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Audit Report No.53 2000–2001
Performance Audit

Commonwealth Management of Leased Office Property

Australian National Audit Office

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Canberra ACT
27 June 2001

Dear Madam President
Dear Mr Speaker

The Australian National Audit Office has undertaken an across agency performance audit in accordance with the authority contained in the *Auditor-General Act 1997*. I present this report of this audit, and the accompanying brochure, to the Parliament. The report is titled *Commonwealth Management of Leased Office Property*.

Following its tabling in Parliament, the report will be placed on the Australian National Audit Office's Homepage—
<http://www.anao.gov.au>

Yours sincerely



P. J. Barrett
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. The ANAO assists the Auditor-General to carry out his duties under the *Auditor-General Act 1997* to undertake performance audits and financial statement audits of Commonwealth public sector bodies and to provide independent reports and advice for the Parliament, the Government and the community. The aim is to improve Commonwealth public sector administration and accountability.

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Abbreviations/Glossary

AEM	Australian Estate Management.
AGS	Australian Government Solicitor.
ANAO	Australian National Audit Office.
APG	Australian Property Group.
Business continuity plan	A plan to deal with a break in business continuity which prescribes the steps the agency should take to recover lost business functions and resources.
City/ metropolitan	Includes state and territory capital cities, surrounding metropolitan areas and surrounding suburban areas.
Commonwealth National Lease	A pro forma lease prepared by the Australian Government Solicitor as guidance for agencies entering into leases with private sector landlords.
Commonwealth sale/lease-back lease	Where an office property, previously owned by the Commonwealth Government, has been sold to the market and new lease agreements with pre-existing Commonwealth Government tenants (lease-back) have been negotiated as part of the sale.
Commonwealth Tenant's Lease	A lease developed by the Commonwealth Property Committee and used during the Commonwealth's property sales program.
Country/ regional	Includes regional cities, smaller country cities and smaller country towns.
CPI	Consumer Price Index.
CTL DAS	Commonwealth Tenants' Lease. Department of Administrative Services.
DFAT	Department of Foreign Affairs and Trade.
DPG	Domestic Property Group.
Finance	Department of Finance and Administration.
FMA Act	<i>Financial Management and Accountability Act 1997.</i>
FMA Agency	Agency governed by the FMA Act.
FMA Regulations	Financial Management and Accountability Regulations.

Grade A accommodation	High quality space including: good views/outlook; quality lobby finish; on-site undercover parking; quality access to/from an attractive street setting; high quality presentation and maintenance; high quality technical services.
Grade B accommodation	Good quality space with a reasonable standard of finish and maintenance. Tenant car parking facilities should be available and basic standards of technical services.
Grade C accommodation	Older style office space of lower quality finish and older style technical services.
Grade D accommodation	Poor quality space with minimal technical services. Typically, these buildings do not have central air-conditioning.
Gross rent lease	Cost of rent for a property includes an allowance for outgoing/property operating expenses (eg. operation of air-conditioning, common area light and power, and lifts during normal office hours).
Health	Department of Health and Aged Care.
Leased office property/ leased office accommodation	Predominantly office/administrative style accommodation leased from a property owner other than the Commonwealth Government, includes shop front style property leased for 'customer service' related activities, but excludes retail space.
Net rent lease	Cost of rent for a property excludes an allowance for outgoing/property operating expenses (ie. the tenant is responsible for all outgoing/property operating expenses).
Outgoings/ property operating expenses	Expenses associated with the operation and maintenance of leased office property, including electricity, gas, cleaning, maintenance and security costs, but excluding rent (including car parking); fitout/refit and any other capital improvement costs (eg. installation of supplementary air conditioning systems).
PMS	Property Management System.

Premium grade accommodation	A landmark office building located in major Central Business District office markets which is a pace setter in establishing rents and includes ample natural lighting; good views/outlook; prestige lobby finish; on-site undercover parking; quality access to/from an attractive street setting; premium presentation and maintenance; state of the art technical services.
Property management activities	Generally includes leasing, valuations, legal/contractual advice, financial management and reporting, PMS management, contract administration, maintenance management, and/or project management.
Ratchet clause	In relation to a provision of a lease for determining rent variations in such a way that rent might decrease, ratchet clause means a provision in that lease that has the effect of preventing, or giving a person the power to prevent, that decrease.
Refit costs	The cost associated with the subsequent fitout of office accommodation during the lease or at the lease renewal stage.
SKM	Sinclair Knight Merz.
Sqm	Square metres.
Sqm/person	Square metres of leased office space per full-time equivalent employee.
The Guidelines	Commonwealth Procurement Guidelines.
The Principles	Commonwealth Property Principles.
Vacant leased office property	The total area of leased office property not occupied at the time of this audit (note: excludes vacant space that has been sub-let to a third party).

Summary and Recommendations

Audit Summary

Introduction

1. The Commonwealth Government is a significant occupier of leased office accommodation nationally.
2. Each Commonwealth agency, irrespective of its size or function, is responsible for managing its leased office property. Agencies vary in the numbers of leases managed, for example from one lease in a single location, to 471 leases Australia-wide by one agency.
3. Agencies have not always been required to manage their own leased office property portfolios. In the 1980s, the former Department of Administrative Services managed all property appropriations and controlled all leased space on behalf of Commonwealth agencies. This role has changed over the years leading to a complete devolvement of property management to agencies. As a result, individuals agencies are required to address the often complex issues associated with leased office property portfolios, including strategic planning, lease negotiations, and contract management.
4. Prior to the sale of the Australian Property Group (APG) by the Department of Finance and Administration (Finance) in 1997, many agencies used APG as their outsourced property management service provider. Some agencies still use the private sector organisation that purchased APG to provide these services.
5. After labour costs, expenditure on property is often the next largest single item of agency expenditure. Against this background, the ANAO conducted a performance audit, including an agency survey and case studies, to determine how adequately agencies are managing their leased office property portfolios.

Audit objectives

6. The objectives of the audit were to:
 - develop a benchmark of the Financial Management and Accountability (FMA) Act agencies' property management performance for current and future comparisons; and
 - form an opinion as to whether the FMA agencies reviewed in the case studies:
 - manage leased office property in accordance with the requirements of the FMA Act and other official guidance; and
 - manage their leased office property effectively.

Audit scope

7. This performance audit is the first property management audit that the ANAO has conducted since the FMA Act came into effect in 1997, with the associated devolution of responsibility to agency heads.

8. The audit included coverage of office accommodation currently leased in Australia from the private sector. This office accommodation was housing the functions and activities of clerical, technical or professional staff, including conference and meeting rooms and ministerial suites but excluding basements, car parks, theatrettes, and cafeterias.

Audit methodology

9. The audit gathered data from a survey of 59 FMA agencies and three case studies. Sinclair Knight Merz provided property management expertise for both the survey and case study agencies.

10. The survey collected data on agencies' leased property portfolios for the year ended, or as at, 30 June 2000. By 14 July 2000, 44 of the 59 agencies had completed and returned their survey, representing a 75 per cent response rate. The survey obtained data on 1505 leases for office properties occupied by the Commonwealth agencies covered.

11. The agencies responding to the survey were grouped into three categories with their responses being analysed accordingly. The grouping of agencies into these categories was intended to recognise differences in function and size across the various agencies, thus allowing for a more coherent analysis. The categories¹ used were:

- departments (13 agencies);
- other large agencies (nine agencies); and
- smaller agencies (22 agencies).

12. Case studies were undertaken in the following agencies to supplement the data obtained from the survey:

- the Department of Foreign Affairs and Trade (DFAT);
- the Department of Health and Aged Care (Health); and
- Centrelink.

¹ Appendix 2 sets out the agencies in each of these categories.

13. These three agencies rented accommodation in office buildings previously owned by the Commonwealth. A sample of 16 of the leases relating to these buildings was reviewed. The buildings in this sample had been sold by the Commonwealth for a total of \$621 million.²

14. The survey data provides information about FMA agencies' leased office property holdings at 30 June 2000. It has also provided baseline data against which future agency performance can be gauged. In addition, individual agencies can use this data to compare their leased office accommodation arrangements with those of similar entities. Such comparisons completed by agencies have the potential to improve property management in Commonwealth agencies.

Conclusions

15. The Commonwealth is estimated to occupy up to 10 per cent of available leased office space in metropolitan Australia, and may well be the single largest occupier of leased office accommodation nationally. In the 1999–2000 financial year, the cost to the Commonwealth was in excess of \$485 million in rent and outgoings. The latter include cleaning and maintenance costs, and management of property portfolios.

16. The amount of space leased is generally above the benchmark range of 15 to 25 square metres per person.³ This indicates that some responding FMA agencies may be renting space in excess of their needs and/or utilising existing space inefficiently. The effects of this can be higher than necessary payments of rent and outgoings. The ANAO has estimated that, during the 1999–2000 financial year, the responding agencies paid approximately \$95.5 million in rent and outgoings for the above-benchmark space held.⁴

² Appendix 3 identifies the leases in the sample.

³ For the purposes of this analysis, a density benchmark range of 15 to 25 square metres of leased office space per full-time equivalent employee has been adopted. The ANAO set a lower and upper range which took into consideration benchmarks such as those contained in a report prepared by the Government Real Estate Group titled *National Office Accommodation Benchmarking—Government Real Estate Groups Working in Partnership*, October 1999. The nominated upper range allows for those agencies that have a diverse geographical network of office locations and a larger proportion of regional offices that tend to achieve less efficient density ratios (that is, a greater number of smaller offices leads to reduced opportunities for economies of scale).

⁴ The above benchmark rent and outgoings expenditure calculations were based on use of the upper boundary of the benchmark range, ie, 25 square metres per person, less the cost of any vacant space identified by respondent agencies.

17. As previously indicated, the ANAO reviewed the effectiveness of the property management of three agencies. On a scale of property management effectiveness, the audit found that:

- Centrelink is managing its leased office property portfolio most effectively; and no specific recommendations have been made to Centrelink in this report;
- Health is generally managing aspects of its leased office property portfolio effectively. Implementation of recommendations in this report should serve to enhance the effectiveness of its property management; and
- DFAT has a more limited approach to managing its leased office property. DFAT should consider implementing the recommendations in this report to assist in achieving more effective management of its leased office property portfolio.

Key Findings

Strategic Property and Business Continuity Planning

18. The level of strategic property planning should have regard to the importance property plays in the delivery of agency outputs and outcomes as well as the materiality of property expenditures. It is the underlying principles of strategic property management that are important to these property plans, not their size or sophistication. The essential feature is that agencies recognise the contribution property makes to the achievement of their objectives and give due consideration to this factor in their strategic planning.

19. Based on the results of the survey, the ANAO found that there was limited strategic property planning by agencies as only 24 per cent of respondent agencies had strategic property plans in place at 30 June 2000. This result may have the effect of inhibiting the focus on longer-term needs of agencies and may result in operating inefficiencies. Potentially, these could be considerable given that, on average, departments lease 27⁵ properties and other large agencies lease 25⁶ properties.

20. Business continuity plans were more commonly found among respondent agencies than were strategic property plans, with almost half of all respondent agencies having business continuity plans in place at 30 June 2000. These plans generally contained clauses relating to building access and alternative accommodation that would be available in the event of an emergency.

21. Based on the case studies, DFAT did not have a strategic property plan in place at 30 June 2000, although steps had been taken at the time of the audit to progress a draft strategic property plan. DFAT also had not implemented the recommendations of its business continuity plan. As the continued effective operation of DFAT's main office, the RG Casey Building, can be crucial to international relations, DFAT's preparation and implementation of a business continuity plan is considered critical.

⁵ This average does not include the Finance portfolio of 310 properties.

⁶ This average does not include the Centrelink portfolio of 471 properties.

22. Health has a strategic property plan for each state/territory office. These are not integrated into a comprehensive strategic property plan to bring together its management strategies at state/territory levels. Health has agreed to draft a comprehensive strategic property plan in consultation with its contracted property management service provider.

23. Centrelink's attention to strategic accommodation planning is considered to be commensurate with the size and characteristics of its leased office property portfolio and the service-related environment in which it operates.

Procurement and Management of Contracted Property Managers

24. In addition to the more than \$474 million spent during 1999–2000 by respondent agencies on rent and outgoings, such as cleaning and maintenance costs, these agencies also allocated in excess of \$11 million to managing their property portfolios. This was spent on services provided both in-house and by outsourced property management service providers.

25. Departments and other large agencies are tending to outsource a greater proportion of their property management function (in excess of 50 per cent on average) than smaller agencies.

26. Only 12 per cent of respondent agencies selected an outsourced property manager through open tender. A factor to consider in analysing these results was the Commonwealth's sale of APG. APG was used by many agencies as their outsourced property management service provider prior to its sale in 1997. In September 1997, the Department of Finance required agencies that had memoranda of understanding with APG to convert those memoranda to legally enforceable contracts with APG's purchaser.

27. The case studies showed that Health and Centrelink had selected property managers through open tender.

28. DFAT continues to use APG's successor under a new contract, which incorporates a wider range of services at an overall increased cost to the Commonwealth. The market was not tested prior to the letting of this new contract and there was not adequate documentation available to indicate why tenders were not sought. DFAT does not document key matters discussed and/or agreed on at meetings held with its contracted property manager. In addition, performance indicators contained in its property management contract are not readily measurable. As a result, DFAT was not able to demonstrate that its contract monitoring arrangements were adequate.

Commonwealth Agency Leases

Profile of leases

29. Survey results indicate that more than 70 per cent of the 1505 leases in the survey were for terms of fewer than five years. This suggests that many agencies forego the potentially lower per annum rentals available with longer-term leases, for the flexibility provided by short term leases. The majority of Centrelink and Health's leases are for periods of less than five years; whereas DFAT's lease for the majority of its leased space is for more than 10 years.

30. In aggregate, respondent agencies have a preference for net rent leases. Net rent leases exclude an allowance for outgoings/property operating expenses, that is, the tenant generally is responsible for all outgoings/property operating expenses. The majority of DFAT's and Health's leases are gross rent leases.⁷

31. Overall, respondent agencies appear to be leasing accommodation of a mid-range Grade B quality.⁸ DFAT's properties are spread across all five categories, with the highest number of properties in Grade B. 76 per cent of Health's leases are for Grade C properties; while all of Centrelink's properties are either Grade B or Grade C.

Distribution of leased space

32. Respondent agencies leased in excess of 1.7 million square metres of office accommodation across Australia at 30 June 2000. 85 per cent of this leased space was situated in city/metropolitan areas.

33. Centrelink was the largest holder of leased space amongst all FMA agencies. The agency was also the largest holder of country/regional leased space at 30 June 2000 with 224 leases covering almost 215 000 square metres.

34. The state/territory distribution of leased office space for each category of respondent agency was in line with the equivalent population for the respective states and territories, with the exception of the ACT, as the majority of agencies have head offices in Canberra.

⁷ Centrelink does not maintain gross or net rent details on its property management system. However, Centrelink has such information in the original lease documents.

⁸ The glossary of terms provides a definition of the different grades of office accommodation.

Expenditure on leased space

35. Agencies are paying above-benchmark rentals in city/metropolitan areas, with the exception of in NSW. The Commonwealth is the largest influence on the market in the ACT, where departments and smaller agencies were paying more than 10 per cent above the benchmarks. In contrast, other city/metropolitan outgoings for items, such as energy costs, generally were below benchmarks.

Leased space density

36. Survey results indicated that, in general, in both city/metropolitan and country/regional areas, densities (that is, square metres per person) are above the benchmark range of 15 to 25 square metres per person. This indicates that responding FMA agencies may be renting space in excess of their needs and/or utilising existing space inefficiently. The effects of this can be higher than necessary payments of rent and outgoings.

37. In terms of the three case study agencies, Health, with a density of 21 sqm/person, was the only agency with a density within the benchmark range. DFAT and Centrelink both had densities of 27 sqm/person.

38. DFAT attributes its relatively low density to the RG Casey Building, which represents over 80 per cent of DFAT's leased office accommodation. The RG Casey Building contains over 16 000 sqm of space that DFAT has identified as special purpose space. This includes lecture rooms, laboratories, training and meeting rooms, crisis centres and various other special purpose areas that are not normally found in conventional office accommodation.

39. Comparison of the benchmark and survey data suggest that⁹ respondent FMA agencies were paying approximately \$89 million per annum for above-benchmark space and an additional \$6.5 million in outgoings at 30 June 2000. In regard to rents, this estimate represents approximately \$71 million (or 79 per cent) in city/metropolitan areas and approximately \$18 million (or 21 per cent) in country/regional areas. In terms of outgoings, this estimate represents approximately \$4.7 million (or 72 per cent) in city/metropolitan areas and approximately \$1.8 million (or 28 per cent) in country/regional areas.

⁹ Excess space is the space rented at 30 June 2000 after subtracting 25 square metres per person and any vacant space identified by respondent agencies.

Lease Reviews at Case Study Agencies

Energy efficiency

40. The Government's energy efficiency policy states that new lease agreements should not include any provision permitting the recovery from the tenant of the cost of energy use by central building services during normal office hours. This seeks to ensure that building owners have an incentive to improve the energy efficiency of central building services.

41. The lease for the RG Casey Building, for which DFAT is the lessee, did not comply with the Government's energy efficiency policy. The Government's energy policy was announced on 20 November 1997. The RG Casey Building was at this time already out to tender. The Government's 20 November energy policy was interpreted and promulgated to Commonwealth agencies on 15 April 1998. Because the RG Casey Building was sold on 24 April 1998, there was little time between announcement of the Government's energy policy and the sale for prospective tenders to be advised of the Government's new policy and for this matter to be addressed in final negotiations before the sale and leaseback were completed. The energy costs for the building are high: an independent assessment in May 2001 commissioned by DFAT rated the building's energy management systems as being at the lowest level on a five point scale. The independent assessment concluded, that amongst other factors, current lease and service arrangements have restricted DFAT's access to detailed energy consumption costs that could assist it to reduce energy costs.

42. These findings indicate the need for stronger promotion of the Government's energy policy. Agencies should also seek advice from the Australian Greenhouse Office (AGO) on leasing provisions that affect the recovery of energy costs for building central services during working hours. AGO advised that an independent review commissioned by the Department of Industry, Science and Technology and AGO of the Commonwealth's energy policy recommended that greater emphasis be placed on marketing of the policy to agencies. This marketing would include promotion of a greater agency awareness of their responsibilities in relation to energy costing in building leases.

Rent Review Provisions in Commonwealth sale/leaseback properties at case study agencies

43. From the analysis of 43 leases managed by DFAT, Health and Centrelink, 32 leases contained clauses that prevent a decrease in rent. This form of clause, known as a ratchet clause, does not allow rents to fall below the previous rent payable during the lease term. Depending on market forces at the time of the rent review, this may prevent the rent from being reviewed to a 'true' market rent. The effect of a ratchet clause is to guarantee the building owner a stable or increasing rental stream for the term of the lease.

44. Sixteen of the 43 leases were for properties that were previously owned by the Commonwealth. All of these leases contained ratchet clauses. These leases, referred to as Commonwealth sale/leaseback properties, were negotiated by Finance as part of the sale arrangement. Finance advised that agencies occupying space in Commonwealth buildings were required to commit to leases in the form endorsed by the Commonwealth Property Committee as required by the Government. Finance further advised that, in accordance with the FMA Act, each agency would have been required to satisfy itself before entering into a lease. In Finance's view, this represents significant influence over the terms of the lease. Two case study agencies indicated that, generally, they had limited influence over the terms and conditions of the leases, including the existence of ratchet clauses. As a result, and not withstanding the above, those agencies were of the view that they are managing leases with terms and conditions over which they had limited influence.

45. The largest building in the ANAO's sample, for which there was a sale/lease back arrangement, is the RG Casey Building in Canberra. DFAT had signed a long-term lease for this building, with the lease expiring in 2012. The lease for this building represented 88 per cent of DFAT's annual rental expenditure for domestic properties. DFAT indicated that it agreed to the lease only because of the deeming deadline imposed on the department, and expressed reservations about a number of commercial aspects of the final lease. Finance could not agree to vary certain provisions of the lease because it considered that DFAT sought to vary some of the essential commercial terms of the lease, including the level of rent, rent review provisions, lease terms, and arrangements for payment of energy costs, contrary to the fundamental principle of user pays. Finance stated that this would have been detrimental to the Commonwealth's divestment program.

Recommendations

46. The ANAO made three recommendations to two case study agencies aimed at improving their property management. The agencies agreed with these recommendations.

Recommendations

Set out below are the ANAO's recommendations with report paragraph references and agencies' responses.

Recommendation No. 1
Para 2.33 The ANAO recommends that DFAT finalise its strategic property plan and implement its business continuity plan in order to assist the department to achieve cost-effective property management.

Response: Agreed.

Recommendation No. 2
Para 2.37 The ANAO recommends that Health ensure that its national strategic property plan and its re-drafted business continuity plan are finalised by the end of the 2001 calendar year in the interests of efficient and effective operations.

Response: Agreed.

Recommendation No. 3
Para 3.31 In order for DFAT to be able to determine whether contract performance is satisfactory, the ANAO recommends that DFAT:

- review the performance indicators set out in the current property management contract and seek to replace them with measurable performance indicators; and
- review the provider's performance regularly, and document key matters discussed and/or agreed at these reviews.

Response: Agreed.

Audit Findings and Conclusions

1. Introduction

This chapter provides a definition of property management in the context of the audit, outlines recent changes in Commonwealth property management. It also outlines reasons for undertaking the audit as well as the objectives, scope and methodology of the audit.

Background

1.1 The Commonwealth Government is estimated to occupy up to ten per cent of available office space in metropolitan Australia, and may well be the single largest occupier of leased office accommodation nationally. In the 1999–2000 financial year, this presence cost the Commonwealth in excess of \$485 million in rent and outgoings. The latter include cleaning and maintenance costs, and management of property portfolios.

1.2 Each Commonwealth agency, irrespective of its size or function, is responsible for managing its leased office property. Agencies vary in the numbers of leases managed, for example from one lease in a single location, to 471 leases Australia-wide for one agency.

1.3 Agencies have not always been required to manage their own leased office property portfolios. In the 1980s, the former Department of Administrative Services managed all property appropriations and controlled all leased space. This centralised management role has changed over the years, leading to a complete devolvement of property management to agencies. The intention of this policy change was to give agencies control over decisions relating to property, and to make them responsible for the associated resource implications. As a result, agencies are now required to address the issues associated with leased office property portfolios, including strategic planning, lease negotiations and contract management.

1.4 After labour costs, expenditure on property is often the second largest single item of agency expenditure. Against this background, a performance audit has been conducted utilising a survey and case studies to determine, among other things, how well agencies are managing their leased office property portfolios.

Property management—a definition

1.5 Property Management is the term used to describe the full range of services for the management of a portfolio of real estate assets. It can be divided into three categories.

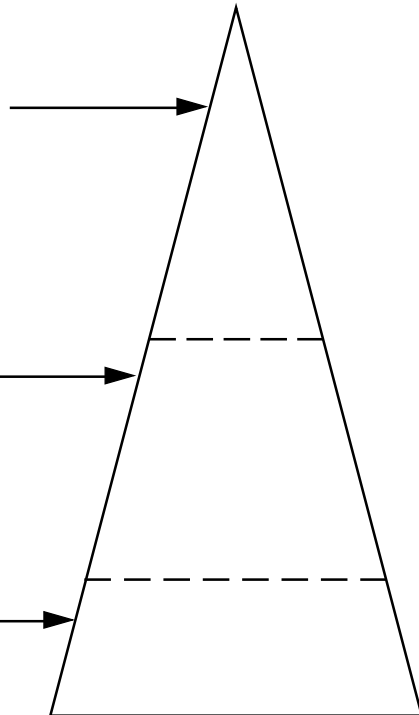
Figure 1.1

The Three Tiers of Property Management

Asset Portfolio Management incorporates the strategic element of the management process. It guides the acquisition, use and disposal of assets (ie, leases on office accommodation) to make the most of their service delivery potential and to manage the related risks and costs over their entire life.

Agency Leased Property Management incorporates the managerial element of the process of managing current and future leased office accommodation requirements. Traditionally, the property manager has been responsible for the daily operations of the property incorporating lease management, operating costs management, budgeting and contract administration.

Agency Leased Property Facilities Management incorporates the operational element of the management process. Facility management is the practice of coordinating the physical workplace with the people and the work.



1.6 The audit examined the Commonwealth’s management of leased office accommodation, focusing on:

- asset portfolio management; and
- agency leased property management.

Recent changes in Commonwealth property management and operations

Pre 1980

1.7 Prior to 1980, the former Department of Administrative Services (DAS) managed multi-occupancy properties and those declared as surplus to the Commonwealth’s requirements. Single occupied premises were managed by the occupant agency and agencies approached the market place on their own behalf.

1981–1987

1.8 During the 1980s, DAS's property management role was broadened. DAS was given direct control over all Commonwealth-budgeted funds relating to property, and it controlled the Commonwealth's own estate and properties leased by Commonwealth agencies.

1.9 As part of this role, DAS developed manuals, standards and guidelines to establish standard practices across the Commonwealth. DAS also developed and maintained a Property Management Information System that included all property used by departments and agencies.

1988–1996

1.10 Government reform led to the rearrangement of DAS's functions. In relation to property management, agencies were given increased ability to make their own property decisions, consistent with a set of general principles to be applied in the provision of common services to government programs.¹⁰ The changes included the introduction of charging for rent and the provision of property services, and additional freedoms for some departments in relation to the lease and fitout of their offices outside the central business district of capital cities.

1.11 In addition, Australian Estate Management (AEM) was formed to carry out the function of nominal owner/landlord of the Commonwealth Estate. In addition, the Australian Property Group (APG) was created to carry out a tenancy advocacy role on behalf of Commonwealth departments and agencies. Both AEM and APG were in the Administrative Services Portfolio.

1996–1999

1.12 During this period, the Government introduced further changes to Commonwealth property management. A key to these changes was the establishment of the *Commonwealth Property Principles* (the Principles). The Principles state that the Commonwealth should only own property where the assessed long term yield exceeds a nominated rate, currently 14 to 15 per cent, or where it is otherwise in the public interest to do so.¹¹

¹⁰ Department of Administrative Services, *Annual Report 1987–88*, AGPS, Canberra, 1988.

¹¹ *Commonwealth Property Principles, Application Guidelines for Agencies*.

1.13 A Commonwealth Property Committee (CPC) was established during the period of implementation of the Principles to oversee a Commonwealth Property Sales Program. This involved sales of those properties that did not comply with the Principles. The CPC was an independent committee reporting directly to the Government. A Commonwealth Tenants' Lease (CTL), used by Finance, was developed in consultation with industry, owners and tenants, and was endorsed by Government as part of the recommendations of the CPC.

1.14 The Commonwealth Property Committee was required to review Commonwealth owned properties against the Principles to determine whether properties should be held or sold. Subsequently, after the joining of DAS with the Department of Finance to form the Department of Finance and Administration, Finance managed the sale of 114 office properties over the financial years 1997–98 to 1999–2000, with proceeds totaling approximately \$1125 million.

1.15 In this period, the Government also reviewed the roles of AEM and the APG. This led to:

- the outsourcing of the building/property management function formerly carried out by AEM;
- the sale of APG, with departments and agencies engaging private firms to carry out a similar role on their behalf; and
- the establishment of the Domestic Property Group (DPG), which was intended to be a strategic planning and co-ordination organisation.

The Department of Finance and Administration's current role

1.16 As indicated above, changes in Commonwealth property management have resulted in a move away from the highly regulated system managed by DAS in the 1980s, to a devolved system where agencies are responsible for their own property management.

1.17 As a result, Finance's current property management role is limited to the management of the Commonwealth's overseas and much reduced domestic property portfolios (excluding Defence-owned properties) on a commercial basis. This portfolio consists of some 400 properties in over 50 countries valued at around \$2.4 billion. The range of properties includes Australian embassies and official residences overseas, and, in Australia, several commercial office buildings as well as law courts, laboratories, detention centres, heritage properties and miners' cottages.

The current legislative framework

1.18 The legislative framework that currently governs Commonwealth property management is as follows:

- the *Land Acquisitions Act 1989* requires authorisation, by a delegate, of acquisitions and disposals of interests in land. Interests in land include leases;
- the *Financial Management and Accountability Act 1997* (the FMA Act) and the *Financial Management and Accountability Regulations*, provide chief executives with autonomy in their financial management. The FMA Act requires all chief executives to promote the effective, efficient and ethical use of Commonwealth resources for which they are responsible.¹² In addition, before a lease is signed, a suitably authorised officer must approve the proposal to spend public money (consisting of the rent and other amounts payable under the lease) in accordance with the FMA Regulations;
- the *Commonwealth Procurement Guidelines* set out the Commonwealth's purchasing policy, and the Guidelines specifically include operating leases on real property. The FMA Regulations¹³ require that an official performing duties in relation to the procurement of property and services must have regard to the Commonwealth Procurement Guidelines, and must make written records of any actions that are not consistent with the Guidelines and reasons for doing so. The Guidelines do not prescribe the procurement method to be used, nor do they set minimum limits on the number of offers to be sought¹⁴, but rather set out the core procurement policies of value for money; open and effective competition; ethics and fair dealing; accountability and reporting; and
- the *Commonwealth Property Principles*, which promote the ownership of property in only exceptional circumstances. These Principles, however, are only relevant to Commonwealth owned properties¹⁵.

1.19 Agencies may also seek guidance from the *Commonwealth National Lease* (formerly the *National Tenant's Lease*), which has been developed by the Australian Government Solicitor (AGS). When negotiating leases with private sector landlords, AGS has advised Commonwealth agencies to use this lease as a starting point for negotiations with building owners. It provides optimum protection of the interests of the lessee, which can reasonably be expected to be accepted by building owners.

¹² *Financial Management and Accountability Act 1997*, Section 44(1).

¹³ *Financial Management and Accountability Regulation* 8.

¹⁴ *Commonwealth Procurement Guidelines*, 1998, page 8.

¹⁵ The scope of this audit specifically excludes properties owned by the Commonwealth.

Audit objectives

1.20 The objectives of the audit were to:

- develop a benchmark of the Financial Management and Accountability Act agencies' property management performance for current and future comparison; and
- form an opinion as to whether the FMA agencies reviewed in the case studies:
 - manage leased office property in accordance with the requirements of the FMA Act and other official guidance; and
 - manage their leased office property effectively.

Audit scope

1.21 This performance audit is the first property management audit that the ANAO has conducted since FMA Act came into effect in 1997, with the associated devolution of responsibility to agency heads.

1.22 The audit included coverage of office accommodation currently leased in Australia from the private sector, where office accommodation is housing the functions and activities of clerical, technical or professional staff, including conference and meeting rooms and ministerial suites but excluding basements, car parks, theatrettes and cafeterias.

1.23 The ANAO is conducting a performance audit of the Commonwealth Property Sales Program, a report on which will be tabled later in the year.

Audit criteria

1.24 Criteria were used to assess whether FMA agencies are adequately equipped to manage their leased office property portfolios and their future property needs. The criteria were:

- agencies have clearly defined asset portfolio management frameworks in place; and
- if property management, or components thereof, is outsourced, that a contract and contract management processes are in place and appropriate performance indicators have been set and are being measured.

Audit methodology

1.25 Re-Engineering Australia was engaged to assist with the planning and conduct of the audit and with preparation of the draft report. To obtain appropriate expertise throughout the audit, the ANAO invited

tenders to provide property management advice, to administer a survey and to analyse its results. Sinclair Knight Merz (SKM) was engaged for these tasks.

Survey of FMA agencies

1.26 A survey instrument was developed in consultation with SKM. The survey contained questions about:

- strategic planning;
- procurement and management;
- leased office accommodation profile;
- fitout; and
- property management systems.

1.27 The survey collected data on agencies' leased property portfolios for the year ended, or as at, 30 June 2000. It was sent to 59 FMA agencies and by 14 July 2000, 44 of the 59 agencies had completed and returned their survey, representing a 75 per cent response rate. The survey collected data on 1505 leases for office properties occupied by Commonwealth agencies.

1.28 The data presented here can be used by individual agencies to compare their leased office accommodation arrangements with those of other similar entities. Such comparisons completed by agencies have the potential to improve Commonwealth property management.

1.29 The following appendices set out:

- the survey instrument (Appendix 1); and
- agencies to which the survey questionnaire was sent, and responding/non-responding agencies (Appendix 2).

1.30 The agencies that responded to the survey were grouped into the following categories and have been analysed accordingly:

- departments (13 agencies);
- other large agencies (nine agencies); and
- smaller agencies (22 agencies).

1.31 The grouping of agencies into these categories is intended to recognise the differences in function and size across the various agencies, thus allowing for a more coherent analysis. For example 'departments' includes all departments and these are generally centralised organisations such as the Department of Veterans' Affairs and the Department of Health and Aged Care. 'Other large agencies' are entities often with a dispersed network of offices. They generally perform a specialised service-related function and therefore one of their requirements is to be accessible to

the public, requiring them to have a stronger regional and ‘over the counter’ presence. They include organisations such as the Australian Taxation Office. ‘Smaller agencies’ also operate as a dispersed network, generally comprising smaller offices often with a public service contact related function. Generally their public service functions are a mix of ‘over the counter’ and ‘over the phone’ activities. Examples are the Administrative Appeals Tribunal and the Australian Competition and Consumer Commission.

Case studies

1.32 Case studies were conducted in the following agencies to supplement the data obtained from the survey:

- the Department of Foreign Affairs and Trade;
- the Department of Health and Aged Care; and
- Centrelink.

1.33 Each agency faces differing property management issues, and it was these differences that the ANAO sought to explore in the expectation that these agencies’ experiences may be of benefit to other agencies facing similar circumstances. For example, in terms of office location:

- the majority of DFAT’s staff are located in one building, the RG Casey Building, in Canberra;
- Health has 37 office leases across Australia, which are generally located in city/metropolitan areas, with approximately two thirds located in Canberra; and
- Centrelink has 471 sites across Australia covering both city/metropolitan and country/regional locations.

1.34 In addition, a sample of leases from each of the three agencies was obtained and reviewed against the Commonwealth National Lease¹⁶ and against terms and conditions that would be expected in better practice private sector leases. The results of this testing were analysed in consultation with SKM. The sample of leases reviewed at the case study agencies of former Commonwealth owned buildings included in the sample are set out in Appendix 3.

¹⁶ The Commonwealth National Lease was developed by the Australian Government Solicitor as guidance for agencies undergoing lease negotiations with private sector landlords. It provides optimum protection of the interests of the lessee, which can reasonably be expected to be accepted by building owners.

Case study agencies—overview

1.35 Table 1.1 shows the basic differences in the cost, size and location of each of the case study agencies' leased office property portfolios.

Table 1.1

Overview of Case Study Agencies for the Financial Year ended 30 June 2000

Agency	Rental for the year ended 30.06.00 \$	Outgoings for the year ended 30.06.00 \$	Sqm Leased as at 30.06.00	Number of Leases as at 30.06.00	City/Metropolitan		Country/Regional	
					% of Leased Area	% of Rental Costs	% of Leased Area	% of Rental Costs
DFAT	19 913 700	2 866 700	50 514	15	99	99.6	1	0.4
Health	14 627 900	3 217 400	60 472	37	98	98	2	2
Centrelink	131 149 400	31 588 315	549 776	471	68	72	32	28

Case study agencies—Department of Foreign Affairs and Trade

1.36 The Department of Foreign Affairs and Trade (DFAT) supports the Government in pursuing its foreign and trade policy objectives.¹⁷ In fulfilling this function, DFAT acts mainly as a policy department. However, some services are provided to the general public, for example, the issue of passport documents. DFAT's role is in contrast to Centrelink's, which is primarily a customer service agency.

1.37 DFAT holds properties in Australia and overseas. The audit focused solely on DFAT's management of its domestic leased office accommodation portfolio.

1.38 Approximately 90 per cent of DFAT's staff are accommodated in the RG Casey Building in Canberra. As DFAT holds a 14 year lease (expiring in 2012) over the RG Casey Building, the majority of DFAT's property management issues relate to the use and management of this building and the management of property services contractors.

Case study agencies—Department of Health and Aged Care

1.39 Health's mission is to lead the development and implementation of health and aged care services policy to achieve government policy and directions¹⁸. Health endeavours to achieve this mission through a network of staff in state and territory offices, supported by a Canberra-based Central Office.

¹⁷ Department of Foreign Affairs and Trade, *Annual Report 1998–99*, DFAT, Canberra, p. 7.

¹⁸ Department of Health and Aged Care, *Annual Report 1998–99*, DHAC, Canberra, p. 14.

1.40 The formation of the Department from the former Department of Health and Family Services, and the transfer of some responsibilities to the Department of Family and Community Services in October 1998, significantly changed the structure and size of Health's central, state and territory offices.¹⁹ This restructure has had property management ramifications, especially in terms of the risk of vacant or under-utilised space.

Case study agencies—Centrelink

1.41 Centrelink provides income support and other payments and referral services to over 6 million customers²⁰ through various means. These services include the payment of the Youth Allowance and Austudy on behalf of the Department of Family and Community Services, and the provision of Job Network Enrolment services on behalf of the Department of Employment, Workplace Relations and Small Business. Centrelink holds over 470 leases that are constantly being negotiated, renewed or terminated. Many aspects of Centrelink's operating environment have an impact on leased office accommodation planning and management, including:

- changes in Government policy. Centrelink delivers a range of services that can change frequently in accordance with Government policy initiatives.²¹ These changes can impact on the way services are delivered, staff numbers and office locations;
- advances in technology. Advances in technology and the way in which customers prefer to access services can influence service delivery methods, which can impact on the amount and style of accommodation required and locations; and
- numbers and characteristics of customers. Customer numbers and demographic characteristics affect the location and number of Centrelink offices.

¹⁹ Department of Health and Aged Care, *Annual Report 1998–99*, DHAC, Canberra, p. 17.

²⁰ Centrelink, *Annual Report 1998–99*, Centrelink, Canberra, p. 2.

²¹ Centrelink, *Annual Report 1998–99*, Centrelink, Canberra, p. 12.

Structure of this report

1.42 Chapter 2 of this report includes data on agencies' strategic property and business continuity planning. Chapter 3 reports findings on the procurement and management of contracted property managers. Chapter 4 presents survey and case study data on agency leases, while Chapter 5 sets out the findings on the sample of leases from case study agencies.

1.43 This audit was conducted in accordance with ANAO Auditing Standards at an estimated cost to the ANAO of \$369 000.

2. Strategic Property and Business Continuity Planning

This chapter discusses the results of the survey and case studies in relation to strategic property and business continuity planning, with comparisons between the two where applicable.

2.1 ANAO's survey contained questions relating to the existence of both strategic property plans and business continuity plans. In addition to the survey coverage, the strategic property planning of the three case study agencies, DFAT, Health and Centrelink, was reviewed in detail and the results reported under separate headings for each.

Strategic property planning

2.2 Strategic property plans enable agencies to identify property requirements, to put in place strategies to obtain accommodation in accordance with those requirements, and to monitor the performance of their leased property portfolios against budgets and benchmarks. Without this tool, agencies run the risk of not achieving efficient or effective use of funds. This may come about as a result of:

- leasing inappropriate office space, for example, in the wrong location or of an inappropriate quality;
- leasing either too much or too little office space; or
- entering into leases with inappropriate terms, for example, lease durations that lock agencies into long term commitments where long term accommodation requirements cannot be reasonably measured.

2.3 The level of strategic property planning should have regard to the importance property plays in the delivery of agency outputs and outcomes as well as the materiality of property expenditures. It is the underlying principles of strategic property management that are important to these property plans, not their size or sophistication. The essential feature is that agencies recognise the contribution property makes to the achievement of their objectives and give due consideration to this in their strategic planning.

2.4 Leases of office accommodation exist to support the broader objectives of agencies. This means that agencies should have strategic accommodation plans that complement their business plans.

2.5 A strategic property plan should:

- be documented;
- set out the period to which it relates;
- complement an agency's business plan;
- set out short to medium term leased office requirements. Where staff projections are difficult to forecast, this limitation should be detailed in the plan;
- put in place strategies to meet accommodation requirements;
- establish benchmarks and/or historical performance, against which the portfolio's current performance can be measured, and require that this measurement take place on a regular basis and be reviewed by management; and
- be reviewed and revised on a regular basis.

2.6 Agencies could include the following examples of key benchmarks/indicators in their strategic property plans:

- density (square metres per person);
- lease duration;
- rent in dollars per square metre;
- outgoings in dollars per square metre, including cleaning costs in dollars per square metre, energy costs per square metre, and maintenance costs per square metre;
- fitout in dollars per square metre; and
- in-house and outsourced property management services in dollars per square metre.

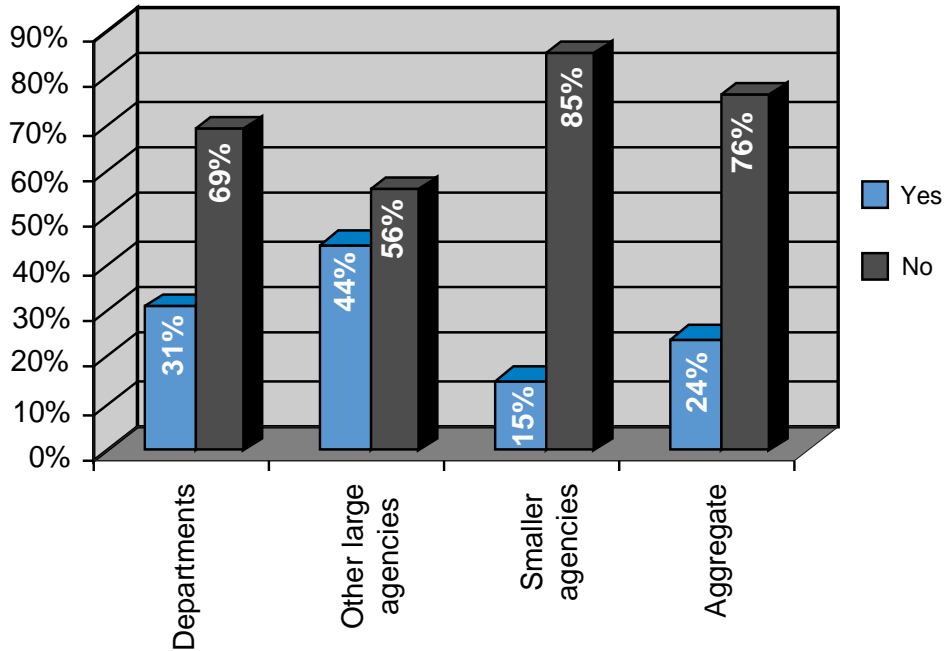
2.7 In order to measure performance against benchmarks, historical information should be maintained for trend analysis and to determine whether benchmarks should be adjusted up or down. This mechanism encourages continuous improvement. However, benchmarks cannot be determined exclusively by reference to historical information. Market influence, particularly for rental levels, can be a significant factor and movements can occur over a relatively short period of time.

Survey

2.8 Figure 2.1 sets out the various percentages of respondent agencies with strategic property plans at 30 June 2000.

Figure 2.1

Percentages of Respondent Agencies with Strategic Property Plans as 30 June 2000 by Agency Type and in Aggregate



2.9 As shown in Figure 2.1, less than 50 per cent of respondent agencies in each category had a current strategic property plan in place at 30 June 2000, with an overall result of 24 per cent of agencies having strategic property plans.

2.10 The relatively small proportion of strategic property plans in place across the respondent agencies indicates a need for the majority of agencies to develop them for effective property management. This limited strategic planning by the majority of respondent agencies inhibits the focus on longer-term needs of agencies and may result in operating inefficiencies. Potentially these could be considerable given that on average, departmental property portfolios contain 27²² leased properties and other large agency property portfolios contain 25²³ leased properties. Agencies should ensure that they have a strategic property plan to assist them in managing their overall property needs. As stated earlier, the level of planning should have regard to the importance property plays in the delivery of agency outputs and outcomes as well as the materiality of property expenditures.

²² This average does not include the Finance portfolio of 310 properties.

²³ This average does not include the Centrelink portfolio of 471 properties.

Department of Foreign Affairs and Trade

2.11 At 30 June 2000, DFAT's domestic leased property portfolio consisted of 15 leases. The RG Casey Building lease in Canberra represented 83 per cent of DFAT's leased office space and 88 per cent of its rental expenditure for the year ended 30 June 2000. The lease over the RG Casey Building expires in February 2012.

2.12 DFAT does not have a current strategic property plan in place, although steps have been taken to progress a draft strategic property plan.

2.13 The ANAO suggests that DFAT finalise its strategic property plan as soon as possible. DFAT should ensure that the plan sets out benchmarks and/or historical data which can be reported against on a regular basis (at least annually).

Department of Health and Aged Care

2.14 Health had 37 leases at the time of the audit.²⁴ In the year ended 30 June 2000, Health spent \$14.6 million on rent and \$3.2 million on outgoings.

2.15 Health's strategic property plans have been prepared for each state/territory portfolio. These strategic plans address all current leases within the state/territory for a three-year period. The format and content of the strategic plans were considered by the ANAO to be of a high standard, and they provide a focused approach to the identification and management of key issues associated with existing leases in a local market context.

2.16 It is suggested that Health develops a national strategic property plan to bring together the state and territory property management strategies. The individual state/territory property plans would remain an integral part of the planning process. Health has agreed to draft a national strategic property plan in consultation with its contracted property management service provider by the end of the 2001 financial year.

Centrelink

2.17 Centrelink holds the largest leased asset portfolio of all agencies, with over 470 individual leases at 30 June 2000, and an annual rental bill of \$131 million.²⁵ Total property related budgeted expenditure of \$193 million represented 11 per cent of Centrelink's 1999–2000 appropriation.

²⁴ Seven of these leases were reviewed in this audit, as set out in Appendix 3.

²⁵ Rental excludes outgoings of in excess of \$31 million.

2.18 Centrelink has a tiered approach to strategic planning. The *Centrelink Strategic Framework (1999–2004)* sets out the high level strategic goals of the agency, and *The Business Assumptions of Centrelink's Service Delivery Model* provides detail. These documents specifically incorporate property issues. Centrelink's approach shows recognition of the importance of leased office accommodation in delivering its services.

2.19 Centrelink is in the process of developing its *Business Plan 2* which should serve to enhance its current strategic management framework and business planning. The Centrelink Board has indicated a need for *Business Plan 2* to incorporate clear directions about an integrated property strategy.

2.20 With the enhancements being developed, Centrelink's attention to strategic accommodation planning is considered to be commensurate with the size and characteristics of its leased office property portfolio and the service related environment in which it operates. These achievements should assist in the efficient and effective management of its leased office property portfolio.

Business continuity planning

2.21 Many agencies provide services to a variety of customers and failure to deliver these services could have very significant consequences for those concerned. To raise awareness of this issue, the ANAO released a *Business Continuity Management Better Practice Guide* in January 2000. The Guide stressed the importance of continuity of public sector business and urged all boards, chief executives and senior managers of public sector organisations and business activities to consider this issue. Continued availability of accommodation is one factor that is important in business continuity and should be addressed in an agency's business continuity plan.

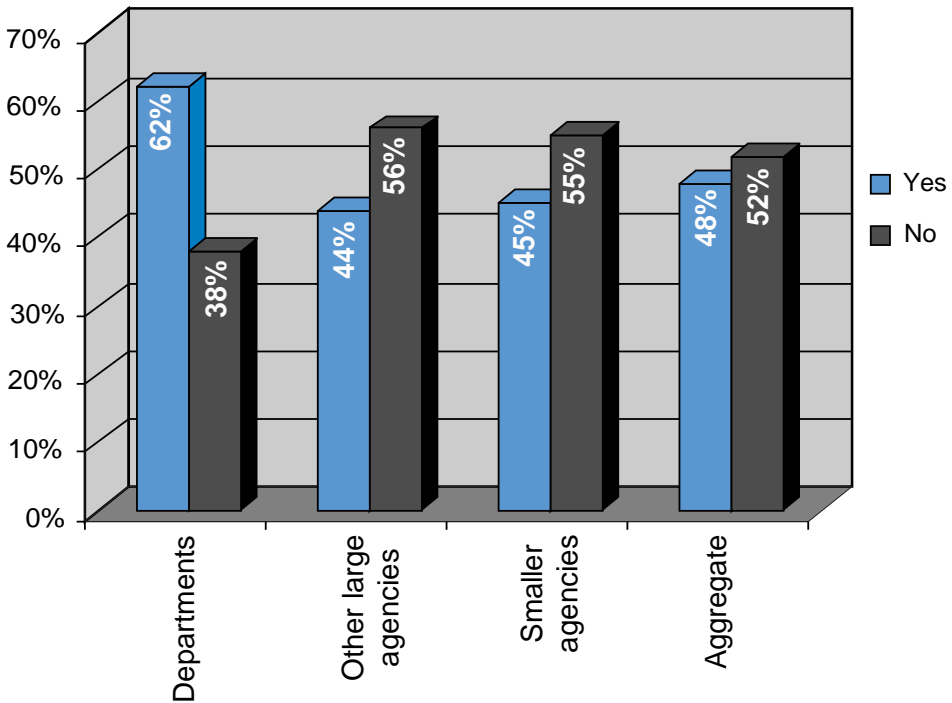
2.22 The availability of leased office property is a risk factor in maintaining business continuity. In the event that the physical locations in which agency staff conduct business become unavailable due to an emergency of some kind, without adequate strategies in place, business continuity is at risk.

Survey

2.23 Figure 2.2 sets out respondent agencies with business continuity plans at 30 June 2000.

Figure 2.2

Percentages of Respondent Agencies with Business Continuity Plans at 30 June 2000 by Agency Type and in Aggregate



2.24 As shown in the Figure 2.2, business continuity plans were more commonly found among respondent agencies than strategic property plans, with almost half of all entities having business continuity plans. These plans generally included clauses relating to building access, and alternative accommodation that would be available in the event of an emergency. Agencies should ensure that they have up to date business continuity plans to ensure they are prepared for the timely recovery of essential services, in the event of a major mishap such as a building fire or flood.

2.25 Agencies without business continuity planning are subjecting themselves to a greater risk of not being able to effect a timely recovery in the event of emergencies that affect their built environs and related business operations.

Department of Foreign Affairs and Trade

2.26 In 1999 DFAT engaged consultants to prepare a property-related business continuity and contingency plan as part of a range of Year 2000 services for the RG Casey Building. After the preparation of this plan, the consultant identified existing systems critical to the sustained operation of the RG Casey Building that would require urgent modification to meet the business continuity needs of DFAT. The recommendations in this report had not been formally accepted or implemented at the time of this audit.

2.27 As the continued functioning of the RG Casey Building is crucial to DFAT's operation, the preparation and implementation of a business continuity plan is considered important. Therefore, it is suggested that the business continuity plan that was prepared by consultants for DFAT be reviewed, and an appropriate business continuity plan be implemented as a matter of priority.

Department of Health and Aged Care

2.28 As part of its Year 2000 contingency planning, Health produced a *Year 2000 Roll Over Plan*. This plan summarised the key procedures that were planned and documented in a comprehensive range of divisional, and state and territory office plans. The state and territory office plans included building systems arrangements, for instance, the provision of essential utilities such as power, air conditioning and lift operation.

2.29 Health sees these plans as a useful set of documents that set out how it would cope in the event of significant disruption. However, Health intends to re-draft these documents to make them a more permanent and fuller business continuity plan, to replace the Year 2000 focus that they currently have.

Centrelink

2.30 Centrelink has both a *Business Continuity Plan* and a *National Disaster Plan*. Whereas the Business Continuity Plan focuses on maintaining Centrelink information technology systems in the event of an emergency, the National Disaster Plan is aimed at maintaining continuity of customer benefits during or following a disaster, which may involve contingencies relating to leased office properties.

Summary

2.31 The survey and case study results indicate that agencies could improve their property management, and hence efficiency and effectiveness, through:

- strategic planning for property needs; and
- preparing business continuity plans, incorporating accommodation related issues.

2.32 In particular, DFAT and Health should make improvements in their strategic planning and business continuity planning through finalising their strategic property plans and, respectively, implementing and finalising their business continuity plans.

Recommendation No.1

2.33 The ANAO recommends that DFAT finalise its strategic property plan and implement its business continuity plan in order to assist the department to achieve cost-effective property management.

DFAT's response

2.34 Agreed. A comprehensive competitive tendering and contracting process for the provision of property management services is being undertaken and will be completed by 1 October 2001. An associated review of our property management arrangements to optimise effective governance over performance, resources, assets and relationships to meet due diligence requirements, and inform the tender process, is also in progress.

2.35 The first task of the incoming contractor will be to finalise a comprehensive strategic property plan.

2.36 The business continuity plan, developed in DFAT as a consequence of Y2K planning, proposed a solution that, when further investigated by the electrical and mechanical engineers involved in the building design, proved to be technically unsound. We have engaged specialist consultants to survey critical mechanical and electrical services in the RG Casey Building to provide the basis for a comprehensive business continuity plan and subsequently a SafetyMap audit. With the cooperation of the building owner we expect to have the plan completed by the end of September 2001.

Recommendation No.2

2.37 The ANAO recommends that Health ensure that its national strategic property plan and its re-drafted business continuity plan are finalised by the end of the 2001 calendar year in the interests of efficient and effective operations.

Health's Response

2.38 Agreed.

3. Procurement and Management of Contracted Property Managers

This chapter reports findings on the procurement and management of contracted property managers.

Procurement

Procurement methods

3.1 As set out in Chapter 1, *Commonwealth Procurement Guidelines* do not prescribe procurement methods to be used by agencies, nor do they set minimum limits on the number of offers to be sought.²⁶ They set out the core procurement principles of:

- value for money;
- open and effective competition;
- ethics and fair dealing; and
- accountability and reporting.

3.2 As a result, agencies are free to choose their own procurement methods so long as these core procurement principles are adopted.²⁷

3.3 This audit has concentrated on two of the core procurement policies: value for money and open and effective competition. The ANAO sought to determine whether agencies, which were the subject of the case studies, had applied these core procurement policies in the selection of their current outsourced property management providers.

3.4 When an agency outsources all or part of a function, it is exposed to a new set of risks and its officers may require a new or different set of skills. For example, if property management services are outsourced, the role of the agency in this area shifts from a need for skilled property managers towards skilled contract managers. The agency should be capable of identifying its needs and developing a contract which reflects these needs. In addition, the agency must be able to monitor the performance of the outsourced property manager to ensure that the terms and conditions of the contract are being met, and to take appropriate and timely action when they are not met.

²⁶ Commonwealth Procurement Guidelines, 1998, page 8.

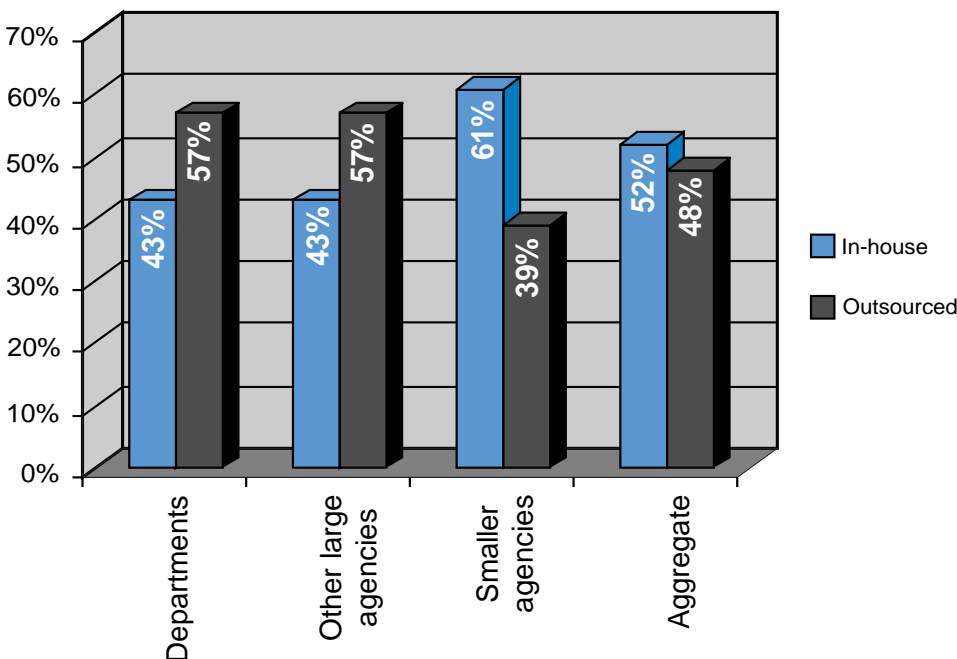
²⁷ Where the core principles set out in the Commonwealth Procurement Guidelines are not adopted, reasons must be documented in compliance with FMA Regulation 8.

Survey

3.5 In addition to the more than \$474 million spent during 1999–2000 by respondent FMA agencies on rent and outgoings such as cleaning and maintenance costs, these agencies also allocated in excess of \$11 million to managing their property portfolios. This was spent on services provided both in-house and by outsourced property management service providers. The extent to which agencies are outsourcing their property management functions is shown in Figure 3.1.

Figure 3.1

Percentage of In-House and Outsourced Property Management at 30 June 2000 by Agency Type and in Aggregate



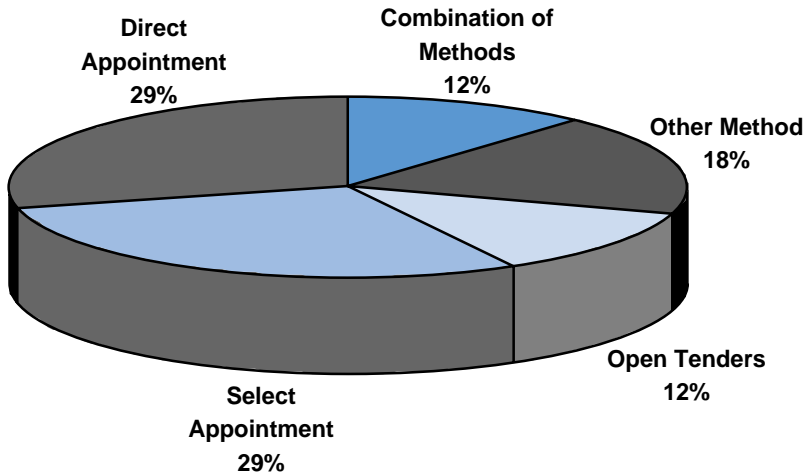
3.6 Figure 3.1 shows that departments and other large agencies are tending to outsource a greater proportion of their property management activities than smaller agencies. It also shows that approximately 50 per cent of property management services are outsourced across respondent agencies.

3.7 Where the core principles set out in the *Commonwealth Procurement Guidelines* are not adopted, FMA Regulations require that reasons must be documented. As indicated above, agencies are free to choose their own procurement methods so long as these key procurement policies are adopted. Better practice would generally be to test the market through a tender process so that the Commonwealth achieves value for money.

3.8 Figure 3.2 sets out the procurement methods used by respondent agencies to appoint their current outsourced service providers.

Figure 3.2

Procurement Methods used to Appoint Current Outsourced Service Providers (All Respondents)



3.9 Nearly 60 per cent of respondent agencies that outsource some or all of their leased property management used either ‘direct’ or ‘select’ appointment to engage their current outsourced property management service providers, rather than putting their contracts to open tender. Only 12 per cent of respondent agencies selected property managers through open tender.

3.10 A factor to consider in analysing these results was sale of the Australian Property Group by the Commonwealth. APG was used by many agencies as their outsourced property management service provider prior to its sale in 1997. In September 1997, Finance required agencies that had memoranda of understanding with APG to convert those memoranda to legally enforceable contracts with APG’s purchaser. The impact of these arrangements is seen in the above data, wherein only a small proportion of service providers was selected through open tender with most property managers appointed through direct and select appointments.

Department of Foreign Affairs and Trade

3.11 DFAT continues to use APG's successor under a new contract, which incorporates a wider range of services at an overall increased cost to the Commonwealth. The market was not tested prior to the letting of this new contract, and there was not adequate documentation available to indicate why a more open process was not sought.

Department of Health and Aged Care

3.12 Health outsources the majority of its property management services, and retains an experienced team of three full time equivalent staff in Canberra to manage the outsourced property management contract and to undertake the remainder of the property management functions.

3.13 The current property management services contract was awarded in 1998 after an open tender process.

Centrelink

3.14 Centrelink's in-house property management function employs approximately 54 full time equivalent staff. The majority of these staff have in excess of five years experience in property related activities. These staff carry out a range of property related activities including:

- strategic planning;
- contract management;
- funds management;
- national standards management; and
- co-ordination of the capital works program.

3.15 In addition to in-house staff, Centrelink employs a property management contractor to provide the following services:

- property management services including lease administration and management of service contracts; and
- real estate services including leasing of new premises and disposal of surplus premises.

3.16 The property management contract was awarded following an open tender.

Management and monitoring of outsourced property management services contracts²⁸

Performance monitoring

3.17 The key aspect of contract management considered in these case studies was the agencies' monitoring of their service providers' performance under the property management contracts.²⁹ Such monitoring is a key aspect because these contracts are relatively high in value and the performance of the contractors can have a direct impact on the efficient and effective use of agency funds through, for instance, advice on measures to reduce energy costs.

3.18 Therefore, essential for agencies was the inclusion of adequate performance measures in their property management contracts. The audit considered case study agencies' monitoring of the performance of their property managers.

Department of Foreign Affairs and Trade

3.19 DFAT's current contract includes performance indicators. However, quantifiable performance indicators have not been set. This makes it difficult for DFAT to assess objectively the provider's performance, such as the contractor's performance in carrying out specified tasks or projects.

3.20 The ANAO was unable to review evidence of DFAT's monitoring of its provider's performance as there was no documentation available on this aspect of its management. DFAT informed the ANAO that it reviewed the contractor's performance prior to the adoption of the current contract. However, the outcome of the review was not documented.

²⁸ Testing of the management and monitoring of outsourced property management services contracts was limited to case study agencies and was not pursued in the survey.

²⁹ The use of property management systems was also considered. Some 57 per cent of respondent agencies either directly or through an outsourced property management service provider, use a property management system. A property management system commonly appears to be part of an outsourced property management services agreement, as only 12 per cent directly use an in-house property management system.

3.21 In order for DFAT to be able to determine whether performance under the property management contract is satisfactory, the ANAO considers that the department should:

- review the performance indicators set out in the current property management contract and seek to supplement them with quantifiable performance indicators;
- assess performance against the performance indicators regularly, with these assessments being documented; and
- where performance is not satisfactory, take and document appropriate action to remedy any performance related problems.

Department of Health and Aged Care

3.22 Health regularly reviews the performance of its contracted property manager. Monitoring is through monthly Contract Control Group meetings. Minutes of these meetings are recorded and action to be taken is documented.

3.23 In addition, Health's contracted property manager prepares a monthly critical dates report which identifies any short, medium and long-term action that is required. This report acts as a valuable strategic management tool for Health and its contracted property manager.

3.24 The above mentioned mechanisms have been established by Health with its contracted property manager to maintain and assess performance against the performance indicators contained within the contract. Monthly Contract Control Group meetings specifically address the contractor's performance in a number of areas including capital expenditure, service contracts (eg cleaning contracts), fault recording/reporting, strategic planning, and issues associated with individual leases.

Centrelink

3.25 The contract awarded to Centrelink's contracted property manager was for a term of three years with two one-year options. The first of these options was in February 2000. Prior to the decision to exercise this option, Centrelink reviewed the performance of its contracted property manager.

3.26 Performance indicators are set out in Centrelink's property management contract. These performance indicators are monitored on a monthly basis through reports tabled at monthly contract management meetings. These meetings are attended by Centrelink representatives, including the Centrelink contract manager, and representatives of the contracted property manager. Discussions at these meetings are minuted.

Summary

Procurement

3.27 Health and Centrelink have adopted the core procurement policies of value for money and open and effective competition set out in the Commonwealth Procurement Guidelines. They have done so by tendering through select and open tenders respectively in procurement of their contracted property management providers.

3.28 DFAT was not able to demonstrate that it has adopted the key procurement policies, as an open process was not undertaken to test the market for its current contractual arrangements.

Management and monitoring

3.29 Health and Centrelink have adequate procedures in place to ensure that the performance of contracted property managers can be measured and monitored on a regular and timely basis.

3.30 Meetings held between DFAT and its contracted property manager are not formally documented, and therefore it is not clear whether monitoring is adequate. In addition, the performance indicators contained in their property management contract are not readily measurable.

Recommendation No.3

3.31 In order for DFAT to be able to determine whether contract performance is satisfactory, the ANAO recommends that DFAT:

- review the performance indicators set out in the current property management contract and seek to replace them with measurable performance indicators; and
- review the provider's performance regularly, and document key matters discussed and/or agreed at these reviews.

DFAT's response

3.32 Agreed. A review of our property management arrangements to optimise effective governance over performance, resources, assets and relationships to meet due diligence requirements and to inform a competitive tender process is in progress. The review, to be completed by 30 June 2001 will identify, define, source, cost and rank options for future domestic property management arrangements and service delivery including the development and implementation of measurable performance indicators. Based on this advice, appropriate staffing and training arrangements will be put in place to ensure best practice management of contracted services, including regular performance review and documentation.

4. Commonwealth Agency Leases

This chapter presents the survey results for Commonwealth agency leases in relation to lease duration and arrangements, the quality of accommodation leased by Commonwealth agencies, the distribution of space, expenditure on leased space and leased space density. Results for case study agencies are also presented.

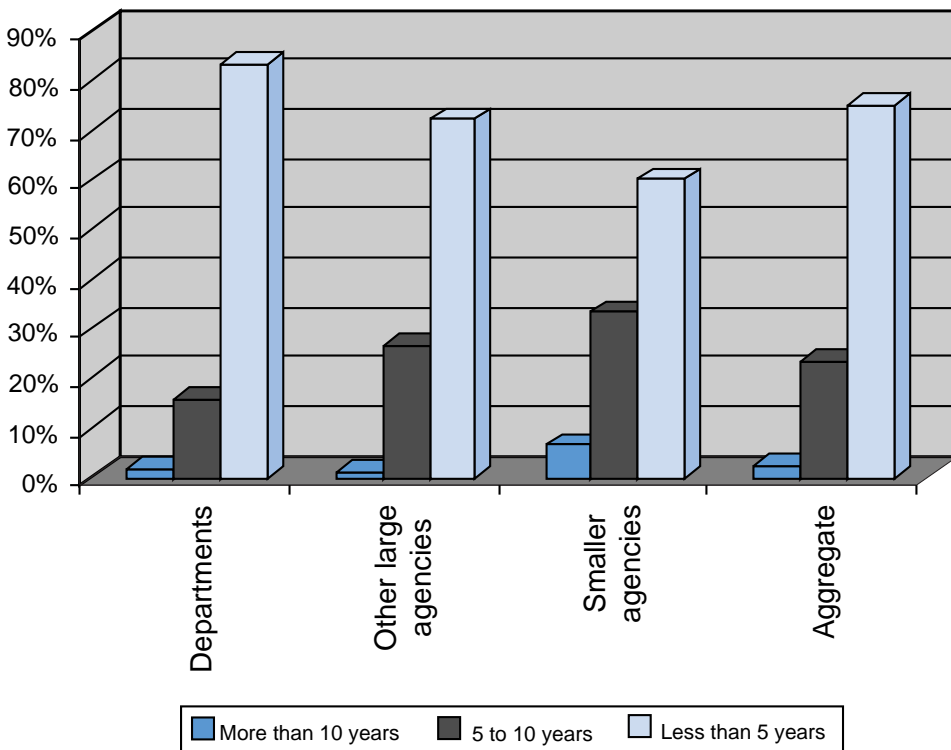
Profile of leases

Lease duration

4.1 The following Figure 4.1 sets out the duration of leases held by respondent agencies at 30 June 2000.

Figure 4.1

Duration of Leases held at 30 June 2000 by Agency Category and in Aggregate.



4.2 Figure 4.1 indicates that short-term leases are more common amongst the agencies. More than 70 per cent of the 1505 leased office properties covered in the survey were leased for fewer than five years. Less than 10 per cent of presently active leases have lease terms in excess of ten years. This lease-term profile is in line with the profile of the NSW State Government's leased office property portfolio in December 1997 where over 80 per cent of all leases held were for periods of 10 years or less.³⁰

4.3 Centrelink and Health follow the pattern shown in the above Figure, with the majority of their leases being for periods of fewer than five years. In terms of the number of leases, the majority of DFAT's leases were for terms of between five and ten years. However, the lease of the RG Casey Building in Canberra represents 88 per cent of the department's annual rental charges, and has a lease term of greater than 10 years.

Health advised that the majority of the department's leases are for less than 5 years, reflecting its strategic planning for occupation of smaller leased premises. However, the majority of the department's larger premises are occupied under long-term leases to take advantage of the more favourable financial terms available through these arrangements. Smaller premises are retained on shorter terms to retain flexibility.

4.5 Although longer-term leases can result in lower per annum rentals, they involve risks to agencies because long-term accommodation requirements are more difficult to predict accurately. If an agency's accommodation requirements reduce after the lease is signed resulting in unused space, the costs to the agency may be in excess of the higher priced short-term leases. However, for those agencies with a core level of staffing, there are advantages in longer-term leases. The high proportion of shorter-term leases suggests a preference for flexibility rather than the relative rigidity of longer-term leases.

³⁰ *Government Office Accommodation*, NSW Auditor-General, 1997.

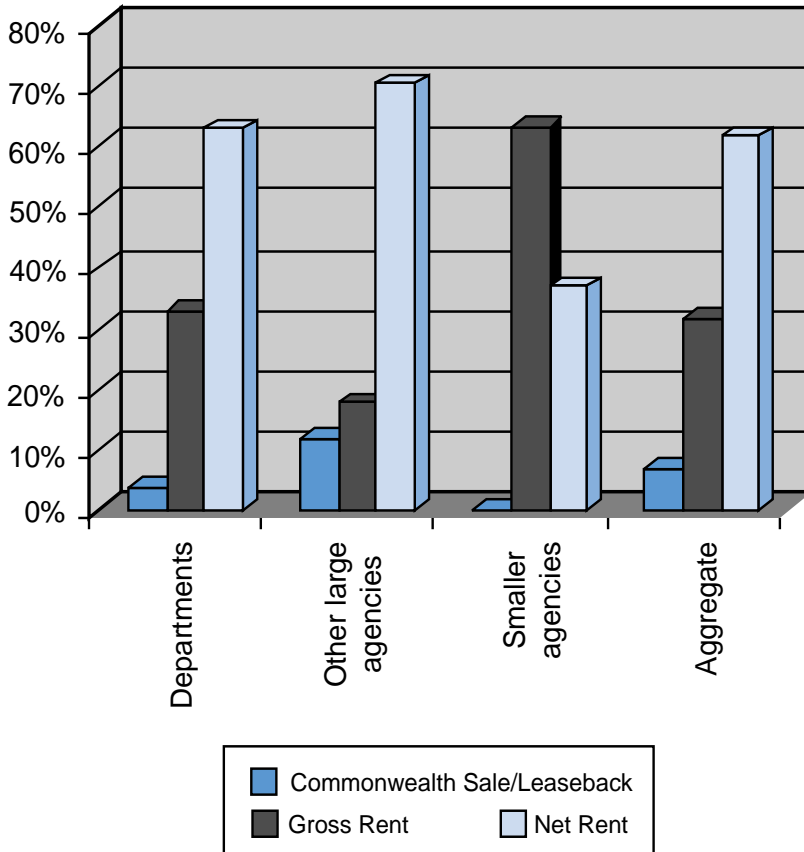
Leasing arrangements

4.6 The following Figure 4.2 sets out the type of leases found in respondent agencies at 30 June 2000. They were either:

- gross rent leases³¹;
- net rent leases³²; or
- Commonwealth sale/leaseback leases.³³

Figure 4.2

Percentage of Lease Arrangements at 30 June 2000 by Agency Type and in Aggregate



³¹ A gross rent lease is a lease where the cost of rent for the property *includes* an allowance for outgoings/property operating expenses (eg, operation of air-conditioning, common area light and power, operation of lifts during normal office hours).

³² A net rent lease is a lease where the cost of rent for the property *excludes* an allowance for outgoings/property operating expenses (ie, the tenant is responsible for *all* outgoings/property operating expenses).

³³ The data collected does not indicate whether Commonwealth sale/leaseback arrangements are gross or net, yet as these are a small proportion of the total leases for all respondent agencies this is not of major concern.

4.7 The majority of leases for departments and other large agencies were net rent leases. These usually operate in newer buildings where there is the capability to measure outgoings for each tenant (ie, separate metering of consumption and associated costs). For most leases, departments and other large agencies are accepting responsibility for payment of all outgoings associated with leases. This situation can increase agency expenditure: for example, if these agencies occupy inefficient buildings then they are responsible for potentially burdensome outgoings expenses. However, they may also be able to manage and improve efficiency in this type of situation and benefit from reduced consumption and associated costs.

4.8 In contrast to departments and other large agencies, smaller agencies appear to have a preference for gross rent leases where they have the authority to do so. This was also the case with DFAT and Health.³⁴

4.9 With gross rent leases, the potential exists for rent to include an allowance for the inefficient operation of building services (eg. air conditioning and lifts). In this situation there is little incentive for the lessor to improve building efficiency, meaning the lessee has less influence/control over costs.

4.10 The ANAO has reported previously on Commonwealth agencies' compliance with the Commonwealth's energy efficiency policy in *Energy Efficiency in Commonwealth Operations*, Audit Report No.47, 1998–99.³⁵ That policy required all agencies to ensure that all newly constructed or substantially refurbished commercial buildings where the agency is majority-tenanted meet Commonwealth building energy use guidelines. A low level of compliance was found in 1998–99. One reason for the low level compliance was that the *Commonwealth National Lease* (CNL) had not been revised to reflect the requirements of the Energy Policy. Also at the time of this audit, the CNL had not been revised to reflect the Commonwealth's Energy Policy.

³⁴ Centrelink does not maintain gross or net rent details on its property management system, however this information can be sourced by Centrelink from original lease documents when required.

³⁵ ANAO, *Energy Efficiency in Commonwealth Operations*, Report No. 47 of 1998–99, ANAO, Canberra, 1999.

4.11 The Government's energy efficiency policy does not dictate a preference for either gross or net rent leases. The policy³⁶ states that new lease agreements should not include any provision permitting the recovery from the tenant of the cost of energy use by central building services during normal office hours. This seeks to ensure that building owners have an incentive to improve the energy efficiency of central building services. Agencies should isolate the cost of energy from other outgoings. This shows transparency of energy costs which acts as an incentive for the agency to ensure that costs are kept to a minimum.

4.12 Gross and net rent leases each have their own advantages and disadvantages. When agencies are negotiating leases, they should be aware of the risks and benefits associated with these leases. Appendix 4 sets out the advantages and disadvantages of gross and net rent leases.

Quality of accommodation

4.13 The quality of Commonwealth leased office accommodation over five quality classes is summarised in Figure 4.3.³⁷ Overall, agencies appear to be leasing accommodation of a mid-range, Grade B quality with the majority of leased properties for all categories and in aggregate of Grade B quality.

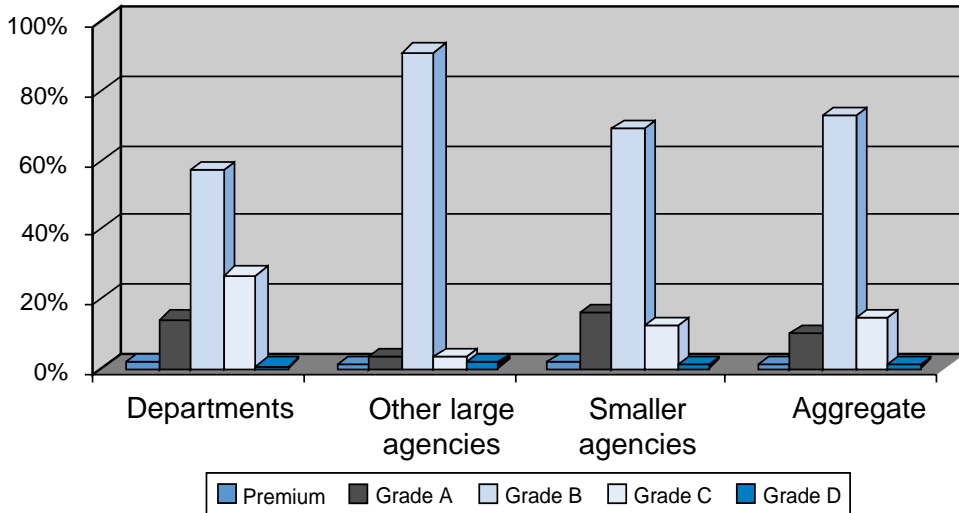
4.14 DFAT's properties are spread across all five categories, with the highest number of properties in Grade B. 76 per cent of Health's leases are for Grade C properties, while all of Centrelink's properties are either Grade B or Grade C.

³⁶ Department of Industry Science and Resources, March 2000, *Measures for improving energy efficiency in commonwealth operations*, Department of Industry Science and Resources, Canberra.

³⁷ The quality classes used throughout this analysis are defined in the glossary of terms.

Figure 4.3

Percentage of Quality of Accommodation at 30 June 2000 by Agency Type and in Aggregate



4.15 Agencies should ensure that the quality of office space is taken into account when leasing decisions are made, to ensure that appropriate standards of accommodation are being leased. The consequences of having inappropriate standards of accommodation can include:

- inefficient use of funds where higher grade accommodation attracts a higher rent;
- staff morale and productivity issues where the standard of accommodation is inadequate; and/or
- client dissatisfaction, where standards are not appropriate for service delivery.

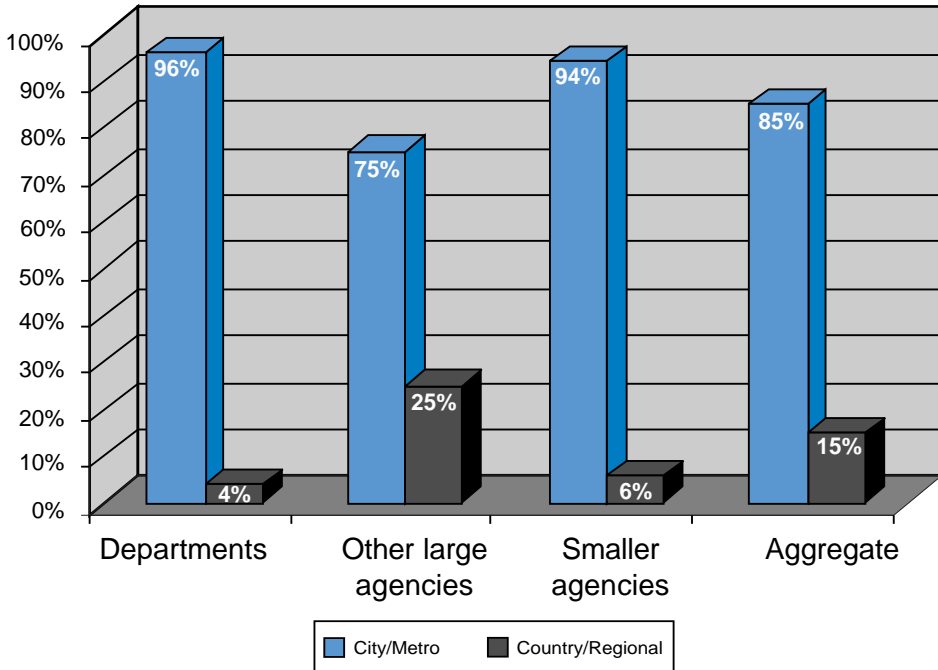
Distribution of leased space

City/country distribution

4.16 Respondent agencies leased in excess of 1.7 million square metres of office accommodation across Australia at 30 June 2000. Figure 4.4 sets out the geographical distribution of this space. The appropriateness of the city/metropolitan and country/regional distribution is important on an individual agency basis, as it is the responsibility of agencies to achieve the outcomes that they have been set to provide, whether those outcomes are in cities or in the regions.

Figure 4.4

Percentage of Geographic Distribution of Area Leased at 30 June 2000 by Agency Type and in Aggregate



4.17 Figure 4.4 indicates that the majority of leased space is located in city/metropolitan areas. The lower city/metropolitan proportion for other large agencies is affected by the location of Centrelink's offices. Centrelink is the largest agency lessee of office space in country/regional areas, with 224 leases covering almost 215 000 square metres. The next largest lessor of country/regional property to Centrelink in this category is the Australian Customs Service with 31 properties covering 7000 square metres.

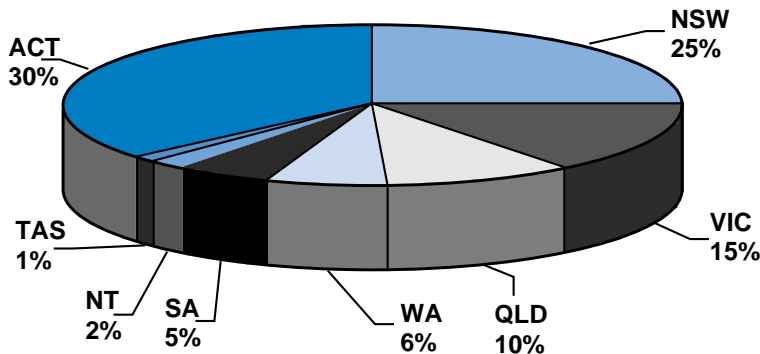
4.18 The ANAO noted that the geographic distribution of rent paid by respondent agencies, which was in excess of \$420 million for the year ended 30 June 2000, closely mirrored the geographic distribution of square metres leased. For example, other large agencies leased 75 per cent of their portfolio in city/metropolitan areas, and this represented 79 per cent of their rental expenditure.

State/territory distribution

4.19 Figure 4.5 sets out for respondent agencies the state and territory distribution of leased space, indicating where Commonwealth offices are located.

Figure 4.5

State and Territory Percentage Distribution of Area Leased at 30 June 2000



4.20 Other than for the ACT, where head offices are generally located, the representation of agencies generally correlates with the population in the states and territories.

Expenditure on leased space

Analysis and benchmarks³⁸

4.21 Respondent agencies provided information for the year ended 30 June 2000, on the following items for state/territory, city/metropolitan and country/regional offices:

- rental expenditure;
- outgoings expenditure;
- leased area in square metres; and
- number of leases.

4.22 This has enabled an analysis of rental expenditure and outgoings expenditure expressed in dollars per square metre (\$/sqm) against established benchmarks. An overview of this data from the respondent agencies is presented below in Table 4.1.

³⁸ For the purposes of this analysis, case study figures have not been separately reported.

Table 4.1
Overview of Survey Results

Agency	Rental for the year ended 30.06.00 \$	Outgoings for the year ended 30.06.00 \$	Sqm Leased as at 30.06.00	Number of Leases as at 30.06.00	City/Metropolitan		Country/Regional	
					% of Leased Area	% of Rental Costs	% of Leased Area	% of Rental Costs
Departments	140 144 180	23 157 688	615 075	635	96	96	4	4
Other large agencies	229 204 600	18 569 422	952 670	623	79	75	21	25
Smaller agencies	50 985 909	12 275 122	205 985	247	96	94	4	6
Total	420 343 689	54 002 232	1 773 729	1 505	87	85	13	15

4.23 The ANAO has nominated rental benchmarks from the *Commercial Property Monitor (CPM) Research Sales and Leasing Monitor and the Property Council of Australia Office Market Report*³⁹ as these benchmarks were considered the most appropriate for comparison against Commonwealth leasing.

4.24 The benchmarks for city/metropolitan leases are shown in Table 4.2. Benchmarks for rentals and outgoings in country/regional areas are not available.

Table 4.2
Rental and Outgoings Benchmarks for Capital Cities

Capital City	Rental Benchmark ⁴⁰ (\$/sqm)	Outgoings Benchmark ⁴¹ (\$/sqm)
NSW	350	63
VIC	180	48
QLD	285	58
WA	165	50
SA	210	n/a
TAS	180	n/a
NT	n/a	n/a
ACT	250	43

n/a: not available.

³⁹ These two sources are used to annually update the propertyweb website, (www.propertyweb.com.au). The data collected by CPM come from various market sources for various rental types.

⁴⁰ Benchmark rentals have been sourced from the Commercial Property Monitor Research web site.

⁴¹ Benchmark outgoings for B and C quality properties have been sourced from the Property Council of Australia.

4.25 Rental benchmarks for July 2000 are being used here to compare rentals and outgoings, which were, in some cases, negotiated in the early 1990s. For this reason benchmarks should be used cautiously.

Rental expenditure—city/metropolitan leases

4.26 On average, the majority of respondent agencies are paying above the benchmark for rentals in city/metropolitan areas other than in NSW, as shown in Table 4.3. The Commonwealth is the largest influence on the market in the ACT. There, departments and smaller agencies were paying more than ten per cent above the benchmarks.

Table 4.3

Respondent Agencies' City/Metropolitan Rentals per Square Metre for the year ended 30 June 2000

<i>State/ Territory</i>	<i>Benchmark (\$/sqm)</i>	<i>Departments (\$/sqm)</i>	<i>Other large agencies (\$/sqm)</i>	<i>Smaller agencies (\$/sqm)</i>
<i>NSW</i>	<i>350</i>	<i>287</i>	<i>330</i>	<i>352</i>
<i>VIC</i>	<i>180</i>	<i>209</i>	<i>221</i>	<i>198</i>
<i>QLD</i>	<i>285</i>	<i>310</i>	<i>281</i>	<i>214</i>
<i>WA</i>	<i>165</i>	<i>196</i>	<i>229</i>	<i>224</i>
<i>SA</i>	<i>210</i>	<i>231</i>	<i>321</i>	<i>328</i>
<i>TAS</i>	<i>180</i>	<i>253</i>	<i>303</i>	<i>238</i>
<i>NT</i>	<i>n/a</i>	<i>283</i>	<i>222</i>	<i>276</i>
<i>ACT</i>	<i>250</i>	<i>294</i>	<i>256</i>	<i>295</i>

Highlighted figures are 10 per cent or more in excess of benchmarks.

n/a: not available.

4.27 The fact that the majority of leases held by respondent agencies are for terms of up to five years (ie. short term) contributes to higher rental costs. The general outcome here indicates that agencies may not be making the most efficient use of their funds. In order to ensure that agencies are achieving value for money leasing deals, particular attention should be paid to market rents available at the time of lease negotiations, so that informed leasing decisions can be made.

Rental expenditure—country/regional leases

4.28 Average rentals in country/regional areas for the financial year ended 30 June 2000, according to respondent agencies, are outlined in Table 4.4.

Table 4.4**Respondent Agencies' Country/Regional Rentals per Square Metre for the year ended 30 June 2000**

<i>State/ Territory</i>	<i>Departments (\$/sqm)</i>	<i>Other large agencies (\$/sqm)</i>	<i>Smaller agencies (\$/sqm)</i>
<i>NSW</i>	<i>247</i>	<i>190</i>	<i>195</i>
<i>VIC</i>	<i>153</i>	<i>162</i>	<i>157</i>
<i>QLD</i>	<i>238</i>	<i>227</i>	<i>183</i>
<i>WA</i>	<i>223</i>	<i>206</i>	<i>141</i>
<i>SA</i>	<i>206</i>	<i>177</i>	<i>166</i>
<i>TAS</i>	<i>73</i>	<i>213</i>	<i>176</i>
<i>NT</i>	<i>231</i>	<i>197</i>	<i>77</i>
<i>ACT</i> ⁴²	<i>n/a</i>	<i>n/a</i>	<i>n/a</i>

n/a: not available.

4.29 It is generally cheaper to rent office space in country/regional areas than in urban/metropolitan areas. The data on country/regional rents in Table 4.4 support this conclusion, given that they are generally significantly lower than in the corresponding city/metropolitan areas and against city/metropolitan benchmarks.

Expenditure on outgoings—city/metropolitan leases

4.30 According to respondent agencies, the costs of outgoings paid by agencies in city/metropolitan areas are largely within the benchmarks. This can be seen in Table 4.5.

Table 4.5:**Respondent Agencies' City/Metropolitan Outgoings per Square Metre for the year ended 30 June 2000**

<i>State/ Territory</i>	<i>Benchmark (\$/sqm)</i>	<i>Departments (\$/sqm)</i>	<i>Other large agencies (\$/sqm)</i>	<i>Smaller agencies (\$/sqm)</i>
<i>NSW</i>	<i>63</i>	<i>15</i>	<i>37</i>	<i>44</i>
<i>VIC</i>	<i>48</i>	<i>43</i>	<i>34</i>	<i>56</i>
<i>QLD</i>	<i>58</i>	<i>40</i>	<i>35</i>	<i>44</i>
<i>WA</i>	<i>50</i>	<i>122</i>	<i>35</i>	<i>85</i>
<i>SA</i>	<i>n/a</i>	<i>34</i>	<i>26</i>	<i>31</i>
<i>TAS</i>	<i>n/a</i>	<i>44</i>	<i>44</i>	<i>11</i>
<i>NT</i>	<i>n/a</i>	<i>67</i>	<i>38</i>	<i>28</i>
<i>ACT</i>	<i>43</i>	<i>33</i>	<i>44</i>	<i>118</i>

Highlighted figures are 10 per cent or more in excess of benchmarks.

n/a: not available.

⁴² All available office accommodation in the ACT is classed as city/metropolitan.

4.31 Where costs exceed the benchmark by a large amount (for example, departments and smaller agencies in WA), there may be a higher proportion of net rent leases. Net rent leases exclude an allowance for some outgoings, and as a result, they will appear as an outgoing expense rather than being subsumed in rental figures. High outgoings figures may also be explained by inefficient buildings (where, for example, air conditioning costs may be higher), inefficient management practices on the part of the agency, or longer than normal hours of operation.

Leased space density

4.32 For the purposes of this analysis, a density benchmark range of 15 to 25 square metres of leased office space per full-time equivalent employee has been adopted. The ANAO set a lower and upper range which took into consideration benchmarks such as those contained in a report prepared by the Government Real Estate Group titled *National Office Accommodation Benchmarking—Government Real Estate Groups Working in Partnership*, October 1999. The nominated upper range allows for those agencies that have a diverse geographical network of office locations and a larger proportion of regional offices that tend to achieve less efficient density ratios (that is, a greater number of smaller offices leads to reduced opportunities for economies of scale).

4.33 Where an agency leases more than 15 to 25 sqm/person, this indicates that it may be renting space in excess of its needs and/or poorly utilising existing space. The effect of this may be higher than necessary payments of rent and outgoings.

4.34 Appendix 5 contains survey data on leased space density. The results of the survey show that in general in both city/metropolitan and country/regional areas, densities are in excess of the benchmark range. These low densities may result in unnecessary rent and outgoings expenditure. Estimates of the latter could be reduced if contractors utilise space rented by these agencies.

4.35 In terms of the three case study agencies, Health, with a density of 21 sqm/person, was the only agency with a density within the benchmark range. DFAT and Centrelink both had densities of 27 sqm/person.

4.36 DFAT attributes its relatively low density to the RG Casey Building, which represents over 80 per cent of DFAT's leased office accommodation. The RG Casey Building contains over 16 000 sqm of space that DFAT has identified as special purpose space. This includes lecture rooms, laboratories, training and meeting rooms, crisis centres and various other special purpose areas that are not normally found in conventional office accommodation.

4.37 Centrelink has its own space standards which range from 11.5 sqm per seat for Call Centres up to 34 sqm/person for customer contact staff in small offices. In addition, Centrelink reported that it reviews its leases annually with an emphasis on identifying opportunities to reduce its space requirements.

4.38 Estimates of the cost of above-benchmark space⁴³ being rented by respondent survey agencies at 30 June 2000 are set out in Tables 4.6 and 4.7. The tables indicate that these agencies are paying approximately \$89 million per annum for this above-benchmark space and an additional \$6.5 million in outgoings⁴⁴, re-emphasising the point made earlier in this report that agencies should periodically review their space allocation against their property needs.

Table 4.6

Estimate of Above-Benchmark Rent Across Location and Respondent Agency Categories

<i>Area</i>	<i>Agency type</i>	<i>Estimated above benchmark rent per annum \$</i>	<i>Actual rent year ended 30.06.00 \$</i>	<i>Above benchmark rent as a % of actual rent</i>
City/Metropolitan	Departments	27 536 209	135 170 742	20
	Large Agencies	24 904 440	181 434 054	14
	Smaller agencies	18 222 096	48 938 215	37
Subtotal	All	70 662 745	365 543 011	19
Country/Regional	Departments	1 951 423	4 973 438	39
	Other large agencies	15 100 328	47 770 546	32
	smaller agencies	1 275 226	2 047 694	62
Subtotal	All	18 326 977	54 791 678	33
Total		88 989 722	420 334 689	21

⁴³ Above benchmark space is the space rented at 30 June 2000 after subtracting 25 square metres per person and any vacant space identified by respondent agencies.

⁴⁴ As rent, this estimate represents approximately \$71 million (or 79 per cent) in city/metropolitan areas and approximately \$18 million (or 21 per cent) in country/regional areas. In terms of outgoings, this estimate represents approximately \$4.7 million (or 72 per cent) in city/metropolitan areas and approximately \$1.8 million (or 28 per cent) in country/regional areas.

Table 4.7**Estimate of Above-Benchmarks Outgoings Across Location and Respondent Agency Categories**

<i>Area</i>	<i>Agency type</i>	<i>Estimated above benchmark outgoings per annum \$</i>	<i>Actual outgoings year ended 30.06.00 \$</i>	<i>Above benchmark outgoings as a % of outgoings</i>
City/Metropolitan	Departments	1 584 047	21 824 431	7
	Other large agencies	1 613 129	16 767 338	10
	Smaller agencies	1 495 619	11 754 456	13
Subtotal	All	4 692 794	50 346 225	9
Country/Regional	Departments	187 306	1 333 257	14
	Other large agencies	1 559 273	1 802 084	87
	Smaller agencies	67 933	520 666	13
Subtotal	All	1 814 512	3 656 007	50
Total		6 507 306	54 002 232	12

4.39 Agencies should set density targets, taking account of industry benchmarks, and monitor their performance against these benchmarks. Agencies may need a number of density targets. For example, lower densities may be developed for country/regional offices or smaller offices, and higher densities may be set for call centres or large offices where economies of scale are likely to be achieved.

4.40 The use and function of the leased space need to be considered in arriving at an appropriate density benchmark. For example, as not all departmental staff have significant amounts of face-to-face customer contact, large customer contact areas are not always a feature of their accommodation. Conversely, other large agencies and smaller agencies may be expected to feature customer contact areas, which consume a significant amount of space. This may explain why departments have higher density than other large agencies and smaller agencies.

Summary

4.41 The survey and case study results indicate that agencies could improve their long term property management, leading to possible reductions in space utilisation and expenditure on leased properties and associated property management through:

- focusing on achieving market rentals;
- setting density targets, taking account of industry benchmarks, and monitoring their performance against these benchmarks. Those targets can be incorporated into strategic property plans; and

- where their use of space is significantly above benchmarks, they should review their space allocation against their property needs. Consideration can then be given to divesting surplus space through such methods as sub-leasing.

5. Lease Reviews at Case Study Agencies

This chapter sets out the findings in relation to the sample of leases reviewed at the case study agencies.

5.1 A sample of leases was reviewed at each of the case study agencies as shown in Table 5.1.

Table 5.1
Sample of Leases Reviewed in Case Study Agencies

<i>Agency</i>	<i>Number of leases at 30.06.00</i>	<i>Number of Leases Reviewed in Sample</i>
DFAT	15	14
Health	37	7
Centrelink	471	22
Total	523	43

5.2 Appendix 3 sets out details of the leases reviewed.

5.3 These leases were reviewed against the terms and conditions contained in the Commonwealth National Lease and against terms and conditions that would be expected in better practice private sector leases.

5.4 Terms and conditions expected to be found in the leases were concerned with:

- rent (cost per annum);
- rent reviews (frequency/dates/methods);
- options for lease renewal;
- responsibility for payment of outgoings;
- lessor's responsibility and frequency of cleaning, re-painting and re-carpeting;
- hours of use/operation of premises; and
- performance parameters for operation of air conditioning and lifts.

5.5 Data on these parameters from the case studies were compared with survey results where appropriate, with additional analyses conducted where issues were not raised in the survey, and agencies' responses sought. This chapter sets out the findings of the two major issues that arose from the lease reviews in the case study agencies.

5.6 ANAO's analysis also incorporated a review of a sample of leases for Commonwealth sale/leaseback properties. Finance negotiated these leases as part of the Commonwealth's property sales program. These leases were modelled on the Commonwealth Tenant's Lease which was developed by the Commonwealth Property Committee in consultation with key stakeholders including the Australian Government Solicitor and selected tenants.

5.7 From discussions with case study agency representatives and reviews of relevant documentation, it is apparent that agencies had limited influence over the terms and conditions of the leases for properties formerly owned by the Commonwealth and now leased by Commonwealth agencies from the private sector because these were settled in the context of the property sales, referred to above. Where agencies have leases with terms and conditions over which there was limited scope for negotiation, agencies may be left with leases that are not in accordance with their current and/or future property needs. This may impact on their ability to efficiently and effectively manage these leases as a component of their property portfolios.

Case study findings

5.8 The findings set out below describe the major issues identified in the review of the 43 leases across the three case study agencies.

Energy efficiency

5.9 As set out in Chapter 4, the Government's energy efficiency policy does not dictate a preference for either gross or net rent leases. The policy states that new lease agreements should not include any provision permitting the recovery from the tenant of the cost of energy use by central building services during normal office hours. This seeks to ensure that building owners have an incentive to improve the energy efficiency of central building services. Agencies should isolate the cost of energy from other outgoings. This exposure of energy costs acts as an incentive for the agency to ensure that costs are kept to a minimum.

5.10 The lease for the RG Casey Building, for which DFAT is the lessee, did not comply with the Government's energy efficiency policy. The Government's energy policy was announced on 20 November 1997. The RG Casey Building was at this time already out to tender. The Government's 20 November energy policy was interpreted and promulgated to Commonwealth agencies on 15 April 1998. Because the RG Casey Building was sold on 24 April 1998, there was little time between announcement of the Government's energy policy and the sale

for prospective tenders to be advised of the Government’s new policy and for this matter to be addressed in final negotiations before the sale and leaseback were completed. The energy costs for the building are high: an independent assessment in May 2001 commissioned by DFAT rated the building’s energy management systems as being at the lowest level on a five point scale. The independent assessment concluded, that amongst other factors, current lease and service arrangements have restricted DFAT’s access to detailed energy consumption costs that could assist it to reduce energy costs.

5.11 The audit findings underline the importance of the promotion of the energy efficiency policy. Agencies should also seek advice from the Australian Greenhouse Office (AGO) on leasing provisions that affect the recovery of energy costs for building central services during working hours.

Rent review provisions and ratchet clauses

5.12 Lease agreements can provide for a rent review. This has the effect of re-determining the rent in accordance with an agreed method. Common methods of rent review include an adjustment to market, in line with movements in the Consumer Price Index, or a fixed percentage or dollar increase.

5.13 Rent review provisions of the sample of 43 leases examined are shown in Table 5.2.

Table 5.2

Rent Review Provisions in Sample of Leases Reviewed

<i>Method of Rent Review</i>	<i>Number of Leases</i>	<i>Number of Leases with Ratchet Clauses</i>
Market	27	26
CPI	7	6
Fixed percentage or dollar	6	n/a ⁴⁵
No rent review provision	3	n/a ⁴⁶
Total	43	32

n/a: not available.

⁴⁵ A fixed percentage or dollar increase implies that decreases in rent are not possible under the rent review provisions of these leases.

⁴⁶ No rent review provisions were contained in these leases given their short term.

5.14 Of the 34 leases with rent review provisions where there could theoretically be a downwards rent review (ie. those that are reviewed to market or to the CPI), 32 of those leases contained provisions precluding such a downwards review. A lease clause that does not allow the amount of rent to decline below the amount payable just prior to the rent review, is termed a ratchet clause. Depending on market forces at the time of the rent review, a ratchet clause may prevent the rent being reviewed to a true market rent. Finance considered that the inclusion of ratchet clauses is standard commercial practice and therefore used in other leases that will generally allow rents not to fall.

5.15 Of the 43 leases examined, 16 were for properties that were previously owned by the Commonwealth. All 16 of these leases contained ratchet clauses. Finance negotiated these leases, referred to as Commonwealth sale/leaseback properties, as part of the sale arrangement, and agencies had limited influence over the terms and conditions of the leases.⁴⁷ Finance affirmed that, notwithstanding, many agencies were able to reduce rental costs, space requirements, and lease terms during these negotiations to suit their program delivery requirements.

5.16 ANAO requested further information on seven of the 16 Commonwealth sale/leaseback leases to determine whether the case study agencies obtained independent legal advice or valuations prior to signing these leases.

5.17 Out of the seven leases, independent legal advice was obtained for four of the leases and internal legal advice was obtained on the other three leases. It is advisable to obtain legal advice where such arrangements are entered into to safeguard agencies' interests. The fact that legal advice was obtained is considered satisfactory.

5.18 Valuations were sought by agencies for three out of the seven Commonwealth sale/leaseback leases reviewed. Although these agencies had limited influence over the provisions of these leases, the FMA Act stipulates the requirement for the efficient and effective use of funds, and it would have been difficult for agencies to determine whether they were receiving value for money without an independent valuation being undertaken. Whether or not agencies obtained independent valuations, the leases would have been deemed to be in place by Finance. Agencies should seek to avoid ratchet clauses in their future lease arrangements, to ensure that they are only exposed to normal market rentals. If agencies are paying in excess of market rentals due to the existence of ratchet clauses, this may indicate inefficient use of Commonwealth funds.

⁴⁷ The Financial Management and Accountability Act requires chief executives to manage the affairs of their agency in a way that promotes efficient, effective and ethical use of Commonwealth resources.

5.19 This is particularly pertinent within the Canberra market which is generally underpinned by a significantly high proportion of office accommodation occupied by Commonwealth Government agencies compared with other major centres, which by comparison, feature a more even representation of government (all tiers) and private sector occupants. There has been a reduction in the size of many Commonwealth Government agencies in recent years. In turn, this reduction contributed to a significant decline in Canberra's property market.

5.20 Office accommodation leases negotiated prior to the decline in the Canberra property market were negotiated during a more buoyant period that created higher rentals compared with those that would have otherwise been negotiated subsequent to the downturn. The effect of a ratchet clause in this situation, for leases determined when the Canberra market was buoyant before the subsequent decline in the market, prevents a 'true market' rental being reflected in subsequent rent reviews, particularly during periods when the prevailing market dictates lower rental values.

5.21 Except during a downturn in the economy, this situation would not be expected to arise in other major centres where there is generally a more evenly balanced occupant profile (ie. government versus private).

5.22 Notwithstanding the above, the impact of a ratchet clause on the sample of leases can only be quantified based on a case by case assessment at each individual rent review.

5.23 The largest building in the ANAO's sample for which there was a sale/lease back arrangement was the RG Casey Building in Canberra. Finance advised that DFAT had been provided with a copy of the proposed lease in late 1996, some twelve months before documents were finalised for the sale. DFAT had signed a long term lease for this building, with the lease expiring in 2012. The lease for this building represented 88 per cent of DFAT's annual rental expenditure for domestic properties. DFAT indicated that it agreed to the lease only because of the deeming deadline imposed on the Department, and expressed serious reservations about a number of commercial aspects of the final lease.

5.24 Finance could not agree to vary certain provisions of the lease because it considered that DFAT sought to vary some of the essential commercial terms of the lease, including the level of rent, rent review provisions, lease terms, and arrangements for payment of energy costs, contrary to the fundamental principle of user pays. Finance stated that this would have been detrimental to the Commonwealth's divestment program. Finance further advised that the,

terms in the lease had underpinned the original decision to construct the RG Casey Building. This was normal commercial practice when a pre-commitment agreement is entered for the construction of properties. The lease, however, was significantly modified to address DFAT's concerns. Additionally, the building was purpose built for DFAT pursuant to a 'pre-commitment' agreement. The nature of its terms and conditions need to be compared with other government leases procured by this method. The RG Casey Building was never available in the 'market'.

Summary

5.25 From this analysis it is evident that the case study agencies are managing Commonwealth sale/leaseback leases that contain provisions over which they had limited ability to negotiate. This can inhibit the agencies' ability to ensure that resources are used efficiently and effectively.

5.26 In order to enhance the efficiency and effectiveness of property management:

- in future, when agencies are negotiating leases with private sector landlords, they should seek to avoid rental ratchet clauses in these agreements; and
- agencies should ensure that future lease agreements are in compliance with the Government's energy efficiency policy by not including any provisions permitting the recovery from the agency of the cost of energy use by central building services during normal office hours.



Canberra ACT
27 June 2001

P. J. Barrett
Auditor-General

Appendices

Appendix 1

Survey Instrument



AUSTRALIAN NATIONAL AUDIT OFFICE

**QUESTIONNAIRE ON
COMMONWEALTH AGENCY
MANAGEMENT OF LEASED
OFFICE PROPERTY**

13 JUNE 2000

Instructions

This questionnaire on Commonwealth Agency Management of Leased Office Property within Australian Public Service (APS) Agencies is being undertaken by the Australian National Audit Office (ANAO) as part of a performance audit being conducted under Part 5, Division 1 of the *Auditor-General Act 1997*. **A response to this survey is required under Sub-Section 32 (1) and (2) of the Auditor-General Act 1997.**

The survey has been forwarded to approximately 70 Commonwealth agencies that are covered by the *Financial Management and Accountability Act 1997*.

ANAO is being assisted by Sinclair Knight Merz Pty Ltd with this questionnaire.

Included in this package is:

1. a questionnaire document
2. a glossary of terms.

Please ensure that you have read the attached glossary of terms prior to completing the questionnaire. If you have any questions in relation to the questionnaire, please do not hesitate to contact Darron Cook from Sinclair Knight Merz Pty Ltd.

The **questionnaire and this page** are required to be completed and returned by **30 June 2000**

by fax or post to:

Darron Cook
Sinclair Knight Merz Pty Ltd
PO Box 2500
Malvern Vic 3144
Fax: (03) 9248 3400
Phone: (03) 9248 3503

After you complete the questionnaire, please answer the following:

1. Did you receive assistance in completing this questionnaire? • Yes • No

If **yes**, please specify (tick as many as applicable):

- Out-sourced Service Provider
- Agency staff in other locations
- Other, please specify: _____

2. HOW DID YOU RATE THIS QUESTIONNAIRE IN TERMS OF DIFFICULTY TO COMPLETE?

- Simple
- Difficult
- Undecided

3. Please provide the details of the person who completed this questionnaire. This will help us if we have any queries in relation to your responses.

Name:

Position:

Signed:

Agency:

Date:

Phone:

Thank you for your assistance

Questionnaire

This questionnaire is being conducted as part of the ANAO's performance audit of Commonwealth Agency Management of Leased Office Property under Part 5, Division 1 of the *Auditor-General Act 1997*.

This questionnaire only concerns **office property leased by your agency from a property owner other than the Commonwealth Government** (ie. **excludes** Commonwealth owned office property).

Please read the attached 'Glossary of Terms' prior to completing the questionnaire.

If insufficient space is provided for comments, **please attach additional information**.

Strategic/Forward Planning for Your Leased Office Property

1. Do you have a current strategic plan for your *leased* property portfolio?
 - No
 - Yes → if **Yes**, please attach a copy to your completed questionnaire.

2. If yes, for what period is your strategic plan valid? (eg.1996–2001) _____

3. Is your strategic plan aligned with your program delivery objectives?
 - No
 - Yes → if **Yes**, briefly explain how: _____

4. Do you have a current business continuity plan (BCP)?
 - No
 - Yes → if **Yes**, please comment on how your BCP takes into account leased Office property issues: _____

Procurement and Management of Your Leased Office Property

- 5a. **Currently**, approximately what proportion of leased office property management activities are conducted in-house/out-sourced.

	In-house (%)	Out-sourced (%)	Total
Leased Office Property Management			100%
Total cost pa. (1999–2000 - projected)	\$	\$	\$

- 5b. Please indicate the **current** number of Full-Time-Equivalent (FTE) agency staff engaged in leased office property management activities, by level of experience.

	< 5 years property experience	5 years + property experience
Number of agency staff nationally (FTE)		

- 5c. Please indicate the procurement method(s) used to obtain your out-sourced leased office property management services (tick as many as applicable)

	Single Quote (direct engagement)	Select Tenders (by invitation)	Open Tenders (advertised)	Other (go to 5d)
Out-sourced leased office property management services	•	•	•	•

- 5d. If "other" for procurement methods are used, please specify:

- 5e. Which level(s) of your agency are delegated responsibility for approval of new leases/lease renewals (tick as appropriate)?

	SES	Non-SES
Leases with annual rental costs <i>less than or equal to</i> \$0.5 million pa.	•	•
Leases with annual rental costs <i>more than</i> \$0.5 million pa.	•	•

Profile of Your Leased Office Property

6a. Please complete the following for your leased office property portfolio as at 30 June 2000 (projected):

City/Metropolitan							
State	Rental Cost incl. Parking (\$)	Outgoings (\$)	Total Area Leased (sqm)	Number of Leases	No. Staff Occupied (FTE)	Vacant Area (sqm)	Total Fitout / Refit Costs (\$)
NSW							
VIC							
QLD							
WA							
SA							
TAS							
NT							
ACT							

Country/Regional							
State	Rental Cost incl. Parking (\$)	Outgoings (\$)	Total Area Leased (sqm)	Number of Leases	No. Staff Occupied (FTE)	Vacant Area (sqm)	Total Fitout / Refit Costs (\$)
NSW							
VIC							
QLD							
WA							
SA							
TAS							
NT							
ACT							

6b. What is the total cost of your vacant leased office property:

Annual (1999–2000 - projected) \$ _____

Cumulative (from date vacated until end of lease - projected) \$ _____

6c. Provide the total number of existing leases that fall into the following lease term categories:

Category	Total No.
Less than 5 yrs	
5 to 10 yrs	
More than 10 yrs	

6d. Provide the total number of existing leases that fall into the following lease type categories:

Category	Total No.
Net Rent Lease	
Gross Rent Lease	
C'wealth Sale/Lease-back	

6e. Provide the total number of existing leases that fall into the following property quality categories:

Category	Total No.
Premium	
Grade A	
Grade B	
Grade C	
Grade D	

Fitout/Refit of Your Leased Office Property

7a. What is the total written down value (WDV) of your fitout/refits as at 30 June 2000 (projected)?

\$ _____

7b. What is the total number of leases as at 30 June 2000 (projected) where the cost of the Original fitout and/or subsequent refits is included in the rent? _____

Property Management System (PMS)

- 8a. Does your agency, either directly or through an out-sourced service provider, use a PMS?
 • Yes • No
- 8b. If **no** to 8a, what method is used to manage your agency's **leased office property**?

- 8c. If **yes** to 8a, is your PMS operated/updated/maintained in-house, or out-sourced?
 • in-house • out-sourced
- 8d. If your PMS is operated/updated/maintained **in-house** please answer 8e. to 8i., if **out-sourced** go to Q9.
- 8e. In which year was your agency's PMS purchased/established? _____
- 8f. What was the total cost to purchase/establish your PMS? _____
- 8g. Is your PMS custom-developed, or a Commercial-Off-The-Shelf (COTS) product?
 • Custom-developed • COTS → If **COTS**, please provide the proprietary name:

- 8h. On which software platform does your PMS operate? (eg. Dbase, MS Access, etc.)

- 8i. What are the key attributes of your PMS and what is the data on your PMS?
 (Tick as many as applicable.)
- Linked to your agency's financial reporting system (eg. ORACLE Financials, SAP, etc)
 - Able to identify and report liabilities (eg. annually, quarterly, monthly, etc)
 - Lease start/end dates
 - Area leased
 - Cost of lease pa.
 - Total No. of Occupants (FTE)
 - Total vacant area
 - Cost of Original Fitout and Subsequent Refits
 - Cost of Outgoings (eg. Cleaning, Energy, Maintenance, etc.)
 - Other attributes 1 (Specify) _____
 - Other attributes 2 (Specify) _____

Other Comments

9. If you have any comments on how your approach to leased office property management could be made more efficient or simple, please specify:

Glossary of Terms	
Term	Definition
<i>Business Continuity Plan</i>	Defines the agency's approach to dealing with a break in business continuity and prescribes the steps the agency should take to recover lost business functions.
<i>Commonwealth Sale/ Lease-back</i>	Where an office property, previously owned by the Commonwealth Government, has been sold to the market and new lease agreements with pre-existing Commonwealth Government tenants (lease-back) have been negotiated as part of the sale.
<i>Fitout Costs</i>	The cost associated with the original fitout of office accommodation at commencement of a lease
<i>Full-Time-Equivalent (FTE)</i>	Actual hours of employment divided by standard hours of employment (eg. a person employed to work 20 hours out of a standard 40 hour week represents 0.5 of an FTE)
<i>Gross Rent Lease</i>	Cost of rent for a property includes an allowance for outgoings/property operating expenses (eg. operation of air-conditioning, common area light and power, and lifts during normal office hours
<i>In-house</i>	Commonwealth Agency employees
<i>Leased Office Property (for the purpose of this Audit)</i>	Predominantly office/administrative style accommodation leased from a property owner other than the Commonwealth Government Note: Includes shop-front style property leased for 'customer service' related activities, but excludes retail
<i>Metropolitan/City</i>	Includes: State Capital Cities Territory Capital Cities surrounding metropolitan areas surrounding suburban areas
<i>National Office Property Quality Grade Matrix (source: Property Council of Australia):- Premium</i>	A landmark office building located in major CBD office markets which is a pace setter in establishing rents and includes: ample natural lighting; good views/outlook; prestige lobby finish; on-site undercover parking; quality access to/from an attractive street setting; premium presentation and maintenance, state of the art technical services.
<i>Grade A</i>	High quality space including: good views/outlook; quality lobby finish; on-site undercover parking; quality access to/from an attractive street setting; high quality presentation and maintenance, high quality technical services.

continued next page

Term	Definition
<i>Grade B</i>	Good quality space with a reasonable standard of finish and maintenance. Tenant car parking facilities should be available and basic standard of technical services.
<i>Grade C</i>	Older style office space of lower quality finish and older style technical services.
<i>Grade D</i>	Poor quality space with minimal technical services. Typically, these buildings do not have central air conditioning.
<i>Net Rent Lease</i>	Cost of rent for a property excludes an allowance for outgoing/property operating expenses (ie. the tenant is responsible for all outgoing/property operating expenses)
<i>Open Tenders (Advertised)</i>	Engagement on the basis of an unlimited/open tender process whereby a need/service is usually advertised and multiple responses (tenders) are received/evaluated
<i>Outgoings/Property Operating Expenses (POE)</i>	Expenses associated with the operation and maintenance of leased office property: Include: electricity gas cleaning maintenance security costs Exclude rent (incl. car parking) fitout/refit any other capital improvement costs (eg. installation of supplementary air conditioning systems)
<i>Out-sourced</i>	External firms under a formal contract/fee for service arrangement
<i>Property Management Activities</i>	Generally includes: leasing valuations legal/contractual advice financial management and reporting PMS management contract administration maintenance management project management
<i>Refit Costs</i>	The cost associated with the subsequent fitout of office accommodation during the lease or at the lease renewal stage.
<i>Regional/Country</i>	Includes: Regional Cities smaller country cities smaller country towns

continued next page

Term	Definition						
<i>Select/Invite Tenders</i>	Engagement on the basis of more than one contractor/consultant being invited to submit quotations						
<i>Single Quote/Direct Engagement</i>	Direct engagement on the basis of a single quotation from a single contractor/consultant						
<i>Total Cost of Vacant Leased Space</i>	<p>The total cost of rent and any other expenses incurred for vacant leased office property. Note: includes instances where vacant leased space has been sub-let to third party at a lesser rental than that incurred by your agency. Any shortfall must be included in the total costs incurred for vacant leased office property. For example:</p> <table> <tr> <td>Total rental cost p.a. for 1,000sqm</td> <td>\$100 000</td> </tr> <tr> <td>Sub-let to third party at lesser rental</td> <td><u>\$50 000</u></td> </tr> <tr> <td>Total shortfall</td> <td>\$50 000</td> </tr> </table>	Total rental cost p.a. for 1,000sqm	\$100 000	Sub-let to third party at lesser rental	<u>\$50 000</u>	Total shortfall	\$50 000
Total rental cost p.a. for 1,000sqm	\$100 000						
Sub-let to third party at lesser rental	<u>\$50 000</u>						
Total shortfall	\$50 000						
<i>Vacant Leased Office Property</i>	The total area of leased office property not occupied at the time of this audit (note: excludes vacant space that has been sub-let to third party)						
<i>Valuations</i>	Rent for leases are normally reviewed to market on a regular basis (eg. every 3 years), at which point a valuation is conducted to review the level of rent based on prevailing market conditions						
<i>Written Down Value (WDV)</i>	Total original construction cost or re-valued amount less accumulated depreciation.						

Appendix 2

Survey Distribution and Responses

Summary

<i>Agency</i>	<i>Surveys Sent</i>	<i>Targeted Agencies⁴⁸</i>	<i>Responses Received</i>	<i>Response Rate</i>
Departments	17	17	13	76%
Other large agencies	10	8	9	90%
Smaller agencies	32	14	19	59%
Unsolicited agencies	—	—	3	—
Total	59	39	44	75%

Departments

<i>#</i>	<i>Agency</i>	<i>Targeted Agency</i>	<i>Response Received</i>
1	Attorney General's Department	✓	✓
2	Department of Agriculture, Fisheries & Forestry	✓	✓
3	Department of Communication, Information Technology and the Arts	✓	✓
4	Department of Defence	✓	✗
5	Department of Education, Training and Youth Affairs	✓	✓
6	Department of Employment, Workplace Relations and Small Business	✓	✗
7	Department of Environment and Heritage	✓	✗
8	Department of Family and Community Services	✓	✓
9	Department of Finance and Administration	✓	✓
10	Department of Foreign Affairs and Trade	✓	✓
11	Department of Health and Aged Care	✓	✓
12	Department of Immigration and Multicultural Affairs	✓	✓
13	Department of Industry, Science and Resources	✓	✓
14	Department of the Prime Minister and Cabinet	✓	✓
15	Department of Transport and Regional Development	✓	✗
16	Department of the Treasury	✓	✓
17	Department of Veterans' Affairs	✓	✓

continued next page

⁴⁸ Targeted agencies received personalised covering letters and two follow up telephone calls to encourage their response to the survey. Non-targetted agencies received the survey with the accompanying letter.

Other large agencies

#	Agency	Targeted Agency	Response Received
1	Aboriginal and Torres Strait Islander Commission ⁴⁹	✓	✓
2	Australian Agency for International Development	✓	✓
3	Australian Bureau of Statistics	✓	✓
4	Australian Customs Service	✓	✓
5	Australian Federal Police	✗	✓
6	Australian Geological Survey Organisation	✓	✓
7	Australian Security Intelligence Service	✗	✓
8	Australian Taxation Office	✓	✓ ⁵⁰
9	Centrelink	✓	✓
10	National Crime Authority	✓	✗

Smaller agencies

#	Agency	Targeted Agency	Response Received
1	Administrative Appeals Tribunal	✓	✓
2	Australia – Japan Foundation	✗	✗
3	Australian Centre for International Agricultural Research	✗	✓
4	Australian Competition and Consumer Commission	✓	✓
5	Australian Electoral Commission	✓	✓
6	Australian Government Solicitor	✗	✗ ⁵¹
7	Australian Greenhouse Office	✓	✗
8	Australian National Audit Office	✗	✓
9	Australian Radiation Protection and Nuclear Safety Agency	✗	✓
10	Australian Transaction Reports and Analysis Centre	✗	✗
11	Classification Board	✗	✗
12	Classification Review Board	✗	✗
13	Commonwealth Director of Public Prosecutions	✓	✓
14	Commonwealth Grants Commission	✓	✓
15	Commonwealth Superannuation Administration	✓	✓
16	Family Court of Australia	✗	✗
17	Federal Court of Australia	✗	✗

continued next page

⁴⁹ Aboriginal and Torres Strait Islander Commission (ATSIC) is not an FMA Agency, however, it was included in the survey in place of the Indigenous Land Corporation and Aboriginal and Torres Strait Islander Land Fund Reserve.

⁵⁰ Incomplete response received.

⁵¹ Australian Government Solicitor advised that they were no longer an FMA agency.

#	Agency	Targeted Agency	Response Received
18	Human Rights and Equal Opportunity Commission	✓	✗
19	IP Australia	✗	✓
20	Migration Review Tribunal	✗	✓
21	National Capital Authority	✗	✗
22	National Competition Council	✓	✓ ⁵²
23	Native Title Tribunal	✓	✓
24	Office of Asset Sales and Information Technology Outsourcing	✗	✓
25	Office of Film and Literature Classification	✓	✗
26	Office of Inspector-General of Intelligence and Security	✗	✗
27	Office of National Assessment	✗	✗
28	Office of Parliamentary Counsel	✓	✓
29	Productivity Commission	✓	✓
30	Professional Services Review Scheme	✗	✓
31	Public Service and Merit Protection Commission	✓	✓
32	Refugee Review Tribunal	✗	✓

Unsolicited agencies⁵³

#	Agency	Targeted Agency	Response Received
1	Australian Trade Commission	✗	✓
2	Environment Australia	✗	✓
3	Equal Opportunity for Women in the Workplace Agency	✗	✓

⁵² Incomplete response received.

⁵³ Surveys were not sent to these agencies. However, they replied because an allied agency within the same portfolio provided them with a copy of the questionnaire.

Appendix 3

Sample of Leases Reviewed at Case Study Agencies

Summary

<i>Case Study Agency</i>	<i>No of Leases Examined</i>	<i>No of Commonwealth Sale/Leaseback Leases Examined</i>
Department of Foreign Affairs and Trade	14	5
Department of Health and Aged Care	7	4
Centrelink	22	7
Total	43	16

Department of Foreign Affairs and Trade

#	State	Address	Commonwealth Sale/Leaseback Lease
1	ACT	R G Casey Building John McEwen Crescent, Barton	✓
2	ACT	Part Lvl 1, John McEwen House 7 National Circuit, Barton	X
3	NSW	Level 18, Westfield Towers 100 William Street, Sydney	X
4	NSW	Level 12, Capital Centre 255 Pitt Street, Sydney	X
5	NSW	State Bank Building 77-79 Hunter Street, Newcastle	X
6	NSW	Kingsford Smith Airport	X
7	NSW	Part Level 29, Westpac Plaza 60 Margaret Street, Sydney	X
8	VIC	Level 13 & Part Level 14, Casselden Pl 2 Lonsdale St, Melbourne	✓ ⁵⁴
9	QLD	Corner Creek and Adelaide Streets Brisbane	✓
10	QLD	Cnr Victoria Pde & Hastings St Thursday Island	✓
11	SA	55 Currie Street Adelaide	✓ ⁵⁵
12	TAS	4th Floor, 25 Argyle Street Hobart	X
13	TAS	Ground Floor, 137 Harrington St Hobart	X
14	WA	17th Floor, Exchange Plaza Perth	X

⁵⁴ Casselden Place is also contained in the sample of leases reviewed at Health.

⁵⁵ 55 Currie St is also contained in the sample of leases reviewed at Health and Centrelink.

Department of Health and Aged Care

#	State	Address	Commonwealth Sale/Leaseback Lease
1	ACT	Albemarle Building, Furzer Street Woden	✓
2	ACT	Penrhyn House, Bowes Street Woden	X
3	NSW	1 Oxford Street Darlinghurst	✓
4	VIC	Casselden Place, 2 Lonsdale Street Melbourne	✓ ⁵⁶
5	QLD	340 Adelaide Street Brisbane	X
6	SA	Commonwealth Centre, 55 Currie Street Adelaide	✓ ⁵⁷
7	WA	Central Park, 152-158 St Georges' Terrace Perth	X

Centrelink

#	State	Address	Commonwealth Sale/Leaseback Lease
1	ACT	15 Bowes Street	X
2	ACT	13 Lonsdale Street	X
3	NSW	477 Pitt Street	✓
4	NSW	275-279 King Street	X
5	NSW	4 Figtree Drive	X
6	NSW	2-12 Macquarie Street	X
7	NT	60-62 Hartley Street	X
8	NT	24 Knuckey Street	X
9	QLD	Corner Creek & Adelaide Streets	✓ ⁵⁸
10	VIC	134-142 Ferrars Street	✓
11	VIC	172 Moreland Road	X
12	QLD	443 Queen Street	X
13	QLD	143 Walker Street	✓
14	QLD	22 Walker Street	X
15	SA	191 Pulteney Street	X
16	SA	55 Currie Street	✓ ⁵⁹
17	SA	Ramsay Walk	X
18	TAS	1-7 Bligh Street, Rosny Park	X
19	VIC	100 Brougham Street	X
20	VIC	20-22 Atherton Road	✓
21	WA	7 Packenham Street	✓
22	WA	200 St Georges Terrace	X

⁵⁶ Casselden Place is also contained in the sample of leases reviewed at DFAT.

⁵⁷ 55 Currie St is also contained in the sample of leases reviewed at DFAT and Centrelink.

⁵⁸ Corner Creek and Adelaide Streets is also contained in the sample of leases reviewed at DFAT.

⁵⁹ 55 Currie St is also contained in the sample of leases reviewed at DFAT and Health.

Appendix 4

Advantages and Disadvantages of Gross Rent and Net Rent Leases

Gross Rent Leases		Net Rent Leases	
Advantages	Disadvantages	Advantages	Disadvantages
<ul style="list-style-type: none"> □ Outgoings associated with the operation of central building services during normal office hours are included in the gross rent and are therefore fixed costs. □ Outgoings associated with the operation of central building services are reviewed regularly by an appointed registered valuer as part of the regular rent review process and contribute to determination of the applicable gross rent. □ Gross rent leases are generally better suited to: <ul style="list-style-type: none"> – older buildings of poorer quality requiring significant expenditure to upgrade central building services to modern performance standards (ie. Sub-B Grade office properties); 	<ul style="list-style-type: none"> □ Costs associated with the operation of central building services during normal office hours are generally not separately metered. The lessee can only influence the central building services component of gross rent payable by commissioning a thorough audit/analysis central building services including an indicative assessment of associated operating costs. □ Little or no potential for the lessee to monitor/improve the efficiency of base building plant and equipment. 	<ul style="list-style-type: none"> □ All outgoings (including those associated with the operation of central building services during normal office hours) are generally paid by the lessee and can be monitored accordingly. Further, decisions can be made by the lessee regarding the need for efficiency improvements to reduce energy consumption etc. □ The rent payable by the lessee represents the 'base market' rent only and is therefore less complex to assess/easier to benchmark as part of the regular rent review process. □ Rent is easier to benchmark with other office properties with net rents due to net rents being 'generally' more common. 	<ul style="list-style-type: none"> □ Costs associated with the operation of central building services during normal office hours are potentially variable (ie. not a fixed component of the rent payable). □ If the lessee does not possess appropriate knowledge and systems to monitor outgoings expenditure, this may result in fluctuations in energy consumption and associated costs. □ As the building ages, there will generally be a reduction in the efficiency of central building services and thus additional costs associated with increased energy consumption etc.

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Gross Rent Leases		Net Rent Leases	
Advantages	Disadvantages	Advantages	Disadvantages
<ul style="list-style-type: none"> - multi tenanted office properties that do not provide separate metering of central building services; and - single tenanted office properties that as a result need not provide separate metering of central building services. 	<ul style="list-style-type: none"> □ Lessor has virtually 100% control over decision to/not to invest capital to improve the energy efficiency of base building plant & equipment. Impact of such would be to reduce the 'central building services' component of gross rent payable by the lessee, but increase (by potentially a greater margin) the 'base market' or 'net rent' payable by the lessee (likelihood of lessor making capital investment is low subject to vacancy rate). □ More difficult to benchmark with other office properties with gross rents due to variables associated with central building service' operating costs. 	<ul style="list-style-type: none"> □ Suited to: <ul style="list-style-type: none"> - newer buildings of higher quality featuring state of the art base building plant & equipment in accordance with modern performance standards (ie. B Grade properties); - multi tenanted office properties that provide separate metering of central building services; and - single tenanted office properties that as a result need not provide separate metering of central building services. 	

Appendix 5

Leased Space Density

Density—city/metropolitan leases

1. Accommodation densities for city/metropolitan areas for nearly all categories of agencies in nearly all states and territories were above the adopted benchmark, as set out in Table A5.1. The accommodation density for some agencies was recorded in the range of 123 sqm/person, 208 sqm/person and 660 sqm/person. These unusually low densities were excluded for the purposes of this analysis.

Table A5.1

Respondent Agencies' City/Metropolitan Densities as at 30 June 2000

<i>State/Territory</i>	<i>Departments (sqm/person)</i>	<i>Other large agencies (sqm/person)</i>	<i>Smaller Agencies (sqm/person)</i>
NSW	27	43	36
VIC	37	48	42
QLD	37	41	53
WA	30	53	46
SA	30	52	42
TAS	25	40	49
NT	24	38	33
ACT	26	34	26

Highlighted figures are 10 per cent or more in excess of benchmark range.

2. This analysis indicates that in general too much space is being leased by agencies, with agencies paying rent and outgoings for space that is not needed. A conclusion is that property management practices can improve.

Density—country/regional leases

3. Agencies holding leases in country/regional locations often accommodate smaller numbers of staff and may be faced with a limited choice of available office accommodation. Small properties with fewer employees do not enjoy the economies of scale of larger office properties, as common areas such as receptions, conference and meeting facilities and corridors are still often required for offices with low staff numbers. The lack of choice in country/regional areas may also force agencies to accept leases for offices with space requirements in excess of their needs.

4. Table A5.2 sets out the densities for respondent agencies in each of the states and territories in country/regional areas. These densities are generally in excess of the adopted benchmarks. This may be due the reasons described above and/or inefficient and ineffective property management practices.

Table A5.2

Respondent Agencies' Country/Regional Densities as at 30 June 2000

<i>State/Territory</i>	<i>Benchmark (sqm/person)</i>	<i>Departments (sqm/person)</i>	<i>Other large agencies (sqm/person)</i>	<i>Smaller agencies (sqm/person)</i>
NSW	15–25	47	41	47
VIC	15–25	50	34	47
QLD	15–25	56	41	47
WA	15–25	41	25	68
SA	15–25	65	57	49
TAS	15–25	46	38	74
NT	15–25	38	35	n/a ⁶⁰
ACT ⁶¹	15–25	n/a	n/a	n/a

Highlighted figures are 10 per cent or more in excess of benchmark range.

n/a: not available

⁶⁰ Staff number data was not provided by other agencies for NT.

⁶¹ All available office accommodation in the ACT is classed as city/metropolitan.

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