

VICTORIAN **ombudsman**

**Investigation into allegations of
improper conduct by CenITex officers**

October 2012

**Whistleblowers Protection
Act 2001**

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Letter to the Legislative Council and the Legislative Assembly

To

The Honourable the President of the Legislative Council

and

The Honourable the Speaker of the Legislative Assembly

Pursuant to section 103 of the *Whistleblowers Protection Act 2001*, I present to Parliament my report of an investigation into allegations of improper conduct by CenITex officers.

A handwritten signature in black ink, appearing to read 'John R Taylor', written in a cursive style.

John R Taylor
Acting Ombudsman

23 October 2012

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Executive summary

1. This report resulted from an investigation into a whistleblower disclosure in relation to procurement of contractors and contract services by CenITex (the centre for IT excellence).
2. CenITex is a Victorian State Owned Enterprise, established by government in 2008, with the purpose of providing information, communication and technology services to government.
3. My investigation discovered numerous breaches of the relevant procurement policies and guidelines, including:
 - Companies and their contractors were awarded significant contracts totalling up to \$4 million without competitive processes. In one instance, a competitive process was ostensibly conducted; but, in reality it was a sham.
 - In some instances, nepotism and favouritism influenced procurement and recruitment practices. Often, the companies or contractors were chosen because they were associates or friends of other contractors already working at CenITex.
 - Some appointments were made on the basis of fabricated or false documentation.
 - Some engagements were initiated or overseen by individuals within CenITex who had a clear conflict of interest and stood to gain financially from the transactions. Such conflicts were often not declared, or declared late, inadequately or misleadingly. Even conflicts that were declared were ill-managed by CenITex. This led to opportunities for improper conduct.
4. Serious improper conduct did occur. One CenITex officer misused his position at CenITex over a number of years, and earlier in another department, to engage and approve invoices from a company in which he had a financial interest (including over \$30,000 for services that were not provided). All the while, the officer was receiving substantial financial benefits from the company.
5. Contractors were also engaged at excessive rates, without any evidence that these were negotiated. Unknown to CenITex office holders, CenITex also paid high fees to companies that were providing contractors to CenITex through recruitment agencies. The companies' roles were not disclosed to CenITex. In one case, the fee paid to a company was 50 per cent of the contractor's \$1,600 daily rate.
6. Procurement practices at CenITex lacked rigour. Internal and external checks, including audits and risk strategies, failed to identify many of the issues. Inadequate procurement controls and checks created an environment where avoiding the guidelines became the norm and sometimes led to improper conduct.

7. Most of the issues identified in this report took place in CenITex's Efficient Technology Services (ETS) program. This division was responsible for delivering complex, high level projects, such as a single network, helpdesk and hosting environment for the Victorian public sector (VPS). The ETS program was staffed predominantly by contractors, with limited knowledge of, or experience in, the VPS. Owing to a flawed, decentralised procurement system, such contractors were able to engage other contractors. Unsurprisingly, poor practices developed as a result.
8. These practices arose because there was, in the ETS program, a combination of a 'can do' mentality, unchecked by the usual restraints and procedures relating to government purchasing practices, and a measure of unaccountability which arose because the parties involved saw their mission as highly specialised and 'urgent'. One ETS Program Manager stated that there was 'pressure' to deliver 'at all costs'. This created an environment where there was an increased risk of cutting corners and improper conduct.
9. The investigation also identified that Mr Peter Blades, CenITex Chief Executive Officer (CEO) at the time, approved an exemption from procurement guidelines which provided notional approval to engage unspecified contractor/s up to the value of \$995,000 without any competitive process and without adequate justification. His decision set a poor example for CenITex staff and contractors in relation to the need to comply with Victorian Government Purchasing Board guidelines on competition and the limited use of exemptions.
10. When such conduct occurs at the top of an organisation, there is a risk that poor practices will occur down the line.
11. The ETS program was 'wound down' in June 2012. In addition, a number of individuals mentioned in this report were dismissed during my investigation, their contracts were not renewed or they resigned.¹ CenITex's own investigations uncovered improper practices in relation to other personnel. I have taken these events into account in formulating my conclusions.
12. Mr Michael Vanderheide was appointed as CEO of CenITex in July 2011. I acknowledge that he is taking steps to improve CenITex. He has provided my investigation with documentation regarding new policies, procedures and initiatives which I consider will go some way to addressing the issues that I have raised. These processes, however, must be coupled with changed attitudes and practices and a stronger focus on compliance if the organisation is to be better positioned to address the issues identified in this report.

¹ During my investigation, "Daniel" was dismissed by CenITex for 'gross misconduct'; "David's" contract was not renewed by CenITex; the contract of "James" was terminated by CenITex; and "Nicholas" resigned from CenITex. Prior to my investigation, "Tim" and "Robert" resigned from CenITex and "Liam's" contract was terminated by CenITex. CenITex's engagement of "Helen" did not go ahead. These names are pseudonyms that I have used for the purposes of my report. Prior to my investigation, Mr Peter Blades, former CEO, resigned from CenITex.

13. In response to my draft report, Mr Vanderheide said:

Thank you for the opportunity to review and respond to your draft Report on an investigation under the *Whistleblowers Protection Act 2001* into allegations of improper conduct by officers at CenITex. I appreciate that you have completed some of the investigations we initiated prior to the commencement of your own investigation and am grateful that your inquiries were able to identify additional issues which CenITex could not have uncovered given our lesser powers and limited resources to fully investigate.

I offer my in principle acceptance of each of the recommendations related to CenITex and intend to periodically advise you as to our progress in their implementation. [emphasis added]

As I indicated when I met with your officers during the course of your investigation, identifying and dealing with instances of impropriety, strengthening our control environment and shifting the organisation's culture to one of greater awareness of probity has been a key focus over the past 12 months. I am pleased your Report acknowledges some of the changes that have been made, which include:

- significant enhancement of the control and monitoring environment associated with procurement processes and decision-making within CenITex;
- the building of a culture of “plain speaking” within the organisation whereby staff are encouraged to feel safe to raise concerns and to challenge poor process;
- the launch of a CenITex specific conflict of interest policy based on the policy developed by the State Services Authority;
- the addition of probity matters as a standing item on the fortnightly CenITex Executive Leadership Team agenda;
- the introduction of centralised management for conflict of interest declarations and a monitoring process for compliance with related management plans;
- a quarterly external review of a broad sample of procurement activities to test for compliance with process and probity principles;
- formal conflict of interest related training for more than 250 staff involved in procurement and recruitment decisions;
- centralisation of the recruitment approval process for both contract and public service staff within the division with responsibility for human resources management; and,
- the establishment of a Contractor Procurement Board with specific responsibility for oversight of contractor engagement and contract extension.

Much has been done and I acknowledge your advice that an ongoing stronger focus on changing practices and on compliance will be necessary to best enable CenITex to continue to address the issues identified in your Report ...

Bearing in mind that we have well over 700 active vendors, it is worth noting that this investigation ultimately relates to the alleged serious impropriety of some individuals associated with only a few companies, some of which were or are interrelated. The vast majority of our vendors are responsible corporate citizens and conduct their business accordingly.

Background

Disclosure

14. In September 2011, I received a disclosure from a whistleblower under the *Whistleblowers Protection Act 2001* (the Whistleblowers Protection Act) containing allegations of improper conduct at CenITex (the centre for IT excellence).
15. The disclosure concerned CenITex's procurement of services and personnel from two companies – Company A and Company B. It alleged that:
 - Company A was engaged by CenITex via an exemption process, instead of being selected from the Whole of Government eServices Panel (the eServices Panel).²
 - A CenITex project manager who had a vested interest in Company B, hired contractors predominantly from Company B and received cash payments as a result. The contractors were hired through a 'complex web of legitimate "pass through" recruitment agencies that mask the shady dealings'.
 - Another CenITex project manager had strong links to vendors supplying services to CenITex as well as being a partner of one of the main suppliers at CenITex.
16. The project managers about whom the disclosure was made were contractors. The Whistleblowers Protection Act establishes my jurisdiction in relation to 'public officers'. It provides several definitions of 'public officer', the most relevant being: 'a member, officer or employee of a public body'. In my view, CenITex's project managers met the definition of 'public officer' under the Whistleblowers Protection Act in that I consider them to be officers or employees of CenITex. In reaching this view, I took into account (among other things) the fact that they appeared to be performing the duties of an employee and were subject to the direction and control of employees at CenITex in relation to the way their duties were performed.
17. I determined that the disclosure met the requirements for a public interest disclosure. Accordingly, I commenced an investigation into the matters raised in the disclosure. The result of that investigation is contained in this report.
18. My investigation confirmed that Company A was engaged via an exemption which did not meet Victorian Government Purchasing Board (VGPB) guidelines.
19. The evidence obtained during my investigation was not sufficient to substantiate the allegation that a CenITex project manager received cash payments for hiring contractors from Company B. However, I identified that CenITex officers subverted procurement processes to engage

² The eServices Panel comprised a panel of information and communication technology service providers. It was dissolved in June 2012, as I concluded this investigation.

Company B and its contractors; and that two CenITex contractors had private business relationships with Company B and misused their positions for its benefit. The third allegation was therefore substantiated.

20. During my investigation, CenITex's contracts with Company A and Company B lapsed. These companies are not currently providing services to CenITex.

CenITex

21. CenITex is an information and communications technology (ICT) agency established by the Victorian Government to centralise ICT support to government departments and agencies.³ It was created as a State Owned Enterprise⁴ on 16 July 2008. It is in effect a monopoly provider of ICT services to most Victorian government departments and agencies. It provides support to 36,800 desktops across 10 of the 11 Victorian Government departments and two major agencies.⁵ In its 2010-11 annual report, CenITex reported that it received \$158 million income from transactions and it recorded a deficit of \$24.9 million.
22. CenITex's stated vision is to be the preferred supplier of 'One ICT Service' for the Victorian public sector. This was to be achieved through the Efficient Technology Services (ETS) program, which was to be delivered by CenITex under the strategic direction and monitoring of the Department of Treasury and Finance (DTF). The ETS program included the transfer of departmental ICT operations to CenITex and the implementation of a single network, one common login process, one hosting environment and one Helpdesk. The ETS program was scheduled to be completed by June 2013. Most of the individuals referred to in this report worked in the ETS program.
23. In June 2012, CenITex advised that it was no longer receiving funding from DTF for the ETS program. As a result, CenITex has wound down its ETS project teams.

Parallel enquiries

Victoria Police investigation

24. On 6 September 2011, *The Age*⁶ reported that Victoria Police had been asked to investigate allegations that CenITex project managers had used a 'two-day-old shelf company' (Company C) to bid for a tender in May 2010. The article reported that the CenITex project managers - who also had a vested interest in the company - sat on the selection panel and awarded 'themselves' a contract for \$145,000. The article said that the company had since earned \$1.5 million from CenITex. The company was not named in the article.

³ CenITex, *CenITex Annual Report 2010-11* <www.cenitex.vic.gov.au>.

⁴ Under the *State Owned Enterprises Act 1992*.

⁵ CenITex, 'About CenITex' (2012) <www.cenitex.vic.gov.au>.

⁶ *The Age*, 'Workers award selves tender', 6 September 2011, M. Fyfe and R. Epstein.

25. CenITex briefed Victoria Police on this matter prior to *The Age* article of 6 September 2011. In January 2012, Victoria Police advised my officers that it intended to investigate this matter. So as not to hinder that investigation, I decided not to investigate the conduct of CenITex officers and contractors in the engagement of Company C. However, I have included this matter as a case study in my report as some of the allegations involving this company reflect conduct I identified during my investigation and some of the people involved in Company C were also involved in other engagements discussed in this report.⁷
26. Prior to my investigation, CenITex terminated its engagement of Company C.

State Services Authority review

27. On 13 September 2011, the Hon. Gordon Rich-Phillips MLC, Assistant Treasurer, requested that the State Services Authority (SSA) undertake a review of CenITex and prepare a report for consideration by Cabinet. The terms of reference were to review:
 - CenITex's governance arrangements
 - CenITex's processes for providing improved service delivery
 - CenITex's financial performance
 - the current shared services operating model⁸ and its viability going forward.
28. The final SSA report was provided to the Assistant Treasurer in February 2012 and has not been made public.
29. My officers invited the Assistant Treasurer to provide me with a copy of the SSA report in order to inform my investigation and avoid any potential overlap or duplication between the SSA review and my investigation. However, I did not receive a response to this request.

Investigation methodology

30. In investigating this matter, my officers:
 - met with the SSA and Victoria Police to discuss their respective review and investigation of CenITex
 - examined CenITex documentation, including board and committee minutes and reports, procurement and recruitment records, and probity and investigation reports
 - reviewed email records
 - summonsed telephone and bank records
 - reviewed records from the Australian Securities and Investments Commission (ASIC), Land Victoria, VicRoads and other agencies

⁷ See the chapter entitled, 'Conflict of interest'.

⁸ This is the model that underpins the creation of CenITex, in order that ICT services across government be shared.

- conducted over 40 formal interviews or meetings, including with current and former CenITex chief executive officers, board members, staff and contractors.

31. All witnesses interviewed on oath or affirmation were offered the opportunity to be legally represented or to be accompanied by a support person. Four requested, and were permitted, legal representation.
32. One witness requested to be accompanied by a support person; however, as this person was also implicated in the alleged improper conduct, I declined this request. The witness was invited to nominate another support person, but decided to attend on his own.
33. All people subject to adverse comments in this report were provided with the relevant sections of my draft report to respond to prior to my finalising its contents.

Governance and oversight

Key issues

34. From the time of its establishment, CenITex was an organisation at risk of developing poor procurement and recruitment practices. This was because of its high rate of change; its high proportion of contract staff, who lacked knowledge of public sector ethics and principles; the high expectations placed on the organisation; and the complex and shared governance arrangements with DTF.
35. This level of risk required strong management and leadership; a focus on structures and processes; and regular and thorough testing of whether those processes were adequate, effective and adhered to. Without these, opportunities were created for staff to take advantage of poor oversight: some chose to do so.
36. My investigation identified:
 - failures in internal checks and balances at CenITex
 - serious improper conduct
 - undeclared and inadequately managed conflicts of interest
 - poor procurement and recruitment practices.
37. The allegations made to me indicated that the internal controls within CenITex should have been stronger. I examined the governance and oversight structures and arrangements, and interviewed officers at both the board and senior management levels to determine whether they contributed to the issues experienced by CenITex; how these issues went unchecked and undiscovered; and what should be undertaken to improve the governance arrangements.

Structure and arm's-length relationship with government departments

38. CenITex was established as a State Owned Enterprise by government in 2008. One common theme associated with the description of entities established under the *State Owned Enterprises Act 1992* (the State Owned Enterprises Act) is the requirement for an arm's-length relationship with government departments. Generally, the board reports direct to the responsible Minister and the Treasurer.
39. This was the case with CenITex. Its *Statement of Corporate Intent* outlines its governance structure and states that 'the service delivery and budgetary governance role is assigned to the CenITex board'. The governance structure provides that the board must establish a number of board committees – an Audit and Risk Committee, a Stakeholder Advisory Committee and a Remuneration Committee.

40. While CenITex was initially established to provide centralised ICT support to government departments and agencies, it subsequently partnered with the Government Services Division of DTF to deliver the government's Efficient Technology Services (ETS) program. CenITex was to deliver the program, with DTF providing funding and strategic direction, as well as monitoring progress.
41. As a result, CenITex's operational activities and its organisation were effectively divided into two separate divisions: a 'business as usual' area and an ETS area. The 'business as usual' area was to provide and maintain an ICT infrastructure for its departmental customers while the ETS program was to deliver a consolidated and standardised ICT service across the whole of government.
42. While CenITex was established at arm's-length from government departments, CenITex's role in implementing the ETS program resulted in its working with DTF, a central government department. Mr Blades, the former CEO stated:
- [The] ETS Program was subject to a different governance structure. This governance structure was imposed by DTF and contained in an MOU [memorandum of understanding] with CenITex.
43. The former Chairman of the CenITex board described 'a somewhat dysfunctional governance regime with the Department of Treasury and Finance'.
44. CenITex witnesses stated that, without the funding available through the ETS program, CenITex would have been unable to undertake its core 'business as usual' activities as insufficient funding was provided by departments and government to support this role.
45. Some CenITex witnesses stated that it was difficult for the board and CenITex generally to work in an environment where CenITex's funding for ETS was very much dependent on 'side door', 'lumpy' and 'drip-fed' funding from DTF on a work-order basis. Some witnesses stated that the funding of ETS on 90-day work orders was problematic and contributed to the poor procurement and recruitment practices that my investigation identified. One witness stated that it was seen as more important to deliver within the 90-day work orders than to follow recruitment or procurement practices.
46. Mr Blades also stated:
- A common theme in the works orders was a requirement that CenITex engage contractors (to ensure the Departments were not faced with employment issues) and that contractors would be employed at market rates. DTF had several officers assigned to managing the ETS program.
47. He said DTF influenced 'the way the ETS program was delivered' and that this placed 'pressures ... on a new organisation which was going through an establishment phase'.

48. In April 2012, the government changed the status of CenITex to a 'reorganising body' under the State Owned Enterprises Act, allowing modifications to CenITex's governance arrangements and moving CenITex closer to government.
49. The Chairman of the CenITex board subsequently resigned and was replaced by Mr Grant Hehir, Secretary, DTF on 1 June 2012. That same month, the remaining five inaugural board members resigned. Mr Hehir is now the only board member.
50. The ETS program was 'wound down' in June 2012.

Risk management - ETS

51. In the ETS program, there was a combination of a 'can do' mentality, unchecked by the usual restraints and caution of government purchasing practices, and a lack of accountability which arose because the parties involved saw their mission as highly specialised and 'urgent'. One ETS Program Manager stated that there was 'pressure placed on "stream⁹ leads" to deliver at all costs'. This created an environment where there was an increased risk of cutting corners and improper conduct.
52. CenITex's Audit & Risk Committee and Internal Auditors identified risks arising from the ETS program in 2009, particularly that 'ETS [was] negatively impacting CenITex BAU [business as usual]'.¹⁰
53. In July 2009, Mr Blades' report to the board referred to the 'urgency' of ETS goals and admitted that 'Working with people new to Government purchasing has caused tension with our ETS colleagues ... [resulting] in non-compliance'.¹⁰
54. Nevertheless, a December 2009 review gave the ETS program an 'adequate' rating and assessed the internal control framework as operating effectively.
55. The board received a number of reviews of its procurement and recruitment areas that gave them a 'fair' rating. However, some concerns were expressed about the practices adopted in the ETS program being different from those in the 'business as usual' area of CenITex. These related to ETS running its own procurement and recruitment processes. Mr Blades said, '[t]his was part of the governance arrangements contained in the MOU'.
56. As ETS was largely comprised of contractors, this meant that contractors were able to engage other contractors, at significantly high rates, and with little (if any) oversight.
57. Despite identifying risks associated with ETS in 2009, CenITex retained an organisational structure that allowed ETS to function in a self-contained way and to avoid the controls applied to normal government business.

⁹ The ETS Program was divided into a number of 'streams', with each stream focussing on a different aspect of the program.

¹⁰ CenITex, board minutes, 20 July 2009, page 2.

58. The procurement and recruitment functions of the ETS program were not centralised within the mainstream functional areas until late 2011 after concerns that a CenITex project manager had awarded a contract to his two-day-old shelf company were identified. Until this time, the ETS program ran its own procurement and recruitment processes and developed its own practices.¹¹
59. Most contractors interviewed during my investigation said they had not received procurement or recruitment training and were not aware of the *Code of Conduct for Victorian Public Sector employees* (the VPS Code of Conduct). It is therefore not surprising that poor practices developed in this unit.
60. Mr Blades said he was ‘surprised’ by this view given the ‘mandatory induction courses held and procurement hurdles, such as attending training seminars to pass a procurement test’.

Processes, audit and compliance

61. In order to determine whether there was evidence available to CenITex which should have drawn its attention to the issues outlined in this report, my investigation examined minutes of the board, the Audit and Risk Committee and the Enterprise Risk Management Review Committee, as well as internal and external audit reports.
62. The board regularly discussed procurement practices. At each meeting, the ‘Exemptions’ and ‘Non-compliance’ registers were tabled and discussed and, according to some witnesses, were the subject of detailed discussions. However, little action appears to have been taken following these ‘discussions’. Board minutes highlighted a number of occasions where concerns were identified in relation to procurement and recruitment issues, although specific issues were not identified nor apparently followed up.
63. A review of the procurement activity was completed in December 2009. It did not identify key issues. This is not surprising as it did not test or assess the internal procurement controls that were in place.
64. An external auditor produced audit strategy reports for the three financial years ending 30 June 2009, 2010 and 2011. These identified that expenditure on contractors, supplies and services carried a moderate risk. The closing audit report for 2009 identified ‘weaknesses in internal control environment’. The closing reports in 2010 and 2011 stated ‘we have not identified any further areas of material fraud risk or exposure’.
65. There have also been a number of commissioned reports prepared by independent organisations which examined procurement exemptions, compliance with the *Statement of Corporate Intent* and probity issues. These included an April 2010 report on CenITex’s compliance with its *Statement of Corporate Intent* and Order in Council; two independent reviews of CenITex’s procurement and contract management; and

¹¹ In response to my draft report, Mr Blades, former CEO said that when he left CenITex in March 2011, the segregation of the ‘business as usual’ and ETS divisions ceased as the board accepted that continued segregation was not practical.

probity reports in March 2009 and 2011. These reports generally found favourably in terms of the governance and integrity arrangements in place in CenITex. While there were some recommendations for improvements, there were no recommendations for major review or restructuring and none identifying significant areas for concern.

66. My investigation identified obvious documentary flaws in procurement records from 2009-11, which were not picked up by the internal and external audit activities.
67. Following the public revelations in September 2011 that a CenITex project manager had awarded a contract to his two-day-old shelf company, an audit strategy document identified a 'lack of internal controls over procurement resulting in fraudulent activity'. Expenditure on contractors, supplies and services was now rated as high risk.
68. Independent probity audits and reviews commissioned by the new CEO of CenITex over the last 10 months have since identified significant probity concerns, consistent with the outcomes of my investigation. The first audit, completed in November 2011, reviewed 41 procurements identified as having issues. It found that the risk of breaches of a number of probity principles was 'high'. These included management of conflicts of interest; competitive process; transparency; and consistency and objectivity. 'High risk' was defined as 'financial/non-financial exposures' requiring 'immediate corrective action'.
69. A second audit, completed in March 2012, reviewed a random sample of 54 procurements and also found the risk for breaches of a number of these probity principles was 'high'.
70. A review of internal controls, completed in March 2012, identified an 'underlying culture within CenITex where compliance with probity principles and processes has not been a priority and a focus'. The review noted 'significant activity and effort' was being invested in improving the overall quality of procurement activities. However, it rated the probity control environment as 'weak' based on 'poor levels of awareness of probity processes and controls, a lack of reference material specific to probity and a low level of priority given to probity controls and processes'. These conclusions are consistent with those identified in my investigation.

Conclusions

71. CenITex's arm's-length relationship with government departments was compromised by its complex relationship with DTF which is a customer and also representative of the stakeholders, as well as being an investor through the ETS program. The board had limited decision-making authority or control over the ETS program, which was managed by DTF.
72. In addition, the high proportion of contractors who lacked VPS knowledge and experience (including at the senior management level), combined with the separate funding arrangements for the ETS program and the pressure to deliver, raised the risk profile for the ETS program.

73. This level of risk required a focus on structures and processes; and regular and thorough testing of whether those processes were adequate, effective and adhered to. However, my investigation identified limited testing of compliance with procurement and recruitment policies and processes prior to late 2011. In the absence of such testing, opportunities were created for staff to take advantage of poor oversight: some chose to do so.
74. In April 2012, the government changed the status of CenITex to a 'reorganising body' under the State Owned Enterprises Act. The composition of the board subsequently changed. The ETS program was 'wound down' in June 2012. I have taken these changes into account in formulating my recommendations.
75. I provided Mr Hehir, Secretary, DTF with an opportunity to respond to my draft report in relation to the ETS program and DTF. In response, Mr Hehir said:

The Department of Treasury and Finance (DTF) notes the seriousness of the report's conclusions, and as acknowledged in the report, confirms a number of governance changes have been made over the last eighteen months to strengthen accountability and integrity as well as to meet compliance obligations. In the report it is confirmed that the Efficient Technology Services (ETS) program is not presently in operation ...

With respect to the DTF governance and oversight arrangements of the ETS program, the report highlights the inherent tension within CenITex between 'business as usual' and the very large project that was ETS. While the DTF governance arrangements needed to be cognisant of that operating environment, it was ultimately a matter for the Board and management of CenITex to resolve the operational requirements.

DTF does not accept that the governance arrangements required, or indeed tacitly supported, improper management behaviours and practices, including procurement and recruitment. The work order arrangement continued until February 2012. DTF notes that, following the change in management and management practices arising on or about this time, the work orders process was able to be followed without resort to improper practice.

Recommendation

I recommend that:

Recommendation 1

CenITex require its internal auditors to undertake a greater proportion of compliance audits than was previously conducted, particularly in high risk areas, to ensure compliance with internal policies and VGPB guidelines.

Response

In response to my recommendation, Mr Vanderheide, CEO, CenITex said:

I offer my in principle acceptance of each of the recommendations related to CenITex and intend to periodically advise you as to our progress in their implementation.

Conflict of interest

Key issues

76. In the public sector, a 'conflict of interest' is a situation where a conflict arises between public duty and private interest. The term refers to circumstances where a public officer could be influenced, or reasonably perceived to be influenced, by a private interest when performing an official function.
77. A conflict of interest is not in itself improper conduct. However, not recognising a conflict, or failing to manage a conflict appropriately, is at best improper, or at worst criminal.¹² Such failures can undermine public confidence in an organisation and lead to improper conduct.
78. The VPS Code of Conduct clearly outlines public officers' responsibilities for declaring conflicts of interest and removing themselves from any associated decision-making process.
79. Despite this, my investigation into CenITex identified conflicts of interest that were not disclosed, were not disclosed adequately, or were not disclosed in a timely manner. Some conflicts that were declared were poorly managed by CenITex. This led to opportunities for improper conduct.
80. Serious improper conduct did occur. One CenITex officer misused his position at CenITex over a number of years (and earlier in another government department) to benefit a company from which he was receiving substantial financial benefits.
81. Other officers misused their positions to benefit CenITex vendors with which they had formed private business relationships.
82. CenITex did not have its own conflict of interest policy and failed to ensure officers were aware of their obligations in relation to this issue.
83. This is particularly concerning given the high number of private contractors at CenITex, who present a significant risk given their limited knowledge or experience of public sector values: all but one of the case studies in this chapter involved contractors.

Improper conduct

84. The VPS Code of Conduct requires that public officers use their power in a responsible way. It states that public officers do not 'use their power to provide a private benefit to themselves, their family, friends or associates' and that they 'exercise power in a way that is fair and reasonable, and family or other personal relationships do not improperly influence their decisions'.
85. My investigation identified that a public officer engaged in improper conduct for the financial benefit of himself and a company with which he was associated.

¹² See Victorian Ombudsman, *Conflict of interest in the public sector*, March 2008.

86. This case study provides a clear example of how a failure to declare or manage a conflict of interest can lead to improper conduct:

CASE STUDY 1 – Officer engages company from which he received \$1,250 per month

“Daniel”¹³ was engaged by a government department (the department) from 2005-08 and by CenITex from 2008-12. He held leadership roles in relation to both agencies’ data centres. Throughout this time, Daniel received financial incentives from Company D (the company) in return for creating business opportunities for the company in these agencies. Daniel did not declare his interest in the company to anyone at the department or CenITex.

The company was registered with ASIC in March 2004 by Daniel’s then wife¹⁴ and the wife of his friend, “John”¹⁵ (who, at interview, described himself as ‘like a director’ of the company). The company provides cleaning and maintenance for data centres.

In his eight years at the department and CenITex, Daniel:

- initiated the engagement of the company within two weeks of starting at the department
- recommended and approved contract extensions for the company
- received the company’s invoices (some of which he created on behalf of the company) and approved them for payment by the department and CenITex
- was CenITex’s Contract Manager for the company’s engagement for two years
- reviewed confidential documentation and forwarded it to John to use in a pending CenITex competitive tender.

In September 2011, CenITex’s procurement unit identified concerns that it had paid the company for services that had not been provided. In an attempt to conceal any wrongdoing, Daniel engaged John to review the matter. John’s role in the company was not disclosed to CenITex.¹⁶ Unsurprisingly, John concluded that the services in question had been provided. CenITex, however, later identified that the company had been paid over \$30,000 for services not provided. In response to my draft report, John said the company ‘continued cleaning without invoicing CenITex to make up for this mistake of communications’.

Bank records show that the company received over \$430,000 from the department and CenITex for the period 2005-12. In his time at both the department and CenITex, Daniel also engaged John for other contracts valued at over \$350,000.

My investigation identified evidence of Daniel’s interest in the company and that he had misused his position at two government agencies. This included:

¹³ This is a pseudonym.

¹⁴ Daniel’s wife ceased to be a director from April 2007, after they separated.

¹⁵ This is a pseudonym.

¹⁶ In response to my draft report, John said that at a meeting to discuss this review, he told CenITex he was involved in the company. This is not supported by the evidence of the CenITex officer who identified issues with the company’s billings and attended this meeting.

- ASIC records, showing the company was registered in his wife's name
- company bank statements and records, which indicated Daniel was a signatory to the account and that the company was paying his monthly vehicle payments
- emails that Daniel sent from his Company D, department and CenITex accounts
- metadata from invoices, which showed that Daniel prepared them.

At interview, under oath, Daniel initially denied his involvement in the company. He eventually admitted that he had received financial benefits from the company over a period of time. These totalled over \$1,250 per month and included payment of his domestic rent and car-related expenses.

After my officers interviewed Daniel, I informed the CEO of CenITex of this matter. The CEO subsequently dismissed Daniel for 'gross misconduct' and indicated that he would refer Daniel's conduct to Victoria Police for investigation.

In response to my draft report, Daniel's lawyer stated that Daniel said he has 'always followed procurement procedure at CenITex and ... Ultimate approval had to come from line management'. However, Daniel clearly breached procurement policies by failing to declare his conflict of interest. In addition, line management approved the engagement of the company, or payment of its invoices, largely on the basis of Daniel's endorsement, without any knowledge of the conflict that affected his decision-making.

In response to my draft report, John stated, 'I recognise the conflict of interest with CenITex and I sincerely apologise as this was not planned ... My position is that I was helping [Daniel] with financial issues as a friend and used [the company] income to help him as he was creating opportunities for this company'.

During my investigation, CenITex advised Company D to cease providing services.

87. Another example of improper conduct was identified by CenITex prior to my investigation, involving over \$1.5 million of public expenditure. The conduct was so serious that the matter was referred to Victoria Police for investigation.
88. So as not to hinder Victoria Police's investigation, I did not investigate this matter. However, it is instructive to note that some of the allegations involving this company reflect conduct I identified elsewhere in my investigation. In addition, some of the people involved were also involved in other engagements discussed in this report:

CASE STUDY 2 – Contractor engages his own 2-day old company

In July 2011, CenITex commissioned an independent auditor to conduct a 'routine probity audit' of CenITex's engagement of Company C (the company). The auditor identified 'serious issues' and referred these to CenITex's senior management for 'urgent attention'.

In August 2011, CenITex engaged KPMG to investigate the matter. The KPMG investigation concluded:

- The company was registered with ASIC in May 2010 by three contractors working in ETS, including “Tim”.¹⁷
- The following day, Tim requested that CenITex’s procurement unit raise a Request for Quotation (RFQ) for \$145,000 worth of services and send the RFQ to three specific organisations, including the company.
- The procurement documentation recommended the appointment of the company and was signed for CenITex by two people, including Tim. The company proceeded to provide services to CenITex.
- The other directors of the company were not involved in CenITex’s engagement of the company and their interest ceased in May 2010.
- Another individual working at CenITex who was involved in the procurement documentation subsequently became a director of the company (in August 2011), after leaving CenITex.
- A fifth individual, “Liam”¹⁸ became a non-executive director of the company in May or June 2011 while working at CenITex. Liam’s contract was subsequently terminated by CenITex because of his involvement with the company.

Prior to KPMG’s review, Tim had resigned from CenITex.

According to CenITex records, in the period May 2010 to October 2011, CenITex approved over \$1.5 million expenditure to the company and the contractors it provided to CenITex.

CenITex terminated its contract with Company C prior to my investigation.

Misuse of position

89. I also identified two instances where CenITex officers misused their positions to benefit a CenITex vendor, with which they had separately formed a business relationship:

CASE STUDY 3 – Misuse of position to benefit Company B

“Robert”¹⁹ was an IT architect for CenITex from 2008 until May 2011.

Following Robert’s recommendation, Company B (the company) was engaged by CenITex in March 2010.²⁰ At interview, Robert said that he commenced private business dealings with the company and took steps to become a company director at around the same time.

Robert did not declare a conflict of interest to CenITex until five months after he commenced private business dealings with the company. Even at that point, he only declared ‘an intent to join [the company] as a director’. In the preceding five months:

17 This is a pseudonym.

18 This is a pseudonym. Liam was given the opportunity to respond to my draft report; however, he chose not to do so on the basis of legal advice.

19 This is a pseudonym.

20 See case study 8.

- Robert had recommended to senior CenITex officers that the company be offered additional work, saying to the officers: 'It is only fair and reasonable that [the company] be given the work'. His recommendation was accepted by the officers, who did not know about his interest in the company.
- Robert forwarded the above contractual discussions to the director of the company, who responded: 'Thanks mate, its [*sic*] looking good'.
- Robert raised concerns with senior CenITex officers that the company's intellectual property had been leaked to other CenITex contractors.
- Robert assisted the company in obtaining a non-government contract with an expected value of \$350,000.

When the business relationship broke down towards the end of 2010, Robert sought \$175,000 from the company for his work. At interview, Robert said: 'I assisted [the company] to get into CenITex and I did all this other extraneous legwork, did business plans for [the company] and all this other stuff. And yeah, and I just thought it [\$175,000] was fair and reasonable'. The director of the company said that neither he nor his company paid Robert.

My investigation identified that Robert misused his public position to benefit the company, from which he stood to make a private gain. Robert left CenITex in 2011.

During my investigation, CenITex's contract with Company B lapsed. Company B is not currently providing services to CenITex.

90. Around the same time that Robert's relationship with Company B broke down, Liam²¹ (a senior ETS Program Manager) formed a private business relationship with Company B:

CASE STUDY 4 – Misuse of position to benefit Company B

Liam was contracted to CenITex from 2009 to 2011, when his contract was terminated owing to his involvement with Company C. At this time, he was a senior ETS Program Manager. In late 2010, Liam was offered the opportunity to become a company director by the director of Company B (the company).

In January 2011, CenITex engaged a number of contractors from the company. Liam recommended that the contractors be engaged by a 'pass through' arrangement, which enabled the company to charge significant, undisclosed fees to CenITex for providing the contractors.²²

Liam was listed as an 'evaluator' on the engagement documentation. However, he said he had no direct role in the engagements and that he was listed as an 'evaluator' to ensure he had visibility over CenITex's spending on contractors. His evidence was supported by the other 'evaluator' on the engagement documentation. However, the other evaluator also stated that the engagements could not be processed without Liam's approval.

²¹ This is a pseudonym.

²² This issue is discussed in the chapter entitled, 'Poor recruitment and procurement practices', case study 12.

Liam did not declare a conflict of interest in relation to the contractor engagements, despite having discussions with the director of the company about 'going into business' together from late 2010.

From at least February 2011, Liam was actively involved in the company. In February 2011, he:

- had a Company B email account
- engaged in discussions about getting a 'virtual office' for the company
- arranged and held company meetings
- contacted third parties on behalf of the company to discuss potential legal action
- prepared profit and loss projections for the company.

It was not until 30 March 2011 that Liam declared his interest in the company to CenITex. Even then, he only declared an 'intention to provide accounting consultancy services'. He failed to reveal his active involvement in the company and his intention to become a company director.

One day later, on 31 March 2011, the company submitted a bid for the 2011 eServices²³ tender. At interview, Liam said he only played a 'minor' role in preparing the submission. When asked to be more specific, Liam said, 'I probably decline to actually answer that one, I think, on the basis, I think - yeah, that could probably get me into trouble'.²⁴ My investigation identified an email from Liam to another individual working on the submission, in which Liam said he was responsible for the financial section of the submission - it is clear from this that he played more than a 'minor' role.

The submission also listed Liam as a referee for the company in relation to its work at CenITex. When asked about this at interview, Liam said he requested that his name be taken out and 'that should have happened'. Liam said, 'If I bought in then [to the company], you know, you can't really be ... recommending a company that you're an owner of'. Nevertheless, Liam's name was included in the submission as a referee. Liam's interest in the company was not disclosed in the submission.

The business relationship between Liam and the company ended on 29 May 2011.

91. Liam also misused his position to benefit Company E by engaging one of its contractors and negotiating a high rate for him. At the time, Liam was contracted to CenITex via Company E and was also a manager of the company; however, he did not declare a conflict of interest in the engagement, as illustrated in the following case study:

²³ The eServices Panel comprised a panel of ICT service providers. It was dissolved in June 2012, as I concluded this investigation.

²⁴ Section 56(3) of the Whistleblowers Protection Act states, 'Subject to subsections (1) and (2) and section 55, a person cannot be compelled for the purposes of an investigation by the Ombudsman of a disclosed matter to produce any document or give any evidence that the person could not be compelled to produce or give in proceedings before a court.' After consideration of Liam's response, my delegate allowed Liam to claim the privilege of self-incrimination.

CASE STUDY 5 – Misuse of position to benefit private company

In June 2009, Liam was asked by Company E (for whom Liam was a manager) to obtain a contract position at CenITex for another Company E contractor: “Matthew”.²⁵ Liam responded that Matthew would need to be interviewed by the CenITex chief IT architect. Liam forwarded Matthew’s resume to the chief architect via email.

The chief architect responded to Liam stating, ‘very strong resume. But I suspect we can find someone who lives and breathes [the role] more than he does’.

Matthew was interviewed for a position at CenITex soon after. Liam said that another contractor won this position. However, Matthew was engaged for another position.

My officers compared the procurement documentation for these two contractors and noted similarities which support the view that the procurement documentation for Matthew was prepared to legitimise his engagement, rather than to document the process, as follows:

- The evaluation panels for the engagements of both Matthew and the other contractor comprised the same three people, including Liam.
- The procurement record for the position that Matthew won includes the same five applicants as the procurement record for the position that the other contractor won, despite the records relating to different roles.

My officers obtained an email exchange which indicated that an ETS senior manager was unhappy with the rate that Company E sought for Matthew as it was equal to the rate being paid for Liam. Liam justified the payment of such a high rate and Matthew was subsequently engaged at the requested daily rate (\$1,210). Although Matthew ended up reporting to the other contractor, his daily rate was slightly higher.

At the end of Matthew’s contract in 2010, it was not renewed. Liam said that he made this decision as he was not happy with his performance.

Despite his involvement with Company E, Liam did not declare a conflict of interest in the appointment of Matthew to CenITex. In fact, Matthew’s procurement record stated that the evaluation team members did not have a conflict of interest.

I consider that Liam misused his public position to benefit Company E. His failure to declare his conflict echoes his behaviour in relation to Company B. There is no reason to presume that Matthew’s engagement represented good value for money in light of the conflict that affected his engagement.

Acceptance of gifts and hospitality

92. The potential problems that can arise from the acceptance of gifts and hospitality by public officers have been highlighted in a number of my public reports.²⁶

²⁵ This is a pseudonym.

²⁶ For example, see my Parliamentary reports: *Conflict of interest in the public sector*, March 2008 and *Corrupt conduct by public officers in procurement*, June 2011.

93. Acceptance of gifts and hospitality may influence the actions of public officers by creating a sense of obligation, which may compromise them. If a third-party observer could reasonably believe that a gift was intended to influence an official in some way, then this perception damages both the reputation of the individual and their employer. Consequently, gifts and hospitality should only be accepted when there is a strong public interest to do so.
94. My investigation confirmed that a CenITex contractor was permitted by CenITex to accept international flights and accommodation valued at thousands of dollars from a CenITex vendor. In my view, this was not in the public interest.
95. While CenITex sought probity advice and implemented a conflict of interest management plan, CenITex did not document the rationale for allowing the contractor to accept the hospitality from the vendor:

CASE STUDY 6 - Acceptance of international flights and accommodation

“David”²⁷ was a Program Manager in the ETS Program. In early 2011, he was invited to be a member of a customer council for Company F (the company): a CenITex vendor. The council provides advice to the company about product development. Members are asked to attend two council meetings per year and to ‘advocate’ for the company.

At interview, David said that he was asked to sit on the council in a private capacity because he had previously dealt with the company outside of CenITex. However, the company’s Account Manager said that the company invited him because he was their principal CenITex liaison at the time.

In May 2011, David accepted international flights and accommodation to San Francisco from the company. He stated that he received approval from CenITex senior management to attend the council meeting and accept the hospitality.

David was asked by his then manager to complete a conflict of interest form. However, David’s declaration stated that he had no conflicts of interest and he did not declare his role on the council or the San Francisco trip. David said this was because he did not have a conflict of interest: he did not sign-off on procurement and was not a financial delegate. He said he ‘only endorse[d] things for payment’. However, he was in a position to influence decision-making in relation to the company given his senior role in CenITex. I, therefore, consider that he had a conflict of interest. The hospitality was not declared on CenITex’s gifts and hospitality register.

In September 2011, David was invited to another council meeting, this time in Spain. The approval of Mr Vanderheide, CEO was sought for David to attend the meeting. In response, Mr Vanderheide obtained independent probity advice. This advice recommended CenITex could send a delegate on the Spain trip, provided that CenITex:

- determined it was in the public interest to send someone

²⁷ This is a pseudonym.

- nominated the appropriate officer to attend
- funded the flights and accommodation.

Despite this advice, Mr Vanderheide orally approved David attending the meeting at the expense of the company (the trip was valued at \$3,472). Mr Vanderheide did not document his decision. However, in response to my draft report, he said that he considered the following factors:

- CenITex had a contract with the company that would be in place for five years, meaning that David would have little, if any, opportunity to engage in procurement associated with the company.
- David intended to travel on his own time and not while being paid by CenITex.
- It was not clear whether CenITex had the right to refuse David's continued engagement with the council given his status as a contractor.
- A conflict of interest management plan was put in place, which included that all of the company's invoices be counter-signed. This was implemented.

While the decision made by Mr Vanderheide was one that was open to him to make, I consider that it would have been preferable to accept and act upon the probity auditor's advice. In my view, it will rarely be in the public interest for a public officer to accept international flights and accommodation from a vendor. If it is considered that there is a public interest, this must be clearly documented by the decision-maker.

During my investigation, David's contract with CenITex lapsed and it was not renewed.

Failure to manage and document conflicts of interest

96. My investigation identified that some conflicts were not adequately managed or documented by CenITex.
97. Declarations of conflicts of interest and any decisions taken in relation to them should be recorded in a register so that there is a record of the process available for scrutiny. A management plan should also be put in place to ensure ongoing management of the conflict.
98. According to Liam, his declaration in relation to Company B (case study 4) was 'filed'. He said he was not asked about his involvement with the vendor, directed to place an entry on CenITex's 'Conflict of interest register of reportable interests' or aware of any steps taken to manage the conflict that he disclosed.
99. Robert declared his conflict in relation to Company B (case study 3) in an email to his manager. While his manager responded to the email laying 'down some ground rules and expectations', the conflict was not recorded on the 'Conflict of interest register of reportable interests'.
100. The reasoning for the decision to allow David to accept international flights and accommodation from a CenITex vendor was also not documented (case study 6). Although, a plan to manage the conflict was implemented.

101. The following case study highlights the failure of a CenITex manager to manage a conflict of interest in relation to the engagement of contractors:

CASE STUDY 7 - Failure to manage conflict of interest

During my investigation, CenITex identified that one of its contractors (“James”²⁸) was a director of an IT recruitment agency (the agency), which had provided two contractors to CenITex (Contractors 1 and 2).

CenITex reviewed the engagement of Contractor 1 from the agency in May 2011. It found that a CenITex Senior Manager had emailed James’ wife, who was a director of the agency, (and another company) to ask her to fill a position. In this email, the CenITex Senior Manager asked that the wife talk to her husband (James) to gain a better understanding of the requirements of the position.

The CenITex Senior Manager claimed he did not know that James was a director of the agency. Even so, his actions demonstrated that he did not recognise that James had a clear conflict of interest in his wife providing recruitment services to CenITex considering James’ role at CenITex.

Key documents related to the engagement of Contractor 1 could not be located by CenITex. These included:

- a selection report or recruitment file for the recruitment process
- an exemption from recruitment requirements, despite the procurement record, signed by the Senior CenITex Manager, stating that a ‘recruitment exemption has been approved for this position’.

CenITex’s review of the engagement of Contractor 2 from the agency in June 2011 found:

- One CenITex contractor signed the selection report as a member of the evaluation panel, but he was not part of the interview process.
- There were two recruitment selection reports for the relevant interviews and position, both prepared by another CenITex contractor. The first report recorded that Contractor 2 was ‘unsuitable’. The second report recorded that Contractor 2 received a higher score and was the recommended applicant.

CenITex’s investigation report included the following comment by Mr Vanderheide, CEO:

I am thoroughly [his emphasis] disappointed in the actions of the three individuals identified as having signed a recruitment report in the knowledge that one of the signatories had no involvement in the process ... What was done was not right [his emphasis]. Preparing and signing the recruitment report in the manner undertaken had the effect of misleading the delegates who subsequently approved the process ... My decision therefore is that final letters of warning be issued to each of the three who signed.

CenITex terminated the engagement of James in 2012. Mr Vanderheide also undertook to remind the CenITex Senior Manager ‘of the expectations of a senior manager with respect to probity principles of fairness and equity’.

28 This is a pseudonym.

A lack of policy and education

102. Until February 2012 (after my investigation commenced), CenITex did not have its own conflict of interest policy to inform staff about their obligations to declare and manage conflicts of interest.
103. The term 'conflict of interest' was referred to only once in CenITex's *Procurement Policy*, which required that evaluation team members sign a conflict of interest form (2008 policy) or 'declare that they do not have a conflict of interest (actual or perceived)' (updated 2010 policy). The procurement policy did not define conflict of interest and it did not discuss how and by whom a conflict of interest was to be managed.
104. In response to my draft report, Mr Vanderheide said that CenITex relied on whole of government policies on the State Services Authority (SSA) website, which defined 'conflict of interest' and detailed how conflicts are to be managed. He said a link to the SSA policies was provided on the CenITex intranet.
105. There also appears to have been little (if any) education of contractors about conflict of interest principles. While members of CenITex senior management informed me that CenITex ran an induction program for new staff, most contractors interviewed during my investigation stated that they did not receive any training on conflict of interest. Most were also unaware of the VPS Code of Conduct²⁹ or the obligations that it imposed on them.
106. Mr Vanderheide said that the induction program has been mandatory for all new staff since 2008 and that CenITex also issues an annual staff bulletin outlining public officer responsibilities and providing a link to the VPS Code of Conduct.

Conclusions

107. The failure of individuals to declare conflicts of interest and CenITex's failure to manage some conflicts created opportunities for improper conduct.
108. My report details situations where these opportunities were taken advantage of and, in several cases, individuals allowed their private interests to interfere with their public duties.
109. My investigation has identified the risks associated with contractors undertaking roles, such as recruitment and procurement, which require a proper understanding of public sector ethics – including the core concept of conflict of interest.³⁰ Contractors often have limited knowledge or experience of public sector values, as was apparent during this investigation. Secondary employment, private business interests and nepotism are issues of particular concern with contractors.

²⁹ The *CenITex 2010-11 Annual Report* states that the Code of Conduct applies to all CenITex staff and contractors. It further states that the code 'is issued to employees on commencement with CenITex and is reissued to all employees and contractors each August'.

³⁰ I have previously reported that a significant vulnerability for the public sector arises in the use of contractors. Victorian Ombudsman, *Annual Report 2010-11*.

110. Given that CenITex did not have a policy and that it provided contractors with limited education, it is unsurprising that the concept of conflict of interest was not well understood among the contractors that were interviewed. Many considered that a conflict of interest did not exist if they had 'integrity', and others believed that a conflict of interest was negated simply by declaring it. Some failed to understand the impact that the perception of a conflict of interest can have on the reputation of CenITex and its officers.
111. There is a need for strong leadership, education and the development of an ethical culture to overcome the conflict of interest issues that I have identified. Such leadership was not apparent prior to Mr Blades' departure from CenITex.³¹
112. In this regard, Mr Blades said:
- I reject the allegation that I did not provide strong leadership, do anything to educate contractors about conflict of interest issues or build an ethical culture to overcome conflict of interest issues.
113. Mr Blades referred to an investigation report commissioned by DTF in March 2009, which he said was 'complimentary of the progress made by CenITex'. Mr Blades said the investigator also emailed DTF, stating: 'I judge that CenITex is well managed and focused on the tasks given it, and they have, in my opinion, a competent management team well led'.
114. The serious issues identified during my investigation do not support this view.
115. Since my investigation commenced, CenITex has developed a conflict of interest policy; strengthened the requirements for declaring conflicts of interest in relation to procurement; and assigned responsibility for monitoring conflict of interest management plans to its legal counsel. I have taken these steps into account in formulating my recommendations.

Recommendations

I recommend that CenITex:

Recommendation 2

Include compliance with the CenITex procurement and recruitment policies, Victorian Government Purchasing Board (VGPB) guidelines and the VPS Code of Conduct as a requirement in the Performance Development Plans of contractors and staff.

Recommendation 3

Provide all staff and contractors with regular training on conflict of interest, the VPS Code of Conduct and the Whistleblowers Protection Act, as well as other matters relevant to their position and responsibility, including procurement and recruitment policies and the VGPB guidelines.

³¹ Mr Blades departed CenITex in March 2011.

Recommendation 4

Regularly remind all contractors and staff of the restrictions on outside employment (as set out in the *CenITex Outside Employment Policy*) and require that, if staff conduct an outside business, trade or profession, this must be immediately declared to their manager so that CenITex can determine whether a conflict of interest exists.

Recommendation 5

Consider the appropriateness of allowing CenITex staff and contractors to accept overseas flights and accommodation from CenITex vendors. If it is considered that there is a public interest in accepting such hospitality from a vendor, ensure this is clearly documented by the decision-maker.

Recommendation 6

Refer “Daniel’s” conduct to Victoria Police for investigation in relation to misconduct in public office and fraud.

Recommendation 7

Consider excluding Company D from future tenders and contracts.

Recommendation 8

Consider cancelling any current engagements related to “John” and his companies and conduct a process that accords with key VGPB purchasing principles prior to re-engaging “John” or his companies.

Response

In response to my recommendations, Mr Vanderheide, CEO, CenITex said:

I offer my in principle acceptance of each of the recommendations related to CenITex and intend to periodically advise you as to our progress in their implementation.

Poor recruitment and procurement practices

Key issues

116. I identified a number of procurement and recruitment decisions that failed to comply with relevant CenITex policies and the VGPB guidelines,³² including:
- an absence of fair and open competition, in particular:
 - a false competitive process
 - a misuse of an exemption
 - a failure to advertise positions.
 - a lack of accountability and transparency, in particular:
 - a failure to negotiate contractor rates
 - non-transparent fees paid for contracted services
 - fabricated records
 - selection of contractors based on past work associations
 - payment for services that had not been provided (pre-billing)
 - poor record-keeping.
117. While my investigation focused on two companies named in the disclosure (Company A and Company B³³), irregularities concerning a number of other engagements were also brought to my attention. Most of the engagements were in the ETS program.
118. The irregularities identified are indicative of a systemic culture at the time that did not prioritise or focus on probity or achieving the best use of public resources. Rather, some officers appear to have focused on achieving outcomes within tight timeframes, a point supported by a number of probity reviews commissioned by CenITex.
119. The practices identified during my investigation led to reputational damage and diminished market confidence in CenITex.

Absence of open and fair competition

120. Open and fair competition is one of the overarching principles for public sector procurement established by VGPB. It requires that agencies take advantage of competitive tension, through public tenders or quotation processes, to maximise value for money opportunities for government.
121. The competitive process must be fair and open – that is, agencies must treat companies and individuals consistently and in accordance with documented processes.

³² VGPB guidelines establish probity principles for public sector procurement, including acting with integrity and impartiality; promoting effective competition; ensuring transparency of process; and identifying and resolving conflicts of interest. While CenITex is not an administrative body subject to VGPB guidelines, CenITex's *Statement of Corporate Intent* commits CenITex to following the guidelines. CenITex's *Procurement Policy* (August 2010) also states: 'CenITex will adhere to all VGPB policies where practical'. Many CenITex contractors interviewed by my office were unsure whether VGPB guidelines applied to CenITex procurement.

³³ Company A and Company B were the subject of probity reviews commissioned by CenITex prior to my investigation.

122. My investigation into CenITex identified that officers often avoided competitive processes, preferring to engage companies and individuals through personal referrals and recommendations. In some cases, exemptions were used to avoid competition and, in another instance, the competitive process was a sham.

False competitive process

123. In one instance, a decision was made to engage Company B and then a competitive process was conducted to support the decision: this amounted to a sham competitive process.

CASE STUDY 8 - Sham competitive process conducted to support decision

Company B was introduced to CenITex by a CenITex contractor (Robert³⁴), who had previously worked with Company B's director (the director) outside of CenITex.

On 20 January 2010, Robert sent the director's résumé to various CenITex officers, including Tim,³⁵ an ETS Project Manager. A day later, Robert sent Tim an invitation to meet with the director.

On 10 February 2010, CenITex issued a Request for Quotation (RFQ) to three companies, including Company B. Company B was not on the eServices Panel at the time, while the other two companies were.

Company B and one other company responded to the RFQ. Company B was subsequently awarded the contract for 100 days at a total cost of \$137,500. The other company that responded quoted less - \$131,500 - for the same period.

The decision to award the contract to Company B is recorded as having been made on 24 February 2010. However, it is clear that the decision to engage Company B was made before the RFQ was issued:

- On 8 February, Robert emailed an ETS consultant to advise that the director of Company B would be offered a position and that Tim was 'working through the process for this'.
- On 10 February, Tim emailed two ETS consultants to advise he had 'progressed the RFQ for [the director]'.
- Also on this day, the director was listed in an ETS organisational chart as reporting direct to Tim.
- On 18 February, Tim requested security passes and email logins for the director.
- At interview with my officers, the director was asked about the purpose of the RFQ and he said, '[T]he intention as far as I'm concerned was to engage my services, right?'.

Tim and an ETS procurement officer were the only members of the RFQ evaluation panel. This is contrary to CenITex's policy that a minimum of three people evaluate quotations for procurement above \$100,000.³⁶ The documentation supporting the selection of Company B contained only a short summary justifying its selection in preference to the other company.

³⁴ This is a pseudonym.

³⁵ This is a pseudonym.

³⁶ CenITex *Procurement Policy*, July 2008.

Prior to my investigation, CenITex commissioned an independent probity review, which noted that the selection documentation for Company B:

is not backed up by evidence of referee checks, nor does it adequately explain to the third party observer how a one-person company with inferior evidence of capacity and capability could be selected in favour of an established eServices Panel member company that was going to charge less.

CenITex policy required that three quotations be sought for engagements of companies costing between \$25,000 and \$150,000. As with other case studies in my report,³⁷ the RFQ process was conducted simply to legitimise the decision to engage Company B. According to Tim, he was 'directed by the HR and procurement personnel [in ETS] as to the necessary processes'.

The original contract with Company B of \$137,500 was later extended by \$372,875. The extension documentation notes (incorrectly) that Company B had initially quoted less to complete the work than was quoted by the other company that responded to the RFQ.

At the extended contract's expiry, the director of Company B was engaged through the Staffing Services Panel (SSP)³⁸ to provide services to CenITex via Company B, for fees totalling an additional \$296,864. In all, over \$800,000 was allocated for the director of Company B's services between March 2010 and November 2011. The individuals involved in the initial engagement of Company B have since left CenITex.

124. The above RFQ was clearly a sham. The requests to other organisations to submit quotations were invitations for them to waste their time and resources. It is unlikely that the other company's quotation was given due consideration as the relevant CenITex officers had already chosen Company B for the role.

Exemptions

125. Exemptions enable an agency to procure goods and services without a competitive process. They are a legitimate procurement mechanism; however, they should only be used in exceptional circumstances and not for the purposes of avoiding competition.
126. My investigation identified an exemption that failed to meet VGPB guidelines and which was used to approve over \$2 million in expenditure for Company A:

CASE STUDY 9 - Non-compliant exemption used for \$2 million expenditure

Company A (the company) was engaged under an exemption which excused CenITex from complying with the need to seek three quotations established in the CenITex *Procurement Policy*.³⁹

³⁷ See case studies 2, 5, 13 and 18.

³⁸ The SSP is comprised of seven recruitment agencies that provide general staffing services and/or specialist information and technology staffing services to Victorian Government agencies.

³⁹ CenITex's *Procurement Policy* applies to the engagement of companies and contractors. It establishes requirements for quotations and public tenders according to monetary thresholds.

David,⁴⁰ the ETS Program Manager responsible for the engagement of the company, gave evidence that this exemption was created specifically to engage the company. However, the exemption form did not refer to the company. Rather, it stated that it was for 'multiple vendors'. The Procurement Exemption Register provided to the board, reporting on this exemption, named five vendors, not including the company. The Register was therefore a false and misleading record. The company was the only vendor engaged under the exemption.

The exemption was approved by Mr Peter Blades, CenITex's then CEO, on 2 October 2009. At the time, he had delegation to approve exemptions under \$1 million.⁴¹ At interview, Mr Blades said that, at the time of the exemption, he was 'new to government' and he generally relied on advice from the Chief Financial Officer and others that VGPB guidelines and internal processes were being followed.

The stated purpose of the exemption was to recruit 'scarce skilled individuals' where recruitment was considered 'urgent'. The recorded reason for the exemption was 'genuine urgency'. The reference to urgency is not supported by the facts: for example, a director of the company was interviewed on 20 August 2009, but he did not commence at CenITex until over two months later.

In addition, VGPB guidelines state that matters of urgency include, 'protection of human, animal or plant life or health, security or safety as a consequence of an unforeseen event or occurrence'. None of these issues were present in the engagement of the company.

The relevant VGPB policy⁴² also states that exemptions are to be used in exceptional circumstances. In my view, exceptional circumstances must be determined on a case-by-case basis. This is inconsistent with the blanket permission created by the exemption. In this regard, the exemption approved by Mr Blades became known internally to CenITex officers as a 'blank cheque'⁴³ as it provided notional approval to engage contractor(s) for unspecified projects up to the value of \$995,000 without any competitive process.

The exemption was valid until 31 December 2009. While there was an option to extend the exemption until 28 February 2010, there is no evidence that this option was exercised. Despite having expired, the exemption was cited in procurement documentation used to engage the company as late as September 2010. It appears that neither the line managers nor the financial delegates identified that the exemption had expired or that the authorised amount had been exceeded.

The exemption was relied on for approved expenditure on the company of over \$2 million.⁴⁴

In relation to this issue, Mr Blades stated:

40 This is a pseudonym.

41 CenITex's *Procurement Policy* (2008).

42 Victorian Government Purchasing Board, *Exemption from Seeking Multiple Quotes, Open or Selective Tendering (Limited Tendering) and ICT IP Default Position Policy*, October 2009.

43 The phrase was sighted by my officers in several internal CenITex emails.

44 The total approved expenditure for Company A and its contractors was almost \$3 million: over \$2 million was approved under the exemption; approximately \$1 million was approved for the engagement of individual Company A contractors through the Staffing Services Panel. While \$3 million was approved, Company A invoiced for over \$1.7 million.

- 'At the time, all exemptions were approved by the board and I had no delegation to approve exemptions'. (However, the Procurement Exemption Register provided to the board states, 'Approver: CEO'. Also, the CenITex *Procurement Policy* stated that exemptions for goods and services between \$150,000 and \$1 million were to be approved by the CEO and that exemptions for over \$1 million were to be approved by the board).
- The exemption was not created to engage the company. Mr Blades said his expectation was that it was to be used to engage the five vendors listed on the register. (However, the exemption form, signed by Mr Blades, did not list any vendors and it was this form that was used to authorise engagements of the company, not the register).
- It was not his position 'that a blank cheque was being given'.
- If it is the case that the exemption was misused by David 'and others outside the scope of the Board's approval, it was not a matter of me setting a poor example but is an example of other people acting improperly'. (However, Mr Blades' decision to sign an exemption form that did not detail the contractors to be engaged or the work to be completed allowed such 'misuse' to occur).

Mr Blades also stated, 'It was accepted within DTF that there was a need to approve large exemptions in the IT environment'. DTF was responsible for strategic direction and monitoring of the ETS program.

During my investigation, CenITex's contract with Company A lapsed. Company A is not currently providing services to CenITex.

127. From mid-2010, CenITex's policy changed and exemptions were required to be approved by the board. In relation to this change, the former Chairman of the board said there was a potential for private sector contractors in CenITex 'to be driven by expediency' and that because there was so much activity at CenITex, 'there was a tendency to rush stuff'. He said that, generally, if an exemption was sought it was because of a lack of planning, rather than an attempt to subvert the process. However, he considered that the best way to manage the risks associated with exemptions was for the board to own the risk.

Failure to advertise positions

128. My investigation identified that at least nine contractors were engaged by CenITex from Company A and Company B without their positions being advertised. On average, CenITex paid around \$1,400 per day for each contractor.
129. There is no reason to be confident that these contractor engagements represented good value for money.

Contract-splitting

130. Contract-splitting involves dividing contracts into smaller amounts in order to avoid requirements for open competition, such as a tender or quotation process, or to circumvent financial delegation thresholds. The following case study highlights an example of what appears to be contract-splitting:

CASE STUDY 10 – Contracts split to avoid tender thresholds

In September 2011, CenITex received an anonymous complaint from a former CenITex employee regarding contract-splitting. The complainant alleged that CenITex's contracts with Company G had been consistently split to amounts around \$100,000 and that a number of contracts were essentially for the same work. CenITex's *Procurement Policy* required that a public tender be conducted for any engagement over \$150,000. The policy also specifically prohibits contract-splitting.

CenITex provided my investigation with a report on purchase orders for Company G from 2009 to 2012. This report showed that Company G was paid over \$40 million for goods and services, spread over approximately 330 purchase orders. Of these, approximately 270 purchase orders were for under \$150,000. This suggests that engagements may have been split by CenITex in order to avoid tender thresholds.

131. I have recommended that CenITex review the engagement of Company G to ensure that CenITex officers have not engaged in contract-splitting.

Lack of accountability and transparency

132. The VPS Code of Conduct requires that public officers demonstrate accountability by seeking to achieve the best use of public resources. Accountability is related to the concept of transparency, which requires that public officers work to clear objectives in an open manner and submit themselves and their decisions to scrutiny.⁴⁵
133. My investigation identified a lack of accountability and transparency in the procurement and recruitment practices at CenITex. There was a failure to negotiate contractor rates, which led to CenITex paying up to 30 per cent above market rates. CenITex also paid undisclosed fees to companies for the provision of contracted services, which led to CenITex paying inflated rates.
134. I identified that some contractors were chosen on the basis of past work associations and referrals, rather than demonstrated merit, and that some records were fabricated to support such decisions. In addition, CenITex paid for services that had not been provided owing to the dishonesty of a Program Manager and a 'deliver at all costs' attitude. As with many of my investigations, I also identified poor record-keeping.

Failure to negotiate contractor rates

135. A significant issue with the procurements I examined was the lack of adequate negotiation of daily contractor rates by CenITex. CenITex was described by one witness as a 'rate-taker'. It appears to have accepted the rates requested by contractors and made no attempt to assess value for money outcomes. This is particularly concerning given the high daily rates paid to contractors by CenITex, which total over \$40 million per annum.⁴⁶

⁴⁵ Independent Commission Against Corruption, *Probity and probity advising*, Sydney, 2005.

⁴⁶ Includes temporary/agency staff, contractors, professional services and managed services.

136. In January 2012, CenITex commenced a review of contractor rates and introduced a 'rate card' – the preferred, market rates to be paid for the various contractor skills acquired by CenITex. CenITex's review identified that 186 of its 204 contractors (over 90 per cent) were being paid 5-30 per cent over market rates.
137. CenITex has used this rate card to renegotiate rates for some existing contracted staff. It advises that this has led to annualised savings of almost \$3 million. The rate card will also form the basis for negotiations with future contractors.
138. This approach provides a basis for CenITex to make the most of its position as a major acquirer of contract IT labour. However, I remain concerned that CenITex did not address this issue earlier. While some failures in procurement processes can be difficult to identify, the complete absence of negotiation of rates with contractors was an obvious failing, which has led to significant wastage.
139. In response to my draft report, Mr Vanderheide said:
- CenITex [has] been focused on better management of contractor rates for some time.
- All contractor rates once approved were posted on the relevant VGPB website. Numerous rate reviews were conducted to market test contract rates against industry. Although ad-hoc at this time (2008-2010) they were often conducted for the high priced contractors. These reviews were often provided to the Department of Treasury and Finance Commercial Division.
- On 7 December 2009 CenITex provided a Status Report on a Review of IT Contractors which included rate comparison analysis. The status report found that contractor rates were typically 15-25% higher than on-going VPS salary rates. As a consequence of this report, CenITex developed and implemented a comprehensive plan to convert contractors to VPS. On 11 February 2011 92% of VPS offers of employment to IT contractors had been accepted.

Excessive rates

140. My investigation identified rates paid to senior contractors that were in excess of the salary of Victorian Government agency heads and appear to be excessive:

CASE STUDY 11 – High rates paid to senior officers

In August 2008, CenITex engaged two contractors at the following rates:

- Chief Operating Officer: \$487,000 for 12 months. His contract was later extended for a further 24 months at an annual rate of \$493,680.
- Chief Information Officer: \$396,000 for 12 months.

At interview, the then Chairman of the board and a board member took the view that the pay rates were justified as the rates were consistent with those paid in the IT industry; the individuals were well credentialed and had the background knowledge needed; and that CenITex's mission was a complex one. They added that it is not uncommon for contractors to be engaged to fill senior government

positions. Their view was that the urgency and nature of CenITex's requirements and the lack of adequate pay scales within the public sector demanded the course adopted in order to recruit suitable staff.

Mr Blades said that the rates were 'acceptable to DTF', which initially engaged the contractors prior to CenITex's establishment, and that the comparison of their rates with those of agency heads 'does not take into account the transitory nature of their engagement, the absence of entitlements ... and the rates paid to IT contractors elsewhere in Government and in the private sector'.

The rates paid to the Chief Operating Officer and Chief Information Officer were well in excess of the salary level of government agency heads and appear to be excessive.

There was also no requirement in their contracts for the contractors to comply with the VPS Code of Conduct.⁴⁷

141. If government agencies are to continue to use contractors in senior positions of authority, then appropriate contracts and arrangements need to be established to ensure they are bound by the VPS Code of Conduct.

Non-transparent fees and false savings claims

142. Some CenITex managers turned to recruitment agencies on the Staffing Services Panel (SSP)⁴⁸ to engage their contractors of choice, avoiding exposing their recruitment to competition from the market. The engagement of contractors through this means led to CenITex paying undisclosed fees to third parties, as the following case study illustrates:

CASE STUDY 12 - Payment of undisclosed fees to third parties

The SSP is comprised of seven recruitment agencies that provide general staffing services and/or specialist information and technology staffing services to Victorian Government agencies.

The recruitment agencies use their own resources and engage 'Tier 2 suppliers'⁴⁹ to find individuals to fill relevant roles. Government agencies may also source candidates and refer them to the recruitment agency for administration, payroll and on-hire back to the government agency.

A number of contractors were provided to CenITex via SSP recruitment agencies, which charged a daily fee. The contractors were selected by the relevant ETS Program Manager, without any competitive process. CenITex referred to this process as a 'pass through' arrangement or 'body shopping'.

Liam,⁵⁰ then a senior ETS Program Manager, recommended the 'pass through' arrangement for the engagement of several contractors from Company B. The procurement records for the relevant contractors indicated that they were being transferred from their existing contract (through an eServices vendor) to a new arrangement through a

47 The CenITex *Annual Report 2010-11* states that contractors are subject to the VPS Code of Conduct; however, most of the contractors interviewed during my investigation said they were unaware of this.

48 The SSP is a State Purchase Contract (SPC). SPCs are standing offer agreements established when multiple Victorian Government entities 'have a common requirement for frequently purchased goods and or services, and value for money can best be achieved through aggregating demand' <www.vgpb.vic.gov.au>.

49 'Tier 2' suppliers are approved recruitment agencies that can be used by the recruitment agencies on the SSP to source staff. A list of approved 'Tier 2 suppliers' is available at <www.vgpb.vic.gov.au>.

50 As discussed in the chapter entitled, 'Conflict of interest', Liam had a private business relationship with Company B.

recruitment agency. Liam advised CenITex decision-makers that this would save 'hundreds of thousands of dollars'.

While the procurement records indicated all of the contractors were already working for CenITex, three of the contractors had never worked for CenITex and were being engaged for the first time.

In addition, Liam and the procurement records failed to disclose the role of Company B in the arrangement.⁵¹ What happened, in fact, was that the contractors were provided by Company B to the recruitment agency to CenITex. The recruitment agency charged CenITex a daily fee per contractor, which was disclosed to CenITex. Company B also charged a daily fee for providing each contractor. For example, one contractor was charged at \$1,600 per day to CenITex for a 130 day contract; Company B retained 50 per cent – over \$100,000. Company B's fees were passed on to CenITex, without its knowledge.

While Liam claimed that the arrangement would save 'hundreds of thousands of dollars', an independent probity review commissioned by CenITex concluded that CenITex had apparently 'paid inflated rates' for the contractors as their 'rates reduced by \$100-\$300 after [Company B] was removed from the contracting arrangement'. Another probity review commissioned by CenITex concluded that the savings claim for one of the contractors was 'inflated by at least 22%'.

One of the contractors provided by Company B later left the company and registered his own company: Company H. The contractor subsequently contracted to CenITex via a 'pass through' arrangement involving Company H. Company H also provided other contractors through the 'pass through' arrangement and received 20 per cent of the fees paid by CenITex for each contractor. The director of Company H did not declare his interest in the company to CenITex. The fees charged by Company H were also not disclosed to CenITex.⁵²

During my investigation, CenITex's contracts with Company B and Company H lapsed. These companies are not currently providing services to CenITex.

143. Fortunately, changed reporting requirements applied by CenITex to its recruitment agencies enabled CenITex to identify these 'pass through' arrangements and associated conflicts of interest.
144. Since 2011, CenITex has required that recruitment agencies provide details of all Australian Business Numbers (ABNs) for contractors that the recruitment agencies provide. CenITex uses this list to check whether two or more contractors are associated with the one company. This reporting led to CenITex identifying issues with the Company A, B, C and D engagements. Such reporting may lead to other government agencies identifying similar issues.
145. In response to my draft report, Mr Hehir, Secretary, DTF said:

There is no provision in the SPC [State Purchase Contract] that allows Masters Vendors to quote fees other than those specified in their respective agreements.

⁵¹ With the exception of one procurement record, which disclosed that the relevant contractor was being provided to the recruitment agency by another company. The record did not identify Company B nor disclose that it would charge a fee.

⁵² CenITex's *Outside Employment Policy* requires that CenITex staff and contractors declare if they are 'conducting a business, trade or profession' in order for CenITex to assess whether the employment creates a conflict of interest.

Fabricated records

146. My investigation identified that some CenITex contractors fabricated records in order to support their decisions to hire particular contractors. The contractors that were hired were identified through personal referrals and recommendations, rather than a competitive process.

CASE STUDY 13 - Identical selection reports

Four contractors were engaged by CenITex from Company B (the company) in early 2011. The documentation supporting their engagements was defective in that it:

- included the same résumé for three of the contractors (the résumé was missing a front page, was unidentified and did not match the qualifications or experience of any of the individuals)
- listed identical key duties for all four contractors, despite relating to different positions
- included identical scores for the key selection criteria for three of the contractors
- included identical selection summaries for three of the contractors, save for different names and position titles
- had clearly been cut and pasted for each contractor as the name of one contractor was in the selection summary of another contractor.

Each procurement record stated that the contractors had been transferred from an eServices vendor; however, my investigation established that only one of the four had worked with the vendor before.

The documentation supporting the selection of the company's contractors listed "Nicholas"⁵³ (a Program Manager) as an evaluator/selection panel member and Liam, a senior ETS Program Manager as either an evaluator/selection panel member or 'ETS approver'. However, at interview on 28 February 2012, Liam gave evidence that he did not attend interviews or evaluate any of the contractors. He said that he was recorded on procurement documentation due to an administrative process he implemented to ensure that he had visibility over CenITex's contractor-spend as a program manager. This was confirmed by a number of other staff members.

Liam's evidence that he did not evaluate any of the company's contractors means that Nicholas, alone, evaluated all contractors (with the exception of one contractor). This conflicts with the records purportedly documenting these engagements, which Liam signed as an 'evaluator' or 'approver'. It is also contrary to CenITex policy to rely on a single evaluator, and against good procurement practice.

Nicholas and Liam told my officers that they were unaware of the identical nature of the documentation, including the résumé, until my officers brought it to their attention.

The officers who approved the contracts apparently did not notice the duplication of material contained in the reports.

Nicholas resigned from CenITex during my investigation.

⁵³ This is a pseudonym.

147. I also identified that records were fabricated to support the engagement of Company A for a \$677,000 contract:

CASE STUDY 14 – False statement in procurement record implying level of competition

In October 2010, CenITex approved \$677,000 expenditure on Company A (the company) without any quotation, business case or other supporting documentation to demonstrate that the procurement represented good value for money or was aligned with CenITex’s business objectives.

The procurement record stated that an eServices Panel vendor had provided a ‘considerably higher’ quotation than the company and therefore ‘we are confident [the company] provides value for money’. However, no such quotation had been obtained when this document was created. This record, like others referred to in this report, was false and misleading. Instead, after the approval was granted, the relevant Program Manager, David, requested a quotation from the company to fit with the approved expenditure.

148. In addition, I identified several instances where procurement documentation falsely stated that contractor positions were advertised, leading those responsible for approving the engagements to believe that the positions were subject to competitive applications. There was no evidence that the positions were advertised.

Selection of contractors based on past work associations or personal referrals

149. My investigation identified that, in a number of cases, contractors and vendors were chosen on the basis of past work associations and personal referrals, rather than on demonstrated merit. There is therefore no reason to be confident that the contracts represented good value for money.

CASE STUDY 15 – Engagement of Company A

Company A (the company) was engaged in 2009 via an exemption.⁵⁴ CenITex procurement files did not record how the company was selected to perform work for CenITex. At the time of its initial engagement, the company was not on the eServices panel and had only been registered as an Australian Proprietary Company for 19 months.

My investigation identified that the company was introduced to CenITex by a CenITex Manager who had previously worked with a director of the company. A CenITex Program Manager (David) subsequently interviewed a director of the company and it was awarded a contract for \$44,000. There was no formal record kept of the contents of the interview and there is no evidence that anyone else was interviewed. CenITex did not conduct a competitive process for this contract or any subsequent contracts that it awarded the company.

In total, CenITex approved expenditure of almost \$3 million for the company and its contractors over the life of its contractual relationship, of which over \$1.7 million was subsequently paid to the company and its contractors.

⁵⁴ See the section entitled, ‘Absence of open and fair competition’ case study 9.

150. Company B was also engaged on the basis of past work associations and a personal referral:

CASE STUDY 16 - Engagement of Company B

CenITex first engaged Company B (the company) following a (sham) Request for Quotation (RFQ) in February 2010.⁵⁵ At the time of the RFQ, the company had no web presence or business cards and was not listed on the eServices Panel. At interview, one of its contractors described it as a company that was 'not mature enough' to win business.

My investigation identified that the company was introduced to CenITex by a CenITex contractor (Robert⁵⁶) who had previously worked with the director of the company. At around the same time, Robert started a personal business relationship with the company.⁵⁷

151. Several Company B contractors were later engaged by CenITex. The CenITex Program Manager responsible for selecting the contractors allowed the director of Company B to play an inappropriate role in their selection and engagement:

CASE STUDY 17 - Director of company influences engagement of contractors

During 2011, Company B (the company) supplied at least six contractors to CenITex. The evidence supporting the director of the company's influence in the selection of these contractors is considerable. Only contractors suggested by the director were interviewed by CenITex. When asked about this at interview, the director said:

I had - you know, the people, and I said to CenITex, "Look, you know, I've got these people that are capable of doing what you wanted to do, interview them if you like, and I can put them in".

One contractor from the company gave evidence to my officers that the director was present at his interview with CenITex. The director of the company said he did not attend interviews; however, he said he did attend 'meet and greets' with the interviewees.

Another contractor told my officers that the director 'was doing the recruiting, he was like an agent'. This is consistent with emails located by my officers, which demonstrate that the director:

- identified individuals with relevant skills to complete CenITex work
- told potential contractors that he could get them an interview with CenITex, assisted them in updating their résumés and provided their résumés to CenITex
- facilitated contractors being interviewed by CenITex for positions by requesting Nicholas⁵⁸ (the Program Manager) 'set up' interviews and emailing electronic invitations to contractors and Nicholas for interviews
- confirmed individuals' rates of pay with CenITex.

⁵⁵ See the section entitled, 'Absence of open and fair competition', case study 8.

⁵⁶ This is a pseudonym.

⁵⁷ See the chapter entitled, 'Conflict of interest', case study 3.

⁵⁸ This is a pseudonym.

It was clearly inappropriate for CenITex to allow the director to influence its engagement of contractors when he stood to benefit financially if contractors from his company were selected.

152. In another case, all three members of an interview panel recommended an applicant with whom they had each previously worked. The appointment was considered a *'fait accompli'*; the procurement documentation was therefore prepared to support the decision:

CASE STUDY 18 – Engagement of former co-worker

During my investigation, CenITex provided me with a probity report it commissioned in July 2011 in relation to the attempted engagement of “Helen”.⁵⁹ As a result of the probity report, CenITex identified irregularities with this engagement and prevented it from going ahead.

The CenITex interview panel for the engagement consisted of three senior CenITex contractors. The probity report found:

- The members of the interview panel were contractors who had worked with Helen, but each declared that they did not have a conflict of interest.
- Individuals' knowledge of candidates was the main driver of candidate identification and selection processes.
- The role was not advertised and there was no job description.
- A CenITex HR Consultant prepared the paperwork for the engagement, although she did not attend the interview of Helen. The consultant inserted the number '4' against the blank key selection criteria section of the report because she said Helen 'ticked all the boxes'. (The number '4' lacked any meaning as no key selection criteria had been developed).
- The CenITex HR Consultant stated that the board had already approved the appointment of Helen and it was considered a *'fait accompli'*.

In addition:

- There was no attempt to assess value for money (i.e. the candidate's daily rate was not queried or negotiated).
- CenITex's records stated the position was a VPS Grade 6 (up to \$175,000 per annum, including contractor premiums), but the contract value was \$356,867.
- The interview panel did not check the paperwork before signing it.

CenITex counselled the officers and contractors involved and the engagement did not go ahead.

Pre-billing and double-billing

153. Pre-billing involves billing for services not yet provided. While it may be common in the private sector, it is generally not acceptable in the public sector as there is a risk that the agency will not receive the services that it paid for. Where it is considered to be appropriate, it needs to be clearly documented.

⁵⁹ This is a pseudonym.

154. My investigation identified that a CenITex Program Manager requested a vendor pre-bill over \$50,000 for services. He requested that this not be disclosed in invoices as he knew CenITex would not pay for pre-billed services:

CASE STUDY 19 - Pre-billing hidden from CenITex

At the end of the 2010-11 financial year, a CenITex Program Manager (David) requested that Company A (the company) 'pre-bill' for over \$50,000 worth of services not yet provided to CenITex. At interview, David said he was instructed by Liam (senior ETS Program Manager) to 'pre-bill' so that ETS could 'carry forward' funding and enable CenITex to consume its 2010-11 budget.

David said he asked the company to submit three invoices for days worked in June 2011 by three contractors, totalling over \$50,000. These invoices do not indicate that they relate to services that had not yet been provided. David said at interview that he requested that this 'pre-billing' not be disclosed to CenITex in the company's invoices as, if it had been clear on the invoices that they were for pre-billing, CenITex 'wouldn't pay them'. David initialled the invoices, thereby indicating to CenITex Accounts Payable that the services had been provided. The invoices were approved and paid by CenITex.

There was no documentation on the CenITex files about the pre-billing. It appears the only record was an email David kept to track the hours owed by the company. According to David, Liam and others 'alluded' that documentation should be kept 'fairly loose'.

While the company submitted invoices in June 2011 for services that had not yet been provided, it also submitted invoices for services that had been provided in that month. This led to invoices that claimed for services provided on more days than there are in the month. For example, while there are 30 days in June, the company invoiced for:

- 43 days for one contractor (21 worked and 22 pre-billed)
- 41 days for another contractor (19 worked and 22 pre-billed).

The company also submitted three additional invoices for a total of 18.5 days worked by unnamed contractors in June 2011.

All the above invoices submitted by the company were paid without question. They totalled over \$100,000.

Poor record-keeping

155. Poor record-keeping hinders effective oversight of procurement and recruitment decisions and creates an environment that allows opportunities for improper conduct.
156. My investigation identified poor record-keeping in relation to a number of engagements. Many of the errors and omissions were apparent on the face of the documentation. Consequently, I consider that in some cases, CenITex decision-makers either did not adequately check the documentation that they were approving or were unconcerned about these shortcomings.

157. An examination of CenITex's procurement records identified the following deficiencies:
- records were falsified to support decisions and expedite the process, rather than to document the decision-making process and justification
 - interviews with applicants were not recorded
 - procurement records were not assigned a tracking number and were submitted without signatures or dates
 - invoices were submitted against incorrect purchase orders and contracts
 - an exemption was used after its expiry and in excess of the authorised expenditure
 - procurement records and invoices failed to identify the name of the contractor being billed for, creating opportunities for double-billing.

Conclusions

158. I have identified significant deficiencies in the procurement and recruitment practices of CenITex. The officers involved, predominantly contractors, failed to comply with CenITex policies and VGPB principles, designed to ensure the best use of public resources.
159. Policies and procedures were viewed by some CenITex contractors as hurdles that needed to be overcome to deliver a project, rather than processes designed to ensure that public monies were spent appropriately. Other contractors said they were unfamiliar with CenITex's internal policies and unaware of VGPB requirements.
160. Companies, and their contractors, were awarded significant contracts valued at up to \$4 million without any competitive process. Creative steps were sometimes employed to get around processes viewed as untimely. In one instance, a competitive process was ostensibly conducted; but, in reality it was a sham.
161. In some instances, nepotism and favouritism informed procurement and recruitment practices. Often, the companies or contractors were chosen because they were associates or friends of other contractors already working at CenITex; some appointments were made on the basis of false and misleading documentation. Others were initiated or overseen by individuals within CenITex who had a clear conflict of interest and stood to gain financially from the transactions.
162. Contractors were also engaged at excessive rates, without any evidence that these were negotiated. Unknown to CenITex office holders, CenITex also paid high fees to companies that were providing contractors to CenITex through recruitment agencies. The companies' roles were not disclosed to CenITex. In one case, the fee paid to a company was 50 per cent of the contractor's \$1,600 daily rate.

163. My concerns about the procurement and recruitment practices of CenITex are supported by audits and reviews commissioned by CenITex after my investigation commenced, which identified an ‘underlying culture within CenITex where compliance with probity principles and processes has not been a priority and a focus’.
164. Such practices can lead to reputational damage and diminish market confidence in CenITex and the public sector more broadly.
165. Most of the contractors involved in the engagements discussed above left CenITex prior to or during my investigation.⁶⁰

Recommendations

I recommend that CenITex:

Recommendation 9

Ensure that all individual contracts require that contract staff be aware of and subject to the VPS Code of Conduct.

Recommendation 10

Conduct a process that accords with key VGPB purchasing principles prior to re-engaging Company A, Company B or their contractors.

Recommendation 11

Review procurement records related to engagements of Company G to determine whether CenITex officers have engaged in contract-splitting.

Recommendation 12

Review its accounts approval and processing practices to reduce the risk of double-billing and pre-billing.

Recommendation 13

Review Company A invoices to ensure that invoiced time has been used and, if necessary, seek reimbursement of any over payment.

Response

In response to my recommendations, Mr Vanderheide, CEO, CenITex said:

I offer my in principle acceptance of each of the recommendations related to CenITex and intend to periodically advise you as to our progress in their implementation.

⁶⁰ See footnote 1.

I recommend that the Department of Treasury and Finance and VGPB:

Recommendation 14

Review the Staffing Services Panel State Purchase Contract to require that recruitment agencies (master vendors) declare subcontracting relationships and provide details of all fees, including those charged by third-parties.

Response

In response to my recommendation, Mr Hehir, Secretary, DTF, said:

There is no provision in the SPC [State Purchase Contract] that allows Masters Vendors to quote fees other than those specified in their respective agreements.

Summary of recommendations

I recommend that:

Recommendation 1

CenITex require its internal auditors to undertake a greater proportion of compliance audits than was previously conducted, particularly in high risk areas, to ensure compliance with internal policies and VGPB guidelines.

Recommendation 2

CenITex include compliance with the CenITex procurement and recruitment policies, Victorian Government Purchasing Board (VGPB) guidelines and the VPS Code of Conduct as a requirement in the Performance Development Plans of contractors and staff.

Recommendation 3

CenITex provide all staff and contractors with regular training on conflict of interest, the VPS Code of Conduct and the Whistleblowers Protection Act, as well as other matters relevant to their position and responsibility, including procurement and recruitment policies and the VGPB guidelines.

Recommendation 4

CenITex regularly remind all contractors and staff of the restrictions on outside employment (as set out in the CenITex *Outside Employment Policy*) and require that, if staff conduct an outside business, trade or profession, this must be immediately declared to their manager so that CenITex can determine whether a conflict of interest exists.

Recommendation 5

CenITex consider the appropriateness of allowing CenITex staff and contractors to accept overseas flights and accommodation from CenITex vendors. If it is considered that there is a public interest in accepting such hospitality from a vendor, ensure this is clearly documented by the decision-maker.

Recommendation 6

CenITex refer “Daniel’s” conduct to Victoria Police for investigation in relation to misconduct in public office and fraud.

Recommendation 7

CenITex consider excluding Company D from future tenders and contracts.

Recommendation 8

CenITex consider cancelling any current engagements related to “John” and his companies and conduct a process that accords with key VGPB purchasing principles prior to re-engaging “John” or his companies.

Recommendation 9

CenITex ensure that all individual contracts require that contract staff be aware of and subject to the VPS Code of Conduct.

Recommendation 10

CenITex conduct a process that accords with key VGPB purchasing principles prior to re-engaging Company A, Company B or their contractors.

Recommendation 11

CenITex review procurement records related to engagements of Company G to determine whether CenITex officers have engaged in contract-splitting.

Recommendation 12

CenITex review its accounts approval and processing practices to reduce the risk of double-billing and pre-billing.

Recommendation 13

CenITex review Company A invoices to ensure that invoiced time has been used and, if necessary, seek reimbursement of any over payment.

Recommendation 14

The Department of Treasury and Finance and VGPB review the Staffing Services Panel State Purchase Contract to require that recruitment agencies (master vendors) declare subcontracting relationships and provide details of all fees, including those charged by third-parties.

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Investigation into the issuing of infringement notices to public transport users and related matters
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Own motion investigation into Child Protection - out of home care
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Report of an investigation into Local Government Victoria's response to the Inspectors of Municipal Administration's report on the City of Ballarat
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Whistleblowers Protection Act 2001 Investigation into the disclosure of information by a councillor of the City of Casey
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Brookland Greens Estate – Investigation into methane gas leaks
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A report of investigations into the City of Port Phillip
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An investigation into the Transport Accident Commission's and the Victorian WorkCover Authority's administrative processes for medical practitioner billing
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Whistleblowers Protection Act 2001 Conflict of interest and abuse of power by a building inspector at Brimbank City Council
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Investigation into corporate governance at Moorabool Shire Council
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Crime statistics and police numbers
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Whistleblowers Protection Act 2001 Report of an investigation into issues at Bayside Health
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Investigation into contraband entering a prison and related issues
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Investigation into the disclosure of electronic communications addressed to the Member for Evelyn and related matters
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Investigation into the use of excessive force at the Melbourne Custody Centre
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Investigation into the Office of Housing's tender process for the cleaning and gardening maintenance contract – CNG 2007
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Investigation into a disclosure about WorkSafe's and Victoria Police's handling of a bullying and harassment complaint
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Own motion investigation into the policies and procedures of the planning department at the City of Greater Geelong
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Investigation into parking infringement notices issued by Melbourne City Council
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Improving responses to allegations involving sexual assault
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Investigation into the handling, storage and transfer of prisoner property in Victorian prisons
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Whistleblowers Protection Act 2001 Ombudsman's guidelines
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Own motion investigation into VicRoads registration practices
June 2005

Complaint handling guide for the Victorian Public Sector 2005
May 2005

Review of the *Freedom of Information Act 1982*
Discussion paper
May 2005

Review of complaint handling in Victorian universities
May 2005

Investigation into the conduct of council officers in the administration of the Shire of Melton
March 2005

Discussion paper on improving responses to sexual abuse allegations
February 2005

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Essendon Rental Housing Co-operative (ERHC)
December 2004

Complaint about the Medical Practitioners Board of Victoria
December 2004

Ceja task force drug related corruption – second interim report of Ombudsman Victoria
June 2004

