Public Infrastructure Bulletin

Volume 1 | Issue 8 Article 12

8-1-2012

PPP: The best option for Queensland social infrastructure?

Norm Jagger
Bond University

Follow this and additional works at: http://epublications.bond.edu.au/pib

Part of the Architecture Commons, and the Business Commons

Recommended Citation
Jagger, Norm (2012) "PPP: The best option for Queensland social infrastructure?," *Public Infrastructure Bulletin*: Vol. 1: Iss. 8, Article 12.
Available at: http://epublications.bond.edu.au/pib/vol1/iss8/12

This Journal Article is brought to you by the Institute of Sustainable Development and Architecture at ePublications@bond. It has been accepted for inclusion in Public Infrastructure Bulletin by an authorized administrator of ePublications@bond. For more information, please contact Bond University's Repository Coordinator.

PPP: THE BEST OPTION FOR QUEENSLAND SOCIAL INFRASTRUCTURE?

NORM JAGGER

INTRODUCTION

The trend by governments to procure infrastructure using Private Sector Financing Initiatives (PFIs) has produced a number of variants such as Alliance Contracting and Public Private Partnerships (PPPs) which are now in common use in Australia. The partnership trend has developed due to unprecedented and extraordinary demands on public funding to upgrade existing infrastructure and to provide new infrastructure. Initially social infrastructure did not appear to be a good PFI prospect primarily because Governments found it unpalatable to shift costs to users.

Recently however, social infrastructure has become more attractive due to cost reductions brought about by risk transfer and whole-of-life value management. There has been a shift towards the use of PPPs to deliver hospitals, schools and prisons.

In May 2005, after four years of deliberation, the Queensland Government took its first PFI steps procuring the $240m Southbank Education and Training Precinct (SETP) as a PPP.

This drawn out process was perceived to be linked to the Queensland Government's reluctance to engage with PPPs. In 10 years of decision making only two projects, the SETP and the Queensland Schools Project (QSP) have reached completion. Both are social infrastructure projects from the education sector.

THE CASE FOR PPPS

As a general rule, the PPP is based on value for money (VFM) principles but it is the element of partnership that makes it attractive to government. A partner to whom whole or partial risk can be transferred and who can share the lifecycle cost burden can bring about considerable cost reductions. When these savings are applied to the infrastructure spending of some government agencies it can represent a very significant cost reduction. The PPP principles however need to be tested to ensure that it is the right vehicle for the project.

It is clear from these principles that the evaluation of a PPP's potential VFM is complex and must address a range of values, not just cost.

The business case for social infrastructure procurement is dependent on the public purse and public value must be evidenced and fully understood. Tinsley and Block (Infrastructure 2008 – Minter Ellison) conclude that PPPs provide an excellent model for effective funding of infrastructure projects, harnessing the efficiency

PRINCIPLES THAT TEST THE SUITABILITY OF THE PPP AS A PROCUREMENT VEHICLE	
Value for money	Not necessarily cheap but able to deliver to a better standard and at a better price than by traditional means.
Risk transfer.	Transferred to the party best placed to deal with it. Not an opportunity to shed responsibility but to engage risk management in a more cost effective manner
Equitable cost sharing	Engages a payment stream where contributions can be made by generations of users over time
Maximising returns from users	Primary users pay charges rather than the cost burden resting on the tax payer
Built and operated according to standards and KPIs	These are enshrined contractually and are enforceable
Innovative design and practice	Moves away from traditional design and traditional practice by supporting cultural reformation and the need to embrace global and technological advancement

Published by ePublications@bond, 2012

and resources of the private sector to achieve quality public policy outcomes.

Speaking at the Alliance Contracting Summit (Melbourne, November 2008) a Victorian Treasury representative made it clear that private sector partners bring improved value outcomes by adding creativity and innovation, financial cost disciplines, timeline discipline and focussed and active risk management. The Treasury review of the reports below substantiate this claim.

Overwhelmingly the PPP is shown to consistently provide value for money outcomes which are readily evident and quantifiable.

THE QUEENSLAND CONTEXT

The driver for social infrastructure is community demand for essential government services.

There are those who argue the case for all public infrastructure to be taxpayer funded. Equally the argument put by treasuries is that where infrastructure provides a greater economic benefit to some community sectors, then a user contribution should be expected.

Governments and bureaucrats are the final arbiters on the balance between these points of view, and as has been the case on numerous occasions public users will vote with their feet. The cost of getting it wrong can be disastrous.

In contrast to the Victorian experience, the Queensland Government has been remarkably reluctant to establish the PPP vehicle. While several projects have been mooted since 2004, most have failed to meet expectations at the business case stage. Only recently commissioned into their operational phases, Queensland's first two PPPs, the SETP and the QSP, have limited evaluation data available.

Each project had a very different outcome to achieve thereby making interesting comparisons between their key features:

A key feature of the QSP was to demonstrate that its innovative funding solution, the Supported Debt Model, could achieve significant value for money through lower financing costs.

The South East Queensland Regional Plan 2009 - 2031 describes social infrastructure as 'community facilities, services and networks which help individuals, families, groups and communities meet their social needs, maximise their potential for development, and enhance community wellbeing.'

EXAMPLES INCLUDE:

- Universal facilities and services such as education, training and health
- Lifecycle-targeted facilities and services, such as those for children, young people and older people
- Specialised facilities and services for groups such as families, people with a disability and Indigenous and culturally diverse peoples.

VICTORIAN TREASURY REVIEW OF REPORTS

REPORT	FINDINGS
Allen's Consulting and Melbourne University, Nov 2007	• 21 PPPs and 33 traditional projects reviewed • Found that PPPs deliver superior cost and time certainty compared to traditional projects
NSW Auditor Performance Audit, March 2006	• The first and second NSW Schools PFPs provided savings of approx 7 per cent and 23 per cent respectively against the Public Sector Comparator
Peter Fitzgerald, 'Review of Partnerships Victoria provided Infrastructure' January 2004	• For the 8 projects reviewed, 'the the weighted average savings was 9 per cent against the risk-adjusted PSC using the then prevailing discount rate'.
UK National Audit Office 'PFI: Construction Performance Report' 5 February 2003	• 78 per cent of PFI projects surveyed were delivered on time or earlier than specified in the contract (c.f. 30 per cent for traditional D&C) • 22 per cent of PFI projects (c.f. 73 per cent for traditional D&C) ran over budget and the price increases were generally small and not due to the consortia charging more for the work originally specified.

The SETP rigorously separated core business from non-core business and successfully transferred optimum risk associated with infrastructure and non-core business. SETP's key feature was innovative design which provided substantial savings in capital and whole-of-life costs.

By all benchmarks the SETP was a remarkably successful PPP finishing four months ahead of time in 2009. It provided a windfall early access for government, recorded no lost time and no disputes, and transferred substantial risk to the private sector for whole-of-life management and maintenance.

Notably amongst its achievements was its green qualification. Ahead of any green star rating for precincts, it maintained commitments to a 5 star equivalent and was subsequently honoured with a Sustainability Award by the Business Southbank Board. Both SETP and QSP have been quietly absorbed onto the Government's asset register with very little public exposure and surprisingly little Government acknowledgement given their overall success.

With great public exposure, the Brisbane City Council with State Government support procured the Clem 7 and Airport Link Tunnel by PPP. Coming hard on the heels of the Global Financial Crisis these projects were heavily reliant on a business case built around volume risk. Clearly the current financial climate is not conducive to a vibrant PPP market or to supporting high volume. Coupled with some project hiccups, doubts about the effectiveness of PPPs are again surfacing. There are now four projects in Australia accruing heavy private sector losses.

In his review of the Sydney Cross City Tunnel Project, Gary Noble notes that PPPs are rarely genuine partnerships with the term partnership having only 'semantic relevance' and used 'primarily for politically or ideological purposes'. He identifies stark differences between the public and private sectors in motivation, role in the economy and in governance requirements. Given these differences, Noble questions the probability of a cohesive partnership being workable over time. Further questions are raised about the public sector use of PPPs. Why are projects such as Clem 7 and Airport Link procured as PPPs? What is the real value of the partnership arrangements to the taxpayer? Are PPPs simply a vehicle to cost shift expensive infrastructure away from the public purse, or conversely to create a supplementary revenue stream factored into the public purse?

Studies show an attitudinal factor prevalent in bureaucrats leaning towards the belief that PPPs provide free infrastructure gleaned from trade-offs and value markdowns. Deliberations by Queensland's Government attempting to extract or construct a more rewarding financial structure fails to account for the cost of doing nothing. Such was the delay to the Queensland Schools Project that the number of schools was significantly reduced.

SOME QUESTIONS THE SECTOR MAY ASK ITSELF COULD BE:

- Is the core business an essential service?
- Is the core business a manifestation of core business commercial?
- Can the business – core or otherwise, be done effectively by other means?
- What impact if any would a privatised entity have on the standard of service?
- Is core business simply an administrative role?

What now will be the cost of the remaining schools? Similarly what will be the final cost of the Sunshine Coast University Hospital (SCUH) after being on the back burner for the past 2 years? What problems will volume risk present for the recently approved Gold Coast Light Rail project? Finally, are delays that satisfy the search for a better deal ever costed and justified?

PUBLIC SECTOR MINDSET

There are remarkable differences in the business approaches taken by the public and private sectors, and between public jurisdictions. In recognition of this Victoria established Partnerships Victoria as a central agency to support the development and ongoing management of PPPs. In April 2010 the New Zealand Central Government Agency convened a workshop to examine their potential for PPPs with a view to establishing the same model. Interestingly, New Zealand has since commissioned three PPPs.

Queensland relies on Departmental agencies to take the lead on PPPs and has no central agency to monitor or manage the downstream contractual outputs. This feature suggests the Government's primary focus is on capital cost only and reveals much about the mindset of its bureaucrats. The public sector must become more business focussed in its approach to cost, value, risk and investment in its infrastructure procurement. The public sector also needs to be prepared to invest in the operating cost of social infrastructure. As a prime user it must willingly make contributions towards the future use of infrastructure for the benefit of its constituents and the cost of excessive deliberation needs to be factored in.

In 2009 the United States Department of Transportation

despatched a Scan Team to undertake a review of PPPs being delivered internationally. As with New Zealand the US is reviewing its own potential for a PPP market and is examining its options for public sector management.

A clear challenge identified by Weingart Brown et al is the need to change the mindset of the public sector to the use of PPPs. High on the list of findings in their 2009 report *Public-Private Partnerships for Highway Infrastructure: Capitalising on International Experience* is 'a necessary public sector mindset and skills base..... which is substantially different from those needed for conventional practices'.

The 2008 Ernst and Young review of PPP social infrastructure projects went further, identifying' innovation and relationship management' as key features of the SEPT success and a key ingredient of all successful PPPs.

These attributes created the scope for significant innovation and led to the project's international recognition at the London PFI awards in 2007. However the same attributes do not appear to be reaping any rewards in the hearts and minds of the Queensland public sector or for the tax-paying public.

THE CHALLENGES AHEAD FOR QUEENSLAND

Queensland Government appears to be a considerable distance from any rational commitment to the use of PPP. Its decision making history is weak and learning appears to be poorly documented and loosely applied. The most successful ventures to date have been in social infrastructure, yet a reluctance to make a program commitment has left the market bewildered and lacking appetite.

In the current economic climate the Queensland Government faces the necessary prospect of procuring future infrastructure via PPP, and of reviewing its internal mechanisms for transacting the business of procurement.

Challenges to such a review would include:

CHANGING PUBLIC EXPECTATIONS

Queensland has experienced spectacular demographic change over the past decade creating a population base that is disproportionate to the existing provision of infrastructure and services. Combined with a level of inertia this has resulted in a failure to remediate the poor condition of existing social infrastructure and services such as schools and hospitals. A greater public awareness of the quality of facilities and services has also developed.

A classic example of this dilemma exists in the Queensland Sunshine Coast where the dramatic demographic shift left its hospital system unable to cope with demand. A new public hospital was mooted as a PPP in 2007, and shelved in 2009. Interestingly a recent press release (15/2/2011) announcing new research centre arrangements for the SCUH implied a scheduled commencement date in 2013 which was confirmed by the Queensland Premier (4/4/2011) as a PPP.

DEFINING CORE BUSINESS

The public sector must become more objective about defining its true core business. It must also exercise greater objectivity in determining the fundamental need for capital assets in the provision of services. There is little evidence to suggest that public ownership of a capital asset provides any material benefit over and above private sector ownership of the asset

The challenge for Queensland is to commit to a system similar to Victoria's and to create a discipline of rigour around the procurement process which affords public transparency and justification.

The 2011 KPMG Infrastructure Australia Review of PPPs identified a clear PPP skills deficiency within the public sector, a view shared by Weingarten et al and by Ernst and Young. This was a key feature emphasised by Auditor General Ian McPhee in his address to the international Public Sector Convention (March 2011). It is a deficiency that can be met by better recruitment practices, but also needs a comprehensive training program for existing public servants. Victorian Treasury requires its public servants to undertake training in Gateway and Investment Logic Management, but these short training workshops do little to provide the higher level skills needed to evaluate, procure and manage large infrastructure projects. In this instance such training should be placed with an institute of higher learning or a University as an overall program to prepare public sector employees for infrastructure procurement and value management.

KEEPING THE PRIVATE SECTOR MOTIVATED

Possibly the greatest challenge faced by the Queensland Public Sector is not only to reignite its own interest in the partnership model, but to keep the private sector motivated. Inherently, the public sector's capacity to source and allocate funds falls well behind the private sector's capacity to access funds. While this phenomenon alone does not justify the need for PPPs it is a highly motivating factor for the public sector.

It is essential to provide and maintain a competitive market where the public sector has relative certainty around price and value, and the private sector has relative certainty around risk and reward and manageable costs. A weak market effectively reduces the pool of competitors and their respective appetites making the principle of certainty impossible to accurately assess. The public sector also needs to manage relative certainty of value over the life of the partnership. Currently, the British Government is reviewing existing PFI contracts to seek potential savings. Risk, passed to the private sector at great cost to the tax payer is too easily resumed by a less than diligent public sector. If value is perceived to diminish over time, public appetite for PPP's will wane.

Queensland needs to clearly define its institutional procurement capability, firstly to assess, evaluate and monitor major contracts, and secondly to ensure that maximum contractual performance is attained. Following the British Government's lead, a review of all major contracts (traditional, alliance and PPPs alike) to determine whether existing procurement practices deliver value for money could be a useful starting point.

Presenting the public sector as a professional business-like entity ready to inspire partnership dialogue with the private sector is just one part of keeping the private sector interested and motivated. PPP reviews are overwhelming in their call for fairer risk allocation, less volume risk and more productive partnership arrangements in PPP contracts of the future. McPhee makes it clear that the partnership factor is meaningless unless bureaucrats vigorously monitor and report on all contractual undertakings. Weingart et al (2008) noted that effective contract management is vital to maintaining the public sector's risk posture and to securing good working relationships with private contractors.

To be effective in the PPP market, Queensland needs a professional unit capable of dealing with and inspiring the private sector, and to give frank and unbiased advice to Government with respect to infrastructure procurement.

CONCLUSION

This paper considers underlying weaknesses in the Queensland Government's infrastructure procurement methodology. There is no apparent urgency to address the structural inefficiency of existing procurement, or to accept learning from its limited experience, or from jurisdictions with far greater experience which are capable of adding value to the State's infrastructure program.

Importantly the absence of any value review of its major projects and failure to heed lessons learned in a way that sets benchmarks and protocols for the infrastructure market, marks Queensland as a state of uncertainty for private sector investment.

Victoria has moved away from traditional contracting and Alliances to embrace PPPs as its preferred procurement model on price and value certainty. Other jurisdictions, nationally and internationally express similar support for the PPP vehicle.

The recent inability of a number of private sector projects to deliver projected outcomes has tarnished the public perception of PPPs. However none of these diminish the value of Queensland's two social infrastructure PPPs which remain relatively successful even by Queensland's own standards. Coupled with lessons from other jurisdictions Queensland should be comfortable about the use of PPPs to procure its future social infrastructure.

The time has come for Queensland to move beyond its cautious stance and accept that PPP is by far and away the best option for addressing its social infrastructure deficits, and to call to account the management of its procurement program.

Queensland must signal a clear commitment to stabilise an interested marketplace and to benchmark value assessment for public digestion in a manner which the public and its servants understand. This can only happen through the creation of an independent body with the political and bureaucratic will to ensure that value is real and is maintained over the whole-of-life.

AUTHORS FOOTNOTE:

Significant changes occurring in Queensland since the time of writing include;

- change of Government (March 2012)
- George St Precinct with greater Private Sector involvement announced (May 2012)
- Projects Queensland established(June2012)
- Sunshine Coast University Hospital PPP announced(July 2012)

REFERENCES

N Jagger, C Yuksel, *A Summary of Good practice*, Southbank Education and training Precinct, Brisbane, 2009.

KPMG, *PPP Procurement: A Review of Barriers to Completion in the Procurement of PPP Projects,* Infrastructure Australia, 2010.

I McPhee, 'Public Sector Accountability', *International Public Sector Convention,* CPA Australia, Melbourne, 2011.

G Matthew, G Brooke, 'The Right Project – The Right Process', *National Infrastructure Summit,* 2008.

Minter Ellison, *Infrastructure 2008: An Ambitious Agenda*, Minter Ellison, Sydney, 2008.

G Noble, 'The Role of Contracts in Public Private Partnerships', *UNSW Law Journal,* Vol 29 No. 3.

Queensland Government, *South East Queensland Regional Plan 2009 – 2031,* Department of Infrastructure and Planning, Queensland, 2009.

N Tanburo, 'An Update on the Australian Alliance Industry: A Treasury View', *Alliance Contracting Summit,* Melbourne, 2008.

J Weingart Brown, et al, *Public-Private Partnerships for Highway Infrastructure: Capitalizing on International Experience,* US Department of Transportation, 2009.

M Wilde, et al, *The Journey Continues: PPPs in Social Infrastructure,* Ernst and Young,

NORM JAGGER

Norm Jagger is an experienced professional in the field of education and infrastructure having held numerous senior positions during his career. Most recent was with Queensland's first PPP, the internationally acclaimed Southbank Education and Training Precinct (SETP) which is now home to the Southbank Institute of Technology. The SETP was judged as the 'Best Global Project to Sign' at the prestigious Public Private Finance Awards in London in 2007. These awards acknowledge and celebrate industry best practice, attracting entries from around the world.

Norm's qualifications include a Graduate Diploma in Education Administration, Bachelor of Education, Diploma of Teaching and an accredited Gateway Reviewer in Australia and New Zealand. He is an Adjunct Professor with the Institute of Sustainable Development and Architecture, Bond University, and practises as an independent consultant to the infrastructure industry.