

Infrastructure Partnerships Australia leads the national infrastructure debate by bringing together both the public and private sectors to promote partnerships in infrastructure provision.



Infrastructure Partnerships Australia

Submission on Sustainable Sydney 2030,
Final Consultation Draft Strategic Plan,
to 2030 Team, Council of the City of Sydney
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Contact

Joanne McCafferty

National Manager, Policy
Infrastructure Partnerships Australia

P | 02 9240 2005

E | joanne.mccafferty@tff.org.au



BUILDING AUSTRALIA TOGETHER

Introduction

Infrastructure Partnerships Australia (IPA) is the nation's peak infrastructure body, representing Australia's leading infrastructure developers, constructors, investors and operators, as well as transport service providers, government departments and agencies.

IPA is dedicated to improving the provision of infrastructure in Australia, recognising the well documented positive relationship between infrastructure capability and economic productivity and performance.

We are acutely aware of the complexity associated with the formation and delivery of infrastructure, particularly in ensuring infrastructure services are 'fit for purpose' and can be managed effectively over the course of their long economic life. To this end, IPA endeavours to facilitate the sharing of knowledge and experience between public and private infrastructure practitioners to support realistic expectations and enduring outcomes, as well as greater opportunities for the private sector to contribute and work in close co-operation with governments in developing infrastructure and services.

IPA welcomes the opportunity to make a formal submission to the 2030 Team of the City of Sydney about the City's plan for the future, Sustainable Sydney 2030.

Our Submission

IPA applauds the City of Sydney for the bold vision it has articulated for the future of Australia's largest capital city, as outlined in the 2030 Team's Final Consultation Draft Strategic Plan 'Sustainable Sydney 2030'. In addition to describing the array of known challenges facing Sydney to 2030, the Draft Strategic Plan argues persuasively for a radical shift in thinking and decisive action by all levels of government, in partnership with the private sector and the community, to secure Sydney's liveability and prosperity for current and future generations.

As the Draft Strategic Plan's commentary recognises, the City of Sydney has core service and regulatory roles and a special symbolic and advocacy role to play at the heart of the Sydney metropolitan area, but it does not have the legal authority nor does it have the financial resources to deliver its 2030 vision for Sydney alone.

In spite of the obvious merit of Sustainable Sydney 2030, the Draft Strategic Plan cannot be delivered without significant support from the Federal Government, a full commitment to the Plan from the NSW Government and changes to Metropolitan Sydney's existing fragmented planning codes, which stymie effective citywide planning.

IPA is particularly interested in Section 10 "Implementation through Effective Governance and Partnerships" of the Draft Strategic Plan which touches on a range of issues relevant to Public Private Partnerships in the infrastructure sector; and Objective 10.5 which contemplates the use of innovative financing and funding approaches for Sydney's infrastructure provision.

Delivering Sustainable Sydney 2030 with Private Sector Participation

The size of the infrastructure investment task described in Sustainable Sydney 2030 is enormous.

Importantly, the City of Sydney recognises that it doesn't face its infrastructure challenges alone and it understands that by involving the private sector it may share some of the burden and identify innovative solutions. The Draft Strategic Plan clearly contemplates engaging in partnership with other government agencies and the private sector in developing firm project proposals.

A number of proposed projects canvassed in the Sustainable Sydney 2030, Draft Strategic Plan would appear, on the face of it, to be well suited to private participation, including:

- interchange connections at city squares – Central, Town Hall and Circular Quay;
- a high frequency north-south rail loop connecting the City Centre, Barangaroo and Central Station and a possible new train station at Park & Pitt Streets;
- undergrounding the Western Distributor;
- Darling Drive connections;
- redevelopment of the Cahill Expressway;
- redevelopment of the airspace at Central Station including a public venue
- renewal projects at Alexandra Canal, Redfern-Waterloo, Everleigh, Glebe and Green Square; and
- integrated waste processing infrastructure, water recycling and development of Green Transformers.

Local government procurement

Many local government assets are suited for private participation. Some of these could be in assets such as roads, pavements, bridges, drainage systems, car parks, childcare facilities, community and council office infrastructure and the like.

Although all options should be evaluated on a case by case basis, there are several models for private sector participation that local governments, including the City of Sydney, can adopt to suit their needs. Table 1 details the range of procurement options.

Table 1: Models for Private Sector Participation

Type of arrangement	Responsibilities of Private Sector	Financial arrangement	Risk sharing	Ownership of assets
Management Contract	Supplies management services in return for a fee	Fixed fee indexed to inflation	Small	Contracting authority
Lease	Runs the business, retains revenue from customers tariffs, pays a lease fee to the contracting authority, but does not finance investment in infrastructure assets	Revenue from customers, operating and maintenance costs, lease fee	Operating and commercial risks: Significant	Contracting authority
Concession (eg. PPPs)	Runs the business, finances investments but does not own the infrastructure assets	Revenue from customers, operating and maintenance costs, finance costs, any concession fee	Operating and commercial and investment related risks: Major	Contracting authority
Divestiture	Runs the business, finances investments and also owns the infrastructure assets	Revenue from customers, operating and maintenance costs, finance costs, any license fee	Operating and commercial and investment related risks: Major	Operating authority

Source: A Discussion Paper on the role of the Private Sector in the Supply of Water and Wastewater Services, Department of Prime Minister and Cabinet, August 2006.

Public Private Partnerships (PPPs)

Government procurement practices have evolved significantly over the years, largely to address the changing requirements of a strong economy and growing population. Private sector participation in the form of Public Private Partnerships (PPPs) in the provision of infrastructure services has been successful throughout the developed world and has found increasing public acceptance in Australia. Successful PPP projects have been delivered in a range of infrastructure sectors in Australia.

IPA believes that properly scoped and well executed PPPs allow for the best share of resources, skills and risk between the public and private sectors in the delivery of public assets.

PPP procurement offers significant advantages to government, industry and importantly, to meet the needs of our growing economy and diverse community, provided that the fundamentals of a stable partnership are achieved. Such fundamentals include harnessing public sector expertise, extensive community consultation, a focus on long term outcomes, and probity and transparency, amongst others.

Independent and arms-length research demonstrates that well structured and well executed PPP projects can deliver superior outcomes to traditionally procured projects. In the UK, which has been at the forefront of development of the PPP procurement framework, there has been a large body of research on PPPs. A study undertaken by Mott McDonald (Mott McDonald, 2002) focused on measuring the relative degree of 'optimism bias'¹ associated with traditional procurement. The study concluded that while UK's PPP projects were found to exhibit relatively neutral 'optimism bias', the bias found in traditional procurement was sometimes

¹ 'Optimism bias' was defined as the percentage differential between the estimated works duration or capex cost at the 'Strategic Outline Case' (SOC) or 'Outline Business Case' (OBC) and Works Completion (WC).

significant (50 % or more). The UK National Audit Office (2003) found that 73% of traditionally procured projects were over budget, and 70% were delivered late. By comparison, just 20% of PPP projects were over budget and a mere 24% over time.

IPA Research

In December 2007, Infrastructure Partnerships Australia launched a landmark report titled 'Performance of PPPs and Traditional Procurement in Australia', commissioned by IPA and undertaken by The Allen Consulting Group and Melbourne University. The study undertook comprehensive analysis of 21 PPP projects and 33 traditional projects around the nation, allowing for the first rigorous and comprehensive comparison between of traditional government-delivered and privately financed and delivered projects. Its key findings were:

- PPPs demonstrate superior cost efficiency over traditional projects ranging from 30.8% (from project inception) to 11.4% (from contractual commitment to final outcome).
- In absolute terms, the PPP cost advantage was economically and statistically significant: On a contracted \$4.9 billion of PPP projects, the net cost over-run was \$58 million (not statistically significant). For \$4.5 billion of traditional procurement projects, the net cost over-run was \$673 million (statistically significant)
- With respect to time over-runs on a value-weighted basis, traditionally procured projects performed poorly. On a value weighted average traditional projects were completed 23.5% behind time. In contrast, PPPs were completed 3.4% ahead of time on average (This is measured from contractual commitment to project completion).
- PPPs are a proven vehicle to deliver government value for money in infrastructure procurement. Approximately \$400 billion is expected to be spent on Australia's infrastructure over the next decade. With 10-15% market share, PPPs would create approximately \$6 billion in potential cost savings (vis a vis traditional procurement) over the decade.
- Project size matters greatly in choice of procurement model. project size and complexity has a marked (statistically significant) negative impact on time over-runs of traditional projects. In contrast timeliness of completion of PPP projects were not negatively impacted by size and complexity of the project.
- The study has uncovered the myth of sovereign 'risk free' borrowing rate. The report highlights the fact that the risk free borrowing rate is not actually equal to the cost of capital. An infrastructure project always has project risk associated with it, irrespective of the fact whether the public or the private sector undertakes it. Thus the cost of capital is equal to the risk free borrowing rate plus the project risk.
- In contrast to commonly held perceptions, PPP projects were far more transparent than traditional projects, as measured by the availability of public data for the study.
- The benefits identified in the study are conservative. Because the study was design and construction centric, it has not captured the long term value delivered from:
 - ✓ Whole of life asset management
 - ✓ Long term risk transfer
 - ✓ Young assets, full risks not adequately captured
 - ✓ Asset quality at end of concession period

Local government & Procurement Models - Managing Risk

As the PPP model has been refined in Australia, the public sector has developed significant expertise in harnessing private support to build infrastructure projects and obtain the best value for money for the community. A description of the most commonly used procurement models is provided in Table 2 below.

Table 2: Procurement Models

<p>Traditional Design and Construction (TDC) The local government, as principal, prepares a brief setting out project requirements before inviting tenders for the design and construction of the project. Private sector contractors undertake to design the project in accordance with the brief, and construct it for an agreed sum, which may be fixed or subject to escalation.</p> <p>Operation and Maintenance Contract (O&M) These projects involve the private sector operating a publicly-owned facility under contract with the local government.</p> <p>Design - Build - Operate – Maintain (DBOM) These projects involve the private sector contractors undertaking to design the project in accordance with a brief from local government setting out the project requirements, and constructing it with an on-going arrangement to operate and maintain the publicly-owned facility under contract with the local government.</p> <p>Lease - Develop - Operate (LDO) This type of project involves a private developer being given a long-term lease to operate and expand an existing facility. The private developer agrees to invest in facility improvements and can recover the investment plus a reasonable return over the term of the lease.</p> <p>Build - Own - Maintain (BOM) This type of arrangement involves the private sector developer building, owning and maintaining a facility. The local government leases the facility and operates it using public sector staff.</p> <p>Build - Own - Operate - Transfer (BOOT) Projects of the Build-Own-Operate-Transfer (BOOT) type involve a private developer financing, building, owning and operating a facility for a specified period. At the expiration of the specified period, the facility is returned to the local government.</p> <p>Build - Own - Operate (BOO) The Build-Own-Operate (BOO) project operates similarly to a BOOT project, except that the private sector owns the facility in perpetuity. The developer may be subject to regulatory constraints on operations and, in some cases, pricing. The long term right to operate the facility provides the developer with significant financial incentive for the capital investment in the facility.</p>

IPA believes that the necessary (if not sufficient) conditions for PPPs to work at the local government level are the following:

- The size of the project in financial terms should be large enough to attract private interest and participation;
- Local governments must properly scope a project before taking it to the market. The local government should authoritatively negotiate a contract that clearly articulates the desired outcomes, with a focus on whole-of-life operation, rather than merely the construction phase;
- For a partnership to work, risks should be placed with those best equipped to manage the risk. Pushing inappropriate risk onto any party in the partnership is inefficient and drives up cost;

- The long-term nature of PPP projects means that some contractual changes are likely to be necessary during the life of the project. Changes relate to the specification, new services, additional building work or design changes and performance measurement arrangements. Appropriate procedures for dealing with change should be built into the contract. This includes procedures to ensure that value for money is maintained when contract changes occur.
- Having staff with the right skills is essential to good contract management. Attention needs to be given early in the procurement process to staffing, training and contract management issues, and how the relationship between the local government and contractor will be developed.
- For a partnership model to be a success, all parties to it must understand what is sought. Bid costs should be reasonable for private parties to evince interest in the project. The information released to market to price a project should be correct, and there is scope for improvement in this area;
- Community consultation is important in all local government infrastructure projects, more so for projects undertaken through PPPs. The government must establish what the community expects and how these expectations can best be satisfied in the project design. After construction, there is often an ongoing obligation for the operator to continue to consult with the community.

The Local Government Act 1993 (NSW) provides the regulatory framework for infrastructure PPPs entered into by NSW local governments. The Act specifies:

1. Guidelines setting out processes and procedures for local governments to follow in negotiating and carrying out PPPs. These guidelines establish procedures to be followed for various stages of a PPP project including:
 - initial stage of establishing a need for the project in question;
 - a preliminary assessment of the council's capacity to undertake the project;
 - the establishment of a probity plan, a community relations plan, a preliminary risk assessment and a form of comparator similar to the Public Sector Comparator used in various State PPP guidelines;
 - assessment to determine whether the project should proceed;
 - approaching and evaluating potential private sector partners through an expressions of interest (EOI) process;
 - taking of detailed submissions from short-listed private sector proponents;
 - selection of the preferred proponent;
 - contract development, approval and management.
2. A project review committee must review significant and high-risk projects defined as:
 - Projects worth more than \$50 million;
 - Projects in which a council's financial contribution is 25% or more of council revenue that is available for spending on facilities or services of the kind to which the project relates

3. Compulsory tendering requirements of the Local Government Act 1993 also apply to PPP contracts. This is aimed at preventing the use of financial entities or project vehicles to circumvent tendering requirements under the Local Government Act 1993.

Local government has faced hurdles entering into PPPs, largely due to the relatively small scale of projects. While many projects contained in Sustainable Sydney 2030 are of significant scale, the City of Sydney should give consideration to 'bundling' smaller projects together wherever possible to ensure the commercial viability and to ensure value for money for ratepayers.

Conclusion

Infrastructure Partnerships Australia commends the City of Sydney on the development of the excellent vision articulated in the Sustainable Sydney 2030 plan. The focus on delivering a green, global and connected Sydney in Sustainable Sydney 2030 is welcome and timely.

IPA recognises that the delivery of better infrastructure and services is a critical aspect of sustaining and enhancing Sydney's economic growth and social development to 2030, and to securing the City's liveability and prosperity for future generations. The high expectations of the community in terms of the services delivered by infrastructure assets means that strong cooperation between the public and private sectors is critical to deliver long-lasting and innovative infrastructure through a partnership.

The issues surrounding infrastructure financing and delivery are complex and this submission provides only rudimentary suggestions on what is a significant and ambitious undertaking by the City of Sydney. We would be very happy if this in any way contributes to the endeavours of the 2030 Team and the wider Council. We hope that our submission is useful to the 2030 Team in the preparation of the Final Strategic Plan on this important initiative.

Should you have any enquiries or queries regarding this submission please do not hesitate to contact Joanne McCafferty, National Manager, Policy, on (02) 9240 2005.



Infrastructure Partnerships Australia
8th Floor, 8-10 Loftus Street, Sydney NSW 2000
www.infrastructure.org.au

T 02 9240 2005
F 02 9240 2055
E contact@infrastructure.org.au