to it commencing, and that approvals for funding would need to be reassessed. The amended process only involved the preferred and reserve tenderers and was in effect a limited tender process. On 29 July 2016, in the course of this audit, the department cancelled the initial and amended request for tender. DIBP extended its contract with Transfield until 31 October 2017 and the department advised the ANAO on 29 August 2016 that it was conducting market testing to determine its next steps.

Recommendations

29. Procurement is core business for Commonwealth entities and deficiencies in capability, process and advice can result in higher than necessary expense for taxpayers and significant reputational risks for the Australian Government and responsible entities. The audit recommendations are intended to address significant weaknesses in the Department of Immigration and Border Protection's (DIBP) administration of procurement.

Recommendation No. 1 That the Department of Immigration and Border Protection address, as a priority:
Paragraph 4.64

- (a) through training and staff selection—the significant procurement skill and capability gaps identified in this audit amongst personnel at all levels, including:
 - the central procurement unit;
 - budget unit;
 - program area staff; and
 - delegates;
- (b) through guidance, training and staff selection—an approach to ensuring that officials have appropriate seniority and experience to undertake key procurement roles, such as chief negotiators and delegates, and effectively manage procurement risk; and
- (c) through guidance, training and a strategic approach to records management—persistent shortcomings in record keeping for procurement activities.

Department of Immigration and Border Protection response: *Agreed*

- Recommendation No. 2** That the Department of Immigration and Border Protection take practical steps to ensure adherence to the requirements of the resource management framework when undertaking procurements, including:
- Paragraph 4.65**
- (a) the obligation to manage all aspects of a procurement process in accordance with the *Commonwealth Procurement Rules*;
 - (b) compliance with Government approved scope and contract value;
 - (c) in respect to open tender processes, adopting a value for money assessment which compares tenderers against other bids;
 - (d) the application of documented eligibility criteria in line with the Request for Tender and consistent with the *Commonwealth Procurement Rules*, with any modifications advised to all potential suppliers;
 - (e) the need for ethical conduct throughout the procurement to ensure consistent and fair treatment of suppliers;
 - (f) the need to recognise and manage actual, potential and perceived conflicts of interest; and
 - (g) the maintenance of clear and complete records of all tender bids, key actions, decisions, conflict of interest and SES disclosure declarations.

Department of Immigration and Border Protection response: *Agreed*

Summary of entity responses

30. The proposed audit report was provided to the department and extracts were provided to:
- Other Australian Government entities—the Department of Defence, Department of Finance, Department of Foreign Affairs and Trade and the Department of the Prime Minister and Cabinet;
 - Non-Government Organisations—Allens Linklaters, Broadspectrum (Australia) Pty Ltd (formerly Transfield Services (Australia) Pty Ltd), G4S, International Organisation for Migration Australia, KPMG, Maddocks, Save the Children; Serco, The Salvation Army, and Wilson Security;
 - Former departmental officials—Mr Martin Bowles PSM (former Secretary of the Department of Immigration and Border Protection); and Mr Mark Cormack (former Deputy Secretary of the Department of Immigration and Border Protection); and
 - Other individuals—The Hon Scott Morrison MP (former Minister for Immigration) and Mr Tony Shepherd AO (former Chair of Transfield and Chair of the National Commission of Audit).

31. Formal responses were received from the department, the Department of Defence, Broadspectrum, KPMG, The Salvation Army and Mr Shepherd. Feedback was received from the Department of Finance, Department of Foreign Affairs and Trade, Department of the Prime Minister and Cabinet, G4S Australia, International Organisation for Migration Australia, Maddocks, Save the Children Australia; Serco Asia Pacific, Wilson Security, Mr Bowles and Mr Mark Cormack. Summary responses (where provided) are reproduced below and formal responses are included at Appendix 1.

Department of Immigration and Border Protection

The procurement of garrison and welfare services for clients at the RPCs in Nauru and PNG has been undertaken in a highly complex and rapidly evolving environment.

When legislation was passed on 17 August 2012 enabling regional processing—four days after the release of the expert panel’s report—the Department needed to establish the necessary operational requirements immediately. Consistent with expectations, the first asylum seekers arrived in Nauru three weeks later on 14 September 2012. The Department met these requirements in an environment that was high-tempo, at the peak of national interest and complicated through logistics and uncertainties involved with processing in foreign countries. Delegates were required to make decisions on complex and high risk matters within very short timeframes.

The environment remains extremely complex. The Department provides support to the Governments of Nauru and PNG, who have effective control over the RPCs. It remains open to these Governments at any time to make decisions which effect immediate changes to the administration of the centres. Accordingly, the Department has to adopt a procurement approach that is sufficiently agile to accommodate this environment.

The Department acknowledges that its decision-making processes in this complex and rapidly evolving environment have not been adequately documented at each stage of the procurement process. The absence of appropriate records makes it difficult to adequately demonstrate that the judgements made were appropriate and that due process was applied.

We have analysed our procurement and contracting practices and identified a number of improvements for implementation. These improvements will be progressively introduced as part of a broad reform programme that will provide confidence that all procurement is conducted in accordance with the Commonwealth Procurement Rules (CPRs) and reflects industry best practice. This programme is detailed in the Department’s full response at the end of this report. Implementation will be monitored closely by the Department’s independently-chaired Audit Committee.

Broadspectrum (Australia) Pty Ltd (formerly Transfield Services Australia Pty Ltd)

The procurement by the Commonwealth of services with respect to the Offshore Processing Centres (OPC’s) involved multiple phases between 2012 and 2015 that evolved and changed over time. It included multiple changes in scope (including resettlement services), introduction of new service requirements and supply chains, transitioning in/out of other service providers and multiple new locations for service delivery. All of these factors are considered relevant to a balanced assessment of the quality of the offering with respect to services provided at the OPCs.

While we have done our utmost to respond in a comprehensive manner to the ANAO's Draft Report, our ability to do so has been constrained in circumstances where the Draft Report that has been provided to us is heavily redacted, incomplete and where we do not have visibility of the information relied on by the ANAO.

KPMG

KPMG was engaged by the Department to provide:

- Negotiation support for the consolidation of contracts in Nauru and Manus Island in December 2013; and
- Financial, commercial and negotiation advice and project support in regards to the onshore and offshore procurement processes in August 2014.

KPMG notes that a benchmark approach, or its equivalent, is commonly used for the procurement of other long term, high value contracts that involve a complex risk allocation, including complex Public Private Partnership (PPP) procurements. KPMG maintains that the use of a Benchmark model for the procurement of Garrison and Welfare Services provides additional complementary analysis to the comparative value for money assessment.²¹

KPMG also maintains that it acted openly and transparently at all times, and provided timely disclosure, with regard to its relationships with potential tenderers and the management of potential conflicts of interest in connection with the Garrison and Welfare Services procurement processes. In particular, KPMG notes that its letter issued in July 2015 was not the first time KPMG had brought its role as Transfield's external auditor and provider of advisory services to the Department's attention. KPMG had advised the Department of its relationship with Transfield on numerous occasions prior to this.²²

21 ANAO comment: a competitive open tender process involves the comparison of all eligible bids to determine value for money. The CPRs also provide that request documentation must include a complete description of evaluation criteria to be considered in assessing submissions. The benchmarking approach was not disclosed to the market in the department's request for tender. This matter is discussed further in Appendix 1 at the end of KPMG's response.

22 ANAO comment: disclosures relating to conflict of interest must be timely in order to enable entities to assess risk and consider appropriate mitigation strategies. This matter is discussed further in Appendix 1 at the end of KPMG's response.

Audit Findings

1. Background

Introduction

1.1 On 28 June 2012 the Prime Minister and Minister for Immigration and Citizenship announced that an expert panel would provide a report on the best way forward to prevent asylum seekers risking their lives on boat journeys to Australia.²³ The expert panel's report, released on 13 August 2012, included a range of disincentives, including the establishment of offshore processing centres²⁴ in the Republic of Nauru (Nauru) and Papua New Guinea (PNG).

1.2 The centres were subsequently established with the agreement of the Nauruan and PNG Governments.²⁵ Under the agreements, the Australian Government was to bear all costs associated with the construction and operation of the centres. Transfers of asylum seekers to Nauru commenced on 14 September 2012 and to PNG on Manus Island²⁶ on 21 November 2012.²⁷

1.3 To underpin operations at the centres, the Department of Immigration and Border Protection (DIBP or the department)²⁸ entered into contractual arrangements for the delivery of garrison support and/or welfare services. Garrison support includes security, cleaning and catering services. Welfare services include individualised care to maintain health and well-being such as recreational and educational activities.

Procurement of garrison support and welfare services in Nauru and on Manus Island

1.4 The department has undertaken a series of procurements relating to the garrison support and welfare services functions. The department applied limited tender procurement methods to acquire the services initially in 2012 and again in 2013–2014 as part of a contract consolidation process. In 2015, the department conducted an open tender procurement process for the services (for a single contract across both islands) which was underway at the time of this audit and was cancelled in July 2016. Figure 1.1 shows a timeline of key policy points and procurement actions.

23 Joint press conference with Prime Minister Julia Gillard: 28 June 2012: Asylum seeker legislation, Expert advisory panel [Internet], available from <<http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22media%2Fpressrel%2F2048153%22>> [accessed June 2016].

24 Offshore processing centres are also referred to as regional processing centres.

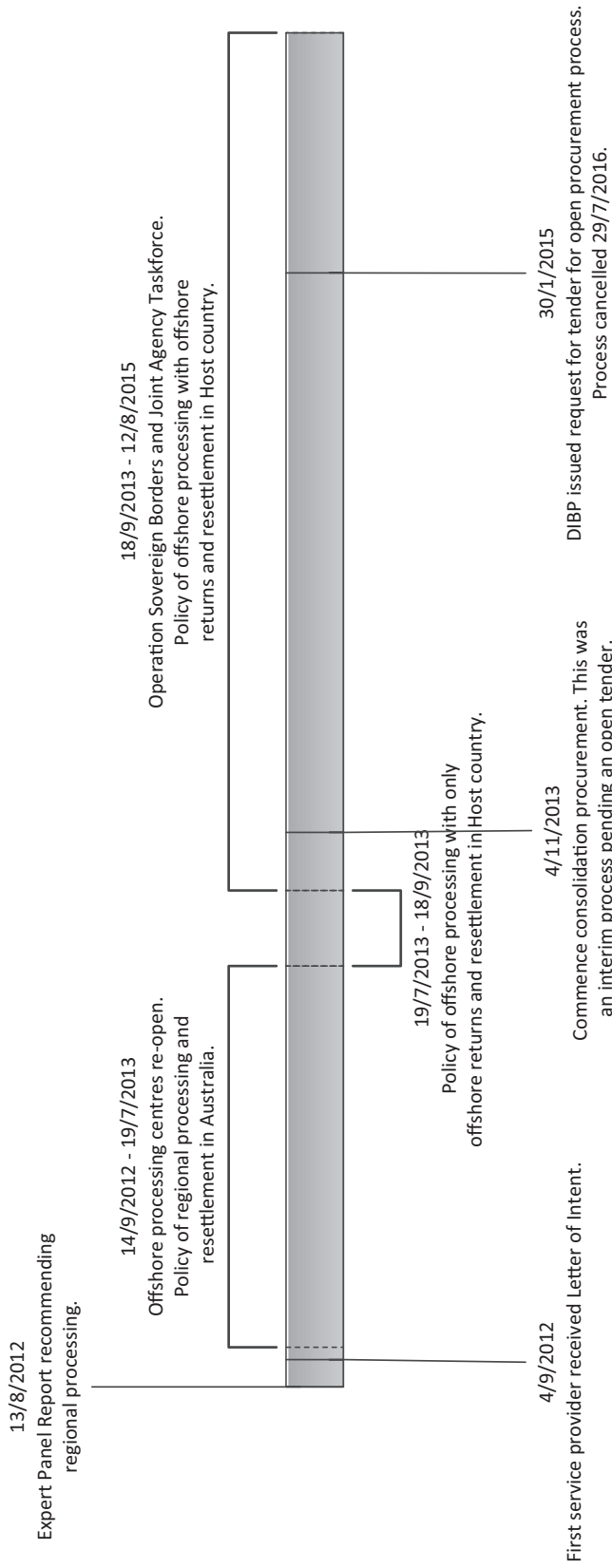
25 To give effect to the arrangements legislation was required to provide for the processing of arrivals in locations outside Australia.

26 On Manus Island asylum seekers are referred to as transferees.

27 Department of Immigration and Citizenship, *Department of Immigration and Citizenship Annual Report 2012–2013*, p.9. [Internet], available from <<https://www.border.gov.au/ReportsandPublications/Documents/annual-reports/2012-13-diac-annual-report.pdf>> [accessed June 2016].

28 At the time the initial procurements examined in this audit were undertaken the department was known as the Department of Immigration and Citizenship.

Figure 1.1: Timeline of key policy points and procurement actions



Source: ANAO analysis of documentation

1.5 In October 2015, Transfield²⁹ became the sole provider of all garrison support and welfare services in Nauru and on Manus Island, and in February 2016 these arrangements were extended to 28 February 2017. They were further extended to October 2017 following the cancellation of DIBP's open tender process in July 2016. The contracts for garrison support and welfare services are set out in Table 1.1. The total combined contract value as at the end of March 2016, as reported on AusTender, was \$3 045 million.

Table 1.1: Garrison support and welfare services contracts since 2012, Nauru and Manus Island

Organisation	Time period	Services provided	Total AusTender value (\$ millions) ^a
Transfield Services (Australia) Pty Ltd	September 2012–March 2014	Nauru—Garrison support	\$351
	March 2014–February 2017 ^b	Nauru and Manus Island—Garrison support and welfare services	\$2190
G4S Australia and New Zealand	October 2012–March 2014	Manus Island—Garrison support	\$245
Save the Children	October 2012–June 2013	Care and support services	\$8
	August 2013–August 2014	Provision of services to minors	\$37
	September 2014–October 2015	Welfare and education services	\$100
	May 2014–January 2015	Refugee settlement services	\$15
The Salvation Army	September 2012–January 2014	Welfare support for single men	\$99
TOTAL			\$3045

Note a: AusTender is the Australian Government's procurement information system. Relevant entities must report contracts and amendments on AusTender within 42 days of entering into (or amending) a contract if they are valued at or above the reporting threshold. For each contract reported, the entity must report the total value of the contract (including GST where applicable).

Note b: Extended to October 2017. Contract extension costs are not included in the table.

Source: ANAO analysis of AusTender information.

Commonwealth procurement

1.6 The Australian Government is a significant purchaser of goods and services and has in place resource management legislation and related policies that establish the framework for procurement and contracting. The *Commonwealth Procurement Rules* (CPRs) establish procurement principles that apply to all Australian Government procurement processes. The CPRs combine both Australia's

29 Transfield Services Group was rebranded on 30 October 2015 and Transfield Services (Australia) Pty Ltd's name changed to Broadspectrum (Australia) Pty Ltd on 30 November 2015. For consistency, the ANAO will use the name Transfield throughout this report for Broadspectrum (Australia) Pty Ltd. As at 13 May 2016 a Spanish company Ferrovial was in the process of taking over Transfield. [Internet], available from <<http://www.transfieldservices.com/news/ferrovial-today-announced-that-it-has-received-acceptances-for-92-05-of-broadspectrum-shares>> [accessed May 2016].

international obligations³⁰ and good practice, and enable entities to design processes that are robust, transparent and instil confidence in the Australian Government's procurement activities. The CPRs are issued under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act)³¹ by the Finance Minister and articulate the requirements for officials performing duties in relation to procurement. The CPRs are revised from time-to-time. The CPRs that apply to this audit are the version of July 2012 and the current CPRs issued in July 2014.³² The audit report reflects which version of the CPRs applied in a given context.

1.7 Achieving value for money is the core rule of the CPRs and requires the consideration of the financial and non-financial costs and benefits associated with procurement. The CPRs recognise that value for money is enhanced by encouraging competition through open tender processes, while also providing for other procurement methods in defined circumstances.

1.8 The PGPA Act requires entities to promote the proper use and management of public resources.³³ Under the CPRs proper use means efficient, effective, economical and ethical use. The CPRs provide that:

6.2 Efficient relates to the achievement of the maximum value for the resources used. In procurement, it includes the selection of a procurement method that is the most appropriate for the procurement activity, given the scale, scope and risk of the procurement.

6.3 Effective relates to the extent to which intended outcomes or results are achieved. It concerns the immediate characteristics, especially price, quality and quantity, and the degree to which these contribute to specified outcomes.

6.4 Economical relates to minimising cost. It emphasises the requirement to avoid waste and sharpens the focus on the level of resources that the Commonwealth applies to achieve outcomes.

6.5 Ethical relates to honesty, integrity, probity, diligence, fairness and consistency. Ethical behaviour identifies and manages conflicts of interests, and does not make improper use of an individual's position.³⁴

1.9 Under the CPRs, officials must also establish processes for the identification, analysis, allocation and treatment of risks when conducting procurements.

1.10 The CPRs describe three methods that officials can use when conducting procurements (see Box 1 below). These are open, prequalified and limited tender. The conditions for limited tender at or above the relevant procurement threshold are set out in Box 2. Regardless of the procurement method chosen, entities must apply the mandatory requirements set out in the two divisions of the CPRs:

30 This includes a range of free trade agreements.

31 The PGPA Act came into effect from 1 July 2014. Prior to this the use of public resources by Government departments was governed by the *Financial Management and Accountability Act 1997* and the Financial Management and Accountability Regulations 1997.

32 The July 2014 CPRs are available from [Internet], <<http://www.finance.gov.au/sites/default/files/2014%20Commonwealth%20Procurement%20Rules.pdf>> [accessed June 2016].

33 PGPA Act section 15, available from [Internet], <<https://www.legislation.gov.au/Details/C2013A00123>> [accessed June 2016].

34 Department of Finance, *Commonwealth Procurement Rules, 2014*. [Internet], available from <<http://www.finance.gov.au/sites/default/files/2014%20Commonwealth%20Procurement%20Rules.pdf>> [accessed June 2016].

- Division 1—rules applying to all procurements regardless of value. Officials must comply with the rules of Division 1 when conducting procurements; and
- Division 2—additional rules that apply to all procurements valued at or above the relevant procurement thresholds (unless exempted under Appendix A of the CPRs, see Box 3 below).

Box 1: Procurement methods and thresholds

The following are extracts from the CPRs:

Open tender—

9.8 Open tender involves publishing an open approach to market and inviting submissions.

Prequalified tender—

9.9 Prequalified tender involves publishing an approach to market inviting submissions from all potential suppliers on:

- a shortlist of potential suppliers that responded to an initial open approach to market on AusTender;
- a list of potential suppliers selected from a multi-use list established through an open approach to market; or
- a list of all potential suppliers that have been granted a specific licence or comply with a legal requirement, where the licence or compliance with the legal requirement is essential to the conduct of the procurement.

Limited tender—

9.10 Limited tender involves a relevant entity approaching one or more potential suppliers to make submissions, when the process does not meet the rules for open tender or prequalified tender.

9.11 For procurements at or above the relevant procurement threshold [see below], limited tender can only be conducted in accordance with paragraph 10.3 [refer Box 2 below for details], or when a procurement is exempt as detailed in Appendix A [refer Box 3 for details].

Procurement thresholds

9.7 When the expected value of a procurement is at or above the relevant procurement threshold and an exemption in Appendix A [refer Box 3 for details] is not utilised, the rules in Division 2 must also be followed. The procurement thresholds (including GST) are:

- for non-corporate Commonwealth entities, other than for procurements of construction services, the procurement threshold is \$80,000;
- for prescribed corporate Commonwealth entities, other than for procurements of construction services, the procurement threshold is \$400,000; or

Box 1: Procurement methods and thresholds

c. for procurements of construction services by relevant entities, the procurement threshold is \$7.5 million.

For the period July 2012–June 2014, under the 2012 version of the CPRs the threshold for procurements of construction services by departments was \$9 million.

Source: Finance, CPRs, 2014.

Box 2: Conditions for limited tender for procurement at or above the relevant procurement threshold

The CPRs outline the following conditions for limited tender:

10.3 A relevant entity must only conduct a procurement at or above the relevant procurement threshold through limited tender in the following circumstances:

a. when, in response to an approach to market

- i. no submissions, or no submissions that represented value for money, were received,
- ii. no submissions that met the minimum content and format requirements for submission as stated in the request documentation were received, or
- iii. no tenderers satisfied the conditions for participation,

and the relevant entity does not substantially modify the essential requirements of the procurement; or

b. when, for reasons of extreme urgency brought about by events unforeseen by the relevant entity, the goods and services could not be obtained in time under open tender or prequalified tender; or

c. for procurements made under exceptionally advantageous conditions that arise only in the very short term, such as from unusual disposals, unsolicited innovative proposals, liquidation, bankruptcy, or receivership, and which are not routine procurement from regular suppliers; or

d. when the goods and services can be supplied only by a particular business and there is no reasonable alternative or substitute for one of the following reasons

- i. the requirement is for works of art,
- ii. to protect patents, copyrights, or other exclusive rights, or proprietary information, or
- iii. due to an absence of competition for technical reasons; or

e. for additional deliveries of goods and services by the original supplier or authorised representative that are intended either as replacement parts, extensions, or continuing services for existing equipment, software, services, or installations, when a change of supplier would compel the relevant entity to procure goods and services that do not meet requirements for compatibility with existing equipment or services; or

f. for procurements in a commodity market; or

Box 2: Conditions for limited tender for procurement at or above the relevant procurement threshold

- g. when a relevant entity procures a prototype or a first good or service that is intended for limited trial or that is developed at the relevant entity's request in the course of, and for, a particular contract for research, experiment, study, or original development; or
- h. in the case of a contract awarded to the winner of a design contest, provided that
 - i. the contest has been organised in a manner that is consistent with these CPRs, and
 - ii. the contest is judged by an independent jury with a view to a design contract being awarded to the winner; or
- i. for new construction services consisting of the repetition of similar construction services that conform to a basic project for which an initial contract was awarded through an open tender or prequalified tender, and when the initial approach to market indicated that limited tender might be used for those subsequent construction services.

Source: Finance, CPRs, 2014.

Box 3: Exemptions from Division 2 of the CPRs

The following is an extract from Division 2 of the CPRs:

Procurements that are exempt from the rules of Division 2 by the operation of Appendix A are still required to be undertaken in accordance with value for money and with the rules of Division 1 of these CPRs.

Division 2 does not apply to:

1. leasing or procurement of real property or accommodation (note: the procurement of construction services is not exempt);
2. procurement of goods and services by a relevant entity from other Commonwealth, state, territory or local government entities when no commercial market exists or when legislation or Commonwealth policy requires the use of a government provider (for example, tied legal services);
3. procurements funded by international grants, loans or other assistance, when the provision of such assistance is subject to conditions inconsistent with this document;
4. procurements funded by grants and sponsorship payments from non-Commonwealth entities;
5. procurement for the direct purpose of providing foreign assistance;
6. procurement of research and development services, but not the procurement of inputs to research and development undertaken by a relevant entity;
7. the engagement of an expert or neutral person, including engaging counsel or barristers, for any current or anticipated litigation or dispute;
8. procurement of goods and services (including construction) outside Australian territory, for consumption outside Australian territory;

Box 3: Exemptions from Division 2 of the CPRs

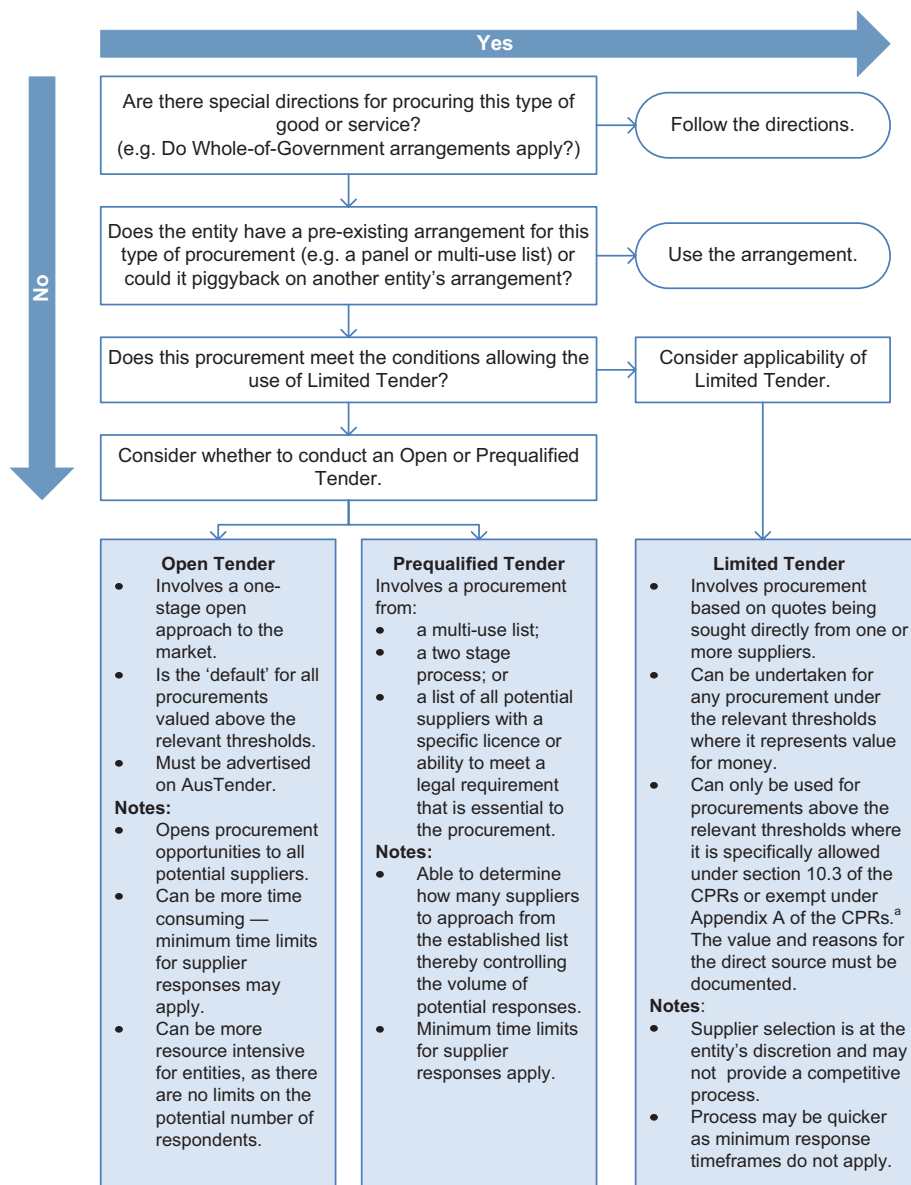
9. acquisition of fiscal agency or depository services, liquidation and management services for regulated financial institutions, and sale and distribution services for government debt;
10. procurement of motor vehicles;
11. procurement by the Future Fund Management Agency of investment management, investment advisory, or master custody and safekeeping services for the purposes of managing and investing the assets of the Future Fund;
12. procurement of blood plasma products or plasma fractionation services;
13. procurement of government advertising services;^[a]
14. procurement of goods and services by, or on behalf of, the Defence Intelligence Organisation, the Australian Signals Directorate, or the Defence Imagery and Geospatial Organisation;
15. contracts for labour hire;
16. procurement of goods and services from a business that primarily exists to provide the services of persons with a disability; and
17. procurement of goods and services from an SME with at least 50 per cent Indigenous ownership.

Note a: This includes information and advertising services for the development and implementation of information and advertising campaigns.

Source: Finance, CPRs, 2014, Appendix A.

1.11 Typical considerations for procurements at or above the relevant threshold are outlined in Figure 1.2.

Figure 1.2: Choosing a procurement method



Note a: Conditions for limited tender for procurement at or above the relevant procurement threshold are presented in Box 2 of this report and the Exemptions from Division 2 of the CPRs are outlined in Box 3 of this report.

Source: ANAO based on Department of Finance guidance.

1.12 The procurement framework emphasises the importance of being accountable and transparent in all procurement activities. Under the CPRs:

Accountability means that officials are responsible for the actions and decisions that they take in relation to procurement and for the resulting outcomes. Transparency involves relevant entities taking steps to enable appropriate scrutiny of their procurement activity.³⁵

Officials must maintain for each procurement a level of documentation commensurate with the scale, scope and risk of the procurement. Documentation should provide accurate and concise information on:

- a. the requirement for the procurement;
- b. the process that was followed;
- c. how value for money was considered and achieved;
- d. relevant approvals; and
- e. relevant decisions and the basis of those decisions.³⁶

1.13 Entities determine their own procurement practices, consistent with the CPRs, through Accountable Authority Instructions³⁷ and, if appropriate, supporting operational guidelines. The purpose of entity central procurement units (CPUs)³⁸ is to provide procurement expertise and advice to entity officials undertaking procurement processes and to assist in ensuring relevant requirements are met. Within DIBP limited tender procurements over the relevant threshold were also required to be agreed by the Chief Financial Officer for amounts above \$1 million.

DIBP advisory processes

1.14 The department's line management has responsibility for procurement matters. DIBP's central procurement unit provides advice to officers undertaking procurement activities. For the purposes of the garrison and welfare contracts, a policy implementation group was established by the then Secretary to provide day to day advice on strategic matters.³⁹ A Secretaries Committee on Immigration, which included central agency participants, was also formed to provide strategic oversight of the implementation of Government policy in this area.

35 Finance, CPRs, 2014, paragraph 7.1, p.19.

36 Finance, CPRs, 2014, paragraph 7.2, p.19.

37 Prior to the introduction of the *PGPA Act 2013* internal requirements equivalent to Accountable Authority Instructions (AAs) were known as Chief Executive Instructions.

38 The responsibilities of such units may include: strategic procurement planning; oversight or management of procurement processes; provision of procurement advice and support; development and maintenance of procurement policy and guidance; provision of procurement training; monitoring of entity procurement activity; and management of contract data and reporting.

39 Mr Martin Bowles PSM advised that during his time as Secretary of the department the policy implementation group met daily and later weekly. The group was comprised of policy, operational and legal officials. The ANAO has not been provided with any records of these meetings.

Audit approach

Audit objective, scope and criteria

1.15 The objective of the audit was to assess whether the Department of Immigration and Border Protection (DIBP) had appropriately managed the procurement of garrison support and welfare services at offshore processing centres in Nauru and Papua New Guinea (Manus Island); and whether the processes adopted met the requirements of the *Commonwealth Procurement Rules* (CPRs) including consideration and achievement of value for money.

1.16 The audit examined procurements conducted since 2012, when the arrangements were first put into place, through to the open tender process which commenced in 2015.

1.17 To form a conclusion against the audit objective, the ANAO adopted the following high level criteria:

- DIBP adhered to the requirements of the financial management framework when undertaking procurements (including procurement and budget requirements); and
- DIBP applied sound procurement practice.

Audit methodology

1.18 The ANAO reviewed DIBP and service provider records; and interviewed relevant DIBP officials (past and present) and stakeholders including service providers, tenderers and Government officials from Nauru and Papua New Guinea. The audit team also visited Manus Island and Nauru during August and September 2015. Fieldwork was conducted between March 2015 and March 2016.

1.19 Due to shortcomings in DIBP's record keeping system, the ANAO's review was based on the available records. In particular, departmental records often took the form of e-mail correspondence. DIBP was not able to provide the ANAO with assurance that it provided all departmental records relevant to the audit. During the period under review in this audit there was a complete turnover of senior departmental personnel responsible for the administration of the procurements.

1.20 The audit was conducted in accordance with the ANAO auditing standards at a cost to the ANAO of approximately \$1 116 208.

2. Establishing the offshore processing centres in 2012

Areas examined

This chapter examines the Department of Immigration and Border Protection's (DIBP) procurement processes and decisions relating to the procurement of garrison support and welfare services when establishing the offshore processing centres. The chapter also examines whether the procurement processes adopted were sound and met the requirements of the *Commonwealth Procurement Rules* (CPRs).

Conclusion

In deciding to establish the offshore processing centres in 2012, the Australian Government sought to achieve immediate outcomes. Asylum seekers first arrived in Nauru within three weeks of the relevant Government decision, providing very little time to put in place all the necessary contract arrangements for the operation of the centre. The department relied on limited tender approaches provided for in the CPRs, relating to urgent and unforeseen circumstances. Whilst this approach was open to the department and justified in the circumstances, more competition could have been applied to encourage better value for money outcomes for the Commonwealth.

The ANAO has identified issues with each of the four procurement processes undertaken at this time, and limited compliance with the CPRs. In summary:

- there was limited specification of the type of services to be delivered, and no estimation of the maximum value of individual procurements, as required by the CPRs;
- the department's available records indicated that with the exception of the process undertaken to engage G4S, DIBP did not establish that the procurement outcomes represented value for money;
- the available evidence indicated that potential suppliers were not always treated fairly or equitably—in engaging Transfield to undertake services in Nauru, the department set aside an earlier approach to Serco without an opportunity to negotiate. The department did not require Transfield to provide a proposal which specified the services delivered and costs, prior to offering Transfield the work;
- there was no available evidence of mechanisms to manage probity risks; and
- there was limited documentation around each of the procurement processes, to transparently record the department's decision-making.

Introduction

2.1 As part of the initial establishment of the offshore processing centres in Nauru and on Manus Island in 2012, the department undertook a series of limited tender procurements for garrison support and welfare services. For each of these procurements the ANAO examined:

- the planning for and use of limited tender;
- value for money;

- contract negotiations;
- probity arrangements; and
- involvement of the central procurement unit (CPU).

In adopting limited tender processes, did the department have regard to the mandatory requirements of the *Commonwealth Procurement Rules*?

For each of the procurements involved in this establishment phase, the department adopted limited tender arrangements. The department relied on the conditions for limited tender in the *Commonwealth Procurement Rules*, relating to urgent and unforeseen circumstances.⁴⁰ Given the circumstances which existed—the department was expected to establish operations for the offshore processing centres in Nauru and on Manus Island immediately—the use of limited tender was justified. However, there was limited specification of the type of services to be delivered, and no estimation of the expected value of individual procurements, as required by the *Commonwealth Procurement Rules*.

Planning for the initial procurements and use of limited tender

2.2 In deciding to establish the offshore processing centres in August 2012, the Australian Government sought to achieve immediate outcomes. While no dates were set for the commencement of the arrangements, the Government considered that the effectiveness of the arrangements in deterring boat arrivals would be determined by the speed with which the processing centres could be agreed with Nauru and Papua New Guinea (PNG), and established. The first asylum seekers arrived in Nauru on 14 September 2012, some three weeks after the Australian Government's decision. In order to procure garrison support and welfare services, the department undertook a series of procurements which resulted in contracts being entered into with Transfield Services, the Salvation Army, G4S and Save the Children.

2.3 The then departmental Secretary, Mr Martin Bowles PSM, advised the ANAO that:

In 2012 and in response to the Report of the Expert Panel on Asylum Seekers, the department worked within an exceptionally tight time period to establish Offshore processing. Planning in this context was exceptionally difficult. The changing nature of the challenges and the dynamic nature of policy development meant that the department often had to develop responses in an agile way to meet urgent requirements. This in and of itself presented significant challenges requiring policy, process, logistics, personnel and service providers to change and evolve in a fluid and often undefinable environment.

Consideration was also given to the operational complexities of service provision in the onshore network (specifically recognising that the network had increased exponentially over the previous 6 months with a significant number of new detention facilities opening). While a single onshore and offshore provider was considered, this was balanced with the risks relating to the service provider's current and future capability (noting the various pressures that continued to be faced in the onshore environment).

⁴⁰ See Footnote 16.

2.4 Department of Finance (Finance) guidance advises officials to ensure that the delegate is aware of the intended approach to market and, depending on the nature, complexity and risk of the procurements, is involved in the planning stages of the procurement.⁴¹ The department commenced the procurement processes for the garrison support and welfare services functions within days of the Australian Government's decision. Reflecting the priority, risks and sensitivities associated with the procurement, senior managers, including the then Secretary of the department, were directly involved in some of the processes.

2.5 Initially the department approached two suppliers (in late August 2012) to conduct all services across both centres. One supplier, Serco (who at the time was the provider of detention services onshore), provided a response. The department also held discussions with a second supplier, the International Organisation for Migration. Subsequently, the department separated the procurement into four processes. Three processes involved the department adopting a sole supplier approach. The fourth process, while also limited tender, involved more than one potential supplier, and so had an element of competition.

2.6 The 2012 *Commonwealth Procurement Rules* (CPRs) provided that an entity must only conduct a procurement at or above the relevant procurement threshold (\$80 000) through limited tender in defined circumstances (known as 'conditions for limited tender' and listed in Division 2 of the CPRs). One circumstance is where, for reasons of extreme urgency brought about by events unforeseen by the entity, the goods and services could not be obtained in time under open tender or prequalified tender.⁴² Each of the procurements undertaken in 2012 was valued at above the procurement threshold. DIBP considered that the circumstances and time pressures it faced to commence operations provided justification for the use of limited tender.

2.7 Where an entity relies on a condition for limited tender under Division 2 of the CPRs, it is also required to comply with the rules for all procurements appearing in Division 1 of the CPRs. While the department had by 2012 acquired extensive experience in the operation of onshore detention centres⁴³ through contractual arrangements, there was limited specification of the type of services required to be delivered, and no estimation of the maximum value of individual procurements, as required by the CPRs.

2.8 The 2012 CPRs stated that the expected value of each procurement must be estimated before a decision on the procurement method was made. The expected value was the maximum value (including GST) of the proposed contract, including options, extensions, renewals or other mechanisms that may be executed over the life of the contract.⁴⁴ The purpose of this requirement was to ensure that the likely Commonwealth financial commitment was properly considered and an appropriate procurement method selected.

2.9 A timeline of key events for the establishment of offshore processing centres in Nauru and on Manus Island is shown at Figure 2.1.

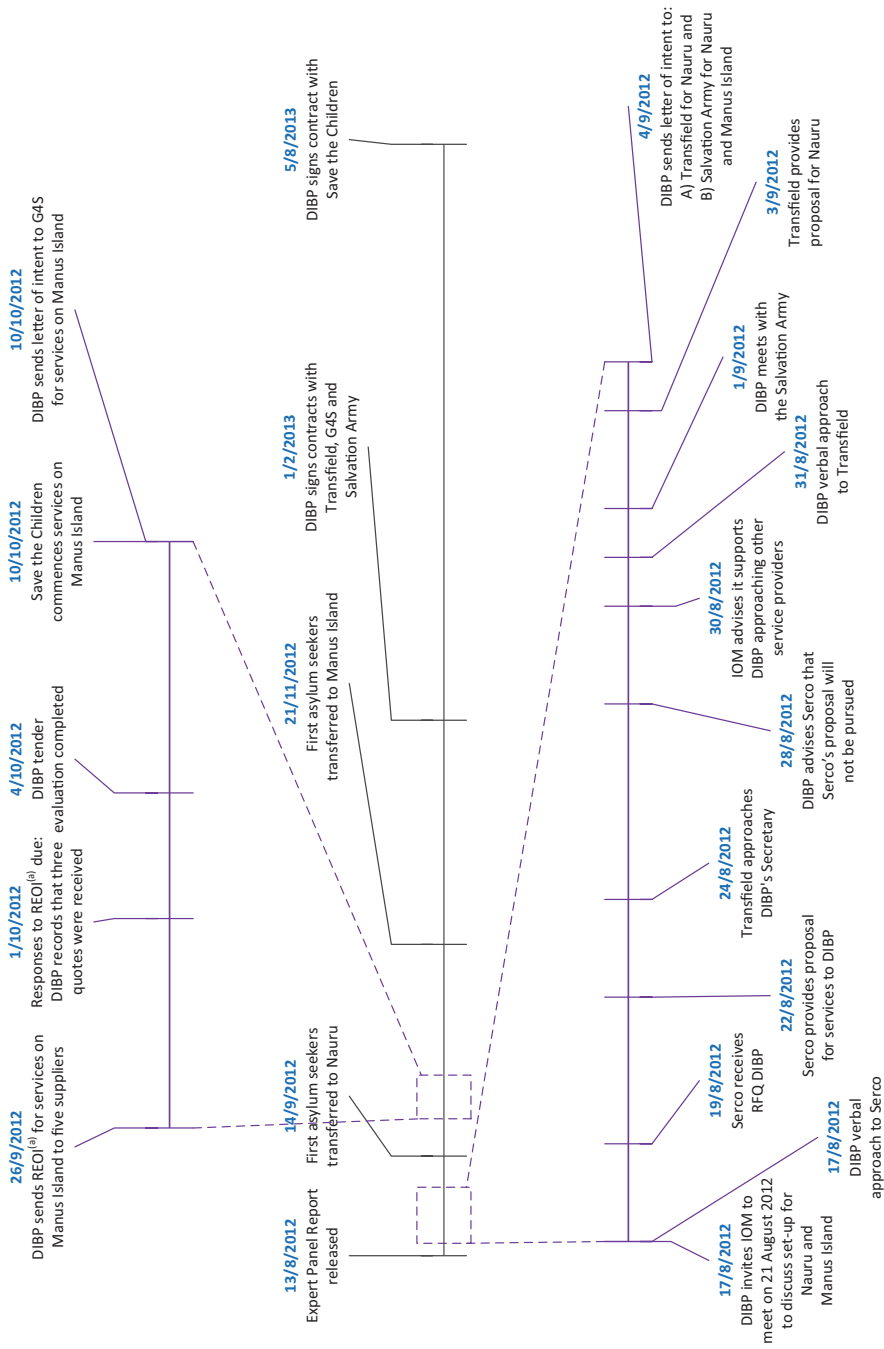
41 Department of Finance, *Buying for the Australian Government, Procurement Process Considerations—Tips*. [Internet] available from <<http://www.finance.gov.au/procurement/procurement-policy-and-guidance/buying/procurement-practice/process-considerations/tips.html>> [accessed June 2016].

42 Finance, CPRs 2012, paragraph 10.3(b).

43 The department also had previous experience operating offshore processing centres in Nauru and PNG between 2000 and 2008.

44 Finance, CPRs 2012, paragraph 9.2.

Figure 2.1: Timeline of key events for the establishment of offshore processing centres in Nauru and PNG (Manus Island)



Note a: Request for expression of interest (REOI).
Source: ANAO analysis of documentation from DIBP and service providers.

Did the department demonstrate value for money through the procurement and negotiation processes?

The department was unable to demonstrate the achievement of value for money in three of the four procurement processes.

- In engaging Transfield the department set aside an earlier approach to Serco.⁴⁵ The department did not require Transfield to provide a proposal specifying services to be delivered and a price. As a result it was very difficult for the department to demonstrate that it had conducted a robust value for money assessment which considered the financial and non-financial benefits of the proposal. Transfield was instead assessed on its ability to respond in a short timeframe.
- The Salvation Army⁴⁶ was also assessed as providing value for money on the basis of availability, without any specification of the services to be delivered or price.
- The department could not make available any records of how Save the Children⁴⁷ was assessed as providing value for money.
- G4S⁴⁸ was engaged following a limited tender procurement that involved a request for expressions of interest from five potential suppliers. This approach introduced competition in an otherwise limited tender procurement.

Contracts with service providers took between 16 and 43 weeks to negotiate, and the department relied on letters of intent or heads of agreement pending contract signature. Service requirements and prices were not settled until contracts were entered into. The approach adopted by the department introduced additional risk for the Commonwealth.

Value for money

2.10 Achieving value for money is the core rule of the CPRs. The 2012 CPRs provided that delegates must be satisfied, after reasonable enquiries, that the procurement achieved a value for money outcome. Determining value for money requires processes commensurate with the scale and scope of the procurement and a comparative analysis of the relevant costs and benefits throughout the whole procurement cycle (whole of life costing).⁴⁹

2.11 Under the CPRs a value for money assessment should include consideration of factors such as:

- fitness for purpose of the proposal;
- the potential supplier's experience and performance history;
- flexibility of the proposal (including innovation and adaptability over the lifecycle of the procurement); and

45 Serco Group Pty Ltd is referred to as Serco in this report.

46 The Salvation Army (New South Wales) Property Trust is referred to as The Salvation Army in this report.

47 Save the Children Australia is referred to as Save the Children in this report.

48 G4S Australia and New Zealand is referred to as G4S in this report.

49 2012 CPRs, paragraphs 4.4 and 4.5.

- whole-of-life costs.⁵⁰

2.12 The ANAO's findings in relation to each procurement process are set out below.

Approach to Serco

2.13 The department initially approached Serco verbally (17 August 2012) and then through a request for expression of interest (19 August 2012) for proposals for garrison support services in the centres in Nauru and on Manus Island. The department's request documentation stated that costs would not be binding, were intended to be indicative only and the information would be used to inform further discussions.

2.14 Serco responded to the request by the department's deadline, indicating its availability to perform the services required. For each location, Serco's proposal provided daily pricing options which varied depending on contract duration (three months, six to nine months and 12 months) and the number of asylum seekers. The proposal included pricing assumptions and details of specified additional costs that would need to be reimbursed by the department.⁵¹ The proposal also stated that costs were indicative only, and based on the limited information and timeframe available. Costs would be subject to review once an adequate scope was developed, contract terms agreed and time was available to access the facilities for a comprehensive review.

2.15 On 28 August 2012 (six days after submitting its response) Serco was advised that DIBP would not pursue the proposal further. DIBP has not provided the ANAO with evidence of a value for money assessment of Serco's proposal or why Serco's proposal was not further considered.

2.16 The then Secretary of the Department Mr Bowles, advised the ANAO that:

a number of internal discussions with the internal Policy Implementation Group were held. To my recollection the discussion to not proceed with the Serco proposal was largely based on the pressures on the onshore network managed by Serco. At the time the Department was exponentially increasing the number of onshore detention centres and increasing onshore detention capabilities. Numbers in onshore detention were increasing and at the height there were approximately 12,000 people in onshore detention centres. Monthly arrivals were continuing to increase, each month seeing a stepped increase on the previous month, these arrivals, aligned to the policy settings at the time were placing the onshore detention network and our service providers under pressure.

2.17 Key events in relation to DIBP's approach to Serco are listed in Table 2.1 below.

50 From 1 July 2014 entities were also required to consider the quality of the goods and services to be provided.

51 For example, the department would be expected to reimburse costs incurred for staff visas, licences and work permits.

Table 2.1: Key events in relation to DIBP’s approach to Serco

Date	Key events in relation to DIBP’s approach to Serco based on review of available documentation
17 Aug 2012	DIBP provided Serco with a verbal brief on services to be delivered.
19 Aug 2012	DIBP provided Serco with a written request for an indicative quote for services in Nauru and on Manus Island.
22 Aug 2012	Serco provided DIBP with an indicative proposal.
28 Aug 2012	DIBP advised Serco that it would not be pursuing the proposal further.

Source: ANAO analysis of DIBP documentation.

Approach to the International Organisation for Migration

2.18 The department’s records of its approach to the International Organisation for Migration (IOM) are limited. They indicate that IOM was approached (or approached the department) verbally in the week ending 17 August 2012. Further discussions were held over the following two weeks. Work at this time included preparing talking points for the Minister to meet with IOM. The department’s records do not indicate whether that meeting occurred. The department has advised the ANAO that it did not provide a request for quote to IOM at the time and did not receive a proposal detailing services to be provided or costs. The department’s records indicate that on 28 August the department provided a draft contract to IOM. The statement of work in this draft contract was incomplete and no fees were included. On 30 August the department determined not to pursue an arrangement with IOM any further.

2.19 The then Secretary of the Department Mr Martin Bowles, advised the ANAO that once negotiations with IOM failed it was decided to focus on Transfield as capacity, capability and timing were critical. Transfield had demonstrated this in their garrison provider work within Defence.

Engagement of Transfield Services

2.20 Available DIBP records indicate that on 24 August 2012 Transfield approached the then Secretary of the department by email to enquire if it could assist in Nauru:

It has been a while since we have spoken. How is it going in the world of the Department of Immigration, I am sure it is very busy to say the least.

Reason for contact is to enquire how Transfield Services can support you in your task in Nauru.

We can leverage DSG capability by mobilising a combination of our HSIP team and our Garrison team. As a trusted and proven partner of the Commonwealth this will give a highly compliant and flexible solution we believe.

We have recently successfully completed a similar exercise at Warmun.

2.21 The then Secretary responded verbally to Transfield and followed up by email on 31 August 2012 about performing garrison support services in Nauru. Later that day the department emailed Transfield a copy of the same request documentation provided to Serco (without deleting the Serco references).

2.22 In commenting on the brevity of the documentation provided, the department’s delegate for the procurement advised Transfield:

I'd be happy to arrange a little more oral briefing this afternoon to put a bit more flesh on the bones, so to speak, of the skimpy paper we forwarded to [Transfield employee]...

2.23 Transfield responded to the department on 3 September 2012 with a two page letter. The letter stated that Transfield understood the scope of the engagement but did not provide details of the services Transfield offered or the associated costs. Subsequently, Transfield provided the department with hourly wage rates for certain categories of workers by email (4 September 2012). There are no available DIBP records to demonstrate that the department attempted to compare the hourly wage rates provided by Transfield with the daily operational rates provided in the Serco proposal.

2.24 On 4 September 2012, the department provided Transfield with a letter of intent advising that it proposed to enter negotiations to agree on an initial Heads of Agreement (HOA) for the provision of interim garrison support services in Nauru. The intention was to finalise the HOA prior to Transfield commencing services on 11 September 2012. The department also advised Transfield that a contract for the provision of garrison support services in Nauru would be finalised as early as possible in October 2012.

2.25 As noted in paragraph 2.10, achieving a value for money outcome requires a comparative analysis of the relevant costs and benefits throughout the whole procurement cycle (whole of life costing), and a process commensurate with the scale and scope of the procurement. Available records indicate that the department solicited limited information from Transfield, making it very difficult for the department to demonstrate that it had conducted: a process commensurate with the value of the procurement; and a robust value for money assessment which considered the relevant financial and non-financial benefits of the proposal. Further, the services to be delivered were not specified by the department and a price was not elicited from Transfield.

2.26 The department acknowledged in its approval documentation that due to the urgency of the situation there was limited scope for value for money assessments to be done on the essential requirements. The department's value for money assessment was made on the basis that Transfield was able to respond and could deliver the required services in a short period of time. There was also no estimate of the full value of the services Transfield would provide until 1 February 2013 (the date of contract execution), when the department obtained internal approval for the commitment of \$184 263 702 for a 12 month period. By this time the department had already approved \$31.6 million under a Heads of Agreement. Transfield signed a contract on 1 February 2013 after having delivered services in Nauru for five months.

2.27 In considering value for money the department was also required, under the CPRs, to consider Transfield's experience and performance history.⁵² A key reason documented by the department for its selection, was that Transfield was on a Department of Defence panel for garrison support services (see Table 2.2).⁵³ Defence advised the ANAO that it did not have such a panel arrangement in place at that time. Defence further advised that it has no record of a request from DIBP seeking its views in August or September 2012 regarding the performance of its garrison

52 Finance, CPRs, 2012, paragraph 4.5b, p.15.

53 On 3 and 4 September 2012 Transfield advised DIBP that labour rate costs in September 2012 were drawn from Transfield's existing Department of Defence Garrison Support contracts for Western Australia and Victoria plus an adjustment factor to take into account the specific hardship and remote living allowances applicable to this location and work, and other factors.

support suppliers. Available DIBP records indicate that it had regard to Defence panel rates but it is not clear how this was possible if no Defence panel existed.⁵⁴

2.28 The department’s value for money assessment is provided at Table 2.2 below.

Table 2.2: Transfield—value for money assessment

Provider, initial expenditure approved and date of approval	DIBP value for money assessment
<p>Transfield \$6.1 million 19 September 2012</p>	<p>DIBP approval documentation states: ‘The Department sought proposals from Serco Australia Pty Ltd and the International Organization for Migration (IOM) for the provision of services. Serco’s proposal did not represent value for money. After discussions with IOM, they advised that the organisation would be unable to provide the services within the time frames required by the Department. Given the urgency of the situation there is limited scope for value for money assessments to be done on essential requirements. Transfield was approached to provide services on Nauru as they are on the Defence panel for Garrison Support services. The costing agreed to with Transfield is based on Defence panel rates, with a percentage increase applied to take into account of the location in which the services are supplied... All Service Providers have been able to respond to and can deliver the required services in a short period of time. This is a key element of the value for money assessment.’</p>

Source: ANAO presentation of DIBP approval documentation.

2.29 The 2012 CPRs required entities to establish processes for the identification, analysis, allocation and treatment of risk when conducting procurements.⁵⁵ Available documentation indicates that key risks were not assessed with respect to the Nauru offshore processing centre when establishing the arrangements. This was subsequently highlighted by Mr Keith Hamburger AM—in his 8 November 2013 *Review into the 19 July 2013 Incident at the Nauru Regional Processing Centre*—as a critical missing element essential to guide decisions relating to infrastructure and operations and to mitigate duty of care risks, particularly in the highly complex offshore processing environment.⁵⁶

54 The Department of Defence advised the ANAO that in the period identified (August or September 2012), Transfield did hold separate Garrison Services Support Contracts with Defence for the Western Australia, South Australia, Northern New South Wales, Tasmania and Victoria regions and a Comprehensive Maintenance Services contract for South Australia. Defence also advised that these were specific term contracts, not panel arrangements. Transfield also advised the ANAO that it had advised DIBP that held a number of contracts with the Department of Defence to provide garrison support services, but these were not panel arrangements.

55 Finance, CPRs, 2012, paragraph 8.2.

56 This report is available at [Internet] <https://www.border.gov.au/ReportsandPublications/Documents/reviews-and-inquiries/executive-report-nauru-2013.pdf> [accessed August 2016].

Engagement of The Salvation Army and Save the Children

2.30 The Salvation Army was engaged to provide welfare services at offshore processing centres between 14 September 2012 and 31 January 2014. The department advised that it engaged The Salvation Army after the organisation approached and offered its services. Save the Children was engaged to provide welfare services at the offshore processing centres between 10 October 2012 and 31 October 2015. The department was not able to provide the ANAO with documents relating to how the initial approaches with these organisations occurred.

2.31 The option of adopting limited tender processes for these procurements, on the basis of urgent and unforeseen circumstances, was available to the department under the CPRs. The department did not document why it adopted a sole source approach over alternatives such as a competitive limited tender process, given there were alternative suppliers of welfare services. While a record of the value for money assessment was available for The Salvation Army, no record was available for Save the Children. The department's value for money assessment for The Salvation Army is provided below at Table 2.3.

Table 2.3: The Salvation Army—value for money assessment

Provider, initial expenditure approved and date of approval	DIBP value for money assessment
The Salvation Army \$2.1 million 19 September 2012	<p>DIBP approval documentation states:</p> <p>'Given the urgency of the situation there is limited scope for value for money assessments to be done on essential requirements.</p> <p>The Salvation Army is a not for profit organisation. They indicated that costings (not finalised at the time) would be based on an actual costs basis (staff and equipment) with a mark-up to cover the corporate and administrative costs incurred Onshore.</p> <p>All Service Providers have been able to respond to and can deliver the required services in a short period of time. This is a key element of the value for money assessment.'</p>

Source: ANAO presentation of DIBP approval documentation.

Engagement of G4S

2.32 G4S was engaged to provide garrison support services at Manus Island following a limited tender procurement that involved a request for expressions of interest being sent to five potential suppliers.⁵⁷

2.33 Potential suppliers were given five days to respond. Sending the request to more than one supplier introduced competition in an otherwise limited tender procurement and provided a firmer basis for the department's assessment of value for money. DIBP's tender evaluation documentation indicates that the department compared the responses of the three suppliers who submitted proposals (including G4S and Transfield).⁵⁸ The department was unable to provide a copy of one

57 The department obtained internal approval to conduct the process as a limited tender some five days after completion of the evaluation process.

58 Two suppliers advised the department they would not be submitting a proposal, with one indicating it was due to the very limited timeframe offered.

proposal from an unsuccessful supplier. The department’s approval documentation reports that Transfield’s bid was found to be four times more expensive than G4S. The remaining supplier’s bid was lower than the other bids but its scope of services was more limited.

2.34 The tender evaluation team recommended the engagement of G4S as the service provider for Manus Island. A summary of the department’s value for money assessment is provided below at Table 2.4.

Table 2.4: G4S—value for money assessment

Provider, initial expenditure approved and date of approval	DIBP value for money assessment
G4S \$30 million 12 October 2012	DIBP approval documentation states: ‘The Evaluation Team considers G4S to be the preferred supplier as they are considered to be value for money due to, but not limited to: the technical evaluation; the price; and the risk.’

Source: ANAO presentation of DIBP approval documentation.

Contract negotiations

2.35 The 2012 CPRs required that unless a relevant entity determines that it is not in the public interest to award a contract⁵⁹, it must award a contract to the tenderer that the relevant entity has determined:

- satisfies the conditions for participation;
- is fully capable of undertaking the contract; and
- will provide the best value for money, in accordance with the essential requirements and evaluation criteria specified in the approach to market and request documentation.⁶⁰

2.36 The department entered into contract negotiations after it placed each of the service providers on the ground in Nauru and on Manus Island. In the absence of a contract, providers operated under a letter of intent or heads of agreement. The department’s correspondence to providers confirmed that it intended to agree on a contract ‘as early as possible’. In the event it took up to 43 weeks for contracts to be signed. Table 2.5 shows the duration of contract negotiations after the commencement of service delivery by each provider.

59 Relating to a procurement above the relevant procurement threshold, as outlined in Division 2 of the CPRs.

60 Finance, CPRs, 2012, paragraph 10.31.

Table 2.5: Duration of contract negotiations after the commencement of services in Nauru and on Manus Island

Service provider	Weeks between commencement of services on site and executed contract	Date services commenced on site ^a	Arrangement under which services commenced, and date arrangement executed
Transfield ^b	20	11 September 2012	Letter of Intent, 4 September 2012
The Salvation Army ^b	20	11 September 2012	Letter of Intent, 4 September 2012
Save the Children ^c	43	10 October 2012	Heads of Agreement, 17 April 2013
G4S ^c	16	10 October 2012	Letter of Intent, 12 October 2012

Note a: Services commenced in Nauru on 11 September 2012 and on Manus Island on 10 October 2012. The services providers had commenced preparation and incurred costs prior to these dates.

Note b: Transfield and The Salvation Army commenced services in Nauru.

Note c: Save the Children and G4S commenced services on Manus Island.

Source: ANAO analysis.

2.37 The department entered the arrangements while still negotiating price and the specifics of the services to be delivered. Services and price were not agreed between the parties until contract negotiations ended. In the case of Transfield this was almost five months after it commenced operations. For G4S it was four months after the commencement of operations.

2.38 The department advised the ANAO that letters of intent and heads of agreement offered less legal protection than a contract but were part of its strategy to mitigate scope and cost risk as it allowed the department to tighten performance specifications and costs, based on a period of actual operation. The department also advised that entering into a contract immediately may have locked the Commonwealth into provisions and arrangements which would be difficult to undo or amend. The approach adopted by the department increased risk for the Commonwealth and DIBP was not able to provide the ANAO with records documenting the strategy or any consideration of risks relating to the approach adopted. For example, a risk based approach would have considered why the contract used for onshore services could not have been adapted to suit the offshore environment or the draft contract prepared and provided to IOM for services on Nauru (see paragraph 2.18) could not have been used. At the very least, it would have been prudent to assess the risks arising from the speedy establishment of the centres.

Did the department establish processes to manage probity risks?

The department was not able to provide the ANAO with evidence that it implemented mechanisms to manage probity risk. The ANAO's review, based on available evidence, of the conduct of these initial procurements indicates that suppliers were not always treated fairly or equally. In particular, Serco's proposal was set aside without an opportunity to negotiate. The available records indicate that the department did not seek probity advice on this proposed course of action or document its decision-making. There are no available records of specific conflict of interest declarations having been made by departmental officers responsible for the initial procurements.

Probity arrangements

2.39 The 2012 CPRs required that officials undertaking procurement must act ethically throughout the procurement. The CPRs advised that ethical behaviour includes:

- recognising and dealing with actual, potential and perceived conflicts of interest;
- dealing with potential suppliers, tenderers and suppliers equitably, including by seeking appropriate internal or external advice when probity issues arise, and not accepting inappropriate gifts or hospitality;
- carefully considering the use of public resources; and
- complying with all directions, including relevant entity requirements, in relation to gifts or hospitality, privacy requirements and the security provisions of the *Crimes Act 1914*.⁶¹

2.40 Based on available evidence, the ANAO's review of the conduct of these initial procurements indicates that suppliers were not always treated fairly or equally. In particular:

- Serco's proposal, which contained indicative costings, was set aside without evidence of a value for money assessment or the opportunity to negotiate; and
- the department advised Transfield that it proposed to enter into negotiations with them one day after receiving Transfield's letter and details of hourly wage rates.

2.41 There is no DIBP documentation indicating that the department sought probity advice on its proposed course of action and no documented record of its decision making. In the course of this audit the then Secretary of the department advised the ANAO that he recalled speaking to internal lawyers relating to probity issues.

2.42 The department was not able to provide the ANAO with:

- evidence that it implemented mechanisms to manage probity risk; or
- records of conflict of interest declarations having been made by departmental officers responsible for the initial procurements.

2.43 In the absence of a procurement specific process to manage probity risk, the ANAO requested access to the more general declarations of interest of relevant Senior Executive Service

⁶¹ Finance, CPRs, 2012, paragraph 6.6.

(SES) staff, to establish whether any relevant declarations had been made by them. The department could not provide all of the declarations for relevant senior executives and advised that records for former staff may not have been retained. On request, the then Secretary, Mr Bowles, provided the ANAO with his declaration to cover the period.

Were relevant approvals by the Chief Financial Officer obtained prior to commencing the procurement process?

The department's central procurement unit had limited effective oversight of the initial limited tender procurements. Available records indicate that program areas with responsibility for conducting the initial procurements obtained the necessary approvals to conduct limited tender procurements from the Chief Financial Officer, but not prior to commencing the procurement process as required by DIBP's financial delegations.

The central procurement unit

2.44 In 2012 DIBP's financial delegations required all limited tender procurements over the relevant threshold (\$1 million) be approved by the Chief Financial Officer (CFO). Under these arrangements the area within the department with program responsibility conducted the procurements while the CFO (who had responsibility for the central procurement unit) approved the use of limited tender for each relevant procurement.

2.45 For Transfield and the Salvation Army the CFO approved the use of limited tender after the program area had already identified the suppliers and had provided letters of intent allowing services to commence.

2.46 CFO approval for conducting a limited tender to engage service providers on Manus Island was sought prior to going out for a request for quote from potential suppliers but was not provided until after the process was completed. G4S commenced operations in October 2012. In January 2013 the program area sought approval to amend the terms of the limited tender from an initial 12 months to include a provision to extend for a further period of 12 months. The Assistant Secretary, Property, Procurement and Contracts Branch (the CPU) noted 'I cannot support a 12 month extension option when our reason for limited tender is urgent and unforeseen', and the CFO approved a limited tender for a period of 12 months with no extension.

2.47 The department has not retained the original limited tender approval documentation for Save the Children. Available documentation indicates that Save the Children commenced providing services in October 2012 and approval for limited tender was obtained on 17 April 2013. Prior to the original Heads of Agreement expiring (on 30 June 2013), the department sought approval (on 24 June 2013) from the Assistant Secretary, Property, Procurement and Contracts Branch (not the CFO) to continue to engage Save the Children for a further seven months via a contract. The basis for this request was under paragraph 10.3(e) of the 2012 CPRs:

for additional deliveries of goods and services by the original supplier or authorised representative that are intended either as replacement parts, extensions or continuing services for existing equipment, software, services or installations, where a change of supplier would compel the agency to procure goods and services that do not meet requirements for compatibility with existing equipment and services.

2.48 On 25 June 2013 the Assistant Secretary approved the request noting that ‘this is an unusual proposal. The services are not of a type usually contemplated under 10.3(e) of the CPRs. However, I consider that this proposal is broadly consistent with the intent of that clause.’

3. Consolidation of contracts in Nauru and on Manus Island in 2013–14

Areas examined

This chapter examines the Department of Immigration and Border Protection's (DIBP) procurement processes and decisions relating to the consolidation of contracts for the procurement of garrison support and welfare services in Nauru and on Manus Island in 2013–14. It also examines whether the processes adopted were sound and met the requirements of the *Commonwealth Procurement Rules* (CPRs).

Conclusion

The department decided to consolidate contracts for the provision of garrison support and welfare services and conducted a limited tender relying on paragraph 10.3(b) of the CPRs—relating to urgent and unforeseen circumstances. The available record does not indicate such circumstances existed. The department first selected the provider and then commenced a process to determine the exact nature, scope and price of the services to be delivered.

The reasons for not continuing with the existing provider (G4S) were not clearly documented. Advice prepared by the department's Central Procurement Unit was not consistent with the CPRs and the Department of Finance (Finance) guidance on key issues. In seeking advice from Finance, the Unit made written statements implying underperformance by service providers which was not supported by the evidence. The department subsequently referenced Finance's support in briefings for its Minister.

Engaging Transfield through limited tender procurement placed the department in a position where it removed competition from the process at the outset. When a price was put forward by Transfield it was higher than anticipated and far exceeded that charged by G4S.

The department applied a benchmark model to demonstrate the achievement of value for money. Overall the benchmark was adjusted above historical costs, upwards to \$372 million, to accommodate a number of service enhancements. The Government had directed the department to reduce per-head costs. The department had no authority to increase the funding value of the contract above historic costs.⁶²

Separate benchmarks were developed for Nauru and Manus Island, but the department determined 'value for money' and claimed savings (against the benchmarks) on a combined basis. While Transfield's bid for Nauru was lower than historical costs, the bid for Manus Island exceeded historical costs by between \$200 million and \$300 million.

The intent of the consolidation was to achieve innovation and savings. In estimating savings the department based its calculations on higher capacity levels which were never achieved. The department was aware of the fall in the number of new boat arrivals in early 2014, but continued to use higher than actual levels to determine expected costs. This approach resulted in a risk of the Commonwealth locking-in a premium for service delivery under the contract.

62 The ANAO reviewed records of PM&C, Finance and DIBP relating to the Government's decisions and Ministerial approvals.

The Prime Minister had requested that per head costs be lower as a result of retendering the contracts, but the department did not calculate a per person cost. Finance advised the ANAO that under the consolidated contract, the per person per annum cost of holding a person in the offshore processing centres in Nauru and on Manus Island at the Mid-Year Economic and Fiscal Outlook 2015–16 in December 2015, was \$573 111. Prior to consolidation Finance estimated the cost at \$201 000.

3.1 The Australian Government commenced Operation Sovereign Borders on 18 September 2013. Operation Sovereign Borders continued the offshore processing of asylum seekers in Nauru and Papua New Guinea (Manus Island). The Government also sought to achieve innovation and savings through consolidating the garrison support and welfare services contracts. At the time, consolidation was considered an interim measure pending an open tender process in 2014.

3.2 Transfield and Save the Children were selected by the department to perform the services. The selection of Transfield (to deliver a consolidated contract) attracted considerable media and parliamentary attention, focusing on:

- the use of limited tender procurement and the exclusion of G4S from the tender process;
- the value of the contract (\$2.1 billion) as reported on AusTender;
- reported contract savings of \$77 million⁶³; and
- recommendations made in the National Commission of Audit (see paragraphs 3.13 to 3.18) including that:

by renegotiating contracts and better targeting of services, the per person cost of operating the onshore immigration network be reduced to 2011–12 levels and similar efficiencies be sought for the offshore network.⁶⁴

3.3 In respect to the consolidation of contracts for garrison support and welfare services in Nauru and on Manus Island, the then departmental Secretary, Mr Martin Bowles PSM advised members of the Legal and Constitutional Affairs Legislation Committee in February 2014, that:

The reason for changing the arrangements on Manus had nothing to do with the performance of the contract. It was to do with trying to get synergies from having one provider working across both islands. The work we have done in the department,⁶⁵ trying to understand how we manage those two islands, led us to believe that the best way to do that was with a single contractor. It will drive logistical improvements and further efficiencies when we can actually put them together. The decision, which was ultimately made by me, was that we would transition out of G4S on Manus to Transfield.⁶⁶

63 In May 2014, the department advised the Parliament’s Legal and Constitutional Affairs Committee that \$2.1 billion was the maximum potential cost of the contract and that the new contract achieved savings of \$77 million.

64 National Commission of Audit Recommendation 46: Containing costs associated with Illegal Maritime Arrivals [Internet] available from <<http://www.ncoa.gov.au/report/phase-one/recommendations.html>> [accessed June 2016].

65 ANAO comment: Available documentation does not include any record of work performed by DIBP on potential improvements or efficiencies arising from one provider.

66 Official Committee Hansard, Senate Legal and Constitutional Affairs Legislation Committee—Estimates, 25 February 2014, Canberra, p. 79. Evidence provided by Mr Bowles. [Internet] available from <<http://parlinfo.aph.gov.au/parlInfo/download/committees/estimate/5972266f-4662->

3.4 The ANAO reviewed whether the procurement process for the consolidated contract was conducted in accordance with the *Commonwealth Procurement Rules* (CPRs) and if the contract achieved the innovations and savings required by Government. In particular, the ANAO examined:

- the planning for consolidation and use of limited tender;
- procurement advice;
- contract negotiations and value for money; and
- probity and conflict of interest.

Was the adoption of a limited tender process on the grounds of urgent and unforeseen circumstances appropriately documented and defensible?

The department again relied on paragraph 10.3(b) of the CPRs⁶⁷ to conduct a limited tender, on the basis of urgent and unforeseen circumstances, to engage Transfield in Nauru and on Manus Island as part of a contract consolidation process. At the time, consolidation was considered an interim measure pending an open tender process in 2014. The available record does not indicate that urgent or unforeseen circumstances existed but suggests that the department first selected the provider and then commenced a process to determine the exact nature, scope and price of the services to be delivered.

- The department decided not to continue with the existing provider (G4S), but did not clearly document its reasons.
- Advice prepared by the department's Central Procurement Unit was not consistent with the CPRs and the Department of Finance (Finance) guidance on key issues. In seeking advice from Finance, the Unit made written statements implying underperformance by service providers which was not supported by the evidence. The department subsequently referenced Finance's support in briefings for its Minister.

Planning for consolidation and the use of limited tender

3.5 The CPRs require that all procurements over the threshold (see Box 1) be undertaken using open tender, unless the conditions for limited tender under paragraph 10.3 can be met, or the procurement is exempt under Appendix A of the CPRs.

3.6 The department began a procurement process which resulted in consolidation of the garrison support and welfare contracts in early November 2013 when the then Minister requested advice on options for service delivery on Manus. Available departmental records indicate that the

[4bc3-a322-e674390efe88/toc_pdf/Legal%20and%20Constitutional%20Affairs%20Legislation%20Committee_2014_02_25_2256_Official.pdf;fileType=application%2Fpdf#search=%22committees/estimate/5972266f-4662-4bc3-a322-e674390efe88/0000%22>](#) [accessed June 2016].

67 Paragraph 10.3 of the 2012 and 2014 CPRs sets out the conditions for limited tender above the relevant procurement threshold. Paragraph 10.3(b) allows limited tender to be conducted when, for reasons of extreme urgency brought about by events unforeseen by the relevant entity, the goods and services could not be obtained in time under open tender or prequalified tender.

options canvassed with the Minister's Office involved the use of limited tender processes which would result in G4S's contracts being taken over by: Serco as an extension to Serco's existing onshore contract; or by Transfield as an extension to its contract in Nauru. The option of Save the Children undertaking the Salvation Army's contract for welfare services was also canvassed.⁶⁸

3.7 Serco advised the ANAO that it was not approached in 2013 to provide services on Manus Island. The department's records indicate that the option of engaging Serco through limited tender was not pursued on the basis that:

it would be bringing a new provider into offshore services and we would have no basis to do a limited tender to just Serco when Transfield has a proven capability in offshore garrison support services.

3.8 A number of firms had approached the department in mid-October 2013 with proposals regarding service provision. Transfield approached the Secretary by email (on 14 October 2013) stating that they had reviewed their operations on Nauru and could offer suggested changes to the contracting model to make it more effective and efficient in delivering stable and successful operations. It was proposed that these changes would result in an overall reduction in cost per transferee. Transfield also stated that it was taking a de facto leadership role on Nauru and could lead the ongoing operations on the Island using an integrated management approach:

The original concept was for the Salvation Army to act as the lead agency however evidence indicates that they are not comfortable with this role. Our assessment is that logistics (to ensure maximum capacity at all times) and intelligence (to ensure voluntary returns and more rapid processing) are the key factors for ongoing success on Nauru. We believe Transfield Services could lead the ongoing operations on the Island using an integrated management approach.⁶⁹

3.9 The then Secretary was also approached by G4S (on 14 October 2013) with a proposal to deliver services in Nauru and on Manus Island. There is no available record of the department having considered that proposal or having responded to G4S.

3.10 The department met with Transfield in mid-November 2013 with a view to having a close-to-agreed proposal ready for execution if approved later that month, and arrangements in place by February 2014. From this point preparations were made for a contract to be entered into with Transfield. The preparations included commercial advice from an external adviser (KPMG) on how a process could be run to determine the price and scope of the services Transfield would provide in Nauru and on Manus Island. Available DIBP email records also indicate that by 17 November 2013, the department had 'the Minister's clearance' to the consolidation proposal. At this time the department considered seeking the Minister's approval for a short contract extension for G4S and The Salvation Army through to the commencement of the new arrangement.

3.11 Other key meetings with service providers which occurred at the time, and related correspondence, included:

68 At the time, Save the Children's contract to provide welfare services in Nauru did not expire until 1 August 2014.

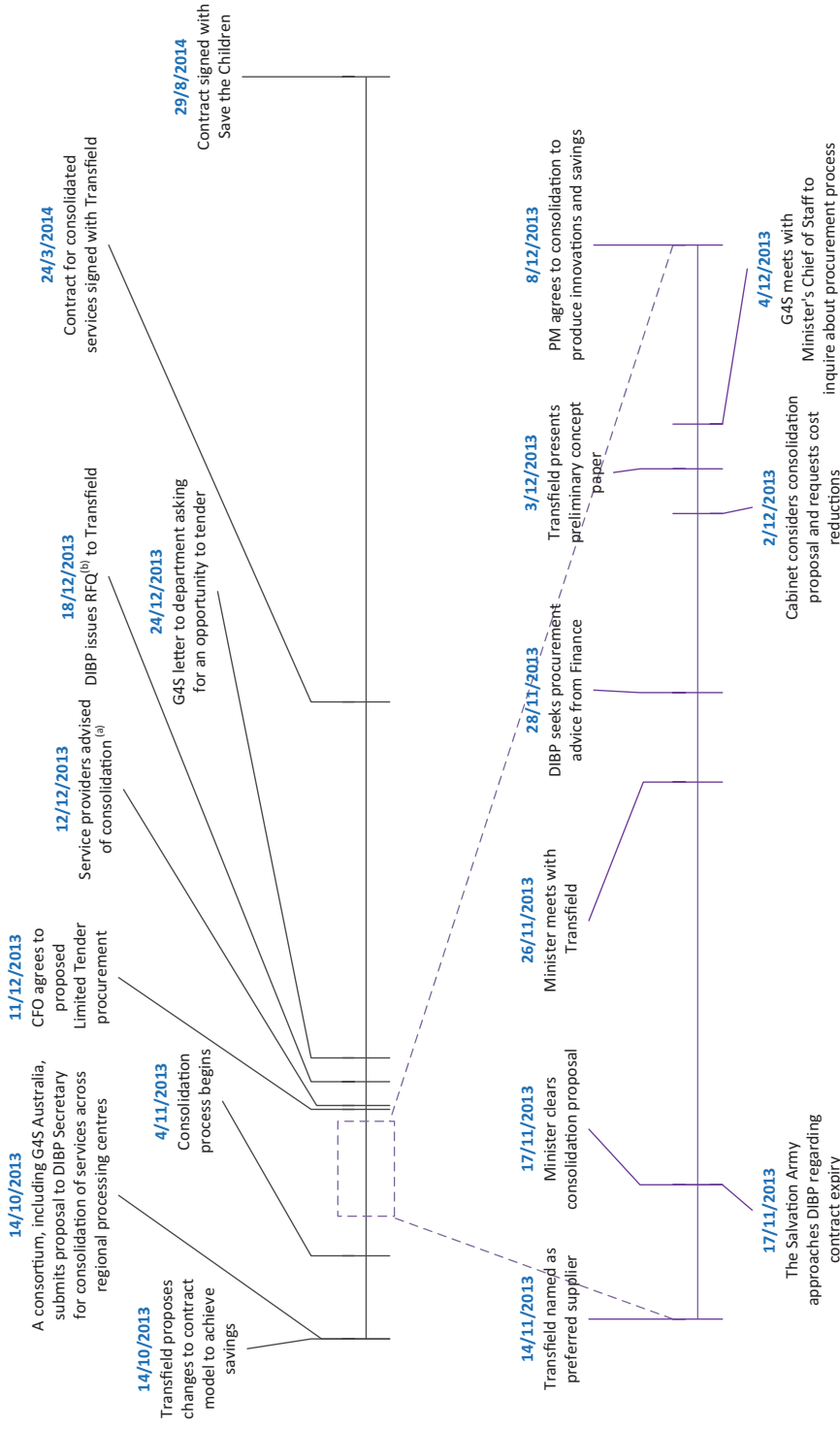
69 At the time The Salvation Army was the lead service provider and the focus of their contract was welfare.

- 16 November 2013—The Salvation Army approached the department for advice on the expiry of its contract. The Salvation Army advised that it was experiencing difficulties in engaging and retaining staff as a result of not yet having a decision on whether its contract would be extended.
- 26 November 2013—the Minister met with Transfield, at the Minister’s request.
- 3 December 2013—Transfield presented the department with a preliminary concept of operations paper for service delivery in Nauru and on Manus Island identifying annual estimated savings of \$14.76 million. In providing this paper to the department, Transfield noted:
 - ‘Further to Transfield Services’ meeting with Minister Morrison last week and a subsequent discussion with Martin Bowles [the then Secretary] yesterday, please find attached Transfield Services’ Concept of Operations for the integration of Nauru and Manus Island into a single service delivery model.’
- 4 December 2013—G4S met with the Minister’s Chief of Staff advising that its contract was due to expire and expressing concern at not knowing if the contract would be extended. In email correspondence with the department, the Chief of Staff observed that G4S had assumed that its existing contract would be extended for an unspecified period and there had been no request for tender. The Chief of Staff also recorded that she had made no comment in this regard (due to probity concerns) except to say that contract management was a matter for the department.
- 12 December 2013—G4S and The Salvation Army were advised of the contract consolidation and a short term extension to their contracts pending their departure from service delivery in Nauru and on Manus Island. Save the Children was not advised of the consolidation proposal, rather the department wrote to them requesting a variation to the extension clause in the contract. The department’s letter also indicated that a longer term extension to 31 October 2015 may be possible, which would include various other amendments to the contract, if appropriate cost reductions could be achieved.⁷⁰

3.12 A timeline commencing with the decision to consolidate contracts on 4 November 2013 through to DIBP signing contracts with Transfield (on 24 March 2014) and Save the Children (on 29 August 2014) is set out in Figure 3.1.

70 The letter sent to Save the Children requested a variation to the extension clause in the contract, from an extension option of ‘one period up to 12 months’ to ‘periods to total of 12 months’. The letter also indicated that a longer term extension to 31 October 2015 may be possible which would include various other amendments to the Contract, if appropriate cost reductions could be achieved.

Figure 3.1: Timeline of key events and decisions for contract consolidation



Note a: Save the Children was not advised of the consolidation.

Note b: Request for quote (RFQ).

Source: ANAO analysis of documentation from DIBP and service providers.

Recommendations by the National Commission of Audit

3.13 The National Commission of Audit was announced by the Treasurer, the Hon Joe Hockey MP, and the Minister for Finance, Senator the Hon Mathias Cormann, on 22 October 2013. The Commission was established by the Australian Government as an independent body to review and report on the performance, functions and roles of the Commonwealth government.

3.14 Commission Chair Mr Tony Shepherd AO had been Chairman of Transfield for a decade until his resignation on 23 October 2013. The ANAO sighted evidence which demonstrated that at the time of his resignation, Mr Shepherd divested himself of all interests in Transfield and shortly thereafter (14 and 15 November 2013) sold his shareholdings.

3.15 The then Secretary of the department (Mr Bowles) met with the National Commission of Audit including the Commission Chair and Secretariat on 28 November 2013, as part of the Commission's consultative processes with Commonwealth entities. DIBP also made a submission to the Commission and there was a subsequent request from the Commission for additional information. There were no DIBP or Commission of Audit records that indicated the department's contracts with Transfield were discussed. Mr Bowles and Mr Shepherd advised the ANAO that the department's contract with Transfield was not discussed.

3.16 In its February 2014 report the National Commission of Audit observed that the detention and processing of illegal maritime arrivals:

has been the fastest growing Government programme over recent years.

3.17 The Commission recommended that:

- (a) by renegotiating contracts and better targeting of services, the per person cost of operating the Onshore immigration network be reduced to 2011–12 levels and similar efficiencies be sought for the offshore network; and
- (b) this process also be supported by an audit of the scope and cost of services currently being provided and how these have changed over time.⁷¹

3.18 In reflecting on the Commission's work, Mr Shepherd advised the ANAO that:

The NCOA was charged with reviewing some \$408 billion in Commonwealth expenditure over three months and concentrated on the main offenders. However, as the ANAO draft [performance audit] report says we were concerned about the growing cost of onshore and offshore processing and recommended steps to contain and reduce these costs. Like many of the Recommendations in the NCOA Report I am not aware of whether there was any follow through by the Commonwealth.

Procurement advice

3.19 DIBP officials responsible for the consolidation process sought procurement advice from the department's Central Procurement Unit (CPU) on the possibility of extending the contracts and/or conducting a limited tender process. The CPU considered that under the CPRs:

71 National Commission of Audit Recommendation 46: Containing costs associated with Illegal Maritime Arrivals [Internet] available from <<http://www.ncoa.gov.au/report/phase-one/recommendations.html>> [accessed June 2016].

a variation to extend a contract beyond the terms of the original contract where the contract has no further options to extend, and where the services are within scope/the same, is possible, so long as a new checklist for procurement is completed in accordance with the CPRs, amongst other things, to confirm that the Department has a continuing need for the Services, has considered and addressed the relevant risks and has ensured that the extension will continue to represent value for money. Subject to the new procurement checklist being adequately completed, it is open to the department to extend a contract to cover service provision during an approach to market.

3.20 That advice was not consistent with Finance guidance, which stated that a:

variation to extend a contract or deed of standing offer beyond the terms of the original contract (rather than exercising an extension option within the terms of a contract), is a new procurement that must be conducted in accordance with the CPRs. Variations to include new extension options generally increase the scope of the contract or panel arrangement and are therefore not allowed.⁷²

3.21 The CPU also proposed as one option, that the procurement could be conducted overseas so the CPRs would not apply. The CPU advised that:

it was open to the department to undertake a limited approach to the market, so long as the procurement process occurred outside of Australia. To facilitate this, the CPU suggested that the department ask staff on Manus or Nauru to undertake this work, or engage Transfield or another process manager to do this, noting that it was unlikely that Transfield would be permitted to tender for the same services that it is managing.

3.22 The advice did not address the risks to achieving value for money in the absence of competition.

3.23 On 28 November 2013, the CPU sought Finance advice on conducting a limited tender relying on paragraph 10.3(b) of the CPRs—relating to urgent and unforeseen circumstances.⁷³ The department advised Finance that:

DIBP has contracts operating in the offshore space, these contracts involve issues with the contract providers and the level of services we are receiving, there is areas of underperformance amongst other issues. We have had a scrutiny and recommendation report recommending that we not take up the extension option available to us due to the underperformance by the service providers and the risk to us knowing this and not ending the contracted services.

Due to Government commitments and the political and sensitive nature of services offshore and at detention facilities we cannot simply end the services whilst we approach the market through an open approach. We therefore seek to engage another service provider who is already providing similar services at another Immigration site and has been previously assessed as representing value for money.

We wish to complete this under CPR exemption 10.3(b) as an interim arrangement until 2015, by which time we expect to have an ATM [approach to market] for existing services and any new or changed services, depending on the nature of Government decisions and policies.

72 Finance, Buying for Australian Government [Internet], available from <<http://www.finance.gov.au/procurement/procurement-policy-and-guidance/buying/procurement-practice/tender-evaluation/practice.html>> [accessed March 2016]. Finance advised the ANAO that advice on variations is unchanged from 2012.

73 See paragraph 2.6 and 2.7 of this audit report.

Based on our conversation/s today, I believe that DoF [Finance] is in agreement that this exemption could be used appropriately as a bridging mechanism whilst further market approaches are undertaken.

3.24 The ANAO was advised by DIBP that the ‘report’ referred to by the CPU was a November 2013 decision brief for the Commander of the Joint Agency Taskforce, prepared by the Joint Advisory Taskforce following a security risk assessment of the Manus offshore processing centre. The department provided a summary of the risk assessment to a Parliamentary Committee in June 2014.⁷⁴ The summary included the risk assessments recommendations which related to improvements to infrastructure at the Manus offshore processing centre including fencing, lighting, installation of close circuit television, relocation of the logistics hub and establishment of a potable water supply.

3.25 The ANAO reviewed the full decision brief and found that the briefing did not recommend that DIBP not take up the extension option available with G4S and the Salvation Army due to underperformance, as had been stated by the CPU in its advice to Finance. Mr Bowles advised the ANAO that:

Whilst the report did not specifically highlight ‘performance issues’ relating to the contract, it did highlight areas for improvement and potential areas of change to the nature of the services provided.

3.26 There was no available record that the department provided any advice or feedback on the recommendations of the assessment to service providers. G4S advised the ANAO that they were not provided with any advice or feedback in relation to the Joint Agency Taskforce assessment. Both G4S and The Salvation Army were advised that the decision with respect to consolidating service providers was not based on their performance.

3.27 The department also advised Finance that the supplier it wished to engage (Transfield) had previously been assessed as representing value for money. As noted in chapter 2 of this audit report, the ANAO’s review indicated that in procuring services from Transfield in 2012, the department did not conduct a robust value for money assessment.⁷⁵

3.28 In response to the information provided by the department’s CPU, Finance advised DIBP on 28 November 2013 that:

limited tender could apply on the basis of poor performance of the existing provider, a new supplier is required immediately, and that the department’s decision is not made following a review to decide whether to exercise the extension option, with the intention of finding a new supplier.

3.29 The department used Finance’s advice to seek approval from the departmental delegate to conduct the procurement as a limited tender under paragraph 10.3(b) of the CPRs. The advice was also used in departmental advice for the Minister’s use in discussions with his colleagues on the consolidation proposal in December 2013. The advice indicated that it was DIBP’s view that Transfield was the best option for service delivery at the offshore processing centres and offered

74 The summary was tabled in response to a Questions on Notice asked at Parliamentary Committee hearings on 26 and 27 May 2014.

75 Transfield was found to be four times more expensive than G4S in the limited tender process conducted for Manus Island in 2012. See paragraph 2.33 of this audit report.

the lowest risk in regards to implementing a consolidated approach to service delivery. The advice outlined the proposed strategy for consolidation, including that:

- the preferred procurement method to achieve innovation and savings would be to approach Transfield directly with a limited tender;
- any public comment should reflect the Government's desire to achieve innovations and savings through the consolidation processes and there was no need to discuss performance issues; and
- in relation to handling and timeframes, following the Government's decision, a request for quote would be sent to Transfield for the provision of garrison and welfare services at both offshore processing centres.

3.30 The department's use of limited tender under paragraph 10.3(b) of the CPRs would have been more defensible if: any G4S performance shortcomings had been documented; G4S had been advised of the department's concerns; and had G4S not taken steps to remedy any documented performance issues after receiving such advice. The ANAO's review indicates that the department did not advise G4S of performance issues during the life of the contract, and payments were never abated. There is no evidence of a loss of confidence in G4S's ability to deliver services. In his December 2013 comments on communications prepared for G4S and The Salvation Army, a DIBP Deputy Secretary noted gaps in the advice:

...In communicating and dealing with G4S and TSA [The Salvation Army], we do not have [a] line on "why is Transfield continuing, and not us". This is another way for the issue of performance to be raised. What do we say about that.

3.31 In reply, the Assistant Secretary responsible for Offshore Detention Services advised that:

...have worked up the lines below. Re the elephant in the room performance issue, not sure what else we can say short of the 'their performance has been better than yours' discussion which we don't want to get into.

3.32 In its correspondence to the department over the decision to end the contract, G4S stated that there had been no indication that such a decision was imminent or was being contemplated:

It was confirmed in our meetings that the decision had nothing at all to do with the operational performance of G4S on Manus and there were no concerns in this respect. Based on this we are at a loss to understand how this decision can have been arrived at without G4S at least being given an opportunity to provide a submission outlining our own capabilities and potential cost efficiencies. Our strong preference is that the Department would reconsider its decision and give us an opportunity to explain how we are best placed to address any desire to achieve cost and operational efficiencies.⁷⁶

3.33 G4S's confidence in relation to its performance was separately demonstrated by its earlier submission to the then Secretary of a proposal (14 October 2013) to deliver services in Nauru and on Manus Island (paragraph 3.9 refers).

76 Correspondence from G4S to DIBP dated 24 December 2013.

Did the process applied to contract consolidation support the achievement of planned savings, innovations and efficiency in service delivery?

DIBP's approach to engaging Transfield through limited tender procurement removed competition from the outset. The services to be provided and related costs were not agreed with Transfield prior to G4S and The Salvation Army being advised that they would exit from service delivery on Manus Island. The proposed costs submitted by Transfield were higher than the department had anticipated and exceeded those charged by G4S and The Salvation Army for service provision on Manus Island.

Ministers expected the consolidation of contracts to achieve innovation and savings. Savings were not realised and the basis which the department relied upon to demonstrate savings was unreliable. In particular:

- The department applied a benchmark model to demonstrate the achievement of value for money. Overall the benchmark was adjusted above historical costs to account for changes to the department's service requirements and contractual approach, upwards to \$372 million, to accommodate a number of service enhancements. The Government had directed the department to reduce per-head costs. The department had no authority to increase the funding value of the contract above historic costs.⁷⁷
- Separate benchmarks were developed for Nauru and Manus Island, but the department determined 'value for money' and claimed savings (against the benchmarks) on a combined basis. This allowed the department to demonstrate 'savings' by offsetting higher costs for Manus Island against lower costs for Nauru. While Transfield's bid for Nauru was lower than historical costs, the bid for Manus Island exceeded historical costs by between \$200 million and \$300 million.

While the department based the negotiated contract price on a high capacity scenario, there was a steady drop off in new asylum seeker arrivals from a high of 1 647 in August 2013 to zero in March 2014. On this basis it was increasingly unlikely that the high capacity levels would eventuate. The resulting contract was volume driven, with significant economies of scale expected at high capacity levels. This contract exposed the Commonwealth to the risk of locking-in a high price for services delivered at lower capacity levels.

There is no available record of specific conflict of interest declarations having been made by departmental officers who were responsible for the procurement. There is also no available documentation to indicate whether the department performed due diligence checks on the successful tenderer (Transfield) or its subcontractors as part of the contract consolidation.

⁷⁷ The ANAO reviewed records of the Department of the Prime Minister and Cabinet, the Department of Finance and DIBP relating to the Government decisions and Ministerial approvals.

The Prime Minister had requested that per head costs be lower as a result of retendering the contracts, but the department did not calculate a per person cost. Finance advised the ANAO that under the consolidated contract, the per person per annum cost of holding a person in the offshore processing centres in Nauru and on Manus Island, was estimated at \$573 111, at the time of the Mid-Year Economic and Fiscal Outlook 2015-16.⁷⁸ Prior to consolidation Finance estimated the cost at \$201 000.

3.34 The Minister sought Government approval for the consolidated contract arrangement in December 2013. In his submission to colleagues, the Minister proposed to explore options to consolidate existing services to enhance consistency, security and efficiency and incorporate innovation and savings into the extension provisions, noting that this was an interim measure pending an open tender process that would be conducted in 2014. In its comments and briefing on the submission, Finance highlighted that the cost of providing services under the consolidated contract was expected to rise by \$93 000 per asylum seeker, taking costs from \$201 000 to \$294 000⁷⁹ per asylum seeker per annum. Finance also noted that the increase in unit costs appeared to be attributable in part to the department entering contracts with higher service provider costs than those factored into the forward estimates. For example, the Transfield monthly costs per asylum seeker had increased from \$13 206 to \$21 742 and the Salvation Army monthly cost per asylum seeker increased from \$1 556 to \$2 490.

3.35 The Government sought a reduction in costs with savings to be delivered through the contract consolidation. On 3 December 2013 the Minister sought and gained the Prime Minister's agreement to proceed with the consolidation at an indicative cost of \$2.6 billion. In responding the Prime Minister made it clear that he expected per head costs to be lower as a result of retendering the contracts. The Prime Minister's agreement to proceed with consolidation did not provide DIBP with authority to increase the value of the contract to accommodate service enhancements or adjustments.

3.36 The department's documentation on the Request for Quote (RFQ) process and subsequent negotiations with Transfield indicates that DIBP officials found it difficult to achieve the savings required by Ministers.

Contract negotiations and value for money

3.37 The department entered into contract negotiations with Transfield and Save the Children in early 2014. The approach taken in these negotiations is outlined below.

78 Released in December 2015.

79 The Department of Finance advised the ANAO that the estimated \$201 000 service provider cost per person per annum was based on the initial estimate of offshore service provider costs as at the 2013–14 Budget. The estimated \$294 000 service provider cost per person per annum was based on a revised estimate of offshore service provider costs as at the 2013–14 Mid-Year Economic and Fiscal Outlook. This later cost estimate reflected a more developed understanding of the cost of service delivery at the offshore processing centres.

Transfield

3.38 On 3 December 2013 in response to the department’s briefing on its proposed approach to the consolidation of services at the Offshore Processing Centres, the Minister noted that this outcome [consolidation]:

...must be managed. Also pls advise on the employment of an external contract negotiation advisor to ensure there is rigorous negotiation to deliver savings from Transfield.

3.39 KPMG was engaged for this role. In advising the department, KPMG proposed benchmarking Transfield’s tendered price against existing contractor payments (the combined cost of G4S and Salvation Army service delivery on Manus Island). KPMG noted that in the context of sole source procurement it was important that the tenderer was aware that the Commonwealth would test value for money against a price benchmark.

3.40 KPMG’s evaluation report on pricing (3 February 2014) raises a number of issues in relation to Transfield’s costs against the benchmark for the number of detainees serviced.

3.41 Transfield’s initial submission introduced four pricing Capacity Bands for each location. During negotiations the number of pricing bands was increased to 14. The change in banding structure is outlined in Table 3.1 below.

Table 3.1: Initial and final capacity bands in Transfield’s submissions

Manus Island number of detainees	Nauru number of detainees	Capacity band under 4 band structure	Capacity band under 14 band structure
0–600	0–800	1	1–2
601–1200	801–1600	2	3–6
1201–1800	1601–2400	3	7–10
1801–2400	2401–3200	4	11–4

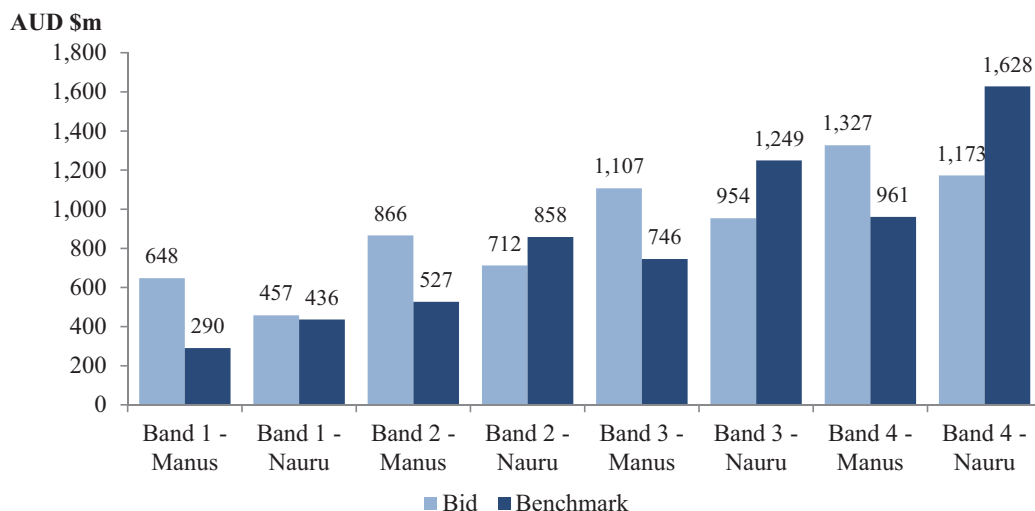
Source: KPMG pricing evaluation report.

3.42 Transfield’s prices represented a price reduction in Nauru. For services on Manus Island the prices represented a significant price increase (KPMG referred to this increase as a premium) when compared to the price benchmark. Overall, KPMG concluded that:

when compared to the benchmark costs, the Respondent’s risk adjusted pricing yields inconsistent results. The Respondent’s pricing for Capacity Band 4 represents a 4.5% saving in comparison to benchmark costs, however the Respondent’s pricing represents a premium of approximately 50.8%, 12.8%, and 2.2% for Capacity Bands 1, 2 and 3 respectively.

3.43 Figure 3.2 shows the risk adjusted total bid costs for Transfield’s initial price against the benchmark for each of the four Capacity Bands for Nauru and Manus Island.

Figure 3.2: KPMG’s risk adjusted total bid cost in \$ millions vs benchmark—by band and facility



Source: KPMG pricing evaluation report.

3.44 The risk adjusted pricing for the centre in Nauru represented savings of 17 per cent, 25 per cent and 28 per cent for Capacity Bands 2, 3 and 4 respectively, compared to the benchmark costs at Nauru. Capacity Band 1 for Nauru represented a 5 per cent pricing premium above the benchmark costs. Pricing at Manus Island represented a significant pricing premium when compared to benchmark costs (as extrapolated from incumbent pricing) of 38 to 128 per cent.⁸⁰ Table 3.2 shows the difference between risk adjusted prices⁸¹ and the benchmark on a percentage basis.

Table 3.2: Difference between Transfield’s risk adjusted price and the benchmark

	Capacity Band 1		Capacity Band 2		Capacity Band 3		Capacity Band 4	
	Manus Island	Nauru	Manus Island	Nauru	Manus Island	Nauru	Manus Island	Nauru
Percentage difference above or below the benchmark	123.2% Above	4.9% Above	64.3% Above	(17.0%) Below	48.4% Above	(25.1%) Below	38.1% Above	(28.0%) Below

Source: KPMG pricing evaluation report 2014.

3.45 After considering the KPMG report, the department’s evaluation committee recommended that: the department enter into negotiations with Transfield; and that a contract be executed

80 KPMG’s report refers to a difference of 128 per cent. The KPMG report’s accompanying table shows a difference for Manus Island of 123.2 per cent. This figure is reflected in Table 3.2 of this audit report.

81 KPMG estimated the value of the bid to DIBP after taking into account the likelihood and impact of certain risks. This bid value was adjusted by KPMG and a risk-adjusted price was presented in the KPMG report.

only if the department could be satisfied that value for money could be obtained. Key matters for negotiation included the performance framework and performance measures, savings measures and clarification that key service delivery elements were adequately covered in the statement of work.

3.46 Transfield provided DIBP with responses to clarification questions and revised pricing information on the issues to be negotiated on 11 February 2014. In a minute to the delegate (the First Assistant Secretary Offshore Detention and Returns Task Group) dated 21 February 2014, the Assistant Secretary for Offshore Detention Services⁸² advised that the final negotiated position represented value for money and also resulted in a number of changes considered to be significant improvements. The delegate was also advised that:

The negotiation process has resulted in a number of significant improvements between the initial bid, and the final negotiated position... Further understanding and clarification of the cost differences between Transfield's Nauru and Manus costs during negotiations allowed the department to have confidence that the additional investment in Manus was justified and required...

3.47 The department also considered that the negotiated performance management framework would contribute to innovation and provide an incentive for cost savings, as Transfield was eligible to share in 50 per cent of demonstrated savings to fixed costs and 15 per cent of savings to pass through costs.

3.48 In respect to value for money the delegate was advised that the negotiated position represented a movement of \$150 million in the Commonwealth's favour. The delegate approved the proposal on the basis that it represented value for money and signed a letter of intent to Transfield (21 February 2014) to cover service delivery until a contract could be drafted.

3.49 The advice to the delegate indicated that the \$150 million movement in the bid price demonstrated a 'saving' against the benchmark, whereas the KPMG report reflected that these were price adjustments agreed to during the negotiation:

The Transfield bid now represents a risk adjusted saving of 5.9% over the benchmark for band 3. This is made up of a saving of 26% on the benchmarked Nauru costs and an increase of 29% on the benchmarked Manus costs (down from 48%), noting the value of the Nauru benchmark is \$1.25bn and Manus \$0.797bn. The benchmark has been calculated based on contract payments for the 12 months to November 2013, uplifted for increased numbers of Transferees, inflation and other assumptions and reflects a conservative estimate of current costs that may not accurately reflect current operational tempo.

3.50 The advice to the delegate also noted that the benchmark for Manus Island did not take into account a number of enhancements offered by Transfield relating to enhanced security, improved catering, reduction in international travel costs and agreement to a performance management framework. Collectively these enhancements were considered to be worth \$60 million, and it proposed that the benchmark be adjusted accordingly. Table 3.3 shows the advice to the delegate included adjustments and negotiated outcomes. This advice was based on Transfield's Capacity Band 3 (refer paragraph 3.41 and Table 3.1).

⁸² The Assistant Secretary had day-to-day carriage of the negotiations.

Table 3.3: Adjustments to the benchmark and other negotiated outcomes (\$ millions)

Description	Value (\$ million)
Initial difference between risk adjusted price and benchmark	32.4 (1.6% over)
Negotiations—efficiency dividend/security/accommodation security	Saving ^a 61.3
Removal of working hours risk	Saving 31.9
Increases to the benchmark for enhanced service	Saving 60.0
Final difference between risk adjusted price and benchmark	120.8 (5.9% under)

Note a: This is a notional saving against the benchmark as opposed to an actual savings against historic costs.

Source: Minute to Offshore Detention and Returns Task Group 21 February 2014.

3.51 In addition to the minute of advice, the delegate received the final report on the negotiations prepared by KPMG, presenting analysis of the proposal and a comparison against the benchmark constructed by KPMG. This report stated that the benchmark price was increased above the historical cost base in order to ensure a like for like comparison of pricing. The report noted that the benchmark was compared against the bid price for each facility, and ‘savings’ were presented as an aggregate (combined Nauru and Manus Island).

3.52 The ANAO compared the benchmark and bid with a projection of the historic cost for each capacity band and found that the benchmark was pitched at above the historical costs at all capacity band levels. Overall the benchmark was adjusted above historical costs by some \$372 million. For Nauru the difference between the benchmark and historical costs was valued at its highest point at \$166 million, while for Manus Island it was \$206 million. The Government had directed the department to reduce per-head costs. The department had no authority to increase the value of the contract above historic costs to cover service enhancements, and was aware of this.⁸³ In seeking internal financial approval for the proposed contract the delegate was advised of the potential need for further policy approvals:⁸⁴

Whilst this is within our garrison and welfare service delivery funding allocation in the demand driven model, it is likely that further policy approval will be required to update the demand driven model for the new contract.⁸⁵

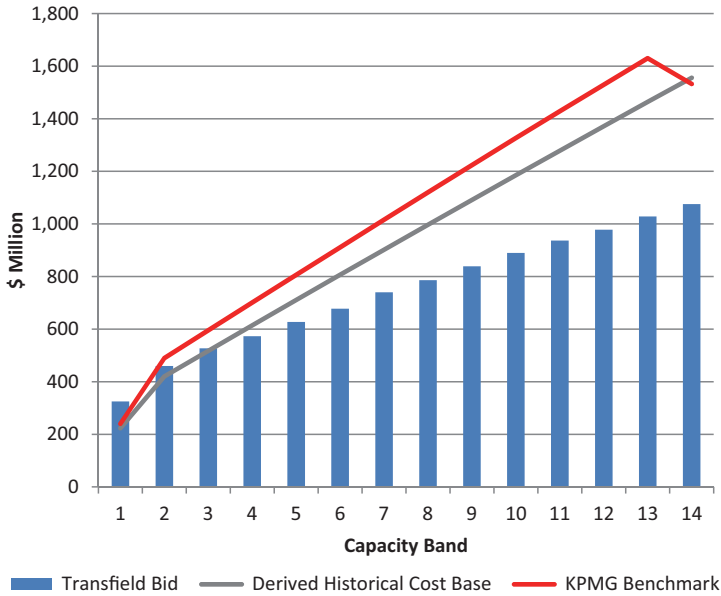
3.53 The ANAO also compared the bid for Nauru and Manus Island separately and against the benchmark and historic costs. The bid price for services in Nauru was lower than the benchmark and historic costs for most capacity levels. For Manus Island the bid was above both the benchmark and historic costs for all capacity levels. Figure 3.3 and 3.4 summarise the ANAO’s analysis.

83 The ANAO reviewed records of PM&C, Finance and DIBP relating to the Government’s decisions and Ministerial approvals.

84 At the time of contract consolidation, funding to DIBP for the offshore processing centres was provided on the basis of a demand driven model. The model was jointly overseen by DIBP and the Department of Finance. This funding model and associated government decisions determined the level of funding to the Department. Funding under the demand driven model was subject to change when there was an increase in detainee numbers, or change to government policy, or facility closure.

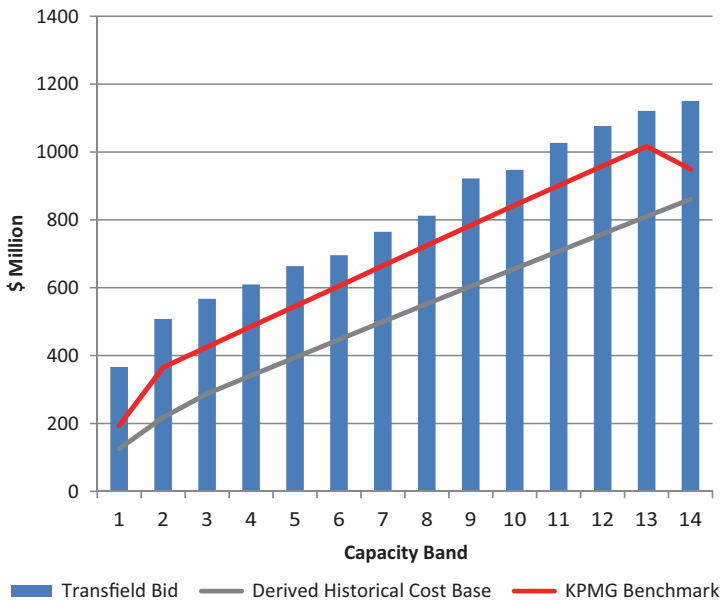
85 ANAO comment: In addition, an internal audit report on the External Funding Model (April 2014) noted that changes to the policy or service delivery processes which flowed to the demand driven model would need to be approved through a submission to Government and approved by Ministers.

Figure 3.3: Nauru bid, benchmark and historic costs



Source: ANAO analysis of the spreadsheet used to prepare the KPMG Price Evaluation Report.

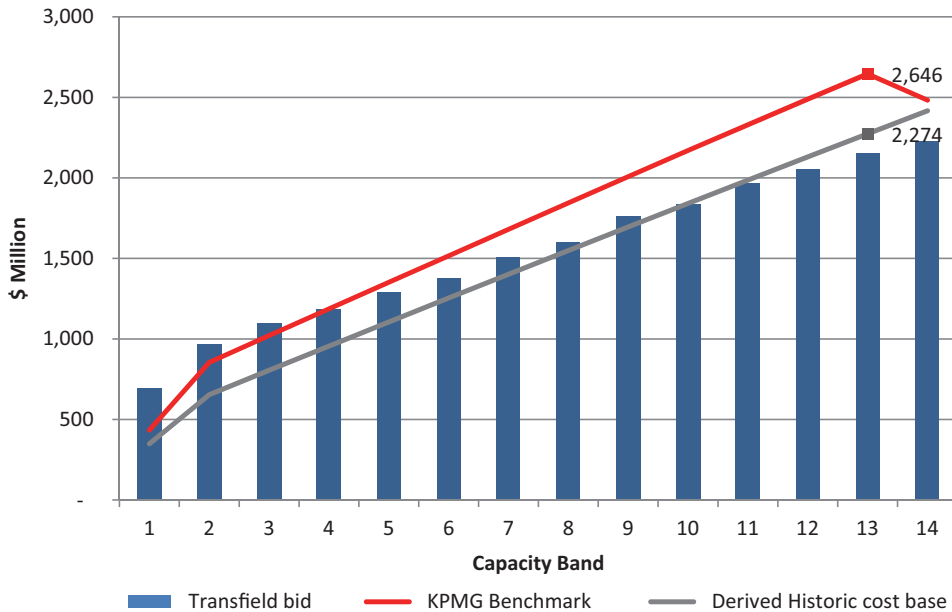
Figure 3.4: Manus Island bid, benchmark and historic costs



Source: ANAO analysis of the spreadsheet used to prepare the KPMG Price Evaluation Report.

3.54 The ANAO’s analysis indicates that the combined value of Transfield’s Nauru and Manus Island bids was over the historical costs at capacity band one through to nine and was only below the historic costs above capacity band ten. The consolidated (KMPG) benchmark (Nauru and Manus Island combined) was above the historic costs by \$372 million at its highest point (the red line in Figure 3.5 shows that the highest point was \$2 646 million for capacity band 13, while the historic cost was \$2 274 million).⁸⁶

Figure 3.5: Combined bid values, benchmarks and historic costs—Nauru and Manus Island



Source: ANAO analysis of the spreadsheet used to prepare the KPMG Price Evaluation report.

3.55 In its final pricing evaluation report, KPMG assessed that post-negotiation Transfield’s bid represented both actual value for money and improved value for money relative to the opening position. In particular, KPMG advised that the increase in the number of pricing bands, from four to 14, had provided an improved value for money outcome due to the more efficient incremental pricing structure, with greater potential price benefits over the benchmark potentially achieved at the higher capacity band levels.⁸⁷

⁸⁶ The KPMG benchmark (the red line in Figure 3.5) included an ‘uplift’ percentage increase to the historical cost base (the grey line in Figure 3.5) of welfare services for each capacity band. Capacity band 14 did not have an ‘uplift’ percentage applied for Nauru or Manus Island, for reasons that are not clear. Had an ‘uplift’ percentage been applied, capacity band 14 (rather than capacity band 13) may have provided the highest point for the benchmark.

⁸⁷ The increase in capacity bands from four to 14 resulted in a more gradual increase in the number of asylum seekers across the bands, which adjusted the pricing to be applied for each additional capacity band by 200 asylum seekers.

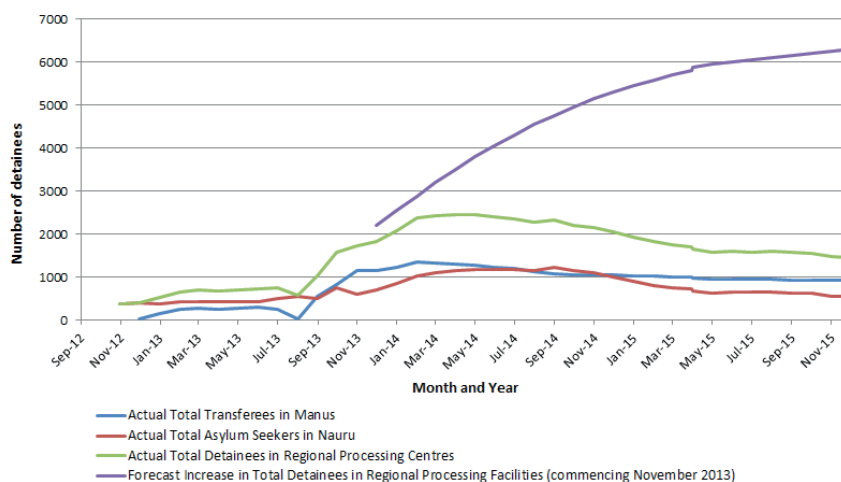
3.56 The available records do not indicate whether in assessing value for money, the department considered the relationship between price and the actual capacity levels of the centres. Advice to the delegate stated that:

Capacity band 3 activity has been used as a baseline based on predicted occupancy levels going forward. Band 4 results are significantly better than band 3 and bands 3 and 4 have been considered to be appropriate levels of activity for the analysis of value for money.

3.57 As outlined in Table 3.1 capacity bands three and four equated to capacity bands 7–10 and 11–14, which ranged from 1201–1800 and 1801–2400 detainees respectively for Manus Island and 1601–2400 and 2401–3200 detainees respectively for Nauru.

3.58 Since opening in 2012, there had been large variations in the number of asylum seekers housed in the centres. Figure 3.6 shows the total number of asylum seekers in Nauru and on Manus Island and Finance forecast numbers commencing from late 2013.

Figure 3.6: Total number of asylum seekers in offshore processing centres by month—actuals and Finance forecast numbers commencing late 2013



Source: Finance briefing and DIBP published monthly statistics.

Note: Actual Total Detainees in Regional Processing Centres represents individuals who were held in the offshore processing centres at a point in time. The variation in actual total asylum seekers over time represents the movement in asylum seekers arriving and leaving the centres. The increase from August 2013 represents individuals who arrived in Australian waters by boat after the July 2013 announcement and who were required to be transferred to an offshore processing centre and could never be settled in Australia. The Forecast Increase in Total Detainees anticipated that the number held across the two centres would be maintained by a flow of around 390 new arrivals a month through to June 2015, beyond which inflow would drop to 50 a month.

3.59 The centres in Nauru and on Manus Island had never reached their full combined capacity of 5600 persons, and there were few new arrivals after December 2013. While the department based costings on a high capacity scenario, there was a steady drop off in new boat arrivals during the contract negotiation period. On this basis it became increasingly unlikely that the high capacity levels would be achieved. The department did not consider the price impact of a volume driven contract with significant built-in economies of scale. Advice to the departmental delegate did not

consider whether constructing a price based on these capacity levels, to achieve economies of scale, might lock the Commonwealth into paying a premium for services delivered at lower capacity levels.

3.60 In April 2014 the Minister for Finance was advised by his department that since December 2013 there had been 373 arrivals in total compared to the MYEFO projection of 541 per month. In addition, reports suggested that the policy of turning back boats, in combination with offshore resettlement arrangements, had generated the fall in the arrival rate. A breakdown of arrival numbers as at 11 April 2014 is provided at Table 3.4.

Table 3.4: Asylum seeker arrival numbers since August 2013 (as at 11 April 2014)

Month	August 2013	September 2013	October 2013	November 2013	December 2013	January 2014	February 2014	March 2014	April 2014
Asylum seeker arrivals (less crew)	1647	853	347	221	369	3	1	0	0

Source: ANAO presentation of advice to the Finance Minister, April 2014.

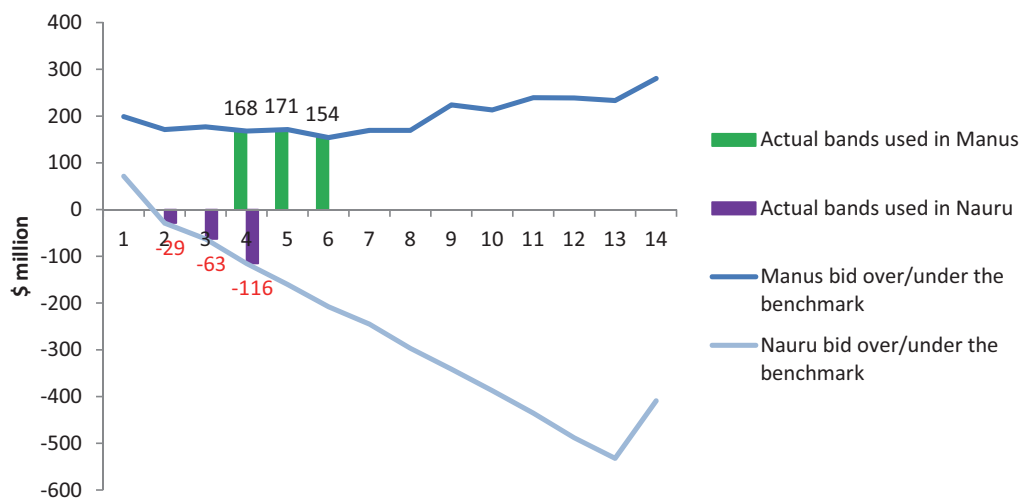
Note: The period of the contract negotiations was January to late March 2014.

3.61 The ANAO’s analysis of the final Transfield bid against the benchmark and actual capacity levels indicates that the higher capacity levels have never been required. Figure 3.7 shows the final tender bid and capacity bands, including the amount over and under the benchmark for each band in the Transfield bid for the centres in Nauru and on Manus Island. The columns show the actual capacity bands used during the contract. In summary, the premium paid (shown in green) outweighs the discount achieved (shown in purple).

3.62 The then Secretary, Mr Bowles, advised the ANAO that:

From the vantage point of 2015–16 the drop off in UMA arrival numbers in Feb 2014 looks clear and distinct. At the time however, there was never certainty that this drop-off of numbers would continue. The flow of UMAs had always had peaks and troughs, and was especially susceptible to the weather cycle and monsoon seasons. Most critically, at the times of the various procurement activities, the posture of the ATM [approach to market] was in the context of the potential for high arrival rates, rather than the lows.

Figure 3.7: Actual band usage shown against the value of the Transfield bid relative to the benchmark



Note: The benchmark is represented at zero dollars.

Source: ANAO presentation of DIBP data.

3.63 A contract for consolidated services was signed by DIBP on 24 March 2014. The Minister was advised (24 March 2014) that the department had negotiated a 5.9 per cent saving overall, valued at some \$121 million, as compared to the benchmark constructed by KPMG. The Minister was also advised that:

Greater savings against benchmark costs have been achieved at higher occupancy levels...

The Transfield contract bid has been compared against the Department of Finance's Offshore Demand Driven Model (DDM) funding allocations for Transfield, G4S and The Salvation Army. Comparing the cost under the contract to the funding allocations using the forecast occupancy levels in the DDM, the cost of the contract is approximately \$44 million less over the 20 month contract period...

Given the operation of the DDM, the Financial Strategy and Services Division has agreed with the Department of Finance to hand back savings of \$25 million across the contract period...

3.64 The Minister was not advised that the resulting contract with Transfield—with a reported (AusTender) value of \$2.1 billion over 19 months—would require the Commonwealth to pay a significant premium over and above the historical costs of services. The Minister was not advised that under the contract actual capacity levels (at the time) represented significant additional expense. The Minister was not advised of the contract price on a per head basis. As discussed at paragraph 3.35, the Prime Minister had expressed an expectation that both total costs and per head costs would be reduced as a result of re-tendering the contracts.

3.65 Subsequent Mid-year Economic and Fiscal Outlook modelling by the Department of Finance of average per head costs, using DIBP's detention network population forecasts, indicated

that the per head cost under the consolidated contract was \$573 111 (based on actual numbers of asylum seekers held) at the end of December 2015.⁸⁸ This equated to a daily rate of over \$1570 per asylum seeker.

3.66 Calculating per person costs would have enabled the department to more accurately advise its Minister of the cost implications of the consolidated contract. It would also have assisted the department to advise the Minister on the placement of asylum seekers to minimise expense to the Commonwealth. The ANAO estimated per person costs (as reflected in the bid), for each facility and capacity band. The ANAO’s analysis indicates that accommodating transferees on Nauru, until it reached full capacity prior to accommodating any transferees on Manus Island, would have lowered the overall expense. The reason for this is that the cost per person was lower in Nauru than on Manus Island. A cost comparison is set out below in Table 3.5.

Table 3.5: Per person costs, for 12 months, based on contract rates

Capacity Band	Manus Island	Nauru
1	\$696 480	\$463 100
2	\$482 440	\$327 610
3	\$431 200	\$300 390
4	\$385 980	\$272 190
5	\$360 290	\$255 490
6	\$330 440	\$241 510
7	\$322 920	\$234 340
8	\$308 670	\$244 010
9	\$318 490	\$217 320
10	\$299 990	\$211 330
11	\$300 110	\$205 400
12	\$292 140	\$199 100
13	\$284 010	\$195 390
14	\$273 230	\$191 520

Source: ANAO analysis.

Save the Children

3.67 The department’s documentation on negotiations with Save the Children for the provision of welfare services to families, children and single women in Nauru, is limited. The available documents indicate that negotiations were protracted and the department sought significant price reductions after determining that the proposal did not represent value for money. In the course of negotiations with Save the Children, the department proposed to the Minister that DIBP seek an alternative quote from Transfield for this work. The Minister expressed a preference to retain the services of Save the Children.⁸⁹

88 The National Commission of Audit in its final report in March 2014 estimated per head costs at around \$420 000. [Internet] available from <<http://www.ncoa.gov.au/report/appendix-vol-2/10-14-illegal-maritime-arrival-costs.html>> [accessed 11 March 2016].

89 The Minister indicated this preference in writing on 3 December 2013.

3.68 DIBP records indicate that the department subsequently sought an informal quote from Transfield to conduct this work. Transfield's quote was found to be 28 per cent higher than Save the Children's final costs.

3.69 In response to departmental requests, Save the Children submitted four pricing revisions. In May 2014, Save the Children wrote to DIBP declining an invitation to submit a further contract change proposal in the terms the department had requested. Save the Children advised that the reductions proposed by the department (which were in the order of 20 to 50 per cent) would change the service offering fundamentally and expose the department, Save the Children, asylum seekers and employees to an unacceptable level of risk:

As an organisation whose mission is to protect and promote the rights and safety of children and their families, and for the reasons outlined above, SCA [Save the Children] cannot in good conscience submit a revised contract change proposal as requested. SCA remains committed to working with the Department to ensure the best possible conditions and services for asylum seeker children and families in Nauru. We would welcome the opportunity to further discuss our contract change proposal and identify additional cost reductions which do not compromise our ability to safeguard the physical, mental and emotional wellbeing of the people in our care.⁹⁰

3.70 The department's records differ from Save the Children's in relation to initial price and negotiated savings. The department's approval record shows a price reduction of \$112.4 million — down from an initial bid of \$196.4 million. Save the Children's documentation shows that the initial bid for services was around \$300 million and the negotiated reduction was around \$150 million. The value of the contract as reported on AusTender was \$100 million.

Probity and conflict of interest

3.71 The department engaged an internal probity adviser to oversee the Request for Quote (RFQ) process between late December 2013 and the end of January 2014. The adviser provided an unqualified sign off for the process.

3.72 KPMG declared its role as Transfield's external auditor and declared that it had also provided other services including tax, financial due diligence and accounting advisory services to the Transfield Group. KPMG did not consider that the provision of such services to Transfield raised any conflict of interest issues and advised the department that no team member who was providing services to DIBP in relation to this project would be involved in the Transfield audit or advisory engagements. KPMG also provided conflict of interest declarations for specific staff in January 2014. In engaging KPMG the department noted in its approvals that no conflicts of interest existed.

3.73 The ANAO's review indicates that there is no available record of specific conflict of interest declarations having being made by departmental officers who were responsible for the procurement. Mr Martin Bowles provided his personal declaration of interest for 2013 to the ANAO on request.

⁹⁰ Save the Children correspondence to DIBP, 30 May 2014.

3.74 Good procurement practice involves entities undertaking due diligence of potential tenderers.⁹¹ The department's Risk Management Plan (for the Offshore Processing Programme) stated that a control in place during the procurement process was that all service providers had undergone due diligence investigations.

3.75 No evidence was found of the department having conducted due diligence checks in relation to the engagement of Transfield or Save the Children. The ANAO found that had due diligence checks been undertaken at the time of consolidation (January 2014), the department would have identified that Transfield's subcontractor (Wilson Parking Australia, trading as Wilson Security) had a Director who had been charged with bribery in Hong Kong in 2012 and that these charges were pending. The person was acquitted of all charges in December 2014.⁹² Had DIBP performed due diligence checks it may not have changed the outcome of the procurement, however DIBP would have made an informed decision and would be better positioned to mitigate any associated risk.

91 The CPRs specify that the Australian Government promotes the proper use and management of public resources. Proper means efficient, effective, economical and ethical. Ethical relates to honesty, integrity, probity, diligence, fairness and consistency.

92 The judgement which led to the charges being acquitted is available at [Internet] <http://legalref.judiciary.gov.hk/lrs/common/ju/ju_frame.jsp?DIS=96532> [accessed August 2016].

4. Open Tender Process from 2014 to 2016

Areas examined

This chapter examines whether selected aspects of the open tender process undertaken by the department for garrison support and welfare services at the offshore processing centres were sound and met the requirements of the *Commonwealth Procurement Rules* (CPRs).

Conclusion

The department's procurement planning processes adhered to many of the requirements of the CPRs. However, there were significant shortcomings in the conduct of the negotiation phase of the open tender process. In consequence the open tender process was amended and was in effect a limited tender involving the preferred and reserve tenderers. On 29 July 2016 the department cancelled the tender. DIBP extended its contract with Transfield until 31 October 2017 and the department advised the ANAO it is now conducting market testing to determine its next steps.

From the outset of the open tender process the department's statement of requirements expanded the services under tender beyond those of the contracts which were in place at the time. The value of these enhancements was estimated at between \$594 million to \$835 million above historical costs. The department did not have Government authority to increase the funding value of the contract to accommodate service enhancements.

Achieving value for money is a core rule of the CPRs. The department's process for determining value for money had flaws. In particular:

- The comparison of the negotiated price against a benchmark was inappropriate. The approach is incompatible with the CPRs which require each eligible tenderer's financial and nonfinancial benefit to be compared on a like for like basis with other eligible tenders.
- The department determined to only enter into negotiations with its preferred tenderer, Transfield. Transfield's overall price increased by \$1.1 billion above its tender bid during negotiations due to the department amending its requirements and accepting further enhancements to services. The department: had no Government authority to increase the value of the contract to cover service additions; and did not communicate the changed requirements to other tenderers and did not seek clarification or repricing from any other tenderers as required by the CPRs.

The effective operation of key oversight mechanisms contributed to the department initiating an amended tender process.

Although the department had many years of experience in managing detention contracts, the outcome and conduct of the tender process suggest that the officers involved in the procurement process did not have the appropriate skills, experience and seniority to: properly assess value for money in an open tender procurement; and successfully manage a complex procurement.

Areas for improvement

The ANAO has made recommendations to address:

- the significant skill and capability gaps identified amongst personnel at all levels in the department, including within the central procurement and budget units; and

- persistent shortcomings in the planning and conduct of the procurements, including in relation to record keeping, consistency and fairness in the treatment of suppliers, and the assessment of value for money.

Introduction

4.1 Ministerial correspondence indicates that the consolidation of garrison support and welfare services contracts in Nauru and on Manus Island was considered an interim measure pending an open tender which would optimise value for money and efficiencies in the service delivery arrangements. The department did not seek policy authority for the service delivery parameters or any additional funding prior to issuing an open tender to the market on 30 January 2015.⁹³ Table 4.1 shows the Government’s anticipated expenditure over the forward estimates for Offshore Management of Illegal Maritime Arrivals at the time of the 2015–16 Budget.

Table 4.1: Offshore Management of Illegal Maritime Arrivals—budget estimates

	2014–15 Actual \$'000	2015–16 Budget \$'000	2016–17 Forward Estimate \$'000	2017–18 Forward Estimate \$'000	2018–19 Forward Estimate \$'000
Offshore Management	857 330	772 854	319 275	313 364	331 910

Source: Australian Government, *Portfolio Budget Statements 2015–16*, Budget Related Paper No. 1.11, *Immigration and Border Protection Portfolio*, Commonwealth of Australia, Canberra, 2015, p.41.

4.2 As discussed in Chapter 1, open tender involves an open approach to the market. Under the *Commonwealth Procurement Rules* (CPRs) it is the default for all procurements valued at or above the relevant threshold⁹⁴ and must be advertised on AusTender. Open tender promotes competition and helps ensure value for money for the Commonwealth. For open tender procurements above the threshold, the CPRs establish how entities approach the market and manage procurement, including requirements for request documentation, conditions for participation, time limits, and the receipting and opening of tender documents.

4.3 The procurement process was underway during this audit. For this reason the ANAO focussed on certain aspects of the procurement. The ANAO examined:

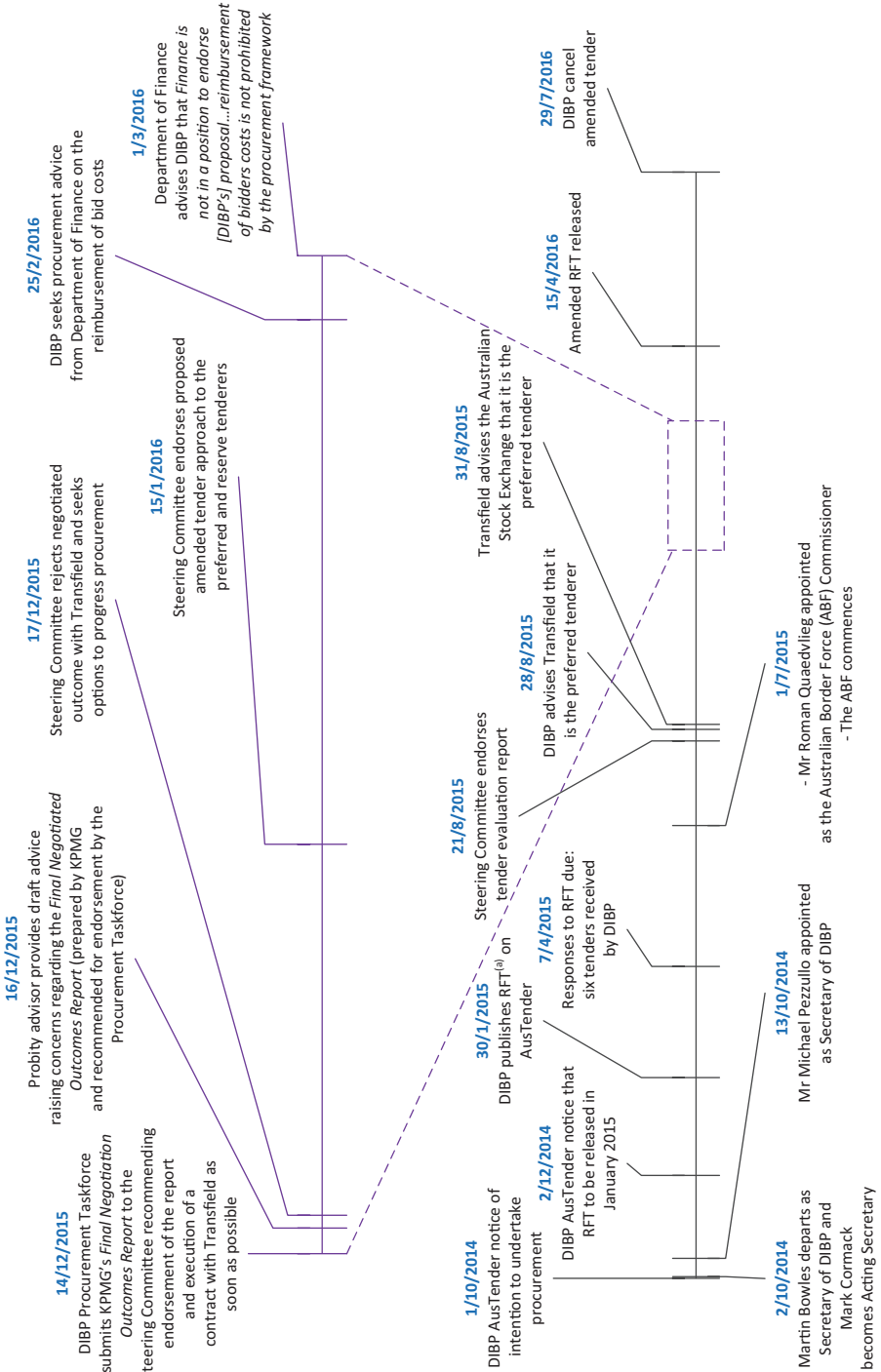
- procurement planning;
- key aspects of the tender evaluation process, including the assessment of value for money; and
- contract negotiations.

A timeline of key events for the open tender process is set out in Figure 4.1.

93 In October 2014 DIBP published an AusTender Notice advising of its intention to undertake the procurement of services for the regional processing centres in Nauru and on Manus Island. In December 2014 DIBP issued a further notice on AusTender advising that the request for tender would be released in January 2015.

94 The current procurement thresholds (including GST) for which the additional procurement rules of Division 2 of the CPRs apply are: \$80 000 for non-corporate Commonwealth entities, other than for procurements of construction services; \$400 000 for prescribed Commonwealth corporate entities, other than for procurements of construction services; and \$7.5 million for procurements of construction services by relevant entities. Finance, CPRs, 2014, paragraph 9.7, p.24.

Figure 4.1: Timeline of key events for open tender process



Note a: Request for tender (RFT).
Source: ANAO analysis of DIBP records.

Did the department adopt tender planning and probity arrangements consistent with *Commonwealth Procurement Rules* requirements?

While aspects of the department's open tender planning addressed the requirements of the CPRs, insufficient consideration was given to:

- The use of benchmarking to determine overall value for money. The department's approach involved comparing only the preferred tenderer's negotiated final costs with a benchmark, and was incompatible with the CPRs. The CPRs require each eligible⁹⁵ tenderer's financial and nonfinancial benefit to be compared on a like for like basis with other eligible tenders.
- The scope of services set out in the statement of requirement. In particular, whether the department had policy authority to expand the services or increase the value of the contract beyond the contracts which were in place. The value of expanded services was estimated by an external adviser (KPMG) at between \$594 million to \$835 million above historical costs. The Government had not provided policy authority to expand the services or increase the funding value of the contract to accommodate service enhancements or adjustments.

4.4 In planning for procurement the CPRs require that entities reflect on the scale, scope and risk of the procurement. Finance guidance also advises on the steps to undertake when planning a procurement. Key steps are outlined in Box 4.

Box 4: Plan the procurement based on an identified need

Finance guidance outlines the procurement process considerations:

- Determine the objectives for the procurement.
- Detail a clear scope of requirements.
- Consult entity Central Procurement Area for advice where appropriate.
- Seek specialist advice where appropriate.
- Research the market to understand capabilities and restraints.
- Ensure probity arrangements are considered, where appropriate.
- Document relevant decisions and justifications relating to the procurement.
- Understand and incorporate Australian Government transparency requirements.

Source: Finance, *Buying for the Australian Government—Procurement process considerations*.⁹⁶

4.5 The department undertook a range of planning activities which were commensurate with the scale, scope and risk of the procurement. Key activities included the development of individual

95 The CPRs require that consideration must be given only to submissions that meet the minimum content and format requirements. On this basis an eligible tender would be one that met these requirements.

96 Available from <<http://www.finance.gov.au/procurement/procurement-policy-and-guidance/buying/procurement-practice/process-considerations/practice.html>> [accessed March 2016].

procurement, project, probity, and tender evaluation plans.⁹⁷ External advisers were also engaged, including:

- KPMG—to provide financial, commercial, negotiation and project support services for the Offshore Detention Services procurement process;
- Maddocks—to provide legal process and probity advice;⁹⁸ and
- Allens Linklaters—to support DIBP’s internal legal resources and provide advice regarding the procurement activity.

4.6 The department established the Offshore Immigration Services Procurement steering committee (the committee) to provide strategic direction and advice to the delegate for the procurement project.⁹⁹ The committee (which included a representative from each host Government) was asked to endorse key processes as the tender proceeded. The committee was supported by a Senior Executive Service (SES) level reference group¹⁰⁰ which also provided support and guidance to the Offshore Procurement Project Coordination Team (the team consisted of personnel from the Services Procurement Taskforce).

4.7 The Central Procurement Unit (CPU) also provided support during the open tender process. The Assistant Secretary of Procurement and Contracts Branch, who heads the CPU, was a member of the Reference Group.

Request documentation

4.8 The CPRs establish some rules relating specifically to request documentation, which are outlined in Box 5.

97 The procurement plan set out the background, planned approach, services requirements, funding, timeframes, communications and stakeholder management plans, risks and approval processes. The project plan set out the objective, assumptions, approach, schedule, governance arrangements, risks, project structure and stakeholder management plan for the project. The probity plan set out the principles and practical procedures to be followed by all persons involved in the procurement process including the need to declare any conflicts of interest. The tender evaluation plan included general information about the procurement process, discussion on governance structure including roles, responsibilities and reporting, and the evaluation process.

98 The probity adviser’s role included assisting with the establishment of probity safeguards (probity briefings, conflict of interest declarations, confidentiality deeds, notice to Departmental personnel) and providing signoffs at various points in the process, at both predetermined stages and on an ‘as required’ basis.

99 The committee was initially chaired by the First Assistant Secretary (FAS), Detention Services Procurement Task Force, and included: stakeholders from DIBP business areas, the Department of Defence, Department of Finance, Department of Foreign Affairs and Trade, and host Governments. Following a DIBP restructure the committee was chaired by the First Assistant Secretary (FAS), Detention Services Division. Since the procurement commenced there were at least three chairs of this committee. The First Assistant Secretary (FAS), Detention Services Division, was also the delegate.

100 This group was comprised of Assistant Secretaries representing each core DIBP business area impacted by the procurement process.

Box 5: Request documentation

The CPRs require:

Notifications to the market

7.9 Relevant entities must use AusTender to publish open tenders and, to the extent practicable, to make relevant request documentation available...

Request documentation

10.6 Request documentation must include a complete description of:

- a. the procurement, including the nature, scope and, when known, the quantity of the goods and services to be procured and any requirements to be fulfilled, including any technical specifications, conformity certification, plans, drawings, or instructional materials;
- b. any conditions for participation, including any financial guarantees, information and documents that potential suppliers are required to submit;
- c. any minimum content and format requirements;
- d. evaluation criteria to be considered in assessing submissions; and
- e. any other terms or conditions relevant to the evaluation of submissions.

10.7 However, relevant entities are not obligated to release confidential information, information sensitive to essential security or information that may impede competition.

10.8 Relevant entities must ensure that potential suppliers and tenderers are dealt with fairly and in a non-discriminatory manner when providing information leading to, or following, an approach to market...

Note: Request documentation requirements outlined in 10.6 to 10.8 apply to procurements at or above the relevant procurement threshold (see Box 1).

Source: Finance, CPRs, 2014.

4.9 The Request for Tender (RFT) included a statement of requirement, a pricing schedule, a description of the evaluation process, the tender evaluation criteria and a draft contract.

Statement of Requirements

4.10 The department determined the objectives for the procurement and developed a statement of requirements as part of the open tender process. The statement of requirements set out the scope of the services to be provided and the performance standards, with the intent of enabling potential suppliers to bid for the work.

4.11 In drafting the statement of requirements the department expanded the services to be delivered beyond that of the contracts in place at the time. KPMG identified (April 2015) the changed requirements as part of determining a suitable benchmark and valued the adjustments (over the five year contract) at between \$594 million to \$835 million. The department had no policy authority to expand the scope of the contract or increase the value of the contract to accommodate service enhancements or adjustments.¹⁰¹

101 The ANAO reviewed records of PM&C, Finance and DIBP relating to the Government's decisions and Ministerial approvals.

Evaluation process

4.12 The RFT stated that the department would assess value for money by considering each tender response against: technical capability; capacity; experience; cost as represented by the assessment of price; the results of financial viability checks; an assessment of risks; and value for money assessment.

4.13 The department's planning approvals noted that in addition to the comparative assessment of value for money, KPMG would be tasked with establishing a benchmark¹⁰² for the services to be tendered:

For evaluation and planning purposes the establishment of a benchmark for the arrangements to be entered into, to aid evaluation and negotiation discussions and to manage expectations within Government would be useful. Noting that there was a benchmarking activity conducted by a consultant as part of the recent consolidation exercise, this should be revisited and expanded where possible to cover all services being tendered. It is part of the Commercial and Financial Adviser's role to establish a value for money benchmark for the services to be tendered.

4.14 KPMG's draft Benchmark—Model Report, dated April 2015, described the benchmarking process as follows:

To the extent that the preferred tenderer's final confirmed offer is lower than the total existing cost established under the benchmark model, the preferred tenderer will be considered to offer the department value for money (VFM) in purely financial terms.

It is important to the note that the development of the benchmark model is a tool that is used to support the overall VFM assessment. The overall VFM assessment includes the following main limbs:

- Limb 1: Competitive Tender Process—The Department has issued the RFT via a competitive, open market approach. The Department will evaluate the tender responses taking into consideration both financial (e.g. pricing) and technical (e.g. service capability) factors to select the preferred tenderer that offers the Department the optimal VFM outcome.
- Limb 2: Benchmark Model—For the preferred tenderer only, a final VFM assessment (in purely financial terms) will be undertaken to compare the cost of the preferred tenderer delivering the services under the new contract relative to the costs of delivering the services under the existing contract (represented by the benchmark model). The focus of this report is on the benchmark model.

4.15 The 2014 CPRs (paragraph 10.6) require that request documentation must include a complete description of evaluation criteria to be considered in assessing submission. In addition, the CPRs require that:

Officials responsible for a procurement must be satisfied, after reasonable enquires, that the procurement achieves a value for money outcome... When conducting a procurement, an official must consider the relevant financial and non-financial costs and benefits of each submission...¹⁰³

¹⁰² The ANAO's review indicated that the same process (comparison of the preferred supplier in an open tender process against the existing cost of services) was used in the 2014 procurement for onshore detention.

¹⁰³ Finance, CPRs 2014, paragraphs 4.4 and 4.5, p. 13.

4.16 The CPRs do not refer to the use of benchmarks. The department's request for tender (RFT) did not include as an evaluation criterion comparison of the preferred supplier against a benchmark. The risk in the benchmarking approach is that:

- not all suppliers would be assessed on the same basis;
- the negotiation process might substantially change the tenderer's bid (price or services) and this may no longer represent value for money against the other tender bids; and
- a comparison of tendered prices against the benchmark would provide the incumbent provider(s) with an unfair advantage over potential suppliers.

Accessing the RFT

4.17 The RFT was released on a restricted AusTender site. To access the site, and thereby access the RFT and other tender-related information, prospective tenderers were advised to complete a 'Further Material Registration Form'. This form required prospective tenderers to submit registration forms for industry briefings and site visits and sign a deed of confidentiality. Prospective tenderers were advised that if they did not submit the specified documents in accordance with the requirements they would not be provided with access to the RFT. The available documentation indicates that although these requirements were established they were not enforced. Forms for all tenderers were not maintained and some forms provided by tenderers were incomplete. In both circumstances prospective tenderers were given access to the site.¹⁰⁴

Record keeping

4.18 The department developed an electronic record structure (g-drive and TRIM folder) to document the procurement process. Once again, while DIBP established a requirement, its use was not enforced. When reviewing the TRIM files the ANAO found that 94 of the 122 TRIM files contained no records, including most request for tender documentation files. For example TRIM did not contain the tender response records as they had not been filed appropriately.

4.19 The department continued to create files for months after the identification of the preferred tenderer, including during the course of this audit. For example, individual evaluations were collected and filed in January 2016 after an ANAO request for these documents. This activity occurred around six months after preferred tenderers were selected. As a result, there is a lack of evidence that these were the actual evaluations prepared by each evaluator in the Garrison and Welfare Services evaluation team (at the time of the final evaluation). The integrity of these documents cannot be guaranteed.¹⁰⁵

Conflict of Interest

4.20 The CPRs establish rules in relation to ethical behaviour. Officials undertaking procurement must act ethically throughout the procurement (2014 CPRs, paragraph 6.6) and are expected to recognise and deal with actual, potential and perceived conflicts of interest. The department retained the majority of records of specific conflict of interest declarations made by departmental officials and external parties (approximately 260 out of 290) involved in the procurement process.

¹⁰⁴ The forms for the preferred and reserve tenderers were maintained and were completed.

¹⁰⁵ These issues are addressed in the department's comments on the proposed audit report. See Appendix 1.

4.21 A number of conflict of interest declarations were signed after the procurement commenced, and there was insufficient detail to determine when these officials first became involved in the procurement. In accordance with section 13(7) of the Code of Conduct contained in the *Public Service Act 1999*, an Australian Public Service employee must: take reasonable steps to avoid any conflict of interest (real or apparent) in connection with the employee's APS employment; and disclose details of any material personal interest of the employee in connection with the employee's APS employment. Agency heads and SES level employees are required to declare in writing, at least annually, their own and their immediate family's financial and other interests that could cause a real or apparent conflict of interest.¹⁰⁶

4.22 DIBP requires annual conflict of interest declarations from all staff and annual personal interest disclosures for SES officers. The ANAO's review indicated that available records did not include annual conflict of interest and personal interest disclosures for each of the departmental officials who occupied delegate positions for the procurement. In addition, annual conflict of interest and personal interest disclosures were not available for ANAO review for 22 out of 47 senior executives identified by the ANAO as being involved in the current or previous procurement activities for the services (conducted in 2012 and 2013–14).

4.23 KPMG was engaged as commercial adviser in August 2014 and at that time advised the department that there were no conflicts of interest that would affect its appointment or that were anticipated to arise in the course of the contract. On 3 July 2015, KPMG again wrote to the department advising of potential conflict of interest issues with individual tenderers—some three months after tenders closed and over ten months after KPMG was engaged. KPMG listed the services it had provided to each of the tenderers in the last 12 months and advised:

we do not consider that providing these services raises any conflict of interest with the Engagement given our strict confidentiality and conflict management policies and procedures (see below), and given that these services are unrelated to the Project identified.

4.24 KPMG advised that the services provided to tenderers included:

- External audit and advisory services provided to Transfield Services (Australia) Pty Limited and to Transfield Services Limited...[and]
- ...internal audit, tax and advisory services to entities related to Serco Group ... in Australia.

4.25 Probity advice provided to the department on 13 July 2015 stated that:

KPMG Personnel are 'personnel involved in the Procurement' for the purposes of the Probity Plan ... given the nature of the engagements and the mitigations as disclosed, we do not have any material probity concerns with KPMG's ongoing engagement in this process.

However, it is important to note the particularly late stage at which the Letter has been provided by KPMG. We understand that KPMG has had a significant role in formulating the pricing requirements and evaluation methodology as part of this process and it is surprising to us that this formal notice has been issued at least 10 months from the date of KPMG's engagement ... and only now that the evaluation process is significantly progressed.

¹⁰⁶ Available from <<http://www.apsc.gov.au/working-in-the-aps/your-rights-and-responsibilities-as-an-aps-employee/declaration-of-interests>> [accessed March 2016].

In this regard, the assurance provided by KPMG in the Letter seems, from a process and probity perspective, to be of considerably less value than if it were received as part of KPMG's onboarding or, at least, as soon as possible after tenderers were registered/confirmed as actively engaged within this process.

The obligations of KPMG Personnel under the Probity Plan (and where relevant, the Tender Evaluation Plan), are in addition to any obligations relating to conflict of interest and confidentiality that KPMG Personnel and KPMG as an organisation may have at law (including in relation to KPMG's work order entered into with the Department in relation to the Procurement).

4.26 This case illustrates the importance of consultants providing meaningful assurance to government clients in respect to potential conflicts of interest.¹⁰⁷

Did the department adopt tender evaluation processes consistent with the requirements of the *Commonwealth Procurement Rules*?

The department's tender evaluation processes were not sufficiently robust to meet a range of applicable CPR requirements. In particular:

- the department was unable to demonstrate that the original tender documents lodged through AusTender were used by evaluation team members for the tender evaluation;
- individual assessor records were incomplete and there were missing documents in relation to various aspects of the process;
- using compact disks rather than TRIM¹⁰⁸ files did not provide sufficient control over the security of the tender documentation and the commercial material contained within those documents; and
- there were significant unquantified pricing risks related to most of the tender bids, which the department did not clarify prior to selecting a preferred tenderer and forming an opinion on value for money of the preferred and reserve tenderers.

The assessment of value for money focused on provider claims and referee reports and did not take into account the department's own contract management experience with suppliers.

Receipt and opening of submissions

4.27 The CPRs establish some rules relating specifically to receipt and opening of submissions which are outlined in Box 6.

107 In response to the proposed audit report KPMG advised that there were numerous discussions between KPMG and Department representatives, between the date of KPMG's appointment and the receipt of tender submissions, in which KPMG's relationship with Transfield was discussed. The ANAO has not been provided with any documentation to support this. KPMG also noted in its response that it had advised DIBP on 10 June 2015 that it was the auditor of Transfield, in the context of submitting its financial viability assessment report on the tender proposals received as part of the department's open tender process. Disclosures relating to conflict of interest must be timely in order to enable entities to assess risk and consider appropriate mitigation strategies. The onus was on KPMG to make declarations relating to conflict of interest before performing that work. This matter is discussed further at Appendix 1.

108 TRIM is the department's official electronic document and records management system.

Box 6: Receipt and opening of tender documents—additional rules for procurements at or above the relevant procurement threshold

The CPRs require:

Receipt and opening of submissions

10.28 Procedures to receive and open submissions must guarantee fairness and impartiality and must ensure that submissions are treated in confidence.

10.29 When a relevant entity provides tenderers with opportunities to correct unintentional errors of form between the opening of submissions and any decision, the relevant entity must provide the opportunity equitably to all tenderers.

10.30 Further consideration must be given only to submissions that meet minimum content and format requirements.

Source: Finance, CPRs, 2014.

4.28 All tenders were submitted through AusTender on or before 7 April 2015. The department adopted a process of downloading tender documents to compact disks for the purpose of distributing tender documents to the evaluation team members. There were three forms acknowledging receipt of the compact disks. These forms were not the standard form used by the department to acknowledge distribution of tender documentation and provided little assurance that a complete set of tender documentation was provided to each evaluation team member. In addition one of the records was created in April 2016 (twelve months after tenders closed).

4.29 While the department created files containing parts of the tender responses, the evaluation team used compact disks for the tender assessment process. DIBP advised that this was to enable printing of the tender responses. Using compact disks did not provide sufficient control over the security of the tender documentation and the commercial materials contained within those documents, or ensure that the tender documentation provided to the evaluation team was accurate and complete. This approach undermined the controls offered by a record management system.¹⁰⁹

4.30 As outlined in the RFT, following the receipt of tenders the department was to complete a registration and initial screening process. The department's evaluation report stated that by the close of the tender (7 April 2015), six tender bids (and three alternative bids)¹¹⁰ for the provision of garrison support and welfare services were received. These bids were intended to be downloaded from AusTender and screened for general completeness.

4.31 While the department conducted financial viability assessments, there were no records of the department conducting independent due diligence checks of corporate information. Transfield had again declared the owners of its major subcontractor, Wilson Security, in its tender. As indicated

¹⁰⁹ These controls relate to information management including that records: can be proven to be genuine, are accurate and can be trusted; are complete and unaltered; are secured from unauthorised access, alteration and deletion; are findable and readable; and are related to other relevant records.

¹¹⁰ DIBP received three alternative tenders from three of the tenderers. The RFT allowed the department to consider an alternative approach that did not meet all aspects of the requirements only where the tenderer submitted a separate tender containing a solution that did. The three tenders who submitted alternative tenders also submitted separate tenders containing a solution that met all aspects of the requirements.

in paragraph 3.75 it would have been prudent for the department to conduct and document due diligence checks for the open tender process. Separate from the tender process in 2016 the department sought advice from Transfield in relation to Wilson Security. Transfield commissioned a report to be prepared by an independent adviser, but considered the report to be commercial in confidence and did not provide it to DIBP. The department did not undertake its own due diligence at this time.¹¹¹

Technical evaluation

4.32 To compare tenderers' bids against the technical specifications set out in the RFT, the evaluation team members assessed each tenderer's response and determined a technical score. These scores were then combined to obtain an overall technical score. In its evaluation report the technical evaluation team concluded that only two of the six responses demonstrated sufficient technical understanding to provide the required services.

4.33 The ANAO's review of available departmental records indicates that the records of the technical evaluation were incomplete. In particular:

- the tenderer listed may not have been the tenderer considered during the evaluation process—one evaluation contains the names of more than one tenderer;
- evaluators are not clearly identified—in some cases there was no evaluator listed or two different evaluators were listed on an evaluation;
- the documentation provided to the ANAO may not be the final document as the dates for creating and/or editing the documents are subsequent to the selection of the preferred tenderer; and
- no records are available on the technical assessment of the alternative tenders.

Pricing

4.34 During the evaluation stage the department's pricing team identified a number of pricing issues and risks relating to all six tenderers.¹¹² A number of pricing issues and risks were quantified. Issues that were unable to be quantified were carried through to be considered during negotiation.

4.35 The team identified that there were significant unquantified pricing risks related to assumptions made in Transfield's tender bid which could have a material impact on price. Transfield had assumed that within a centre, one compound would be filled to maximum capacity prior to another compound being opened. Based on preliminary departmental analysis detailed in the Pricing Evaluation Report, the additional cost of operating separate compounds across both sites could vary between \$40 and \$257 million over the life of the contract. The evaluation report noted that only Transfield's tender bid provided any assumptions as to how transferees would be placed within the centres.¹¹³

111 To evidence that the report had been prepared, Transfield provided DIBP with a copy of a letter and explanatory report from the independent adviser relating to the engagement and final completion of the report.

112 Common issues across all tenderers related to assets, taxation and pass through costs.

113 The pricing team noted that the RFT did not provide guidance on how transferees should be placed within the centres and therefore, it was not possible to determine whether other tenderers made similar assumptions to Transfield. The pricing team further noted that Transfield's assumption was not inconsistent with the

4.36 The ANAO also identified discrepancies between pricing information contained in tender submissions and information recorded in the pricing evaluation.

Assessment of value for money

4.37 An open (competitive) tender involves comparing tenderers' submissions against each other in accordance with the evaluation criteria outlined in the RFT. The 2014 CPRs set out factors to consider in conducting this analysis, including fitness for purpose and a supplier's experience and performance history.

4.38 The department's evaluation report stated that to establish value for money the evaluation team considered: the technical assessments; cost (represented by the assessment of price); the results of financial viability checks; referee checks; additional information; and an assessment of risk. The ANAO's review indicated that in practice the department's comparative assessment was limited. The department focused on the claims in tenderer bids and referee reports and the ANAO saw no evidence of the department drawing on its own direct contract management experience with suppliers. For example, there was no evidence of consideration of Transfield's performance in relation to facilities maintenance and hygiene issues which had been documented in consecutive Chief Medical Officer Reports. The evaluation panel assessed Transfield's (now Broadspectrum) claims in respect of its experience to be:

... outstandingly convincing and credible, and had high level of confidence in Broadspectrum's ability to deliver, and often exceed requirements.

4.39 The Evaluation Committee ranked Transfield first and another tenderer (Serco) second in terms of value for money. Remaining tenderers were not ranked for value for money. On 28 August 2015 DIBP advised Transfield that it was the preferred tenderer and Serco that it was the reserve tenderer. On 31 August 2015 Transfield advised the Australian Stock Exchange that it had:

... been notified that it has been selected as the preferred tenderer to provide welfare and garrison support services for the Department of Immigration and Border Protection at the Offshore Processing Centres in Nauru and Manus Province. Subject to completion of a contract, the Company will be responsible for providing these services for a further five years.¹¹⁴

information contained within the RFT.

114 Available from <<http://tse.live.irmau.com/IRM/PDF/1979/TransfieldServicespreferredtendererforDIBPcontract>> [accessed 17 March 2016].

Did the department's negotiation processes facilitate value for money?

The department determined to only enter into negotiations with the preferred tenderer (Transfield). During the course of negotiations the department amended its requirements and accepted enhancements and adjustments to services which flowed through to a \$1.1 billion increase in Transfield's overall price. The department did not seek clarification or repricing from any other tenderers and instead set out to determine value for money by comparing the negotiated price with a benchmark. The benchmark was the cost of services provided in Nauru and on Manus Island, which had been procured via a non-competitive limited tender process in 2013–14. The approach adopted was not consistent with an open tender which requires that eligible tender bids are compared on a like for like basis.

The delegate had determined to finalise the procurement process and sign the contract. There are no available records to demonstrate that the delegate: considered if sufficient funds were available to enter into the commitment; considered if additional policy authority was required to accommodate the service enhancements negotiated; or questioned the increased cost of the bid.

4.40 It was open to the department to enter into negotiations with both the preferred and reserve tenderers. The department decided to only enter into negotiations with the preferred tenderer. There is no available record of the basis for this decision. In recommending to the delegate that the department proceed to negotiations, the Evaluation Committee noted that: a number of unquantifiable pricing issues required clarification; and changes to the department's requirement (since the RFT was issued) would require agreement during negotiations with the preferred Tenderer.

4.41 Available documentation indicates that the changed requirements were not communicated to other tenderers and the department did not seek clarification or repricing from any other tenderers.¹¹⁵ In contrast, paragraph 10.12 of the 2014 CPRs requires that:

When, during the course of a procurement, a relevant entity modifies the evaluation criteria or specifications set out in an approach to market or in request documentation, or amends or reissues an approach to market or request documentation, it must transmit all modifications or amended or reissued documents:

- a. to all the potential suppliers that are participating at the time the information is amended, if known, and, in all other cases, in the same manner as the original information; and
- b. in adequate time to allow potential suppliers to modify and re-lodge their submissions, if required.

4.42 In addition, the department's Accountable Authority Instructions (AAIs)¹¹⁶ stated at the time, that:

115 The department advised the ANAO that non-shortlisted tenderers were notified on 31 August 2015 that they were unsuccessful, and therefore were no longer participating in the process at the time the information was amended.

116 The department's AAIs are issued under section 20A of the *Public Governance, Performance and Accountability Act 2013*. AAIs provide instruction to officials on resource management and all staff must act in accordance with them.

3.50 You must avoid a potential supplier, or group of potential suppliers, gaining an unfair advantage.

3.51 You must provide to all potential suppliers all modifications, amendments or reissued documents and allow adequate time, if required, for them to modify and re-lodge submissions, where the evaluation criteria or specifications set out in an approach to market or in request documentation are modified, or where an approach to market or request document is amended or reissued.

3.52 You must ensure that a supplier who has assisted in the design of specifications in procurement does not have an unfair advantage over other potential suppliers.¹¹⁷

Reaching agreement with the preferred supplier

4.43 The negotiation team¹¹⁸ reached agreement on a final negotiated outcome with Transfield in December 2015. The final confirmed offer included a price increase of \$1.1 billion compared to Transfield's original tendered bid.¹¹⁹ The department's negotiation report noted that the price increase was due to:

- the clarification and specification of particular tenderer assumptions, unquantified risks and non-priced risks identified during the evaluation stage (58 per cent); and
- enhancements identified during the negotiation stage (42 per cent).¹²⁰

4.44 To determine whether Transfield's final negotiated offer provided overall value for money, the department only compared Transfield's price with the benchmark (the cost of the existing services provided by Transfield),¹²¹ rather than the price in other tender bids. The department's Final Negotiated Outcomes Report noted that Transfield's final confirmed offer was lower than the total existing cost established under the benchmark model and therefore represented value for money:

After consideration of all negotiated items, the final cost of the negotiated G&W [garrison support and welfare] contract is expected to be approximately 34% lower than the existing contract costs. This figure is based on Transferee numbers as at 30 June 2015, is in nominal terms over a five year period, and takes into account the additional service requirements, as well as the application of both inflation (assumed 2.5%) and the efficiency dividend (of 3.25%).

4.45 The available records indicate that by 14 December 2015, a contract with Transfield (now Broadspectrum) was being prepared for the delegate's approval and signature.¹²² A recommendation from the negotiation team to the committee was that the delegate execute the contract.¹²³ The department's records also indicate that the delegate was planning to disband the

117 DIBP, Accountable Authority Instructions—Resource management framework, 1 July 2015, p. 26. This requirement was also included in DIBP, Accountable Authority Instructions, 1 July 2014, p.24.

118 The negotiation team was led by the Assistant Secretary, Services Procurement Task Force.

119 Based on the negotiation scenario, which assumed transferee and refugee numbers as at 30 June 2015.

120 For example, this included over \$300 million to maintain the current proportion of locally engaged staff.

121 The benchmark was discussed in paragraphs 4.12–4.16 of this audit report.

122 The delegate was the First Assistant Secretary, Detention Services Division.

123 On 28 October 2015 a four-month extension to Transfield's existing contract (which was due to expire on 31 October 2015) was put into place to allow for the completion of negotiations and transition. Pursuant to that extension the existing contract would expire on 29 February 2016 (unless otherwise extended by the parties). On 26 February 2016 the parties did agree to a further extension of the contract, with the

procurement taskforce as the procurement was expected to be finalised. No concern was raised at this stage as to whether the service enhancements fell within the scope of the Government authority or if there was funding available to cover the overall price of Transfield's tender bid.

4.46 In October 2015 the Minister for Immigration and Border Protection had written to the Prime Minister and the Minister for Finance regarding a funding shortfall and seeking authorisation to enable DIBP to enter into a five year financial commitment for the delivery of services in Nauru and on Manus Island. In his response the Finance Minister (8 November 2015) authorised the accountable authority (the departmental; Secretary) to consider entering into arrangements which involve expenditure of \$3.0 billion to 28 February 2021. The Minister also indicated that his authorisation did not provide policy authority or create an appropriation. Further, it did not provide funds to meet any claims against the Commonwealth, or remove any obligations on the part of departmental officials to promote proper use and management of public resources under the *Public Governance, Performance and Accountability Act 2013*.

4.47 The ANAO's review indicated that there was no subsequent approach for additional funding.¹²⁴ The Minister was required to return to Government in the context of the 2016–17 Budget with an audit of service levels as part of a Holistic Review of onshore and offshore detention and offshore processing policy assumptions and operational framework. The review had not included the offshore arrangements.

4.48 Within the offshore arrangements, the department has previously committed funding beyond its policy authority. In June 2015 the department had entered into commitments beyond the available funding for the Illegal Offshore Management Programme 3.5. This resulted in the Minister seeking additional authority from the Prime Minister to cover supplier invoices. The Minister advised the Prime Minister that Programme 3.5: Illegal Maritime Arrival Offshore Management was insufficiently funded to meet the supplier costs associated with major offshore contracts and the Program required a further \$110 million in administered appropriation to meet financial year commitments. The Minister also indicated that if funding was not made available there was a risk that supplier invoices would not be paid.

4.49 The Prime Minister agreed to move funding from Onshore Management (Programme 3.3) to cover the shortfall. In responding to the briefing from his department, the Prime Minister indicated that DIBP needed to improve its administration to avoid a recurrence.

arrangements coming into full effect under that extension on 1 March 2016.

124 Table 4.1 of this audit report shows anticipated expenditure for offshore management of illegal maritime arrivals at the time of the Budget 2015–2016.

Did the department establish effective oversight controls?

A steering committee and independent probity adviser were key oversight mechanisms for the open tender process. Both were consulted after the negotiation team had reached agreement on a final negotiated outcome with Transfield and prior to the anticipated contract signing. The probity adviser identified that the department's negotiation report appeared to include substantial modifications to the statement of requirement from that released to the market and that Transfield appeared to have been permitted to make material changes to its original tender, including significant overall price increases. The probity adviser considered that these developments raised significant probity and process risks, including the risk that the department was not in a position to determine whether the changes continued to represent best overall value for money compared with other tenderers.

After considering this advice the steering committee decided it was unable to determine whether the final negotiated outcome with Transfield demonstrated best value for money. The effective operation of these oversight mechanisms contributed to the department initiating an amended tender process. The Minister was advised of the amended tender process prior to it commencing, and that approvals for funding would need to be reassessed. The amended process only involved the preferred and reserve tenderers and was in effect a limited tender process. On 29 July 2016, in the course of this audit, the department cancelled the initial and amended request for tender. DIBP extended its contract with Transfield until 31 October 2017 and the department advised the ANAO on 29 August 2016 that it was conducting market testing to determine its next steps.

Probity advice

4.50 Prior to contract signing the department consulted with the steering committee advising of the final negotiated outcome. In this context the probity adviser raised a number of concerns:

The Negotiation Report details the outcomes of the Department's negotiations with the preferred Tenderer, Transfield Service (Australia) Pty Ltd (Transfield). We note that we have not been involved in those negotiations.

In particular the outcomes in the Negotiation Report highlight:

- a significant price increase from the prices as tendered by Transfield as assessed during the evaluation stage (i.e. by approx. A\$1.1 billion)
- what appears to be substantial amendments to the existing Statement of Requirement (SOR) as released to the market.

Broadly, we understand these have resulted from:

- further clarification and specification of particular 'tenderer assumptions', 'unquantified risks' and 'non-priced risks' identified during the evaluation stage (of approx. \$642 million); and
- 'enhancements' and 'other movements' identified during the negotiation stage (of approx. \$461 million).

4.51 The probity adviser further stated that:

The changes negotiated with Transfield, when considered as a whole, are significant and material in light of scope of the initial Procurement. These negotiated outcomes potentially raise significant probity and process risks in the context of an open and competitive tender process such as this Procurement.

4.52 In light of the department's updated requirements, the probity adviser also stated:

First, it is unclear whether there has been any substantive qualitative consideration or assessment of the capacity or capability of Transfield to actually deliver against the (significantly) modified service arrangements resulting from the negotiations. In this regard, the CPRs require the Department to consider the relevant financial and non-financial costs and benefits of each Tender.

Secondly, it is unclear how using the 'benchmark' in this section of the Negotiation Report as a primary basis for comparative analysis of price is relevant... While we understand that the department's benchmark model formed part of the evaluation methodology, this 'benchmark' does not determine overall value for money. The TEC's¹²⁵ primary consideration of overall value for money was properly focussed on comparisons between tendered solutions offered according to the published evaluation criteria, including tendered price. Accordingly, while references in the Negotiation Report to "expected cost reductions" of 34% ... clearly highlight the difference between what the Department currently pays and what it may potentially pay under the Transfield tender, this information should not be taken as being determinative of value for money as part of this Procurement.

Instead, comparative assessment between tendered solutions provides a sound basis for such determination and, in this regard, the Negotiation Report states that:

The Department notes it is not possible to identify the potential cost impact associated with negotiating any issues with any other Tenderer (as the Department did not enter into negotiations with those parties). As such, the cost for other Tenderers (as evaluated) does not include any potential cost associated with any issues that would have been negotiated with those parties.

4.53 The probity adviser concluded that:

The Negotiation Report highlights what appears to be substantial modifications to the SOR [Statement of Requirement] from that released to the market and, as a result, Transfield appears to have been permitted to make material changes to its original tender, including significant overall price increases.

This raises significant probity and process risks, including the potential risk that the Department is not currently in a position to adequately assess and/or determine whether the changes to Transfield's tender resulting from the negotiations (including increases in tendered pricing) continue to represent best overall value for money for the Department compared with other tenderers received and evaluated.

As such we recommend that the Department consider, from an overall value for money perspective, its options in regards to:

- re-opening the existing process to allow one or more other tenderers an opportunity to respond to the 'new' or substantially 'modified' requirements (and re-evaluate those additional requirements according to the relevant evaluation criteria); or
- commencing a new procurement process for the 'new' or 'altered' requirements.

125 ANAO comment: TEC refers to the Tender Evaluation Committee, also referred to as the Evaluation Panel or team.

Amending the open tender

4.54 Following its consideration of this advice the steering committee decided it was unable to determine whether the final negotiated outcome with Transfield demonstrated best value for money. The department formed a committee of senior departmental representatives to review and consider the scope and impact of the outcomes of the negotiation on the procurement. The delegate decided not to suspend negotiations underway between the Department and Transfield pending this review.

4.55 Three options were presented to the steering committee:

- (a) commence negotiations with the Reserve Tenderer and continue negotiations with Transfield to seek an amended offer from both;
- (b) seek a revised offer from both Transfield and the reserved tenderer; or
- (c) commence a new procurement process.

4.56 The department decided to proceed with option b)—seek a revised offer from Transfield and the reserved tenderer (Serco). The department advised both Transfield and Serco of its decision and invited them to participate in the process. This would involve each party submitting an amended tender reflecting the department’s updated requirements. In advising the Secretary of the status of the procurement, the delegate provided details of the \$1.1 billion increase in bid value, but did not indicate that any of these additional costs related to service enhancements. The Secretary did not comment on the increase in the bid price, but did request that the delegate:

Move more quickly on briefing MIBP [Minister for Immigration and Border Protection] and others as required.

4.57 The Minister was subsequently advised of the amended process. The Minister was further advised that approvals for financial commitments beyond the current financial year would need to be reassessed.

Procurement advice

4.58 The department sought (on 12 and 25 February 2016) and obtained advice from the Department of Finance in relation to the reimbursement of tenderers’ costs for the amended tender process. Finance advised on 1 March 2016 that:

The procurement framework is a devolved framework. This means that, as previously advised, Finance is not in a position to endorse your proposal. Also, we reiterate that it is not common practice for entities to reimburse bidding costs, nor is it a practice Finance actively encourages. However, we recognise that precedent has been set to reimburse bidders in exceptional circumstances. Importantly, we have no guidance or experience in reimbursement terms and conditions.

We can confirm that generally, reimbursement of bidders’ costs is not prohibited by the procurement framework.

Your emails mention an amended or revised tender. We assume this means that you’ve completed an unsuccessful tender process and are now undertaking a new tender process. It is unclear the extent to which the original procurement documentation has been modified for this subsequent procurement. In relation to the reimbursement payment we observe the following.

The payments appear to partially be compensation for the failed process; reimbursement of tendering costs weren't required in the first process. This indicates:

- Deficiencies in the first procurement process that should be rectified prior to reapproaching the market; and/or
- That tenderers submitted inadequate bids, making it appear unreasonable to give them another opportunity.
- The costs of re-submitting a bid should be less than an entirely new response, with much of the ground work done in preparing the initial bid. Consistent with the above point, we would assume that there should be minimal costs in restructuring and submitting a bid.
- The CPRs require procurement processes to be commensurate with the scale and scope of the procurement, so we would infer that bidding costs of up to \$200,000 would indicate a significant tender response. If this isn't a significant procurement, then perhaps consider revising/simplifying your tender documentation.
- Only two market participants are being asked to participate in the second tender process; this may suggest a perceived conflict of interest that must be carefully managed, especially if the first tender process was an open tender process.
- Immigration should carefully consider the likelihood of tenderers bidding if they didn't receive payment. Further, Immigration should consider the precedent it is setting in responding to a request for reimbursement, rather than determining without influence that reimbursement is necessary.

Such exceptional circumstances would be where the nature of the market is such that in order to obtain a value for money outcome, suppliers must be supported in submitting tenders to Government procurements. We'd contend that these markets would have limited competition, or relatively small suppliers that couldn't otherwise absorb the costs of participating in a tender process...

...More broadly, we would encourage Immigration to carefully consider its new procurement process and document any relevant decisions, including the use of exemptions and/or limited tender¹²⁶ conditions.

4.59 In respect to the revised process, Finance referred the ANAO to clause 10.12 of the CPRs which relates to modification of evaluation criteria or specifications, Finance advised that:

our interpretation of the intent of clause 10.12 of the CPRs is that any modification to evaluation criteria or specifications occurring after the tender had closed would need to be advised to all potential suppliers (i.e. all those that had submitted a response to the original tender), unless they failed to meet either the conditions for participation or the minimum format and contents requirements.

4.60 An amended request for tender was released on 15 April 2016 and this procurement was underway at the time of the ANAO's audit and the receipt by the department of the ANAO's draft audit report. While the department's records indicate that the process was considered a continuation of the open tender, the amended process was in effect a limited tender involving the preferred and reserve tenderers.

126 ANAO comment: Limited tender involves an entity approaching one or more potential suppliers to make submissions, where the process does not meet the rules for open tender or prequalified tender. 2014 CPRs, paragraphs 9.8–9.10.

4.61 The department advised the ANAO on 29 August 2016 that:

since the finalisation of the audit, the request for tender (DIBP RFT 28/14) and subsequent request for amended tender (DIBP RFAT28/14) detailed in Part 4 were cancelled by the Department on 29 July 2016. The Department is now conducting market testing to determine our next steps. To accommodate this, the Department has extended its contract with the current provider to October 2017.

Recommendations

4.62 Procurement is core business for Commonwealth entities and deficiencies can result in higher than necessary expense for taxpayers and significant reputational risks for the Australian Government and responsible entities.

4.63 This audit highlights significant weaknesses in the Department of Immigration and Border Protection's administration of procurement. The audit recommendations are intended to address:

- the significant skill and capability gaps identified amongst personnel at all levels in the department, including within the central procurement and budget units; and
- persistent shortcomings in the planning and conduct of the procurements, including in relation to record keeping, consistency and fairness in the treatment of suppliers, and the assessment of value for money.

Recommendation No.1

4.64 That the Department of Immigration and Border Protection address, as a priority:

- (a) through training and staff selection—the significant procurement skill and capability gaps identified in this audit amongst personnel at all levels, including:
 - the central procurement unit
 - budget unit;
 - program area staff; and
 - delegates;
- (b) through guidance, training and staff selection—an approach to ensuring that officials have appropriate seniority and experience to undertake key procurement roles, such as chief negotiators and delegates, and effectively manage procurement risk; and
- (c) through guidance, training and a strategic approach to records management—persistent shortcomings in record keeping for procurement activities.

Entity response: *Agreed*

Recommendation No.2

4.65 That the Department of Immigration and Border Protection take practical steps to ensure adherence to the requirements of the resource management framework when undertaking procurements, including:

- (a) the obligation to manage all aspects of a procurement process in accordance with the *Commonwealth Procurement Rules*;
- (b) compliance with the Government approved scope and contract value;
- (c) in respect to open tender processes, adopting a value for money assessment which compares tenderers against other bids;
- (d) the application of documented eligibility criteria in line with the Request for Tender and consistent with the *Commonwealth Procurement Rules*, with any modifications advised to all potential suppliers;
- (e) the need for ethical conduct throughout the procurement to ensure consistent and fair treatment of suppliers;
- (f) the need to recognise and manage actual, potential and perceived conflicts of interest; and
- (g) the maintenance of clear and complete records of all tender bids, key actions, decisions, conflict of interest and SES disclosure declarations.

Entity response: *Agreed*



Grant Hehir
Auditor-General


Canberra ACT
13 September 2016

Appendices

Appendix 1 Entity responses

Department of Immigration and Border Protection

- 1 SEP 2016
C/GD



Australian Government
**Department of Immigration
and Border Protection**

DEPUTY SECRETARY

Dr Tom Ioannou
Group Executive Director
Performance Audit Services Group
Australian National Audit Office
GPO Box 707
Canberra ACT 2601

Dear Dr Ioannou

Thank you for the opportunity to provide comments on the audit report on *Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services*.

Complex and constantly evolving operating environment

Before responding to the report and its recommendations, I think it worthwhile to clarify the circumstances in which these procurements took place – particularly in the very early stages of establishing the regional processing centres (RPCs).

In accepting all 22 recommendations of the *Report of the Expert Panel on Asylum Seekers*, commissioned and prepared over a seven-week period during which more than 2700 people arrived illegally by boat, then Prime Minister Gillard announced that the government would be in a position to commence arrangements within days after the passage of legislation to begin regional processing in Nauru and Manus (Papua New Guinea).

There had been more illegal maritime arrivals in the first seven months of 2012 (6,953) than the number who arrived in total in 2011 (4,793). Australia's onshore immigration detention network had been rapidly expanding and was under considerable strain: almost 7,000 people were in held detention, of whom about 95 per cent were boat arrivals.

When legislation was passed on 17 August 2012 enabling regional processing – four days after the release of the expert panel's report – the Department needed to establish the necessary operational requirements immediately. Consistent with expectations, the first asylum seekers arrived in Nauru three weeks later on 14 September 2012. The Department met these requirements in an environment that was high-tempo, at the peak of national interest and complicated through logistics and uncertainties involved with processing in foreign countries. Delegates were required to make decisions on complex and high risk matters within very short timeframes.

The environment remains extremely complex. The Department provides support to the Governments of Nauru and PNG, who have effective control over the RPCs. It remains open to these Governments at any time to make decisions which effect immediate changes to the administration of the centres. Accordingly, the Department has to adopt procurement processes that are sufficiently agile to accommodate this environment.

This has meant, in particular, adjusting the service levels throughout the tender and negotiation of the contracts to match changes on the ground. The Department considered it

6 Chan Street Belconnen ACT 2617
PO Box 25 BELCONNEN ACT 2616 • Telephone: 02 6264 1111 • Fax: 02 6225 6970 • www.border.gov.au

important ensure that the services being procured kept pace with emerging needs of clients within the RPCs, particularly at a time when media and numerous external scrutiny bodies were evaluating (and continue to evaluate) the quality and standard of services being provided within the RPCs. The changes introduced were essential to the overall well-being of individuals at the RPCs and included measures such as increasing the number and type of meal choices and increasing the quality and availability of cultural liaison services to refugees and transferees.

The Department believes that these decisions were consistent with its overall policy authority under Operation Sovereign Borders and funding and appropriation levels were adjusted, in accordance with the Cabinet agreed processes, at the Commonwealth Budget updates over the period in question.

Throughout each stage of each procurement process, the Department carefully considered the selection of tenderers. A number of factors were considered before any decisions were made to set aside tender bids. These included the capability of tenderers to set-up services quickly, the market and risk implications of having the same contractor delivering services to the RPCs and the onshore detention network and the emerging security needs at the centres.

Response to the specific recommendations

The Department acknowledges that its decision-making processes in this complex and rapidly evolving environment have not been adequately documented at each stage of the procurement process. The absence of appropriate records makes it difficult to adequately demonstrate that the judgements made were appropriate and that due process was applied.

The Department takes its responsibilities for the use of public monies seriously and agrees that the two recommendations will strengthen the capability of the Department to undertake efficient, effective and ethical procurement. We have analysed our procurement and contracting practices and identified a number of improvements for implementation. These improvements will be progressively introduced as part of a broad reform programme that will provide confidence that all procurement is conducted in accordance with the Commonwealth Procurement Rules (CPRs) and reflects industry best practice. This plan is set out in Attachment A and has three main elements:

1. We will immediately introduce stage gate reviews to ensure that all complex, high risk and/or high value procurements are being undertaken in accordance with commercial best-practice, and the requirements of the CPRs and appropriate probity requirements;
2. We will increase independent assurance over all complex, high-risk and/or high-value procurements, as part of regular health checks overseen by the Chief Audit Executive and the Chief Finance Officer; and
3. Reforms over the next 12 months will be implemented to strengthen the internal procurement framework, improve information management and increase the skills and capacity of Departmental staff to manage major procurements.

The Department also takes its information security obligations seriously and complies with the Australian Government Protective Security Policy Framework (PSPF) and Information Security Manual (ISM) to ensure the protection of its people, information and assets meet the standards set for Australian Government agencies. All individuals employed by the Department maintain a security clearance provisioned by the Australian Government Security Vetting Agency appropriate to the information that they handle. The Department has recently completed its required compliance reporting for the PSPF with no significant non-compliances being identified. An extensive capability has also been set up to independently monitor and search electronic records.

I would like to acknowledge the difficulties that the ANAO has encountered in finding relevant documents to support this audit. I note in particular, that some documents and files were only found by the Department after the audit report was finalised. The audit report also makes note of documents that appear to have been created after procurement processes were finalised and in the course of the ANAO Audit. The Department requires all of its officers to make full information available quickly to the ANAO and has no tolerance for misconduct. The matters raised by the ANAO in this audit have now been referred to the Integrity and Professional Standards Branch for formal investigation.

Status of Open Tender Process

As a final note, I wish to advise that, since the finalisation of the audit, the request for tender (DIBP RFT 28/14) and subsequent request for amended tender (DIBP RFAT28/14) detailed in Part 4 were cancelled by the Department on 29 July 2016. The Department is now conducting market testing to determine our next steps. To accommodate this, the Department has extended its contract with the current provider to October 2017.

If you would like further discuss our response to the audit report, please contact the Chief Audit Executive, Mr Stephen Hayward, on 02 6264 1427, or the Assistant Secretary Risk and Assurance, Ms Lisa-Ann Howgego, on 02 6264 2022.

Yours sincerely



Dr Jill Charker
Chief Operating Officer
Deputy Secretary Corporate

19 August 2016

Attachment A: Action Plan

The Department recognises the importance of efficient, effective, economical and ethical and procurement practices and has both short and longer term plans to increase the contracting and procurement capability.

Action	Timeframe	Lead officer(s)
<i>Immediate actions (until end October 2016)</i>		
Immediately enhance processes for approving complex, high-risk procurements through a system of assurance steps, including specific thresholds for high-risk procurements (to be developed in consultation with the CRO) and assistance for delegates making complex procurement decisions. The CFO and Chief Audit Executive will oversee and sign-off that each high-risk procurement has been undertaken appropriately, prior to delegate approval. These enhancements will be embedded in the Procurement Reform Programme.	End September 2016	Chief Finance Officer Chief Audit Executive
Complete health check by internal audit of the process and planning for current, planned procurement around garrison and welfare, health and settlement services.	End September 2016	Chief Audit Executive, Chief Finance Officer
Review conflict of interest processes and declarations for all procurements above a defined risk and value threshold (to be based on contract diagnostics undertaken by the Chief Audit Executive)	By September 2016	Chief Audit Executive General Counsel
Enhance governance arrangements for high risk procurements including mandating the use of steering committees with membership to include the Department's principal assurance areas; CFO, CAE and General Counsel. Under enhanced governance arrangements, steering committees will be tasked with considering issues including risk, probity, contestability, achievement of value for money, compliance and outcome delivery.	By end October 2016	Chief Audit Executive Chief Finance Officer
Develop a simplified and enhanced risk assessment framework for procurements to ensure that high risk procurements are appropriately managed and have the early involvement from risk, probity, contracting and legal experts.	By end October 2016	Chief Risk Officer
Strengthen the policy and guidance on the engagement of independent commercial, probity and contract management advisors in procurements.	By end September 2016	General Counsel Chief Finance Officer

Action	Timeframe	Lead officer(s)
Medium Term Reforms (October 2016 to December 2017)		
<p>Implement the information management strategy to ensure the right people can access the right information at the right time, to support informed, effective decision making. This strategy has a range of initiatives, which include:</p> <ul style="list-style-type: none"> • Implementing robust leadership and governance of information, underpinned by clear policies and standards. • Building information management capability, including tools and procedures that facilitate timely and reliable access to information across multiple systems • Building the capacity for sustainable information management by instilling appropriate disciplines in our people, processes and systems. This includes ensuring that information is created, stored and used in accordance with legislation. 	Progressively to June 2017	First Assistant Secretary Corporate Services
<p>Whole-of-Department Procurement and Contract Management Reform. Fast track the inflight reform program to encompass all procurement and contract management functions across the Department.</p> <p>This work will include improved guidance, education and training as well as longer term system improvements. Capability uplift will be ensured across the Department generally, with particular focus on areas undertaking high risk procurement and contract management through implementation of an enhanced Skills and Competency framework that addresses the prerequisite requirements needed to effectively conduct procurement and manage contracts.</p> <p>Improved contract management will build upon the contract management framework that is being developed in the Detention Services Division. The framework has been developed using the ANAO Better Practice Guide, guidance from the Chartered Institute of Procurement and Supply and other leading best practice guidance.</p>	June 2017	Chief Finance Officer
<p>Increase coverage within the Department's Strategic Assurance Programme for 2016/17</p> <p>The Department's assurance programme for 2016/17 will have a specific focus on procurement and contract management. This will include contract diagnostic internal audit which will assess the appropriateness of the Department's management of its contracts for completeness and validation.</p>	Throughout 2016/17	Chief Audit Executive
<p>Enhance accountability of the Department's procurement and contract management risk through the enterprise risk process.</p> <p>Procurement and contracting has been identified as one of the Department's 11 enterprise risks.</p> <p>Under the risk management framework, Deputy Secretary Corporate (Band 3) will oversee the management of this risk. The level of risk and the need for any further improvements will be discussed quarterly at the Department's risk committee.</p>	Ongoing	Deputy Secretary Corporate

Department of Defence



Australian Government
Department of Defence

Mr Dennis Richardson
Secretary

Air Chief Marshal MD Binskin, AC
Chief of the Defence Force

SEC/OUT/2016/187
CDF/OUT/2016/778


Ms Edel Kairouz
Executive Director
Australian National Audit Office
PO Box 707
Canberra ACT 2601

**AUSTRALIAN NATIONAL AUDIT OFFICE PERFORMANCE AUDIT -
PROCUREMENT AND CONTRACT MANAGEMENT OF GARRISON SUPPORT
AND WELFARE SERVICES AT OFFSHORE PROCESSING CENTRES ON
NAURU AND MANUS ISLAND**

1. Thank you for your correspondence which contained the S19 Proposed Report for the abovementioned subject audit.
2. Defence's formal response to the Proposed Report is at Attachment A.
3. We would like to take this opportunity to formally thank the ANAO for the time and resources they have allocated to the audit. This audit focuses on the Department of Immigration and Border Protection and there are no formal recommendations for Defence.


Dennis Richardson
Secretary

12 August 2016


MD Binskin, AC
Air Chief Marshal
Chief of the Defence Force

9 August 2016

Attachments:

1. Proposed Amendments, Editorials and Comments

PO Box 7900 Canberra BC ACT 2610 Telephone 02 6265 2851 – Facsimile 02 6265 2375

Defending Australia and its National Interests

PROPOSED AMENDMENTS, EDITORIALS AND COMMENTS

PROPOSED REPORT

ANAO PERFORMANCE AUDIT -: PROCUREMENT AND CONTRACT MANAGEMENT OF GARRISON SUPPORT AND WELFARE SERVICES AT OFFSHORE PROCESSING CENTRES IN NAURU AND MANUS ISLAND

Reference	Quote from report with relevant word(s) underlined	Comment or Correction With actions or changes where appropriate, in bold	Group/ Branch
Paragraph 2.23	In considering value for money the department [DIBP] was also required, under the CPRs, to consider Transfield's relevant experience and performance history. ³⁸ A key reason documented by the department for its selection, was that Transfield was on a Department of Defence panel for garrison support services. ³⁹ Defence advised the ANAO that it did not have such a panel arrangement in place at that time. Defence advised that it has no record of a request from DIBP seeking its views in August or September 2012 regarding the performance of its garrison support suppliers. Available DIBP records indicate that it had regard to Defence panel rates but it is not clear how this was possible if no Defence panel existed.	Defence has not identified any documented advice to DIBP regarding Transfield contracts with Defence in the period identified (August or September 2012). In the period identified (August or September 2012), Transfield did hold separate Garrison Services Support Contracts with Defence for the Western Australia, South Australia, Northern New South Wales, Tasmania and Victoria regions and a Comprehensive Maintenance Services contract for South Australia. These were specific term contracts, not panel arrangements.	E&IG

Footnote 38	Finance, CPRs, 2012, paragraph 4.5.p.15	N/A	E&IG
Footnote 39	Transfield advised DIBP that labour rate costs were drawn from Transfield's existing Department of Defence Garrison Support Centre contracts for both Western Australia and Victoria.	Defence has no comment.	E&IG
Table 2.2	[Text redacted] Transfield was approached to provide services on Nauru as they are on the Defence panel for Garrison Support services. The costing agreed to with Transfield is based on Defence panel rates, with a percentage increase applied to take into account of the location in which the services are supplied ... [Text redacted]	Defence has not identified any documented advice to DIBP regarding Transfield contracts with Defence. In the period identified (August or September 2012), Transfield did hold separate Garrison Services Support Contracts with Defence for the Western Australia, South Australia, Northern New South Wales, Tasmania and Victoria regions and a Comprehensive Maintenance Services contract for South Australia. These were specific term contracts, not panel arrangements.	E&IG
Paragraph 3.16	On 28 November 2013, the CPU [DIBP's Central Procurement Unit] sought Finance advice on conducting a limited tender relying on	Defence has no comment.	E&IG
paragraph 10.3(b) of the CPRs	relating to urgent and unforeseen circumstances. ⁵⁶ The department advised Finance that: <i>DIBP has contracts operating in the offshore space, these contracts involve issues with the contract providers and the level of services we are receiving, there is areas of underperformance amongst other issues. We</i>	The Defence Procurement and Contracting Branch has not identified a "scrutiny and recommendation report (from the Joint Agency Taskforce, which included Defence) or any documented input to or comment on a "scrutiny and recommendation report [from the Joint Agency Taskforce, which included Defence).	E&IG

	<i>have had a scrutiny and recommendation report [from the Joint Agency Taskforce, which included Defence] recommending that we not take up the extension option available to us due to the underperformance by the service providers and the risk to us knowing this and not ending the contracted services. ...</i>		
Footnote 56	[ANAO discussion relating to CPRs].	N/A	E&IG
Paragraph 3.17	The department has not been able to produce the relevant report to the ANAO to verify this statement, and [text redacted].	No Defence comment.	E&IG
Paragraph 4.6	The department [DIBP] established the Offshore Immigration Services Procurement steering committee (the committee) to provide strategic direction and advice to the delegate for the procurement project, ⁷⁶	No Defence comment.	E&IG
Footnote 76	The committee was initially chaired by the First Assistant Secretary (F AS), Detention Services Procurement Task Force, and included: stakeholders from DIBP business areas, the Department of Defence, Department of Finance, Department of Foreign Affairs and Trade, and host Governments. [Text redacted]	No Defence comment.	E&IG

ANAO comment

Paragraph and footnote numbers have changed in finalising the report. Paragraph 2.23 is now paragraph 2.27, footnote 38 is now footnote 55, footnote 39 is now footnote 56, Table 2.2 is unchanged, paragraph 3.16 is now 3.23, footnote 56 is now footnote 78, paragraph 3.17 is now 3.24, paragraph 4.6 is unchanged and footnote 76 is now footnote 111.

Broadspectrum (Australia) Pty Ltd



Level 10, 111 Pacific Highway
North Sydney
Locked Bag 917
North Sydney NSW 2059
Telephone: +61 2 9464 1000
Facsimile: +61 2 9464 1111

25 August 2016

Dr. Tom Ioannou
Group Executive Director
Performance Audit
Australian National Audit Office

BY EMAIL: tom.ioannou@anao.gov.au

Dear Dr Ioannou,

Australian National Audit Office (ANAO) proposed audit report on Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services

We refer to your email of 20 June 2016 and subsequent correspondence with your office and thank you for providing us with a copy of the ANAO's proposed audit report on Offshore Processing Centres in Nauru and Papua New Guinea (**Draft Report**), issued under section 19 of the Auditor-General Act 1997.

Attached to this letter, are the following documents prepared by Broadspectrum (Australia) Pty Ltd (**Broadspectrum**) in response to the Draft Report:

1. **Annexure 1**, Letter of Reply, being Broadspectrum's formal response to the Draft Report, which we understand will be reproduced in full as an appendix to the final report; and
2. **Annexure 2**, Summary Response, being a short summary of the length requested which we also understand will be published in full at the end of the final report summary.

We have also separately provided the ANAO with a list of Editorial Matters on 17 and 24 August 2016, which we have also requested that the ANAO consider incorporating, where appropriate in the text of the final report.

Broadspectrum welcomes the opportunity to respond to this proposed Draft Report as a means of assisting the continual improvement of procurement practices of the Commonwealth and it hopes that the responses provided will assist the ANAO in finalising its report.



While we have done our utmost to respond in a comprehensive and detailed manner, our ability to do so has been constrained in circumstances where the Draft Report that has been provided to us is heavily redacted and incomplete, and where we do not have visibility of documents and information relied on by the ANAO. Accordingly, there may be aspects of our response to the Draft Report where the ANAO considers it would be assisted by further detail or clarification. Where that is the case, please let us know and we would be happy to assist further.

If you have any questions or require any further information please contact our Chief Executive of Logistics, Consulting and Welfare, Derek Osborn on (03) 8823 7535 or derek.osborn@broadpectrum.com or myself.

We look forward to receiving the final report prior to its tabling in Parliament.

Yours faithfully,

A handwritten signature in black ink, appearing to read "G. Hunt", is written over a horizontal line.

Graeme Hunt
Managing Director and Chief Executive Officer

CC Edel Kairouz

Email: Edel.Kairouz@anao.gov.au

Annexure 1: TO BE PUBLISHED AS PART OF THE FINAL ANAO REPORT

Response of Broadspectrum (Australia) Pty Ltd

Summary

Broadspectrum welcomes the opportunity to respond to the ANAO's proposed audit report on Offshore Processing Centres in Nauru and Papua New Guinea (**Draft Report**) and to assist the ANAO in this important review. Broadspectrum delivers a broad range of services that are essential to clients across multiple sectors. Our approach integrates a focus on optimising performance, integrity and output of our clients' businesses and assets to deliver real business outcomes safely and responsibly, with a diverse, collaborative and caring workforce.

We deliver safe, efficient and sustainable services, supported by robust systems and processes and a commitment to proactively managing our environmental, social and governance responsibilities. To this end, good corporate citizenship is an essential part of our business strategy.

We operate in the Defence, Property, Social, Infrastructure, Resources and Industrial sectors, and provide Logistics, Facilities Management, Consulting, Construction, Care, Welfare, Operations, Maintenance, Well Servicing, and Business Support services.

We have a strong track record of delivering long-term, complex contracts for a range of clients including the Commonwealth and state governments.

As the ANAO is aware, the procurement by the Commonwealth of services with respect to the Offshore Processing Centres in Nauru and Papua New Guinea involved multiple phases between 2012 and 2015 that evolved and became increasingly complex in response to the dynamic and changing conditions affecting the OPCs and the associated expectations of contractors. It included multiple ongoing changes in scope, the introduction of new service requirements and supply chains, transitioning in and transitioning out other service providers, multiple new locations for service delivery and the introduction of resettlement services and facilities. All of these factors are considered relevant to a balanced assessment of the quality of the offering with respect to services provided at the OPCs.

While we have done our utmost to respond in a comprehensive and detailed manner to the ANAO's Draft Report, our ability to do so has been constrained in circumstances where the Draft Report that has been provided to us is heavily redacted, incomplete and where we do not have visibility of the documents and information relied on by the ANAO. Accordingly, there might be aspects of our response to the Draft Report where the ANAO considers it would be assisted by further detail or clarification. Where that is the case, please let us know and we would be happy to assist further.

Some of the Key matters which Broadspectrum requests be considered by the ANAO in finalising its proposed audit report are as follows:

1. Consideration of non-financial factors

The proposed report appears to us to focus heavily on the financial cost of submissions made by service providers over the various tenders and it is not evident as to whether the report has taken into account other relevant factors.. In particular, it was not apparent from the Draft Report that the ANAO has considered non-financial factors such as the complex and evolving nature of the service requirements, the quality of the proposed service delivery, the experience and performance

history of Broadspectrum (both as a provider of Garrison Services and as a long standing provider of services to Government) and (as discussed further below) the characteristics of the cohort that would ultimately access the services provided.

Broadspectrum was (and remains) conscious that OPC service providers would be operating in an environment that was dynamic and that consistent and high quality service provision would therefore require that the service provider consider a delivery model that was responsive and flexible at both an organisational and workforce level. For these reasons, the OPC contracts are unique and it is challenging to measure value through the application of traditional pricing mechanisms.

Broadspectrum’s approach to formulating proposals and pricing is to consider the evaluation criteria, weigh up all relevant factors that are important to consider in proposing a fair price that covers the reasonable cost of providing the particular services in the environment we operate and on the terms required by our clients, as well as taking into account the risks we are being asked to assume. Broadspectrum’s approach also includes providing as much certainty as possible about the likely cost of services to our clients in circumstance of the procurement.. In the instances where Broadspectrum has been given the opportunity to extend into new service lines, or to take over from existing service providers, Broadspectrum has always sought to ensure that it identified and implemented any efficiencies that could be derived from having multiple services lines delivered by the same provider and identified opportunities for innovation or enhancement to historical service delivery.

2. References to cost and price and comparisons between amounts

The proposed report makes a number of references to prices and amounts that we are having difficulty reconciling with our own records and information. For example, the following amounts:

Para	Page	Extract of proposed report	Broadspectrum’s comments
4 & 1.5	3 & 13	In October 2015, Transfield became the sole provider of all garrison support and welfare services in Nauru and on Manus Island, and in February 2016 these arrangements were further extended through to 28 February 2017. The contracts for garrison support and welfare services are set out in Table 1.1 on page 14. The total combined contract value as at the end of March 2016, as reported on AusTender, was \$3045 million.	It is not apparent from the Draft Report how each of the amounts comprising \$3045 million was calculated.
3.2	37	The selection of Transfield (to deliver a consolidated contract) attracted considerable media and parliamentary attention, focusing on: <ul style="list-style-type: none"> the use of limited tender procurement and the exclusion of G4S from the tender process; the value of the contract (\$2.1 billion) as reported on AusTender; reported contract savings of \$77 million; and recommendations made in the National Commission of Audit. 	It is not apparent from the Draft Report how the amount of \$2.1 billion was calculated. Transfield announced a contract value of \$1.2B to the market in Mar 2014.

We respectfully suggest that the ANAO provide more detail in the final report of the calculations on which it has relied upon to derive these figures. In particular, it should be clarified precisely what portion of various ‘whole of contract’ figures the ANAO believes were received by Broadspectrum.

We further suggest that where comparisons are made in the final report between prices offered by competing service providers, that the report note any material differences between the service provider’s proposals that would affect a “like for like” assessment, including any relevant assumptions, qualifications or differences in scope or value. This is essential to ensure that Broadspectrum’s offering and pricing is fairly assessed in a context where the evolution of the procurement process between 2012 and 2015 involved multiple fundamental changes in scope, introduction of new service lines and supply chains, transitioning in and transitioning out other service providers, multiple new locations for service delivery and the introduction of resettlement services and facilities.

3. DIBP’s RFT 28/14 and Broadspectrum’s submissions and negotiations

References are made in the proposed report to the tender process conducted by the Department following the submissions made by Transfield in and post April 2015, pursuant to RFT 28/14.

Transfield’s submission in response to the Department’s RFT 28/14 was made and received in confidence and (as we understand it) remains to be determined. We respectfully suggest that in these circumstances, it is necessary and appropriate that confidentiality be maintained with respect to both Transfield’s submission to the Department and the negotiations between the Department and Transfield with respect to RFT 28/14.

Noting the above, should the ANAO nonetheless publish the proposed report to include such matters, we note that the negotiations were complex and lengthy and factored numerous changes in scope and service delivery and many elements of Broadspectrum’s original offer were substantially changed. As the negotiation process progressed (as is typical in the finalisation of contracts for long term and complex service delivery) both Broadspectrum and the Department determined at various stages that they would make concessions and accept compromises that represented departures from their opening ‘offer’ but which were determined to be appropriate given the manner in which the negotiations had evolved.

ANAO comment

Paragraph and page numbers have changed in finalising the report. Paragraph 4, paragraph 1.15 and paragraph 3.2 are unchanged. Page numbers have changed.



20 Brindabella Circuit
Brindabella Business Park
Canberra Airport ACT 2609

PO Box 7396
Canberra Business Centre ACT 2610
Australia

ABN: 51 194 660 183
Telephone: +61 2 6248 1111
Facsimile: +61 2 6248 1122
www.kpmg.com.au

Dr Tom Ioannou
Australian National Audit Office
Group Executive Director
Performance Audit

Our ref KPMG Response to ANAO Report
on Procurement for Offshore
Processing

18 August 2016

Dear Dr Ioannou

KPMG's Letter of Reply and summary response to the KPMG extract of the ANAO's Proposed Audit Report on Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services

Thank you for the opportunity to provide a Letter of Reply and summary response to selected extracts of the redacted ANAO's proposed audit report on *Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services* that was provided to KPMG on Thursday 21 July 2016.

Prior to providing specific comments on the ANAO review, I would like to provide an overview of KPMG's role advising the Department on the activities covered by the scope of the ANAO review.

Background on KPMG's engagements with the Department

KPMG did not provide financial and commercial advisory services in respect of establishing the offshore processing centres in 2012 (as covered in section 2 of the ANAO review).

KPMG was engaged by the Department in respect of the following two engagements, which are the subject of the scope of the ANAO's review.

Engagement 1: Negotiation support to the Department for the consolidation of contracts in Nauru and Manus Island (as discussed in section 3 of the ANAO proposed audit review)

KPMG was appointed in December 2013 to provide financial and business advisory services, including negotiation support in respect of the Department's negotiations with Transfield Services (Australia) Pty Limited (Transfield) to consolidate the contracts in Nauru and Manus Island. KPMG's role in providing services to the Department concluded in March 2014 post execution of the contract extension between the Department and Transfield.

KPMG's engagement did not commence until after the Department had determined that it would engage in a limited tender process with Transfield.

KPMG, an Australian partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.

Liability limited by a scheme approved under Professional Standards Legislation.



Engagement 2: Financial and commercial advice in regards to the onshore and offshore procurement processes (as discussed in section 4 of the ANAO proposed audit review)

KPMG was appointed on 20 August 2014 to provide financial, commercial, negotiation and project support in respect of the Offshore Detention Services procurement process. This engagement also covered negotiation support in respect of the finalisation of the onshore detention service contracts as well as advice in regards to the procurement of Health Services, both of which are outside the scope of the ANAO review.

KPMG's role during the Garrison and Welfare Services procurement included the provision of financial, commercial, negotiation and project support services for the following stages of the procurement:

- RFT preparation;
- RFT release;
- Evaluation; and
- Negotiation.

The Department was responsible for certain key elements of the RFT, such as the preparation of the Contract and the Statement of Requirements and the evaluation of the legal and technical elements of the RFT responses.

Specific comments on the extract provided to KPMG

Based on our review of the extract provided to KPMG, I would like to provide comments on the following matters:

- The use of benchmark models
- KPMG's declarations to the Department

Each of the above issues are discussed in turn in the following sections.

The use of benchmark models

The benchmark models developed for the offshore procurement processes were developed in a manner similar to the approach used to develop a "Public Sector Comparator (PSC)". The use of a PSC is a key pillar in demonstrating quantitative Value for Money (VFM) on large, complex Public Private Partnership (PPP) procurements. In our view, the procurement of Garrison and Welfare services shares many similarities to a PPP procurement process – both involve the procurement of services via a long term, high value contract that involves a complex risk allocation.

As per Infrastructure Australia's National PPP guidelines, "*the purpose of the PSC is to provide governments with a quantitative measure of the value for money it can expect from accepting a private sector Proposal to deliver the output specification compared to public sector delivery*"¹ and "*the PSC is the key management tool in the quantitative assessment of value for money*"

¹ Refer section 2.2 of Volume 4 to the National PPP Guidelines



during the tender process and the evaluation and comparison of RFP Responses. The RFP Responses will be assessed against the PSC to determine whether they offer value for money in respect of quantitative analysis.² While the guidance notes the 'inherent limitations' of a PSC, it also notes that "a complete value for money assessment requires consideration of qualitative factors along with the quantitative assessment."³

With the above background, we provide the following specific comments on extracts of the ANAO's proposed audit report.

	Reference	ANAO relevant extract	KPMG response
1	Paragraph 18, first bullet point Paragraph 3.42	Para 18 - Overall the benchmark model was adjusted above historical costs...to accommodate a number of service enhancements. Para 3.42 -...the benchmark price was increased above the historical cost base in order to ensure a like-for-like comparison....	The benchmark model was adjusted to account for changes to the Department's service requirements and contractual approach (including risk allocation). As commercial and financial advisor, KPMG facilitated a workshop with the Department to adjust the historical costs to reflect changes from the existing contractual requirements to the Department's new requirements as articulated in the Request for Tender (RFT) documentation including the draft contract, statement of requirements, pricing mechanism and performance framework. The purpose of the process was to adjust the historical costs for changes to the Department's requirements, such that the benchmark model reflected a like-for-like comparison against the proposals that would be received. Such an adjustment approach is necessary to ensure a like-for-like comparison between the responses and the RFP specifications / contract. Failure to undertake such an adjustment may lead to misleading comparisons if there are significant changes in scope and / or changes to other elements, such as the Department's terms and conditions, including overall risk profile.

² Refer section 3.1.1 of Volume 4 to the National PPP Guidelines

³ Refer section 3.1.2 of Volume 4 to the National PPP Guidelines

	Reference	ANAO relevant extract	KPMG response
2	Paragraph 18, second bullet point	Para 18 - The Department determined 'value for money' and claimed savings (against the benchmarks) on a combined basis.	<p>While separate benchmarks were developed for Nauru and Manus Island, this approach was predominantly undertaken to assist in the negotiation process.</p> <p>As the limited tender process involved the consolidation of contracts in Nauru and on Manus Island into a single contract, we believe it was appropriate to combine both benchmarks to determine an overall value for money position. Further, aggregating both benchmark models avoided the possibility of complications arising from the allocation of overhead and management costs between Manus Island and Nauru.</p>
3	Paragraph 21, first bullet point, Paragraph 24 and Paragraph 4.46	<p>Para 21 - Use of benchmarking to determine overall value for money ... is incompatible with the CPRs which require each eligible tenderer's financial and non-financial benefits to be compared on a like for like basis with other eligible tenders.</p> <p>Para 24 - The Department ... set out to determine value for money by comparing the negotiated price with a benchmark.</p> <p>Para 4.46 - The Department only compared Transfield's price with the benchmark rather</p>	<p>As discussed in the introduction to this section, the use of a benchmark model approach shares many similarities to the use of a PSC on PPP projects. As noted in the PPP guidelines, the PSC is 'the key management tool in the quantitative assessment of value for money during the tender process and the evaluation and comparison of RFP Responses'.</p> <p>The open tender process did involve a comparison of each eligible tenderer's financial and non-financial benefits on a like-for-like basis with other eligible tenders. This analysis was a pre-requisite to selecting the preferred tenderer and was conducted in accordance with the evaluation approach outlined in the RFT.</p> <p>The benchmark model complemented (rather than replaced) this comparative assessment and was used to assist in negotiations with the preferred tenderer. At the end of negotiations, the benchmark model was also used to compare the cost of the preferred tenderer delivering the services under the new contract relative to the costs of delivering the services</p>

Reference	ANAO relevant extract	KPMG response
	<p>than the price in other tender bids.</p>	<p>under the existing contract (represented by the benchmark model).</p> <p>In determining whether Transfield's final negotiated offer represented overall value for money, the Department presented the original evaluation outcomes, including the original evaluation pricing. As stated in the first bullet point of the Negotiated Outcomes Presentation "the purpose of this presentation is to update the Steering Committee on the negotiation outcomes with the Preferred Tenderer for Garrison and Welfare Services, with reference back to the evaluated outcome." The subsequent slides presented the information from the evaluation process, such as the evaluation scores, pricing and the number of unquantified pricing issues / risks identified during evaluation. The remainder of the presentation explained the movement from Transfield's evaluated price to its final negotiated price.</p> <p>In addition, to the comparative assessment of tenderers that was undertaken during the evaluation phase, the benchmark model allowed the Department to undertake a:</p> <ul style="list-style-type: none"> • comparative analysis of the preferred tenderer's price against historical costs (adjusted where relevant to ensure a like-for-like comparison); and • whole of life cost analysis (as the benchmark model included the costs over the life of the contract). <p>As noted in section 2.21 of the proposed ANAO report "determining Value for Money requires a comparative analysis of the relevant costs and benefits throughout the whole procurement cycle (whole of life costing) and a process commensurate with the scale and scope of the procurement."</p>



Reference	ANAO relevant extract	KPMG response
		While we recognise that the use of a benchmark model may not be necessary for all Commonwealth procurements (particularly low value procurements), given the scale and complexity of this procurement we believe the use of a benchmark model, similar to that used in other complex procurements was appropriate. As such, we do not believe that the use of a benchmark model is incompatible with the CPRs.
4 Paragraph 22	Para 22 - There were significant unquantified pricing risks..., which the Department did not clarify prior to selecting a preferred tenderer and forming an opinion on value for money.... This approach was not consistent with the CPRs.	Section 4.5 of the Commonwealth Procurement Rules ⁴ requires that an "official must consider the relevant financial and non-financial costs and benefits of each submission". During the evaluation process, the Department identified a number of risks associated with all submissions. Where possible, the Department attempted to quantify these risks. In some instances it was not possible to quantify the value of those risks as a financial cost. However, the number and severity ranking of the unquantified risks were considered by the Evaluation Committee in determining the selection of the preferred tenderer and when undertaking its value for money deliberations during the evaluation process.
5 Figures 3.3, 3.4 and 3.5	Derived historical cost base	We note that the ANAO has calculated a 'derived historical cost base' and has labelled the relevant figures as such. We also note that the source of these figures is the "ANAO Analysis of the KPMG Price Evaluation Report". KPMG's pricing report did not calculate a derived historical cost base. We do not have

⁴ <https://www.finance.gov.au/sites/default/files/2014%20Commonwealth%20Procurement%20Rules.pdf>

	Reference	ANAO relevant extract	KPMG response
			<p>any visibility as to how the ANAO calculated its derived historical cost base.</p> <p>We also note that comparing a derived historical cost base may not represent the actual cost of providing the services as it would not take into account changes to the scope of the services during the contract term. As noted in point 1, our report was based on the use of a benchmark model approach, which was adjusted to allow for like-for-like comparison between the responses and the RFP specifications / contract.</p>

Conflict of Interest

KPMG maintains that it acted openly and transparently at all times, and provided timely disclosure, with regard to its relationships with potential tenderers and the management of potential conflicts of interest in connection with the Garrison and Welfare Services procurement processes. In particular, KPMG notes that it had brought its role as Transfield's external auditor and provider of advisory services to the Department's attention:

- in an e-mail to the Department on 22 January 2014 which confirmed that "we (KPMG) are the external auditor of Transfield, and we also provide limited advisory services to the Transfield Group". The e-mail also outlined that KPMG does not consider the provision of such services to Transfield raises any conflict of interest issues and provided further confirmation that "no team member who is providing services to you in relation to the Project will be involved in the Transfield audit or advisory engagements"; and
- in an e-mail to the Department on 24 January 2014 which clarified that, in addition to the external audit role (a statutory role) for the Transfield group of companies, "KPMG has (in the preceding 24 month period) also provided certain tax services, IT Advisory services, financial due diligence services and accounting advisory services". The e-mail again reiterates that we do not consider these services to raise any conflict of interest issues and sets out KPMG's conflict management and ethical divider procedures.

Following the e-mail communications in January 2014, as stated in paragraph 3.59, the Department noted in its approvals that no conflict of interest existed.

There were also numerous discussions between KPMG and Department representatives, between the date of KPMG's appointment and the receipt of tender submissions, in which



KPMG's relationship with Transfield was discussed. KPMG also made reference to the fact that it is the auditor of Transfield in its financial viability assessment report, a draft of which was provided to the Department on 10 June 2015.

KPMG's formal letter in July 2015 was provided in a timely manner following the Department's request to formalise prior communication between KPMG and the Department. The letter was by no means the first time KPMG had brought its relationship with Transfield to the Department's attention and was not therefore the first declaration of a potential conflict of interest with Transfield.

KPMG also notes the statement at paragraph 4.25 of the ANAO Report, which states as follows:

"... and it is surprising to us that this formal notice has been issued at least 10 months from the date of KPMG's engagement"

With regard to this statement, whilst KPMG was engaged by the Department in August 2014, the tender process itself did not commence until January 2015 and the tenderer parties were not known until the receipt of tender submissions in April 2015.

Summary Response

KPMG was engaged by the Department to provide:

- Negotiation support for the consolidation of contracts in Nauru and Manus Island in December 2013; and
- Financial, commercial and negotiation advice and project support in regards to the onshore and offshore procurement processes in August 2014.

KPMG notes that a benchmark approach, or its equivalent, is commonly used for the procurement of other long term, high value contracts that involves a complex risk allocation, including complex Public Private Partnership (PPP) procurements. KPMG maintains that the use of a Benchmark model for the procurement of Garrison and Welfare Services provides additional complementary analysis to the comparative value for money assessment.

KPMG also maintains that it acted openly and transparently at all times, and provided timely disclosure, with regard to its relationships with potential tenderers and the management of potential conflicts of interest in connection with the Garrison and Welfare Services procurement processes. In particular, KPMG notes that its letter issued in July 2015 was not the first time KPMG had brought its role as Transfield's external auditor and provider of advisory services to the Department's attention. KPMG had advised the Department of its relationship with Transfield on numerous occasions prior to this.



*Australian National Audit Office
KPMG's Letter of Reply and summary response to the
KPMG extract of the ANAO's Proposed Audit Report
on Offshore Processing Centres in Nauru and Papua
New Guinea: Procurement of Garrison Support and
Welfare Services
18 August 2016*

We welcome the opportunity to further discuss any of the matters contained in this letter. We would also welcome the opportunity to provide further comments on any updated ANAO report if changes are made to the ANAO report as a consequence of this letter of reply.

Should you have any queries on any matter contained within this letter, please contact me at gbrooke1@kpmg.com.au.

Yours faithfully

Graham Brooke
Partner

ANAO comments

Paragraph numbers have changed in finalising the report. Paragraph 18 is unchanged, paragraph 3.42 is now 3.51, paragraphs 21 is now 22, paragraph 24 is now 25, paragraph 4.46 is now 4.44, paragraph 2.21 is now 2.25, paragraph 22 is now 23, paragraph 3.59 is now 3.72, paragraph 4.25 is unchanged,

Benchmarking

A competitive open tender process involves the comparison of all eligible bids to determine value for money. The CPRs also provide that request documentation must include a complete description of evaluation criteria to be considered in assessing submissions. The benchmarking approach was not disclosed to the market in the department's request for tender.

The ANAO observes in chapter 4 of this audit report that in the open tender reviewed:

- comparison against a benchmark was not identified as an evaluation criterion in the Request for Tender and the CPRs require all evaluation criteria to be advised to potential suppliers (see paragraphs 4.15 and 4.16);
- the benchmark used was the cost of services being provided to the department at the time, which was the result of a non-competitive limited tender; and

- only the preferred tenderer was compared against the benchmark. This occurred after the department significantly changed the scope of requirements. The department should have compared the preferred tenderer's bid against other tenderers' bids for the same scope of services and used that to determine value for money in the circumstances.

Derived cost

In relation to the comment in point 5 relating to the 'derived' cost, this expression appears in the KPMG spreadsheets reviewed by the ANAO. These spreadsheets were used to support KPMG's Pricing Evaluation Report.

Conflict of interest disclosures

The timing of KPMG advice regarding conflict of interest is addressed in paragraphs 4.23 to 4.26 of this audit report:

- KPMG was engaged as commercial adviser in August 2014 and at that time advised the department that there were no conflicts of interest that would affect its appointment or that were anticipated to arise in the course of the contract; and
- on 3 July 2015, KPMG again wrote to the department advising of potential conflict of interest issues with individual tenderers—some three months after tenders closed and over ten months after KPMG was engaged.
- The ANAO has not been provided with documentation indicating that there were numerous discussions between KPMG and departmental representatives, between the date of KPMG's appointment and the receipt of tender submissions, in which KPMG's relationship with Transfield was discussed.

KPMG notes that it advised DIBP on 10 June 2015 that it was the auditor of Transfield, in the context of submitting its financial viability assessment report on the tender proposals received as part of the department's open tender process.

- Disclosures relating to conflict of interest must be timely in order to enable entities to assess risk and consider appropriate mitigation strategies. The onus was on KPMG to make declarations relating to conflict of interest before performing that work.

The Salvation Army



Salvos Legal Limited
T/AS Salvos Legal
ABN: 14 147 213 214

Our ref: LG/NAC/150867

16 August 2016

All correspondence to:
PO Box A288
SYDNEY SOUTH NSW 1235

Dr Tom Ioannou
Group Executive Director
Performance Audit
Australian National Audit Office

Senior Associate
Nameeta Chandra O2 8202 1549
Email: nameeta.chandra@salvoslegal.com.au

Partner
Luke Geary O2 8202 1517
Email: luke.geary@salvoslegal.com.au

By Email: Tom.ioannou@anao.gov.au

Dear Dr Ioannou,

EXTRACT FROM ANAO PROPOSED AUDIT REPORT ON OFFSHORE PROCESSING CENTRES IN NAURU AND PAPUA NEW GUINEA: PROCUREMENT OF GARRISON SUPPORT AND WELFARE SERVICES.

We act as solicitors for The Salvation Army (TSA).

We refer to your email dated 20 July 2016 with respect to the proposed audit report on Offshore Processing Centres (also referred to as Regional Processing Centres) located at Nauru and Papua New Guinea.

Thank you for providing to TSA an extract of the proposed audit report.

From the extract provided, we understand that the Australian National Audit Office (the 'Office') may not publish the names of persons involved, but for the names of members of Parliament. Accordingly, we have adopted this practice in our response.

Further, in our response a reference to the Department means the Department of Immigration and Border Protection and its earlier emanations.

For your consideration we have provided the following comments (adopting the subheadings in the extract):

References to the 2012 process to establish the centres

Reference to timeline

With respect to the timeline set out in the extract, we refer to the following additional dates, which you may wish to include or make reference to in your final report:

1. On 17 August 2012, TSA's Territorial Director of Social Mission and Resources wrote to the Honourable Chris Bowen MP.
2. On 23 August 2012, TSA's National Secretary and Territorial Director of Social Mission and Resources attended a meeting with Minister Bowen.

Level 2, 151 Castlereagh St, Sydney NSW 2000
PO Box A288, Sydney South NSW 1235
T (02) 8202 1555 F (02) 8202 1590

Salvos Legal
salvoslegal.com.au



3. On 1 September 2012, TSA's Territorial Director of Social Mission and Resources met with Department representatives with respect to the Regional Processing Centre.
4. On 4 September 2012, a letter of intent was received by TSA from the Department (already included in your timeline).
5. On 7 September 2012, a meeting was held with the Department, representatives from the Nauruan government and the Service Providers.
6. On 10 September 2012, TSA's first group of staff arrived at the Nauru Regional Processing Centre.
7. On 14 September 2012, the first group of asylum seekers were transferred to Nauru (already included in your timeline).
8. On 3 October 2012, TSA and the Commonwealth of Australia (represented by Department) (the 'Commonwealth') entered into a Heads of Agreement pursuant to which TSA agreed to provide welfare and support services to asylum seekers (referred to as transferees) housed in the Regional Processing Centre located on Nauru in return for payment to TSA for the performance of those services.
9. On 15 October 2012 and 18 October 2012, Salvation Army Officers and staff arrived at the Manus Island Regional Processing Centre, respectively.
10. On 21 November 2012, the first group of asylum seekers were transferred to the Manus Island Regional Processing Centre (already included in your timeline)
11. On 1 February 2013, TSA and the Commonwealth (represented by the Department) entered into a contract pursuant to which TSA agreed to continue to provide welfare and support services, amongst other things, to the transferees in the Regional Processing Centres located on Nauru and Manus Island and the Commonwealth agreed to pay TSA for the provision of those services.

Reference to Table 2.3 The Salvation Army – value for money assessment

We seek a copy of this document; as such we would be grateful if you could advise of the providence of this document so we can make the relevant enquiries with the Department.

References to 2013-2014 contract consolidated process

Paragraph 3.10 – Other key meetings which occurred at the time, and related correspondence, included:

In addition to what is contained in the extract, we note the following:

1. On 16 November 2013, TSA's Humanitarian Mission Service's Chief Executive Officer emailed the Assistant Secretary responsible for Offshore Detention Services, seeking information in relation to the contract extension. TSA's Humanitarian Mission Service's Chief Executive Officer advised the Assistant Secretary that "[f]urther to the meeting with DIBP and TSA personnel in Canberra on 14 November 2013 and earlier correspondence, you will be aware of the difficulties that TSA is having in engaging and retaining staff as a result of not yet having a decision on whether our contract with the Commonwealth will be extended."
2. On 12 December 2013, the Department informed TSA, that it intended to pursue a consolidated framework for the future provision of services at the Regional Processing Centres, and notified TSA that it wished to extend the Contract for a period of two months from 1 February 2014 to 28 March 2014.
3. On 12 December 2013, the Department's Deputy Secretary informed TSA's Humanitarian Mission Service's Chief Executive Officer that the decision with respect to consolidating service providers was not based on TSA's performance.

LG/NAC/150867

Additional Information

We noted the following additional information which you may wish to include or make reference to in your final report:

1. On 24 December 2013, TSA's Humanitarian Mission Service's Chief Executive Officer provided notice to the Department that TSA did not agree to the extension of the Contract, however, that TSA remained committed to working with the Department and the new provider to complete transition arrangements as smoothly and effectively as possible.
2. On 21 February 2014, TSA concluded its services at the Regional Processing Centres.

If you have any questions or require further information please do not hesitate to contact Ms Nameeta Chandra on 02 8202 1549 or by email at nameeta.chandra@salvoslegal.com.au.

Yours faithfully



LUKE GEARY
PARTNER

ANAO comment regarding points 1 and 2

Paragraph numbers have changed in finalising the report. Paragraph 3.10 is now 3.11.

The department was not able to provide the ANAO with documents relating to how the initial approach to The Salvation Army occurred.

Mr Tony Shepherd AO

From: Anthony Shepherd

Sent: Saturday, 30 July 2016 8:01 PM

To: Edel Kairouz

Subject: Fwd: Extract ANAO Proposed Audit Report on Offshore Processing Centres in Nauru and Papua New Guinea: Procurement of Garrison Support and Welfare Services

Dear Edel, thank you for the opportunity to comment on the draft introduction.

By way of introduction my experience as a private citizen appointed to government bodies both Commonwealth and State has not always been a pleasant one given that ones motives and integrity are frequently publicly challenged without due consideration of the facts or indeed without any proper opportunity to explain or respond.

Before accepting the appointment to the National Commission of Audit I notified the Commonwealth in writing of any potential conflicts of interest including my role with Transfield Services.

I retired from Transfield Services at the AGM on 23 October 2013 having foreshadowed my departure when reappointed at the AGM in 2010.

I was conscious of the need to avoid any hint of conflict of interest and accordingly asked my financial advisor Fitzpatricks to sell all the remaining shares I held in Transfield Services. Fitzpatricks has confirmed the sale in a letter a copy of which I have forwarded separately.

The NCOA was charged with reviewing some \$408 billion in Commonwealth expenditure over three months and concentrated on the main offenders. However, as the ANAO draft report says we were concerned about the growing cost of onshore and offshore processing and recommended steps to contain and reduce these costs. Like many of the Recommendations in the NCOA Report I am not aware of whether there was any follow through by the Commonwealth.

In terms of the wording of the draft I am not sure of the relevance of my prior appointment at Transfield Services but at least it should be made clear that:

1. I advised the Commonwealth in writing of the potential conflict.
2. I not only retired from Transfield Services but also sold any shareholding I had in the company.
3. The NCOA Report could not in anyway be construed as being beneficial to Transfield Services or any other provider.

Regards

Tony Shepherd