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Mr Gary Swain
Secretary
Department of Treasury and Finance
GPO Box 147
HOBART TAS 7000

Dear Mr Swain

SUBMISSION TO GOVERNMENT BUSINESS REVIEW

I congratulate the Government, with Treasury's valuable input, on taking the initiative to review the Government business portfolio as set out in the *Government Business Governance Reform, Draft Plan* of November 2024.

I am writing from my perspective as a former manager in Treasury's Shareholder Policy and Markets Branch, as well over a decade in the private sector where my work includes corporate finance, transactions and economic advice for a wide range of clients across the private and public sectors. Please note that comments in this submission are personal opinions and may not reflect the views of the businesses that I work for, any of my clients or any of their counterparties.

As a general statement, governments of any political persuasion do not make good shareholders as commercial operations and investments are inevitably managed through a prism of political risk, while there is also a reluctance to report bad news for the same reason. Also, government businesses rarely make adequate commercial returns for the capital that the public invests in these businesses and lack the investment discipline imposed by capital markets. These issues are evident across many jurisdictions.

For these reasons, a review of the entire Government business portfolio is critical, including a principles-based approach for ongoing public ownership, assessments of the appropriate ownership model and a view to identifying businesses that should be divested or restructured. While some businesses have a role in delivering core public services or facilitating economic growth, several businesses could perform this function within a fully commercial mandate outside the current constraints of public ownership.

A key example is TasNetworks, which operates under a well-established regulatory model that encourages efficient capital and operating expenses, transparent pricing structures, and clear boundaries for non-regulated businesses. This business has significant value in its regulated and unregulated assets that could be realised through a competitive divestment process, in which there is a pool of domestic and global capital available for stable, long-term returns from infrastructure assets.

Similarly, Aurora Energy operates in a competitive market with low barriers to entry. The services it provides are offered by competing retailers and, for major commercial and industrial customers seeking products that support renewable transactions, it often lacks an ability to present innovative approaches to risk management.

A robust strategic analysis framework should be applied to this review, which could include the principles such as whether:

- there is a genuine case for public ownership;
- customer outcomes (including service levels and pricing) and efficiency (including both operating costs and capital investment) can be improved under different ownership models;
- the businesses are delivering sufficient financial returns, measured on standard metrics such as the Return on Invested Capital (ROIC) relative to the Weighted Average Cost of Capital (WACC); and
- the potential divestment valuation exceeds the retention valuation.

As suggested, Government businesses must be subject to a continuous disclosure regime for financial performance.

The proposed "assurance review" mechanism should apply to all government businesses. However, as these reviews appear to be more focused on non-financial performance (eg infrastructure projects, organisational capability, workplace culture, risk management, WHS performance), complementary external reviews of the financial performance and a valuation of each business should be undertaken applying standard corporate finance techniques (not accounting-based metrics) in a similar manner to equity research reports for listed companies.

The external assurance reviews and financial performance reports should be undertaken on a regular cycle, perhaps biennial for the former and annually for the latter. They should be delivered to Parliament rather than Shareholding Ministers, given the latter does not guarantee any transparency to the ultimate owners of these businesses.

Parliament's Government Business Scrutiny Committee hearings have significant barriers to being an effective part of the governance framework, such as asymmetric access to information and political filtering. The hearings would be improved considerably if the experts engaged for the assurance reviews and financial performance reports were able to appear independently in the hearings.

I am encouraged by the suggestion that transparent mechanisms for funding and reporting on community service obligations will be implemented. However, on a note of caution, this has been a common policy position for governments for over three decades — since the Hilmer reforms commenced National Competition Policy in 1993 — yet this principle has never been consistently implemented in Tasmania or other jurisdictions.

A broader and more robust principle should be implemented that requires all annual reports and statements of corporate intent to report on their ROIC and benchmark WACC, along with specifically identifying and justifying the cause of any shortfalls (ie lower revenue, higher costs or non-commercial investment decisions). Also, if the risk profile of Government business increases, the benchmark WACC must also increase, which should be transparent.

The reporting framework must include transparency on decisions that are taken with a view to facilitating economic growth, and the resulting commercial impacts, otherwise this policy driver is likely to become an excuse for retaining underperforming businesses without a clear ongoing assessment of whether the community value of the facilitation role exceeds the financial cost to the community through lower returns to Government.

The draft plan has a strong emphasis on capital expenditure, which is appropriate. The Tasmanian Government businesses have a long and sorry history of failed infrastructure projects — including IT systems, notably Aurora's billing system — but typically without the accountability and transparency that would occur in the private sector, particularly with listed companies. While mandating the gateway review process is a minimum standard, a broader capital investment framework should be implemented including a principle that any investment that is material to a business, from both a scale and risk perspective, should be subject to strict gateway processes and project management approaches. The mandate must also apply to IT system projects.

Project management and gateway reviews must be reported to Shareholding Ministers rather than confined within the relevant businesses. However, a more innovative approach could be a whole-of-portfolio approach, such as project management office function, to facilitate regular and robust oversight to Ministers and their agencies on all major projects. This function would be able to interrogate the businesses' internal PMOs and reach their own conclusions for reporting to Ministers.

There is also a tendency in many Government businesses to deliver projects internally. Few Government businesses have the management depth, project management experience, and/or resources to deliver major projects. This appears to be one of the factors behind TT-Line's failure in the Devonport berth redevelopment fiasco. Government businesses should be considering alternative delivery approaches — including funding models that keep the capital investment and associated risks off the State's balance sheet — for significant infrastructure projects, such as alliances, early contractor involvement, public-private partnerships, and tolling (or virtual tolling) arrangements for generation infrastructure. A specific requirement to consider alternative delivery and funding models — perhaps even a stated preference for external delivery and funding — and Ministerial advice on the businesses' decision-making should be incorporated in the capital investment framework.

Finally, from my past experience and engagement with other agencies, the State Service and particularly Treasury may need to strengthen their internal commercial capability, including:

- strategic analysis;
- financial analysis, particularly focusing on corporate finance techniques;
- infrastructure delivery models; and
- gateway and project management reviews.

Please let me know on [redacted] if any issues in this submission can be clarified or I can provide any further assistance.

Yours sincerely

Phil Bayley
Principal
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