The Parliament of the Commonwealth of Australia

$ CALL US AGAIN $

REVIEW OF THE AUDITOR-GENERAL'S EFFICIENCY AUDIT REPORT ON THE CONTROL OVER MANPOWER AND PROPERTY BY THE OVERSEAS TELECOMMUNICATIONS COMMISSION (AUSTRALIA)

Report by the House of Representatives
Standing Committee on Expenditure
November 1986

Australian Government Publishing Service Canberra 1986

ISBN 0 644 05613 4

Printed in Australia by C. J. THOMPSON, Commonwealth Government Printer, Canberra

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Secretary:	Mrs S.M. Harlow (until 1.9.86) Mr M.E Aldons (since 8.9.86)

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*The nominee of the Chairman of the Joint Committee of Public Accounts who, in accordance with clause (2) of the resolution of appointment, is a member of the Expenditure Committee.

Foreword

This report is a review of an efficiency audit of the Auditor-General's Office on the Control over Manpower and Property by the Overseas Telecommunications Commission (Australia). The Committee thanks the organisations that made submissions to the inquiry as well as the witnesses who gave evidence at the hearings in Canberra.

The audit of OTC was one of the first efficiency audits of a public authority business enterprise undertaken by the Auditor-General's Office. The Committee was disappointed with the time taken to conduct the audit and by its limited scope. After all, the effectiveness of an audit depends to some extent on the findings being current. The narrow scope of this audit led to a concentration on areas of OTC which, while important, were of declining significance.

During the inquiry it became clear to the Committee that OTC's ability to fulfill its obligations would be improved by a more predictable government policy towards dividend payments. Such a policy would improve planning and in particular capital investment.

The Committee was also attracted to OTC's suggestion that it be given the opportunity to extend its services into consulting and to engage in joint ventures within Australia. Such a move would reflect confidence in OTC's already developed expertise.

As Chairman of the Sub-committee, I would like to thank my fellow Committee members for their time and effort spent on this inquiry. My thanks also go to the Committee Secretariat who worked on this report: Mrs Sue Harlow, Secretary of the Committee until 1 September 1986, Mr Malcolm Aldons, Secretary from 8 September 1986, Ms Catherine Stobo, Ms Alison Stanford and Ms Heather Chapman.

David Hawker, MP
Sub-committee Chairman

Contents

Recommendations

Recommendation 1. The Public Service Board expedite its current reviews of technical officer classifications so that a broader review of technical officer training that will take into account the length of the training period can be instigated.

Recommendation 2. The Government review the basis for determining the dividend that OTC pays to the Commonwealth and in so doing,take into account the requirements for capital reinvestment.

Recommendation 3. OTC's legislation should be amended to allow it to expand its activities in the field of telecommunications, particularly where they may lead to import replacement and generation of manufacturing activity.

Chapter 1

Introduction

1.1 This is the 7th review of an Auditor-General's Efficiency Audit (EA) Report that has been carried out by the House of Representatives Standing Committee on Expenditure. It follows publication in September 1984 of the Report of the Auditor-General upon audits, examinations and inspections under the Audit and other Acts. Included therein is the Report of the Efficiency Audit of the Control over Manpower and Property by the Overseas Telecommunications Commission (Australia).[1]

1.2 The Expenditure Committee and the Joint Committee of Public Accounts share the parliamentary task of examining efficiency audit reports and a process of consultation between the two committee chairmen decides which committee examines a particular efficiency audit report. On 28 February 1985 it was proposed and confirmed that the Expenditure Committee would review the EA report on OTC's control over manpower and property.

1.3 Members of the Committee undertook inspections of OTC's international radio operating room in Martin Place and Paddington facilities in April 1985. A Sub-committee was formed on 9 April 1986 to conduct the review.Evidence was taken at two public hearings in Canberra on 17 April and 18 September 1986 and in subsequent correspondence with some of the witnesses. Part of the second hearing was conducted *in camera* to allow the

[1] *Report of the Auditor-General*, September 1984, Parliamentary Paper No. 170/1984, A.G.P.S., Canberra 1984

Committee to consider evidence relating to OTC's strategic business plans which were tabled as a confidential exhibit at the first hearing.

1.4 The objectives of the Committee in carrying out this review were the same as those examined in earlier reviews of EA reports, that is to:

- examine the response of the Commission; and
- assess the substantive content of the audit exercise and the quality of the EA report.

1.5 The assessment of the quality of an EA report is really something that should come out in the wash - the aftermath of the evidence-taking stage of the inquiry. The examination of the responses of the audited organisation can be grouped into 3 broad categories:

- examination of Audit recommendations the auditee agrees with

  - in which case the Committee would be concerned with implementation;

- examination of Audit recommendations the auditee disagrees with

  - in which case the Committee could become involved in deciding which party has the stronger case, and

- development by the Committee of suggestions/recommendations made in the EA report.

Chapter 2

Examination of OTC's Response and Evaluation of the Audit Exercise

The EA Report

2.1 The audit of OTC was one of the first efficiency audits of a public authority business enterprise undertaken by the Audit Office. Audit first conducted a preliminary examination of the Commission to identify suitable areas to audit. A number of possible areas were considered and a decision finally was made to concentrate on the systems for resource utilisation where Audit believed it could provide useful comment. [1]

2.2 The EA report examined 5 matters, namely:

- *procedures used by OTC to control the use of technical manpower and property resources;*
- *technical manpower (estimating staffing needs)* and *technical training* (trainee intake and length of training time);
- review of property resources and examination of lease/buy option for office accommodation;

[1] Evidence, p.7

- areas of declining activity and areas incurring losses; and
- substantial losses on telegraphic services and losses on international and coast radio services.

2.3 The recommendations are not numbered in the EA report, however the Committee identified 16 on which separate action was required. The Audit recommendations, OTC's response and brief comments on each are set out in Appendix II.

2.4 In relation to technical manpower, Audit examined OTC's methods of estimating technical staff requirements and how they are utilised, particularly the switching operators, radio operators, engineers and technical officers. The report notes the low priority given to automation of operations in the labour intensive telegraph and radio operations areas and the poor degree of mobility of staff in these areas. The 7 recommendations made cover systems for estimating staff requirements, selective workload reviews and for increased automation. The recommendations are listed on page 250 of the Audit report.

2.5 In considering technical training by OTC, Audit identified two areas of concern. The first related to the fluctuations in trainee intake which ranged from nil in 1977 to a peak of 292 in 1981 and back to nil again in 1983. Audit considered that a steady intake would result in a better matching of resources to numbers. However the EA report does not examine the reasons for the fluctuations or query whether there was a need to continue taking on trainees in the short term. The second area concerned the length of training time which Audit suggested could be reduced from 4 years to 3 without diminishing standards. OTC had been considering this issue and had commissioned an independent study on the subject. Although initially in favour of such a move, OTC did not press ahead with it because of a lack of enthusiasm from other organisations involved. Audit recommended that OTC should follow up the question of shorter training periods with the Public Service Board and other organisations.

2.6 As indicated above, Radio Operations is a labour intensive area of OTC's activities and one which had been reporting losses for a number of years. The loss services Audit covered were the telegraphic service where there had been substantial loss, and international and coast radio services. On the latter, Audit said OTC should give greater attention to the technology available and reconsider automation of message format and other opportunities for improving efficiency. In respect of international and coast radio services, Audit suggested that rationalisation and an improved management information system would reduce losses.The five recommendations made centre on these aspects and the agreement with the Department of Transport for recovery of costs in relation to the provision of the Safety of Life at Sea (SOLAS) service.

2.7 The final area of OTC's activities that Audit examined was the utilisation of property resources. Audit considered that OTC needed to regularly review its property needs to ensure that unused properties are disposed of. It also recommended that OTC should keep under review future opportunities for buying or building lower cost Head Office accommodation and develop a long term plan to obtain cheaper accommodation. The three recommendations reflect these concerns.

OTC's Response

2.8 Action has been taken on all of the recommendations: 14 have been implemented; one has been partially implemented; and some action was taken on one, but further action rests with another agency.

2.9 The recommendations not fully implemented are recommendations numbers 4 and 8 (as identified by the Committee). The Committee considers that the reasons given by OTC for not fully implementing the 4th recommendation, ie. to develop key workload indicators, are satisfactory.

2.10 The 8th recommendation concerns reducing the training period for technical officers. This is a complex question involving other authorities, eg. Telecom, ABC, Australia Post, the Departments of Aviation, Defence, Transport, Science and Housing and Construction. It would be difficult therefore, for OTC to take unilateral action to reduce training time. In evidence the Public Service Board indicated that generally there is little support for reducing the training time and that there are other priorities deserving of attention. However, the question will be examined in the context of a fundamental review of technical officers following the completion of a series of related reviews. [2] These related reviews are due to be completed between December 1986 and June 1987 and the fundamental review is scheduled for completion by the end of 1987. The Committee considers that action should proceed more quickly as significant cost savings could result if training time is reduced by one year, and recommends that:

Recommendation 1 – The Public Service Board expedite its current reviews of technical officer classifications so that a broader review of technical officer training that will take into account the length of the training period can be instigated.

The Quality of the EA report

2.11 Audit has selected a small yet discrete part of OTC's operations for inquiry and report. The Committee is satisfied that the inquiry has achieved worthwhile results in that the majority of the Audit suggestions for change have been accepted and implemented by the Commission. It does appear that the Audit was a catalyst that has resulted in OTC disposing of 16 surplus properties the total value of which amounted to $1.3 million, and in taking action to dispose of a further 11 properties.[3]

2.12 The Commission has said that most of the problems identified by Audit were known to Management and were being remedied. [4] This is a standard response of organisations subject to external review. It is very difficult to be certain about causal connections between what an external review identifies and what action is taken or the speed and direction of that action. Obviously other factors come into play. One of these factors would certainly be the length of time Audit took to complete the report. OTC was advised by the Auditor-General on 29 September 1982 that an audit was to be undertaken and the report was tabled in Parliament on 4 September 1984. As OTC is an organisation that must be responsive to

[2] Evidence, p.50

[3] OTC submission, 11 March 1986, p.6

[4] Evidence, p.68

rapid technological change it would seem essential for an audit report to be prompt and timely so that it does not run the risk of being irrelevant. Nevertheless, the Committee points out that efficiency auditing is part of the public accountability mechanism and the identification of problems by Audit, together with suggestions for change, require the audited organisation to explain to the Parliament the action it has taken or is proposing to take. In its report, Parliament and Public Expenditure, the Expenditure Committee appointed in the 31st Parliament said that efficiency auditing by the Auditor-General "is a function which should be encouraged if for no other reason than that other reviews conducted by the administration remain 'internal working documents' and so are not available to the Parliament".

2.13 *There are two disappointing aspects of this EA report and both* can be traced to the same source - the lack of skills about markets and market behaviour. First, in examining the substantial losses of the labour intensive telegraphic service Audit identified the wrong problem. The losses of the international telegram service should have been examined by means of a market analysis. This would have shown that the market share was falling because of consumer preference for other services such as facsimile and ISD, and would have then suggested a market survey to test the long term viability of the telegraphic service.

2.14 The second is the narrow scope of the audit. Given the length of time the audit took, this a particularly disappointing feature. OTC is a large enterprise which earns more than $400 million a year, and, to a large extent, is protected from competition in the marketplace by a legislative monopoly. In these circumstances, an examination of OTC's specific services, with an emphasis on the efficiency of resource use, as well as a wider examination *of the Commission's financial structure,* could have been a worthwhile endeavour even if the results of such an industry analysis were favourable to OTC. Any lack of skills in such analysis could have been supplemented by the use of consultants.

Chapter 3

Other Matters

Investing in the Future

3.1 Having gained some insights into the field of overseas telecommunications during the course of this inquiry the Committee would like to make some observations about OTC having regard to the debate on levels of investment funds that has emerged following the publication of the report to the Department of Communications by OECD economist, Henry Ergas, entitled "Telecommunications and the Australian Economy".

3.2 OTC is a profitable organisation funded from internal sources. Unlike most other Commonwealth statutory authorities, it pays all Commonwealth taxes and duties including corporate income tax. However, whilst its financial perfomance is strong, it states that:

> its financial structure continues to demonstrate a relatively low level of equity capital invested in the business, supported by a growing proportion of non-current liabilities and an increased level of debt. [1]

This is of particular concern to OTC as telecommunications is a high-growth, capital-intensive business with major projects extending into the next decade. It claims further that:

[1] OTC Annual Report 1986, p.28

> A large part of the problem has been caused by the distribution of a very high proportion of after-tax profits as dividends. [2]

Under the *Overseas Telecommunications Act 1946*, dividend payments are determined by the Minister for Communications with the concurrence of the Minister for Finance, having considered the advice of the Commission. [3] It is OTC's view that:

> the Commonwealth's present method of determining a dividend target is unsatisfactory. Decisions are, in practice, made by the Government on a year-to-year basis and the long term needs of the business become subordinate to the Commonwealth's budgetary demands...In 1983, the Government agreed to set a dividend target for the five-year period to 1987-88 of 10% of Capital and Reserves in order that the Commission could plan its capital expenditure programme and utilise a combination of debt and equity to finance large submarine cable projects. The 1985/86 target was altered to 12.5% of Capital and Reserves. [4]

The 1986/87 target has been set at 15%. [5]

3.3 One of the major issues raised in the Ergas report concerns the need for higher levels of investment funds for OTC and Telecom. Mr Ergas noted that investment finance available to the telecommunications authorities since the early 1980s has not allowed them to meet reasonable levels of network development. To recover from past shortfalls, and to meet an increasing demand for telecommunications services both from households and businesses, a real increase of some 10-15% on present annual investment levels is required immediately, followed by growth in real terms of 4-8% annually. [6]

3.4 The Committee noted that there is considerable pressure on OTC to meet the demands of Government in providing a substantial dividend in

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[2] ibid, p.28

[3] ibid p.28

[4] ibid, p.29

[5] Evidence, p. 81

[6] *Telecommunications and the Australian Economy*, Report to the Department of Communications, A.G.P.S., Canberra 1986 p.49

addition to paying company tax and the demands of the industry through capital investment. Rather than determining the dividend on the basis of a percentage of Capital and Reserves, OTC has suggested that a more equitable basis would be an agreed percentage of after-tax profits and suggests 40% as appropriate. [7] Growth could be sustained without increasing new debt finance. Costs could be kept down. OTC has informed the Committee that its prices are determined on a cost-plus basis. These costs include payments to Telecom Australia for the use of terminals, payments to overseas countries, payments for satellite services, hedging costs and interest payments, and, company tax and dividends. Because dividend payments to the Commonwealth form part of OTC's cost structure, the effect of this will be to increase OTC's prices unless there are compensating reductions in other costs. The Committee recommends that:

Recommendation 2 – The Government review the basis for determining the dividend that OTC pays to the Commonwealth and in so doing, take into account the requirements for capital re-investment.

3.5 As old services become obsolete, eg. telegrams, and some newer services become cheaper and technologically easier to operate so that they come into personal use, eg. facsimile services, OTC needs to diversify its activities into areas such as consultancies, design of equipment and joint ventures. At present, however, its legislation authorises it only to provide international communications. OTC has a submission before Government seeking a widening of its powers to allow it to diversify its activities beyond it current charter. As OTC has the capacity to undertake new forms of activity, and in the light of the obvious advantages such as reducing dependence on overseas technology and generation of manufacturing activity the Committee recommends that:

Recommendation 3 – OTC's legislation should be amended to allow it to expand its activities in the field of telecommunications particularly where they may lead to import replacement and generation of manufacturing activity.

[7] OTC Annual Report 1986, p.29

3.6 In making this recommendation the Committee observes that it would be self-defeating for Government to so amend the legislation but at the same time to stifle opportunities for OTC to diversify its activities by requiring increased payments of dividends without new injections of capital.

John Mountford MP
Chairman
13 November 1986

Appendix I

List of Witnesses

Mr Bruce MacDonald, Director of Audit,
Australian Audit Office, Canberra,
Australian Capital Territory

Mr Valerio Paul Manera, Director of Audit,
Australian Audit Office, Canberra,
Australian Capital Territory

Mr Michael John Jacobs, Regional Manager,
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Mr Frank Louis Stephen Martinelli,
Regional Program Manager (Victoria)
Pay and Classification, Public Service Board,
Canberra, Australian Capital Territory

Mr Ronald Gregory Flood, Executive Manager,
Telephone Services,
Overseas Telecommunications Commission
32 Martin Place,
Sydney, New South Wales

Mr Robert James Cruikshank, Director,
Corporate Affairs,
Overseas Telecommunications Commission,
32 Martin Place,
Sydney, New South Wales

Appendix II

Audit Recommendations, OTC's Response, Committee's Comments

Recommendation 1 :-	Complete business plans for all services and integrate manpower planning processes with plans. (Audit Report p.250)
Response :-	Business plans completed October 1985. Each plan embodies human resource requirements over 3 year period which are integrated into OTC's overall manpower plans. (OTC submission, p.3)
Comments :-	Recommendation has been implemented.

Recommendation 2 :-	Implement new financial management system (Audit Report p. 250)
Response :-	The Financial Management Information System (FMIS) was fully operative by December 1984. (OTC submission, p.3)
Comments :-	Recommendation has been implemented. Work began on development of the FMIS well before the commencement of the efficiency audit.

Recommendation 3 :-	Incorporate non-financial management information systems including staffing and traffic reports into FMIS (Audit Report p.250)
Response :-	Some non-financial data has been incorporated and other systems are progressively being aligned with the categories in the FMIS. (OTC submission, p.4)
Comments :-	Recommendation has been implemented.

Recommendation 4 :-	Develop key workload indicators to assist in control over staff levels and staff costs. (Audit Report, p.250)
Response :-	Use of workload indicators does not lend itself to most areas of a high technology industry. Nor are they appropriate in some essential watch-keeping areas where staffing is not related to traffic volumes. Research activities also are unsuited to the application of workload indicators. In general terms, control of labour usage is through financial budgets. However,workload indicators are used where they are meaningful, such as in the labour intensive telegram service. (OTC's submission, p.4)
Comment :-	Recommendation has only been partially implemented.

Recommendation 5 :-	O & M staff to undertake selective workload reviews based on analysis of workload indicators. (Audit Report p.250)
Response :-	Responsiblity for budget performance including manpower costs is with Branch Heads. In efforts to reduce and contain costs, they call on O & M staff to conduct workload reviews using, where appropriate,workload indicators. (OTC submission, p. 4)
Comment :-	Recommendation has been implemented.

Recommendation 6 :-	In the labour intensive telegraph service automation of message format conversion should be reconsidered along with other opportunities for improvements in efficiency. (Audit Report p.250)
Response :-	Some automation of message format has taken place. Further automation is dependent on new operational arrangements with Telecom in late 1986. Staff reductions will take place as well as cost containments with increased automation. (OTC submission, p.40

Comment :- Recommendation has been accepted and is being implemented progressively.

Recommendation 7 :- Rationalise further operating rooms in the telegraph service. (Audit Report p.250)

Response :- As indicated above, staff reductions will take place progressively. A major rationalisation package for the area is being negotiated with staff and the Department of Employment and Industrial Relations. (OTC submission, p.4)

Comment :- Recommendation has been accepted and is being implemented progressively.

Recommendation 8 :- Opportunities for shortened training periods for technical officers should be taken up in conjunction with other government authorities involved and the Public Service Board. (Audit Report p.253)

Response :- OTC put the proposal to the other authorities involved and all were doubtful that the period could be reduced. The PSB did not respond directly to OTC's proposal, but it non-supportive views were known from its response to a similar proposal in relation to the Department of Aviation. (OTC submission, p.5)

Comment :- Recommendation accepted but no action resulted. In evidence, the PSB that they intended to incorporate this question into a fundamental review of technical officer instructors which will not get under way until other related reviews in train at present, are completed. (Evidence, pp50-52)

Recommendation 9 :-	Radio services to be rationalised to eliminate continuing losses and improve efficiency. (Audit Report p.263)
Response :-	Rationalisation is continuing. New transmitters have been installed at one location and $4.5 million will be spent on rationalisation and modernisation of two other locations. Staff reductions will ensue as a result. (OTC submission, p.5)
Comment :-	Recommendation is being implemented.

Recommendation 10 :-	Develop long term plans for radio operations including a business plan. (Audit Report p.263)
Response :-	As noted previously, business plans have been developed for all services including radio operations. (OTC submission, p.5)
Comment :-	Recommendation has been implemented.

Recommendation 11 :-	Provide information on the cost of individual services and unconnected and unused capacity. (Audit Report p. 263)
Response :-	Detailed information is provided through the FMIS. (OTC submission, p. 5)
Comment :-	Recommendation has been implemented.

Recommendation 12 :-	Determine full costs of non-mandatory services such as the airline service and review requirement for continuation. (Audit Report p.263)
Response :-	The cost of the airline service has been reviewed but the revenue impact is minor. The service has been modernised and the tariff increased to ensure that it is profitable. There are no other services of this type. (OTC submission, p.5)

Comment :- Recommendation has been implemented.

Recommendation 13 :- Complete review of costing systems to enable information and recovery of full SOLAS costs from the Department of Transport. (Audit Reportp.263)

Response :- The systems have been reviewed and comprehensive information is available from the FMIS. External consultants were commissioned to report on appropriate financial arrangements for the future. (OTC submission, p.5)

Comment :- Recommendation has been implemented. At the second hearing on 18 September 1986 OTC witnesses advised that an agreement has been negotiated with the Department of Transport that is satisfactory to both parties. (Evidence, pp 103-104)

Recommendation 14 :- Regularly review the economics of utilisation of property resources and report results to management. (Audit Report p. 278)

Response :- Procedures have been improved with the availability of relevant information on a cost centre and service basis from the FMIS and the computerised land values register and assets register. Quarterly reports are made to the Board. Sixteen properties have been disposed since April 1983, with action proceeding on a further eleven properties. (OTC submission, pp 5-6)

Comment :- Recommendation has been implemented.

Recommendation 15 :- The Commission should keep under review future opportunities, including the options of purchasing or building, for lower cost head office accommodation. (Audit Report p.268)

Response :- Since the audit was completed OTC has contracted to purchase an office building under construction on the fringe of the Central Business District of Sydney. Substantial savings will result compared to leasing of accommodation. Occupancy is anticipated for early 1987. (OTC submission, p.6)

Comment :- Recommendation has been implemented

Recommendation 16 :- OTC should develop a long term plan to secure less costly accommodation. (Audit Report, p.268)

Response :- As noted above, action has been taken to obtain less costly accommodation for Head Office. All other property holdings are reviewed to determine whether less costly options are available. (OTC submission, p.6)

Comment :- Recommendation has been implemented.
