

SOUTH AUSTRALIA

Report

of the

Auditor-General

for the

Year ended 30 June 2002

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Supplementary Report

**Report on the Process of Procurement of
Magnetic Resonance Imaging Equipment by the
North Western Adelaide Health Service**

By Authority: J. D. Ferguson, Government Printer, South Australia



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Gentlemen,

**Auditor-General's Supplementary Report: Report on the Process of Procurement of
Magnetic Resonance Imaging Equipment by the North Western Adelaide Health Service**

Pursuant to the provisions of section 36(3) of the *Public Finance and Audit Act 1987*, I herewith provide to each of you a copy of my Supplementary Report 'Report on the Process of Procurement of Magnetic Resonance Imaging Equipment by the North Western Adelaide Health Service'.

Yours sincerely,

K I MacPherson
AUDITOR-GENERAL

Supplementary Report: Report on the Process of Procurement of Magnetic Resonance Imaging Equipment by the North Western Adelaide Health Service

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EXECUTIVE SUMMARY

BACKGROUND

On 7 May 2002, Dr R Davies, whilst an employee of North Western Adelaide Health Service (NWAHS), (Dr Davies resigned on 30 June 2003) executed documentation for the supply to NWAHS of a 1.5 Tesla Magnetic Resonance Imaging (MRI) machine from Philips Medical Systems Australia Pty Ltd (PMSA). The cost of the machine exceeded A\$2 million. The Crown Solicitor subsequently advised that this documentation created enforceable contractual obligations between NWAHS and PMSA for the purchase of the machine. In executing the relevant document Dr Davies purported to act on behalf of NWAHS. In so doing, Dr Davies acted without the authority or prior approval of relevant authorities, including the Board of NWAHS, the Department for Human Services (DHS), the Minister for Health, or the State Supply Board.

At the time of the execution of the document for the acquisition of the 1.5 Tesla MRI machine, there was, to Dr Davies' knowledge, an already existing contract for the purchase of a 0.5 Tesla MRI machine. The purchase of the 0.5 Tesla MRI machine had been approved by the proper authority¹ and reflected the implementation of a policy decision made at Cabinet level by the then Government of the day.

FUNDAMENTAL PRINCIPLES

Good and proper public administration necessitates adherence by public sector employees to those principles and values that are essential to protect the community from the arbitrary exercise of governmental power and the misapplication of public monies.² These principles and values include compliance with relevant statutory requirements and the obligation of public employees to act with impartiality and objectivity, and with loyalty and fidelity to the Government of the day, in this case the then Liberal Government.

Public sector employees³ are required to serve governments of any political persuasion and must not knowingly and intentionally frustrate the implementation of the legitimate policy goals of the Government of the day.

This is an issue that transcends the party political process and goes to the values that underpin the system of government in this State. It is not for public employees to anticipate the outcome of a general election in deciding whether or not to implement a particular decision already made by the Government of the day, especially where these decisions are made outside the period of any caretaker conventions.

¹ ie the NWAHS Board.

² Adherence to these principles is also essential to protect public sector employees themselves from accusations of political partisanship and even of acting corruptly.

³ Ministerial Staffers whose employment tenure is directly related to the political fortunes of their Minister are, in my opinion, required to comply with those principles and values applicable to all government employees in discharging governmental functions within their Ministerial offices.

In matters where it is sought to persuade a government to change a decision, it is essential that this be done transparently, through proper processes, and by the proper authority or authorities. In this matter, the change in the contractual arrangements was done intentionally and without the knowledge of the proper authorities.

There was also a failure to disclose the unauthorised change to contractual documentation in a timely way to those in authority who were entitled to be so informed. This compounded the seriousness of this matter.

In my opinion, failure to comply with the abovementioned principles undermines public confidence in the administrative processes of government.

AUDIT OPINION

For the reasons stated in this Report, in my opinion, the financial transaction in this matter was not conducted properly. I am also of the opinion, for the reasons stated in this Report, that the conduct of Dr Davies (the then Head of the Department of Radiology at the Queen Elizabeth Hospital (QEH) campus of NWAHS) and Mr Campos (the then Chief Executive Officer at QEH), as public employees, is a matter that should be brought to the attention of the Government and the Parliament.

In my opinion, the financial transaction in this matter was not conducted lawfully. In my opinion, the financial transaction was conducted unlawfully in that it was entered into by a public employee, ie Dr Davies, who lacked the lawful authority to do so, who acted in a manner contrary to his duty as a public employee, and who in so doing, may have unlawfully interfered with the contractual rights of his employer. Further, prima facie Mr Campos did not ensure compliance with the appropriate Treasurer's Instructions to ensure that there was compliance with the relevant (contracting and expenditure) authorisations within NWAHS.

WHAT WENT WRONG AND WHY

Three key (and, in my opinion, wrong) decisions were made in this matter.

First, a decision was made to defer delivery of MRI equipment that had been authorised and contracted for by the then (Liberal) Government of the State in order to 'create a space' within which political promises of additional funding made by the then (ALP) Opposition could be fulfilled, if it won the 2002 election.

Secondly, a decision was made after the 2002 election to secure delivery to NWAHS (QEH) of MRI equipment the purchase of which had not been properly authorised, in anticipation of what were thought to be likely approvals.

Thirdly, documents that had legal and financial consequences for NWAHS and the Government of South Australia were (in one case ie a purchase order) altered and (in another case ie a grant) executed, without lawful authority.

In my opinion, responsibility for the first two decisions rests with Dr Davies and Mr Campos. In my opinion, responsibility for third decision (unauthorised alteration and execution of documents) rests with Dr Davies.

Dr Davies and Mr Campos embarked upon a course of action that they knew was incompatible with the timely implementation of a lawful decision of the then Liberal Government manifested in the form of an approved contractual arrangement (ie for the acquisition of an 0.5 Tesla MRI machine for the QEH). That course of action was contrary to their duty as public employees, ie to act with loyalty and fidelity and to faithfully implement the lawful policy and other decisions of that Government.

Dr Davies knowingly and intentionally changed a purchase order and accepted a quote that, in my opinion, had the result of interfering with the existing contractual arrangements between NWAHS and PMSA.

Mr Campos concurred with Dr Davies in arranging for PMSA to deliver to QEH a 1.5 Tesla MRI machine knowing that this was contrary to the existing approved arrangements and the existing contract, albeit on the basis that PMSA would swap the 1.5 Tesla MRI machine for a 0.5 Tesla MRI machine if the necessary approvals were not forthcoming. In fairness to Mr Campos, it must be stated that he neither expected nor knew that Dr Davies would execute documentation that created a new contractual relationship with PMSA.

Mr Campos' conduct raises issues that, in my opinion, concern matters of propriety and regularity in public administrative arrangements. In essence, his conduct involved questions of judgment. Nonetheless, in my opinion, that judgment should have been exercised in accordance with the applicable legal requirements as was incumbent on him as Chief Executive Officer of the QEH and the principles that inform the conduct of public employees transacting public business. His conduct was inconsistent with what was required of a Chief Executive Officer in the circumstances that confronted him, that is, to act openly with his Board and DHS and his responsibility to ensure compliance with applicable regulatory and administrative requirements.

I have also considered whether the conduct of this transaction generally, and the actions of Dr Davies and Mr Campos in particular, were justified by the statements made by representatives of the then Opposition, both prior to, and after the announcement of the calling of the election on 9 February 2002. The election resulted in a change of Government. The statements in question were political promises of additional funding. They were not statements that justified or authorised the decision to proceed with an acquisition of a particular strength MRI machine, or in fact any MRI machine, at that, or any later time, without approval from the relevant authorities. Accordingly, in my opinion, Dr Davies and Mr Campos were not justified in acting as they did by those statements.

When they made the decision to put delivery of the 0.5 Tesla MRI machine on hold, there should have been full and prompt disclosure to the Board of NWAHS (or at the very least the QEH sub-Board), and to DHS. When they made a decision to invite a fresh quote for a 1.5 Tesla MRI machine, full and prompt disclosure of the commencement of a new procurement process should have been made. Notwithstanding the fact of discussions with DHS regarding the matter of the MRI machines, the fact of these decisions (and particularly the last of them) was withheld from relevant authorities, until late in the process.

It is not for public employees to frustrate or in any other way impede the implementation of the lawful decisions of the Government of the day.

In their comments on my draft report, both Dr Davies and Mr Campos submitted to me that in placing the order for the 0.5 Tesla MRI machine 'on hold' they were serving the Government of the day, and that it is therefore unfair to criticize them for doing so. In effect, their argument is that because the incoming Government had clearly signalled a desire to provide additional funding for MRI equipment at QEH, they had an obligation to create the space necessary for the new Government to fulfil its wishes.

In my opinion, this argument is unsound. The fact is that before the election that resulted in the change of government at the beginning of 2002 was called, a contract for the acquisition of the 0.5 Tesla MRI machine had been entered into. Dr Davies and (particularly) Mr Campos were obliged to pursue and facilitate the due execution (ie the performance) of that contract, unless and until the responsible parties (ie the NWAHS Board, DHS or Executive Government, not Dr Davies or Mr Campos) decided otherwise. If delivery of the 0.5 Tesla MRI machine was to be suspended, that required a decision (at the least) of the Board of NWAHS. No such decision was made by the Board. Proper conduct of the matter would also have entailed the Board, DHS and the Minister being advised quite plainly that any consideration of additional funding for upgraded MRI capacity at QEH had to be in the context of a contract for the acquisition of the 0.5 Tesla MRI machine having already been entered into.

It was not a trivial matter to 'switch' to a 1.5 Tesla MRI machine. The probity issues and the procurement processes alone were significant, but they do not appear to have been appreciated, let alone been the subject of a comprehensive briefing to the Minister.

It was also submitted to me that the incoming government's request for a business case for 'new' MRI machines required that the order for the 0.5 Tesla MRI machine be put on hold. In my opinion this is not correct. It is also not the course of action that was decided upon by the Chief Executive of the Lyell McEwin campus of NWAHS. This submission blurs the fact that it is the conduct of Dr Davies and Mr Campos in the period prior to the calling of the 2002 General Election that is the basis for the criticism that has been made in this Report regarding the failure to act with loyalty and fidelity to the Government of the day.

Dr Davies submitted that had he 'not acted as he had, to preserve, by the only means open to QEH, the option of QEH acquiring a 1.5 Tesla MRI machine the government's promise [of additional funding] would never have been fulfilled and the funding allowed in the budget could never have been put to that use.' In my opinion, in making this submission Dr Davies fails to understand his responsibilities as a public officer and this comment provides a further insight into Dr Davies' approach in this matter. It was not his role or function to convert a political promise into a legal and practical outcome, but in my view, that is what he (successfully) set out to do.

SOME OTHER MATTERS THAT ARE RELEVANT TO THIS TRANSACTION

Other aspects of this matter give rise to concerns that in my opinion should be brought to the attention of the Government and the Parliament.

Errors of Judgment and Improper Behaviour

The facts of this matter reveal several points at which errors of judgment (at the least) were made by Dr Davies and Mr Campos.

In my opinion, Mr Campos committed an error of judgment in not insisting that the important negotiations with PMSA relating to the procurement of the MRI machines (and especially those relating to the procurement of the 1.5 Tesla MRI machine) for QEH be primarily conducted by his procurement staff, rather than a member of his medical staff. In my opinion, this error of judgment provided the opportunity for Dr Davies to commit the unauthorised act of executing documentation with PMSA for the 1.5 Tesla MRI machine.

In my opinion, Mr Campos also failed to take sufficient care to protect NWAHS from the very risk that he had identified in his conversations with Dr Davies — that the approvals required for the 1.5 Tesla MRI machine would not be forthcoming, and the right to revert to the 0.5 Tesla MRI machine would need to be exercised.

In my opinion, Dr Davies committed a serious breach of his duties as a public employee in executing contract documents on behalf of NWAHS at a time when he knew the required approvals were not in place.

Dr Davies knew that he had changed the contractual documentation with PMSA, that the order for the approved 0.5 Tesla MRI machine had been 'put on hold', that the order with PMSA was now for a 1.5 Tesla MRI machine and that there was no approval by a proper authority for a 1.5 Tesla MRI machine. Further, he knew that delivery of a 1.5 Tesla MRI machine was to be made to QEH. Notwithstanding these important facts, he remained silent regarding his actions in a meeting with DHS officers in which he was informed that fresh State Supply Board and Cabinet approvals were necessary for the acquisition of a 1.5 Tesla MRI machine. Dr Davies' silence is significant in the context of the reason for this meeting.

On the basis of all of the evidence, Dr Davies, in my opinion, at this meeting must have known that DHS officers were not aware that he had changed the documented contractual relationship with PMSA to purchase a 1.5 Tesla MRI machine.

On the basis of all the evidence, in my opinion, Dr Davies should have disclosed to the DHS officers what he had done. I am satisfied that this matter would have progressed very differently had he done so. This is not to deny that others (such as Mr Campos) should also have made disclosure to DHS of the arrangement that had been entered into with PMSA (to the extent that they had knowledge). Nonetheless, Dr Davies did not make the disclosure that, in my opinion, he should have made when he had the opportunity to do so.

The Importance of Procedural Regularity

The facts of this matter also illustrate the importance of procedural regularity in public administration. The control arrangements within government are designed to limit the possibility of abuse of power and authority by any particular person or entity within the public sector. They also create an essential safeguard for the achievement of the policy objectives of government. These control arrangements break down when there is (as in this case) a lack of openness by those that have a responsibility to ensure compliance with the applicable controls.

Public employees who pursue objectives that are at odds with approvals that have been given after consideration by proper authorities, and who thwart, in this case secretly, the implementation of approved arrangements, in my opinion, behave improperly.

Irrespective of the motives of Dr Davies and Mr Campos, their conduct compromised the Government's position vis a vis PMSA in this matter. To claim that their actions were merely pre-emptive of arrangements that they anticipated could or would be made in any event is not to the point. The decisions they made to put the existing contract 'on hold', to have the 1.5 Tesla MRI machine delivered, and (in the case of Dr Davies), to execute documentation with contractual consequences, were not their decisions to make.

Public Employees Engaging with the Political Process

Public employees are employed to implement the lawful policy objectives of the Government of the day, and in a manner consistent with the values that inform and direct public sector employment. In this matter, the Government of the day had decided to acquire a 0.5 Tesla MRI machine. That decision had been made by the proper authorities. In my opinion, Dr Davies engaged with the political process in order to secure a different outcome for QEH.

There can, in my opinion, be no criticism of the fact that a public employee has political affiliations or contacts (or both), provided there is no compromise of his or her obligations as a public employee to the Government of the day. It is also important to emphasise that, in my opinion, it is open to any member of the Parliament to contact a public sector agency to seek information and in some circumstances, advice. It is for the public sector employee, having regard to any instructions that may have been lawfully given, to conduct him or herself in accordance with those instructions and within the appropriate boundaries consistent with that employee's obligations to the Government of the day. It would generally be accepted that a public sector employee is under a standing direction to refer inquiries by a member of Parliament⁴, other than routine administrative matters, to the employee's Chief Executive.

To deliberately frustrate the implementation of a lawful decision entered into by the Government of the day, in anticipation of the outcome of an election, in my opinion, is at least to act improperly, if not unlawfully. Conduct that knowingly and intentionally, and without justification, interferes with the contractual rights of an employer, resulting in damage to that employer, is unlawful, ie tortious.

The Matter of Political Accountability

NWAHS is a statutory body with corporate personality and a governance structure prescribed by the *South Australian Health Commission Act 1976* (the SAHC Act).

The proper scope and nature of the relationship of the Minister to NWAHS is set out in the SAHC Act.

⁴ Particularly any matters raising policy issues.

In my opinion, the communication by the former Minister (for Human Services) of 23 October 2001 with the Board of NWAHS was not consistent with the SAHC Act. Nonetheless, I accept that it was a communication made in good faith.

Likewise the 3 July 2001 letter from the then Chief Executive, DHS, to the then Chair of the Board of NWAHS in purporting to impose conditions on its ongoing funding of NWAHS that included, amongst other things, a requirement that NWAHS Board appoint a DHS nominee to its sub-Boards, with that nominee empowered to exercise certain financial powers independently of the Board, was, in my opinion, inconsistent with the statutory scheme of an independent board of management of hospitals contemplated by the SAHC Act.

The result of the two communications was to place the members of the Board of NWAHS in a difficult position. Accountability for the financial position, in particular, of NWAHS was blurred, and transparency was lost. The Board continued to have the statutory responsibility for the administration of the hospital but was handicapped in the discharge of its duties.

The Legal Advice Obtained by DHS

As discussed in this Report, NWAHS eventually asked DHS to seek legal advice as to its position with PMSA. However, the information provided to the legal adviser in the brief seeking legal advice was not sufficiently comprehensive. The result was that only 'preliminary' legal advice as to the State's position was obtained.

The absence of proper, comprehensive and definitive legal advice meant that legal and commercial options that might have been in the interests of the State were not identified, let alone explored.

The Quality of the Procurement Process Generally and the Lack of Competitive Tension

The controls associated with the conduct of the procurement process in this matter generally were inadequate in terms of good and proper public administration.

The letter that initiated the process with the potential suppliers (ie Appendix C to this Report) was little more than a request for information, yet it was used as a basis for the whole of the process that followed.

The process adopted was largely free of competitive tension in relation to price or contract terms, particularly once the announcement was made of the additional \$1.5 million funding. The manner in which the process was conducted, at least for QEH, was that the customer was a taker of offered terms, rather than an indicator of desired terms. In my opinion, this is not best practice procurement, even for second hand equipment.

The length of time taken for the process also meant that issues arose as to the particular MRI machines on offer. The 1.5 Tesla MRI machine finally purchased was not the 1.5 Tesla MRI machine originally offered by PMSA in response to the August 2001 letter from NWAHS. At the time NWAHS had the option to return the 1.5 Tesla MRI machine and substitute a 0.5 Tesla MRI machine, it also appears that PMSA would have had to have

located another 0.5 Tesla MRI machine, as the device originally offered had been sold elsewhere. This may have been material to the legal position of the parties.

It is unnecessary for me to chronicle all of the defects in the procurement process that was undertaken. Suffice it to say that there is a need for DHS to work further with NWAHS to improve the level of understanding at NWAHS of best practice procurement, and the responsibility and accountability framework that applies to procurement in the South Australian public sector. In particular, there is also a need to emphasise the proper, but limited, role that clinical staff should have in procurement activity for hospitals.

Furthermore, in my opinion, it would be constructive for DHS to consider ways in which the approvals processes for time sensitive procurements might be expedited.

Other matters that in my opinion should be brought to the attention of the Government and the Parliament are discussed in section 7.2 of this Report.

1.0 WHY THE AUDIT EXAMINATION WAS CONDUCTED

1.1 Background

On or about 21 June 2002, North Western Adelaide Health Service (NWAHS) took delivery of a Magnetic Resonance Imaging (MRI) machine at its Queen Elizabeth Hospital (QEH) campus from a company within the global Philips Group.

The machine that was delivered was a '1.5' Tesla strength machine. The purchase price was \$2.234 million (plus GST).

The arrangement for the acquisition of this machine was made notwithstanding the fact that Cabinet and the State Supply Board had previously approved the acquisition of a lower strength (0.5 Tesla), lower cost MRI machine. Neither had approved the acquisition of the 1.5 Tesla MRI machine.

1.2 Request for Examination to be Undertaken

By letter of 8 August 2002, the Honourable Patrick Conlon MP, Acting Treasurer advised the Auditor-General that the Department of Human Services (DHS) was conducting an internal audit review of the circumstances surrounding the acquisition of the 1.5 Tesla MRI machine. The Acting Treasurer also asked:

Since this matter is of material consequence, and relates to control issues within DHS and NWAHS, I would be grateful if you would give consideration to undertaking a review of the matter as part of your audit responsibilities under the Public Finance and Audit Act 1987.

The request was affirmed when the Honourable Kevin Foley MP, Treasurer, wrote to the Auditor-General on 13 August 2002.

Having regard to the materiality of this transaction and other matters of importance to the Government and the Parliament, I have undertaken an audit examination as part of my responsibilities in respect of NWAHS under the *Public Finance and Audit Act 1987*, and the *South Australian Health Commission Act 1976* (the SAHC Act).

1.3 This Report

This Report outlines the manner in which the examination was undertaken, some of the evidence obtained in the course of its conduct and the opinion(s) reached on its completion.

2.0 SCOPE OF THE EXAMINATION

The scope of the examination was as follows:

- ascertaining the facts relating to the conduct of the procurement process that resulted in the acquisition of the 1.5 Tesla MRI machine, including aspects of the related funding, approval and negotiation processes;

- forming a view as to whether the process was conducted lawfully, and was otherwise conducted properly in the circumstances;
- to the extent that unlawful or improper conduct was identified (if any), forming an opinion as to the matters that caused or contributed to the commission of that conduct; and
- forming an opinion as to whether the controls exercised by DHS and NWAHS in relation to the expenditure of money, the acquisition of property and the incurring of liabilities were sufficient to provide reasonable assurance that the financial transactions of NWAHS were conducted properly and in accordance with law.

3.0 AUDIT MANDATE

Section 36 of the *Public Finance and Audit Act 1987* sets out the requirements for the reporting responsibilities of the Auditor-General. In particular, section 36(1)(a)(iii) requires that the Auditor-General prepare an annual report that states whether, in the Auditor-General's opinion:

... the controls exercised by the Treasurer and public authorities in relation to the receipt, expenditure and investment of money, the acquisition and disposal of property and the incurring of liabilities is sufficient to provide reasonable assurance that the financial transactions of the Treasurer and public authorities have been conducted properly and in accordance with law

...

Section 36 also requires that I set out any (other) matter that should, in my opinion, be brought to the attention of Parliament and the Government.

Finally, section 36(3) provides that I may prepare a Supplementary Report relating to a matter to be dealt with in an annual report, and deliver that Supplementary Report to the Parliament.

This Report is a 'Supplementary Report' within the meaning of that section.

4.0 CONDUCT OF THE EXAMINATION

In the course of my audit of this matter, I have examined relevant documentation, and interviewed relevant participants.

In the interests of natural justice, I provided on a strictly confidential basis, the whole of, or extracts from, a draft of this Report to a number of individuals, including those whose conduct was subject to adverse comment in the draft. My purpose in so doing was to give each such individual an opportunity to make submissions to me in relation to the draft. Most (though not all) of those individuals made written submissions to me on the draft. I gave careful consideration to each of those submissions, and as a result of them made a number of changes to the draft in finalising this Report.

In this audit examination, I have applied the standard of proof on the balance of probabilities in dealing with issues and in drawing conclusions.⁵

On the basis of all of the evidence available to me I have formed an opinion as to whether the transaction that was undertaken was conducted properly and in accordance with law.

I have also considered whether the circumstances of the matter give rise to any other issues that, in my opinion, should be brought to the attention of the Government and the Parliament.

5.0 CONTEXT — THE RESPONSIBILITY AND ACCOUNTABILITY FRAMEWORK FOR PROCUREMENT IN THE SOUTH AUSTRALIAN PUBLIC SECTOR

5.1 Introduction

In order to express the opinion required by section 36(1)(a)(iii) of the *Public Finance and Audit Act 1987* in respect of the procurement process conducted by NWAHS for the 1.5 Tesla MRI machine for QEH, regard must be had to the responsibility and accountability framework within which procurement processes must be undertaken within the public sector in South Australia generally, and by public hospitals in particular.

That framework derives from several separate legislative provisions, and provides that a number of entities have a role in public hospital procurement.

5.2 NWAHS

NWAHS is an incorporated hospital established under the SAHC Act. It was gazetted as such on 28 September 1995. Its two principal ‘campuses’ are the Queen Elizabeth Hospital (QEH) at Woodville South and the Lyell McEwin Health Service (LMHS) at Elizabeth Vale. QEH and LMHS were each formerly incorporated hospitals in their own right, but they ceased to exist as legal entities when NWAHS was incorporated.

Section 28 of the SAHC Act provides that an incorporated hospital is a body corporate. Subject to its constitution, it has power, amongst other things, to acquire and dispose of real and personal property, and to acquire or incur any other rights or liabilities.

Section 29 of the SAHC Act contemplates that an incorporated hospital will be administered by a Board of Directors constituted in accordance with its approved constitution. Section 29(2) provides that the Board may delegate its powers arising under its constitution to a committee appointed by the Board, or to any member of the Board, or officer or employee of the hospital.

Thus the SAHC Act contemplates that an incorporated hospital’s powers (eg to enter into a contract) will be exercised by (or with authorisation from) its Board. However, the Board’s

⁵ See Dixon J, *Briginshaw v Briginshaw* (1938) 60 CLR 336, 362.

power to contract for the acquisition of goods and services is subject to other legislation. It can also be constrained by the Minister responsible for the SAHC Act.

5.3 The Minister

The Minister's role in connection with the operation of the SAHC Act is, broadly, to promote the health and wellbeing of the people of the State.⁶ In so doing, the Minister's functions include, but are not limited to, acting to ensure that hospitals incorporated under the Act are operated in an efficient and economical manner, and to ensure the proper allocation of resources between such hospitals.

The Minister is able to delegate any of his or her powers or functions under the SAHC Act.⁷

The Minister may issue a direction to an incorporated hospital,⁸ but such a direction must be in writing, and must be published in the Government Gazette.⁹ The Minister is not entitled to give a direction that affects clinical decisions relating to the treatment of a particular patient, for the sale or disposal of land, buildings or equipment that is not held by the Crown, or relating to the employment of a particular person, or the assignment, transfer, remuneration, discipline or termination of a particular employee.¹⁰

5.4 State Supply Board

Section 14 of the *State Supply Act 1985* requires every 'public authority' to comply with any directions given or policies, principles or guidelines issued to the authority by the Board in the performance of its functions.

Section 14A provides that the chief executive officer of a 'public authority' is responsible for the efficient and cost effective management of the supply operations of the authority subject to and in accordance with the policies, principles, guidelines and directions of the Board. In this context, 'supply operations' include the procurement of goods or services required by the authority for its operations.

NWAHS, as an incorporated hospital under the SAHC Act, is a 'public authority' for this purpose.¹¹

The State Supply Board issued a policy document of general application in May 1998 (Issue No. 1). It is still current. Amongst other things, it sets out the State Supply Board's expectation that chief executives and agencies will observe the highest standards of integrity, probity and professional conduct in procurement processes. It also states that:

⁶ SAHC Act, section 15(1).

⁷ Section 17(1).

⁸ Section 29C.

⁹ Section 29C(3).

¹⁰ Section 29C(2).

¹¹ State Supply Regulations 1996, regulation 5(c)(ii).

- Chief Executives will be accountable for procurement decisions and for the efficient and effective expenditure of public funds, and
- Chief Executives will ensure that agency procurement activity conforms with the Government's 'Purchasing Strategically' policy framework,¹² State Supply Board policies, Treasurer's Instructions, the Prudential Management Framework and other South Australian Government policy requirements.¹³

The policy document also outlines a process of accreditation by which agencies can undertake procurement up to certain dollar limits without reference to the State Supply Board. DHS is accredited by the Board under that process to undertake procurement of goods and services up to a value of \$500 000.

In June 2000, the State Supply Board issued a further policy document (No 2), entitled 'Contracting Approvals and Processes'. That policy document makes it clear that for purchases over an agency's accreditation limit, a purchase recommendation detailing certain matters should be submitted for consideration and approval by the State Supply Board before a contract is awarded.¹⁴

Whilst it is clear that these State Supply Board policies have been published at large (eg on the Board's internet site), they have not been specifically issued by the Board to NWAHS. As explained in this Report, in the relationship between DHS and NWAHS, on the basis of all of the evidence, the Board and management of NWAHS implicitly accepted as a matter of operational policy that it comply with State Supply Board policies, principles and guidelines as an administrative requirement as distinct from a statutory obligation.

5.5 The Treasurer

Section 41 of the *Public Finance and Audit Act 1987* enables the Treasurer to issue instructions, amongst other things, requiring that procedures, set out in the instructions, be followed in the course of financial administration by the Treasurer and public authorities. Failure to comply with an instruction issued by the Treasurer under the section is an offence.¹⁵

The Treasurer has issued an Instruction (No. 8) dealing with 'Expenditure for Supply Operations, and Other Goods and Services'. It is intended to set out requirements additional to those that may apply by virtue of the *State Supply Act 1985*.¹⁶ It includes separate sections dealing with approvals to enter into contracts for supply operations and other goods and services on the one hand,¹⁷ and authority to incur expenditure of public monies (ie the

¹² Published on the Internet - see www.statesupplyboard.sa.gov.au/purchasing_strategically.

¹³ State Supply Board Policy Issue No. 1, May 1998, page 9.

¹⁴ State Supply Board Policies, No 2, Contracting Approvals and Processes, page 6.

¹⁵ Section 41(2).

¹⁶ Treasurer's Instruction 8.11.

¹⁷ Treasurer's Instructions 8.12 to 8.14.

authority to make a payment under a contract) on the other.¹⁸ The former is commonly referred to as a 'contracting authority'; the latter is commonly referred to as an 'expenditure authority'.

5.5.1 Contracting Authority

So far as approval to enter into contracts is concerned, Treasurer's Instruction No. 8 recognises that authority to enter into a contract that is binding upon a public authority may be derived from the enabling legislation for the public authority (eg the SAHC Act). In the absence of specific authority in enabling legislation, then authority to enter into a contract must be obtained from Cabinet, the responsible Minister or the relevant Chief Executive Officer (CEO) or other authorised officer of the public authority, depending on the dollar value of the proposed contract expenditure. As at the date of this Report, the relevant dollar values are as follows:

- Contract expenditure (including GST) of \$4 million or more — Cabinet approval required.
- Contract expenditure of more than \$500 000 but less than \$4 million — approval from relevant Minister required.
- Contract expenditure of \$500 000 or less — CEO (or other authorised officer) approval is required.¹⁹

5.5.2 Expenditure Authority

In the case of the authority to incur expenditure, the Chief Executive of a public authority is obliged not to permit any liability for the expenditure of public monies to be incurred unless the expenditure is necessary for the conduct of a public authority and the requirements of the *Public Finance and Audit Act 1987*, [and] *any other Act, law or instruction have been observed in all respects* [emphasis added].²⁰

The Treasurer's Instructions also purport to regulate the conduct of procurement processes generally. The Chief Executive of a public authority (other than prescribed authorities under the *State Supply Act 1985*) is required to ensure that officers of the public authority enter into contracts and otherwise undertake procurement in accordance with State Supply Board contract delegations, procurement standards, policies and guidelines that are appropriate for the public authority.²¹

5.6 DHS

In the particular case of NWAHS, DHS has imposed further controls.

¹⁸ Treasurer's Instructions 8.20 to 8.25.

¹⁹ Treasurer's Instruction 8.13. Note that other limits can be set by the responsible Minister - see Treasurer's Instruction 8.13.1 and Treasurer's Instruction 8.21.

²⁰ Treasurer's Instruction 8.20.

²¹ Treasurer's Instruction 8.15.

On 3 July 2001, the then Chief Executive of DHS wrote to the then Chair of the Board of NWAHS advising that in view of the (unsatisfactory) financial performance of NWAHS in the 2000-01 financial year, DHS felt the need to 'take a greater role in the management decisions that affect the expenditure and service levels of the hospitals'. The Chief Executive advised that certain conditions as to the funding provided to NWAHS would be imposed until further notice. Those conditions included, but weren't limited to, the following:

- A DHS nominee to be a member of the Board 'Finance Committee' at each site (a reference to QEH and LMHS);
- Board agendas and papers to be provided to that nominee at the same time as they are distributed to board members;
- Funding not to be provided by DHS to meet costs associated with:
 - New positions
 - New appointments
 - New and renewal of contracts
 - Purchase orders above \$50 000
 - Overseas and interstate travel
 - Equipment > \$5000

unless DHS nominee endorses the expenditure before the commitment is made.

- A weekly report detailing all staffing changes to be provided to DHS nominee.

The Chief Executive's letter further indicated that she expected that virtually all current delegations in place would be revoked, and replaced with the revised delegations reflecting the new controls.

A copy of this letter is Appendix A to this Report.

The CEO of QEH advised senior QEH staff²² of the new controls on 12 July 2001, with an additional requirement that items falling within the scope of the constraints imposed by DHS had to be submitted to him for consideration, and that items could then be submitted to DHS only if he supported them.

In my view, the actual and intended effect of these conditions was to place DHS rather than the Board of Directors of NWAHS in a position in which it, ie DHS was responsible for 'managing' NWAHS (or at least its finances and staffing), effectively from the commencement of the 2001-02 financial year.

Whilst the imposition of the conditions by DHS was clearly motivated by a proper concern as to the financial position of NWAHS, it is another question as to whether the imposition of the conditions was consistent with the SAHC Act, ie a lawfully enforceable requirement. In my

²² Including Dr Davies, who was a member of the Operations Executive Committee of the Hospital, which had been provided with the information relating to the changed delegations.

view, the insistence of a DHS nominee on the 'sub-Boards' of NWAHS, and the indirect empowerment of that nominee via the funding conditions, was inconsistent with the statutory scheme of an independent board of management of hospitals contemplated by the SAHC Act. Notwithstanding this inconsistency with the SAHC Act, the context in which the lawfulness and propriety of the acquisition of the 1.5 Tesla MRI machine by NWAHS must be reviewed includes a governance framework implicitly accepted by the Board and management of NWAHS, within which it was known and accepted that no officer or employee of NWAHS had authority to enter into a contract for the acquisition of goods with a value in excess of \$5 000 without the approval of DHS.

5.7 NWAHS Board and Its Sub-Boards

Mention should also be made of the governance arrangements in place for NWAHS through most of the period during which the events under examination took place. As discussed earlier, each incorporated hospital is intended to have a Board of Directors that administers its affairs. In practical terms, the NWAHS Board replaced the (two) boards of its predecessor incorporated hospitals. Ms Anne Skipper was the Chair of the Board of NWAHS until late 2001. On 23 October 2001, the Honourable Dean Brown MP, as (then) Minister for Human Services, wrote to Ms Skipper asking her to implement revised governance arrangements for NWAHS (involving sub-Boards with full delegations for each of the two NWAHS campuses), 'to provide a much more focussed approach to managing the two sites'.

Specifically, the Minister indicated:

Under the new arrangements, the role of the NWAHS Board will be to meet periodically to oversee the Board's strategic plan for the two sites, to sign off on financial reports, and any other necessary business.

The two sub Boards will have full delegated powers of the NWAHS Board and their composition will be decided by the Minister. Their role will be to oversee the management of the two sites on a month by month basis.

I would appreciate your early implementation of these arrangements.

A copy of this letter is Appendix B to this Report.

The Board implemented the Minister's request, with the result that the NWAHS Board now has two committees, referred to as 'sub-Boards', responsible for management oversight at each of the QEH and LMHS campuses. [Also the Board appointed a 'chief executive' for each campus, rather than a single chief executive for NWAHS.]

Although some arrangements were made to keep the NWAHS Board apprised of the decisions made by the sub-Boards (eg to enter into contracts), the result is that the Board is in a position in which decisions can be made by the sub-Boards that go materially to the financial position of NWAHS without involvement of the full Board, yet the full Board retains the statutory responsibility for the operations of each of the QEH and LMHS campuses and remains responsible for signing off the financial statements of NWAHS. This gives rise to important governance issues, in that some Board members (at least those who are not

appointed to both sub-Boards) are required to take responsibility for financial outcomes over which they have at best limited control. In my opinion, this is an unsound administrative arrangement.

In my opinion, the communication from the then Minister of 23 October 2001, although made in good faith, was not consistent with the SAHC Act.

In his comments on this section of the draft report, the Honourable Dean Brown MP indicated that his letter followed some discussions with a number of Board members who supported the proposal. Specifically, he indicated that the administrative arrangements referred to in the letter were agreed to with the (then) Chair of the Board, and that he was not advised by the senior departmental officers who were involved in the new arrangements that they compromised the Board, or that they contravened the SAHC Act.

Following receipt of those comments, I reviewed NWAHS' Annual Report for 2001-02. Aspects of the governance arrangements requested by the then Minister are disclosed in that report (on page 2 of the report). They provide some of the context for them, which includes a recommendation that in consequence of the resignation of Anne Skipper as Chairman of the NWAHS Board in October 2001, the parties work towards dissolution of the NWAHS Board and constitution of separate boards for QEH and LMHS. Implementation of such a recommendation would probably have required dissolution of NWAHS and the reincorporation of QEH and LMHS as incorporated bodies under the SAHC Act, or other amendments to the SAHC Act.

I have carefully considered the submission by the Honourable Dean Brown MP. I remain of the view that the arrangements requested in the letter of 23 October 2001, although made in good faith, were not consistent with the SAHC Act.

6.0 EVENTS UNDER EXAMINATION — THE CIRCUMSTANCES OF THE ACQUISITION

6.1 An Acquisition Process Begins

NWAHS wrote to a number of potential suppliers of second-hand MRI machines in August 2001. A copy of an example of its standard letter to those potential suppliers is Appendix C to this Report.

Amongst the companies that responded was Philips Medical Systems Australia Pty Ltd (PMSA). It indicated that it had second-hand MRI machines of various strengths available, ranging from 0.5 Tesla to 1.5 Tesla.

6.2 An Acquisition is Approved

Following extended discussions between DHS and NWAHS, in November 2001, the State Supply Board and (finally) Cabinet approved a proposal to acquire two used MRI machines

(of 0.5 Tesla) for NWAHS via a lease at a cost of \$2.45 million over seven years.²³ One machine was intended for QEH, the other for LMHS. The funds necessary to pay for the machines were not to come from general revenue. Rather a 'non-operating' account of NWAHS (the Non Operating Radiology Private Practice Fund) was to provide the necessary monies.

The Fund referred to was and is administered by NWAHS. It is comprised of 'excess private practice earnings' paid in by doctors with a right of private practice at NWAHS. The Fund comprises monies that in the relevant sense have become public funds, albeit funds administered by the hospital rather than Treasury.

The Cabinet approval was considered something of an achievement for NWAHS. It had lobbied for an MRI capacity to service its patients over a considerable period, in part to avoid the need to transport patients to other hospitals that already had the technology (eg the Flinders Medical Centre) for MRI examinations. A key player in those lobbying efforts was Dr Roger Davies, Director of Imaging, an employee of NWAHS, though the campaign to obtain access to the technology also had the support of NWAHS' Board and its Chief Executive Officers.

6.3 A Purchase Order is Issued

Cabinet's decision was made on 19 November 2001. A purchase order was raised on the same day for the machine intended for QEH. A copy of this purchase order is Appendix D to this Report. The purchase price for that machine was marked as 'TBA', with delivery indicated for 3 December 2001. In addition, the purchase order was marked 'Order placed subject to negotiations' and in accordance with 'quotation NG:RA 270801'. It was signed by the authorised NWAHS staff member Mr Derek Mason, who was also nominated on the form as 'queries person'.

6.4 A Contract is Entered Into

On 22 November 2001, DHS forwarded to Dr Davies and Mr Mason a copy of the State Supply Board approval for the 0.5 Tesla MRI machines. A copy of this advice is Appendix E to this Report. The State Supply Board's approval was quite explicit — two used 0.5 Tesla MRI machines, to be leased over seven years at a cost of \$2.45 million.

On 23 November 2001, Dr Davies accepted a PMSA quote (of the same date) for \$1.317 million for the machine intended for the QEH campus, thereby fixing the price payable by NWAHS for that machine. A copy of this quote, including Dr Davies' acceptance of it, is Appendix F to this Report.

In my view, Dr Davies had no actual authority to accept the quote. It seems likely that he was informally 'delegated' to sign off on the detailed specification of the machine to be purchased (given the specialist technical nature of that task, and his expertise in the area), but he had no actual authority, in effect, to conclude a contract with PMSA. Dr Davies

²³ For completeness, it should be noted that the proposal that the then Minister took to Cabinet also included MRI capacity (a 1.0 Tesla MRI machine) for the Women's and Children's Hospital.

assumed the authority to do so was encompassed within the scope of the task of agreeing the specification for the machine to be purchased with PMSA.

In any event, so far as PMSA was concerned, Dr Davies was either held out, or held himself out, as having the requisite authority. No one from NWAHS appears to have advised PMSA to the contrary at this or any subsequent relevant stage.

In the circumstances, in my view, the outcome was that at least by 23 November 2001, a contract binding upon NWAHS for the acquisition of the 0.5 Tesla MRI machine for the QEH campus had come into existence, though that contract may have been subject to the execution of a financing document with a third party financier, and (perhaps) confirmation of the delivery date.

In his comments on the draft report, Dr Davies disputed the conclusion that his action in signing the PMSA document on 23 November 2001 (which he also denied was a quote) gave rise to a contract binding on NWAHS. In my opinion, the nature of the document (a copy of which is Appendix F to this Report) is clear on its face, including and in particular on the page Dr Davies signed. I do not accept Dr Davies' submission on the point.

6.5 The Contract is put 'On Hold'

The contract did not then immediately proceed. The State election held in early 2002 had yet to be called, but in late 2001, the state of the health system in South Australia was a political issue. Although it is not clear who initially sought out whom, Dr Davies was at various times in contact with opposition members of Parliament such as the Shadow Minister for Health (Honourable Lea Stevens), and advisers such as Mr Randall Ashbourne, with whom he was acquainted.

One such contact was made shortly after the arrangement just referred to with PMSA was entered into. On or about 5 December 2001, the Shadow Minister advised Dr Davies that the ALP would provide additional (ie taxpayer) funding for MRI machines. On the morning of 6 December 2001, the then Opposition Leader issued a news release that included the following passage:

State Labor Leader, Mike Rann, has announced that a Labor Government will commit \$1.5m in capital funds towards magnetic resonance imaging (MRI) machines at the Queen Elizabeth and Lyell McEwin Hospitals. Labor has also committed \$250,000 in recurrent expenditure to cover on-going costs to run both machines.

A copy of this news release is Appendix G to this Report.

Dr Davies discussed this development with PMSA. Clearly the additional funding presented the possibility of acquiring stronger, more expensive MRI machines for NWAHS. The problem was the order just confirmed. The evidence put to this examination suggests that Dr Davies indicated to PMSA that he would prefer not to proceed to install the 0.5 Tesla MRI machines just ordered, probably until the outcome of the election was known. For obvious commercial reasons, PMSA was willing to put delivery of the

0.5 Tesla MRI machines on hold pending the outcome of the election. In an internal PMSA email of 10 December 2001, the following passage appears:

This is I believe an opportunity both Roger and PMSA need to take advantage of the issue being the existing orders for the 0.5T. I propose that we confirm a delivery date of May 2002 and give them until end of March to upgrade the system specs to an agreed spec and price that we set now. The issue will [be] how long before the 0.5T systems are fully committed ... I need this finalised in principle before I meet with Roger this Wednesday ...

Dr Davies met with the Chief Executives from the two NWAHS campuses in the week of 12 December 2001 to discuss the developments. The CEO, LMHS indicated that he was content to proceed with the 0.5 Tesla MRI machine that had already been approved. However the CEO, QEH (Mr Peter Campos) authorised Dr Davies to explore the possibility of an upgrade to the machine already ordered for QEH provided the order for the 0.5 Tesla MRI machine wasn't compromised.

On 18 December 2001, the then Minister for Human Services issued a media release announcing the decision to let contracts for the two (0.5 Tesla) MRI machines for the hospitals.

On 19 December 2001, the NWAHS Board was advised of the approval received to proceed with the two 0.5 Tesla MRI machines.

On 23 January 2002, the QEH sub-Board was advised that the two MRI Machines had been ordered, and that delivery was awaited.

6.6 A Change of Government and a New MRI Machine is Proposed

There was a change in Government in March 2002.

Shortly after the election, on 18 March 2002, Dr Davies participated in revising the 'business case' document for the MRI Machine for the QEH, now proposing the acquisition of a more expensive 1.5 Tesla MRI machine, and taking into account the promised additional funding. He forwarded the revised document to a number of parties, including Mr Ashbourne, now with the Department for the Premier and Cabinet, asking for it to be forwarded to the Minister for Health. A copy of Dr Davies' email to Mr Ashbourne is Appendix H to this Report.

The new Premier and Minister for Health visited QEH on 22 March 2002. A news release was issued. A copy of the news release is Appendix I to this Report.

The release included the following passage:

Ms Stevens says Labor will also keep its promise to provide new MRI machines at the QEH and the Lyell McEwin Hospital to stop the costly and potentially dangerous transfer of patients from the north and west to Flinders Medical Centre for urgent scans.

The Minister has asked the Chief Executives of both hospitals to immediately prepare business plans to buy and install the machines - instead of the second-hand machines promised by the former Government after Labor said it would fund new ones.

Shortly after the visit, PMSA provided Dr Davies with a quote for an upgrade to the MRI machine already on order to a 1.5 Tesla MRI machine. The quote was for \$2.234 million (plus GST). Although it is not clear precisely when that quote was provided (or indeed how many iterations of the quote there were), Dr Davies provided the text of such a quote dated 4 April 2002. A copy of the document provided is Appendix J to this Report. It is stated to be valid for 30 days.

Dr Davies says that following receipt of the quote, he sought instructions from the CEO of each NWAHS campus. Whilst the CEO of LMHS again confirmed that he wanted to proceed with the previously approved 0.5 Tesla MRI machine, the CEO of QEH (Mr Campos) decided to keep options open. Dr Davies says he was told by Mr Campos to 'hold off' committing to the 1.5 Tesla MRI machine now on offer as long as possible to see if the Ministerial approval for the 1.5 Tesla MRI machine was to be forthcoming. Mr Campos says his reference to 'holding off' was intended to be taken as a reference to proceeding with delivery of the 0.5 Tesla MRI machine to see whether approval for the 1.5 Tesla MRI machine was to be forthcoming. Either way, the matter of the machine for QEH did not proceed at that point.

On 12 April 2002, NWAHS submitted a proposal or 'business case' for the 1.5 Tesla MRI machine to DHS.

On 19 April 2002, PMSA provided NWAHS with a quote for the building works necessary to deliver and install the 1.5 Tesla MRI machine. Installation was to be no simple task. The MRI equipment is of a size that made it necessary to deliver it via a crane through a hole that had to be cut into the wall of the QEH building. The quote for the necessary building and related works (which would take about a month) was approximately \$214 000. The works required were more extensive than those that would have been required to accommodate the 0.5 Tesla MRI machine.

On 22 April 2002, the NWAHS Board was advised that a business case for an upgraded MRI machine had been forwarded to the Minister.

6.7 Late April 2002

Dr Davies has said that he met with the Minister for Health (Honourable Lea Stevens) on 26 April 2002 to discuss the matter. Minister Stevens has denied such a meeting took place on that date. She has provided this examination with detail of her movements on that date. Her office has also provided evidence that the meeting with Dr Davies that had been scheduled for that date was in fact cancelled, to be rescheduled at a later date. I am satisfied that Dr Davies' recollection on this point cannot be accepted.

In any case, Dr Davies does not assert that he was authorised to do anything in particular as a result of the alleged conversation with the Minister. To the contrary, he says that his purpose was to seek the Minister's active consideration of the revised proposal (ie that the hospital acquire the 1.5 Tesla MRI machine). He says that he was clear that the Minister intended to approve the acquisition on receipt of the relevant paper work from DHS. But he does not assert that he had that approval as a result of the conversation he alleges took place on 26 April 2002. As Dr Davies said in his evidence to this examination:

The purpose of the meeting was not to, in any sense, confirm that the Minister's intention to approve. The purpose of the meeting was to brief her to get the DHS consideration of the business case to a conclusion. I had no reason to think that the conclusion wouldn't be for the 1.5T machine that I understood had been announced during the election.

The statement of the then Opposition did not indicate the size of the MRI machine intended to be acquired.

In his comments on the draft report, Dr Davies disputed this point. His submission was, in effect, that the references to \$1.5 million additional funding reflected a clear intention to provide a 1.5 Tesla MRI machine for QEH (as that was the amount that Dr Davies had himself provided (then) Shadow Minister Stevens as being the amount necessary to provide a 1.5 Tesla MRI machine). Specifically, Dr Davies submitted '... it was obvious to all participants, including Dr Davies, that the government was committed to spend the \$1.5m funds that the government had indicated it was prepared to allocate towards the cost of a new 1.5 machine at QEH'.

In my opinion, this view is incorrect. In my opinion, at no time did the Government have a binding commitment to, or grant the requisite approvals for, a purchase of a 1.5 Tesla MRI machine, until Cabinet made its 'after the event' decision in October 2002.

6.8 The First Week of May 2002

Dr Davies reported to QEH's Operations Executive on 1 May 2002 to the effect that a revised business case had been submitted, and that NWAHS had opted (in that document) to pursue the 1.5 Tesla MRI machine. Mr Campos was present at that meeting.

Following that meeting, Mr Campos and Dr Davies discussed the matter again. The 4 April 2002 quote from PMSA was about to expire, and Dr Davies clearly thought a decision was required as a matter of urgency. Although the accounts of the conversation that took place differ slightly, I am satisfied that Mr Campos acceded to a suggestion from Dr Davies that he (Dr Davies) be authorised to explore with PMSA its willingness to deliver the 1.5 Tesla MRI machine on the basis that if the required approvals were not forthcoming, it could be swapped for a 0.5 Tesla MRI machine. In Mr Campos' mind, a key element of his instruction to Dr Davies was that PMSA was to assume all risks of the required approvals for the more powerful machine not being forthcoming. On the basis of all of the evidence, neither Mr Campos nor Dr Davies raised the detailed issue of how much NWAHS would have to pay if the need arose to revert to the 0.5 Tesla MRI machine.

On 6 May 2002, Mr Campos approved the commencement of the building works that would be necessary to install the 1.5 Tesla MRI machine. No evidence of Mr Campos' authority from DHS to do so was provided to this examination.

6.9 7 May 2002 — An Offer is Accepted and a Purchase Order is Altered

7 May 2002 was a Tuesday. It was some two months after the date by which PMSA had originally hoped the hospital would have made its choice as between the 0.5 Tesla and the

1.5 Tesla MRI machine, and it was two or three days after the 4 April 2002 quote for the 1.5 Tesla MRI machine had technically expired.

For some days prior to the 7th, PMSA had been increasing the pressure for a decision on Dr Davies.

PMSA's representatives visited Dr Davies on 7 May 2002. They brought with them another quote for a 1.5 Tesla MRI machine (this time dated 17 April 2002), together with the purchase order for the 0.5 Tesla MRI machine that had been issued in November 2001.

The company's message was that the time for a decision had come. Specifically, unless the existing order was upgraded, a 0.5 Tesla MRI machine would be 'put on the ship' and delivered to QEH. Dr Davies put the proposition he thought he was authorised to put by Mr Campos — that the hospital would commit to the 1.5 Tesla MRI machine provided it could revert to a 0.5 Tesla MRI machine at a later date, if the required approvals were not forthcoming. Dr Davies says that it was agreed by PMSA that the hospital could exercise this right of reversion at no additional cost.

On that basis, and during the 7 May 2002 meeting, Dr Davies accepted PMSA's formal offer of 17 April 2002 for a 1.5 Tesla MRI machine. A copy of the offer, and Dr Davies' acceptance, is Appendix K to this Report. On its face, the acceptance is unconditional.

During the meeting, Dr Davies also amended the form of purchase order forwarded in November 2001 to refer to 1.5 Tesla unit. Dr Davies says that he amended it to ensure consistency with the accepted offer for the 1.5 Tesla MRI machine. A copy of the amended purchase order is Appendix L to this Report.

It is apparent from the purchase order itself that Dr Davies did not attempt to hide his identity in amending the document; indeed he initialled the alteration, and wrote his name on the amended document adjacent to the alteration.

The result was that documentation was executed that, on its face, unconditionally committed NWAHS to acquire the 1.5 Tesla MRI machine at the price quoted by PMSA, and on the terms and conditions referred to in the quote. Dr Davies' evidence is that, in effect, he trusted that PMSA would honour the agreed right to revert to a 0.5 Tesla MRI machine. However, his confidence was such that the right to revert would not be needed, and so at best, all that was agreed on price was that the 0.5 Tesla MRI machine would not cost more than the 1.5 Tesla, should the hospital need to revert to the less powerful machine. Dr Davies did not focus on the cost to the Hospital of exercising the right to revert to the smaller machine.

Neither Mr Campos nor Dr Davies appear to have sought advice on the deal they were doing with PMSA from their procurement officers, their Board, DHS or their lawyers. Neither of them had authority to enter (or authorise entry) into the agreement with PMSA. In effect, they assumed the risk for NWAHS that the approvals necessary to proceed with the acquisition of the 1.5 Tesla MRI machine would be forthcoming. Mr Campos and (particularly) Dr Davies appear to have judged that the risks involved in taking the steps they had taken were acceptable given the political developments of which they were both aware, and the risk mitigation they thought they had undertaken via the agreement to the right of

reversion. Specifically, Dr Davies seems to have regarded the possibility of the acquisition of the 1.5 Tesla MRI machine not being approved following the necessary processes as a theoretical one only.

From PMSA's viewpoint, Dr Davies' willingness to sign the documents that had been presented at the meeting would have further reinforced Dr Davies' apparent or ostensible authority to enter into arrangements of this nature on behalf of NWAHS.

By the end of that Tuesday meeting, in my view, it is the case that NWAHS was unable to deny that a conditional contract to supply a 1.5 Tesla MRI machine had been entered into. That contract had not been authorised by any person with actual authority to do so. Mr Campos, who was not present at the meeting, does not appear to have considered at the time what Dr Davies may have had to do in order to secure PMSA's agreement to the course of action (ie the right of reversion) he had authorised Dr Davies to explore.

In responding to the draft report, more than one party raised the question of whether the conduct of the various parties (and especially Dr Davies) did in fact give rise to a contract or contracts binding upon NWAHS for the acquisition of one or more MRI machines.

So far as the events of November 2001 are concerned, in my opinion, the issue of the purchase order and the acceptance of the quote and specification for the 0.5 Tesla MRI machine was sufficient to create a contractual relationship between NWAHS and PMSA. In my opinion, legal obligations arose in November 2001.

In my opinion, the events of May 2002 (specifically Dr Davies' alteration of the purchase order, and his acceptance of the quote for the 1.5 Tesla MRI machine) had the effect of varying the existing contract for the 0.5 Tesla MRI machine.

6.10 9 May 2002 — A Meeting with the Minister's Chief of Staff

On 9 May 2002, Dr Davies met with Mr Geoff Loveday, Chief of Staff to the Minister for Health, at Parliament House. The appointment was intended to involve the Minister and Mr Loveday. However, the Minister was unable to attend at the last minute due to her Parliamentary commitments. Although the fact that this meeting took place is undisputed, significantly different accounts of what was discussed have been presented to this examination. Dr Davies says this was a follow up meeting to the 26 April 2002 meeting with Minister Stevens which Minister Stevens says never took place, and that I am satisfied, on the basis of all of the evidence did not take place.

Mr Loveday says this was Dr Davies' second (unsuccessful) attempt to meet with the Minister on the issue of an MRI machine for QEH (the first being the attempt on 26 April 2002). Dr Davies says that Mr Loveday should have left the meeting clearly understanding that commitments had been entered into with PMSA. Mr Loveday says Dr Davies should have left the meeting a disappointed man, understanding that although the Government would honour its commitment to provide additional funding for NWAHS for MRI machines, no decisions as to the procurement of upgraded or alternative machines could be made until the new Government's first budget was handed down in July 2002. Dr Davies says that he was told that no announcements could be made until the budget was handed down. The

evidence of Mr Loveday is consistent with the Ministerial and departmental (ie DHS) conduct in this matter.

6.11 Disclosure to DHS

Neither Dr Davies nor Mr Campos thought to inform DHS promptly of the conditional commitment entered into with PMSA on 7 May 2002. Nevertheless, by 15 May 2002, 'rumours' had reached Mr Mark Leggett, Director, Strategic Procurement at DHS, that NWAHS was purchasing a 1.5 Tesla MRI machine. In his evidence to this examination, so far as Mr Leggett was concerned, the rumours were, at the time, unsubstantiated.

Dr Davies met with Mr Leggett and other DHS officers on 24 May 2002. Dr Davies informed those officers that NWAHS wanted to buy a 1.5 Tesla MRI machine. Mr Leggett advised Dr Davies that fresh State Supply Board and Cabinet approvals would be required for that to happen.

The rumours Mr Leggett had heard were thereby confirmed. Mr Leggett and his officers sought to obtain the information that they thought necessary to prepare a submission to the State Supply Board and Cabinet for approval to purchase the more powerful machine. Mr Leggett indicated that he would 'do his best' for Dr Davies in terms of the new approvals processes that would be required.

Dr Davies acknowledges that he may have been informed during this meeting of the need for the new approvals, but he says that such a statement was not something he would have particularly noted. His understanding was that Mr Leggett's group (ie the DHS Strategic Procurement Unit) had the responsibility of progressing the matter through all necessary approval processes. So far as he was concerned, the prime decision maker (ie the Minister) was fully committed (at least to providing the additional \$1.5 million funding), so the meeting was, in effect, about 'the paperwork'. Dr Davies concedes that he did not disclose the fact that he had altered a purchase order and accepted a quote for a 1.5 Tesla MRI machine from PMSA to DHS officers at that meeting.

Dr Davies knew that he had changed the contractual documentation with PMSA, that the order for the approved 0.5 Tesla MRI machine had been 'put on hold', that the order with PMSA was now for a 1.5 Tesla MRI machine and that there was no approval by a proper authority for a 1.5 Tesla MRI machine. Further, he knew that delivery of a 1.5 Tesla MRI machine was to be made to QEH. Notwithstanding these important facts, he remained silent regarding his actions in a meeting with DHS officers in which he was informed that fresh State Supply Board and Cabinet approvals were necessary for the acquisition of a 1.5 Tesla MRI machine. Dr Davies' silence is significant in the context of the reason for this meeting.

On the basis of all of the evidence, Dr Davies, in my opinion, must have known that DHS officers were not aware that he had changed the documented contractual relationship with PMSA to purchase a 1.5 Tesla MRI machine.

In my opinion, Dr Davies should have disclosed what he had done to the DHS officers. I am satisfied that this matter would have progressed very differently had he done so. This is not to deny that others (such as Mr Campos) should also have made disclosure to DHS of the arrangement that had been entered into with PMSA (to the extent that they had knowledge

of it). Nonetheless, Dr Davies did not make the disclosures that he should have when he had the opportunity to do so.

Following that meeting, Mr Leggett asked NWAHS to provide some background material for the purpose of his preparation of the various submissions that would be necessary to obtain the approvals to purchase the 1.5 Tesla MRI machine.

On 31 May 2002, David Norton, Executive Director of Corporate and Redevelopment Services of NWAHS provided Mr Leggett with a 'Summary of Events to Date' document. That document included the statements that 'Agreements have been entered into with Philips for two 0.5 Tesla machines', and that 'Philips have indicated that the 1.5 Tesla machine included in the original tender is still available and that they will provide this as an alternative to the 0.5 Tesla machine'.

Though Messrs Leggett and Norton were not aware of the fact at the time, the second statement – that the 1.5 Tesla MRI machine included in the company's original response in August 2001 was still available - was not true.

6.12 A 1.5 Tesla MRI machine is Delivered

On 27 May 2002, PMSA wrote to Dr Davies (cc Messrs Campos and Martin of NWAHS) confirming likely delivery of the 1.5 Tesla device on 19 June 2002. On the same date, Mr Campos (Chief Executive QEH) wrote to DHS, referring to the revised business case that had been provided to DHS on 12 April 2002 and to the building works that had been commenced, asking for approval to proceed.

On 28 or 29 May 2002, the Minister for Health indicated to DHS that the QEH proposal to upgrade to a 1.5 Tesla MRI machine should be considered after the new Government's first budget was brought down. This decision does not appear to have been communicated by DHS to Mr Campos in a timely fashion. Mr Campos says the first he became formally aware of it was on 22 July 2002 (see below).

On 31 May 2002, the Minister says she met with Dr Davies. The Minister says that she confirmed the funding promised during and immediately after the election would be forthcoming, but that nothing would be done or decided until after the budget was handed down. The Minister says she wasn't told the 1.5 Tesla MRI machine was already on its way.

Dr Davies has said to this audit review that in light of his clinical commitments, it is unlikely that he met with the Minister on 31 May 2002. However, Dr Davies also initially said to this examination that he was at QEH on 31 May 2002. Dr Davies' mobile phone records tend to suggest otherwise. On the basis of all of the evidence, in my opinion, Dr Davies' recollection on this point is not to be accepted.

On 21 June 2002, the 1.5 Tesla MRI machine was delivered to QEH.

On 1 July 2002, PMSA wrote to NWAHS to confirm delivery of the 1.5 Tesla MRI machine, and to indicate that delivery and the building works should be complete by 12 July 2002, with installation and commissioning to commence after that date. A copy of this letter is Appendix M to this Report.

On 2 July 2002, Mr Leggett of DHS provided a Parliamentary Estimates Committee briefing note for his Minister to the effect that the 0.5 Tesla MRI machine for LMHS had been installed, but that the MRI Machine for the QEH had been delayed pending the additional funding required for the more powerful machine (expected 2003-04). At the same time, he asked that one of his officers check the accuracy of that advice with NWAHS.

On 3 July 2002, Mr Leggett received an email that confirmed that the QEH had an MRI machine on site. In my opinion, Mr Leggett erred in not promptly drawing this information to the attention of his Chief Executive or his Minister, particularly in light of the Estimates Committee briefing he provided on the previous day.

On 17 July 2002, Mr Norton provided an updated 'Summary of events to date' document to Mr Leggett. The fact that the 1.5 Tesla MRI machine had been delivered to the QEH was not included in that summary. Mr Norton has advised this examination that he thought such information 'irrelevant' in the context. However Mr Leggett knew that the 1.5 Tesla MRI machine was on site.

6.13 PMSA Seeks Authority to Proceed to Install the 1.5 Tesla MRI machine

On 18 July 2002, PMSA wrote to Dr Davies indicating a requirement for written authorisation for installation of the 1.5 Tesla MRI machine. The company indicated that if the authorisation was not forthcoming, PMSA would remove the 1.5 Tesla MRI machine and charge NWAHS the ensuing building and removal costs (with the quantum of those costs to be advised). A copy of this letter is Appendix N to this Report.

6.14 A Decision is Made to Reject the 1.5 Tesla MRI machine

On 22 July 2002, Mr Campos met with senior DHS staff (including Dr Tom Stubbs, Executive Director, Metropolitan Division and Mr Leggett). At that meeting, it was decided (and Mr Campos was instructed) that the 1.5 Tesla MRI machine should be returned, and a process commenced to procure another 0.5 Tesla MRI machine. The originally offered 0.5 Tesla MRI machine was no longer available. Mr Campos confirmed this outcome, and some concerns as to it, by email to Dr Stubbs the following day.

On 23 July 2002, presumably to ascertain the cost of the exercise of the option to revert to a 0.5 Tesla MRI machine, Dr Davies faxed PMSA for a price for supply of a 0.5 Tesla MRI machine. On the same date, he emailed Mr Ashbourne (of the Department of Premier and Cabinet) with his concerns as to the scenario that appeared to be developing ie that the option to revert to a 0.5 Tesla MRI machine was to be exercised. A copy of Dr Davies' email to Mr Ashbourne is Appendix O to this Report.

Dr Davies says he discussed the issue raised by his fax of 23 July 2002 with PMSA. He says that PMSA indicated during the conversation that the price for reverting to the 0.5 Tesla MRI machine would be the same as the price that had been agreed for the 1.5 Tesla MRI machine. Dr Davies says he told PMSA he thought that position had to be a 'try on', and that a better outcome than that could be negotiated, but if that was PMSA's position, it had better put that in writing.

Accordingly, on 25 July 2002, PMSA wrote to Dr Davies. A copy of this letter is Appendix P to this Report. By that letter, PMSA confirmed delivery and 'partial' installation of the 1.5 Tesla MRI machine, enclosed a proposal to replace the 1.5 Tesla MRI machine with a 0.5 Tesla MRI machine (for the same price as had been agreed for the 1.5 Tesla MRI machine), and asked for written confirmation as to the option the hospital wished to choose within 14 days.

Also on 25 July 2002, Minister Stevens was provided a written briefing from DHS dated 24 July 2002 formally advising her of the delivery of the 1.5 Tesla MRI machine to NWAHS.

On 2 August 2002, NWAHS (Mr Norton) wrote to PMSA indicating that NWAHS wished to pursue removal of the 1.5 Tesla MRI machine.

6.15 Legal Advice is Sought

On or about 6 August 2002, at the request of NWAHS, DHS (Mr Leggett) sought advice as to NWAHS' legal position in the matter from the 'in house' DHS branch of the Crown Solicitor's Office.

The legal advice was provided on 7 August 2002. It was to the effect that PMSA had an enforceable contract with NWAHS for the supply of the 1.5 Tesla MRI machine. It was clearly stated to be preliminary advice. In fact only a very few of the relevant documents were provided to the lawyer who gave the advice. There is no evidence that some relevant documents (eg the PMSA correspondence of 18 July 2002 confirming the option to swap a 0.5 Tesla MRI machine for the installed 1.5 Tesla MRI machine) were provided. Accordingly, the advice did not (indeed could not) accurately reflect the legal position of the parties at the time.

Also on 7 August 2002, PMSA responded to NWAHS in a manner generally consistent with the position it took in the 25 July 2002 letter. A copy of this letter is Appendix Q to this Report.

6.16 A Final Decision is Made

On 8 August 2002, Minister Stevens discussed the situation that had arisen with some of her Ministerial colleagues. In view of the legal advice, and other factors, it was decided that the acquisition of the 1.5 Tesla MRI machine would be confirmed. A news release was issued on 9 August 2002. A copy of this release is Appendix R to this Report.

The Chief Executive of DHS advised the Chief Executive Officer of QEH later that month to proceed to complete the acquisition of the 1.5 Tesla MRI machine. PMSA was advised in writing of the decision on 22 August 2002. Cabinet noted the acquisition and approved the resulting expenditure on 28 October 2002.

7.0 AUDIT ANALYSIS AND OPINION

7.1 Was the Acquisition of the 1.5 Tesla MRI machine Conducted Properly and in Accordance with Law?

On the basis of all of the evidence put to this audit review, the acquisition of the 1.5 Tesla MRI machine was not authorised prior to a commitment being entered into by any of the Board of NWAHS, DHS, the Minister for Health, the State Supply Board or Cabinet.

Dr Davies purported to vary a purchase order, and accept a quote from PMSA on behalf of NWAHS for the purchase of a 1.5 Tesla MRI machine without approval from anyone, other than a less than precise instruction from Mr Campos to secure delivery of the machine on condition that it could be returned. As indicated above, in my opinion, a contract was entered into, and public funds were committed without authority from the bodies that would be required to assume budgetary responsibility for meeting the obligations incurred (ie the Minister of Health, DHS and the Board of NWAHS).

These circumstances give rise to issues that concern fundamental principles of public administration.

Good and proper public administration necessitates that public sector employees adhere to governmental principles and values that are essential to protect the community from the arbitrary exercise of governmental power and the misapplication of public monies. Adherence to those principles also protects public sector employees from allegations of wrongdoing, even corruption.

These principles and values include compliance with relevant statutory requirements and the obligation of public employees to act with impartiality and objectivity, and with loyalty and fidelity to the Government of the day.

Public sector employees are required to serve governments of any political persuasion. They must not knowingly and intentionally frustrate the implementation of the legitimate policy objectives of the Government of the day.

This issue transcends the party political process and goes to the values that underpin the system of government in this State. It is not for public employees to anticipate the outcome of a general election in deciding whether or not to implement a particular decision of the Government of the day, especially where these decisions are made outside the period of any caretaker conventions.

In matters where it is sought to persuade a Government to change a decision, it is essential that this be done transparently and through proper processes and by the proper authority or authorities. In this matter, the change in the contractual arrangements was done intentionally and without the knowledge of the proper authorities. There was also a failure to disclose the unauthorised contractual commitment in a timely way to those who were entitled to be so informed. This failure to disclose compounded the seriousness of this matter.

In my opinion, failure to comply with these principles undermines public confidence in the administrative processes of government.

It is beyond argument that public employees have an obligation to comply with legislation that applies to them in the performance of their duties. In this matter, two separate legislative provisions are relevant — the *State Supply Act 1985* and the *Public Finance and Audit Act 1987*.

7.1.1 Application of State Supply Board Contract Guidelines, Policies, etc

As discussed earlier, so far as the *State Supply Act 1985* is concerned, section 14 provides that a public authority (including every member or officer of the authority) is bound to comply with any directions given or policies, principles or guidelines issued to the authority by the

State Supply Board in the performance of its functions. The State Supply Board did not formally 'issue' its key policies (those published on its web site) to hospitals incorporated under the SAHC Act to the extent that, in my opinion, is contemplated by section 14.

Although the State Supply Board did not formally 'issue' its policies, principles and guidelines to NWAHS (QEH), ie a 'public authority' under the State Supply Act, the administrative arrangements that operated in the relationship between DHS and the Incorporated Hospitals under the SAHC Act, including NWAHS (QEH), did apply the State Supply Board policies, guidelines, etc as an 'administrative' requirement as distinct from a 'statutory' obligation. In my opinion, NWAHS, as a matter of administrative policy that was implicitly adopted by its Board and management was required to comply with the State Supply Board policies, principles and guidelines.

In my opinion, because there was a failure to comply with the requirements of the State Supply Board contracting policies, principles and guidelines, the contract for the acquisition of the 1.5 Tesla MRI machine was not conducted properly.

7.1.2 Application of Treasurer's Instructions

In my opinion, NWAHS is a 'public authority' for the purposes of the *Public Finance and Audit Act 1987*.

With respect to this matter, Treasurer's Instruction 8.12 is relevant. This Instruction provides as follows:

8.12 If the enabling Act of a public authority authorises its governing body or employees to enter into contracts or to delegate that authority, the Chief Executive must ensure that those authorisations are complied with.

In this case, NWAHS' enabling Act (the SAHC Act) provides that incorporated hospitals are bodies corporate with perpetual succession and a common seal, and that subject to their approved constitutions, are capable (amongst other things) of acquiring personal property and of acquiring or incurring any other rights or liabilities.²⁴ The SAHC Act also provides²⁵ that the Board of an incorporated hospital (which is responsible for the administration of the hospital) may delegate any of its powers to board committees, board members or to an officer or employee of the hospital.

Accordingly, notwithstanding the absence of a specific provision in the SAHC Act that says (in so many words) that an incorporated hospital has power to enter into contracts, in my opinion, they clearly do.²⁶

Treasurer's Instruction 8.12 creates a legal duty on the Chief Executive of a public authority to ensure that the employees of the public authority comply with the terms of any delegations

²⁴ SAHC Act, section 28.

²⁵ Section 29.

²⁶ The Hospital's constitution for example gives it power amongst other things to acquire real and personal property.

from the governing body of the public authority, and respect, for example, any financial limits that might be imposed on such delegations.

Neither Mr Campos nor Dr Davies was authorised to enter into the contractual commitments for the acquisition of the 1.5 Tesla MRI machine. In my opinion, notwithstanding his ignorance of Dr Davies' actions in altering the purchase order, and accepting the PMSA quote, it is arguable that in allowing Dr Davies to have the carriage of important negotiations with PMSA, rather than authorised NWAHS procurement officers, Mr Campos did not ensure compliance with the relevant authorisations.

7.1.3 Other Unlawful Conduct

The transaction was conducted unlawfully in the sense that it was entered into by a public employee, ie Dr R Davies, who was acting contrary to his duties as a public employee, and in particular beyond the scope of his lawful authority. In my opinion, Dr Davies' conduct constituted an unlawful interference with the contractual relations between NWAHS and PMSA.

7.1.4 Acquisition Not Conducted Properly

In my opinion, on the basis of all of the evidence, the acquisition of the 1.5 Tesla MRI machine was not conducted properly.

Dr Davies and Mr Campos agreed to a course of action (ie placing delivery of the 0.5 Tesla MRI machine on hold) that they knew was incompatible with the timely implementation of a lawful decision of government — the approved contractual arrangement for the acquisition of the 0.5 Tesla MRI machine. That course of action was contrary to their duty as public employees.

In my opinion, Dr Davies, without the approval of a proper authority, deliberately accepted a quote, and altered a purchase order, knowing that the result was likely to be that the existing contractual arrangements between NWAHS and PMSA would be varied.

Mr Campos concurred with Dr Davies in arranging for PMSA to deliver the 1.5 Tesla MRI machine to QEH, knowing that this was contrary to the existing approved arrangements and contract, albeit on the basis that PMSA would swap the 1.5 Tesla MRI machine for a 0.5 Tesla MRI machine if the necessary approvals were not forthcoming.

Mr Campos' conduct raises issues that, in my opinion, concern matters of propriety and regularity in public administrative arrangements. In essence, his conduct involved questions of judgment. In my opinion, that judgment should have been exercised in accordance with the applicable legal requirements as was incumbent on him as Chief Executive Officer of the QEH and the principles that inform the conduct of public employees transacting public business. His conduct was inconsistent with what was required of a Chief Executive Officer in the circumstances he faced, that is, to act openly and in good faith with his Board and DHS, and to ensure compliance with applicable regulatory and administrative requirements.

7.1.5 Statements in the Course of an Election Campaign

I have also considered whether the conduct of the transaction generally, and the actions of Dr Davies and Mr Campos in particular, were justified by the statements made by representatives of the then Opposition, both prior to, and after the announcement of the calling of the election on 9 February 2002, or the public statement made by the new Government in March 2002.

The statements in question were political promises of additional funding. They were not statements that justified or authorised the decision to proceed with an acquisition of a particular strength MRI machine, or in fact any MRI machine, at that, or any later time, without approval from the relevant authorities. Accordingly, in my opinion, neither Dr Davies nor Mr Campos were justified in acting as they did by those statements.

7.1.6 What Should Have Happened?

When Dr Davies and Mr Campos made the decision to defer delivery of the 0.5 Tesla MRI machine, there should have been full and prompt disclosure to the Board of NWAHS (or at the very least the QEH sub-Board), and to DHS. When a decision was made to invite a fresh quote for a 1.5 Tesla MRI machine, full and prompt disclosure of the commencement of a new procurement process should have been made. Also when Dr Davies purported to enter into a contract to purchase the 1.5 Tesla MRI machine (albeit subject to conditions), full and prompt disclosure should have been made. Notwithstanding the fact of ongoing discussions with DHS regarding the matter of the MRI machines, these decisions (and particularly the last of them) were withheld from relevant authorities, until late in the process.

In all the circumstances, when the decision was taken not to immediately proceed with the purchase of the 0.5 Tesla MRI machine for QEH, the Board of NWAHS and DHS should have been briefed, and a fresh procurement process to acquire a machine other than that approved by DHS, the State Supply Board, and by Cabinet, should have been initiated.

The fresh procurement process may not have involved public tenders; indeed a sole source negotiation with PMSA may have proceeded in any event. After all, a contract had just been entered into with PMSA, and negotiations would have been necessary in order to inform relevant decision makers of the likely 'break' cost for the existing contract (ie the cost of cancelling the order just placed). But it is also possible that it would have been decided that in the interests of achieving the best possible value for money outcome, payment of the break cost and another check with likely suppliers as to the availability and cost of MRI machines stronger than 0.5 Tesla might have been prudent.

At the end of the day, the decision to contract for the supply of the 1.5 Tesla MRI machine should have been made by the Board of NWAHS, or DHS, with the endorsement of the State Supply Board and (perhaps) Cabinet, particularly in light of the change of Government that occurred in early 2002.

That no such fresh procurement process was initiated is undisputed.

Instead, as mentioned, Dr Davies purported to enter into a contract with PMSA in the name of NWAHS. In effect, he judged that it was extremely unlikely that the political promises by the Premier and the Minister for Health would not be honoured come budget time, and that it was worth taking the risk of assuming the required authority in order to secure the 1.5 Tesla MRI machine then on offer by PMSA.

However the judgement was not Dr Davies' to make.

As a result of the conduct of Dr Davies, those with the requisite authority to make the decision to purchase the 1.5 Tesla MRI machine — the NWAHS board, DHS, the Minister, and (perhaps) the State Supply Board and Cabinet — were denied the opportunity to give proper consideration to the available options, including proceeding without a fresh process with PMSA. The proper function of each of the bodies mentioned was improperly usurped. Proper consideration of the political, clinical, financial, risk and legal issues to which the procurement gave rise was precluded by the manner in which the procurement was handled.

In short, in my opinion, the contract for the acquisition of the 1.5 Tesla MRI machine was not properly entered into. In my opinion, the improper conduct referred to was serious, going to the heart of the accountability and responsibility framework for the expenditure of public funds in South Australia.

By his conduct, Dr Davies also 'gazumped' relevant officers in relation to the procurement. On the basis of all of the available evidence, no consideration was given to constructing a process whereby some competitive tension could be introduced to the acquisition of the more powerful machine (eg by checking with possible alternative suppliers of MRI machines stronger than 0.5 Tesla). Nor does consideration appear to have been given to the relative value for money that might have been offered by an MRI machine of some other strength, since no enquiries were made as the availability of other machines once the promise of additional funding was in the public domain.

A proper consideration of these and other issues by the relevant authorities was precluded by the manner in which the 1.5 Tesla MRI machine was procured.

7.2 Issues of Concern

A number of aspects of this matter give rise to cause for concern that should, in my opinion, be brought to the attention of the Government and of the Parliament.

7.2.1 Conduct of Mr Campos and Dr Davies

The facts of this matter suggest several errors of judgment (at the least) were made by Mr Campos and Dr Davies.

In my opinion, Mr Campos committed an error of judgment in not insisting that the procurement of the MRI capacity (and especially the procurement of the 1.5 Tesla MRI machine) for QEH be conducted primarily by his procurement staff, rather than a member of his medical staff. In my opinion, this error of judgment provided the opportunity for Dr Davies to commit the unauthorised act of executing documentation with PMSA for the 1.5 Tesla MRI machine.

In my opinion, Mr Campos also failed to take sufficient care to protect NWAHS from the very risk that he had identified in his conversations with Dr Davies — that the approvals required for the 1.5 Tesla MRI machine would not be forthcoming, and the right to revert to the 0.5 Tesla MRI machine would need to be exercised.

In my opinion, Dr Davies committed a serious breach of his duties as a public employee in executing contract documents on behalf of NWAHS at a time when he knew the required approvals were not in place. In my opinion, in doing so, he was also interfering with an existing contractual relationship for the acquisition of a 0.5 Tesla MRI machine. On the basis of all the evidence, I am satisfied that he knew he lacked the authority to do that which he purported to do.

7.2.2 The Importance of Procedural Regularity

The facts of this matter also illustrate the importance of procedural regularity in public administration. The control processes within government are designed to limit the possibility of abuse of power and authority by any particular person or entity within the public sector. These control arrangements break down when there is (as in this case) a lack of openness by those that have a responsibility to ensure compliance with the applicable controls.

Public employees who pursue objectives that are at odds with approvals that have been given after consideration by proper authorities, and who thwart, in this case secretly, the implementation of approved arrangements, in my opinion, behave improperly.

Irrespective of the motives of Dr Davies and Mr Campos, their conduct had the consequence that the legal position of NWAHS in its relationship with PMSA was compromised. Unilateral action of this type undermines the control processes within government. To claim that their actions were merely pre-emptive of arrangements that they anticipated could or would be made in any event is not to the point. The decision they made to put the existing contract 'on hold' was not their decision to make.

7.2.3 Public Employees Engaging with the Political Process

At its most basic level, public employees are employed to implement the lawful policy objectives of the Government of the day in a manner consistent with the values that inform and direct public sector employment. In this matter, the Government of the day had decided to acquire a 0.5 Tesla MRI machine. That decision had been made by the proper authorities. In my opinion, Dr Davies engaged with the political process in order to secure a different outcome for QEH.

There can be no criticism of the fact that a public employee has political affiliations or contacts (or both), provided there is no compromise of his or her obligations as a public employee to the goals of the Government of the day. To frustrate the implementation of a lawful decision entered into by the Government of the day, in anticipation of the outcome of an election, in my opinion, is at least, to act improperly, if not unlawfully. Conduct that knowingly and intentionally, and without justification, interferes with the contractual rights of an employer, resulting in damage to that employer is unlawful.

7.2.4 The Matter of Political Accountability

NWAHS is a statutory body with corporate personality and a governance structure prescribed by the SAHC Act.

The proper scope and nature of relationship of the Minister to NWAHS is to some extent set out in the SAHC Act.

The communication by the former Minister (for Human Services) of 23 October 2001 with the Board of NWAHS was not consistent with the SAHC Act. Nonetheless I accept that it was a communication made in good faith.

Likewise the 3 July 2001 letter from the then Chief Executive, DHS, to the then Chair of the Board of NWAHS in purporting to impose conditions on its ongoing funding of NWAHS that included, amongst other things, a requirement that the NWAHS Board appoint a DHS nominee to its sub-Boards, was inconsistent with the statutory scheme of an independent board of management of hospitals contemplated by the SAHC Act.

The result of the two communications was to place the members of the Board of NWAHS in a difficult position. Accountability for the financial position in particular of NWAHS was blurred, and transparency was lost.

7.2.5 Important Non-Disclosures to Responsible Entities

Notwithstanding the assumption by DHS of management of at least the finances and human resources of NWAHS, it is apparent that at several materially significant times, important information was withheld from DHS by NWAHS officers. Examples include the failure of:

- Dr Davies on 24 May 2002 to disclose to the Strategic Procurement Unit of DHS the fact that a commitment to acquire the 1.5 Tesla MRI machine from PMSA had already been entered into; and
- Mr Campos on 27 May 2002 to disclose the fact that the 1.5 Tesla MRI machine was on its way when he sought approval to proceed with its purchase.

7.2.6 The Legal Advice Obtained by DHS

Legal advice was sought by DHS at a late stage in the matter. The legal advice was sought from the outposted Crown Solicitor's Office lawyers located in DHS. A very limited documentary brief was provided by the Strategic Procurement Unit of DHS. Important and relevant documents were not included in the brief. The result was that the legal advice was inadequate as a basis for decision making by government.

Given the amounts involved, and the importance of the matter, definitive (and not 'preliminary') advice should have been obtained before final decisions were made.

The absence of proper, comprehensive and definitive legal advice meant that legal and commercial options that might have been in the interests of the State were not identified, let alone explored.

7.2.7 Awareness and Involvement of the Board of NWAHS

Neither the Board nor the sub-Board was kept fully informed; equally, neither significantly enquired as to the conduct of the procurement process. In my opinion, this is not surprising

given the extent to which DHS assumed the role of manager of the business of NWAHS, particularly its procurement activity and the fact that as a matter of policy the NWAHS Board implicitly accepted this as the operational arrangement for its affairs in procurement.

For the reasons discussed in this Report, this situation is not satisfactory as a proper structure for the governance of NWAHS. As provided under SAHC Act, the Board of NWAHS is the accountable body. Under the arrangements that operated in relation to this transaction, the Board acquiesced in its displacement as the responsible entity. In so doing, it failed to understand its statutory independence under the SAHC Act, subject only to formal Ministerial direction.

7.2.8 The Quality of the Procurement Process Generally

The conduct of the procurement process in this matter generally was unsatisfactory. The letter that initiated the process with the potential suppliers (ie Appendix C to this Report) was little more than a request for information, yet it was used as a basis for the process that followed. Selection of both preferred supplier and machine proceeded on the basis of the responses to that letter. In reality, the process adopted was largely free of competitive tension in relation to price or contract terms, particularly once the announcement was made of the additional \$1.5 million funding. As mentioned, the manner in which the process was conducted, at least for QEH, was that the customer was a taker of offered terms, rather than an indicator of desired terms. This is not best practice procurement, even for second hand equipment.

The length of time taken for the process also meant that issues arose as to the particular MRI machines on offer. The 1.5 Tesla MRI machine finally purchased does not appear to have been the 1.5 Tesla MRI machine originally offered by PMSA in response to the August 2001 letter from NWAHS. At the time NWAHS had the option to return the 1.5 Tesla MRI machine and substitute a 0.5 Tesla MRI machine, it also appears that PMSA would have had to have located another 0.5 Tesla MRI machine, as the machine originally offered had been sold elsewhere. This may have been very significant to the legal position of the parties at the critical times — it may have been arguable, for example, that no binding contract for the purchase of a 0.5 Tesla MRI machine existed once the ‘drop dead date’²⁷ for the machine originally offered had expired.

It is unnecessary for me to chronicle all of the defects in the procurement process that was undertaken. Suffice it to say that there appears to be a need for DHS to work further with NWAHS to improve the level of understanding at NWAHS of best practice procurement, and the responsibility and accountability framework that applies to procurement in the South Australian public sector. In particular, there appears to be a need to emphasise the proper but limited role that clinical staff should have in procurement activity for hospitals.

There also appears to be a need for DHS to consider ways in which the approvals processes for time sensitive procurements might be expedited. As matters presently stand, in the circumstances of the matter under examination, if properly conducted, at least five different approvals should have been obtained before a binding commitment to the supplier for the 1.5 Tesla MRI machine was entered into.

²⁷ This was a phrase used by the parties to indicate the expiry date of offers, etc.

7.2.9 The Quality of the 'Business Cases'

This financial transaction was subject to a review by DHS' internal audit group which provided its report to a number of parties, including the NWAHS Board.

I agree with the comments made in the DHS Internal Audit Report as to the quality of the financial information provided to DHS in relation to the MRI procurement process. The report noted inconsistency in information in documents submitted to DHS, including the business cases for the MRI machines.

7.2.10 Review of Controls

The Internal Audit Report also indicated that there were major weaknesses in internal control measures regarding procurement at QEH.

The NWAHS Board responded to the Internal Audit Report by accepting the internal audit recommendations, and directing management to implement them.

In my view, the response required goes beyond the matters referred to in the Internal Audit Report. Particular focus appears necessary on centralising contracting authorities, and in adopting a clear policy requirement that a single point of contact (with all appropriate authority) be identified for the hospital's tenders and the like. That single point of contact should not in the ordinary course be a member of the hospital's clinical staff — it should be an appropriate member of the hospital's administrative staff with appropriate levels of procurement authority and expertise.

In my opinion, the Board should give urgent consideration to a thorough review of the contracting authorities that are in place. It is not enough for the Board to provide DHS with assurance that future proposals for capital expenditure will be properly considered by the Board (though that is clearly desirable). The Board should also nominate those NWAHS officers who have authority (within appropriate financial limits) to enter into contracts on behalf of the Board and promulgate this information within the hospital.

7.2.11 The Relationship of DHS with NWAHS

The relationship between DHS and NWAHS is governed by the SAHC Act. This Act provides, that subject to formal direction by the Minister, the governing body of NWAHS is its government appointed Board. In cases of major capital expenditures it is clearly necessary for central government agencies, ie DHS, Department of Treasury and Finance and the Department for the Premier and Cabinet to be involved and for financial controls to be firmly in place.

In my opinion, the control arrangements that were sought to be implemented by DHS in this matter were not consistent with the legislative intention as set out in the SAHC Act. This is not to suggest that what DHS sought to do was not necessary in the circumstances of the affairs of NWAHS, but to simply point out that, in my opinion, it went about the imposition of controls in a manner that was not authorised via the SAHC Act.

7.2.12 Submissions made by Certain Individuals in Response to a Draft of this Report

As mentioned above, a number of individuals were invited to comment on various aspects of this Report. A number of the submissions that have been made merit a specific response, because the issues they raise, in my view, are important.

7.2.12.1 Formation of Contracts

More than one party raised the question of whether the conduct of the various parties (and especially Dr Davies) did in fact give rise to a contract or contracts binding upon NWAHS for the acquisition of one or more MRI machines.

So far as the events of November 2001 are concerned, I am satisfied that the issue of the purchase order and the acceptance of the quote and specification for the 0.5 Tesla MRI machine was sufficient to create a contractual relationship between NWAHS and PMSA. In my view, legal obligations arose in November 2001.

In my opinion, having regard to all the circumstances of, and surrounding the relationship of Dr Davies with PMSA, the events of May 2002 (specifically Dr Davies' alteration of the purchase order, and his acceptance of the quote for the 1.5 Tesla MRI machine) had the effect of varying the existing contract for the 0.5 Tesla MRI machine.

The point is that, in my opinion, Dr Davies' actions in this regard were unauthorized and inappropriate, regardless of the technical legal or 'contractual' outcome.

7.2.12.2 Fidelity to the 'Government of the Day'

Both Dr Davies and Mr Campos submitted that in placing the order for the 0.5 Tesla MRI machine 'on hold' they were serving the Government of the day, and that it is therefore unfair to criticize them for doing so. In effect, their argument is that because the incoming Government had clearly signalled a desire to provide additional funding for MRI equipment at QEH, they had an obligation to create the breathing space necessary for the new Government to fulfil its wishes.

The evidence submitted to me was that the 0.5 Tesla MRI machine was not constructed in such a way as to facilitate a simple 'building brick' style upgrade to a 1.5 Tesla MRI machine by way of a larger or stronger magnet. Rather, the 0.5 Tesla MRI machine could only be 'upgraded' to one of 1.5 Tesla strength by replacement.

Thus (so the argument goes) to have continued to pursue delivery of the 0.5 Tesla MRI machine once the additional funding was in the offing would have been contrary to the wishes of the Government of the day.

In my opinion, this argument is unsound. The fact is that before the election that resulted in the change of government at the beginning of 2002 was called, a contract for the acquisition of the 0.5 Tesla MRI machine had been entered into. Dr Davies and (particularly) Mr Campos were obliged to pursue and facilitate the due execution (ie the performance) of that contract, unless and until the responsible parties (the NWAHS Board, DHS or Executive Government, not Dr Davies or Mr Campos) decided otherwise.

If delivery of the 0.5 Tesla MRI machine was to be suspended, that required a decision (at the least) of the Board of NWAHS. No such decision was made by the Board. Proper conduct of the matter would have entailed the Board, DHS and the Minister being advised quite plainly that any consideration of additional funding for upgraded MRI capacity at QEH had to be in the context of a contract for the acquisition of the 0.5 Tesla MRI machine having already been entered into.

It was not a trivial matter to 'switch' to a 1.5 Tesla MRI machine. The probity issues and procurement processes alone were significant, but they do not appear to have been appreciated, let alone been the subject of a comprehensive briefing to the Minister.

Dr Davies submitted that had he 'not acted as he had, to preserve, by the only means open to QEH, the option of QEH acquiring a 1.5 machine, the government's promise [of additional funding] would never have been fulfilled and the funding allowed in the budget could never have been put to that use.' In my opinion, in making this submission, Dr Davies fails to understand his responsibilities as a public officer and the comment provides a further insight into Dr Davies approach in this matter. It was not his role or function to convert a political promise into a legal and practical outcome, but in my view, that is what he (successfully) set out to do.

Dr Davies also submitted that he was entirely justified in believing that there was an unqualified commitment by the Government of the day to a 1.5 Tesla MRI machine and, that his actions should only be seen as actions taken in good faith to fulfil the directions of his Chief Executive Officer and in keeping with the public commitment made by the Government of the day.

As to this submission, as indicated in the report, in my opinion, Dr Davies acted well beyond the scope of any authority he was given by his Chief Executive Officer (Mr Campos) and nothing in the political statements to which he has referred justify his actions.

7.2.12.3 But the Government could always have Reverted to the 0.5 Tesla MRI machine

Dr Davies also submitted that a number of individuals (including Messrs Campos and others at NWAHS, staff in the Premier's Office (ie Mr Ashbourne) and officers of DHS' Strategic Procurement Unit) knew of the arrangement for the delivery of the 1.5 Tesla MRI machine and, that any one of them could have initiated steps to terminate it or 'repudiate the publicly announced funding commitment with the same outcome. In the event that the publicly announced policy was changed for any reason the QEH could and would have reverted to the 0.5 machine.'

First it must be said in response to this submission that no one apart from Dr Davies and PMSA appear to have known (until some months later) that Dr Davies had altered a purchase order and accepted a quote for the 1.5 Tesla MRI machine. Certainly Mr Campos was entitled to expect that whatever else Dr Davies had done, he had at least ensured that the hospital had a right to revert to the 0.5 Tesla MRI machine.

However, it is not correct, in my opinion, to infer that it would have been a simple matter to revert to the lower powered machine. First, as Dr Davies knew, the 0.5 Tesla MRI machine that had been originally contracted for was no longer available, and if the right was exercised, another machine would have had to have been procured. Secondly, as Dr Davies also knew, the price for the replacement machine would have been different from that previously agreed and authorized (even if NWAHS had been able to negotiate a better outcome than the 'same price' commercial proposition PMSA put to NWAHS in July/August 2002). Thirdly, had the matter been properly considered from a procurement and probity viewpoint (which Dr Davies did not do), there were good reasons why it was inappropriate to agree with PMSA to purchase an unspecified 0.5 Tesla MRI machine, even if that agreement were conditional on rejecting the 1.5 Tesla MRI machine.

The fact is that no one in NWAHS, DHS or Executive Government knew of the documents signed by Dr Davies with PMSA in May 2002 until some months later. That state of affairs is wholly unsatisfactory, and is Dr Davies' responsibility. It is not the fault of others that they didn't take steps to protect the Government's position when the risks assumed by Dr Davies for the Government and for NWAHS were not known.

7.2.12.4 The Conduct of PMSA

It was also submitted that my report needed to comment upon the actions taken by PMSA, in effect, 'taking advantage' of the conduct of Dr Davies in circumstances in which it was said to be well aware of due procurement process in Government.

I have no doubt that PMSA acted commercially and in its own interests in this matter. That is not grounds for criticism of the company.

8.0 RECOMMENDATIONS

I recommend that the matters referred to in this Report be considered as appropriate by Executive Government, the State Supply Board, DHS and by the Board of NWAHS.

In particular, I recommend that the:

- Minister for Health in conjunction with DHS and NWAHS, give consideration to the governance structures at NWAHS, and regularise the current arrangements to ensure compliance with the SAHC Act;
- State Supply Board give consideration to the question of whether its policies, principles and guidelines have been adequately 'issued' to the public authorities under the *State Supply Act 1985*, including in particular the incorporated hospitals and health centres under the SAHC Act.