

CORRECTED VERSION

PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

Private sector investment in public infrastructure subcommittee

Inquiry into private sector investment in public infrastructure

Melbourne – 20 August 2002

Members

Mr R. W. Clark

Ms S. M. Davies

Mr T. J. Holding

Mr P. J. Loney

Mr G. K. Rich-Phillips

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Witness

Mr G. Joyce, Graeme Joyce Pty Ltd.

The CHAIRMAN — I welcome Mr Graeme Joyce from Graeme Joyce Pty Ltd. All evidence taken by this subcommittee is taken under the provisions of the Parliamentary Committees Act and is protected from judicial review. However, any comments made outside the precincts of this hearing are not protected by parliamentary privilege. All evidence given today is being recorded by Hansard. Witnesses will be provided with proof versions of the transcript early next week.

Mr Joyce, would you care to make an opening statement to the committee before going to questions?

Mr JOYCE — I am happy to take questions.

The CHAIRMAN — From your experience, could you outline to this committee what you believe to be the positive aspects of a partnerships approach in Victoria and any significant barriers that you perceive there may be to successful outcomes to partnerships in Victoria?

Mr JOYCE — I have been involved in private sector infrastructure delivery for a number of years. I have a few notes here; if you do not mind, I will refer to them on the way through.

The CHAIRMAN — Sure.

Mr JOYCE — Some of the things that I think are the demonstrated benefits of private sector involvement in infrastructure are cost savings. I think there is a net present value saving of using the private sector. I think that comes generally from their ability to manage and price risk. I have been involved on both sides of the fence, public and private. I do not think the private is any better inherently than the public. In fact I think these days public life is much more difficult than private sector life, to be honest, because of some of the politics that go around doing a job. But certainly their ability to manage and price risk is superior in the private sector. I am happy to elaborate if anyone has any queries on the way through.

The CHAIRMAN — That is an interesting point and one in which the committee does have an interest. Could you expand on why you believe that to be so?

Mr JOYCE — I believe the private sector have less outside influences than the public sector. If we look at the problems that Transurban had in constructing the City Link, for example, I think their ability to manage and commercially solve those problems was far superior than would have happened in the public sector. Let's look at a couple of examples. With the tunnels they had lots of trouble, which has been well publicised — with the construction of the tunnels. Those problems were worth tens if not hundreds of millions of dollars. There is every likelihood, if that had been public sector delivery, that those problems would have still been there as technical problems. If the state had been directly contracting with a design-and-construct contractor and they had those same problems, the facts are there are not many people in the state who have the commercial nous, the delegated responsibility and, if you like, the will to solve problems worth tens if not hundreds of millions of dollars. The private sector were able to dig into their pockets and solve it with dollars. Does that make sense, Mr Chairman?

The CHAIRMAN — Yes.

Mr JOYCE — I worked with Transfield for a couple of years. I know the owners of Transfield quite well. They had a commercial driver; they had a figure in mind; they were able to sit around the table and solve those issues with Transurban, who had similar drivers in mind. Who would have been able to do that in the state? I acted for many, many years when I was at Melbourne Water as a project manager trying to resolve contract disputes. It is very difficult, because people are working within delegated authorities; they are quite concerned to keep ministers' names out of the press; there are a lot of problems, a lot of drivers on them, that are not just purely commercial. That does not mean they are any worse at it — often they are better at it — but they have a lot of impediments to solving commercial issues. That is the sort of thing — they can manage and price risk and control risk a little bit better, if that makes sense.

The CHAIRMAN — Yes.

Mr JOYCE — The second point I was going to make is that I think it is more strategically beneficial. I have a sheet here that I would like to use. It is something I have used over the years in a lot of my presentations. What I have outlined here is what I call the asset life cycle. There is nothing revolutionary here but basically all assets go through the cycle.

If I just read through it quickly: there is a need for a product — if there is a shortage of water there is a need for a dam or there is a need, alternatively, to do water conservation, or whatever. So then you come up with the ideas to

solve that need, so they would go to outline 2, on water shortages et cetera. There are then concepts for solving those ideas. We come up with preliminary design, detailed design, construction, commissioning, operation and maintenance, and decommissioning.

If you like, I will just run through the sort of spiel I give a lot of people.

The CHAIRMAN — Yes.

Mr JOYCE — I guess in the 1950s and 1960s the public sector did every step in that asset life cycle. If you think back bodies like Vicroads, Melbourne Water and the Public Works Department had people who did every step in that process. Probably in the 1960s people started to contract out the construction arm of that activity, so they would go out for a construction contract — previously they were doing it themselves, if you recall. The reason they did that of course was that their construction requirements would ebb and flow, so why have a construction force that was for the peak and they could never downsize during the ebbs? So they contracted that out.

To move forward, in the 1980s people started contracting out detailed design sections. For example, when I was at Melbourne Water it sold off its design section. Then it got revolutionary and had a look at design and construction, and it started outsourcing commissioning in operations and maintenance. What a BOOT — build, own, operate, transfer — project essentially does is outsource those four arms, somewhere between preliminary design right through to decommissioning potentially. This is a long-winded way of saying it. What is one of the great strategic benefits in that? It allows the state to concentrate where I think it is best — on the needs, ideas and concepts. So it would not be running around busily constructing things and managing design and construction disputes, it would be at the strategic end of life. I think that is a great strategic benefit.

If we come back to the shortage-of-water issue, where the state best adds value is in the strategic answer to that water shortage issue, not out there managing contract disputes over the price of a contract. If we go a bit further, let us look at the issue again of the shortage of water. If there is a need, and that is the shortage of water, by the time you have come up with the idea you are either going to build a dam or you are going to concentrate on water conservation or whatever you have locked in prices pretty well. All the stuffing around at the construction end has only about a 5 per cent or 10 per cent impact on the final cost. That is where all the headlines are — that something went 10 per cent over cost — but really if you are going to solve that water shortage problem by building a dam you have locked in \$2 billion. It might be \$1.7 billion or it might be \$2.3 billion, but you have made the decision up front. So it allows the public sector to do what it does best — that is, the strategic approach to problem solving. That is what I believe.

The CHAIRMAN — Within that, the one area of risk that the private sector does not need to consider but the public sector does is political risk. How do you factor that into what you are doing in here? Where is the appropriate place? How should that be factored into the project?

Mr JOYCE — Political risk invariably stays with the public sector ultimately. Again, I would argue that with most projects by the time you have gone through the needs, ideas and concepts phase you have locked in the sort of political risk around the process, and I do not think the delivery mechanism for detailed design, construction and commissioning has a giant impact on it.

For every project that has been delivered through a Partnerships Victoria (PV) type of process or a public-private partnership (PPP) that has gone sour — for example, Seal Rocks — there will be equally one that has been delivered under a more traditional mechanism that has gone sour — for example, Federation Square. So you can never ignore that political risk. But I would strongly argue that it was around the concept and the idea of both of those projects that things went wrong. So it is not really the project delivery mechanism, like PPP versus D and C et cetera; it was some flawed either implementation of ideas or concepts and probably in both cases some contract administration issues that were not up to scratch.

The CHAIRMAN — I would also see political risk as operating between the decommissioning and decommissioning periods; that is probably the greatest period where political risk is a factor, and it is how you deal with that, and issues such as the appropriate role of ministerial responsibility within that. How should those sorts of issues be dealt with?

Mr JOYCE — I think we might be talking slightly at cross-purposes. Could you give me an example of perhaps a practical political risk there? I tend to see it diminishing.

The CHAIRMAN — Fully privatised electricity generation, for example. If you have a power station that is not online the government is seen as having to take responsibility for that, yet the minister may have no direct role, direct responsibility or directly supplied information. It is those sorts of issues that I am talking about.

Mr JOYCE — I am not an expert on the electricity industry, but let us use that example.

The CHAIRMAN — It is a general principle.

Mr JOYCE — I am happy to address that. It is a similar concept to what I am used to — that is, the water example I have been going back to. In electricity I would argue that the requirement to have adequate electricity capacity can never leave the public sector. It is an inherent reason why we have this Parliament building; it is why we elect officials to look after the greater good. But contracting out the ownership of assets in that supply chain should not be confused with the greater need of the public sector to manage the long-term requirements there.

The CHAIRMAN — I absolutely agree with what you are saying; I am just asking how we do that within the arrangements.

Mr JOYCE — I think through clarity about what we are contracting out. I do not think the state ever contracted out, for example, in electricity, the requirement for long-term capacity to be in the network. That requirement stayed with the state, and the state then has to understand what it did contract out and what stayed in house.

The CHAIRMAN — Is the state then unimpeded in making a decision to put more capacity into the system?

Mr JOYCE — It depends on what the contract said, but it comes back to the strategic set-up of those contracts, and for the state to understand what it wants to remain in control of and how it will remain in control of it.

Mr THEOPHANOUS — I am sorry to have come in the late on this conversation, which I am very interested in, and the issues surrounding it. Political risk is not an issue that concerns me greatly. I think political risks exist almost irrespective of what you do; they can exist in the public sector or in the private sector. What I heard, though, was that you were making a generalisation that the public sector does strategic planning and delivery better in some way, and that it should concentrate on that and that the private sector should be engaged to deliver the actual services. That is an interesting way of looking at it but one that I would ultimately have to reject. Isn't the real issue nothing to do with who has the greater capacity in strategic thinking or any of that stuff? The real issue is value for money. And if the private sector is unable to deliver at a lower cost in some way or another to the public sector, isn't that really the bottom line?

Mr JOYCE — There is no doubt about that. What I was saying — it might have been just before you came in — was that I believe the private sector has demonstrated it can manage and price risk at a lower level than the public sector.

Mr THEOPHANOUS — What examples are you using to justify that statement? I can think of a large number of examples where the opposite is true, where the contracting out procedure and all the rest of it has resulted in a greater cost than could have been the case if it had been delivered by the public sector.

Mr JOYCE — Are there examples? I do not really know of specific examples, but if we bring it back to the Partnerships Victoria policy, for example, that tried to address that exact issue by looking at the public sector comparator. That is exactly what the public sector comparator is designed to do — to make that very transparent. I think quite a few of the deals that have gone on until the past few years probably did not or were not capable of explicitly being able to show which one was cheaper and which was not. But I agree with you 100 per cent. The public sector comparator, which is a very misunderstood beast, is designed to do exactly that — that we look at the total risk adjusted cost that public sector delivery would give, and when bids come in from the private sector if they are lower than that the project goes ahead, and if they are not the project does not necessarily go ahead. That is the whole process that has been adopted under Partnerships Victoria — to explicitly put a price on that value for money, which is the difference between the actual bids and the risk-adjusted net present value of public sector delivery.

Mr THEOPHANOUS — I can tell you there are some that have not got over that hurdle.

Mr JOYCE — That is fine, I agree, they should not go ahead then. That is the ultimate test.

Mr THEOPHANOUS — I thought you were suggesting some other criteria about strategic capability.

Mr JOYCE — No, I was asked to talk about some of the benefits of private sector delivery. I have a check list: the first was cost savings, and certainly under Partnerships Victoria — —

Mr THEOPHANOUS — If I could ask you one further question: I do not know whether it fits into this category but sometimes the loser is not the public sector and the loser is not the private sector but the loser is the consumer, where the consumer finishes up paying additional costs basically because the private sector might be in a position to charge the consumer more as a result of the arrangement than the consumer would otherwise pay.

The electricity industry is an example of that, where effectively there is some competition among the five distributors but there is also, on the networking costs, no competition.

Mr JOYCE — I agree.

Mr THEOPHANOUS — The charges there are subject to a whole range of different things, and whether the consumer is being ripped off or not, as opposed to the taxpayer, would have to be a big issue. Similarly I would argue that City Link at a cost of \$2 billion will cost the commuter, as opposed to the taxpayer, very much more than \$2 billion over the 34-year life span. It is going to cost an absolute fortune.

Where in there is the public interest? How do we determine even if one can say strictly from the point of view of the government that City Link was a good deal, and from the point of view of the government the electricity sell-off was a good deal, but was it a good deal from the point of view of the public? Is that not a question that governments should ask?

Mr JOYCE — There is no doubt about that. To look at how that has been looked at in Partnerships Victoria, of course there is a large section there on public interest. Both those projects were implemented prior to Partnerships Victoria. I will answer both your examples to the best of my ability.

If the electricity deals are such that now and in the future the public of Victoria end up paying ridiculously high prices for electricity because we have structured little mini-monopolies, if you like, then I would agree, they have stuffed up the deal. I cannot put it more bluntly than that.

It does not sort of affect the whole equation, though, but from a consumer point of view it is a bad deal and there is no doubt they have mismanaged it, but that comes down to the people who structured the transaction at the time and how they allocate risk. We have to remember that the state received amazing prices for those deals as well. All of that had to be balanced into the equation.

Mr THEOPHANOUS — Does that not mean from a government point of deal it was a good deal?

Mr JOYCE — I always have trouble when you say ‘government’ as distinct from ‘public’. The government is an extension of the public, if you understand what I am saying. I am not disagreeing with you, I think I am agreeing. If it means that ultimately I am paying a lot more for my electricity, I will think it is a bad deal. I am not sitting here saying that every private sector transaction that has ever gone on is a good deal and that all stakeholders have been looked after, but if, for example, the sale price on electricity was a fantastic deal at the time and ultimately the protections are not there on price increases, or whatever — and I am not close to those transactions — then it is not a good deal, or potentially it is not a good deal.

Mr THEOPHANOUS — I am saying it is probably a good deal from the point of view of the government but not necessarily from the point of view of the public, and there is a distinction that you can make there.

Mr JOYCE — And City Link is probably even more transparent there. Let’s look at the deal on City Link as well from a number of aspects.

I worked in the public sector for many, many years. I am not here public sector bashing; I think they do a marvellous job under incredible duress. I would argue very strongly that if the public sector, Vicroads, had been managing that contract, I believe — and it is a personal opinion — they would have struggled to finish that project with the problems it faced and certainly the industry — lots of people in the industry believe — the state would have been involved in massive litigation for a number of years, given the magnitude of the commercial issues on that project. It is one of the benefits of private sector delivery.

The whole issue of user pays is an incredibly complex one. I happen to live in the western suburbs. I can see a giant inequity that I have to pay a toll on that side of the city and when I drive over the Eastern Freeway there is no toll. But that is a whole argument about user pays, which again conceptually I actually believe in, but there is no doubt there are inequities in having tolls on that side of the city and not on other freeways.

I am looking at freeways in a different guise at the moment. I think the acceptance of tolls on City Link by the general public has been amazing. It comes back to a statement before about political risk and I want to pick this up, that certainly the greatest political issues on that project, for example, happened during the construction phases because the newspapers love cracked tunnels or bridges that are not quite open. You don't read about that much now. You don't even read in letters to the editor that much complaint about City Link.

Often I talk to my friends about that and there is real acceptance of City Link as a project. It is quite interesting, the little economic equations that I know most of my friends do now on using or not using that facility. That is probably a little aside from what you were saying, but I do not believe it is all evil or downside. It delivered a project at no cost to government and, yes, it is a user-pays thing for 20 years.

Mr THEOPHANOUS — Thirty-four, actually.

Mr JOYCE — The magnitude of those tolls can be argued, the structure of those tolls can be argued.

Mr THEOPHANOUS — I think somebody did some numbers on a proposal to get rid of one of the tolling points on the Tullamarine Freeway. I think when it was put that City Link put the proposition that to get rid of the one tolling spot on that Tullamarine Freeway, they would be prepared to forgo it but at virtually three-quarters of the cost of the total project. That is a measure of how profitable that is going to be not for one or two years but for 34 years.

I understand the issues you have raised, but you could also equally say, 'Let's contract the whole thing out; there are other models that could be used beyond the user-pays model: governments can contract out the whole thing and shift the risk off in that way without necessarily going down the user-pays model'.

Mr JOYCE — I can debate that with you. I like user pays; philosophically it is a great way to move forward, but there is no doubt there are inequities when you have a tiny segment of the system as user pays and the rest of it is not. That is where I basically come from.

The CHAIRMAN — Without going to the philosophical, what I was raising earlier with relation to political risk is a much different question to what was being raised then. What I was raising was if you take City Link for example, it was a private sector project delivered by the private sector, and so on, but still public infrastructure. What is the appropriate government's accountability and ministerial responsibility regime attached to that? That is what I was getting at, not simply for City Link but any project of that type, and how do you continue to ensure ministerial responsibility as we know it under the Westminster system attaches to that type of project? That is the question I was raising.

Mr JOYCE — I do not have a straightforward answer to that question.

The CHAIRMAN — In that answer and hopefully in the short time we have we will talk about your other views of the positives of the policy and whether you believe there are significant barriers currently existing.

Mr JOYCE — I will just run through these other points I wrote down; we have talked about these on the way through anyway.

One point was the transfer of risk. Obviously these projects are very efficient at transferring risk from the public sector into the private sector. The private sector was accountable for delivering City Link by a certain time. Very little risk remained with the public sector other than the appearance — I would put that under the banner of political risk — of it not being available by a certain date. But ultimately Transurban and its financiers and equity holders were the ones who suffered from any delays in that project, and that was a very efficient risk transfer.

The next point I wrote when I looked at asset life cycle was commercial transaction. One of the things I got exposed to very early on in relation to the benefits of outsourcing different elements which were traditionally public sector roles was the fact that you suddenly had a commercial structure around what were otherwise very loose arrangements. I will give a very simple, corny example. I remember back in the mid-80s when we got a new chief executive at Melbourne Water we were starting on an outsourcing journey and he talked about being involved for about three days on a dispute in Melbourne Water's kitchen. Back in those days they used to have large cafeterias

and here was the chief executive of Melbourne Water being tied down on a dispute with some kitchen hands, and he said, 'I don't think that is what I am employed for'. That is a very simple example: if you contract out, for example, a kitchen facility you have a hard commercial arrangement between the person giving that service and an organisation. BOOT projects are just a very extravagant extension of that. There is a commercial relationship between the person providing the service and the responsible state body.

The final point — which is related to that last point and is a sub-issue of BOOT projects, and you will not hear many people talking about it — was that one of the great side benefits of BOOT projects is that they lead to massive cultural change in an organisation. I was involved in the Grampians Water project, and I said to the chief executive when I went into that role as project director that his organisation would not be the same once he had the deal up, and that was no doubt correct. It forced the organisation to look at the life-cycle costing issues of a project and not just say, 'Let's build another water treatment plant because the water is not up to quality'. It forced it to look at how it was going to perform over the next 30 years, so it forced massive cultural change within the organisation, if that makes sense.

The CHAIRMAN — Yes.

Mr JOYCE — That is my little check list. The next part was how to enhance the process.

The CHAIRMAN — Yes. Basically, do you discern any significant impediments or obstacles at the moment?

Mr JOYCE — I wrote down a few little dot points on this. I believe the biggest impediments to successful implementation and integration of private sector involvement in infrastructure — and I am speaking broadly here — are education and understanding. Within the last month I have sat in meetings with heads of government departments who really did not understand a thing about what the private sector's role was in private sector infrastructure development. There is a massive need for the public sector to become more knowledgeable about where and how, for example, Partnerships Victoria is applicable.

The CHAIRMAN — Do you believe the converse of that also applies and that the private sector is not necessarily as fully attuned to issues of public interest and so on as is the public sector?

Mr JOYCE — I do not think they are as concerned. Their strength — like myself and like a lot of people — is their weakness. They are so determined to be out there making a buck, trying to keep their job, looking over their shoulder and working hard that they do not have a lot of time for thinking through a lot of those issues. As I said before, in my experience they are nowhere near as strategic. They are good at what they do, which is a pretty narrow slice of skills. If you are in public life you had better be good at a very broad spectrum of issues or you will not survive very long in this day and age. The private sector is much narrower in its spectrum of skills.

Mr CLARK — At 5 minutes past 2, can I ask you specifically about your experience with the Westgate international container terminal project and how that worked or did not work as a public-private partnership (PPP), and what you thought went well and what you thought might not have gone so well?

Mr JOYCE — I was a project director on the Westgate container terminal project. It was a fascinating project outside the guidelines of a lot of private sector participation projects or PV projects, but we certainly followed the Partnerships Victoria process. That project was all about trying to attract capital generally from overseas to construct a third container terminal in Melbourne.

My client, who was Melbourne Port Corporation, considered the process a success to a certain extent because the process was always about testing the market on the commercial viability of a third operator in the port of Melbourne. Ultimately we were not able to find a third operator who could make a commercial business out of that process.

It is worth remembering that the essence of Partnerships Victoria is nothing magic. The process it follows has been around for 20 years — in fact, a lot longer. In that process we looked for expressions of interest in the prospect and then we asked for detailed proposals, and we did not receive a detailed proposal that was capable of acceptance, and that demonstrated value for money for the state.

If you look at the options in the terms we have been talking about today, an alternative would have been a state delivery process, for example, with the state going down there and investing tens of millions of dollars in the hope that the project would be successful. Has that answered your question?

Mr CLARK — That answers a large part of it. How did you find working under the partnerships framework for a project like that?

Mr JOYCE — At times I was very frustrated by it because it was long winded, but that was the nature of the transaction; it was quite a complex transaction. The concept of an expression of interest, calling for requests for tenders, et cetera, is nothing new to me.

Mr CLARK — More generally, do you have any comments to make on the Partnerships Victoria policy both as a policy and in terms of how it has been applied in Victoria since the time it was announced?

Mr JOYCE — Generally the policy works. What is the policy? The policy is nothing more than processes that are pretty rigorous tender processes which people like myself are very used to going through. What it has done, though, is give a very clear framework — a blueprint, if you like — for us to glue a project to. It is a good process. As I said before, I certainly think that education about what is in it and what it means, and demystifying some of the terms in it, certainly requires a lot of work.

The CHAIRMAN — I am not sure if you will have a view on this, but a number of submitters have put to us that they believe the \$10 million threshold for going into Partnerships Victoria is too low and that a more appropriate threshold might be \$100 million of net present value, or NPV, a lot of which is related to their view about bid costs. A \$10 million project probably involves almost as significant bid costs as a \$100 million project, and yet the return is inherently less. Do you have a view about that threshold issue? Should there be a threshold?

Mr JOYCE — I have very strong issues on a few sub-issues that are raised there. A value has to be put somewhere to tie the process together. If you want my gut reaction, about \$40 million or \$50 million would be the right size. Notwithstanding that, you mentioned something on the way through — that is, transaction costs. Transaction costs are one of the big negatives that have to be worked on. I probably should have written that down and made that more explicit.

What causes the transaction costs? First, these projects are quite complex. I do not know if there are any lawyers in the room, but these deals have certainly tended to become a bit of a lawyers picnic, and that is very unfortunate, and a lot of that should be standardised to a great extent. So probably from a process perspective that is one of the great advances that could be made.

The contracts that underwrite these deals, 90 per cent of them are the same on every transaction. There is no reason why the transaction costs are so high. I should not say there is no reason; one of the reasons is they are not that frequent. It is not as if you have an Australian standard off the shelf. We should be working very hard — whoever the 'we' is, probably Treasury — to come up with standardised-type contracts and get out of the loop which often happens here, and where it sometimes takes years to close out a deal.

The CHAIRMAN — Mr Rich-Phillips might correct me if I get this wrong, but we were told about it the other day. Are you aware of the UK arrangement that uses the best and final offer (BAFO) process? Do you have a view about that?

Mr JOYCE — Yes. I guess in Australia conceptually, that is not outside Partnerships Victoria, I have a very strong view that it is up to the public sector to get its risk profile and its requirements for a transaction in place and very clear and very well thought through before it goes to the market. If the state says the risk profile has to be so wide and so big, and that is reflected in the contract — and I am talking conceptually — then that is what the private sector should bid on, and not go out with loosely constructed contracts that are not clear on risk allocation, and then we get highly qualified bids. We should be asking for as near as possible a BAFO when they submit their final tender. We should be asking for bids that should be capable of acceptance.

The CHAIRMAN — And a lower level of documentation at that stage.

Mr JOYCE — A document ready to sign, that the state is ready to transact, that is what we should be going out with. We are ready to sign this; that is the deal we want.

You will have to shut me up on this one because I can talk about this for hours. Just quickly on that, you will often hear the private sector saying it cannot accept a certain risk. You can say to that same person, 'I will give you \$1 billion to take it and we will see if you can take it'. You are never talking about whether they can or cannot accept a risk; it is how much you are willing to pay for it. That is one of the great things about these projects; it really does identify, allocate and price risk in a transparent way.

The CHAIRMAN — Thank you, Mr Joyce, for your time today, and for your submission.

Mr JOYCE — If there is anything anyone would like to follow up, I would welcome it.

Witness withdrew.

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Melbourne – 20 August 2002

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Witnesses

Dr A. Smith, Director; and

Ms M. Baker, Melbourne City Link.

The CHAIRMAN — I welcome Dr Alf Smith and Ms Mary Baker from the Office of the Director, Melbourne City Link, to this public hearing on private sector investment in public infrastructure. All evidence taken by this subcommittee is taken under the provisions of the Parliamentary Committees Act and is protected from judicial review. However, any comments made outside the precincts of the hearing are not protected by parliamentary privilege.

All evidence given today is being recorded by Hansard. As witnesses, you will be provided early next week with proof versions of the transcript.

Dr Smith, are there any brief comments you would like to make in opening before we go to some questions?

Dr SMITH — If you have a few minutes there are a few comments that I would like to make. Thank you for the invitation to appear before you today. I have looked at the committee's terms of reference and I believe you have set yourselves an enormous task; they are very comprehensive.

As you may be aware, my experience in City Link dates back some considerable time. I have been working on the project since late 1992. During that period I have seen the project evolve from a concept to a detailed project brief, through the bid phase, to the selection of Transurban as the preferred consortium, and then through what unfortunately turned out to be a difficult construction phase, and finally on to what I now believe is a successfully operating toll road.

It has been a fascinating and many-faceted experience. As the Treasury submission acknowledges, public-private partnership practice is evolutionary. It is important when you look back on a project like City Link that you recognise it is a product of the early 1990s, and is a reflection of the requirements, the circumstances and the knowledge of that time. It reflects the policy framework of the government of the day, remembering it was initiated by one government, pursued by another government, and was brought to fruition under a third government. It also goes back in City Link's case to the difficult financial situation that was encompassing Victoria in the very early 1990s.

I thought it might be useful to reflect on some lessons I have garnered from my experience with City Link, and I will try to go through those quickly for the committee.

Firstly, for a project to be successful it is necessary that both the state and the private sector want the project and that both recognise its benefits and its worth.

Secondly, public-private projects involve a considerable degree of lead time in planning. From the state's point of view, the preparation phase is essential, and during that phase the objectives must be clear and specified, and the must-haves — those essential criteria — must be spelt out, communicated to and understood by the private sector.

Thirdly, both parties need to understand the various phases of the project — the preparation, the bid, bid assessment, construction, opening and completion — because each phase requires specific skills and a particular focus which changes as the phases progress.

Fourthly, it is also true that it is important not to be distracted by the immediate tasks. During construction, or during negotiations prior to construction, most people concentrated on the engineering side of City Link. As construction progressed, the emphasis turned to opening the link, marketing it and developing customers, and now particularly as it is in operation, City Link is really a service. It is about selling travel time savings, safety and comfort of road use. The road is a means to provide the service; it is not an end in itself.

Fifthly, the necessary organisational structures to manage the state's interests need to be established, and established early. This sounds simple, but it is essential to recruit good, skilled people with a range of disciplines, and also a range of individuals who are prepared to step outside their disciplines and work together with others to provide creative solutions to emerging issues. The experience of City Link shows that the emerging issues are going to come from mostly unexpected areas, as well as some that are more likely to be expected.

Sixthly, the recruitment of expert advisers is a must. Inevitably, these types of projects involve complex commercial agreements, and there will be a need to draw on specialist skills, not just commercial and legal, but also engineering, traffic modelling, and a whole range of skills from time to time.

Seventh, and a fundamental one, is you need to establish good working relationships between the state and the private parties and maintain those for the life of the project. I will come back to this towards the end of my comments.

Eighth, depending on the significance of the project, particularly one the size of City Link, there is quite a demand on government, the bureaucracy and on ministers. Decisions are often needed in short time frames. They usually take considerable resources in analysing and then briefing ministers and cabinet committees and then in monitoring. All that means is that these projects, particularly the large ones, demand considerable resourcing.

Ninth, risk management is always a vexed issue, as I am sure you have discovered. The very allocation of risk is a matter of judgment, but more important is the effective management of that risk as the project moves forward. Vigilance is required to manage that risk profile not only from the government's perspective but also from the private sector's perspective.

Tenth, major public-private projects inevitably span governments; this is something I have referred to already. Obviously that creates challenges for the parties.

Eleventh, and very critically, once established, ongoing contract management is essential. You must never lose sight of the main game; there is an ongoing commitment that is required over the life of the contract, not just during the construction phase.

Twelfth, learning and sharing experiences amongst and within government is a must. I am sure Treasury has spoken to you on that; it is establishing a whole range of procedures to enable that to happen.

Finally, explaining what is happening in these complex projects is a difficult task. Trying to communicate that to the public is a complicated task. These are relatively new concepts, they are complicated concepts, and ensuring that all the major contractual documentation is publicly available is a step in the right direction to help that.

I would like to return and make a further comment about contract management; I think I have given an indication that this is critical. I believe it is essential to establish close working relationships with your partners or the concession holders but also remembering that the role of government is to monitor and to regulate those. It is an interesting dichotomy that you are meant to be facilitating, encouraging and developing but at the same time making sure that the public interest is being looked after and the contracts are being honoured.

You need to keep other areas of government informed, acting as a means of communication to the central agencies and working closely with them to facilitate quick decisions when required. Often the private sector wants very quick decisions and often appropriately so. You need to ensure there are adequate internal resources to accommodate the proposals from the franchise or concession holder, even if they come up with more than one proposal or there is more than one issue at a time. I love the day we only have one issue on our plate at a time — we usually have a whole range of issues from the significant to the not-so significant. You need to ensure there is adequate succession planning. In a contract that goes until January 2034 there is no doubt that there will be many different groups and generations of parties, not only on the government side but also on the private sector side. How you keep those relationships going and the information maintained to maintain the corporate knowledge is critical.

Finally, if I can conclude on this, you need to stay ahead of the game and try to anticipate the future, not only what the manager wants but what the concession holder wants, what the government of the day wants and what the community is expecting. There is no doubt also that over the next 30 years the expectations of City Link from all those parties will change.

The CHAIRMAN — Can I start by asking you whether you are aware of the Partnerships Victoria policy and framework?

Dr SMITH — Yes.

The CHAIRMAN — Perhaps I can ask you then, in your particular project what substantial differences would that have made to the way in which your project was developed and carried through? Would it have made a difference?

Dr SMITH — It is a difficult question to answer, because as I have said I believe that a project is very much a creature of its time and the environment and therefore it is difficult to put a different policy environment on to a project. It would have made some difference. There certainly would have been more emphasis on the public sector comparator. That is not to say that there was not emphasis on looking at the various ways of delivering the project right from government doing it through to the build, own, operate and transfer (BOOT) approach, but when a decision was made that was not documented — the time was not taken to document that in detail, as the

Auditor-General has pointed out. I believe that analysis was done, but it would have been done in a more systematic way and would have been documented to a greater extent.

I am not sure that the risk allocation would have changed much if you put up the same commercial and financial environment as prevailed in the early 1990s. It is a different environment now. If you were doing the project now you may have amended the risk allocation in some areas, but if you put it back into the environment of the early 1990s with the financial difficulties facing Victoria at the time, I do not believe the risk allocation was a function of the model of delivery: whether it was then IIPV, or Partnerships Victoria, it was more a function of the environment of the time. I think that during the 1990s we all learnt a lot about managing these types of projects, so hopefully we will do it more efficiently the next time around.

The CHAIRMAN — Can I ask you then your view of any significant barriers or impediments that may exist that would militate against getting successful PPP projects up in Victoria?

Dr SMITH — You are talking in general terms?

The CHAIRMAN — Just in general terms.

Dr SMITH — I have been focusing on the City Link project, so I am not perhaps the best person to ask. No, I am not aware of any.

The CHAIRMAN — I suppose we have gone through, from your point of view, what the key issues are from City Link and what lessons can be learned from there. Given that and what you have just said, your experience is very much confined to that project rather than a more general applicability?

Dr SMITH — Yes.

The CHAIRMAN — Can I ask you then through that, one area we have been looking at is the relative expertise of the public sector and the private sector to make risk assessment. What was your view of that during your project?

Dr SMITH — Again, I think City Link was a little unusual because it was the first road BOOT project in Victoria and the largest BOOT project in Victoria at the time; in fact, one of the largest in Australia. Therefore, the experience of both the government and the private sector was somewhat limited. There was obviously experience from New South Wales with a number of toll roads in Sydney and we drew on that both in terms of consultation with officers from the New South Wales government and in terms of some of the advisers we appointed. I would have thought that at the time we did it there was not a lot of difference because of the newness of that model of delivery in Victoria and in the Victorian business community.

Speaking more generally, I would have thought that was an area where the government does need to make sure it keeps adequate resources because the private sector, particularly I believe the legal firms, are very good at spreading that knowledge internally in their firms with very good training; and if you look at the ability of legal firms to deal with these types of projects now compared to nearly 10 years ago, it is fundamentally different and has drastically increased. I think your point behind that question is a very good one — that is, we have to be careful to keep the skills available to government up in that area or the private sector will have more knowledge.

The CHAIRMAN — One of the criticisms that is often levelled at the public sector is that it is risk averse and that that impacts on what it thinks up. Is that your experience?

Dr SMITH — If I could emphasise that these are very much my personal comments — I think all of my comments are but this in particular — the whole structure of working in government tends to force most bureaucrats to be risk averse — they are not rewarded for taking risks. In fact, I have jokingly said to various people in discussions about this, ‘You are half-mad managing these types of projects in government because you are always living on the knife edge and making commercial judgments as well as small political judgments and community judgments, and one day you are going to get them wrong and nobody is going to like you from that day onwards.’

I think there is an issue, a very significant issue of how you get good broad advice. One way of doing that is to employ very good consultants to advise you who are less, I suppose, constrained by the usual bureaucratic processes. Maybe older age helps you too, because you have less to lose if you make a mistake in one sense; I put myself in that group now. Certainly if you are looking at career bureaucrats or people who are looking for a career

in whatever area, you are asking them to make very difficult judgments or recommendations to ministers or to governments, and if they get it wrong there can be very adverse consequences for their career.

The CHAIRMAN — A personal view of mine is that the term ‘risk averse’ as applied to the public sector is actually a view that has developed as a modern perspective and is not necessarily correct, in that I do not think that it is essentially risk averse. I think they were operating in an environment where risk was not a high priority, so they did not need to consider risk. They were not actually being averse to it, but it was not within the parameters of their consideration.

Dr SMITH — Certainly, if you are going back 15 years ago; it is very much the case now. City Link makes many judgments. Fortunately we have managed to make the vast majority of them work where we have taken risks. You occasionally wonder why you are taking a risk, because there is a downside, and if the downside had eventuated I wonder where I might have been at this point in time — almost certainly not sitting here today.

Mr CLARK — It is often alleged that City Link gave a unjustifiably high rate of return to the private sector providers and conversely the public and motorists are paying an reasonably high price for using City Link. What do you say to that contention, both in terms of looking at cost and return ex ante and after the event or as events have unfolded; do you think that allegation is correct in either sense?

Dr SMITH — Those questions are always easier to answer with the benefit of hindsight and with the benefit of changed circumstances. If you look at the extent of the construction risk and the range of other risks that were transferred to Transurban and its consortium members, in particular the degree of tolling risk that they took, the only response that we can make is that it was bid in the market at the time and it was in response to a very competitive bidding framework that produced that risk return.

Also, remember that back in those days interest rates were higher and inflation was higher. So that if you would translate even the same project into today’s interest and inflation environment you would automatically expect a lower risk and a lower return. Also, just a greater knowledge in both government and the private sector in developing and managing these types of projects would have led to a better understanding of the risks and a better pricing of the risks. It was very much in my mind a function of the time, reflecting a trade-off then of either doing it this way or not at all for quite a number of years.

I just repeat that I believe it was a vigorous bid competition, and therefore it was what the market was requiring at that point of time. I suppose what I am saying is that the market today has a lower requirement, but that is a function of a different environment.

Mr RICH-PHILLIPS — One of the points you touched on in your presentation was the issue of succession planning when you have a long-term project. Would you outline what mechanisms are used currently with Transurban and City Link and the ways in which that can be carried across to other projects or improved — and even shorter-term projects, of 10 or 15 years? Municipal BOOT schemes are still going to have those issues.

Dr SMITH — It is a very difficult issue, succession planning, because, particularly when you have been working with a project for some time, it does not matter how good or conscientious you are about documenting things, a lot of the knowledge is in your head — all the reasons behind decisions and a lot of the negotiations and so on.

We are doing a number of things in the Office. We are developing what is called a users guide, which is trying to write down as much of the contract management and the background to various issues as we can, so that it is there. It will not be a finished project until 2034 because it is a live product and we are continually updating it. There is also the whole filing system. So there is a range of procedures you can put in place.

The next step is then to make sure that you have a range of people in the Office who, although they are employed for particular specialities and particular skill sets, have a understanding of what is happening in other areas. So that if one person does leave a range of people can help a new person in that area come up to speed and to understand the issues. The key point I think is to be able to keep not a large but a sufficient core of expertise in that group — what you call, I suppose, the senior level management group of four or five people — so if one does leave the others can help a new person. We have had on the whole an incredible stability of employment in the Authority or in the Office, but we have had staff changes and we have generally been able to get new people up to speed quite quickly because the broader framework is there.

I think the real risk for government is if three or four people who know much about a project and all but one leave at one stage, or they all leave. The gap then would be very difficult.

Mr RICH-PHILLIPS — I guess it is one thing to store that corporate knowledge in a filing cabinet in the corner, but it is quite different to actually having it in the heads of the senior management team. As you have natural attrition, from the senior management team, is that going to become more of an issue for you?

Dr SMITH — Potentially, yes, and it is very difficult to address that. We are trying to address it. As I said, the best way of addressing it is to have the changes happening gradually in a paced way. Over the next 32 years you are obviously going to have a whole lot of changes in the people leaving, but you hope that they are going to occur one or certainly no more than two at a time within a short period of each other. I have emphasised that with a central group of four or five people you still have a core of it at any one time that has that recollection and that knowledge base — and also by spreading it around the department wider a range of other people get to understand at least some aspects of City Link.

Mr RICH-PHILLIPS — Also with respect to the public sector partner, do you ensure that those relationships are maintained? I would expect there would be a higher turnover in the relevant public sector area than within your own organisation. Is it a problem maintaining that sort of parallel?

Dr SMITH — No. In fact, Transurban has also had very limited turnover of staff, but as the project has developed their organisational structures have changed and additional people have come on board; and it is very important to get close to those senior people quickly and to develop a working relationship with them so that if a problem comes up at least you can talk about it, even if you do disagree about the issue. Obviously one of the significant functions of all the key people on the government side is to keep that relationship going with their counterparts, and I am sure it is vice versa with Transurban. City Link Melbourne work at the same — keeping relationships going with the key government people, and that is not just in the Office but in the wider areas of government.

Mr RICH-PHILLIPS — Is there anything in the contract you operate under requiring a detailed documentation of the corporate knowledge? Is that something that should be a contractual requirement?

Dr SMITH — I think it is more an internal matter and therefore not appropriate for documentation between the state and the concession holder.

Mr RICH-PHILLIPS — If a private party does not do that because it is not a requirement, in 10 or 15 years you could be in a situation that is almost unworkable, due to lack of — —

You have obviously had the turnover?

Dr SMITH — I may have misunderstood your question. There is a requirement on Transurban to keep documented all the information they need to run, operate and maintain City Link. What I have been talking about is more the commercial overlay over that, and that is where there is no requirement. I suppose in one way it is addressed. There are regular monthly meetings with Transurban, and that is one way also of getting new people to increase their knowledge base very quickly — by attending these meetings where a whole range of issues are discussed. At present we have two such meetings a month: one on a more operational level, looking at the operation of the toll road, City Link and all aspects of that; then what is a higher level one, which is looking at the project in a total sense and looking at the more strategic issues.

So the first is addressing how the road operated last month; what are the likely issues to come up in the next month; what are the big events, particularly with the forthcoming Masters Games, and so on. Issues like that are being discussed often at those operational meetings. Then the strategic one is looking at the broader relationship between government and Transurban.

Mr CLARK — At a governmental level there must also be issues, such as change of ministers et cetera, particularly when unexpected. Has that impacted on City Link?

Dr SMITH — I suppose we have been fortunate in that over the full life of the project we have had only four ministers; it has been going almost a full 10 years, and that is an incredible amount of stability. So, no, it has not, but it is certainly something that could impact on it in the future. Very soon after the current government came to office it was addressing quite difficult issues on City Link.

Mr HOLDING — I would like to follow up one of the questions Mr Clark asked about the return on investment to Transurban and whether or not in hindsight you felt that all of the relevant issues had been taken into account when the original concession deed was negotiated. I wonder if you could provide the committee with your assessment as to whether or not the concession deed as it was enacted at the time and as it exists now would have passed the public interest tests or criteria which exist now in the Partnerships Victoria document? I know it is a difficult and hypothetical question, but protecting the public interest is obviously a very important part of any public–private partnership, and it would be interesting to assess a project as significant as City Link against that sort of criteria, given what has occurred since.

Dr SMITH — I emphasise that these are my personal comments. I believe it did pass those tests. They are obviously more advanced tests now than they were under the Infrastructure Investment Policy of Victoria. I think it is fair to say it is mostly a matter of political judgment in a couple of aspects of City Link. It is well known that there have been differences between the major political parties in this state on those, and we just have to accept that as a fact.

I believe overall City Link is very much in the public interest, and the documentation reflected that. I understand that either individuals or parties could have taken a different view on particular aspects, but I think they are more political decisions rather than things that are in the province of bureaucrats to negotiate. If I am being a bit obscure, what I am saying — and I think what you are getting around to and hinting at is the tolling of the existing Tullamarine and Monash freeways — is that in the end that is a matter of political decision. It is not a matter of bureaucratic judgment.

If you put that to one side, I believe the contractual arrangements protected the public interest in most ways. There are some things that we would do better if we did it again; we are fools if we do not learn from our experience. If you want to go into detail, the whole of what we call schedule 5 in City Link, which related to the community consultation on things like the noise walls and other issues during construction, was documented in a way that, sitting around a table with Transurban, we thought worked perfectly. But when we got out there in the real world we found the contractors had very limited experience in communicating with the public in that environment, particularly in an environment where time was money with a BOOT project; and just as significantly the community had very little experience in being consulted in that environment.

An engineer can put a technical drawing in front of a member of the public, or me for that matter, and we may say that looks okay, but then when a 6 metre noise wall goes up somewhere the members of the public did not see that in the drawing but the engineers did. I think we should hasten to add that on the Western Link that was a difficulty; it is an area where the Melbourne City Link Authority took an active role once the problem was identified, and we learnt; and the experience on the Southern Link, which happened some 6 to 12 months later, was a much more structured and informed process because everybody had learnt from the Western Link experience, and hopefully now we would have much better ways of doing it.

For example, one of the things the authority did was engage a member of staff for 12 months whose sole role was to communicate with the affected members of the public — to go out and sit at their kitchen table and explain what an engineering drawing meant, try to get them to visualise what was meant, and bring the concerns back so we could understand those concerns and then try to have them addressed to the best of our ability.

Mr THEOPHANOUS — I shall ask you the question that I also asked the previous witness. Do you make a distinction between a project being in the best interests of the government and a project being in the best interests of the public?

Dr SMITH — Generally, no; in fact, very rarely would I make that distinction.

Mr THEOPHANOUS — So if the City Link deal was good for the government would it automatically have to be good for the public?

Dr SMITH — I would view that the government was representing the public in negotiating that deal and therefore I would be looking at a deal that was generally good for the public in some definition of that phrase. I think different people may have different views on what that phrase would mean. If there is an issue of good for the government, I am not sure what that means from my perspective.

Mr THEOPHANOUS — Let us say it was a deal which reduced government debt. Certainly the electricity industry would fall into that category, but even City Link would in the sense that a considerable amount of government debt would have been generated to build it using the public purse. So you could argue that it was in

the interests of the government to have it dealt with in the private sector, but it might not be in the interests of consumers, or of commuters in this case. Do you make that distinction?

Dr SMITH — I think you are looking there at different financing aspects. If you go back to the early 1990s with Loan Council requirements et cetera it was unlikely that the government would have been able to borrow the funds that were needed to build the City Link. So the issue that was being addressed was whether City Link should go ahead as a BOOT project or whether it should be deferred for a number of years until all the loan pressures had been reduced and it could have been funded by government borrowings.

I believe the congestion was such that the removal of the congestion — and the benefit cost analysis we had done with Allen Consulting Group Pty Ltd confirmed this — was a strong benefit from doing City Link when it was done, and delaying that would actually remove the community benefit. There is no doubt that with tolls, individual users, particularly users of the Link, are paying for the infrastructure. That is a political debate. I can make the observation that presumably a lot of members, a lot of country people are quite happy with that arrangement because they pay for it only when they use it. You could argue there are equity issues around metropolitan Melbourne, but again that is a political decision, not one that is appropriate for a bureaucrat to pass judgment on.

Mr HOLDING — Do you not assess that as part of the process when you look at the project in terms of establishing whether or not it is in the public interest? Would you simply say, ‘That is a political decision’?

Dr SMITH — It is an issue identified, but it is addressed by a political decision.

Mr THEOPHANOUS — There are certainly issues of equity in the metropolitan region about the fact that the Eastern Freeway is government funded and people who live in that corridor do not pay a toll, whereas the other one is not government funded and people in that corridor do pay a toll. Can you see the inequity issues there?

Dr SMITH — Yes. There is an inequity issue there, yes. The point — and it is far from a perfect answer — is that those people do have an alternative route, but the alternative routes are not necessarily that attractive, depending on where they are going. Sometimes the alternative routes are quite viable alternatives.

Mr THEOPHANOUS — That is what I am getting at. Even if you agree to a user-pays principle there would be an issue about whether you apply user pays more universally than what is current, or more equitably I guess. Is that correct?

Dr SMITH — There is an issue, but the answer to that question specifically is yes. But you could put it into a broader question. There is the whole issue of how do road users pay for services they consume. At the moment it is mainly done through taxes on petrol and a whole range of other charges. There is a whole economic debate about whether they are an efficient and equitable way of allocating charging for those uses or not. You can envisage alternative ways of charging.

Mr THEOPHANOUS — There were some figures I saw that suggested City Link would repay its construction costs within 12 to 14 years and essentially that meant about 20 years of ongoing impost on the Victorian motorist, which would be paid for by consumers at an ever-increasing price of tolls on City Link. Are those figures in the ballpark?

Dr SMITH — I have two comments. The real toll price is prescribed in the concession deed, so the tolls can only increase in line with inflation or by a formula. In the first period it can be by inflation or a formula that is set out, so Transurban does not have an unfettered ability to increase tolls. Secondly, the detailed financial models have been thoroughly looked at, and I think what you are saying is that there is a return to equity over the life of the project.

Mr THEOPHANOUS — What I am saying is not only is there a return but that return far exceeds what would have been the cost to the taxpayer of a taxpayer-funded model.

Dr SMITH — No, that is quite a different question. There are two issues. There is an issue that you can pay back construction if somebody will lend you the money at no interest rate or you somehow had the money and you could do that obviously in a much shorter period. I have not done the calculations but the time period you said could be quite reasonable for that. But if somebody had given you the money at no interest for that period, if they then charged you interest and then wanted something for the risk they took, then it takes a longer period to go back. I reiterate that not only did we in assessing the bids analyse those financial projections, but we also built in a number of safeguards in case those projections were wrong and their returns were higher.

As most of you would be aware, there is a revenue sharing. If revenue is higher than projected that is done depending on how much higher it is — a matrix is set out in the concession deed to generate the revenue sharing. If by some circumstance that says it is particularly successful, the concession terminates early — it does not go for its full length. So there are mechanisms built in to protect the public's interests in those circumstances, but that is not to go back on the point that I think you are making — that when a private sector puts equity in a project like this they expect a return on it, and that is beyond the construction costs. Where the construction costs are the same, if the government had done it or it was done in a BOOT project, it is a fairly complicated issue about relative efficiencies and relative timeliness and tax concessions, and there is a whole range of factors that affect that. It is not a simple analysis. A lot of those analyses are simply done by taking the construction cost and using that, but it is much more complicated than that.

Mr HOLDING — On the revenue sharing arrangement, does that mean that the toll could be reduced to that extent, or is that an option between government and Transurban?

Dr SMITH — What it means as written is if revenue sharing did occur the money would come to government. It would be a matter for the government of the day whether it would be able to negotiate with Transurban to reduce tolls.

Mr HOLDING — Is that further referring to Mr Theophanous's points about the difference between the government's interests and the public interest? The government may very much appreciate that revenue stream, but it is motorists who are paying for it.

Dr SMITH — That depends on the view of the government on whether City Link is a taxing mechanism or not. I think it is on the public record to say that the view of the government of the day when the contract was negotiated was that it was not a tax on motorists, and the financial arrangements reflected that. I think the reason it is not dealt with in the concession deed is because, (a), it is not the most likely event, and (b), it would depend on how much money is coming back, which is also a function of how long you are in the concession.

Mr THEOPHANOUS — I make the comment that you would have a lot of trouble convincing somebody in 25 years time who was paying \$50 to go through an ageing City Link system that it was a good deal 25 years early to not have had it built by the government.

Dr SMITH — That is a political judgment. The only comment I make about ageing infrastructure is that Transurban has an obligation to keep their road and the technology up to date. That is not to say that a bridge or tunnel built 25 years earlier is likely to be the same. Even if it is maintained to the highest possible standards it is not the same as a new bridge or tunnel.

The CHAIRMAN — If I may ask a concluding question that may seem to flow from that discussion, but it is meant as a more general question? Do you have a view on how potential windfalls should be dealt with within public-private partnership arrangements?

Dr SMITH — It is best if they can be documented in some way, and I think we have done and attempted to do that at City Link, and there was an earlier attempt.

The CHAIRMAN — I did not necessarily mean to particularise that.

Dr SMITH — I understand the breadth of your question. I think it is essential that the windfalls are dealt with, because it is not sustainable if there is a negative windfall — in other words, if the operator or the decision-holder is losing money they are not going to put, or at least they are going to economise on effort if not on other things; if there is a windfall to the operator at the expense of the users that is unsustainable from a broader public policy perspective. It is essential that windfalls are dealt with in some way. That would vary from project to project, and would depend on where the funding source is coming from. I think what Mr Theophanous was probing, and rightly so, is where that is coming from the public as a direct charge there is a particular sensitivity if the operator is judged to be making an excessive profit.

The CHAIRMAN — I was actually coming from a different direction. The Auditor-General in England, for example, has reported that in a number of projects there a quick windfall was obtained by almost immediate refinancing after the contracts were signed, and there have been no provisions about windfall. He made those comments about it, and I was very much asking about it in a more general sense.

Dr SMITH — And it is important that they are dealt with in some way. In fact, I think we need to develop a general mechanism that picks them up somehow. That may be quite difficult to negotiate, and I am sure it is an area for Treasury. It is an area we have put our minds to in various instances with some of the changes that have come along to make sure that where possible, and I think in all cases, the windfall has been kept. If there is one it has been identified and allocated, if it happens, or shared in some way. Again it is often a matter of judgment. Some of the windfalls are large and immediate; others are much less large and less clearly identifiable.

The CHAIRMAN — Thank you for your attendance this afternoon. If there are any matters that the committee may wish to follow up, it will do so with you.

Dr SMITH — Most certainly if there are any matters to be followed up, please contact me or Ms Baker.

Witnesses withdrew.

CORRECTED VERSION

PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

Private sector investment in public infrastructure subcommittee

Inquiry into private sector investment in public infrastructure

Melbourne – 20 August 2002

Members

Mr R. W. Clark

Ms S. M. Davies

Mr T. J. Holding

Mr P. J. Loney

Mr G. K. Rich-Phillips

Mr T. C. Theophanous

Chairman: Mr P. J. Loney

Staff

Executive Officer: Ms M. Cornwell

Research Officer: Ms C. Williams

Witness

Ms C. Hilder, Director, Policy, Australian Council for Infrastructure Development.

The CHAIRMAN — I welcome Ms Cecilia Hilder, director of policy, Australian Council for Infrastructure Development, to this public hearing on private sector investment in public infrastructure.

All evidence taken by this subcommittee is taken under the provisions of the Parliamentary Committees Act and is protected from judicial review. However, any comments made outside the precincts of this hearing are not protected by parliamentary privilege. All evidence given today is being recorded by Hansard. As a witness you will be provided with a proof version of the transcript early next week.

Ms Hilder, would you care to make an opening statement to the committee before going to questions?

Ms HILDER — Certainly. My opening statement is that my laptop is not working, so copies of the slides I will be referring to will be distributed. I have chosen to give a presentation today and basically what I have done is address the terms of reference that were originally set out. As I understand it my task here is to really summarise the submission that AusCID made back in April, so I have undertaken to do that.

I first wanted to make sure that the committee knew a little bit about AusCID. I also wanted to make the point that infrastructure matters. Sometimes in the debate about procurement methods the issue of infrastructure and service provision to the community gets a little bit lost, and it is important to note the importance of infrastructure to the community. I also want to talk about public–private partnerships (PPPs), which AusCID supports as one method of procurement of infrastructure for the community. Finally, I want to go through the eight terms of reference that the committee has.

Who is AusCID? We are the principal industry association for private investment in Australian infrastructure. We have about 100 members at this stage representing about \$60 billion of infrastructure assets and we have been in operation since 1992, so we are 10 years young. If anybody is interested in a list of our membership it is contained in our submission and I have brought copies of it for you today.

Our membership comes from a range of organisations, including banking and finance, construction and other advisory firms. I would like to give a quote about the importance of infrastructure to the community from the 2001 Australian Infrastructure Report Card:

Infrastructure is vital to the Australian economy. It underpins the delivery of essential services and drives economic growth. Given that Australia's infrastructure affects every Australian every day, it is of paramount importance that it meet today's needs and through careful planning, maintenance and construction, tomorrow's needs as well.

At the end of last year AusCID commissioned some research about public–private partnerships and their acceptance within the community, and in order to do that it was appropriate to give a definition of public–private partnerships. I think this committee heard this definition back in April, but allow me to give it to you again so we know what we are talking about and so we are really clear about what a PPP is, because there has been some misunderstanding in the community, particularly of late:

A public–private partnership or PPP involves government and private sectors working together to deliver infrastructure or services that are traditionally provided by government. It often involves private financing, construction and management, with the government approving and then supervising the project.

The key point I would like to make is the last part of the quote:

Unlike privatisations, PPPs usually involve the provision of a new service or facility.

That is an important distinction that needs to be made. Why PPPs? The following is an extract from our submission:

The best reason for procuring infrastructure services through PPPs is that they can deliver value for money benefits. Value for money means much more than merely obtaining infrastructure services at the lowest cost. It also includes quality of customer service, ability and need to adapt dynamically to changing consumer demands and consideration of economic and social impacts.

It is important to note that value for money is not simply about economics.

I have listed some benefits of PPPs. I think this committee has been exposed to those on a prior occasion and they are certainly detailed at length in our submission. They involve reduced risk and allocation of risk; earlier project delivery, which is one of the really good benefits that PPPs can bring — and you may already have some examples of that here in Victoria; increased efficiency; a customer focus — the community and customers are something that matter to me a great deal, and for the private sector to encourage people to come back it has to make sure that its

service is right; and finally, a whole-of-life approach. An important attribute that the PPP process brings to infrastructure procurement is looking at the overall cost over a long period of maintenance of a facility. That is really important.

I wanted to point out a couple of quotes regarding traditional procurement methods and public sector delivery. There has been a propensity of late to hear a great deal about problems with privately procured infrastructure, but it is important to remember that things have not always gone to plan in public procurement either.

I refer the committee to a quote, which I know it has seen before, from the UK National Audit Office which states that in the UK, 73 per cent of UK projects are delivered over budget — this is under traditional procurement — and 70 per cent of UK projects are delivered late.

More recently an article has been published in the Journal of the American Planning Association, which was only published last month. It was a research project that looked at something like 258 traditional public works projects, and the findings are quite interesting. It is estimated that between 1910 and 1998 project estimates were short of the final costs on average 28 per cent. The biggest errors were in rail, which ran on average 45 per cent over estimated costs. Bridges and tunnels were 34 per cent over, and roads 20 per cent. If anyone wants a copy of that let me know. Are there any questions?

The CHAIRMAN — There will be. We will wait until the end of your presentation.

Ms HILDER — I have a slide noting that PPPs are not peculiar to the UK or Victoria. I think those are the jurisdictions about which we hear the most, but it is worth recognising that they are in around 140 countries. There have been over 450 projects in the UK. I have popped Ireland in because I think Ireland has done something that is quite good, and that is to engage and educate the community about public–private partnerships and the way in which that procurement method operates. On its web site it has a tag line saying something along the lines, ‘Your plan, your future’, and I think that community involvement is something from which we could learn.

Is there a downside? Of course nothing is perfect. Yes, the transaction costs in public–private partnerships are quite significant. Over time — and I will discuss this a little later — it is foreseeable, and certainly this has occurred in the UK, that the transaction costs with experience and with practice have been able to be reduced, and this is particularly important for smaller projects. It would be remiss not to address the fact that there has been some inappropriate risk allocation. We have recently seen some examples of that. It is important to get that right.

I will not go through the terms of reference one by one but I have listed them initially for the committee. The first one, and a way in which AusCID could be of particular use to this committee, is its database of major infrastructure projects. That was compiled last year by AusCID. It looked at PPPs and privatisation projects across 14 infrastructure sectors. As of late last year, there were 209 signed projects — there have been a few more since then — with a total cost of \$71 billion. Of those 209, only 32 of them are privatisations.

It is interesting to look at Victoria because Victoria is clearly the dominant jurisdiction. Victoria accounts for nearly a third of the total number of projects, and by value that is around 56 per cent of all projects. There are 49 infrastructure PPPs in Victoria, which is about 28 per cent of the Australian total, and the total value of Victorian PPPs is around \$10 billion. They are big figures.

I will not go into depth with the Melbourne City Link example in addressing the issue about the community. I cite that example under the topic of community because I think it is a project that has had a direct impact — and I would suggest a positive one — on the community. A significant risk was transferred and accepted by the private sector, and when things did not go quite right that was settled in the vicinity of \$200 to \$300 million by the private sector rather than by the taxpayer.

There are some issues about legislative and policy frameworks. I quote from the AusCID submission:

The current challenge in Victoria is execution in adherence with the policy ... the private sector needs to have confidence that the PPP guidelines are being observed when projects are ‘in the trenches’.

I suggest the policy that we have in Partnerships Victoria is quite a good one and one that AusCID supportS. It is important that it is adhered to when projects are coming online. Implementation is the challenge.

On the issue of government models I have made two points. AusCID supports the important ongoing role of the Auditor-General in contract oversight and reviewing the value-for-money test. There have been some suggestions recently that it is a little strange that the Auditor-General might look at say the Spencer Street station deal. That is

part of the policy; that is something we would support; that is something our members would support. Those transparency and accountability measures are important to investors. It gives them certainty; that is what they like.

The second point on government models that I have popped in there is the importance of having well-trained and experienced public sector staff. Partnerships need to be equal, or as equal as they can be. In training the public sector, I think this government has already done so and is working on that issue. The importance of that cannot be underestimated.

Again on the issue of transparency — and a point I guess I have already made — when you are talking about accountability for investors, investors require and prefer certainty. Therefore government efforts to protect the public interest through greater transparency is supported by private sector investors. Sometimes when the private sector is involved there is a temptation to think that things are done behind closed doors, and so forth. I do not think that is the case. In fact I know it is not. As I said, we would support accountability and transparency.

In looking at evaluating the private sector — and I have gone into this in more detail in the submission — it is a little early to do that under the new method of Partnerships Victoria. When comparisons are made, they need to take account of the full and true cost of public sector delivery. You have to compare apples with apples; realistically value cost and time overruns under public sector delivery when you are comparing public and private sectors; and there needs to be value in a monetary sense in valuing the monetary risk passed on to the private sector. It needs to be a real comparison in that regard.

Risk allocation — and I am sure you have heard a great deal about risk allocation — again the principles remain the same. It should be allocated to the party best able to manage or deal with it. When a risk is shared — and I think this is really important — a true partnerships approach should be adopted. This is particularly the case in long-term partnerships.

Finally, transferring risk to the private sector for the sake of it should not be undertaken. There needs to be careful consideration up front of degree and types of risks. It is not just a matter of foisting it all on one side.

Under the issue of other relevant matters, I have already spoken about transaction costs but I will speak about it again, because it is important to the private sector. With some of the projects that have been put forward of late there has been concern from the industry about the high level of transaction costs, to the point where it may be difficult for some players to be involved if we do not work towards minimising those costs. It also, as I said earlier, has the potential — and I guess has already to some extent — to preclude some smaller projects.

I have listed some ways to do that. Standard contracts — with more experience we can develop standard contracts, and that would cut down some of the costs. Other simple and logical things include more efficient project and contract administration. Another is that governments need to be clear about what they want. That is very important. Governments also need to adhere to tendering time lines. Failure to do that can really blow things out significantly, so they are all things to work towards.

A couple of other points I have included are more federal in nature but impact on the states, including federal tax issues. I am sure you have heard about section 51AD and division 16D before. We are assured that there will be remedies to that in the not-too-distant future, but for some time now those tax arrangements have been a disincentive to private sector investment, which in turn affects state procurement.

Just as a point to think about more than anything, I mention a national infrastructure strategy. While states are these days predominantly responsible for procuring schools, hospitals, roads and so forth, we do have roads that go over state boundaries, we do have gas pipelines that go over state boundaries, we have railways with different gauges that go over state boundaries. In our country with a large landmass and a small population it is important that we get it right.

Two final quotes — I said to somebody last week that I am a bit of a quote boffin, so bear with me. This is from a Pricewaterhousecoopers report that was given last year and I think it has some relevance to us in Victoria, particularly in the context of recent debates here:

Public comment on PPPs is poorly informed and, in some cases, misleading. The overall impression created in the media is negative — that PPPs are worse than what they have replaced, and are responsible for many current problems in the delivery of public services. Most of their impressions are inferences and are contradicted by what users say about their projects.

The final slide is really to make the point that PPPs are about choice. PPPs are not the silver bullet, they are not *the* answer. The aim is not to have everything privately procured. I would suggest that PPPs are one answer for some provision of infrastructure in Australia. The question is:

Is the community better off with the service delivered under a PPP or by traditional means?

This does not preclude traditional means in any way. It is a truth, not the truth.

The CHAIRMAN — Perhaps if I can just go to a few things that occurred to me on the way through: on page 9, the government models, where you are saying the Australian Council for Infrastructure Development (AusCID) supports the important ongoing role of the Auditor-General, can I ask you at what point you believe the Auditor-General should be involved? Given that the practice for the Auditor-General here is different to the practice in, say, the United Kingdom where the National Audit Office participates very early on in the process and actually makes a judgment about whether it is delivering value or not, what is your view of the appropriate point at which the Auditor-General should become involved?

Ms HILDER — Some of this is also about looking forward because we really only have recently had Spencer Street announced and we have some more projects to come. I guess in terms of looking forward we need to see how that process pans out. I think the Auditor-General's report on Spencer Street station during November will be a good starting benchmark to see what Australia needs. I am often very wary, particularly because we are in a federation, of comparing the United Kingdom with Australia; I think it is sometimes a bit of an apples and oranges thing. My response to that would be, I think, adherence to the policy as we have it in the first case, and secondly to assess it as we go. It is to some degree a work in progress.

The CHAIRMAN — You don't think there should be an early role of assessing whether the value for money component was in fact evidenced if you like, was properly conducted at that point, and making a judgment? I will give you an example: while I was there the Audit Office reported to me on one particular project which was a £75 million project, a considerable project. They reported that when they looked at the value-for-money component, the public comparator component, it was reported to them that there had been a public benefit. They asked to see that assessment. The assessment was that the public benefit was £100 000 in a £75 million project.

Ms HILDER — I take your point.

The CHAIRMAN — But it then went further, that they had not factored into their calculations the cost of the people that the public sector used to do the evaluations and the work on the project, so even the £100 000 was debatable. That is why I am asking what is your view of the point at which those sorts of things should become involved. There they have an up-front role: they actually do some evaluations prior to contract letting. Here it is very much post.

Ms HILDER — Again we may have to see how it goes. Getting back to your point about factoring in the cost of people to do the PSC, again I made the point about evaluating the private sector. I think in terms of spending taxpayers' money it will be terrific when we get to the point where as a matter of course the public sector factors in those kinds of costs because then that is a true reflection of the real cost of doing these things and the infrastructure delivery, whether you do it traditionally or not. However, I think we will have to see how we go with examples at the moment to see at what point the Auditor-General assesses the PSC, for example.

The CHAIRMAN — Again under the broad issue of government models, does AusCID have a view regarding how the traditional, if you like, ministerial responsibility under a Westminster system can be protected with the contractual arrangements for PPPs?

Ms HILDER — When we talk about risk allocation there are certain things that governments should do. I think this is in many ways the essence of PPPs. It is about letting governments do what they do best so that you put in place all of the other things that the private sector does right, whether it be construction, financing — all of those sorts of things. In terms of the formal Westminster aspects, I think they are protected. I do not see how there is any —

The CHAIRMAN — I was thinking more of the ability of a responsible minister, for example, to stand up in the house and respond fully and appropriately to questions about arrangements which may be precluded under contractual arrangements at the moment.

Ms HILDER — I do not think that is the usual practice, particularly these days with the contracts being on the web; anything — I believe it is over \$10 million — has to go public. This committee did a report on

commercial in confidence which I read with great interest. We have learnt a lot about those kinds of accountability measures and I am reasonably comfortable at this stage. I think it is a work in progress and I think it is also something that we have to watch very carefully but I am not so sure that ministers are particularly precluded or restricted in their actions.

The CHAIRMAN — It is an interesting one. The Canadians are actually requiring that it be written into arrangements exactly how ministerial accountability will be ensured within the arrangements.

You talked about transaction costs. Do you have a view, firstly, of threshold, whether the \$10 million threshold is the appropriate threshold? We have received some submissions saying they believe that is too low, that a more appropriate threshold might be in the area of \$100 million, given bid costs.

Ms HILDER — I would actually over time like to see potentially a lower threshold. It may be that the Australian market is significantly smaller than, say, the United Kingdom, so it may be that the volume of projects needed in order to improve those transaction costs for the things I spoke about — standardised contracts and processes — is less. It would be terrific if we could get down to the lower levels of \$2 million or \$3 million. I think it is about doing it smarter, not necessarily setting arbitrary thresholds.

The CHAIRMAN — Just to follow that through, are you saying that some of the big costs currently being incurred by the private sector are not necessary to be incurred?

Ms HILDER — I would not say that they are not necessary at the moment. I think at the moment, in the early stages of this, there are some challenges that need to be worked through, but over time we will get better at it. I would not say that they are not necessary at the moment.

The CHAIRMAN — Just following that through, some of our previous evidence has referred to the United Kingdom using a process called best and final offer (BAFO); are you aware of that?

Ms HILDER — I am aware of it but it is not something about which I know a great deal.

The CHAIRMAN — I was going to ask you whether you had a view on whether that sort of process can reduce transaction costs?

Ms HILDER — I could not offer you a view on that at the moment. I can certainly get back to you.

The CHAIRMAN — You comment that ‘public comment on PPPs is poorly informed’. Do you have a view on why is that is so?

Ms HILDER — My view is that this is hard stuff, to be honest. We are dealing with major projects. This is complicated financing; this is tricky stuff if you start throwing around phrases like PSC, whole-of-life costing, BAFOs, BOOTs, all sorts of things. I think that for us as a organisation to some extent, government and the private sector themselves really need to work at the communications challenge. I cited the Irish example because the Irish seem to be having success in getting the message through. For me personally I like that challenge. I think it is important that the public are informed and we find ways to speak to people so that they can identify with how it is that their roads, bridges, gas pipelines and so forth are being built. I think that is an important challenge and one that needs to be met head on.

Mr CLARK — First of all, I think the committee would value a copy of that costing of public works document that you referred to during the course of your presentation.

Ms HILDER — Sure.

Mr CLARK — Secondly, in relation to the cost of capital, there has been a lot of debate about what sort of premium is paid for capital under a PPP type of project. From your experience, are you able to give any ballpark indication to the committee of the magnitude of that premium compared with a pure public sector borrowing rate, and what does the public sector get in exchange for paying that premium on the cost of capital?

Ms HILDER — I think you were present at the national infrastructure summit last week, where this was raised. I have actually addressed the issue. I did not address it today. The cost of funds, the cost of borrowing is something that is quite complicated and something that people seem to get wrong a lot of the time. The best way to describe it, I guess, is when the private sector looks at the risks of a project and getting financing for that project, the cost of capital is based on that individual project. When the government tries to procure something, its risk is

not based on the individual project; it is based on its overall access to capital. I think that that distinction is where the problem arises.

If you actually take out that difference, when you look at the efficiencies that are gained through PPPs, Andersen reported — I should not say their name, should I? — something like 17 per cent differences, I think, you can get down. Again, that is part of the communications challenges, to actually point out that the cost of capital, the difference between public and private, is not so great and the efficiencies that can be gained from the private sector can make moves in the right direction for taxpayer value.

Mr RICH-PHILLIPS — Would you say that the reality of the cost of capital is the same, given the risk is same on an identical project?

Ms HILDER — I think it has to be done on a project-by-project basis. I don't think you can ever say it is 'the same'.

Mr RICH-PHILLIPS — But on a given project, whether it is government financed or private sector financed, the cost of capital would be the same because it is the same risk profile?

Ms HILDER — There may be a slight difference, but again the efficiencies that can be gained, quite often — depending again on the project — can make up that difference.

Mr RICH-PHILLIPS — On page 9 of your slides there is a quote from your submission:

The current challenge in Victoria is adherence with the policy ... the private sector needs to have confidence that the PPP guidelines are being observed when projects are 'in the trenches'.

What prompted that? Is there a belief in the marketplace among the private sector that these guidelines are being prepared but in reality are not being adhered to?

Ms HILDER — I think it is just a recognition that there is a difference. AusCID recognises that there is a difference between written policy and implementation — and keep in mind that was a quote from back in April, before we really started to have many projects in the pipeline. So I think it is more just a recognition that from previous experience in other places this has the potential to happen, but I do not think it is — at that point certainly, when that was written — quite so applicable, given the time lines: it is now four or five months on. But certainly it needs to be recognised and understood that it can be a problem.

Mr RICH-PHILLIPS — Have there been any examples brought to AusCID's attention with particular government agencies or areas where the public sector needs to improve its understanding of implementing the policy?

Ms HILDER — I think Treasurer Brumby at the national infrastructure summit last week made a couple of comments that I can get to you that were in a media release that recognised that there are a couple of items that need to be addressed, particularly in relation to big costs and a couple of other things.

Mr RICH-PHILLIPS — It is more a Treasury end of the process?

Ms HILDER — Yes.

Mr RICH-PHILLIPS — Have you had any feel yet through your client members on particular agencies at the operational level, rather than at the Treasury level? Is it a policy that is recognised and accepted among the government departments, as distinct from Treasury?

Ms HILDER — A very important part of getting PPPs up and running is a whole-of-government approach. I am not sure that in Victoria we have that yet. I do not have examples of it being a problem per se, but I do not have examples of a whole-of-government approach, equally — I hope I am not being too contradictory — but I think that is something we do need to work on.

The CHAIRMAN — There was one issue I was going to pick up with you on the way through, talking about risk transference acceptance. You mentioned the Burnley Tunnel and so on. I put the proposition that construction risk is one of the easier ones to identify and allocate but some of the other risks are much more difficult. What is your experience with the identification and allocation of risk in other areas? If you take for example the Sydney airport rail link, the allocation of patronage was risk there — the way in which that was seen to

be not all that clever. What is your experience with the ability of the public sector and the private sector to correctly identify and allocate risk — leaving aside construction, which I think is relatively easy, in that sense?

Ms HILDER — A couple of points. I think one of the benefits of PPPs is a focus on risk — it really turns the mind to the things that can go right or wrong with a project and I think that, particularly with major projects, over a long time, involving a lot of money, is always a good thing — to know what might go wrong is a benefit. I cited something like 209 signed projects. I would suggest overall we have not done too badly. Those projects on which risk has not been allocated or based have sometimes been worn by the private sector, so that has no call on the taxpayer. There are examples from overseas: I think there is a national laboratory in the UK; the company involved in that has gone down to the tune of £68 million, which would otherwise be worn by the taxpayer.

The CHAIRMAN — That is right. There are various examples where you can say that the incorrect identification of risks has led to a cost against one or the other party. Without going into that we seem to be reasonably well off in identifying construction risk and allocating that, and practice here and elsewhere would suggest that that is being done quite well.

In your submission you say that you believe that project briefs should be done on an outcome basis rather than an output basis. If you are actually going to do them on outcome, I would think you would have to become pretty sophisticated in your risk assessment of a whole range of risks.

Ms HILDER — Yes, and I think again the more you do the better you get at it, and we are getting better. Again, if you look back at public sector procurement, at some examples, we have not always got that right.

The CHAIRMAN — Not necessarily now, but would you be in a position to give the committee a bit of an example of what you would consider to be a output-based PPP that may have left risk or whatever inadequate and how that may have been treated if it had been outcome based? How would you do that differently as a outcome-based PPP?

Ms HILDER — Sure, I will do up a little thing for you.

The CHAIRMAN — I think that would be useful, if you would not mind.

Ms HILDER — That is not a worry.

Mr RICH-PHILLIPS — The committee heard evidence earlier that suggested that the specifications for public-private partnership projects should be tighter and that if they were tighter it would allow potential tenderers to submit tenders to best and final offer stage and therefore reduce tender costs to those individual firms. That would seem to be inconsistent with having an outcome rather than output approach. Do you see a trade-off there?

Ms HILDER — I think it is not so much a trade-off as getting the balance right. I think it is difficult because I have argued that the government needs to be clear on what it wants in order to reduce transaction costs, but equally if the government is too prescriptive it stifles innovation, and one of the greatest benefits of PPPs is the private sector's ability to be innovative in its solutions for major projects. So it is about balance, and that is a tricky line to get at times.

The CHAIRMAN — Thank you, Ms Hilder, for your attendance today at this hearing and for your submission previously. The committee would be grateful if it could in future come back to you about the issues or whatever that are raised during the course of this inquiry.

Committee adjourned.