PUBLIC ACCOUNTS COMMITTEE

INQUIRY INTO PROJECT PLANNING AND FUNDING APPLICATIONS FOR MAJOR WESTERN AUSTRALIAN INFRASTRUCTURE PROJECTS

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Report No. 9

Presented by:
Hon J.C. Kobelke, MLA
Laid on the Table of the Legislative Assembly
on 18 November 2010

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COMMITTEE'S FUNCTIONS AND POWERS

The Public Accounts Committee inquires into and reports to the Legislative Assembly on any proposal, matter or thing it considers necessary, connected with the receipt and expenditure of public moneys, including moneys allocated under the annual Appropriation bills and Loan Fund. Standing Order 286 of the Legislative Assembly states that:

The Committee may -

1 Examine the financial affairs and accounts of government agencies of the State which includes any statutory board, commission, authority, committee, or trust established or appointed pursuant to any rule, regulation, by-law, order, order in Council, proclamation, ministerial direction or any other like means.

2 Inquire into and report to the Assembly on any question which -

(a) it deems necessary to investigate;

(b) (Deleted V. & P. p. 225, 18 June 2008);

(c) is referred to it by a Minister; or

(d) is referred to it by the Auditor General.

3 Consider any papers on public expenditure presented to the Assembly and such of the expenditure as it sees fit to examine.

4 Consider whether the objectives of public expenditure are being achieved, or may be achieved more economically.

5 The Committee will investigate any matter which is referred to it by resolution of the Legislative Assembly.

INQUIRY TERMS OF REFERENCE

On 25 November 2009 the Public Accounts Committee resolved to conduct an inquiry with the following terms of reference:

> The Public Accounts Committee will examine and report on the best approaches to decision making for major infrastructure projects in Western Australia, with particular reference to:
>
> 1 the robustness of project planning and assessment processes; and
>
> 2 whether funding cases are appropriately developed and presented to maximise access to Federal Government funding.

CHAIRMAN'S FOREWORD

As a rapidly growing and physically large state, Western Australia faces enormous infrastructure demands. The *2010–11 State Budget* includes $7.6 billion in its Asset Investment Program. However, there are many important and worthwhile projects that have to wait their turn on the priority list. There are also several major projects to which the current government has committed without allocating the funds necessary to bring them to fruition.

To maintain our high standard of services, meet the growing demands for these services and facilitate the rapid expansion of the Western Australian economy, it is essential to build the required infrastructure. Given that Western Australia does not have the financial capacity to meet all of its required infrastructure demands, it is important that maximum value is derived from infrastructure investment and that there are robust processes to aid priority setting and decision-making. To fail to do this will hold back the state's development and result in lower standards of services than could be expected.

To augment the state's capacity to build essential infrastructure, governments look for funding assistance from the federal government and the private sector. In both cases the state enhances its opportunities to acquire additional funding sources if it has an appropriate set of processes for the planning and acquisition of the required infrastructure. Infrastructure Australia makes recommendations to the federal government on funding for the states based on the projects having strong business cases. Given a common view that Western Australia has not always received a commensurate fair share of the Commonwealth funds distributed to the states, it would serve our interest to ensure that funding submissions from Western Australia are of a higher standard.

In recent years the state government has been developing the policies and organisational structures and recruiting the skilled people needed to achieve better outcomes. The state government is implementing the Strategic Asset Management Framework (SAMF), which requires agencies to undertake a five-stage process for capital investment. This has been followed by the Works Reform Program which includes organisational changes to drive the SAMF processes. This report devotes considerable effort to summarising these policies, processes, and structures. With SAMF and Works Reform still being implemented it is not possible to judge their effectiveness at this time. That being said, the Committee was impressed with SAMF and Works Reform, and is keen to see them fully implemented and the promised benefits achieved.

Full utilisation of these policies will give greater confidence that projects can be delivered on budget and on time. Having more accurate and reliable information at the time of the decision to commit to a project will deliver more value for money outcomes and provide a more informed basis for setting priorities between competing projects.

The decision to commit funding to a major project is always a political decision. And so it should be. No matter how detailed and accurate the analysis and planning for a project, there is usually a large element of subjective judgement in proceeding with one project before another. Western Australia Police gave an example of the dilemma. Limits on funding requires a choice to be made between replacing an aging helicopter or upgrading ICT essential to effective policing or replacing

an old and inadequate police station. Such decisions are not easily reduced to a number that measures efficiency or best outcomes between competing demands. Determining the priority for funding these projects requires a decision at the political level.

An infrastructure project targeted at developing a vast, resource rich state may involve a considerable financial risk to the state. However, based on a thorough assessment of the benefits and risks, a bold political decision can well serve the state's long-term interests.

In the 1890s the commitment to deliver water to the goldfields from Mundaring was estimated to cost 2.8 million pounds, which represented 80 per cent of the then State budget. Similarly the commitment in the 1970s to bring natural gas from the Pilbara to Perth, underpinned by a take or pay contract, initiated the gas developments which are now a major contributor to the state and national economies. Both projects have been significant contributors to economic development while placing very high levels of financial risk on the state, which subsequent governments had to manage.

Projects with popular appeal, if committed to politically without the evaluations provided by SAMF, can result in scarce money being spent on ineffective or even wasteful projects. The Liberal election promise in 2005 to build a canal to bring water from the Kimberley to Perth was costed at $2 billion. A more thorough study showed the price was likely to be $14.5 billion and carry a high level of risk. The Labor election promise in 2001 to build a sealed road from Tom Price to Karratha in the Pilbara was expected to cost $100 million. Labor won the election, and after spending $180 million the new road is only part constructed. Populist decisions can easily put sound economic management at risk.

The 2008 election commitment to construct a gas pipeline from Bunbury to Albany and the decision to inject $678 million of public money into the Oakajee Port project are instances where the benefit of the expenditure cannot be assessed as there was no analysis done prior to commitment. If business cases have now been completed, the Committee was given no evidence of it. The Commonwealth Government, in committing half of the $678 million to the Oakajee Port project, has made it subject to a business case and a rate of return on their equity contribution. The state government has made its commitment without any similar caveat.

It is concerning when the decision-making for a large and costly project is 'purely political' in the sense that it is decided without thorough planning and a business case study.

An infrastructure 'pipeline' or plan outlining the government's upcoming projects was highlighted by industry as a means to help them better prepare and align their resources. This would allow industry to participate more efficiently in the infrastructure construction market. Such a 'pipeline' may also assist in providing political parties with a list of well defined and worthwhile projects from which to make political promises.

Some infrastructure projects are primarily developed to achieve specific social outcomes. However, if there is no analysis of all the options, including non-infrastructure solutions, it is dubious as to whether the state is getting real value for money and can be guaranteed of achieving the desired social outcomes. Where a project is primarily to meet social needs and has marginal

direct economic benefit, then it is incumbent on the decision makers to determine the mechanisms by which the social outcomes will be delivered and the results measured.

For all infrastructure projects, it is essential that the costs and benefits are identified by proper planning and the preparation of a robust business case.

This report does not assess the worthiness of any particular project. It does, however, make recommendations that go to the need for a better level of evaluation of the costs and benefits of every project and the need to follow SAMF to the greatest extent possible, even for fast-tracked projects.

This report may be too technical to have a wide readership. Its value will be in supporting the fullest possible implementation of SAMF and Works Reform. This report is directed at senior public servants, ministers and members of parliament, and the media. It may be a forlorn hope, but if media coverage can look more to value for money and the thoroughness of project planning and development, rather than simplistic cost blowouts and construction delays, then our state and its people will be the beneficiaries.

Thanks must go to my fellow Committee members for their contribution to the ongoing work of the Public Accounts Committee and particularly this Inquiry.

On behalf of the Committee I would like to thank Loraine Abernethie, our Principal Research Officer, and Mathew Bates, our Research Officer, for the work they have invested in this report. I also acknowledge the assistance of Ms Isla Macphail who was the Principal Research Officer at the commencement of this inquiry.

HON J.C. KOBELKE, MLA
CHAIRMAN

ABBREVIATIONS AND ACRONYMS

AASB	Australian Accounting Standards Board
AMC	Australian Marine Complex
AMC–CUF	Australian Marine Complex—Common User Facility
ANAO	Australian National Audit Office
AusLink Act	AusLink (National Land Transport) Act 2005 (Cwth)
BAF	Building Australia Fund
BCA	Benefit-Cost Analysis
BCR	Benefit-Cost Ratio
BFS	Bankable Feasibility Study
BHPB	BHP Billiton
BMW	Building Management and Works
CBA	Cost-Benefit Analysis
CEIID	Centre for Excellence and Innovation in Infrastructure Delivery
COAG	Council of Australian Governments
the Committee	Public Accounts Committee
CSO	Community Service Obligation
CUF	Common User Facility
CUI	Common Use Infrastructure
Cwth	Commonwealth of Australia
DBFM	Design, Build, Finance, Maintain
DBFO	Design, Build, Finance, Operate
DBOM	Design, Build, Operate, Maintain
DoC	Department of Commerce
DHW	Department of Housing and Works
DITRDLG	Department of Infrastructure, Transport, Regional Development and Local Government

DPC	Department of the Premier and Cabinet
DRDL	Department of Regional Development and Lands
DSD	Department of State Development
DTF	Department of Treasury and Finance
DTF-SP	Department of Treasury and Finance, Strategic Projects
EACR	Economic Audit Committee Report: *Putting the Community First: Partnering with the Community and Business to Deliver Outcomes*
EERC	Expenditure and Economic Review Committee (previously ERC)
ERC	Expenditure Review Committee (now EERC)
FIFO	Fly-in Fly-out
FM	Facilities Management
FSH	Fiona Stanley Hospital
GCS	Guaranteed Construction Sum
GSP	Gross State Product
GTE	Government Trading Enterprise
the Hub	Perth City Link–Public Transport Hub
IA	Infrastructure Australia
IA Act	*Infrastructure Australia Act 2008* (Cwth)
IAC	Infrastructure Australia Council
Inalco	Innovative Aluminium Company
MOU	Memorandum of Understanding
MRWA	Main Roads Western Australia
MUIP	Multi-User Infrastructure Package
Muja A and B	Muja Power Station Stages A and B
National PPP Guidelines	National Public Private Partnership Guidelines
NBF Act	*Nation-building Funds Act 2008* (Cwth)
NBP	Nation Building Program

NBPNLT Act	*Nation Building Program (National Land Transport) Act 2009* (Cwth)
NFIT	New Facilities Investment Test
NOP	Non-owner Participant
NPBH	New Perth Bunbury Highway
OAG	Office of the Auditor General
OECD	Organisation for Economic Co-operation and Development
OPR	Oakajee Port and Rail Pty Ltd
OSP	Office of Strategic Projects
PCL	Perth City Link
the Plan	Nation Building Economic Stimulus Plan
PPC	Perth Police Complex
PPP	Public Private Partnership
PSC	Public Sector Comparator
RBS	Royal Bank of Scotland - RBS Group (Australia) Pty Limited
RFP	Request for Proposal
RNO	Ravensthorpe Nickel Operation
SAMF	Strategic Asset Management Framework
SAP	Strategic Asset Plan
SCI	Statement of Corporate Intent
SDP	Strategic Development Plans
TOC	Target Outturn Cost
VMS	Value Management Study
Works Reform	Works Reform Program
WSBS	Wellington Street Bus Station

EXECUTIVE SUMMARY

Western Australia's population and economy have grown significantly over recent years and continue to grow steadily. This growth necessarily impacts on the provision of government services throughout the state and will require increased public investment. In turn, there will be a need for more effective and efficient infrastructure that will deliver real benefits to the state. There is a clear expectation that the successful implementation of the Works Reform Program, including the Strategic Asset Management Framework, would ensure that taxpayers receive improved value for money outcomes from these large infrastructure projects. Allied to this, the State needs to maximise opportunities for funding major infrastructure projects from federal funds or through private enterprise where appropriate. By accessing Commonwealth funding the State is able to provide levels of infrastructure greater than that possible using its own resources. There is concern that Western Australia does not receive as much Commonwealth funding for major infrastructure projects as it might.

The Committee examined a range of projects as examples of decision-making on major infrastructure projects, and an overview of these is provided in Chapter 2.

These issues are discussed in Chapters 1 and 2.

Strategic Asset Management Framework and its Application

One way of achieving the desired outcomes from infrastructure is through robust long-term planning to increase certainty and minimise risks associated with infrastructure projects. Western Australia's infrastructure procurement mechanism is the Strategic Asset Management Framework (SAMF), which consists of 11 policies and guidelines designed to improve public sector asset management and capital investment. SAMF is designed to ensure a value for money outcome for infrastructure procurement and is generally accepted as providing a robust framework for planning and delivering infrastructure.

SAMF has been a step in the right direction to improving the procurement of infrastructure. At this point, SAMF cannot be said to have been fully implemented, and there remain inconsistencies with its application. It is anticipated that, when fully implemented, SAMF will result in improved infrastructure delivery.

It is clear that good long-term planning delivers substantial benefits. It is equally clear that government decisions are necessarily political. Sometimes political decisions in relation to infrastructure will not be taken with the depth of planning and investigation considered appropriate for such major projects. It is anticipated that the full implementation of SAMF in a transparent manner, will lead to better-informed decision-making and improved value for taxpayers. The full implementation of SAMF will also avoid agencies getting approval from government on poorly prepared proposals which result in major cost escalations and significant time delays.

These issues are discussed in Chapter 3.

Identification of Service Delivery Needs

At the planning stage SAMF requires agencies to clearly identify service delivery needs and to consider all possible options in responding to that need, including non-asset solutions. The Perth Police Complex provides evidence of an agency responding to clearly identified gaps in service delivery as determined through needs analysis. Western Australian Police's analysis showed that the existing East Perth Lockup and the Perth Police Station at Curtin House were inadequate to the needs of modern policing and, after considering all options, a new, centrally-located police complex was determined to be the best response to filling service delivery gaps.

Some agencies and Government Trading Enterprises can more readily forecast and calculate demand and, therefore, their service delivery needs. For example, Main Roads Western Australia can measure freight and commuter traffic, and can utilise population projections and other statistics to help determine current and future need. The New Perth Bunbury Highway and Gateway WA were two road projects examined by the Committee where Main Roads Western Australia was able to demonstrate need using demand forecasts. Similarly, Western Power assesses future electricity demand through taking into account population growth, and economic and industrial development forecasts to determine when new infrastructure is required. This was in evidence in the two Western Power projects that the Committee examined, namely the Mid-West Energy Project Stage 2 and the South West Transmission Line Reinforcement project.

Some projects are developed in response to perceived social needs. This is largely the case with the Ord East Kimberley Expansion Project where Commonwealth funding has been provided for the improvement of social infrastructure in the region, including health and education facilities. State funding is being provided for the expansion of the Ord irrigation area, with the aim of expanding the economic base of the region and providing employment opportunities for local Indigenous communities. A claimed social benefit has been used to justify the project rather than an economic net benefit. Social needs are often more difficult to quantify and it is unclear as to whether the proposed social outcomes will be delivered.

The final determination of infrastructure priorities is always a political decision. When a project is committed to without the time to complete the full SAMF process, it is important that SAMF be applied to the fullest degree possible to deliver maximum benefits for these 'fast-tracked' projects.

Successive governments have agreed that there is a need for a new port in the Mid-West due to the constraints of the existing infrastructure at Geraldton Port. The current iteration of Oakajee Port Common Use Infrastructure consists of the government-funded breakwater, turning basin and other infrastructure. Under the previous proposed arrangements, the port was to be fully funded by the private sector. The current government claims that the reason for public funding is to make the port a multi-user, multi-function facility. This different model is in response to the government's vision of establishing a value-adding industrial estate adjacent to the port. It is not clear that there is sufficient industry demand for on-shore value-adding and, therefore, the need for the multi-function Common Use Infrastructure at Oakajee Port. If the industry demand does not eventuate, considerable public money will have been expended on a project that has not been supported by rigorous analysis of need. If SAMF had been applied in the conception and development of the project, need would have been clearly identified and the initial cost-benefit analysis would have revealed potential risks for consideration and mitigation.

Similarly, the Bunbury to Albany gas pipeline is an election commitment of the current government. The advice to the Committee is that no substantial work has yet been completed on preparing a business case for the project. The $20 million budget allocation to the project is designated for corridor establishment. There is still time for SAMF principles to be applied to ascertain need and develop a sound cost-benefit analysis. If, as a result of the analyses, the project is found not to have a net economic benefit, the government should be transparent about its decision to either proceed or cancel the project.

These issues are discussed in Chapters 2 and 4.

Concept Development

Concept development and evaluation are the next stages in SAMF, and allow for value for money to be realised through the assessment of possible infrastructure solutions and the subsequent evaluation of preferred options. It is important that concept development is used as a means of optimising the cost and performance of the proposed project.

In developing the Perth Police Complex, Western Australia Police sought to maximise efficiencies in the delivery of police services by co-locating the Perth Police Station, the Perth Watch House and a Magistrates Court. Costs associated with constructing separate projects for the different components of the Perth Police Complex have been minimised and efficiencies for the organisation have been maximised.

Perth City Link is a major urban renewal project requiring substantial changes to public transport infrastructure, principally the sinking of a section of the Fremantle railway line and the relocating underground of the existing Wellington Street Bus Station. The Public Transport Authority commissioned a study which concluded that a major bus station should be retained at its current location and that an underground bus station was both feasible and the preferred option. Despite this conclusion, the Public Transport Authority conducted a further study to consider the option of redeveloping Wellington Street Bus Station as an on-street facility. This study found that an on-street facility would result in an interchange spread over a wider area and would result high operating and fleet procurement costs over a 30 year period. Given the results of these studies, Public Transport Authority decided to proceed with the underground bus station option. It is unclear whether the full cost and service delivery implications of sinking the bus station have been factored into the costings.

These issues are discussed in Chapter 5.

Concept Evaluation

To assist government in determining the most appropriate project response to a service delivery shortcoming, concept evaluation aims to quantify outcomes by assigning values for comparison. It consists of evaluations of agency performance, financial impacts, economic outcomes and social impacts.

Agency performance is measured against the outcomes agencies are expected to deliver. For example, one of Main Roads Western Australia's key outcomes is the reliable and efficient

movement of people and goods. Prior to commencing the New Perth Bunbury Highway, Main Roads Western Australia was able to quantify the effectiveness of the highway's contribution to the agency's outcomes and objectives by modelling the impact of the New Perth Bunbury Highway on travel times and accident rates for travel between Safety Bay Road and Lake Clifton.

The Australian Marine Complex was developed by the then Department of Commerce and Trade. The expected service delivery of this agency, now the Department of Commerce, is to promote economic development in Western Australia. The concept evaluation for the Australian Marine Complex included a broad macro-economic assessment of industry demand to estimate the economic and financial impact of the Australian Marine Complex. Ernst & Young was engaged to conduct this analysis and estimated that, at full capacity, the Australian Marine Complex would result in $260 million in additional economic activity and would employ over 1,600 individuals.

The Department of State Development is the lead agency for the Oakajee Port Common Use Infrastructure project aiming to establish a value-adding industrial estate adjacent to the port. Both the Department of State Development and the Under Treasurer have acknowledged that government investment in the Common Use Infrastructure is a 'policy decision'. Rather than being concerned with establishing project need and undertaking concept evaluation, the Department of Treasury and Finance's involvement in the project is focussed on assisting with project delivery. According to the Department of State Development, government control of the Common Use Infrastructure helps to ensure the development will cater for the longer-term needs of the state. While this may be the case, it is difficult to confirm due to an apparent lack of rigorous economic evaluation that identifies the government's Common Use Infrastructure model as the best option.

Social impact analysis identifies those who gain and those who lose from a proposed project. SAMF recognises that this is difficult to quantify and provides a number of criteria that agencies should consider when assessing social impact. For example, Western Power altered the location of key infrastructure on the South West Transmission Line Reinforcement Project because perceived environmental and social impacts could not be overcome within the project's scheduled completion date.

Western Power's project was amended to avoid a negative social impact. Projects such as the Ord East Kimberley Expansion Project, however, are promoted as generating a positive social impact.

These issues are discussed in Chapter 5.

Business Cases

Agencies present the results of their evaluations in the form of business cases, which are the primary mechanism by which agencies propose infrastructure projects to government. They are used by Cabinet and the Economic and Expenditure Review Committee to determine which infrastructure projects will be funded and which will form the basis of applications for federal funding. Evidence suggests that, with some exceptions, business cases have not been comprehensive or well-developed. Fast-tracked projects are also decided upon prior to business cases determining whether value for money will be achieved by the project. The consequence of these two situations is that government is not making fully informed funding decisions.

Business cases also require agencies to define project delivery options, including joint ventures, financing alternatives and private sector involvement. The majority of infrastructure funding is by way of budget appropriations, using state and/or federal contributions, or private investment through public private partnerships. A key factor in the State's ability to attract federal and/or private funding is the rigour with which business cases are developed.

These issues are discussed in Chapter 5.

Attracting Federal and Private Funding

The Department of State Development is the lead agency for the development of the Western Australian Government's submissions to Infrastructure Australia (IA) for federal funding. IA has provided detailed guidelines for developing applications, including specific jurisdictional requirements. The Department of State Development submitted to Cabinet projects that it assessed as meeting IA's requirements for 'Projects which were well developed'. Cabinet submitted seven of these to Infrastructure Australia for the 2009 funding round. However, Infrastructure Australia did not consider any of these as being 'ready to proceed'. Instead, Infrastructure Australia classified Western Australia's applications as 'Threshold', 'Real Potential' or 'Early Stage' projects. Nevertheless, some of these Western Australian projects received federal funding support.

The federal funding contribution for Oakajee Port Common Use Infrastructure is in the form of an equity injection and is subject to the Commonwealth's analysis of the Bankable Feasibility Study showing a positive cost-benefit outcome and a commercial rate of return. It is not clear what the impact on the state government's contribution to the project would be should the Commonwealth funding not be forthcoming.

Another option agencies are required to consider is the potential for private involvement in the form of a public private partnership. While there is potential for public private partnership projects to provide value for money outcomes and reduced government risk, there are also a number of drawbacks such as high project development costs. Public private partnerships are only suitable for public infrastructure provision in the right circumstances, and governments must ensure that potential public private partnership projects are subjected to rigorous scrutiny. The decision as to which is the best procurement model for a project is part of the SAMF process, therefore, any decision to procure a project using a public private partnership should arise from this process. If the decision to use a PPP is purely political it can create uncertainty for industry and fail to provide value for money over the life of the project.

These issues are discussed in Chapters 2, 7 and 8.

Delivering the Asset

SAMF is a sequential process for asset acquisition and there are risks associated with running these processes concurrently. The Auditor General found that many of the issues associated with delivering Fiona Stanley Hospital were a result of the concurrent operation of critical SAMF elements. This resulted in three major changes to the project scope and, consequently, four significant alterations to the estimated project budget. Such significant project and budget

amendments have a number of flow-on effects including those on government budget planning, the ability of government to accurately assess project opportunity costs and public confidence in government capabilities.

The Western Australian Government has a detailed policy document, *The Infrastructure Procurement Options Guide*, which requires agencies to consider a number of factors when deciding the best procurement methodology. Primarily, agencies need to understand the risk exposure attached to the various procurement models and select the most appropriate model that manages the unique risks attached to their project. For example, Main Roads Western Australia selected an alliance contract for the delivery of the New Perth Bunbury Highway as this model is generally considered the most appropriate contracting type when managing tight time constraints—in this case, due to federal funding conditions—and where there may be a large number of complex or unpredictable risks.

These issues are discussed in Chapter 6.

Works Reform

The Works Reform Program (Works Reform) was initially introduced to address a number of major problems in relation to the procurement of building related projects and programmes. As part of ongoing reform, the works function of the then Department of Housing and Works was transferred to the Department of Treasury and Finance, with the works functions now allocated to two business units, namely Building Management and Works and Strategic Projects. One major role of these units is to achieve better alignment between current and intended SAMF implementation. These units take a lead role in planning non-residential building projects and in the development of their business cases. The Under Treasurer allocates projects to these units, with Strategic Projects generally assigned high risk, sensitive, potential public private partnership, unique or high value (over $100 million) projects. There is strong collaboration between Building Management and Works and Strategic Projects, with assistance provided by the Centre for Excellence and Innovation in Infrastructure Delivery. The impact of Works Reform on agency implementation of SAMF needs to be independently evaluated.

These issues are discussed in Chapter 3.

Risk

SAMF is intended to reduce risks and maximise the likelihood of achieving a value for money outcome for infrastructure projects in Western Australia. The two broad types of risk identified are demand risk and construction risk. In relation to demand risk, proper application of SAMF requires agencies to identify and quantify service delivery needs, which serves to reduce the possibility of under-utilisation of the infrastructure constructed.

The possible construction risks associated with delivery stages are reduced if projects only proceed once they are fully scoped, thus reducing the incidence of scope and design changes during construction. Construction risks are further reduced through the selection of the contract and delivery model most appropriate for each project.

Risk can be further mitigated if agencies learn the lessons of previous projects, and this can only occur if projects are subjected to rigorous evaluation, as provided for in SAMF. The proper application of SAMF also requires agencies to have staff who are experienced in project management, including planning, development and delivery, and who have the requisite skill sets. This has been an ongoing problem for government generally, and Works Reform is currently implementing a number of strategies to enhance its skills base.

These issues are discussed in Chapter 9.

Risk also arises for projects resulting from political imperatives due to the limited application of the asset planning, and concept development and evaluation stages of SAMF. The demand and construction risks associated with such projects can be reduced through the development and publication of an infrastructure project pipeline.

Refinement of SAMF is an ongoing process and Works Reform is intended to improve agencies' application of SAMF processes. As Works Reform is a relatively recent programme and still being implemented, the system has not produced sufficient outcomes to allow the impact of the reforms to be assessed. While the Department of Treasury and Finance should evaluate the outcomes of SAMF reviews and Works Reform, such evaluations should be conducted with the assistance of independent advisors.

It is the Committee's intention to examine a small number of infrastructure projects to assess the degree to which the Strategic Asset Management Framework is being applied and whether the anticipated outcomes are being achieved. The Committee will report the results in its annual report.

These issues are discussed in Chapter 10.

FINDINGS

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Finding 1

Government Trading Enterprises are not currently required to comply with the Strategic Asset Management Framework. Their compliance with the framework was a recommendation of the Economic Audit Committee. The government is yet to respond publicly to this recommendation.

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Finding 2

The Strategic Asset Management Framework is generally accepted as a robust foundation for asset management in Western Australia. Shortcomings in project planning and delivery have tended to be the result of failures to ensure adherence to the framework.

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Finding 3

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Finding 4

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Finding 5

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Finding 6

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Finding 7

When social benefits are the primary justification for major project investment, comprehensive analysis must be undertaken to ensure the claimed social benefits are deliverable and the project will provide value for money.

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Finding 8

Promoting the economic growth of Western Australia and its related community development demands may involve a substantial element of risk. Thorough risk assessment and mitigation measures must be undertaken to manage this risk, thereby reducing the chance of redundant investment.

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Finding 9

It is generally accepted that a new port in the Mid-West is needed, based on reliable information suggesting that the expansion of iron ore mines in the region will exceed the capacity of Geraldton Port, which has expansion constraints.

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Finding 10

The need for government funding of the Common Use aspects of Oakajee Port is not clear, particularly given both the lack of detail in relation to the extent to which the private and public iterations vary and the reasons why they vary.

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Finding 11

The co-location of a range of services at the Perth Police Complex exemplifies the potential to maximise value through the use of value management studies that identify innovative responses to service delivery needs.

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Finding 12

The need for fitting buses with satellite tracking technology necessary for the operation of the Perth City Link underground bus station was not included in the original costing for the project.

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Finding 13

Economic evaluation is an important element for project selection, particularly for projects responding to a perceived economic need, as it allows the best option(s) to be selected.

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Finding 14

The decision to fund the Common Use Infrastructure of the Oakajee Port project was made without a cost-benefit analysis. Therefore, at the time the decision was made, it was not clear whether this arrangement represented the best value for money for the state.

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Finding 15

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Finding 16

A well-developed business case is essential for effective infrastructure decision-making, and can only be as robust as the concept development and evaluation processes that underpin it.

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Finding 17

The involvement of the Department of Treasury and Finance's Building Management and Works, and Strategic Projects in the development of business cases has the potential to enhance both Strategic Asset Management Framework compliance and the quality of agency business cases.

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Finding 18

There will always be a need to fast-track some infrastructure projects due to changing circumstances and political imperatives.

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Finding 19

Applying the Strategic Asset Management Framework processes to fast-tracked projects will help ensure the best possible infrastructure outcomes.

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Finding 20

Alliance contracts can provide an appropriate delivery model for infrastructure in some circumstances, including where there are:

- a large number of unpredictable risks with complex interfaces; or
- very tight time constraints; or
- there is a need for owner involvement during delivery.

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Finding 21

In developing a list of funding recommendations Infrastructure Australia assesses funding submissions against a number of criteria, and places particular emphasis on the rigor of the cost-benefit analysis.

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Finding 22

Submissions from Western Australia to Infrastructure Australia were assessed by the Department of State Development as being 'well developed' projects; however, Infrastructure Australia did not classify any of the Western Australian submitted projects as being well developed or 'ready to proceed'.

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Finding 23

None of the Western Australian projects submitted to Infrastructure Australia in the 2009 round for federal funding were classified as 'ready to proceed', the ratings being 'threshold', 'real potential' or 'early stage'.

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Finding 24

Failure to provide well developed and robust submissions to the federal government will decrease the potential for Western Australian projects to receive federal funding.

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Finding 25

The selection of an appropriate project delivery contract can minimise the level of the State's risk exposure during the construction stages of a project. Many of the possible risks encountered during the delivery stage can be reduced if projects only proceed once they have been fully scoped, thus reducing the risk of costly scope and design changes following the commencement of construction.

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Finding 26

Industry welcomes the Centre for Excellence and Innovation in Infrastructure Delivery briefings outlining proposed infrastructure projects as this assists potential bidders to prepare for upcoming opportunities.

RECOMMENDATIONS

Page 38

Recommendation 1

Works Reform should be independently evaluated to ensure that the reform is delivering the desired or anticipated outcomes.

Page 50

Recommendation 2

The State Development Agreement for the Oakajee Port and Rail Project should be made public.

Page 50

Recommendation 3

The Minister for State Development should publish the differences between the private and public iterations of Oakajee Port Common Use Infrastructure, together with the needs analysis underpinning the decision to provide public funds.

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Recommendation 4

Government organisations should be encouraged to undertake value management studies to identify innovative responses to their service delivery needs.

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Recommendation 5

The Minister for State Development should publish details of any economic evaluation undertaken as to the benefits derived from the commitment of public funds for the Oakajee Port Common Use Infrastructure project.

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Recommendation 6

For fast-tracked projects, it is important that the Strategic Asset Management Framework be applied to the greatest extent possible to ensure optimal outcomes.

Page 114

Recommendation 7

The Department of Treasury and Finance and the Department of State Development should ensure that the funding applications to the federal government are well developed, contain robust cost-benefit analyses and comply with Commonwealth funding submission requirements.

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Recommendation 8

The government should publish its Public Private Partnerships policies and processes to ensure their transparent and consistent application, and to improve value for money outcomes.

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Recommendation 9

The government should develop, maintain and publish a Government Sector Infrastructure Plan that details all medium to large infrastructure projects being considered, and provides an assessment of each project's stage of development.

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Recommendation 10

The Strategic Asset Management Framework requirement for a post-project assessment should be universally applied and involve an independent party.

MINISTERIAL RESPONSE

In accordance with Standing Order 277(1) of the Standing Orders of the Legislative Assembly, the Public Accounts Committee directs that the Minister for State Development and the Treasurer report to the Assembly as to the action, if any, proposed to be taken by the Government with respect to the recommendations of the Committee.

CHAPTER 1 INTRODUCTION

1.1 Background

In recent years, Western Australia's population and economy have grown significantly. In the five years to June 2009, the state's population had increased by 13.2 per cent for an average annual growth rate of 2.5 per cent.[1] This rate of population growth is well above the national average of 1.8 per cent.[2] Projections show the population is set to more than double to around 5.37 million by 2056.[3] Similarly, the state's economy has also experienced rapid expansion, with average annual growth in Gross State Product (GSP) exceeding four per cent since 1989–90.[4]

Continued growth in the state's population and economy will necessarily impact on government and the provision of government services, and will require increased public investment, including investment in infrastructure.

Infrastructure is an essential driver of economic growth and development, helping to generate wealth and prosperity, an improved standard of living, and social and environmental benefits.[5] Engineers Australia's *2005 Western Australian Infrastructure Report Card* acknowledged that 'one of the major challenges facing Western Australia was meeting demand for new infrastructure related to the strong economic and population growth, while meeting the need for replacing or upgrading aging infrastructure'.[6] Their *2010 Report Card* points to areas such as road maintenance and renewal, local roads, gaps in mass transit services to north-east Perth, the grain rail network and gas distribution networks as requiring attention. Access to the airport is considered a 'major concern', while challenges confronting potable water infrastructure require priority funding. Further, ageing electricity transmission and distribution infrastructure needs to be addressed.[7]

The combination of continued economic growth, an expanding population and the above-mentioned infrastructure challenges will contribute to a 'considerable increase in public

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1 Australian Bureau of Statistics, *3235.0 – Population by Age and Sex, Regions of Australia, 2009, Western Australia*, 5 August 2010, p.1.

2 Parker, G, 'Population Boosted by New Workers', *The West Australian*, 6 August 2010, p.14.

3 Australian Bureau of Statistics, *3222.0 – Population Projections Australia 2006 to 2101*, 4 September 2008, p.51.

4 Australian Bureau of Statistics, *1367.5 – Western Australian Statistical Indicators, March 2005*, 2005, p.1.

5 The link between infrastructure and economic growth is well documented. See, for example, Engineers Australia, 2005 Western Australian Infrastructure Report Card, Engineers Australia, Western Australian Division, West Perth, 2005; Henckel, Timo and McKibbin, Warwick, 'The Economics of Infrastructure in a Globalized World: Issues, Lessons and Future Challenges', Conference Proceedings, Brookings Institution, Washington DC, 4 June 2010; Property Council of Australia, *Building Wealth through Infrastructure. Setting Priorities and Valuing Gains in New South Wales*, report prepared by Centre for International Economics, Centre for International Economics, Canberra, May 2006; OECD, *Infrastructure to 2030: Telecom, Land Transport, Water and Electricity*, 2006; Helm, Dieter, 'Infrastructure Investment, the Cost of Capital, and Regulation: An Assessment', *Oxford Review of Economic Policy*, vol. 25, no. 3, 2009; Productivity Commission, *Review of National Competition Policy Reforms*, Inquiry Report No. 33, Commonwealth of Australia, Canberra, 28 February 2005; and PricewaterhouseCoopers, *Review of Major Infrastructure Delivery*, for Infrastructure Australia, December 2008.

6 Engineers Australia, *2005 Western Australian Infrastructure Report Card*, Engineers Australia, Western Australian Division, West Perth, 2005, p.i.

7 ibid., pp.ii–iii.

investment needs'.[8] In Western Australia, these investment needs are exacerbated by a number of factors, including:

- the geographic size of the state;
- demand for infrastructure outweighing government's funding capacity;
- increases in both the number and complexity of projects being managed by government;
- increased demand for infrastructure in remote areas—including social infrastructure, and port and road expansions—due to the mining and resource sectors; and
- the increasing cost of delivering infrastructure as a result of the competing demand for labour and materials from the resources sector.

These factors have impacted upon the delivery of infrastructure in Western Australia, and projects have met with construction delays and budget overruns. In addition to the technical and structural problems outlined above, factors internal to the operation of government departments may also explain some cost overruns and construction delays.

This issue has already been acknowledged by government in the Works Reform Program (Works Reform), which has noted an 'agency culture' of 'understating project costs and delivery timeframes'.[9] This agency culture may be related to either:

- 'optimism bias', which arises when project proponents 'judge future events in a more positive light than is warranted by actual experience';[10] or
- 'strategic misrepresentation', which results from project proponents 'deliberately and strategically overestimate[ing] benefits and underestimate[ing] costs in order to increase the likelihood that it is their projects, and not the competition's, that gain approval and funding'.[11]

Evidence reviewed by the Public Accounts Committee (the Committee) confirms Building Management and Work's (BMW's) view that these factors are present in Western Australia.

Clearly, the state's growing need for increased and improved infrastructure has had, and continues to have, significant budget implications for government, with successive state governments committing substantial amounts of money for capital works. The *2009–10 Annual Report on State*

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8 Henry, K et al., *Australia's Future Tax System: Final Report*, Report to the Treasurer, Commonwealth of Australia, Canberra, December 2009, Executive Summary, p.1.

9 Building Management and Works, Department of Treasury and Finance, *Works Reform Business Solution Plan*, Government of Western Australia, Perth, June 2009, p.15.

10 Flyvbjerg, B, 'From Nobel Prize to Project Management: Getting Risks Right', *Project Management Journal*, vol. 37, no.3, August 2006, p.6.

11 ibid.

Finances reports public sector infrastructure investment of $6.8 billion.[12] The *2010–11 Budget* includes $7.6 billion in its Asset Investment Programme.[13]

Government expenditure on infrastructure should deliver real benefits to the state and provide value for money. In order to achieve these outcomes, the government must have in place—and follow—infrastructure delivery policies and processes that work to address the various technical, structural, psychological and political factors outlined above. Without these policies, the likelihood of delays and budget problems increase, and the opportunity to access funding from both the Commonwealth Government and the private sector decreases.

Access to Commonwealth funding allows the State to provide levels of infrastructure beyond its capacity using own-source revenue. The Committee is concerned that Western Australia's share of Commonwealth funding does not reflect its contribution to the national economy or the needs arising from the state's growing population, and that Western Australia fares poorly in comparison with other jurisdictions.

Given the above, it is essential that the state's infrastructure is implemented as a result of strong planning and management by government. It is acknowledged that political decisions will be made on major projects for the advancement of the state and that internal government jostling will continue. These realities make robust government planning and management all the more important.

Due to the importance of infrastructure, the amount of public money invested in it, and the necessity of rigorous planning to effectively meet the state's infrastructure needs, the Committee determined to inquire into the robustness of planning processes for major infrastructure projects, including funding options for these projects.

1.2 Inquiry Process

On 25 November 2009 the Committee resolved to conduct an inquiry into the best approaches to decision making for major infrastructure projects in Western Australia.

(a) Evidence Gathering

An advertisement calling for submissions was placed in *The West Australian* newspaper on Saturday 12 December 2009. Submissions were also invited from a number of state government agencies. In addition to this, evidence was taken by the Committee in a series of briefings and hearings from relevant stakeholders. In total, the Committee:[14]

- received 33 submissions;

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12 Government of Western Australia, *2009–10 Annual Report on State Finances*, p.1.

13 Department of Treasury and Finance, *2010–2011 Budget Overview*, Government of Western Australia, Perth, 2010, p.8.

14 Lists of submissions, hearings and briefings are provided in Appendices One, Two and Three.

- conducted documentary research;
- held 13 formal public evidence hearings;
- received a range of briefings from relevant stakeholders; and
- attended the *WA Major Projects Conference 2010: Securing the State's Economic Future*, which was held in Perth on 29–30 March 2010.

(b) Project Selection

The Committee chose to examine a number of projects and selected those that provide a sample of infrastructure types, contracting models, and regional and metropolitan locations. Examination of these selected projects allowed the Committee to gain a better understanding of how infrastructure decisions are made, the planning processes in place and the work required of agencies to comply with those processes. While the Committee selected individual projects, it was not the Committee's intention to audit these projects or the associated contracts or other related agreements. As the terms of reference indicate, the purpose of the Inquiry was to investigate planning and funding of the state's infrastructure to ensure its delivery in a way that increases certainty, provides value for money and minimises risk to Western Australia.

A number of factors impact upon infrastructure funding in general, and major resource infrastructure in particular, including highly complex legislation and formal agreements at both state and federal levels. This report, though, is largely concerned with funding in the context of the Strategic Asset Management Framework (SAMF) process, and how adherence to that process can improve public sector asset management and ensure a value for money outcome for infrastructure procurement in this state.

CHAPTER 2 FUNDING AND FINANCING WESTERN AUSTRALIAN INFRASTRUCTURE INVESTMENT

2.1 Background

Governments provide public infrastructure for a number of reasons, namely in situations of natural monopoly, for the provision of public good, to subsidise services or to provide fiscal stimulus. Such provision necessarily 'involves the interrelated activities of investment, funding and financing'.[15] This interrelation is clearly demonstrated by the following Productivity Commission Statement:

> *Use of capital funds is sustainable when investment is undertaken for projects that ensure the solvency of the service provider. This means that the project must yield more than it costs in net present value terms and thus increase net worth. Public infrastructure investments that require public funding (the costs exceed the revenue flow) will be assessed by the market based on the government commitment to the funding. This will be affected by the nature of the financing vehicle as well as views on sovereign risk. It may or may not be influenced by the characteristics of the infrastructure investment itself.*[16]

Clearly, as Brealey, Cooper and Habib state, the criteria for public sector investment 'cannot be identical to those for private-sector investment for … government intervention in the economy is motivated by the very limitations of the criteria for private-sector investment'.[17] The balance of this section explores the interrelated issues of funding and financing of infrastructure projects, and provides an outline of selected significant infrastructure projects.

(a) Why Governments Fund Infrastructure

The private sector, by definition, operates to make a profit. For the private sector to consider providing or delivering a service that requires infrastructure, there must be a market operating that will provide a return on investment. Positive returns on investment can only occur when the real costs of the infrastructure investment can be passed on to consumers. For the private sector to be involved in the road, water or electricity markets, consumers would have to bear the full costs of delivering roads, water or electricity respectively.

The difficulty of providing infrastructure on a commercial basis is a significant issue in Western Australia where the geographical spread of the population often requires subsidisation of the cost of providing essential services such as electricity and water. Because user charges currently levied

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15 Chan, Chris, Forwood, Danny, Roper, Heather and Sayers, Chris, *Public Infrastructure Financing: An International Perspective*, Staff Working Paper, Productivity Commission, Melbourne, March 2009, p.11.

16 ibid., pp.13–14.

17 Brealey, R, Cooper, IA and Habib, MA, 'Investment Appraisal in the Public Sector', *Oxford Review of Economic Policy*, vol. 13, no. 4, 1997, p.18 of pp.12–28 as cited in Chan, Chris, Forwood, Danny, Roper, Heather and Sayers, Chris, *Public Infrastructure Financing: An International Perspective*, Staff Working Paper, Productivity Commission, Melbourne, March 2009, p.12.

on consumers for those services do not cover the real costs of service provision, a community service obligation (CSO) is paid by government to utility providers to cover the shortfall.

(b) Government Financing of Infrastructure

There are two key financing vehicles available to government—pay-as-you-go and capital-market financing. Options for generating public funds for infrastructure projects generally include:

- *current operating incomes from the collection of taxes and service charges;*
- *special levies such as development contributions;*
- *reserves set aside for general or specific investment purposes;*
- *proceeds from asset sales; and*
- *intergovernmental transfers such as federal and provisional grants.*[18]

Capital market financing options include borrowing or equity contributions from the private sector.

Decisions about which finance vehicle is appropriate are affected by various factors including:

- *infrastructure characteristics, which affect an asset's revenue raising capacity and user profiles;*
- *fiscal and macroeconomic conditions restricting the use of some financing options;*
- *institutional arrangements determining how public infrastructure assets are operated and financed; and*
- *perceptions of the role of government and the resultant views as to how government should be involved in the delivery of services and managing the economy.*[19]

The most often-used financing vehicle for the states and Territories is budget appropriations, with 63 per cent of public infrastructure in Australia financed by this means, while off-budget financing through Government Trading Enterprises (GTEs) represents 32 per cent of public infrastructure funding, with public private partnerships (PPPs) providing the balance of five per cent.[20]

General budget appropriations provide opportunity for increased political scrutiny and monitoring, which, in turn, makes government financing relatively transparent and accountable. There are, however, disadvantages such as the potential for 'fund diversion creating cash flow constraints on

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18 Chan, Chris, Forwood, Danny, Roper, Heather and Sayers, Chris, *Public Infrastructure Financing: An International Perspective*, Staff Working Paper, Productivity Commission, Melbourne, March 2009, p.20.

19 ibid.

20 ibid., p.21. Note that Victoria relies less than other states on off-budget financing through GTEs due to the privatisation of its electricity GTEs.

efficient development of the infrastructure asset', and the possibility of reduced incentives for exploring user charges, or other efficiency measures.[21]

Off-budget financing through GTEs also has advantages and disadvantages. The capacity of GTEs to generate revenue through user charges makes them well placed to provide infrastructure with considerable public good characteristics. GTE borrowing also 'places limits on discretionary use of cash flows, and enhances scrutiny and discipline on investment and financing decisions'.[22] Set against these advantages is the possibility that budget processes intended to improve accountability and transparency of capital expenditure may be bypassed because the reporting requirements for GTEs are different from general government agencies.

(c) Public Private Partnerships

In line with developments internationally, PPPs have become an increasingly popular method by which Australian governments have sought to procure and provide public infrastructure and associated services. This trend is reflective of the potential benefits that can be derived as a result of engaging the private sector in the provision of public goods and services. Primarily, and in the right circumstances, PPPs have the capacity to provide significant value for money to taxpayers as a result of cost savings and other efficiencies offered by private sector expertise, and importantly, through the identification and allocation of risk to the PPP partners.[23] The advantages and disadvantages of PPPs are discussed in more detail in Chapter 8.

2.2 Overview of Selected Projects

The following section presents an outline of the selected major Western Australian infrastructure projects examined by the Committee. The selection has provided the Committee with the opportunity to sample a range of infrastructure types and contracting models across regional and metropolitan locations. An examination of the funding and financing arrangements for these projects suggests that Western Australia reflects the national situation in which the most often-used financing vehicle is budget appropriations, followed by off-budget financing through GTEs, with PPPs providing a relatively small proportion.

(a) Oakajee Port Project

The construction of a deep water port at Oakajee was proposed in the 1990s to provide access for iron ore projects in the Mid-West. However, the collapse of the Kingstream iron and steel project stalled the development of the port until the early 2000s when it was revisited with a view to building a rail network and port to serve a number of smaller iron ore projects for which the development of individual infrastructure would be commercially unviable.

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21 ibid. The Productivity Commission's working paper explores these issues in greater detail.

22 ibid., p.91. The productivity Commission's working paper notes the discipline on decisions may be reduced if borrowing decisions are made through a central agency rather than individual GTEs.

23 Webb, R, and Pulle, E, 'Public Private Partnerships: An Introduction', *Research Paper No. 1 2002–03*, 24 September 2002. Available at: http://www.aph.gov.au/library/pubs/rp/2002-03/03RP01.pdf. Accessed 31 March 2009.

When the state government completed the formal request for proposal documentation for the right to build the Oakajee deep water port, the construction was proposed to be fully funded by private investment.[24]

Following the 2008 election, support for the project continued; however, instead of being a privately funded port, it was now to receive substantial government funding. The state government has now committed to contributing to the common use infrastructure (CUI) at the port. In support of this decision, Premier Barnett argues that:

> *Oakajee is about far more than iron ore. The region is rich in a variety of natural resources and the port will provide an important stimulus to the establishment of a new mining-based industry in the region, the economic spin-offs of which cannot be underestimated. The building of a world-class industrial estate adjacent to the port and the development of rail infrastructure will also allow us to take a further step towards economic maturity. It will provide the opportunity to finally make more of our natural resources through value adding. Western Australia has lacked a site for sophisticated processing of our vast reserves of mineral and gas resources. Oakajee is a chance to build something that this state does not have; namely, an industrial estate adjacent to a deep water port, close to an established city in a resource-rich region. It provides the opportunity to attract our customers, mainly manufacturing companies, which can bring some of their production capacity to Western Australia to transform our natural resources into higher value products. As such, it will finally enable us to broaden our economy from the selling of raw materials to the production and export of a wider range of processed and semi-processed products. Oakajee will provide Western Australia with a more sophisticated future with a wider range of industry and employment.*[25]

According to the Department of State Development (DSD):

> *the government has made the decision that the common-user infrastructure requires government funding. That reflects the nature … of the unique opportunity that is created by opening up the Mid West to development, and the challenges and complexities associated with many, many, potential miners and the requirements for major infrastructure to make that happen.*[26]

In relation to differences between the privately and publicly funded iterations of the CUI, DSD advised that:

> *the design and operation of the common use infrastructure (CUI), including the breakwater, turning basin and other infrastructure, provides for genuine third party access and the capability to develop the port as a multi-user, multi-function port over time.*[27]

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24 Hon. Alannah MacTiernan, MLA, (then Minister for Planning and Infrastructure), Media Statement, 27 February 2008; 'Oakajee Port moves Closer Towards Development' *Mining News*, 27 February 2008.

25 Hon. Colin Barnett, Premier, MLA, Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 10 March 2009, p.1503.

26 Ms Anne Nolan, Director General, Department of State Development, *Transcript of Evidence*, 5 March 2010, p.18.

27 Submission No. 32 from Department of State Development, 3 September 2010, pp.2–3.

A reasonable conclusion to draw from this is that Premier Barnett has a broader vision for the Oakajee CUI, requiring a variation to the infrastructure plan, with the government to contribute directly to the project funding.

Following the government's policy decision to invest in the CUI, the *2010–11 State Budget Papers* show $678 million as the total government investment in the Oakajee Port project, with $339 million to be provided by both the Commonwealth and state governments for the CUI component.[28] Oakajee Port and Rail Pty Ltd (OPR) is the nominated infrastructure provider for the project and is contributing $160 million over 12 months for detailed studies and planning for the development of the Bankable Feasibility Study (BFS).[29]

The Commonwealth contribution was announced in May 2009 as part of the Building Australia Fund.[30] Negotiations have yet to be finalised and it has not been determined whether the $339 million contribution is capped.[31] This will depend on the analysis of the BFS.

The Commonwealth's contribution will take the form of an equity injection, that is, the Commonwealth would effectively 'have an ownership stake' and expect its investment to be 'ultimately commercial'.[32] The terms and conditions of this arrangement are yet to be finalised, with the state government, Infrastructure Australia (IA) and the Commonwealth Department of Infrastructure, Transport, Regional Development and Local Government (DITRDLG) currently discussing potential ownership structures.[33]

As with all projects developed from a government vision, the Oakajee Port project is based on an assessment of current and potential market demand which is very much dependent on the price for iron ore. All such projects necessarily contain an element of risk due to the possibility that the market could change or the vision of new industries may not come to fruition.

(b) Perth Police Complex

The Perth Police Complex (PPC) will replace the existing Central Metropolitan Complex and the East Perth Watch House with a purpose built facility. The PPC was proposed in response to the poor state of the existing Watch House, which was inadequate as a modern policing facility. Curtin House, the location of the current Perth Police Station, is overcrowded and does not provide the level of facilities required for a major police station.

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28 Department of Treasury and Finance, *Budget Statements, Budget Paper No. 2, Volume 1, 2010–11 Budget*, Government of Western Australia, Perth, 20 May 2010, p.133; and Ms Gail McGowan, Deputy Director General, Department of State Development, *Transcript of Evidence*, 5 March 2010, p.6.

29 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.5 and p.10.

30 Ms Gail McGowan, Deputy Director General, Department of State Development, *Transcript of Evidence*, 5 March 2010, p.3.

31 Ms Anne Nolan, Director General, Department of State Development, *Transcript of Evidence*, 5 March 2010, p.15.

32 ibid., p.16 and p.17. See also: Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.10.

33 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.10; and Mr Michael Deegan, Infrastructure Coordinator, Infrastructure Australia, *Committee Briefing*, 18 August 2010.

The PPC will comprise the Perth Watch House, the Perth Police Centre (Perth Police Station, district specialist units and Central Metropolitan District Office) and a Magistrate's Court.[34] Its proximity to the Northbridge precinct and Perth CBD is viewed as yielding benefits, including optimisation of police visibility and improvements to police response times.[35]

The PPC's approved budget is $113 million and it is understood that the cost of this project will be met entirely through state government funding.[36] In late August 2010, BGC was awarded the contract for the construction of the facility, and it is anticipated it will be ready for occupation in late 2012.

(c) New Perth Bunbury Highway

The New Perth Bunbury Highway (NPBH) was constructed to provide a more efficient connection between Perth's metropolitan area and the rapidly growing South West region. The existing roads were reaching capacity and, during holiday periods, long delays and traffic jams were a regular occurrence, particularly around Mandurah. Furthermore, large sections of the existing route were not dual carriageway, which increased the risk (and prevalence) of serious or fatal motor vehicle crashes.

The NPBH comprises an extension to the Kwinana Freeway, the construction of the Forrest Highway and additional road works such as upgrades to Greenlands, Lakes and Paganoni Roads.[37] Main Roads Western Australia (MRWA) reports the project costs at March 2010 totalled $724.5 million.[38]

Originally the federal government capped its AusLink funding at $170 million, with the Western Australian Government contributing an equal amount. When the budget increased to $630 million in 2007, the federal government increased its capped funding to $330 million. The state government was responsible for the balance and for picking up any shortfall on project delivery.[39] The State's budget appropriation portion now stands at $323.5 million, plus $71 million generated by the sale of surplus MRWA land.

The highway was constructed using a 'hybrid' alliance contracting model and was opened to traffic in September 2009, three months ahead of schedule.

(d) Gateway WA

The Perth Airport and Freight Access Project is known as Gateway WA, and consists of road network improvements to support the redevelopment of Perth Airport and improve access to the

34 Submission No. 21 from Western Australia Police, 10 June 2010, p.3.

35 ibid.

36 Submission No. 21 from Western Australia Police, 10 June 2010, p.7; and Hon. Rob Johnson, MLA, (Minister for Police), Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 17 June 2010, p.5158.

37 Submission No. 2 from Main Roads Western Australia, 15 January 2010, pp.4–5.

38 ibid., p.16.

39 ibid., p.18. See also: Submission No. 22 from Main Roads Western Australia, 15 January 2010, pp.3–4.

Kewdale/Forrestfield area.[40] By 2015, traffic on the road network is projected to increase by approximately 30 per cent.[41] Many of these roads were already either at or in excess of capacity in 2007.

In the lead up to the December 2007 federal election, Labor (then in opposition) committed to contributing $350 million toward Gateway WA, provided the state government contributed an equivalent amount. The combined total of $700 million included $177 million allocated for a number of Tonkin Highway projects in an AusLink 2 application for the Perth Urban Transport and Freight Corridor.[42]

In November 2008, Western Australia made a submission to IA requesting $600 million for the project.[43] The Department of the Premier and Cabinet (DPC) submission states that 'it is proposed that the project be funded jointly by federal and state governments'.[44] It is understood that the funding split between state and federal governments is 'still to be determined' and that it 'is very much up to the commonwealth and IA how they see that funding'.[45]

According to MRWA, at the time of giving evidence there had been no 'clear indication as to … the proportion of the grant arrangements'.[46] While some jurisdictions have had projects 100 per cent federally funded, others have received funding on a shared 50 per cent basis, with Commonwealth and state governments contributing 50 per cent each. Others have required private sector funding.[47]

The State's request for funding from the Commonwealth in 2008 was not successful; however, IA did not reject the project entirely, listing Gateway WA as one of 28 projects that 'will form a "pipeline" of projects for further analysis and consideration'.[48] In November 2009 the Western Australian Government made a repackaged submission to IA, and listed this as the State's 'number one capital works priority'.[49] IA's subsequent report to the Council of Australian Governments (COAG) lists the repackaged project in its 'Real Potential' category of Competitive International Gateways projects.[50]

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40 Submission No. 3 from the Department of the Premier and Cabinet, 12 February 2010, p.17.

41 Department of Transport, *Perth Airport Transport Master Plan: Preliminary Version*, report prepared by AECOM Australia Pty Ltd, 15 March 2010, p.47.

42 Submission No. 3 from the Department of the Premier and Cabinet, 12 February 2010, p.15 and p.16; and Mr Robert Arnott, Engineer/Project Director, Main Roads Western Australia, *Transcript of Evidence*, 5 March 2010, p.6.

43 Submission No. 3 from the Department of the Premier and Cabinet, 12 February 2010, p.25. The estimated total project cost was $525 million in 2008 dollars or $600 million in outturn dollars.

44 Submission No. 3 from the Department of the Premier and Cabinet, 12 February 2010, p.25.

45 Mr Menno Henneveld, Commissioner of Main Roads Western Australia, *Transcript of Evidence*, 5 March 2010, p.6.

46 ibid.

47 ibid.

48 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.17; and Mr Menno Henneveld, Commissioner of Main Roads Western Australia, *Transcript of Evidence*, 5 March 2010, p.2.

49 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.18.

50 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities*, Australian Government, Canberra, June 2010, p.50.

As part of the 2010 federal election campaign federal Labor 'pledg[ed] to fund up to 80 per cent of the cost, up to $480 million, from 2011-12, subject to further assessment'.[51]

(e) Perth City Link–Public Transport Hub

It has been a long-held objective of successive governments to sink the railway lines at the Perth Railway Station and connect the CBD and Northbridge. Since the late nineteenth century, much of the land adjoining the railway has been under-utilised. The Perth City Link (PCL) project will be a major urban renewal project; however, most of the cost for the project results from the requirement to relocate the transport infrastructure underground, thus making available the space required for the urban renewal to take place.

The funding arrangements for the PCL project have a complicated history and are yet to be finalised. Funding is comprised of budget appropriations via state and Commonwealth funds, together with local government contributions. In October 2008, Premier Barnett wrote to the then Prime Minister, Kevin Rudd, outlining the State's 'priorities for the purposes of the National Infrastructure Audit', listing the Northbridge Link at number three.[52]

The Premier reported that $9 million of State funds had been committed and that additional funding of an estimated $263 million was required to sink the railway line to the Entertainment Centre site.[53] Mr Barnett further reported that should the government decide to sink the existing bus station, approximately $205 million in additional funding would be required.[54] The letter suggested that of the estimated $263 million, $132 million was to be contributed by the state government, with the balance sought from the Commonwealth.[55]

A funding proposal for sinking the railway line between Perth Station and Lake Street was submitted to IA in December 2008[56] and IA's report to COAG for December 2008 listed the 'Northbridge rail cutting link' as worthy of further analysis.[57] However, this project or any reference to Perth City Link–Public Transport Hub does not appear in the June 2010 IA report to COAG.

The Northbridge Link Rail Cutting project was assessed by the Australian National Audit Office as 'having a *Basic* profile with a *Strong* BCR [benefit-cost ratio], but the Office of the Infrastructure Coordinator noted the BCR was "based entirely on unconventional benefits"'.[58]

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51 Hon. Anthony Albanese, MP, (Minister for Infrastructure and Transport) and Hon. Julia Gillard, MP, (Prime Minister), *Gateway WA - Perth Airport and Freight Roads*, Media Statement, 30 July 2010.

52 Hon. Colin Barnett, MLA, Premier of Western Australia, Letter to the Prime Minister of Australia, 30 October 2008.

53 Hon. Colin Barnett, MLA, Premier of Western Australia, Letter to the Prime Minister of Australia, 30 October 2008, p.7. The Perth Entertainment Centre site is being redeveloped by its owner, Australian Capital Equity.

54 Hon. Colin Barnett, MLA, Premier of Western Australia, Letter to the Prime Minister of Australia, 30 October 2008, p.7.

55 ibid., p.8.

56 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.43.

57 Infrastructure Australia, *A Report to the Council of Australian Governments*, Australian Government, Canberra, December 2008, p.68.

58 Auditor General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No.2 2010–11 Performance Audit, Commonwealth of Australia, Canberra, 2010, p.96 and pp.108–109.

This gave rise to concerns about the robustness of the claimed BCR and led the Infrastructure Coordinator to 'conclude that the project needed to be re-analysed using a conventional economic framework'.[59]

IA assessed the project as being of insufficient merit to warrant inclusion on its Final Priority List of December 2008, but the Northbridge Rail Link was added to the list of pipeline projects by the Infrastructure Council in May 2009.[60] The Council held the view that it should be flagged as a project of interest with Infrastructure Australia.[61]

When the federal government committed $236 million through its Major Cities Project funding programme, the project was costed at $468 million.[62] DITRDLG describes the project as 'the important first stage of an urban redevelopment project for Northbridge … involv[ing] the sinking of the central city section of the Perth to Fremantle railway line and construction of a new rail platform'.[63]

In May 2009, Premier Barnett advised the Legislative Assembly that he was 'pleasantly surprised' at the Commonwealth's $236 million funding commitment for the entire project, including the new bus station, and stated that the Northbridge Link would 'still be a 50–50 project'.[64]

However, the *2010–11 State Budget* lists the Perth City Link–Transport project as having a total cost of $609.3 million.[65] According to the Department of Transport and Infrastructure, the Commonwealth contribution is $236 million,[66] while the City of Perth is contributing $25 million plus land valued in 2004 at $6 million.[67] The Committee notes that given the revised budget figure of $609.3 million, the State's contribution will now be well over 50 per cent of the total cost.

The Committee notes that the Wellington Street Bus Station (WSBS) must be relocated in order to achieve the urban renewal objectives of the PCL. The model selected for the new underground WSBS requires the installation of satellite tracking devices on all buses in the Transperth fleet, a cost not included in the PCL budget estimates.

It is understood that two proponents—City Rail Joint Venture (Brookfield Multiplex and Laing O'Rourke) and Perth City Link (John Holland and GHD)—have been short-listed for the next assessment phase of the project.

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59 ibid., p.114.

60 ibid., p.121.

61 ibid.

62 Department of Infrastructure, Transport, Regional Development and Local Government, 'Major Cities Projects', 25 January 2010.

63 ibid.

64 Hon. Colin Barnett, MLA, Premier of Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 13 May 2009, pp.3931-32. The MOU for this funding, at clause 22, discusses the need for the State to consider PPP and private sector involvement.

65 Department of Treasury and Finance, *Budget Statements, Budget Paper No. 2, Volume 2, 2010–11 Budget*, Government of Western Australia, Perth, 20 May 2010, p.445.

66 Department of Transport and Infrastructure, *Project Details. Northbridge Rail Link (The Hub) - (WA)*, 13 October 2010.

67 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.43.

(f) Ord–East Kimberley Expansion Project

The Ord–East Kimberley Expansion Project, originally a nation-building venture of the 1960s, will be expanded from the existing 14,000 ha under irrigation to include a further 8,000 ha of irrigated land.

Funding for the project has two components: an irrigation expansion project funded by the state government; and a number of housing, health and education initiatives to be federally funded.[68]

The State's funding contribution, capped at $220 million, is being allocated from the Royalties for Regions Program.[69] Mr Paul Rosair, Director General, Department of Regional Development and Lands (DRDL) explained:

> *it is a good point to note that we have a fixed budget of $220 million for the expansion. Obviously, to expand into Weaber Plains, two fundamental infrastructure items are needed: water and a road. That is the minimum requirement of the job. That then enables us to have a contingency component within the project, that if the $220 million, costed out, provides for a sealed road out to the site, or a gravel road, and the channel expanded and improved. […] If, then, there is some capacity left within the $220 million, we can look at additional infrastructure like power, telecommunications and some further on-farm infrastructure. But it is from the start a fixed allocation of $220 million that we are working within.*[70]

The federal government has committed $195 million to the project through the Nation Building Economic Stimulus Plan (the Plan).[71] This allocation is to provide 'infrastructure relating to health, aged care, early childhood development and family services, education and vocational training, social and transition housing, transport and sporting and community facilities'.[72]

In May 2010, construction of the first major component of the irrigation expansion was commenced by the Moonamang Joint Venture between Leighton Contractors and Indigenous Business Australia.[73]

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68 Mr Paul Rosair, Director General, Department of Regional Development and Lands, *Transcript of Evidence*, 5 May 2010, p.1. See also: Department of Regional Development and Lands, *Ord–East Kimberley Development Plan*, Government of Western Australia, Perth, nd.

69 Submission No. 12 from Department of Regional Development and Lands, 20 April 2010, p.1; and Mr Paul Rosair, Director General, Department of Regional Development and Lands, *Transcript of Evidence*, 5 May 2010, p.1 and p.3.

70 Submission No. 12 from Department of Regional Development and Lands, 20 April 2010, p.1; and Mr Paul Rosair, Director General, Department of Regional Development and Lands, *Transcript of Evidence*, 5 May 2010, p.3.

71 Hon. Kevin Rudd MP, then Prime Minister, in Department of Regional Development and Lands, *Ord–East Kimberley Development Plan*, Government of Western Australia, Perth, nd, p.3.

72 Hon. Gary Gray, MP, then Parliamentary Secretary for Western and Northern Australia, in Department of Regional Development and Lands, *Ord–East Kimberley Development Plan*, Government of Western Australia, Perth, nd, p.3.

73 Hon. Colin Barnett MLA, (Premier) and Hon. Brendon Grylls MLA, (Minister for Regional Development), *Construction Begins on $220 million Ord-East Kimberley Expansion Project*, Media Statement, 14 May 2010.

(g) Australian Marine Complex

The Australian Marine Complex (AMC) was first proposed in the late 1990s as the 'Jervoise Bay Project' following the implementation of then federal Defence Minister Kim Beazely's 'two oceans policy', and the expansion of HMAS Stirling at Garden Island as a major fleet base. The AMC comprises two separate projects, planned and delivered at different times. The Jervoise Bay Project was opened in 2003 as the Australian Marine Complex–Common User Facility (AMC–CUF).

The total cost of the AMC–CUF was $180 million, with funding coming from both state and federal governments. The Commonwealth's Federation Fund contributed $80 million and the State provided the balance.[74]

The state government initially agreed to provide $90.1 million in funding for the Upgrade Project from the following sources:

- $81.1 million from the Department of Treasury and Finance (DTF) paid to LandCorp as an equity injection;
- $5 million from the Australian Submarine Corporation; and
- $4 million from the Royal Australian Navy.

Following revised costings the state government 'agreed to support the infrastructure upgrade providing the tender cost [did] not exceed $174.3 million'.[75] However, the total project costs were later revised to $170.3 million as the Royal Australian Navy capital contribution was not forthcoming.[76] In all, 'about half a billion dollars has been invested in the project, with some of that recouped through land sales revenue'.[77]

The AMC was based on a development vision that has now been realised. The 'economic benefit' derived from work completed at the AMC has steadily increased, and for 2009 was in excess of $350 million.[78]

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74 Mr John O'Hare, General Manager, Marine and Defence, Department of Commerce, *Transcript of Evidence*, 23 June 2010, p.5; and Submission No. 23 from Department of Commerce, 2 June 2010, p.8.

75 Submission No. 23 from Department of Commerce, 2 June 2010, p.5.

76 Submission No. 23 from Department of Commerce, 2 June 2010, p.5; and Mr John O'Hare, General Manager, Marine and Defence, Department of Commerce, *Transcript of Evidence*, 23 June 2010, p.5.

77 Mr Ross Holt, LandCorp, *Transcript of Evidence*, 23 June 2010, p.6. This figure is comprised of the $180 million for the AMC–CUF, $170.4 million for the AMC–CUF Infrastructure Upgrade project, approximately $14 million for development of the technology park facility, and the provision of land and of amenity upgrades by LandCorp, together with $35 million in support for a load-out facility for Chevron's Gorgon project.

78 Submission No. 23 (Attachment A) from the Department of Commerce, 2 June 2010.

(h) Ravensthorpe Nickel Operation

In 2001 BHP Billiton (BHPB) acquired the laterite ore deposit of the Ravensthorpe Nickel Operation (RNO) and in 2004 'agreed to progress the RNO to full construction and operation'.[79] BHPB looked to domicile most of its workforce locally in Ravensthorpe and Hopetoun, and entered into negotiations with the state and local governments in relation to the infrastructure required to support the expanded population.

The state government signed a Memorandum of Understanding (MOU) with BHPB for the delivery of the Multi-User Infrastructure Package (MUIP) to provide 'immediate improvements to the infrastructure capacity within the Shire [of Ravensthorpe], as well as ensuring long-term benefits for the community through the implementation of key community infrastructure projects'.[80]

The cost of the proposed MUIP was estimated at $55 million, with $18.4 million to be provided by the state government, with the balance to be provided by BHPB and the federal government, which was asked to match state funds.[81]

The final sources of funding were:

- $9.8 million from the federal government;[82]
- $18 million from the state government;
- $6.1 million from agency budgets; and
- $9.5 million from BHPB.[83]

These figures do not include the arrangements made between BHPB and the Shire of Ravensthorpe for the operation of the airport, for payments in lieu of shire rates and for payments to a Community Development Fund. It is understood that BHPB agreed to:

- underwrite the airport facility 'to a maximum of $40,000 per annum';
- enter into a rate deed whereby the annual payment to the Shire was $240,000 (indexed); and to
- contribute $120,000 annually (indexed) to the Community Development Fund.[84]

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79 Submission No. 20 from Department of State Development, 3 June 2010, p.1.

80 ibid., pp.1-2.

81 ibid., p.2.

82 ibid., p.3. This funding was provided to the Shires of Esperance and Ravensthorpe for upgrading local roads and the Ravensthorpe community facilities.

83 ibid., pp.3–4. This does not include the Esperance Port Authority's $31 million capital works programme.

84 ibid., p.6.

The RNO was closed and placed on care and maintenance in January 2009, resulting in significant cost to the community and local businesses, and the under-utilisation of the infrastructure already built by government. In December 2009 BHPB sold the mine to a Canadian firm which is proposing to reopen the mine. [85]

(i) Bunbury to Albany Gas Pipeline

The Bunbury to Albany Gas Pipeline project was a 2008 election commitment made by then Opposition Leader, Hon. Colin Barnett, MLA. At the time of this Inquiry, it was not clear what the project's capital cost would be or how the project would be funded. However, in August 2008 Mr Barnett 'pledged to build a natural gas pipeline from Bunbury to Albany' for an estimated cost of $225 million.[86]

Mr Barnett stated that the pipeline 'would be funded by a partnership between the public and private sector'.[87] In October 2008, the Minister for Energy, Hon. Peter Collier, MLC, said that 'while the project will be funded by the Government', he would 'consider privatising the pipeline once it is built'; 'ultimately', he said, 'it will pay for itself'.[88] However, the Committee is not aware of any cost-benefit analysis (CBA) having yet been undertaken.

The Minister for Energy indicated that the $225 million cost for the project was 'fairly accurate'.[89] However, Ms Gail McGowan, Director General, DSD, advised that the department was not aware of the year in which the $225 million figure was based, confirming that:

- the 'figure was nominated in the election commitment with no further analysis on that costing';
- current dollar costs had not been updated; and
- it is 'anticipate[d] the indicative costings will be worked on' when the pipeline route is finalised. [90]

The *2010–11 State Budget Papers* show that $20 million has been allocated toward this project from the Royalties for Regions programme. When asked whether Commonwealth funding might be available, Ms McGowan stated that 'it is probably too early to say at this stage. We would

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85 Mills, M, 'Cursed Mine Gets Shot in the Arm', *Australian Mining*, 15 September 2010.

86 Hon. Colin Barnett, MLA, (then Opposition Leader), cited in *Libs Promise $225 Million Gas Pipeline*, Media Statement, ABC News, 23 August 2008 See also: *Bunbury to Albany Gas Pipeline a Priority: Energy Minister*, Media Statement, ABC News, 2 October 2008.

87 Hon. Colin Barnett, MLA, (then Opposition Leader), cited in *Libs Promise $225 Million Gas Pipeline*, Media Statement, ABC News, 23 August 2008.

88 Hon. Peter Collier, MLC, (Minister for Energy), cited in *Bunbury to Albany Gas Pipeline a Priority: Energy Minister*, Media Statement, ABC News, 2 October 2008.

89 ibid.

90 Ms Gail McGowan, Deputy Director General, State Initiatives, Department of State Development, *Transcript of Evidence*, 16 June 2010, p.6.

always be looking for opportunities to obtain commonwealth funding where it is reasonable to do so'.[91]

(j) Muja A and B Refurbishment

The 40 year old Muja Power Station Stages A and B (Muja A and B) are obsolete and inefficient coal fired generating units that were decommissioned in May 2007. In March 2007, Verve Energy had called for Expressions of Interest for 'future uses of the plant, and/or the site of Muja stages A and B, which [was] offered as leasehold'.

A refurbishment option proposed by Innovative Aluminium Company (Inalco) was announced by Minister Collier in May 2009, and has led to the creation of Vinalco Energy, a joint venture partnership between Verve Energy and Inalco. Verve Energy advised that the joint venture would be formed to 'refurbish, upgrade and recommission Muja A and B stations', and that 'the joint venture parties will have equal share'.[92]

Funding required for the project 'will be approximately $145 million which will cover capital expenditure, pre operating expenses and capitalised interest during construction'.[93] Inalco will provide the capital necessary for the project and, apart from some relatively small working capital contributions, Verve's contribution to the project is limited to a bank guarantee for the project cost of approximately $145 million:

> *Verve is not contributing. Aside from close to $2 million in working capital, it is assumed that if the project gets a go-ahead, it is likely that there will be a requirement to drop $2 million each party. Working capital must kick the project off with cash flow. Beyond that, there is the facility with the banks, which is about $145 million; that will be broken down to approximately $110 million in the EPC [Engineering, Procurement and Construction] contract. There will be some project funding in there. There are other bills, such as transmission access of approximately $4 million or $5 million as well, and development cost recovery going back to Inalco. That is what makes up the $145 million. Aside from a security deposit made to the IMO, Verve will not contribute to that $145 million; it will be project funded.*[94]

The project was described by Verve Energy's Chief Executive Officer in May 2010 as being 'on time', with due diligence 'currently underway'.[95]

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91 ibid.

92 Submission No. 13 from Verve Energy, 22 April 2010, p.1; and Mr Antonio Narvaez, General Manager, Strategy and Business Development, Verve Energy, *Transcript of Evidence*, 5 May 2010, p.2.

93 Submission No. 13 from Verve Energy, 22 April 2010, p.2.

94 Mr Antonio Narvaez, General Manager, Strategy and Business Development, Verve Energy, *Transcript of Evidence*, 5 May 2010, p.5.

95 Ms Shirley Int'Veld, Advisor to the Minister Representing the Minister for Energy, Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 3 June 2010, p.508.

(k) Mid-West Energy Project Stage 2

Western Power's proposed expansion of the power transmission network in the Mid-West is planned for implementation in two stages. Stage 1 is a 330 kV network from Pinjar to Eneabba, with a feeder line to the proposed Karara iron ore mine, underpinned by increasing demand for energy from this iron ore project.

The second stage is intended to address supply constraints affecting Geraldton and is reliant on the successful completion of stage one.[96] The Mid-West coast is also considered a prime location for the placement of wind turbine farms, which require sufficient transmission capacity to connect to the network.

The Mid-West Energy Project Stage 2 consists of the extension of the 330kV network from Eneabba to Geraldton, the Mid-West's major regional centre.[97]

Stage 2, which is dependent on Stage 1 proceeding, was submitted to IA for funding under the 'Creation of a True National Energy Market' theme. IA lists 'Mid-West Energy–Stage 2' as an initiative that has 'Real Potential' and shows the total value of the project is $795 million, which is understood to include Stage 1 and a private investment component.[98]

(l) Collie to Perth Transmission Reinforcement Project

The proposed Collie to Perth transmission reinforcement project is a 330kV Power Line designed to increase the capacity of the South West Interconnected System which supplies the majority of electricity to the South West region of the state.[99] While the detailed estimate of the project costs was reviewed in 2009, this information is commercial-in-confidence.[100]

It is understood that the project has the potential to facilitate the development of renewable energy generation, and it is possible that it may fit IA's 'True National Energy Market' objective.[101] However, due to uncertainty surrounding investment in new generation capacity in the South West, the project is currently on hold.

2.3 Concluding Remarks

It is clear that in Western Australia there is a diverse range of infrastructure projects, many of which have highly complex design, delivery and funding requirements. Given this complexity, and the factors impacting upon the infrastructure investment needs of the state, there is the potential for increased levels of project-related risks.

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96 Closed Submission No. 10 from Western Power, 19 April 2010, p.7.

97 ibid., p.3.

98 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities*, Australian Government, Canberra, June 2010, p.50.

99 Closed Submission No. 11 from Western Power, 20 April 2010, p.3.

100 ibid., p.10. The Committee determined to maintain the commercial-in-confidence status of the project cost estimates.

101 ibid., pp.13–14.

While the Committee has not undertaken a complete analysis of the selected infrastructure projects, its examination of various projects has revealed a number of factors that contribute to achieving a value for money outcome for any infrastructure project. These include, but are not limited to, the importance of:

- long-term planning;
- well-developed business cases;
- selecting appropriate contract and funding models;
- ensuring effective risk management strategies are in place

It is therefore important that government appreciates the importance of developing, implementing and evaluating suitably rigorous policy and procedures for the planning and provision of infrastructure throughout the state. The Western Australian Government is currently undertaking a programme of works reform and is refining the Strategic Asset Management Framework (SAMF), which is the endorsed policy for the management of infrastructure projects by government agencies in Western Australia.

The balance of this report examines these issues in more detail.

CHAPTER 3 THE STRATEGIC ASSET MANAGEMENT FRAMEWORK

3.1 Origin of the Strategic Asset Management Framework

The Strategic Asset Management Framework (SAMF) is the endorsed policy of the Western Australian Government in relation to the management of infrastructure provision by government agencies. It consists of 11 policies and guidelines which have been designed to improve asset management and capital investment in the public sector.[102]

SAMF arose from recommendations in the Functional Review Taskforce established by the Gallop Labor Government in July 2002 and was rolled-out in August 2005.[103] The previous set of policies relating to asset management were developed in the mid-1990s, and it has been noted that during the intervening years the quality of strategic asset management had declined—an outcome the implementation of SAMF was intended to reverse. [104]

SAMF covers assets at each stage of their life cycle from planning and delivery through to ongoing maintenance and disposal. The importance of asset maintenance and disposal is acknowledged, particularly for ensuring value for money; however, this report focuses on assets in the first two stages identified in SAMF, namely planning and delivery.

The current state government's Works Reform Program (Works Reform) has driven a more robust implementation of SAMF and involves the realignment of agencies and the provision of resources to them.

3.2 Coverage of the Strategic Asset Management Framework

(a) SAMF Requirements

SAMF is intended to be applied by 'general government agencies, public financial corporations and public non-financial corporations'.[105] Public Non-Financial Corporations include agencies like the Public Transport Authority, the various Port Authorities around the state and Government Trading Enterprises (GTEs), including Western Power, the Water Corporation and Synergy.[106] Public Financial Corporations include the Western Australian Treasury Corporation and

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102 Department of Treasury and Finance, *Strategic Asset Management Framework Overview*, August 2005, p.1. Available at: http://www.dtf.wa.gov.au/cms/uploadedFiles/00_samf_overview_082005.pdf. Accessed on 3 August 2010.

103 Hon. Geoff Gallop, MLA, Premier, Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 25 February 2003, p.4552.

104 Mr MG Bradshaw, Representing the Minister for Housing and Works, Western Australia, Legislative Assembly, *Estimates Hearings* (Hansard), 10 June 2005, p.495.

105 Department of Treasury and Finance, *Strategic Asset Management Framework for Western Australian Public Sector Agencies*, August 2005, p.1.

106 Department of Treasury and Finance, *2010–11 Budget: Economic and Fiscal Outlook, Budget Paper No. 3*, May 2010, p.188.

RiskCover.[107] In effect, all public sector agencies and organisations are identified as being subject to the asset acquisition guidelines contained in SAMF.

There are some exceptions to the requirement for agencies to follow SAMF, and the way in which these exceptions are presented in policy documents may lead to some confusion. Agencies required by legislation to produce Statements of Corporate Intent (SCI) and Strategic Development Plans (SDP) are not required to produce Strategic Asset Plans (SAPs).[108] There is, however, an expectation that they adopt key elements of SAMF in meeting their statutory obligations.[109] There is some ambiguity as to whether agencies that produce SCI and SDP are exempt from the totality of SAMF or simply from the requirement to produce a SAP.[110]

(b) Government Trading Enterprises and SAMF

Evidence suggests that GTEs do not follow SAMF when managing their own asset acquisitions,[111] but it is not clear that this has caused sub-optimal outcomes in relation to asset acquisition. Mr Richard Mann, Executive Director of Department of Treasury and Finance's Strategic Projects business unit (DTF-SP), noted that many GTEs 'tend to be very well advanced in asset management', to the extent that they are 'more advanced' than their counterparts in the non-residential building portfolio.[112] The inconsistency between the general government sector and the GTE sector was one catalyst for the introduction of Works Reform (see section 3.5).[113]

As a general principle, policy consistency across government is a desirable outcome, and ensuring that GTEs are covered by and follow the requirements of SAMF may be a worthy objective. It is not always clear, however, that change for consistency's sake is always worthwhile, especially where there is broad agreement—and evidence—that existing structures are achieving excellent outcomes.

Western Power, for example, reports that in the 2008–09 financial year over 90 per cent of capital projects were delivered ahead of schedule and under budget,[114] and the Water Corporation has been identified as an organisation that manages its asset acquisition professionally.[115]

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107 ibid.

108 Department of Treasury and Finance, *Strategic Asset Plans*, August 2005, p.3.

109 ibid.

110 Department of Treasury and Finance, *Strategic Asset Management Framework for Western Australian Public Sector Agencies*, August 2005, p.1.

111 Ms Josephine Quealy, Program Manager, Economic Audit Implementation Unit, Department of Treasury and Finance, *Briefing*, 10 August 2010.

112 Mr Richard Mann, Executive Director, Department of Treasury and Finance-Strategic Projects, *Transcript of Evidence*, 18 June 2010, p.11.

113 ibid.

114 Western Power, *Annual Report 2009*, p.13.

115 Richard Mann, Executive Director, Department of Treasury and Finance-Strategic Projects, *Transcript of Evidence*, 18 June 2010, p.11; and Ms Josephine Quealy, Program Manager, Economic Audit Implementation Unit, Department of Treasury and Finance, *Briefing*, 10 August 2010.

In addition to normal business planning processes, some GTEs, including Western Power, are subject to further regulatory planning requirements. Western Power, for example, is subject to the New Facilities Investment Test (NFIT), a methodology applied by the Economic Regulation Authority to assess that the agency is planning to construct the right asset 'at the right time and [for] the right price'.[116]

This additional regulatory test, adjudicated by an independent body, builds in a level of robustness to Western Power's planning that may be lacking from agencies that do not share this regulatory requirement. Although Western Power does not follow SAMF, a review of the documentation associated with the proposed Mid-West Energy Project and the Collie to Perth Transmission Reinforcement Project indicated that Western Power's asset planning process is similar to SAMF.

Although the Economic Audit Committee's recommendation that GTEs be covered by the requirements of SAMF is acknowledged,[117] the following extract from DTF-SP's submission should be noted:

> *whilst the existing suite of SAMF policy and guideline documents is intended for application to all public sector infrastructure types, the current drafting (particularly detailed guidelines) is tailored to asset management of non-residential buildings. The SAMF review will produce revised documents that are better aligned to the full range of infrastructure types and therefore more readily applicable by all Government agencies.*[118]

Finding 1

Government Trading Enterprises are not currently required to comply with the Strategic Asset Management Framework. Their compliance with the framework was a recommendation of the Economic Audit Committee. The government is yet to respond publicly to this recommendation.

3.3 A Robust Framework

SAMF is generally regarded as a robust framework for the management of government asset acquisitions.[119]

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116 Closed Submission No. 10 from Western Power, 19 April 2010, p.18.

117 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.97, Recommendation 19: 'Require all investment decisions by State Government agencies, including GTEs, to be reviewed by the DTF to assess compliance with Strategic Asset Management Framework principles prior to submission to Cabinet'.

118 Submission No. 16 from Department of Treasury and Finance Strategic Project, 31 May 2010, p.4.

119 Mr Richard Mann, Executive Director, Department of Treasury and Finance-Strategic Projects, *Transcript of Evidence*, 18 June 2010, p.4, and. Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.5.

Nevertheless, the Under Treasurer Tim Marney noted that the Department of Treasury and Finance (DTF) had contributed to SAMF's shortcomings as it had failed to ensure that the policies were properly implemented by lead agencies.[120] DTF-SP elaborated on this view:

> *Over time, the pattern of Government investment decision making on major new non-residential building projects without business cases has lead to a culture within the public sector that undervalues the importance of business cases as the basis for investment decision-making. This has been to the detriment of high-quality project planning.*[121]

Other reviews of asset management in Western Australia have found SAMF to be an adequate and robust policy framework. The Economic Audit Committee (EACR) made several recommendations relating to the application and scope of SAMF rather than changes to the actual policies contained within it.[122] Similarly, DTF's *Works Reform Business Solution Plan* notes that:

> *over many years, the SAM Framework has been poorly adhered to, which has led to poorly articulated planning documents that have failed to address the objectives of each phase.*[123]

Diagram 3.1 provides an overview of the SAMF process together with details of other processes that are intended to run concurrently with SAMF. Readers may find it useful to refer to the diagram in later sections, as the report has been constructed to reflect the stages in the SAMF process.

Finding 2

The Strategic Asset Management Framework is generally accepted as a robust foundation for asset management in Western Australia. Shortcomings in project planning and delivery have tended to be the result of failures to ensure adherence to the framework.

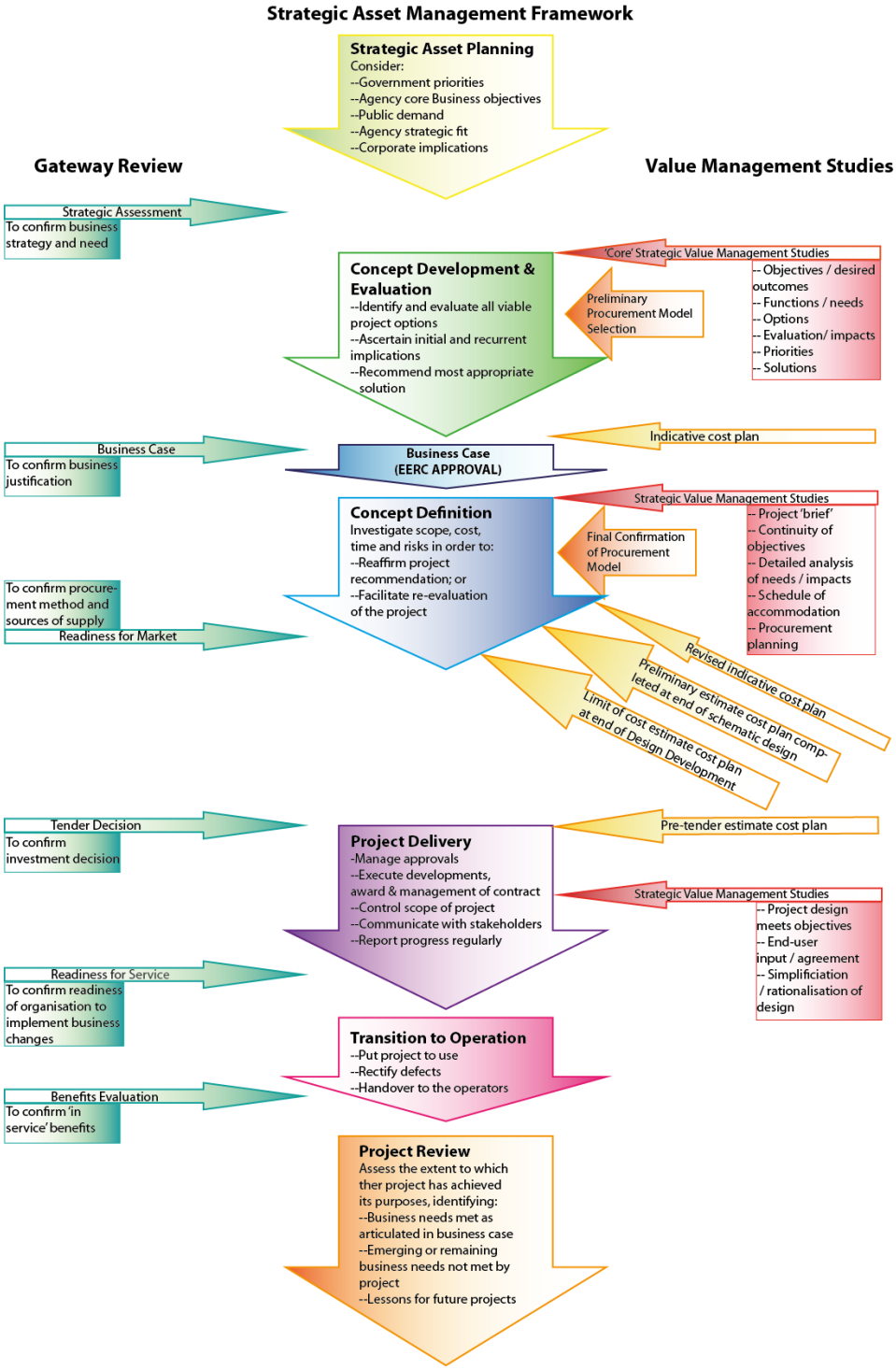
120 ibid.

121 Submission No. 16 from Department of Treasury and Finance Strategic Project, 31 May 2010, p.3.

122 Economic Audit Committee, *Putting the Community First: Partnering with the Community and Business to Deliver Outcomes*, October 2009, pp.97–101.

123 Department of Treasury and Finance, *Works Reform Business Solution Plan*, June 2009, p.15.

Diagram 3.1: SAMF and Associated Project Development Processes[124]



[124] Adapted from Department of Treasury and Finance SAMF guidelines.

3.4 Asset Planning

SAMF requires agencies to develop Strategic Asset Plans (SAPs) in which the capital investment, maintenance and asset disposal arrangements for an agency are detailed across a ten-year period.

Agencies must identify the ideal mix of assets and other resources required to best support the agency's delivery of core services, and must conduct regular evaluations to determine the extent to which its assets continue to support service delivery.

The evaluation process determines whether assets are under-performing and whether they remain fit for purpose, and includes evaluating the:

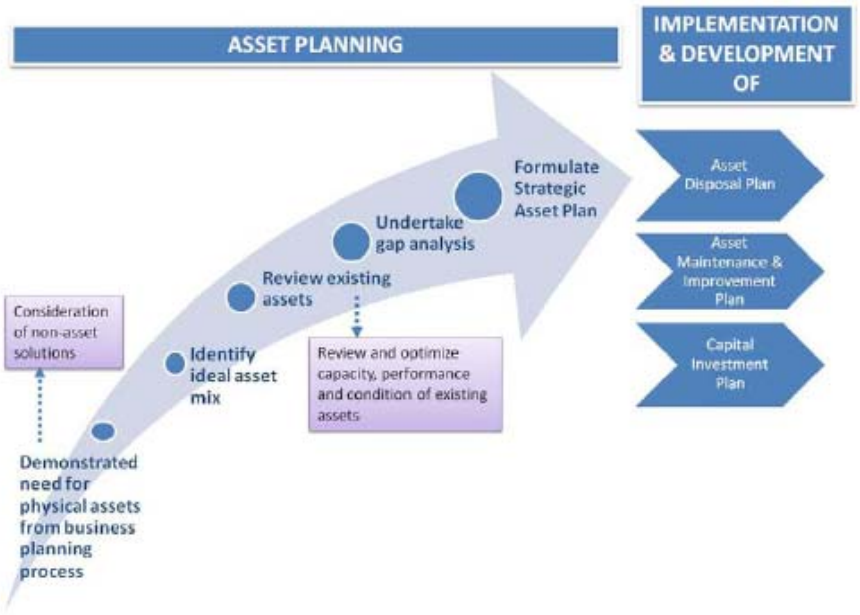
- relevance of the asset(s) to the agency's future service delivery needs;
- performance of the asset in supporting current service delivery;
- areas that need improvement;
- options for improving performance; and
- options that should be selected.[125]

Evaluation should also include a prediction of the future performance of assets with a view to assisting long-term planning outcomes.

If shortcomings in the agency's asset portfolio become apparent, SAMF requires the agency to undertake a gap analysis to quantify the extent to which the existing asset portfolio is suitable for the delivery of the services that the assets are intended to support. Agencies are encouraged to consider non-asset solutions—which may include redeployment of resources, changes to service delivery and the renovation of existing assets—to maximise the value for money outcome for the State and minimise the risk that assets will be constructed unnecessarily. A summary of the asset planning process is contained in Diagram 3.2 below.

[125] Department of Treasury and Finance, Strategic Asset Plans, August 2005.

Diagram 3.2: Asset Planning Workflow[126]



3.5 Proceeding with Capital Investment

(a) Capital Investment Plans

SAMF requires agencies to undertake a five-stage process for capital investment, which involves the development of a Capital Investment Plan in which agencies identify both short- and long-term capital investment priorities, and outline proposed expenditure on buildings, plant and equipment, engineering, information technology and vehicles.

There is no requirement for the assets identified in the Capital Investment Plan to be scoped in detail; rather, broad project concepts are provided to be 'tested for organisational relevance, and financial, social and economic justification, as far as seven to 10-years ahead'.[127] DTF reviews the Capital Investment Plans and advises the [Economics and] Expenditure Review Committee[128] on the financial implications of the plans.

(b) Concept Development and Evaluation

Concept development and evaluation is critical in influencing the final cost over the life of the project, and will usually occur around five or six years before delivery of an asset. Agencies have an opportunity to adopt a number of approaches to meet service delivery needs and they are again

126 Department of Treasury and Finance, *Works Reform Business Solution Plan*, June 2009, p.13.

127 ibid.

128 The Expenditure Review Committee (ERC) has since been replaced by the Economics and Expenditure Review Committee.

encouraged to consider non-asset solutions at this stage of the process. Chapter 5 examines concept development in the context of the projects reviewed in the course of this Inquiry.

Running concurrently with concept development is the project evaluation stage. Here the types and levels of risk should be identified in order to select the preferred option in terms of its efficiency and effectiveness, budgetary implications, costs and benefits to the society as a whole, and the impact on unquantifiable social factors.

DTF's *Project Evaluation Guidelines* provide detail as to the requirements for project evaluation, including the role of cost-benefit analysis (CBA), the aim of which is to compare:

> *[t]he quantifiable benefits that accrue, as a result of the project, with the costs of finance and other resources devoted towards the project (e.g. the labour employed). These costs are known as the opportunity cost of government funds and resources. The focus is on the economic efficiency of the allocation of resources, and costs and benefits are measured in terms of the economy as a whole, regardless of who the net benefits accrue to.*[129]

At this stage agencies should also consider whether the project is suitable for a Public Private Partnership (PPP) arrangement (see Chapter 8).

Agencies are expected to select the preferred option after taking into consideration the benefits, functional value, cost and their capacity to deliver an asset based on the analysis of the data. The process and results should then be documented in sufficient detail to allow for external scrutiny of the process.[130]

(c) Business Cases

Once the preferred option has been selected, agencies then develop a detailed business case for submission to DTF and subsequent approval by the Expenditure and Economic Review Committee (EERC). DTF-SP now plays a more active role in the preparation of business cases for high-risk projects as business cases are the primary tool for sound project planning, strategic assessment and investment decision making.[131]

The SAMF *Business Case Guidelines* require agencies to provide an extensive array of detail regarding the project concept, including the:

- extent of the unmet need and the demand for services underpinning the proposal;
- identified target population and benefits the project will bring to the population;
- rationale for timing of the project; and

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129 Department of Treasury and Finance, *Project Evaluation Guidelines,* August 2005, p.23.

130 Department of Treasury and Finance, *Capital Investment Policy for Project Proposals,* August 2005, p.12.

131 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.2.

- reasons why the demand can not be met by existing systems and facilities.[132]

Agencies must also demonstrate that the project can be delivered in accordance with the proposed costs and timeframes.

Business cases must include a demonstration of the quantifiable impact the project will have on the agency's outcomes and services, and a Financial Justification Statement identifying, among other things, potential risks, annual capital and operating costs over the life of the project, and the impacts upon other projects and initiatives. [133]

Additional information required includes: a Budgetary Implications Report, detailing the net impact of a project; capital and recurrent funding requirements including other funding sources considered; the results of a social impact analysis; and an agency recommendation. [134]

(d) Project Definition

At this stage, the documentation necessary for taking a project approved by the EERC through the tendering process is compiled in sufficient detail for a final decision to be made. The project definition must fit within the expenditure constraints placed by the EERC when approval was granted, and the lead agency must inform DTF of any risk that the project definition will result in project overruns.[135]

Project definition plans are intended to identify the precise functions and physical areas that will be included in the project. Concepts that were approved in the business case should be developed further, using language appropriate for contractors involved in the design and construction phases.[136] Project definition plans ideally include detail of the:

- project objectives, including its scope and any changes where there is an impact on the scope or cost of delivery;
- functional Requirements Schedule, where the main operations accommodated within the proposed building are outlined, together with the operations' relationships to one another;
- critical Time Plan and implications, incorporating definitive completion dates or implementation duration;
- accommodation schedule that allocates a name and appropriate space for each room/group of rooms;

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132 Department of Treasury and Finance, *Business Case Guidelines*, August 2005, p.2.

133 ibid., p.4.

134 ibid., p.5.

135 Department of Treasury and Finance, *Capital Investment Policy for Project Proposals*, August 2005, p.13.

136 ibid., p.14.

- site certification demonstrating that the sponsor agency has unencumbered ownership of the land on which the project is to be constructed;
- risk assessment outlining the known or anticipated risks associated with the project, including an assurance that these have been communicated to all stakeholders; and an
- updated cost plan that details the stages for cost planning in the asset acquisition process.

(e) Project Delivery

This stage centres on preparing a design solution and associated contract documentation. This is then followed by proceeding to tender, tender acceptance and construction. At this stage of the process, agencies ensure the design is finalised before *design freeze* as changes after this point may incur additional project costs.

Once the tender documents are finalised, the agency will be in possession of a pre-tender estimate and should confirm that the total budget does not exceed the authorised budget estimate. Any revision must be approved by the EERC. Once cost is confirmed to be within budget, tenders may be called.[137]

(f) Post-Implementation Evaluation

The *Capital Investment Policy for Project Proposals* requires that agencies conduct a post-implementation review on all projects over $5 million within 15–24 months of completion. This determines the extent to which the project is meeting its objectives and intended functions, and provides an opportunity to learn from major cost variations. A post-implementation review also helps to prevent 'scope creep' in future projects. [138]

3.6 Works Reform and the SAMF

The Works Reform Program (Works Reform) was introduced to address key problems with the procurement of building-related projects and programmes.[139] It is ongoing and has already had an impact on the implementation of SAMF. It is ongoing and has already had an impact on the implementation of SAMF. Work is also being undertaken by DTF to continue to refine SAMF and enhance agency compliance.

This section outlines the extent of Works Reform and its impact on SAMF and DTF as the agency responsible for the framework.

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137 Department of Treasury and Finance, *Cost Management Guidelines for Building Projects*, August 2005, p.17.

138 ibid., p.18.

139 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.85.

(a) Initial Changes

Early in 2008, the Office of Strategic Projects (OSP) was formed as a unit of the then Department of Housing and Works (DHW), with its Executive Director reporting to the Minister for Works.[140] The office was set up to establish a consistent and comprehensive approach to managing major projects and to retain the expertise gained through the management of the New Metrorail project.

At the time of the reforms, OSP's creation it was intended to:

- address commonplace cost overruns and time delays on major government works projects; and
- improve the retention of key government project management personnel within the public service.[141]

Works Reform aims to achieve a better alignment between how SAMF is implemented and how it is *intended* to be implemented. In December 2008, the 'works' function of DHW was transferred to DTF, with the new Building Management and Works (BMW) business unit becoming operational in February 2009.[142] The new unit comprised OSP and the DHW Works and Building Services division, and included revised roles for both OSP and BMW, with OSP to be incorporated into DTF as a new "Strategic Projects" business unit (referred to as DTF-SP) alongside BMW.

According to the Under Treasurer, 'the Building Management and Works or the strategic projects businesses are very much delivery focused and have a role up front in helping agencies articulate, or actually drafting, the business case for an asset'.[143]

Having BMW and DTF-SP as business units reporting to Treasury gives DTF:

> *various points of responsibility along the continuum of the life of a project. That now includes the development of business cases; the development of project definition plans, which is kind of getting finer detail in the planning; and then ultimately in the procuring and contracting for the delivery, whether it is a traditional construction contract, or a design and construct, or a design, build, own and operate. That now sits with the Department of Treasury and Finance.*[144]

The transference of Works functions to Treasury may also help to achieve greater accountability through transparency. It has been argued that increased transparency can be achieved if, amongst other things, 'cost–benefit analysis and other types of *ex ante* appraisal [… are] shifted from

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140 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.1.

141 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.1.

142 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.2.

143 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.6. See also p.4.

144 ibid., p.4.

promoters to more neutral ground, for instance with the Treasury, in order to reduce risks of agency problems'.[145]

In this view, infrastructure projects should be vested in one and only one project organisation with a strong governance framework and strong contract-writing skills with the capacity to:

- 'set up and negotiate contracts that will effectively safeguard its interests, including in equity risk allocation'; and
- 'enforce accountability vis-à-vis contractors, operators, etc'.[146]

Echoing this view, Mr Hugh Funder, Senior Adviser (Infrastructure Advisory), Royal Bank of Scotland (RBS), advised the Committee that the RBS has found it 'reassuring' that the works division of DHW was transferred to DTF. For the RBS, having a single agency point of contact in terms of the public works functions is the preferred option.[147]

3.7 BMW and DTF-SP as DTF Business Units

Organisationally, DTF has seven business units that report to the Under Treasurer. Three of these are procurement related, namely BMW, DTF-SP and Government Procurement. The balance of the corporate group is comprised of Shared Services, State Revenue, Corporate Services and Treasury.[148]

This section outlines the respective roles of BMW and DTF-SP, and the collaborative work they undertake.

(a) Building Management and Works

In April 2009, Cabinet endorsed a new lead role for BMW in the development of business cases and project managing the non-residential building program.[149] BMW then developed 55 initiatives as the means of implementing the necessary changes. These initiatives were subsequently endorsed by the Treasurer.[150]

BMW is now responsible for three core areas, namely:

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145 Flyvbjerg, Bent, 'Survival of the Unfittest: Why the Worst Infrastructure gets Built—and What We can do About It', *Oxford Review of Economic Policy*, vol. 25, no.3, 2009, p.359.

146 ibid., p.360.

147 Mr Hugh Funder, Senior Adviser (Infrastructure Advisory), Royal Bank of Scotland, *Transcript of Evidence*, 8 September 2010, p.8.

148 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

149 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.5.

150 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

- the planning and delivery of new buildings, including investment decisions on these buildings;
- assisting agencies with the management of the existing building portfolio, including investment decisions on maintenance planning; and
- helping government accommodate its public servants, including investment decisions for office accommodations.

This represents a major change in the management of Works business in Western Australia. Prior to Works Reform, government agencies endeavoured to work through the asset development process themselves, with varying degrees of success. Now that BMW's role is mandated, the processes can no longer be seen as optional.

Generally speaking, projects that are valued at less than $100 million are undertaken by BMW by default; those with a value in excess of $100 million are allocated to DTF-SP. BMW may at times manage projects in excess of $100 million, with the decision regarding the allocation of projects made by the Under Treasurer. The types of projects that the BMW team manages are non-unique non-residential buildings such as high schools and primary schools.[151]

The internal structure of BMW aims to facilitate better project planning and development. Within BMW there are six units, each performing a particular Works Reform function, including two Infrastructure Delivery groups that have their portfolios divided in a way that closely aligns with Treasury's structure for interfacing with government agencies on all budget matters.

As part of the model, the business case is signed by both the Under Treasurer and the agency. This allows the responsible Minister to have confidence that the business plan will receive support through the EERC.[152]

Works Reform is intended to be an evolving process. At the time of this report, DTF was undertaking a review of the SAMF, which was expected to be released by the end of 2010.[153]

BMW expects the review will result in a renewed or refreshed version of SAMF that will incorporate the findings of the preparatory Works Reform investigations—such as land assembly reform—as well as initiatives to allow agencies to better apply SAMF.[154] The current SAMF is designed to specifically apply to asset management of non-residential buildings, and it is expected that the revised SAMF will be 'better aligned to the full range of infrastructure types and therefore more readily applicable by all Government agencies'.[155]

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151 ibid.

152 ibid.

153 ibid.

154 ibid.

155 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.4.

BMW believes that, while agency reactions have been mixed, there is strong support for the Works Reform model. Individual BMW surveys of Chief Executive Officers, Asset Leaders and Building Occupiers/Tenants shows that while evidence of the full implementation of SAMF is still low, agencies are not averse to the reforms.[156]

(b) Office of Strategic Projects

According to DTF-SP, it has 'a significant role in planning and leading the development of business cases for high-risk projects, in collaboration with the responsible line agency and DTF's Treasury Business'.[157] Projects are assigned to DTF-SP 'by the Under Treasurer in agreement with Agencies or as directed by the Economic and Expenditure Review Committee',[158] and generally have the following characteristics:

- high-risk;
- unique;
- have a sensitive stakeholder environment
- high profile;
- suitable for public private partnership (PPP);
- programs that could later underpin multiple projects; and
- have a capital cost greater than $100 million.[159]

Projects with a capital cost greater than $100 million are usually treated as strategic, as costs are a significant risk factor. Some higher risk, smaller value projects may also be assigned to DTF-SP if the Under Treasurer considers it to be strategic.[160]

DTF-SP collaborates with the proposing agency to develop 'the plan to evaluate the project proposal and produce the Business Case' and provides guidance as the agency 'addresses the performance, social impact and recurrent cost components of the Business Case'.[161]

At the time of writing, DTF-SP had completed one project, namely One40 William Street, and had been assigned a further 17 projects.[162] DTF-SP projects tend to be those with unique characteristics, or those that have not been built in the state for many years. Examples include a

156 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

157 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.2.

158 Building Management and Works, Strategic Projects, 'Our Approach', nd. Available at: http://www.dtf.wa.gov.au/cms/content.aspx?id=3713. Accessed on 1 September 2010.

159 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, pp.2–3.

160 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

161 Building Management and Works, Strategic Projects, 'Our Approach', nd. Available at: http://www.dtf.wa.gov.au/cms/content.aspx?id=3713. Accessed on 1 September 2010.

162 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.3.

major city hospital, a state theatre or a fully outsourced prison.[163] The development of such projects requires a different skills set from that found in BMW, which is generally involved in non-unique projects.[164]

DTF-SP is also responsible for reporting to government on the performance of major projects, including building and infrastructure projects outside its direct oversight. The performance reporting has been streamlined over the past two years due to the requirement for agencies to provide bi-monthly project information to DTF-SP and the establishment of a committee of senior asset delivery agency officers identifying major projects worthy of attention by government.[165] The information is strongly focussed on time, cost and quality performance, as well as key issues—including stakeholder, communications and risk issues—and noteworthy milestone events.

DTF-SP prepares a summary of projects that assesses performance levels in key areas by assigning red, amber or green marks. An amber signal would apply where a project's forecast out-turn cost was more than 10 per cent but less than 20 per cent greater than the current approved budget.[166]

The summary report identifies trends in emerging risks and provides an overall view of how projects are performing in terms of those trends.[167] From this information a 'WA Government Major Projects Report' is prepared through the Minister Assisting the Treasurer for submission, also on a bi-monthly basis, to the EERC, which provides the government with 'a view on how we are performing against that group of major projects'.[168] At the time of the DTF-SP submission there were 37 major projects in the Report.

DTF-SP currently has the following projects on their list:[169]

- New Royal Perth Hospital
- New Children's Hospital
- Queen Elizabeth II Medical Centre Central Plant
- Albany Health Campus
- Old Treasury Building Redevelopment
- State Rehabilitation Service (incorporated into Fiona Stanley

163 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

164 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

165 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, pp.3-4, and Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6.

166 ibid., p.7.

167 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6.

168 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6.

169 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.3.

Hospital)

- Primary Schools Package (PPP)
- QEII Medical Centre Car Parking
- Midland Health Campus
- Busselton Health Campus
- Acacia Prison Expansion
- Eastern Goldfields Regional Prison
- Albany Entertainment Centre
- Fiona Stanley Hospital
- 140 William Street
- Joondalup Health Campus
- Perth Arena
- State Theatre Centre

Projects such as the Perth City Link and the Perth Waterfront, both of which meet the above criteria, are not being managed by DTF-SP.

Finding 3

Some projects that meet the criteria for assignment to the Department of Treasury and Finance Strategic Projects are being managed by portfolio agencies.

(c) BMW and DTF-SP Collaboration

There are strong links between BMW and DTF-SP, due primarily to their collective responsibility for leading the development of business cases.[170] BMW and DTF-SP are collaborating on the development of a range of asset management guidelines, procedures, processes and templates to guide project management through all phases from inception to operation.[171]

In forming a project team, DTF-SP calls upon significant resources from the BMW team, and while DTF-SP has a relatively small proportion of the non-residential building projects under its purview, the complex, high value, high risk characteristics of these projects means that DTF-SP receives approximately half of overall Works funding. BMW, on the other hand, which has approximately 200 projects, operates with the remaining 50 per cent of funding.[172]

A key advantage of collaboration between BMW and DTF-SP with Treasury is that the Under Treasurer has the capacity to leverage the linkages within DTF. For example, a PPP project team would include people from Government Procurement as well as BMW, DTF-SP and Treasury, encouraging the movement away from a traditional silo approach.

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170 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6; Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

171 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.4.

172 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

Further collaboration is manifest in the Centre for Excellence and Innovation in Infrastructure Delivery (CEIID), which was established in 2007 as a 'collaborative alliance between key infrastructure delivery agencies, government trading enterprises and other Government bodies'.[173] While CEIID does not have a direct role in the coordination and delivery of specific infrastructure projects in Western Australia, its aim is to 'improve collaboration, share knowledge and drive reform across a broad spectrum of activities associated with public works, infrastructure delivery and strategic asset management'.[174]

Member organisations include government agencies involved in infrastructure delivery and GTEs such as Main Roads Western Australia (MRWA), the Water Corporation and Fremantle Ports. CEIID is seeking to expand its membership to also include energy provider GTEs.[175]

Given its broad membership, an advantage of the CEIID collaborative alliance is the breakdown of the traditional silo approach to project development and delivery. The dissemination of knowledge via CEIID about how BMW and DTF-SP are delivering infrastructure projects encourages consistency of approach among member organisations.[176]

Organisations such as MRWA and the Water Corporation have a great deal of project management expertise and advanced, well organised asset management strategies, and are therefore able to bring enormous value to CEIID.[177] They are considered 'more advanced than … the non-residential building portfolio, which is one of the reasons Works Reform was introduced'.[178] Both DTF-SP and BMW agree that CEIID has been enormously successful and has produced useful results.

Collaboration is also enhanced by CEIID's interaction with industry. For example, BMW recently held a forum at which 350 people representing all sections of industry were briefed by the Minister, the Executive Director of DTF-SP and the 10 Works agencies to provide information on their works programmes. The forum was organised a result of feedback from an earlier CEIID forum at which industry advised government that it needed earlier provision of project information.[179]

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173 Submission No. 25 from Department of Treasury and Finance, 15 April 2010, p.1; and Submission No. 24 from Department of Treasury and Finance, 31 May 2010, p.1.

174 Centre for Excellence and Innovation in Infrastructure Delivery, *Strategic Plan 2008–2011*, p.2, included in Submission No. 25 from Department of Treasury and Finance, 15 April 2010, p.1; and Submission No. 24 from Department of Treasury and Finance, 31 May 2010, p.1; Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

175 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.2; and Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

176 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.2; and Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

177 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.11.

178 ibid.

179 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

When DTF-SP was established, the synergies between its work and that of CEIID were recognised, and while DTF-SP provides CEIID with additional resources, this effort:

> *dovetails very much with services that we are providing as part of, in particular, the broader works reform program but also management initiatives that are part of our role of providing a central government repository for the development of project management expertise and procedures.* [180]

The respective roles of BMW and DTF-SP, and the collaboration between them, allows agencies to focus on the strategic planning elements of infrastructure delivery. This necessarily requires all agencies to have appropriately skilled and experienced staff to undertake these tasks (see Chapter 9).

DTF's internal assessment of selected major infrastructure projects shows that 'the projected project cost outturns at December 2009 compared with March 2009 demonstrat[e] that the strong governance, and performance monitoring controls now in place have been effective'.[181] The methodology utilised to allow this conclusion has not been provided in the report and the Committee believes other factors may also have contributed to the projects' improved budget performance. Therefore, as with any government programme, Works Reform should be independently evaluated to ensure that the reform is having the desired or anticipated outcomes.

Recommendation 1

Works Reform should be independently evaluated to ensure that the reform is delivering the desired or anticipated outcomes.

180 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.2.

181 Building Management and Works, Department of Treasury and Finance, *Works Reform Progress Report 2009*, Department of Treasury and Finance, March 2010, p.16.

CHAPTER 4 STRATEGIC ASSET PLANNING

In a report for Infrastructure Australia (IA), PricewaterhouseCoopers noted that project selection processes should require that projects only be selected for development if they reflect a demonstrated need.[182] The result of developing projects without due consideration to underlying need has been found to contribute to the delivery of many 'poorly performing public projects'.[183]

The requirements of robust cost-benefit analyses—which are the tools used in Western Australia for measuring the potential benefits of projects against their likely costs—can only be met if the needs that the project is expected to satisfy are clearly articulated. The proper identification of and response to need has significant implications for the overall success of a project, particularly in terms of the extent to which it represents value for money and minimises opportunity cost.

This chapter examines the role of Strategic Asset Plans (SAPs)—and their development in response to articulated needs—in the context of achieving value for money in the development of sound infrastructure projects.

4.1 Establishing Need

It is broadly recognised that projects should only be selected if they reflect a demonstrated need, proceeding only 'if they address clearly identified problems and provide the greatest net benefit to stakeholders'.[184] Generally, in the context of infrastructure provided by the state government, need can be viewed as a gap in an agency's service delivery. That is, the current mix of infrastructure assets does not allow the agency to provide the services expected of it. Under Treasurer Tim Marney noted the importance of informed planning processes that allows agencies:

> *to focus…on planning their service delivery requirements much better… so that we can have a very clear picture of the asset requirement going forward over the next 10 years, rather than being in catch-up mode constantly,* [which] *is where we tend to get asset decisions that are suboptimal.*[185]

Nevertheless, a key problem with asset management in Western Australia has been a 'lack of real data to support need for many proposed capital works projects and failure to articulate the objective of the project'.[186]

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182 Infrastructure Australia, *Review of Major Infrastructure Delivery*, report prepared by Price Waterhouse Coopers, December 2008, p.4.

183 Prasser, S, 'Overcoming the 'White Elephant' Syndrome in Big and Iconic Projects in the Public and Private Sectors', in John Wanna (ed.), Improving Implementation: Organisational Change and Project Management, ANU e-Press, Canberra, 2007, p.61.

184 Infrastructure Australia, *Review of Major Infrastructure Delivery*, report prepared by Price Waterhouse Coopers, December 2008, p.4.

185 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, Transcript of Evidence, 1 April 2010, p.6.

186 Department of Treasury and Finance, Works Reform Business Solution Plan, June 2009, p.15.

The Committee recognises there will be times when projects are developed to meet unforseen or urgent needs within tight timeframes or where planning processes fail to 'adequately determine and describe projects that will meet the service objectives of agencies'.[187]

While most of the projects examined in this report enabled ready identification of their need, others were more difficult to identify.

4.2 The Breadth and Depth of Infrastructure Needs

The scope of any government's infrastructure needs is as broad as the scope of its various responsibilities, which invariably impacts upon investment decisions. The breadth of some agencies' infrastructure needs was demonstrated by the Western Australian Police, in evidence before the Committee:

> *We consider, for example, the IT needs of our organisation, which are very large and complex. We also consider the needs of our major fleet, which includes helicopters and boats, and the replacement of large vehicles et cetera. We consider the difficulties we have with some of the buildings, which are perhaps not critical with respect to the service delivery issues but may be very critical with respect to the current state of the buildings… We might have to decide how important it is to get a police helicopter compared with spending $20 million worth of IT improvements in our organisation.*[188]

Addressing service delivery sits at the centre of any robust infrastructure needs analysis. Ideally, any government investment decision should be informed by a full consideration of 'all reasonable service delivery options'.[189] SAMF provides agencies with tools to assist the process including 'gap analyses' designed to determine whether existing assets are suitable for the 'optimal delivery of the services that the assets are intended to support'.[190]

Finding 4

Identifying need and appropriate responses has significant implications for the overall success of a project, particularly in terms of value for money and the minimisation of opportunity costs.

4.3 Identifying and Quantifying Needs

Following the conclusion of the needs analysis process, agencies may identify several needs arising from service delivery gaps that can only be met through the procurement of new infrastructure. Agencies are required to document these needs (and their infrastructure responses)

187 ibid.

188 Mr Greg Italiano, Executive Director, Western Australia Police, Transcript of Evidence, 18 June 2010, p.8.

189 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.3.

190 Department of Treasury and Finance, Strategic Asset Plans, August 2005, p.10.

in their SAPs. These are submitted to the Department of Treasury and Finance (DTF) and Cabinet, to provide government with an overview of potential future capital investment.

Understanding how these projects come to be on a SAP first requires an understanding of how the need they are responding to was identified. In terms of the projects examined by the Committee, some agencies enjoyed an advantage through the ability to more easily identify need than others. In circumstances where demand can be measured and projected, agencies can quantify usage and make projections about future demand.

Main Roads Western Australia (MRWA), Verve Energy and Western Power are three agencies that were able to quantify a demand-based need for new infrastructure in relation to the projects examined in this report. The Committee also received evidence relating to the demand for new port infrastructure in the Mid-West, underpinning the need for the Oakajee Port—although there is debate about the appropriate response to this need (see Chapter 5).

Other projects examined by the Committee have not quantified need in the same manner as those mentioned above.

(a) Determining Need through Demand Projections

The New Perth to Bunbury Highway (NPBH) had been the subject of several funding submissions to the Commonwealth Government. A submission made in 2001 noted the population of the region was projected to grow to 280,000 residents by 2021.[191] The subsequent submission in 2006 anticipated that by 2031 the region was to be home to 388,000 residents,[192] an increase which reflected the significantly higher levels of population growth in Western Australia since the 2001 submission.

Traffic volumes arising from population growth were cited as the impetus for the new highway, with freight and commuter traffic between Mandurah and Perth increasing by approximately seven per cent per annum.[193] The existing route was highlighted as problematic due to its dual role of providing access to coastal communities and of providing a through-route for freight and other traffic heading to the South West. The mix of freight and urban traffic increased the risk of crashes—risks that would continue to grow in line with the growth of the population.[194]

The Gateway WA Project is another project where the need for the infrastructure upgrades was reasonably easily quantified due to the nature of the service delivered by roads. If a road is designed to handle only a certain number of vehicle movements per day, and that number is exceeded—or is projected to be exceeded—then the need for action to address the service delivery shortcoming is clear. By 2015 the number of vehicle trips using the road network in proximity to

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191 Main Roads Western Australia submission to the Australian Land Transport Development Program, Perth – Bunbury Corridor, Peel Deviation, Construct Dual Carriageway, October 2001, p.5.

192 Main Roads Western Australia, AusLink Project Proposal Report, Perth – Bunbury National Corridor: New Perth – Bunbury Highway, May 2006, p.35 and p.37, in Submission No. 5 from Main Roads Western Australia.

193 Submission No. 2 from Main Roads Western Australia, 15 January 2010, p.6.

194 ibid.

Perth Airport is forecast to increase by approximately 30 per cent.[195] Many of these roads were already either at capacity or exceeding it in 2007.[196]

Often, infrastructure is needed to facilitate broader economic development, such as Western Power's two-stage Mid-West Energy Project, the first stage underpinned by increasing demand for energy from iron ore producers. Western Power notes that without the demand from one customer in particular—the Karara mine site operated by Gindalbie Metals Ltd—the first stage would not be necessary for several years.[197]

The Committee focussed on stage two of the project, which is intended to address supply constraints affecting Geraldton and which is reliant on the successful completion of stage one. Western Power notes that meeting existing 'underlying load growth' in the region would require only minor augmentation of the existing power transmission infrastructure. In making its assessment of future demand, however, Western Power has taken account of regional economic and industrial development forecasts and concluded, following broad consultation, that a 330kV transmission line is the appropriate asset response.[198]

The experience in relation to the Collie to Perth transmission line demonstrates the benefits of remaining flexible in response to shifts in demand. In 2007 Western Power identified the need to provide additional bulk transmission capacity in order to meet 'forecast increases in generation in the South West region'.[199] The increased demand for power transmission was to be met through the construction of a new 330kV double circuit transmission line connecting Collie to Perth. With the new power generation developments being deferred, the demand growth underpinning the need for the project diminished and Western Power has decided to delay implementation of the project.

(b) Determining Need through Service Delivery Shortcomings

Some needs are more difficult to quantify, although they can still be identified. The previous chapter outlined the importance of agencies conducting an assessment of existing asset mixes in order to determine the extent to which the assets meet ongoing requirements. In the case of the new Police complex in Northbridge, a combination of factors, including increasing 'demand' due to population increases and the inadequacy of the existing facilities, have resulted in the perceived need for the new complex.

Western Australia Police's assessment of its existing assets found that the existing Watch House, which was constructed in the 1960s, had been criticised for a number of years due to:

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195 Department of Transport, Perth Airport Transport Master Plan: Preliminary Version, report prepared by AECOM Australia Pty Ltd, 15 March 2010, p.47.

196 2007 Perth Urban Corridor Strategy: Building our National Transport Future, June 2007, p.6 and p.8.

197 Submission No. 10 from Western Power, 19 April 2010, p.7.

198 ibid., pp.7–8.

199 Submission No. 11 from Western Power, 19 April 2010, p.7.

> *non-compliance with the Building Code of Australia, fire safety provisions, health standards, Custodial Design Guidelines developed as a result of the Royal Commission into Aboriginal Deaths in Custody; and recommendations arising out of Coronial inquiries.*[200]

The Royal Commission into Aboriginal Deaths in Custody described the East Perth Lockup as 'archaic and wholly inadequate'.[201] The new complex is anticipated to:

> *support frontline best practice policing to meet the current and future needs of the Perth Central Business District and Northbridge community. The 24 hour Perth Watch House will provide overnight (up to 48 hours) detention for 72 persons …[and] will be operational 24 hours per day, 7 days per week including public holidays.*[202]

The Western Australia Police identified the construction of a new complex as an appropriate response to the failure of its existing asset mix to deliver the quality of service required.

Finding 5

The need for new infrastructure to meet service delivery requirements can be more readily identified and quantified for projects where demand and/or service delivery shortcomings can be measured.

(c) Determining Need through the Analysis of Other Factors

The Committee also examined infrastructure projects that, in terms of how their need was identified, were not so easily categorised and may have been developed in response to perceived social needs or economic shortcomings. Projects such as the Perth City Link and the Ord-East Kimberley Development Project have not been advanced on purely economic grounds. On the other hand, the Australian Marine Complex (AMC) in Henderson, south of Perth, is a project driven by the ideal of achieving an economic objective—the promotion of a new industry sector.

(i) Social Outcomes

A primary driver for the Ord-East Kimberley Development Project was the economic development of the East Kimberley Region with the view to improving the social development of communities resident in the region. The Department of Regional Development and Land's submission suggests that improved social outcomes will result from economic development:

200 ibid., p.2.

201 ibid.

202 Submission No. 21 from Western Australia Police, 3 June 2010, pp.1–2.

> *A key objective of the State is to strengthen the regional economy, in particular focusing on improving the socio-economic circumstance of the traditional owners, and closing the gap in health, employment, justice, housing and education outcomes.*[203]

A business case prepared for the project by Marsden Jacob in 2008 states that:

> *the largest single benefit from major projects in the East Kimberley not captured in the formal economic modelling nor in the benefits and costs quantified* [in earlier sections of the business case], *is the benefit for the indigenous community.*[204]

As noted at the introduction to this chapter, the success of a project depends greatly on the extent to which it has been defined by the need or shortcoming that it is responding to. The Ord-East Kimberley Project relies on a detailed documentation of socio-economic shortcomings the project is addressing, with the business case prepared in 2008 highlighting:

- A lack of jobs and structural weaknesses in the employment market, including:
  - high rates of unemployment;
  - reliance on Community Development Employment Programs;
  - Indigenous labour immobility; and
  - concentration of Indigenous labour in a narrow band of industry types.
- Strong population growth but only limited growth in employment opportunities.
- Prominent social problems, including:
  - reliance on income from welfare payments;
  - significantly shorter life expectancies than the general population due to a number of health problems;
  - low rates of home ownership amongst Indigenous communities; and
  - average weekly incomes of up to 75 per cent lower than non-indigenous residents of the region.[205]

Based upon the Marsden Jacob report, it would be hard to justify the expenditure of $220 million on purely economic grounds.

Project Director, Mr Peter Stubbs, noted the emphasis given to providing Indigenous employment opportunities during the construction phase:

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203 Submission No. 12 from the Department of Regional Development and Lands, 20 April 2010, p.4.

204 Department of Industry and Resources, Ord Expansion Project: Business Case Evaluation, report prepared by Marsden Jacob, August 2008, p.46.

205 ibid., pp.46–53.

> *When we went to market to select a contractor to do the civil engineering and construction works, the threshold tender criteria was set at 40 per cent of the value of the assessment [of the …] demonstrated ability to engage, employ and support the Indigenous objectives consistent with the native title agreement. That is a high threshold; nationally that is sort of breaking new ground because more typically tender thresholds are around 10 to 15 per cent.*[206]

Addressing social needs through new infrastructure can be an entirely appropriate course of action for government to take. However, thorough investigation needs to be undertaken to identify and determine the desired social outcomes and to ensure that the infrastructure spending is the best vehicle for achieving those outcomes.

Finding 6

Projects which are assessed as having a low level of economic benefit may still be justified on the basis of their social outcomes.

Finding 7

When social benefits are the primary justification for major project investment, comprehensive analysis must be undertaken to ensure the claimed social benefits are deliverable and the project will provide value for money.

(ii) Economic Outcomes

Infrastructure can also be driven by a perceived economic need. Most infrastructure investment will result in some form of economic benefit, although the effectiveness of this will vary. The Organisation for Economic Co-operation and Development (OECD) estimates that increasing the public infrastructure stock by one per cent leads to an increase in output of around 0.2 per cent. The most recent Inter-Generational Report prepared by the Commonwealth Department of the Treasury notes that the results for Australia are in line with those of the other OECD nations.[207]

In regard to investment in the road projects described earlier, it is clear that investment does not simply help to alleviate traffic problems but also plays an important role in boosting economic

206 Mr Peter Stubbs, Director, Ord-East Kimberley Expansion, Department of Regional Development and Lands, Transcript of Evidence, 5 May 2010, p.12.

207 Commonwealth Department of the Treasury, Australia to 2050: Future Challenges, January 2010, p.23.

activity by boosting productivity. Better road networks increase labour mobility, and provide more efficient means for goods and services to access markets.[208]

The AMC project appears to have been driven by the objective of achieving a greater—and more diverse—economic return from the extraction of minerals and energy in Western Australia. In 1989 the Commonwealth House of Representatives Standing Committee on Industry, Science and Technology produced a report titled *The North West Shelf – A Sea of Lost Opportunities*. The Western Australian Department of Commerce (DoC) provided the following summary of the report in its submission to the Committee:

> *This report put forward the view that major national resource projects which exploit a non-renewable resource should contribute to the economy in more ways than simply through direct revenue, royalties and taxes. The report identified industry, infrastructure and skills management as areas these projects must develop. Government was seen as having a responsibility to ensure that both the direct and indirect benefits of these projects to the nation were maximised*.[209]

Another report by the same committee in 1998 criticised the failure to take action on the recommendations contained in the earlier report. The findings in the two reports, and the Western Australian Government's Jervoise Bay Masterplan, formed the basis for a submission to the Federation Fund in the late 1990s, which allowed the initial investment in the area. The Committee's focus has been on later stages of the investment relating to upgrades of the Common User Facilities, including:

- an extension of the existing eastern wharf;
- electricity upgrades;
- blasting earthworks for the creation of suitable commercial and industrial land; and
- construction of a floating dock.[210]

Mr John O'Hare, Manager of the AMC for the Dept of Commerce, noted that in terms of demand, there were 'a lot of nay-sayers' in the marine, defence and oil and gas industries, stating:

> *We were very, very fortunate, to be perfectly candid, that the economic situation as it evolved in terms of economic growth did favour the decision.* [211]

Mr Ross Holt, Chief Executive Officer of LandCorp, elaborated further:

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208 Henry, K et al., Australia's Future Tax System: Final Report, Report to the Treasurer, Commonwealth of Australia, Canberra, December 2009, Vol. 2, p.374.

209 Submission No. 23 from the Department of Commerce, 27 May 2010, p.3.

210 ibid., pp.14–16.

211 Mr John O'Hare, General Manager, Marine and Defence, Department of Commerce, Transcript of Evidence, 23 June 2010, p.9.

> *It was somewhat an act of faith that therefore the government needed to do what it could to try to retain as much of* [industrial fabrication for defence and the oil and gas sectors] *work as possible, because of the flow-on benefits that were spoken about and multiplier impacts. A vision is good, but then there was a concept developed. The appetite of the private sector was assessed, so the market was tested and it was found there was not a receptiveness in the private market to take this on. The government then went back, and if you like, regathered all the intelligence and looked at, if it were to undertake the development itself, what form would that development take. There was a whole lot of input, as John said, from various industry players, but somewhat non-specific and without any commitment. That was a lot of joining up the dots and trying to get a level of understanding of what was the potential—the upside, downside, high growth and low growth cases, external studies, such as the Ernst and Young study and other supporting studies.*[212]

It would seem that, from the experience with the AMC, government provision of infrastructure to promote an industry sector can achieve the desired economic objectives. It should be noted, however, that the government's investment in the project carried considerable risk, particularly given scepticism by many industry participants.

The project demonstrates that risks can be offset and excellent outcomes achieved if the risks are identified and mitigation strategies put in place. In this case, that involved liaising with industry and altering the proposed project once feedback had been provided, although as Mr Holt noted, the feedback was 'non-specific' and 'without any commitment'.

The Committee also examined another project designed to provide support to a specific industry: the Ravensthorpe Nickel Operation (RNO). This project involved the provision of community infrastructure, including a new primary school, financial support to the local government for upgrades to essential services, the construction of wastewater treatment facilities and a variety of road upgrades. Provision of these services was required in order to enable workers at the mine to live in the local community, rather than operate on a fly-in, fly-out (FIFO) basis.

When approving resource developments in the regions, government may face two choices in relation to maximisation of the potential opportunities provided by the development. They may:

- make a serious commitment to developing the region through the provision of local infrastructure to encourage sustainable local workforces to allow the local community to derive benefits from the development; or

- allow the project to proceed on a totally FIFO basis, which might be to the detriment of the local community as the community receives significantly fewer benefits from a major development in their locality.

Regional development requires government commitment to community infrastructure if the communities are to benefit from resource development projects. Government support for the RNO

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[212] Mr Ross Holt, Chief Executive Officer, Landcorp, Transcript of Evidence, 23 June 2010, p.9.

project was justified on the need to diversify the local economy and to provide the upgrades to local infrastructure necessary to support a rapid expansion in the local population and economy. [213]

Although support was provided to both the AMC and the RNO for broadly similar reasons, in the RNO's case the support was, arguably, lesser in scope and targeted at promoting a regional economy's development. This is to say that the identified need in both cases was economic. However, the risks associated with the AMC were identified through a wide consultation process before construction commenced, while the Department of State Development (DSD) acknowledges that key risks associated with the RNO emerged only after the project had commenced, including:

> - *BHPB's 100% under-estimation of the required local workforce, announced 5 years after Cabinet committed to the MUIP;*
> - *the incapacity of the Shire to manage the vastly increased scale of the project post-2006;*
> - *technical flaws in the understanding of the nature of the nickel deposit and consequent failures within the engineering and design of the beneficiation plant; and*
> - *a global financial crisis resulting in an 80% drop in the world price of nickel during the ramp-up phase of commissioning the project.*
>
> *It would appear that these risks were not identified prior to the development of the project. In particular, it was only during the plant construction phase that BHBP informed its stakeholders of the changes contemplated and their scale.* [214]

Both the RNO and the AMC were projects with economic development aspects. However, in the case of the AMC the economic aim was explicit: developing a new infrastructure facility to support the growth of a number of enterprises with diversified operations relating to marine and resources sectors. In the case of the RNO, although it also had economic development features, government support was intended primarily as a means to support regional development by providing the infrastructure necessary for an increased population and economic activity.

While both projects had risks for the government, the AMC risk was mitigated by the rigor with which the planning was undertaken together with the diversified nature of the client base being supported by the AMC. In contrast, the RNO's regional development aims were underpinned by only a single resource project, exposing the government's investment to the volatility of world minerals prices.

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213 Submission No. 20 from the Department of State Development, 31 May 2010, pp.2-9.

214 ibid., p.7.

Finding 8

Promoting the economic growth of Western Australia and its related community development demands may involve a substantial element of risk. Thorough risk assessment and mitigation measures must be undertaken to manage this risk, thereby reducing the chance of redundant investment.

The Oakajee Port is an infrastructure development where the funding arrangements have undergone change in recent years. In general terms, the Committee accepts that a new port is required. There is reliable information to suggest that the expansion of iron ore mines in the Mid-West will exceed the capacity of Geraldton Port, which is constrained in terms of expansion due to its geographic location in the heart of the city of Geraldton and its inability to handle Cape size vessels.[215]

Using the framework outlined above, it can be argued that there is a demand-based need for a deep-water port in the Mid-West.

The need for the injection of $780 million of combined Commonwealth and state government funding has not been clearly established, given that there had been a commitment from the private sector to provide a fully privately funded facility.[216] It might be that the port infrastructure to be provided by the government is significantly different from that which was to have been provided by the private sector.

In response to a question in relation to possible differences between the privately and publicly funded port iterations, DSD advised:

> *the State is setting robust technical and planning requirements for the project to ensure the State's objectives are met. This includes ensuring that the design and operation of the common use infrastructure (CUI), including the breakwater, turning basin and other infrastructure, provides for genuine third party access and the capability to develop the port as a multi-user, multi-function port over time.*[217]

This response does not clarify the differences between the privately and publicly funded port iterations.

The Oakajee State Development Agreement was made available to the Committee on a 'closed' evidence basis and the Committee has not disclosed its contents in this report. The Committee does note, however, that the agreement contains a number of commitments and obligations on the parties which go to matters affecting financial obligations and the use and operation of the port. This may result in further or ongoing financial obligations for the state. The Committee believes

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215 Ms Anne Nolan, Director General, Department of State Development, Transcript of Evidence, 5 March 2010, p.2.

216 Hon. Alannah MacTiernan, MLA, (then Minister for Planning and Infrastructure), *Oakajee Port and Rail to Build New Mid-West Iron Ore Port*, Media Statement, 29 July 2008.

217 Submission No. 32 from Department of State Development, 3 September 2010, pp.1–2.

that given the significant public funding towards this project, there is a strong public interest argument for the agreement to be made public.

Finding 9

It is generally accepted that a new port in the Mid-West is needed, based on reliable information suggesting that the expansion of iron ore mines in the region will exceed the capacity of Geraldton Port, which has expansion constraints.

Recommendation 2

The State Development Agreement for the Oakajee Port and Rail Project should be made public.

Finding 10

The need for government funding of the Common Use aspects of Oakajee Port is not clear, particularly given both the lack of detail in relation to the extent to which the private and public iterations vary and the reasons why they vary.

Recommendation 3

The Minister for State Development should publish the differences between the private and public iterations of Oakajee Port Common Use Infrastructure, together with the needs analysis underpinning the decision to provide public funds.

(iii) Hybrid Outcomes

The Perth City Link[218] is an example of a project where the identified needs are both economic and social, and where secondary needs relate to the efficient operation of public transport. The project consists of two separate, though connected components: sinking rail infrastructure west of the city train station and sinking the Wellington Street Bus Station (WSBS).

As noted by the Department of the Premier and Cabinet (DPC) in its submission to the Committee, sinking the transport infrastructure will achieve the following objectives:

- Removal of a major barrier in the city;
- Creation of a mixed-use transit oriented precinct and public spaces which will have the effect of increasing the amenity and permeability of the city;
- Increasing short- and long-term economic activity, jobs and investment in the city;
- Providing sufficient capacity in the bus and rail systems to allow for future network expansions and integration of the public transport systems with future development.[219]

The State's November 2008 submission to Infrastructure Australia described the primary benefit as allowing:

> *for the redevelopment of a section of the City that has been crying out for activity. It will also provide a significant benefit through the integration of the Northbridge Precinct which contains much of Perth's restaurant and night life activity, with the Perth CBD.*[220]

A follow-up submission in April 2009 placed greater emphasis on the public transport related benefits to be achieved from the development of the project. Re-branded as 'The Hub' the submission noted that the project will allow:

> *the City to expand to capture the additional value from other government and private sector projects currently underway as well as provide a catalyst for future private investment to flow into the central city area and into precincts adjoining the Hub… It will also enable the release of land for development by the private sector.* [221]

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218 The area comprising the Perth City Link has split the city since the 1880s. It is composed of a large reserve running between Roe and Wellington Streets from William Street west to Delhi Street. The railway reserve was also used as Perth's main goods and marshalling yard; the last of these marshalling yards and container sheds were removed in the 1980s. Since that time, much of the 13.5 ha site has sat empty and under-utilised. The Northbridge Link Masterplan notes that the 'physical barrier created by the Link area has been a key factor in the land use character and experience of the city', see East Perth Redevelopment Authority, *The Link Masterplan*, June 2008, p.6. What this means, in effect, is that the city's northward expansion has been constrained by the presence of the rail reserve—the central business district (CBD) stretches along a narrow east-west axis, bound on the south by the Swan River and on the north by the rail reserve.

219 Submission No. 2 from the Department of the Premier and Cabinet, 11 February 2010, p.40.

220 Western Australian Government Submission to Infrastructure Australia, Northbridge Link: Removing the Railway Barrier, November 2008, p.3, in Submission No. 6 from the Public Transport Authority, 19 March 2010.

221 ibid., p.4, in Submission No. 6 from the Public Transport Authority, 19 March 2010.

Mr Reece Waldock, CEO of the Public Transport Authority, noted the project allows for fully connected rail lines with all of Perth's suburban rail lines which will improve system flexibility during times of high demand, including special events.[222]

Mr Waldock explained that several areas of Perth's northeast are served exclusively by buses connecting to the WSBS, which:

> *feeds what we call the north–eastern corridor. I refer to Alexander Drive and Fitzgerald Street, which extend into Mirrabooka and Morley. The whole area is growing fast and public transport is key. What we are doing with the bus bridge and the brand new underground bus station is giving customers not only a better service but also one that is far more effective and efficient.*[223]

The social benefits accruing from the new property and public space developments on the former rail land are difficult to quantify, as is the need driving the development. This difficulty was perhaps reflected in the economic analysis of the project conducted by the state government, which was found by IA to be 'inadequate', while the Benefit-Cost Ratio (BCR) was found to be 'critically flawed'. [224]

4.4 Considering the Options

The final stage of the Strategic Asset Planning process is for agencies to identify various options for responding to the needs identified during the process. It may be that the construction of a new asset is not the most appropriate response. SAMF outlines a number of alternatives that agencies should consider, including:

- demand management;
- asset redeployment to relocate assets where they my be better utilised;
- asset refurbishment;
- utilising the private sector; and
- doing nothing.[225]

It is only once this process has been completed that agencies should include projects on their capital investment plans in preparation for the next stage: developing the right asset.

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222 Mr Reece Waldock, Chief Executive Officer, Public Transport Authority, Transcript of Evidence, 2 March 2010, p.7.

223 ibid., p.6.

224 Australian National Audit Office, Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List, July 2010, p.140.

225 Department of Treasury and Finance, Strategic Asset Plans, August 2005, p.10.

Although the Committee did not examine the extent to which agencies consider non-asset solutions at this stage of the asset planning process it notes the following issue identified in DTF's 'Works Reform Business Solution Plan':

> *a focus by agencies on project definition and delivery of the building, resulting in a failure to assign adequate resources to articulate service delivery standards, demand management or consideration of non-asset solutions.*[226]

The proper identification of need is central to achieving value for money through the delivery of a new asset. Obviously, if a range of options have not been considered prior to the decision to develop a new asset, then the extent to which a value for money outcome can be achieved can be questioned, as all options cannot be said to have been considered.

[226] Department of Treasury and Finance, Works Reform Business Solution Plan, June 2009, p.15.

CHAPTER 5 DEVELOPING THE RIGHT ASSET

5.1 Concept Development

The Strategic Asset Management Framework (SAMF) identifies the concept development stage as critical in terms of its ability to influence the final cost of a project over its life and central to the achievement of a value for money outcome. This chapter gives attention to the importance of agencies developing the right asset through a robust concept development and evaluation phase. There are a range of evaluation tools available, some of which will be examined here.

(a) What is Value?

The *Value Management Practice Guidelines* published by the Western Australian Government's Centre for Excellence and Innovation in Infrastructure Delivery (CEIID) defines value as:

> *Value is defined as the quantum of needs achieved at minimum cost. Value can be achieved through many different aspects of a project, such as co-location/collaboration, non-asset solutions, economic and social benefits and lower risk. Nevertheless the equation remains the same, achieving value through the maximisation of the outcomes against minimum cost.*[227]

The Department of Treasury and Finance's (DTF's) *Value Management Guidelines* describe value as:

> *the benefit to the client offered by a project….ensuring that the right choices are made about obtaining maximum benefit for the client within time, cost and quality constraints.*[228]

As the representative of projects' end users, DTF's approach to value is appropriately client-centric—maximised benefit and quality, and minimised cost and time.

(b) SAMF Requirements and Concept Development

SAMF provides a step-by-step process through which agencies can progress their concept development. The initial step is the application of strategic justification criteria to ensure that the project concept is:

- consistent with general government (and agency) policy and strategic outcomes;
- justified on the grounds that the private sector is failing to efficiently provide the proposed project services; and
- developed with appropriate consideration of current and future economic conditions.[229]

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227 Centre for Excellence and Innovation in Infrastructure Delivery, *Value Management Practice Guidelines*, April 2009, p.2.

228 Department of Treasury and Finance, *Value Management Guidelines*, August 2005, p.1.

If projects cannot meet these criteria SAMF recommends that they should be abandoned without further evaluation.

(i) Defining Outcomes and Service Delivery Strategies

Concept development commences with a restatement of the desired project outcomes and associated service delivery strategies. At this stage the agency is expected to be able to develop the concept to a level of detail that enables comparison of the project to the agency's strategic direction, and the quantifiable contribution the project is expected to make to achieve this direction.

(ii) Defining Proposed Project Functions

The second stage develops a range of project functions and establishes the relationship between these and the service delivery strategies of the previous stage. Needs analysis may be utilised to assess whether the project can achieve the desired outcomes for lower costs, including through scaling back, relocation or even avoiding the project completely.

(iii) Defining Project Options

The third stage is to develop a range of options that respond to the project outcomes and functions. Joint ventures, financing alternatives and private sector involvement should also be given full consideration and a realistic base case of 'doing nothing' against which the various options can be benchmarked must also be developed. SAMF outlines a range of questions to consider during the options development process including: alternative locations for and size of the project; private sector involvement; and whether economies of scale can be achieved.

Western Power's experience with the Southwest Transmission Line Reinforcement Project is noteworthy here. Eight different 'network augmentation' options were considered, as were two non-network solutions.[230]

Timing

At this stage consideration of project timing is critical because premature development may lead to excess capacity and subsequent under utilisation.[231] Western Power's delivery of the STLR Project, has been delayed following uncertainty regarding electricity generator demand for new transmission infrastructure, which demonstrates the benefits of a flexible approach to the timing of infrastructure delivery. Despite deferring the project, the associated planning has not been wasted as the project will go ahead in the future with environmental and other planning approvals already in place.[232]

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229 Department of Treasury and Finance, *Project Evaluation Guidelines,* August 2005, p.7.

230 Western Power, *Proposed Major Augmentation to the Electricity Network – 330KV Transmission Line to Support Electricity Load in the Perth Metropolitan Area,* November 2008, p.5 in Submission No. 11 from Western Power, 19 April 2010.

231 Department of Treasury and Finance, *Project Evaluation Guidelines,* August 2005, p.11.

232 Submission No. 11 from Western Power, 19 April 2010, pp.3-4.

Financing

Financing options, including the involvement of the private sector, should be given consideration at this stage (see Chapters 2, 7 and 8).

(iv) Preliminary Procurement Planning

A preliminary timeline should also be developed during the concept development process that includes key dates and project milestones.[233]

(c) The Role of Value Management Studies

A value management study (VMS) is a process through which stakeholders in a project are given the opportunity to be involved in the decision-making process through an examination of the relevant options for the design and construction of the project. This is said to lead to a refinement of the design brief and identification of budget constraints.[234]

It is considered an 'organised and creative approach to optimise the cost and performance of a facility'.[235] DTF view VMS as not simply a cost-cutting tool, but providing other benefits, including: improved communication; teamwork and cooperation; increased awareness and ownership by stakeholders; time savings through focus of effort; enhancement of risk management measures; and the promotion of innovative service delivery processes. [236]

VMS usually take the form of a workshop and are led by an independent and appropriately qualified facilitator familiar with the design and construction process and with the roles of the professionals involved in the design team. The success of the VMS is thought to depend on having the right mix of skills represented. Issues considered during a VMS include co-location, non-build solutions, rationalisation, risk, combination and simplification.

Although no longer mandatory, DTF believe projects that are unusual in design, construction or maintenance, or are estimated to cost more than $5 million, should be automatically considered for a VMS.[237] The *Works Reform Business Solution Plan* recommended that DTF's Building Management and Works (BMW) business unit should become a leader in the development of business cases, and the application of supporting tools, including Value Management.[238]

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233 Department of Treasury and Finance, *Project Evaluation Guidelines*, August 2005, p.12.

234 Department of Treasury and Finance, *Value Management Guidelines*, August 2005, p.1.

235 Cha, H. S. and O'Connor, J. T., 'Optimizing Implementation of Value Management Processes for Capital Projects', *Journal of Construction Engineering and Management*, vol. 131, no. 2, 1 February 2005, p.241.

236 Department of Treasury and Finance, *Value Management Guidelines*, August 2005, pp.2-3.

237 Department of Treasury and Finance, *Value Management Guidelines*, August 2005, p.5.

238 Department of Treasury and Finance, *Works Reform Business Solution Plan*, June 2009, p.71.

(d) Concept Innovation as a Driver of Value

One of the key purposes of a VMS is to optimise the performance of a facility, which can be achieved in a number of ways, including through co-location of services to promote innovative service delivery. The Perth Police Complex (PPC) was the subject of at least one VMS.[239]

The Western Australia Police outlined the driver behind the 'Frontline First' policy, as 'delivering policing services' and spending money on the programs and issues that 'make the biggest impact at the front end'.[240] The practical implication of this was to maximise the application of funds in support of activities considered frontline by seeking efficiencies in other 'back of house' activities.

Co-locating the Magistrate's Court, the Watch House and the Central Perth Police Complex in one centralised location is an innovate solution to efficiently using police resources so that emphasis can remain on delivering services at the front end. The Committee was advised:

> *[the design concept] is also about achieving efficiencies in processing detainees…and minimising the number of officers we need in the watch-house by its very design, including glass fronts, rather than what we currently have. There are currently probably about 15 people in the watch-house because of its [poor] design. They have to walk down corridors and there are bars; there are a lot of risks there. The risks will be significantly reduced in the planned watch-house.*[241]

In terms of the co-location of police services:

> *by having the watch-house joined up with that facility…creates those efficiency gains in terms of the time to transport detainees...It will provide a very good service for Northbridge in terms of our ongoing operations on Friday and Saturday evenings….[and] will, in effect, provide security for the Perth watch-house. To have a Perth watch-house on its own, the perimeter security would have to be rather extensive to protect it. Having a 24/7 police establishment actually achieves that without any real expense.*[242]

The approach to the Perth Police Complex has successfully maximised the benefits offered by the project, through using an innovative approach to the building's design. Not only have costs associated with constructing separate projects for the different components of the complex been minimised, but efficiencies for the organisation have been maximised:

- As there is a 24-hour police station attached to the Watch House, some security concerns have been alleviated.
- The Watch House's advanced design reduces the number of staff required.

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239 Submission No. 21 from Western Australia Police, 3 June 2009, p.9.

240 Mr Dominic Staltari, Assistant Commissioner, Western Australia Police, *Transcript of Evidence*, 18 June 2010, p.10.

241 ibid., p.3.

242 ibid., pp.3–4.

- The integration of the Magistrate's Court with the Watch House reduces the resources required for the transport, dispatch and receipt of prisoners.

Finding 11

The co-location of a range of services at the Perth Police Complex exemplifies the potential to maximise value through the use of value management studies that identify innovative responses to service delivery needs.

Recommendation 4

Government organisations should be encouraged to undertake value management studies to identify innovative responses to their service delivery needs.

(e) Other Methodologies for Concept Development

VMS may not always represent the best or only approach to determining the most appropriate option for responding to a service delivery need. A Government Trading Enterprise (GTE) might encounter difficulty developing innovative solutions to some of its infrastructure delivery requirements, while other aspects of the VMS process may prove quite helpful.

Other circumstances include those where agencies are working backwards from a government vision or, to a lesser extent, a government election promise. Although VMS may not always be feasible in those circumstances, agencies should still assess different infrastructure options in response to these proposals or promises, so as not to jeopardise a value for money outcome.

In the development of the Australian Marine Complex (AMC), stakeholder input was sought regarding the scope of the proposed works from industry groups, and marine construction and engineering companies in the sector in which the government was trying to support growth. These stakeholders indicated the scope of the initial proposal was too ambitious and possibly unnecessary, which resulted in a reduction in scope of the proposed works.[243]

Developments associated with the Perth City Link (PCL) indicate consideration was given to the best response to the requirements of the project, although in this case the situation is complicated by the project's nature. The PCL is primarily an urban renewal project, the principal aim of which is to reconnect Northbridge and the city, thus activating an under-utilised area that requires the sinking of public transport infrastructure in the area, including the Wellington Street Bus Station (WSBS).

[243] Mr Ross Holt, Chief Executive Officer, LandCorp, *Transcript of Evidence*, 23 June 2010, p.9.

The Perth Transport Authority (PTA) assessed a number of options to relocate the WSBS and, in 2004, a review conducted for the PTA concluded that a major bus station should be retained 'in the city centre at the current location [Wellington Street] and that it be closely integrated with rail facilities'.[244] The PTA continued:

> *It was determined that an underground facility was both feasible and the preferred option given the objectives of the land use planners for the land just west of the Horseshoe Bridge.*[245]

Importantly, despite this finding, the PTA conducted a further study to consider the option of redeveloping WSBS as an on-street facility and found that option would require a higher number of bus stands, would result in an interchange spread over a wider area and would have:

> *significantly higher operating costs and fleet procurement costs over a 30 year period and result in a major increase in bus movements along Wellington Street and side streets, significantly impacting on traffic circulating in the CBD.*[246]

(f) The Dangers of Poor Concept Development

The key danger associated with poor concept development is that a project will be delivered that does not represent value for money, through its failure to:

- meet clearly defined service delivery needs, resulting in an under-utilised or unnecessary asset;
- maximise the range of service delivery needs met by the project;
- consider innovative, non-asset based solutions;
- meet time or cost estimates; and
- identify and eliminate unnecessary expenditure.

As outlined in earlier sections of this chapter, many of these dangers relate to negative impacts on the likelihood of achieving value for money through the delivery of the project.

The concept development of the PCL concluded that an underground bus station was the preferred option in financial terms, particularly for the operation of buses in the city centre. However, what is not clear is whether the concept development behind the decision took into account the need to fit buses with the satellite tracking technology required to operate the new station.

The Committee understands the initial project cost of $205 million does not include 'any component for fitting real-time tracking or vehicle management systems on the existing bus

244 Submission No. 30 from the Public Transport Authority, 13 August 2010, p.2.

245 ibid.

246 ibid., pp.2–3.

fleet'.[247] The danger here being, if this technology was not included in the concept development, government has announced a project cost that does not reflect the full capital expenditure required to make the project fully operational.

Finding 12

The need for fitting buses with satellite tracking technology necessary for the operation of the Perth City Link underground bus station was not included in the original costing for the project.

In March 2010 the Auditor General published an audit of the *Planning and Management of the Perth Arena* and found the lack of a 'client agency' for the Perth Arena resulted in a failure to identify what was wanted from the project.[248] In other words, there had been no concept development process through which the client agency (now VenuesWest) could outline its service delivery needs and engage in a process of developing the project in detail.

Changes to the design following the tendering stage, in particular the decision to construct an underground car park, were found to have 'increased costs to the state and delayed completion of the Arena'.[249] It is possible that the need for an underground car park may have been identified earlier in the process if detailed concept development had been conducted by a lead agency, which may have lowered the likelihood and extent of cost overruns with the project.

It is accepted that concept development processes are not a panacea. Complex projects are likely to encounter complex problems; however, a properly conducted concept development process should enable agencies to have a highly evolved understanding of their projects, and the needs to which they are responding, and should enable the early identification and mitigation of project risks.

5.2 Concept Evaluation

SAMF notes that properly conducted project evaluation is a necessary contribution to 'sound resource allocation decisions by Government, to maximise the State's economic growth and social welfare'.[250] Project evaluation is necessary because it:

- facilitates better government decision-making by presenting a balance between the strategic, financial, economic and social issues;
- makes clear the up-front costs and recurrent obligations generated by the project;
- ensures proper examination of all available options and inherent risks; and

247 ibid., p.3.

248 Auditor General for Western Australia, *The Planning and Management of Perth Arena,* Report 1, 10 March 2010, p.16.

249 ibid., p.19.

250 Department of Treasury and Finance, *Project Evaluation Guidelines*, August 2005, p.2.

- provides a sound basis for review by DTF.[251]

There are five steps in the project evaluation process, broadly represented as processes designed to answer the following questions:

- Why is the project needed? – answered by Concept Development.
- What is the project's impact on agency performance? – answered by Performance Evaluation.
- Is the project affordable? – answered by Financial Evaluation.
- What is the project worth? – answered by Economic Evaluation.
- Should the project go ahead? – answered through consultation with the client agency, DTF and Cabinet.[252]

(a) Performance Evaluation

The first step in carrying out performance evaluation draws upon earlier work conducted during the concept development process, confirming each of the agency's outcomes and services that will be affected by the project's service delivery strategies and functions. Once identified, these impacts should be quantified in terms of the effectiveness with which they contribute to the agency's outcomes and objectives.

In the case of Main Roads Western Australia (MRWA), which identifies the 'reliable and efficient movement of people and goods' as one of its key outcomes,[253] the decision to construct the Perth to Bunbury Highway was supported by the quantification of efficiency gains following the construction of the new highway.

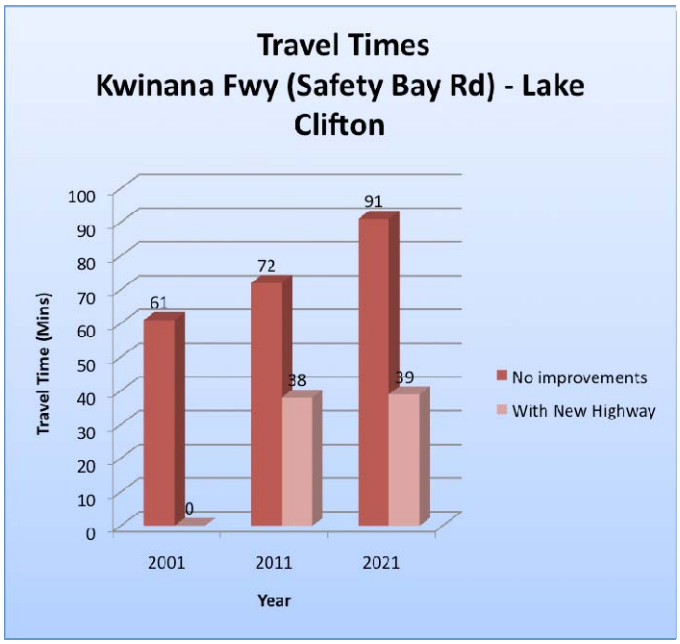
Figure 5.1 demonstrates the projected travel times between Safety Bay Road and Lake Clifton with and without the construction of the new highway.

251 Department of Treasury and Finance, *Project Evaluation Guidelines,* August 2005, p.2.

252 ibid., p.6.

253 Main Roads Western Australia, *Annual Report 2009*, 2009, p.17.

Figure 5.1 Travel Times[254]



The MRWA example demonstrates detailed studies were completed identifying and quantifying how the project was proposed to impact on the achievement of MRWA's outcomes. These studies were completed prior to commencing or committing to the project. Not all projects examined by the Committee follow this pattern.

The proposed Bunbury to Albany Gas Pipeline presents a useful example of a situation where government has made a commitment to a project prior to the completion of necessary performance evaluations. In its presentation to the Committee, the Department of State Development (DSD) acknowledged it had not done work relating to identifying outcomes and that it did not know when that work would be completed.[255]

(b) Financial Evaluation

Financial evaluation is aimed at demonstrating a project's financial viability and budgetary impact. For commercial projects this requires an estimation of the return on investment and project profitability, while for non-commercial projects a definition of the most efficient means of delivering the desired service delivery strategies is required.[256] A detailed financial evaluation should clarify the full financial consequences of the proposed project and should be done in the context of the project's economic and social evaluation.

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254 Submission No. 2 from Main Roads Western Australia, 15 January 2010, p.10.

255 Ms Gail McGowan, Deputy Director General, State Initiatives, Department of State Development, *Transcript of Evidence*, 16 June 2010, p.3.

256 Department of Treasury and Finance, *Project Evaluation Guidelines*, August 2005, p.15.

SAMF provides detailed steps to arrive at a financial evaluation assessing the value for money presented in the project, and notes the following regarding importance of financial evaluation:

> *The rigour and results of the financial evaluation have a significant influence on the relative rating and priority given to project options, where those with stronger cases for investment, with demonstrably higher benefits and lesser costs, will tend to be favoured over weaker options. In this context, projects that have been poorly evaluated, and that offer little confidence in the benefits afforded by the project, will be allocated lower priority.*[257]

The Committee received extracts of several financial evaluations from the various agencies it examined during the course of its Inquiry. Many contained commercially sensitive information that cannot be detailed in a public report. It is noted, however, that projects inspired by political action—that is, political projects, or government imperatives—often do not go through this rigorous financial evaluation process prior to funding approval, or do so in a truncated form, once a project has been approved. There is an increased danger in these circumstances of cost overruns or benefit shortfalls due to the failure to properly identify these factors.

(c) Economic Evaluation

Given the nature of most public sector projects, governments cannot reasonably expect to generate direct returns on their investments. As a result, comprehensive evaluation will need to include measures of wider economic benefits in order to assist with the decision to proceed with a project or not.[258] Cost-benefit analysis (CBA) is the most commonly used economic evaluation technique, and follows a similar process to that required for financial evaluation.

In 1997 the then Department of Commerce and Trade commissioned a 'broad macro-economic assessment of industry demand to estimate the economic and financial impact' of the AMC development.[259] This undertaking supports DoC's stated outcomes, which include seeking the 'enhancement of the State's economic sustainability and prosperity'.[260] To that end, the analysis found that the investment in the Common User Facility (CUF) could result in Western Australia attaining a 2.5 per cent share of future additional project work for the state, estimated at the time to be worth approximately $100 million per annum in additional work.

Furthermore, it was estimated that $160 million in repair and maintenance work could be generated from the site. At full capacity, the AMC was estimated to result in $260 million per annum in additional economic activity and, at full site capacity, would employ over 1,600 individuals directly, and over 4,200 individuals indirectly.[261]

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257 ibid., p.22.

258 ibid., p.23.

259 Submission No. 23 from the Department of Commerce, 27 May 2010, p.10.

260 Department of Commerce, *Annual Report 2008–2009*, September 2009, p.26.

261 Submission No. 23 from the Department of Commerce, 27 May 2010, p.11.

This demonstrates it is possible that different evaluation criteria can overlap. The DoC, for example, identifies one of its agency outcomes—against which it must conduct a performance evaluation—as the promotion of economic development. The AMC project itself was designed to stimulate economic development, so it is no surprise that the economic and performance evaluation metrics should be quite similar.

Similar to the experience outlined with financial evaluation, many projects considered to be 'government imperatives' do not appear to have undergone a rigorous economic evaluation. In relation to the State's provision of Common Use Infrastructure (CUI) for the Oakajee Port project, the Under Treasurer noted the following:

> *At various points through the EERC process, advice was provided by DTF through to government on [Oakajee]. Being perfectly honest, as I am required in this forum, this was one of those projects where it was a clear commitment of the government. So it was one where our attention, after initial analysis, turned to what the best way is to deliver this, rather than questioning whether or not it was required or what the cost–benefit was.*[262]

In response to a direct question relating to the conduct of a CBA, DSD responded:

> *The decision for Government to fund the CUI [the Common Use Infrastructure of the Oakajee Port] was a policy decision. This reflected the Government's intention to broaden the scope of the project and enable the Oakajee port to be developed as a genuine multi-user, multifunction port over time with close links to the Oakajee Industrial Estate that the State is developing.*[263]

In relation to the benefits associated with government involvement with Oakajee, DSD provided the following information:

> *The multi-user, multi-function nature of Oakajee Port is different to other ports that are currently being developed that are largely single-product and single user (or a defined small number of users). Government has traditionally owned CUI infrastructure at multi-user, multi-function ports (including Geraldton, which Oakajee will be an extension of).*
>
> *The Mid West iron ore industry is characterised by a number of smaller operators. Unlike other port developments that have been developed in the past (such as iron ore ports in the Pilbara) or are under development now, none of the companies or mining projects are sufficiently large or commercially robust enough to justify investment in the port in their own right.*
>
> *Government investment in (and control of) the CUI provides the opportunity to ensure the development is designed to cater for the longer term needs of the State and the region.*[264]

It might be true that the government's investment in the CUI will 'cater for the longer term needs of the State and the region'. However, without the conduct of a rigorous economic evaluation, in

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262 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.4.

263 Submission No. 32 from the Department of State Development, 3 September 2010, p.3.

264 ibid.

which all options are considered, it is not clear that the State's investment in OPR in this form represents the most effective means for catering to the State's longer term needs.

The Oakajee project summary provided to the Infrastructure Australia Council (IAC) in January 2009 did not include a profiling assessment; nor did it contain the result of an economic appraisal.[265] The IAC was instead informed that:

> *the Western Australian Government has identified Oakajee – a greenfield site north of Geraldton – as its preferred option for a new port.*
>
> *The Western Australian Government's original request was for funding for common use facilities at the port for iron ore purposes. The revised submission (January 2009) re-focuses on establishing infrastructure to enable a multi-user, multi-purpose port. This will lay the foundations for a future 'Oakajee Industrial Estate' for industrial expansion in the region and expanded, integrated transport infrastructure.*
>
> *Due to the recent changes to the approach of the submission and the broader focus that it now entails, it has not been possible for the Western Australian Government to undertake a cost–benefit analysis in the form outlined by Infrastructure Australia.*[266]

In February 2010 the Australian National Audit Office (ANAO) was informed by Infrastructure Australia (IA) that:

> *the Oakajee Port Development – Common Use Infrastructure proposal was subsequently assessed as not being sufficiently developed to meet the criteria for recommendation as being 'ready to proceed'. It was however assessed as having sufficient potential merit to warrant further consideration, following development of the business case. As a result, it was included in the 'priority pipeline'.*
>
> *The assessment of the Oakajee Port Development – Common Use Infrastructure proposal will be continued when the Western Australian Government provides a copy of the bankable feasibility study currently being finalised by the Oakajee Port Development.*[267]

The Committee's request to gain access to the Bankable Feasibility Study (BFS) was denied by DSD on the grounds that it contains commercially sensitive information.[268] Despite this, it seems reasonable to assume that the BFS fills the role, at least in part, of a traditional business case, and contains an evaluation of the economic impact of the project as a whole. It is less clear, however, that the BFS contains an economic evaluation of the government's specific contribution to the CUI, although it should be noted that the business case to be developed subsequent to the delivery

265 Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Canberra, 2010, p.139.

266 ibid.

267 ibid., pp.139–140.

268 Submission No. 31 from the Department of State Development, 3 September 2010, p.1.

of the BFS will seek to analyse the 'economic outcomes that the CUI will deliver as a standalone asset'.[269]

Nevertheless, the Commonwealth contribution to the project is contingent on the analysis contained in the BFS demonstrating a positive cost-benefit outcome[270] and a commercial rate of return.[271] If a positive cost-benefit outcome is not demonstrated in the BFS, and the Commonwealth does not proceed with its equity injection, it is not clear what impact this would have on the state government's contribution to the project.

Finding 13

Economic evaluation is an important element for project selection, particularly for projects responding to a perceived economic need, as it allows the best option(s) to be selected.

Finding 14

The decision to fund the Common Use Infrastructure of the Oakajee Port project was made without a cost-benefit analysis. Therefore, at the time the decision was made, it was not clear whether this arrangement represented the best value for money for the state.

Finding 15

The Commonwealth funding for the Oakajee Port Common Use Infrastructure is contingent on the Bankable Feasibility Study demonstrating a positive cost-benefit outcome and commercial rate of return.

Recommendation 5

The Minister for State Development should publish details of any economic evaluation undertaken as to the benefits derived from the commitment of public funds for the Oakajee Port Common Use Infrastructure project.

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269 Submission No. 2 from the Department of the Premier and Cabinet, 11 February 2010, p.11.

270 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities*, June 2010, p.58. IA will make a recommendation regarding the project once it has reviewed the business case.

271 Ms Anne Nolan, Director General, Department of State Development, *Transcript of Evidence*, 5 March 2010, p.20.

(d) Social Impact Analysis

Social impact analysis identifies sectors of the community that would gain and lose should a project go ahead. SAMF identifies common social impact areas as including: the environment; heritage; sustainability; native title; quality of life; and law and order. [272]

There is difficulty assigning quantifiable values on social impact categories. Therefore, SAMF requires that they be assessed in the following terms:

- *whether the impact is isolated, localised or far-reaching;*
- *the expected duration, timing and spread of the impact;*
- *the extent specific target groups in the community and/or industry will be affected, either positively or adversely, and*
- *the level of political sensitivity and public interest.*[273]

Community consultation is helpful in assisting to identify and analyse the significance of social impacts.[274] Western Power established a Community Reference Group in relation to its Southwest Transmission Line Reinforcement Project, a regulatory requirement under the New Facilities Investment Test (NFIT).[275] As a result, an assessment was made that a number of environmental and social issues in relation to the proposed Eastern Terminal were sufficiently significant to warrant the project's alteration. Western Power developed an alternative option because those issues 'would not be resolved in time to complete the project'.[276]

Sometimes projects are chosen largely on the basis of potential socio-economic benefits. The Ord River Stage 2 project could only be justified on the basis of the socio-economic benefits it could provide for the local Indigenous communities.[277] As part of its 2008 business case, Marsden Jacob commissioned a study which examined the social impact of the project, highlighted the significant social disadvantage in the area and claimed that the fortunes of the Indigenous community 'were bound up in the Business Case for Ord Stage 2'.[278]

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272 Department of Treasury and Finance, *Project Evaluation Guidelines*, August 2005, p.26.

273 ibid., p.27.

274 ibid.

275 Submission No. 11 from Western Power, 19 April 2010, p.8.

276 Western Power, *Proposed Major Augmentation to the Electricity Network – 330KV Transmission Line to Support Electricity Load in the Perth Metropolitan Area*, November 2008, p.35 in Submission No. 11 from Western Power, 19 April 2010.

277 The reference in this report to Ord Stage 2 relates to the provision of agriculture-related infrastructure and not the Commonwealth-funded social infrastructure that is being provided in parallel.

278 Taylor, J., *Ord Stage 2 and the Socioeconomic Status of Indigenous People in the East Kimberley Region*, August 2008, p.140, in Department of Industry and Resources, *Ord Expansion Project: Business Case Evaluation*, report prepared by Marsden Jacob, August 2008.

The study found that the forecast economic development eventuating from the project could alleviate the cost to government in terms of welfare provision and other 'social pathologies'. However, no clear evidence was presented of how clear social outcomes would arise from the expenditure. The study also suggests the local Indigenous community want further developments to occur 'in ways that protect environmental and cultural values', which it was noted will introduce additional complexities for the development of the Ord River project.

(e) Project Recommendation

The final stage in the evaluation process is to provide a formal recommendation as to which project should proceed and which should not. SAMF requires agencies to evaluate the results of the evaluations in terms of prioritising the following factors:

- Benefits – determined by the extent to which a project is considered to contribute to defined government goals;
- Importance – influenced by a variety of factors, including government commitments, the urgency of the project, the consequences of not taking action and public expectations; and
- Achievability – an assessment of an agency's capacity to deliver a project, the reliability of estimates, the degree of community support or opposition, and the potential for scope and cost creep. [279]

SAMF notes that projects that have been poorly evaluated or that do not provide sufficient confidence in the associated benefits or cost projections are more likely to be afforded lower priority by government.

It is at this stage that DTF reviews evaluations and provides advice to the Treasurer and the Expenditure and Economic Review Committee (EERC). DTF's role is to verify the veracity of the assumptions underpinning the evaluations and to assess whether the evaluation methodology utilised is consistent with SAMF requirements.[280] Finally, agencies are required to present the results of their evaluations in the form of a business case.

5.3 Development of the Business Cases

(a) Adherence to the Strategic Asset Management Framework

Business cases are the primary tool for sound project planning, strategic assessment and investment decision making. They pull together a high level of detail on the results of the preparatory work the agency has completed through the strategic planning and concept development and evaluation phases. Ideally, the business case outlines the decision making

[279] Department of Treasury and Finance, *Project Evaluation Guidelines*, August 2005, p.29.

[280] ibid., p.30.

process and associated risks; an analysis of the costs, benefits and social impact; and the required capital and recurrent funding, including financing options.

Cabinet and the EERC use business cases in deciding which of the multitude of competing projects will be funded. As the *Economic Audit Committee Report* (EACR) states:

> *under the SAMF, planning for individual projects that involve the delivery of assets requires the preparation of high-quality cost-benefit based business cases and project delivery plans that help Cabinet make informed decisions about funding for such projects.*[281]

Comprehensive and well-developed business cases are more likely to result in improved planning and budget appropriation processes, as well as reduced risk and increased certainty for government capital investment than those which are developed 'on the run'.

It is reasonable to suggest that if agencies are following SAMF and IA guidelines, the preparation of robust business cases should be a relatively straightforward process. Nevertheless, evidence suggests that government planning and delivery of infrastructure 'is often based on insufficient business case rigour and fails to meet time and budget constraints'.[282]

Building Management and Works (BMW) highlighted the following problems associated with business case preparation:

- business cases prepared late in the planning cycle;
- business cases developed with insufficient alternative options considered and a lack of objectivity by agencies to explore options other than the initial preferred option; [… and]
- an agency culture of understating project costs and delivery timeframes at business case stage, resulting in regular requests for budget increases and milestone extensions during the project definition and procurement stages.[283]

Similarly, the Department of Treasury and Finance, Strategic Projects (DTF-SP) acknowledges 'a number of investment decisions on major non-residential building projects have been made without robust planning, and suggested that:

> *over time, the pattern of Government investment decision making on major new non-residential building projects without business cases has lead to a culture within the public sector that undervalues the importance of business cases as the basis for investment decision-making…to the detriment of high-quality project planning*[284]

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281 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.84.

282 ibid., p.79.

283 Building Management and Works, Department of Treasury and Finance, *Works Reform Business Solution Plan*, Government of Western Australia, Perth, June 2009, p.15.

284 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.3.

This response highlights that the nature and/or urgency of given projects, combined with the nature of the political cycle, does not always allow for robust preplanning and forecasting.

Evidence presented to the Committee revealed mixed adherence to guidelines for business case development, ranging from the detailed and well developed to the significantly underdeveloped. For a range of reasons, it seems agencies might prepare an initial CBA for their projects, but do not always go on to incorporate this into a well-developed business case.

It is accepted that 'the potential for poorly prepared or non-existent business cases to result in inefficient and ineffective service delivery outcomes is considerable. Scope, cost and time blowouts in the delivery of infrastructure are practically inevitable'.[285]

Due to commercial-in-confidence considerations, the Committee cannot sufficiently assess in detail the business cases for each project it considered. DTF-SP Executive Director, Mr Richard Mann, believes the decision to proceed with the One40 William Street project, which is 'part of the overall new Metrorail process', was:

> *subject to government consideration of an extremely detailed and robust business case which fully examined a range of options and which in turn was based on a very thorough examination of rail routes through the CBD that formed a part of a comprehensive master plan.*[286]

DTF-SP sees the One40 William Street project as a success, with 'no significant cost issues', demonstrating that 'if the detailed planning forms the basis of government decision-making, there is a good likelihood of a very good result'.[287]

Despite the best efforts of agencies, Under Treasurer Tim Marney recognises 'we have a long way to go to build our capacity in developing robust business cases that we can then convert into project definition plans'.[288]

This comment reflects one of the key problems identified in the *Works Reform Business Solution Plan*, namely the 'poor business case development for capital investment'.[289] In light of this, the Government's Works Reform policy aims to strengthen asset planning and business cases for capital investment, with BMW to support agencies through the various stages of the SAMF planning processes.[290]

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285 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.84.

286 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.8.

287 ibid.

288 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.5.

289 Building Management and Works, Department of Treasury and Finance, *Works Reform Business Solution Plan*, Government of Western Australia, Perth, June 2009, p.14.

290 Building Management and Works, Department of Treasury and Finance, 'Works Reform. Reform Focus', nd.; and Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.5.

The state government currently has a non-residential buildings portfolio of over $20 billion. Management of that portfolio has been devolved to agencies and BMW is currently developing strategies to allow government to better manage its non-residential buildings portfolio, including moving away from reactive maintenance.[291] This means that for new buildings, BMW aims to introduce sustainable maintenance plans.

High risk projects or those over $100 million are allocated to DTF-SP. Like BMW, DTF-SP has 'dedicated project planning units…solely established for business case development'.[292] DTF-SP submits that, in particular, 'its role in leading the development of business cases for high-risk projects…provides a unique opportunity for a centrally managed, consistent and robust approach from the early stages of project planning'.[293]

The implementation of the Works Reform Program (Works Reform) is expected to enhance the role of DTF in the development and provision of public assets, which will mean Capital Works projects will be managed in a more robust, effective and consistent way, in line with SAMF.

Finding 16

A well-developed business case is essential for effective infrastructure decision-making, and can only be as robust as the concept development and evaluation processes that underpin it.

Finding 17

The involvement of the Department of Treasury and Finance's Building Management and Works, and Strategic Projects in the development of business cases has the potential to enhance both Strategic Asset Management Framework compliance and the quality of agency business cases.

(b) Getting Business Cases to Cabinet

As has been noted at various points in this report, SAMF is a DTF responsibility. As Mr Marney stated at hearing, SAMF is DTF policy and it is the responsibility of DTF to ensure that it works.[294] The incorporation of Works into DTF, and the creation of BMW and DTF-SP as distinct business units alongside Treasury, have allowed for much higher levels of collaboration.

291 ibid

292 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6.

293 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.5.

294 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.5.

According to Richard Mann, this 'facilitates the involvement of the Treasury analysts right through the business case development process rather than in a pure review role'. [295] DTF currently submits business cases led by BMW and DTF-SP to government for consideration of the investment decision and according to Mr Mann, this helps to:

> *ensure that…service delivery requirements are properly incorporated into the options that we put forward in any business case.*[296]

Collaboration within and between DTF and agencies should result in greater agency confidence that the project will receive EERC support. It should also result in a more effective across-government strategic asset investment plan, something that is difficult to achieve 'on an individual agency basis'.[297]

Notwithstanding the above, at the present time, BMW, DTF-SP and Treasury do not prioritise the projects put forward to the EERC. Mr Tim Marney outlined the process of providing recommendations to government as follows:

- Agencies submit their capital works proposals to Treasury;
- Treasury analysts work with agencies to better understand the nature of the proposals;
- Treasury analysts review agencies' capital works proposals, evaluating them against objective criteria to achieve some consistency 'at least in absolute terms of the cost–benefit of individual capital proposals';
- Projects are then brought together for relative assessment;
- Forums of Treasury analysts are held at which they present their analyses; and
- The results are considered by the broader Treasury executive, a relative ranking is determined, and recommendations are sent to the EERC.[298]

Following this process, government makes its decision, usually in consultation with line ministers and ministers' agencies through the EERC processes.

As detailed previously, the three assessment criteria used in the budget process are importance, benefits and achievability. These criteria do not receive equal weighting, and a subjective or qualitative judgement is made between the three. As the Under Treasurer explained, it is difficult to compare the cost-benefit of a school and a new hospital wing with the length of a road in a regional area or with an additional port berth. Mr Marney advised the Committee that:

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295 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6.

296 ibid., p.6.

297 ibid., p.5.

298 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.1 and p.2.

> *there is no explicit scoring system. The projects are evaluated against those criteria, but it would be, I think, seriously misplaced rigour to pretend that you could score them rigorously and compare those scores in a relative sense to form other recommendations.*[299]

The importance of the project to government and the importance of the ongoing service delivery of the critical services of law and order, health, education, child protection and so on achieve a higher ranking in considerations than other projects that might be considered more discretionary. Understandably, another factor that informs Treasury assessment is the quality of the agencies' proposal. As Mr Marney pointed out:

> *some agencies will put forward a project with very well articulated benefits because it has mapped its service delivery needs quite rigorously and therefore the benefits are clearly linked to their service outcomes. In other cases, it is not as direct. … If the benefits cannot be articulated well and easily, we must question whether there are any benefits.*[300]

5.4 Fast-Tracking Projects

The delivery of effective and efficient infrastructure requires not only a robust planning and delivery system, but agency adherence to that system. Although the SAMF process is accepted as providing a robust planning and delivery framework, it is generally acknowledged that not every infrastructure project is the result of agencies' identification of their service delivery needs. Some projects are generated through decisions made at the political level, often reflecting election commitments or government priorities. As the EACR notes:

> *government will introduce new infrastructure projects into its overall planning at short notice, or bring forward or defer already planned projects, in order to meet or pursue political objectives, or to take advantage of a short-lived window of strategic opportunity.*[301]

DTF-SP accepts that 'circumstances sometimes dictate that key decisions cannot wait for a business case to be prepared and must be based on the information available at the time'.[302] Nevertheless, DTF-SP also argues, and the Committee agrees, in order to minimise the risks to the State, this should be the exception and not the rule.[303]

While there is a clear role for vision in government, and governments sometimes see the need to deliver what can be described as iconic projects, the approaches to such projects attract the risk of downgrading, distorting or ignoring 'many of the key elements of good project management'.[304]

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299 ibid., p.2.

300 ibid.

301 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.98.

302 Submission No. 16 from Department of Treasury and Finance Strategic Projects, 31 May 2010, p.3.

303 ibid.

304 Prasser, Scott, 'Overcoming the "White Elephant" Syndrome in Big and Iconic Projects in the Public and Private Sectors'', pp.47–67 in Wanna, John (ed.), *Improving Implementation: Organisational Change and Project Management*, ANU e-Press, Improving Implementation: Organisational Change and Project Management, 2007, p.51.

Several problems are identified as being associated with government proposed 'iconic,' 'landmark' or 'signature' projects, the most relevant here being risks associated with:

- overt and covert political interference in setting the project goals; and
- timeframes that are 'compressed, uncertain, or established to meet election cycles', with minimal stakeholder consultation.[305]

The EACR also notes that 'a study of some major projects in the public sector in Australia has pointed to the importance of appreciating that political imperatives should not replace the need for a strong business case'.[306] While the issue of risks are discussed elsewhere, it is important to note here that undertaking a project on a fast-tracked basis significantly compresses the planning process, thus:

> *raising the risk that SAMF principles may be bypassed or dealt with superficially in order to meet deadlines imposed by the Government. Once again, the risk is that this will result in Cabinet making decisions about such projects on the basis of less than full information, to the potential detriment of the State.*[307]

In such circumstances, 'Cabinet may decide to proceed with a poorly evaluated project that has an excessively low estimated cost or an overly optimistic completion date when more extensive analysis would have given a clearer picture of the risks associated with the project'.[308]

DTF-SP and BMW acknowledge that the need to fast-track projects is a fact of life, but this does not 'alleviate the agency or the entity responsible for delivering that project from complying with good asset management policy and practice'.[309] It is reasonable to expect that all infrastructure decisions will be based on the best information possible.

The need to fast-track projects has been considered in the Works Reform process being undertaken by DTF. The EACR states that 'where infrastructure projects are fast-tracked, the application of SAMF becomes even more critical to ensuring successful project outcomes, notwithstanding the shorter planning timeframes'.[310]

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305 ibid.

306 Wanna, John (ed.), *Improving Implementation: Organisational Change and Project Management*, ANU e-Press, Improving Implementation: Organisational Change and Project Management, 2007, cited in Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.84.

307 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.98.

308 ibid.

309 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.4; Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010; and Ms Josephine Quealy, Program Manager, Economic Audit Implementation Unit, Department of Treasury and Finance, Briefing, 10 August 2010.

310 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.98.

Fast-tracking is not about truncating the SAMF process, applying it selectively, or simply going through the process faster.[311] Although the agency responsible for delivering a fast-tracked project must still comply with SAMF and do so quickly, 'it still needs to do it well'.[312]

DTF-SP will, in accordance with Works Reform, assist agencies with this fast-track process. As mentioned, agencies are required to develop Strategic Asset Plans (SAPs) ten years out, and also are encouraged to begin preparation of good quality business cases several years in advance of the four year estimates period. It is the Committee's view that the provision of well considered and developed business cases also has the potential to reduce risks associated with projects that arise through government imperatives.

DTF believe that while it is possible to meet all SAMF requirements in a reduced time frame, it is a very resource intensive process for all involved,[313] as proposing agencies need to resource appropriately and undertake that planning in a shorter period.

The EACR noted the need for implementing SAMF to fast-tracked projects 'through a process that applies enough resources in a truncated timeframe to ensure informed decision-making by Government and sufficient clarity for planning, procurement and delivery of the project'.[314] The resources should be sufficient to allow necessary planning and scoping studies to be conducted.

Finding 18

There will always be a need to fast-track some infrastructure projects due to changing circumstances and political imperatives.

311 Ms Josephine Quealy, Program Manager, Economic Audit Implementation Unit, Department of Treasury and Finance, Briefing, 10 August 2010; and Mr Anthony Kannis, Executive Director, Infrastructure and Finance, Department of Treasury and Finance, 2 August 2010.

312 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.4.

313 Ms Josephine Quealy, Program Manager, Economic Audit Implementation Unit, Department of Treasury and Finance, Briefing, 10 August 2010; and Mr Anthony Kannis, Executive Director, Infrastructure and Finance, Department of Treasury and Finance, 2 August 2010.

314 Economic Audit Committee, *Putting the Public First Partnering with the Community and Business to Deliver Outcomes*, Government of Western Australia, Perth, October 2009, p.98.

Finding 19

Applying the Strategic Asset Management Framework processes to fast-tracked projects will help ensure the best possible infrastructure outcomes.

Recommendation 6

For fast-tracked projects, it is important that the Strategic Asset Management Framework be applied to the greatest extent possible to ensure optimal outcomes.

CHAPTER 6 DELIVERING THE ASSET

6.1 Project Definition Planning

The Project Definition process was outlined in some detail in Chapter 3 of this report, where it was noted that the process involved preparing documentation to take a well-defined project through to tender. It involves taking concepts that were approved in the business case and further defining them, including through the identification of the precise functions and physical areas.

This stage of the asset acquisition process has not been the principal focus of this Inquiry and, therefore, a great amount of evidence has not been sourced on this topic. This is not to suggest that project definition planning is unimportant. Rather, projects should only reach this stage of the process once they have gone through robust concept development and evaluation—as required in the Strategic Asset Management Framework (SAMF), which outlines a sequential process for asset acquisition. The risks associated with commencing the project definition process prior to the completion of a detailed business case outlining the precise scope and functions of the proposed project are also acknowledged. In particular, there is a risk that the project will fail to deliver the intended benefits to the state and, relatedly, fail to deliver value for money.

The experience of the Fiona Stanley Hospital (FSH) project is of relevance in this context. The management of the project was the subject of a report by the Western Australian Auditor General (OAG). As noted earlier, SAMF is structured sequentially in order to ensure that projects are scoped in sufficient detail before commencing on the next stage in the process. The OAG found, in relation to the FSH project, that SAMF stages—including business case, procurement plan and project definition plan—had been run concurrently in order to meet announced timeframes.[315] This was found to have resulted in sub-optimal planning in terms of both cost and time projections.

Table 6.1 provides an outline of the effect of the concurrent preparation of the critical elements of the processes outlined in SAMF. The initial cost estimate for FSH (at that time known as the Southern Tertiary Hospital) included in the *2004–05 State Budget* was $420 million.[316] This estimate was made prior to the commencement of a business case and prior to scoping of the hospital in terms of size or the services it was to provide. Work on the business case commenced in September 2005,[317] and the initial scope of the hospital was detailed at the same time. The *2006–07 State Budget* identified a revised cost of $742 million for the project.[318] In November 2006 the scope of the hospital again increased and the *2007–08 State Budget* contained a revised cost of $1.092 billion.[319] In April 2007 the Business Case was submitted five months late to the FSH Steering Committee, which rejected it on the grounds that:

315 Auditor General for Western Australia, *Fiona Stanley Hospital Project*, Report 5, 23 June 2010, p.22.

316 Department of Treasury and Finance, *2004–05 Budget: Budget Statements, Budget Paper No. 2*, May 2004, p.547.

317 Auditor General for Western Australia, *Fiona Stanley Hospital Project*, Report 5, 23 June 2010, p.23.

318 Department of Treasury and Finance, *2006–07 Budget: Budget Statements, Budget Paper No. 2*, May 2006, p.535.

319 Department of Treasury and Finance, *2007–08 Budget: Budget Statements, Budget Paper No. 2*, May 2007, p.581.

- the cost estimates lacked detail and were insufficiently robust;
- there was a lack of project risk assessment or mitigation strategies; and
- recurrent costs associated with the hospital were not defined.[320]

The project definition plan was submitted at the same time as the business case and was based on an assumption that the preferred option in the business case would be approved.[321] In a significantly revised business case submitted in December 2007 the scope and size of the hospital was again increased and the final figure of $1.76 billion was arrived at. Government approved the business case in June 2008.[322]

Perhaps the most striking feature to present itself in Table 6.1 is that, once the final business case and associated project definition plan were presented, the cost of the project appeared to stabilise at $1.76 billion. The OAG found that significant scope changes were responsible for increasing both the area and cost of the project. Once the scope had been finalised, costs appear to have been kept under control.

Whilst this Inquiry did not extensively examine project definition planning, the experience of the FSH illustrates the risks associated with failing, first, to adequately scope the extent of the project before announcing timing and costing estimates and second, (and most relevantly to this section), failing to have a solid understanding of the scope before moving to the project definition phase. The OAG's view on the effect of this is worth quoting at some length:

> *The outcome of the additional time and effort was a more detailed project scope, a revised and significantly increased, but more realistic project budget, and a longer delivery timeframe. This provided government with greater certainty before inviting tenders for early contractor involvement. It also reduced the risk of potential scope changes later in the process, when changes are likely to cost more and lead to unplanned construction delays.*[323]

While the FSH is not a project that was examined in detail by the Committee, it serves to illustrate a number of major points:

- Committing to a budget for a project prior to it being properly scoped has a flow on effect for budget forward estimates.
- Announcing a budget for a project prior to it being properly scoped means that the budget is not based upon a complete assessment of the opportunity costs of proceeding with the project.

320 Auditor General for Western Australia, *Fiona Stanley Hospital Project*, Report 5, 23 June 2010, p.23.

321 ibid.

322 ibid.

323 ibid.

Table 6.1: Budget and Scope Timeline for the Fiona Stanley Hospital[324]

Date	Business Case Event	Scope	Budget
2004–2005		Total area for hospital not yet determined	$420 million
September 2005	WA Health commences work on the Business Case for FSH.	Total hospital area 100,000 m^2 Services and facilities identified: –general acute, rehabilitation, and acute mental health inpatient facilities –emergency department –neonatal nursery, renal dialysis –operating theatre and procedure suite facilities –medical imaging, radiotherapy, pathology –ambulatory, therapy and day rehabilitation facilities furniture, fixtures and equipment –non clinical support facilities (kitchens, administration areas) –education and research facilities	$742 million
November 2006		Increase in hospital total area to 116,000 m^2 Amended and additional services and facilities: –increased areas for pathology, theatres, bio-medical engineering and cell tissue manufacture –advanced medical imaging	$1.092 billion
April 2007	Business Case submitted to the FSH Steering Committee, which was rejected due to: cost estimates lacking detail and being insufficiently robust; a lack of project risk assessment or mitigation strategies; and recurrent costs associated with the hospital were not defined.		
December 2007	Final business case, including project definition plan, submitted for review.	Increase in hospital total area to 144,000 m^2 Amended and additional services and facilities: –single bed room increase from 40% to 83% of total hospital beds –ecological sustainability development to improve building quality –efficiencies and energy consumption design changes to promote staff well-being in working environment –extra furniture, fixtures and equipment due to increase in clinical services	$1.76 billion
June 2008	Business Case approved by government.		
April 2009		No increase in total hospital area RPH to remain open Amended and additional services and facilities: –neonatal, obstetrics, maternal mental health unit	$1.76 billion

[324] ibid., p.17 and p.23.

- Public confidence in government's ability to provide value for money through the provision of infrastructure most likely will be undermined.

6.2 Delivery Models

Once a project definition plan has been completed, it is sent to the relevant agency's chief executive officer and the responsible minister for approval for it to proceed to the delivery stage. The delivery stage is the point in the asset acquisition process during which the project will be designed and constructed within the limits of the approved business case and project definition plan.

This section of the report focuses on the options available to government utilising non-private finance initiatives. Chapter 8 details where and how a project might be procured utilising a Public Private Partnership (PPP) model.

It is at the Project Definition stage that the final confirmation as to the type of delivery methodology should be made.[325] Large projects where multiple elements are being delivered—for example, the Mandurah Rail Line—can proceed using combinations of the contract types detailed below. The Western Australian Government's *Infrastructure Procurement Options Guide* recommends that the following issues should be considered when deciding the best procurement methodology:

- *understand project drivers and constraints including budget, timelines, stakeholder commitments, market capacity, etc;*
- *rigorously investigate alternative procurement delivery models before project options are finalised in the evaluation stage;*
- *involve key stakeholders and experts as early as possible in the planning and development of projects;*
- *challenge assumptions in order to better achieve desired outcomes; and*
- *use practical analytical techniques in the decision making process.*[326]

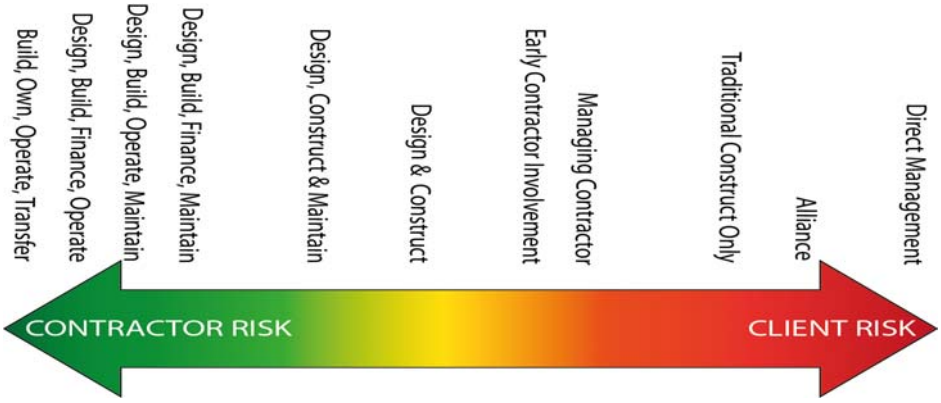
The following section provides an overview of a number of the contracting models available to government agencies and includes discussion of examples where appropriate.

Diagram 6.1 below is adapted from a Department of Treasury and Finance (DTF) document and outlines the continuum of government risk exposure through the various contracting models outlined on the following pages.

325 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, 2009, p.6.

326 ibid.

Diagram 6.1: Continuum of Government Risk Exposure[327]



(a) Construct Only Models

'Construct only' contracts represent the traditional model for the delivery of major government financed infrastructure projects in Western Australia. It is the longest used and best understood procurement type, and necessary skills for the implementation of this type of model are readily available in Western Australia.[328] In this style of contract, the project proponent will generally engage an independent designer who will design the scope of work, typically before a construction contract has been awarded.[329] Usually, contracts of this type allow for adjustments in price with the consequence that the final payment made to the contractor will usually not equal the earlier amount agreed.[330] According to the New South Wales Government's *Procurement Practice Guide*, tenders for the construction contract should not be released until the work has been fully designed. The selected construction contractor will then have the responsibility to ensure that the completed architectural design is ready for construction.[331] Construct only contracts are generally used when an agency seeks to maintain as much control over the design of a project as possible. Other circumstances where this contracting model may be used include when:

- the scope is defined and changes to design or scope creep are unlikely;[332]
- the work involves the construction of repetitive types of facilities, including schools and police stations;[333]

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327 Adapted from: Mr Richard Mann, Executive Director, Department of Treasury and Finance Strategic Projects, 'Procurement Strategy for Delivery of WA Government Major Projects' (Briefing), 21 July 2010. Available at: http://www.ceiid.wa.gov.au/Docs/SAIP2010/CEIID_SAIP_Breakfast_Presentation_2010.pdf. Accessed on 28 September 2010.

328 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, 2009, p.18.

329 Stephenson, Andrew, Clayton Utz, *Alliance Contracting, Partnering, Cooperative Contracting Risk Avoidance or Risk Creation*, June 2000, p.2.

330 ibid.

331 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.3.

332 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, 2009, p.17.

333 ibid.

- there is a large pool of potential tenderers, which leads to a competitive selection process;[334]
- there is enough time within the project program for the detailed design work to be completed before tenders are called; and [335]
- the best design can be developed without having to involve possible builders or other specialists.[336]

Benefits of this contracting model include the ability of an agency to exert maximum control over the design of a project as it develops, which ensures that unique requirements are incorporated into the design. In terms of the projects examined by the Committee, it is noteworthy that the Perth Police Complex (PPC)—a project that has already been highlighted as being particularly innovative—is being progressed using a construct only contracting model.[337] The maximised ability of the Western Australia Police to influence design is reflected in the unique approach to integrating various policing functions into the one building.

The first stage of Western Power's Mid-West Energy project is to be completed using a construct only contract.[338] The second stage of this project has not yet been approved.

(b) Design and Construct

With 'design and construct' contracts, the project proponent prepares a design brief which outlines the functional and key user requirements for the works, but the brief is 'less fully developed than the design documentation required for a Construct Only contract'.[339] The project proponent will then seek tenders for the completion of the works outlined in the design brief.[340] Advocates for this style of contracting note that—subject to good management—there is less scope for cost overruns than under a traditional construct only model.[341] This is partly due to the fact that the contractor is usually better placed to manage design risks, especially given that the contractor prepares most of the design and associated documentation.[342] Generally, design and construct contracts are appropriate where:

- there is no requirement for an agency to control the design or determine design details;

334 ibid.

335 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.3.

336 ibid.

337 Hon. Rob Johnson, MLA, (Minister for Police; Emergency Services; Road Safety), *Tender Announced for Perth Police Complex*, Media Statement, 26 August 2010.

338 Main Roads Western Australia, 'Briefing on the State Asset Investment Plan 2010–2014, 21 July 2010. Available at: http://www.ceiid.wa.gov.au/Docs/ Accessed on 18 September 2010.

339 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, 2009, p.18.

340 ibid.

341 Stephenson, Andrew, Clayton Utz, *Alliance Contracting, Partnering, Cooperative Contracting Risk Avoidance or Risk Creation*, June 2000, p.2.

342 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.3.

- the likelihood of the project brief changing once a contract has been entered into is low; and
- contractors are expected to offer innovative design solutions that result in cost savings.[343]

It is worth noting that the Perth Arena was initially offered as a design and construct contract; however, in an attempt to minimise the contract price, the contract was changed to a construct only model, which resulted in the State retaining the risk of cost increases and delays arising from design changes.[344]

(c) Managing Contractor

The 'managing contractor' model was developed in Australia in the early 1990s by Clayton Utz in response to the needs of the Department of Defence. Since that time it has been used by Defence for most of its large multi-element projects,[345] and is the contracting model utilised for the construction of the FSH.[346] This model is also being used for aspects of works associated with the East Kimberley Expansion Project, including $92 million for education and health projects.[347] The New South Wales Government notes that Managing Contractor contracts are only needed for 'major projects with special needs'. [348]

The managing contractor model generally involves a two-stage contract consisting of an initial planning stage, where the project is scoped, design development is undertaken, cost plans developed and planning approvals sought, and a final delivery stage, where design is finalised based on the outcomes of the planning stage, and the project is delivered.[349] The managing contractor will typically sub-contract these various roles to other parties, in line with a traditional procurement approach.[350] The important difference, however, is that under this model the process is undertaken on a fully 'open book' basis, enabling close consultation with the project proponent, who has the final decision regarding which subcontractors are used.[351]

CEIID details that the managing contractor typically:

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343 ibid., p.7.

344 Auditor General for Western Australia, *The Planning and Management of Perth Arena,* Report 1, 10 March 2010, p.16.

345 Tsirogiannis, Nicholas and Misko, Marko, 'Relationship Contracting: The Managing Contractor Model', *Project Insights (Clayton Utz Newsletter)*, 16 September 2009. Available at: http://www.claytonutz. com/publications/ Accessed on 16 September 2010.

346 Department of Treasury and Finance, 'Strategic Projects: Construction', nd. Available at: http://www.dtf. wa.gov.au/cms/content.aspx?id=3717. Accessed on 14 September 2010.

347 Hon. Brendan Grylls MLA, Minister for Regional Development, Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 24 June 2010, p.4677.

348 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.12.

349 Tsirogiannis, Nicholas and Misko, Marko, 'Relationship Contracting: The Managing Contractor Model', *Project Insights (Clayton Utz Newsletter)*, 16 September 2009. Available at: http://www.claytonutz.com/publications/newsletters/. Accessed on 16 September 2010.

350 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.11.

351 Tsirogiannis, Nicholas and Misko, Marko, 'Relationship Contracting: The Managing Contractor Model', *Project Insights (Clayton Utz Newsletter)*, 16 September 2009. Available at: http://www.claytonutz.com/publications/newsletters/ Accessed on 16 September 2010.

- *is paid a management fee and may receive incentive payments for achieving target price, schedule and other key parameters;*
- *undertakes some or all of the design activities;*
- *may perform some of the construction works but does not necessarily do so;*
- *is responsible for preliminaries (e.g. crane hire, site sheds, supervision services etc), general project requirements (e.g. security, insurances etc) and project management (e.g. scheduling, coordinating, liaising, monitoring, reporting etc);*
- *prepares the trade packages and conducts the tenders, selects suppliers in close collaboration with the client;*
- *warrants the quality of the whole of the works; and*
- *warrants the completion of the works by the date for Practical Completion.*[352]

Remuneration of the managing contractor is managed on a combination of reimbursable and lump sum components. The reimbursable component consists of the actual costs incurred for materials, subcontractors and consultancy arrangements,[353] while the lump sum component covers the services and work performed by the managing contractor.[354] The fee structure typically allows for incentive payments to be made if the project meets agreed completion or cost targets.[355]

During the first stage the managing contractor compiles a firm estimate of the cost of delivering the project and submits a guaranteed construction sum (GCS). If the proponent accepts the GCS the managing contractor warrants that it will not be exceeded (unless the proponent initiates design variations).[356] There is scope for the managing contractor to achieve target completion dates by commencing early construction works prior to design completion.[357]

The FSH project exhibits many of the features detailed above. In August 2010, the stage 2 contract was signed for $1.63 billion and the Minister for Health noted that the contract 'establishes a maximum amount for cost of construction'.[358] This suggests that a GCS has been negotiated as part of the second stage of the managing contractor agreement. Furthermore, construction of the

352 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, 2009, p.35.

353 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.11.

354 Tsirogiannis, Nicholas and Misko, Marko, 'Relationship Contracting: The Managing Contractor Model', *Project Insights (Clayton Utz Newsletter)*, 16 September 2009. Available at: http://www.claytonutz.com/publications/newsletters/ Accessed on 16 September 2010.

355 ibid.

356 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.11.

357 ibid.

358 Hon. Dr Kim Hames MLA, (Minister for Health), *Fiona Stanley Hospital Stage Two Contract Awarded*, Media Release, 11 August 2010.

hospital has been underway since December 2009,[359] indicating that the managing contractor was taking advantage of the opportunity to complete early construction works.

(d) Early Contractor Involvement

'Early Contractor Involvement' is a relationship between a contractor and an owner that engages the contractor from the early design stage and allows the contractor to contribute its construction knowledge and experience to design.[360] An advantage of this type of contracting model is the improved collaboration between contractor and designer during the construction phase. Additionally, having been engaged up front, the contractor can make inputs on a continuous basis during early design stage, thus providing the best opportunity to influence project cost.[361]

The Queensland Government's Department of Main Roads describes early contractor involvement as a negotiated design and construct contract.[362] Contractor and designer can be selected as soon as a business case has been approved. Contractors are then selected through a 'non price selection process, similar to, but shorter than, a project alliance with a big emphasis on the proposed team'.[363] Queensland operates these contracts in two stages[364]—similar to the process outlined in the Managing Contractor model described immediately above.

The Albany Health Campus is currently going ahead under the early contractor involvement model and the Great Northern Highway upgrade was also constructed using this model.[365]

(e) Alliances

(i) Background

'Alliance' contracts are founded on the principle that there is mutual benefit for both the contractor and the client to deliver a project at the lowest possible cost.[366] An alliance requires participants to commit to common objectives, make decisions collectively, adopt an open information sharing posture and conduct business operations in a non-adversarial fashion.[367]

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359 Hon. Dr Kim Hames MLA, (Minister for Health), *Fiona Stanley Hospital Takes Shape with New Prototype Rooms*, Media Release, 10 December 2009.

360 Song, L, Mohamed, Y, and AbouRizk, SM, 'Early Contractor Involvement in Design and Its Implication on Construction Schedule Performance', *Journal of Management in Engineering*, vol.25, no.1, p.13.

361 ibid.

362 Queensland Government Department of Main Roads, *Early Contractor Involvement Fact Sheet*. Available at: http://www.iaq.com.au/images/PDF/ECI%20Fact%20Sheet.pdf. Accessed on 16 September 2010.

363 ibid.

364 ibid.

365 Main Roads Western Australia, 'Briefing on the State Asset Investment Plan 2010–2014, 21 July 2010. Available at: http://www.ceiid.wa.gov.au/. Accessed on 18 September 2010.

366 Queensland Government Chief Procurement Office, *Relational Procurement Options – Alliance and Early Contractor Involvement*, July 2008, p.7.

367 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.13.

There are numerous types of alliance contracts—from 'pure' at one extreme through to 'competitive' at the other, with hybrid arrangements falling somewhere in between. Pure alliances adopt unanimous decision-making processes for alliance members and do not provide for a deadlock-breaking mechanism. In pure alliances, the non-owner participants (NOPs) are selected on the basis of non-price criteria[368] and there is no process for the distribution of liability between alliance participants.[369] NOPs usually include designers, consultants, management service providers, suppliers and construction contractors.[370] Early identification of a target outturn cost (TOC) is usually required in an alliance process and it is expected that the actual cost of the project will come in below the target cost. NOPs are usually paid their base costs plus agreed corporate overhead and profit margins, although this is dependent on target costs and performance being met. If targets are not met, margins are reduced according to agreed formulae. Other incentives may include the payment of agreed shares of savings.[371]

Competitive alliances share the features of pure alliances outlined above; however, NOPs in a competitive alliance are selected on the basis of both non-price criteria and outturn price (i.e. TOC) criteria.[372] In this method, the alliance owner funds the design activities of short-listed tenderers to develop concept designs for the project. This enables tenderers to submit TOCs and target schedules which the alliance owner can assess for value for money.[373]

There is no clear definition of what constitutes a hybrid alliance, although they can deviate from pure alliances by:

- adopting deadlock breaking mechanisms;
- adjusting 'painshare' arrangements by fixing liabilities;
- allocating (rather than sharing) specific project risks;
- allocating responsibility for project delivery to an alliance contractor; and
- excluding negligence from the alliance no-disputes clause or the cost of rework due to errors by non-owner participants.[374]

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368 Victorian Government Department of Treasury and Finance, *In Pursuit of Additional Value: A Benchmarking Study into Alliancing in the Australian Public Sector*, prepared by Evans & Peck and the University of Melbourne, October 2009, p.11.

369 Queensland Government Chief Procurement Office, *Relational Procurement Options – Alliance and Early Contractor Involvement*, July 2008, pp.9–10.

370 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.13.

371 ibid.

372 Victorian Government Department of Treasury and Finance, *In Pursuit of Additional Value: A Benchmarking Study into Alliancing in the Australian Public Sector*, prepared by Evans & Peck and the University of Melbourne, October 2009, p.11.

373 Queensland Government Chief Procurement Office, *Relational Procurement Options – Alliance and Early Contractor Involvement*, July 2008, p.9.

374 ibid., p.10.

It has been noted that the various procurement guidelines used by state governments favour a non-price selection methodology for NOPs, but that the reasons given are inconsistent and anecdotal.[375]

There is general agreement that alliance contracts tend to be beneficial for complex projects that proceed for longer periods (greater than 12 months).[376] Other common project characteristics for which an alliance delivery method is recommended include where there are a large number of complex or unpredictable risks; complicated stakeholder issues; very tight time constraints; or outcomes that cannot be clearly defined.[377]

(ii) University of Melbourne Study

In October 2009 a report prepared by a number of state Treasury Departments titled, *In Pursuit of Additional Value: A Benchmarking Study into Alliancing in the Australian Public Sector,* reviewed the extent to which value for money is achieved in an alliance contracting process. The report was based on a five-year study of 14 projects covering a variety of major infrastructure types. A key finding of the report was that the actual outturn cost of the examined projects exceeded the business case estimate in the order of 45–55 per cent.[378] This compared unfavourably with the results of an examination of the actual outturn costs for projects delivered through the use of PPPs, which saw an increase of between five and ten per cent.[379] As Diagram 6.2 below demonstrates, the cost increase for projects procured using traditional means was closer to 20 per cent.[380] Notably, it was found that for projects with NOPs selected under a price competitive system, the TOC was between five and ten per cent less compared to non-price competition on the basis that project elements like design costs and on-site development costs were lower when using price competition.[381]

What Diagram 6.2 does not show is that the level of rigor for costings at the business case stage is significantly greater for PPPs than for alliance models. As described above, alliance models tend to be used where time is a critical risk and other risks cannot be fully scoped. Therefore, it is reasonable to expect that the cost escalations associated with an alliance would be greater than other models as an alliance, by definition, is generally used for projects where there are complex or unpredictable risks, tight time frames and outcomes that cannot be clearly defined prior to construction commencement.

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375 Victorian Government Department of Treasury and Finance, *In Pursuit of Additional Value: A Benchmarking Study into Alliancing in the Australian Public Sector*, prepared by Evans & Peck and the University of Melbourne, October 2009, p.14.

376 NSW Procurement, *Procurement Practice Guide: Contracts used for Construction Projects*, July 2008, p.14.

377 Victorian Government Department of Treasury and Finance, *In Pursuit of Additional Value: A Benchmarking Study into Alliancing in the Australian Public Sector*, prepared by Evans & Peck and the University of Melbourne, October 2009, p.11.

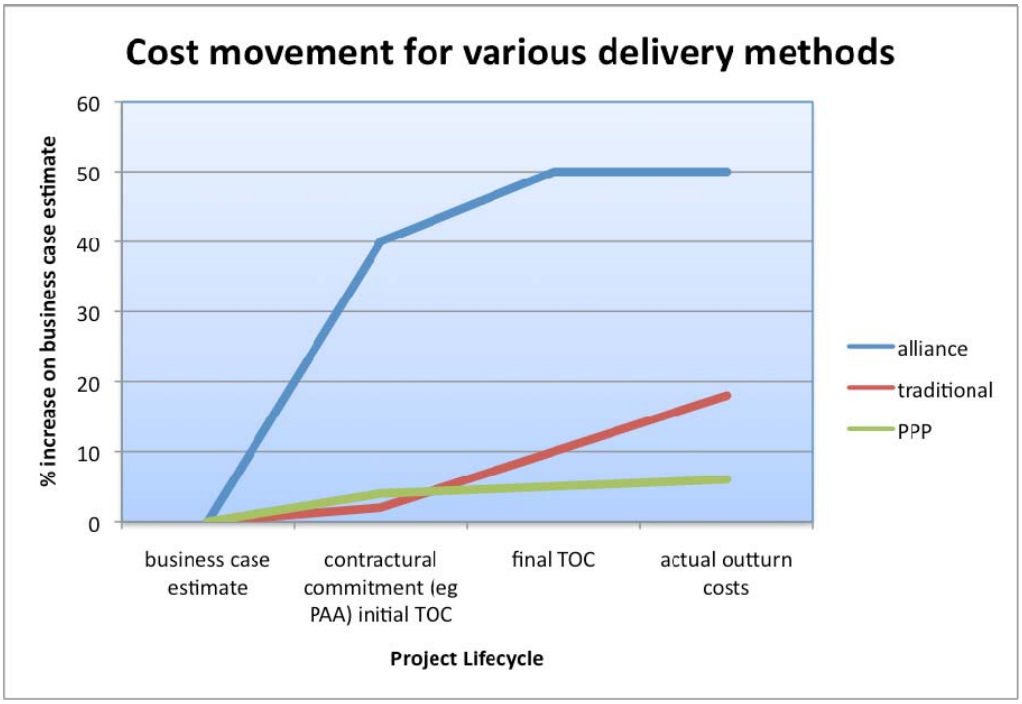
378 ibid., p.35.

379 ibid., p.47.

380 ibid.

381 ibid., p.37.

Diagram 6.2: Cost Movement for Various Delivery Methods[382]



As noted earlier in this section, most state governments recommend a non-price selection methodology for NOPs. The University of Melbourne study found that many of the arguments in support of this approach were unfounded. Instead, the study highlighted the important role played by price in achieving value for money:

> *Price is the value placed on what is exchanged. This value includes tangible and intangible factors. Price represents that value and allows buyers to make a choice amongst potential purchases and provides a mechanism for competition amongst sellers in an open market economy.*
>
> *In the case of alliancing, introducing price-competition as a selection criterion allows the buyer (or Owner) to assess the seller's cost basis compared to its competitors. The buyer will also consider non-price elements to make an informed decision to optimise the VfM outcome. It is difficult for a buyer to make a value for money assessment without considering price as a key element as they need to understand the various trade-offs between price and non-price. Introducing price as a selection criterion provides a positive tension that causes sellers to innovate and provide the best cost solution to address the overall project objective.* [383]

One of the primary motivators for government agencies using alliance contracts was the ability to achieve early project commencement and the ability to progress the development in parallel with

382 ibid., p.47.

383 ibid., p.56.

project approvals.[384] The study recommended that alliance contracts be further developed as a strategy for the delivery of projects that are 'complex with significant risks that cannot be dimensioned in the business case or soon thereafter'.[385] The study also recommended that competitive alliances be adopted as the default contract type in government policy guidelines.[386]

(iii) Use in Western Australia

Main Roads Western Australia (MRWA) provided detailed information regarding its use of a hybrid alliance contract when completing the construction of the New Perth to Bunbury Highway (NPBH), one of the major projects examined by the Committee. In August 2005, MRWA invited Requests for Proposal and evaluated three consortia 'using a rigorous evaluation process designed to identify the Proponent most capable and best able to work with Main Roads in an Alliance'.[387] MRWA then elected to review two short-listed bidders in a price competitive process. The two consortia were provided with four months to complete a Project Target Cost.[388]

MRWA explained that an alliance contract was chosen for the following reasons:

> *The decision to use an alliance contract was primarily due to the number of project risks that required joint management, the potential for significant community/stakeholder issues; tight completion dates and budget; and the strategic importance of the project to Main Roads and Government.*
>
> *The decision was also founded on the belief that an alliance will focus on solutions, foster innovative thinking and be driven by the values that incorporate the views of stakeholders and the community. It would also provide access to resources (during a period of skill shortage) and create opportunities for staff learning and development.*[389]

MRWA's methodologies are noteworthy given the recommendations of the University of Melbourne study outlined above. The first issue of note is the reasons given for the selection of an alliance contract—the road project was complex, of an unprecedented size, and required prompt commencement due to the funding deadlines imposed by the Commonwealth Government. MRWA's representatives acknowledged that the choice of an alliance contract had been dictated by the imposition of the funding and timing conditions by the Commonwealth:

> *It did dictate the form of contract that went out. Obviously, as has been outlined, we went out with a form of alliancing, and that was after a risk workshop was undertaken towards early 2005. We obviously had to come up with a form of procurement that gave us the flexibility to deal with that. Clearly, at this stage we still did not have all our environmental approvals, so I believe a fairly rough—almost a fairly simplistic concept was done for the Peel deviation, and obviously we still needed to do some more design to*

384 ibid., p.35.

385 ibid., p.91.

386 ibid., p.92.

387 Submission No. 2 from Main Roads Western Australia, 15 January 2010, p.15.

388 ibid.

389 ibid., p.14.

> *get quantities and understand properly how many culverts and drainage designs there were. So the broad-brush stuff had to be done.*[390]

The second factor of note is the choice to conduct a price competitive process in order to select the NOPs involved in the project. If the findings and recommendations of the University of Melbourne study are viewed as something of a benchmark for alliance contracting, then it can be said that, in terms of the NPBH at least, MRWA has been conforming to best practice.

Diagram 6.3 Cost Estimates for the New Perth to Bunbury Highway[391]

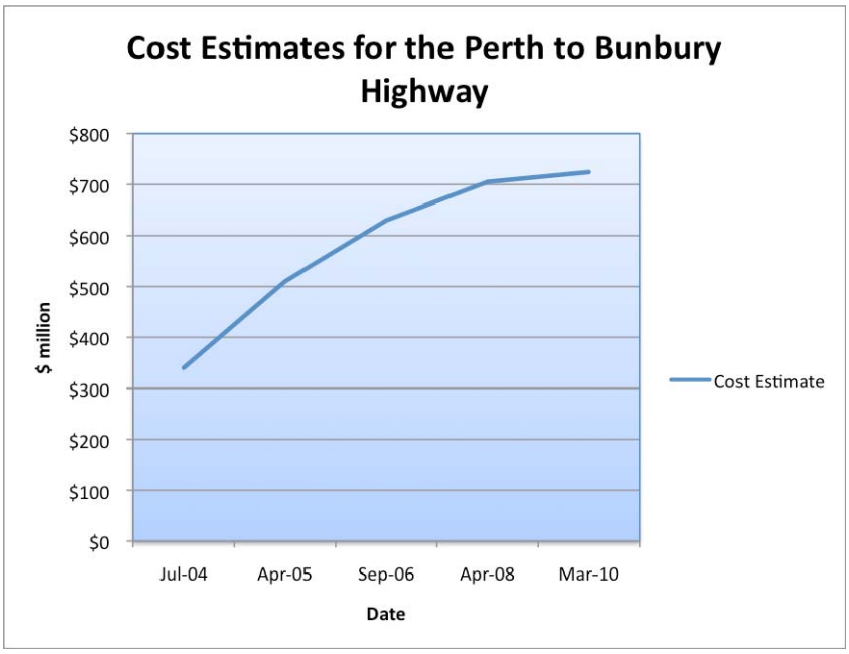


Diagram 6.3 represents the various movements in cost estimates for the NPBH project and has been adapted from evidence provided by MRWA. The initial estimate for the cost of the project in July 2004 was $340 million.[392] After a series of escalations through the life of the project, the figure at March 2010 was $724 million; and MRWA admitted that this could increase further, depending upon the outcome of legal action arising from the acquisition of land.[393]

The cost escalations require explanation, particularly given the findings of the University of Melbourne study. Most importantly, the initial figure of $340 million was calculated in 2004 using 'dollars of the day': the cost of completely constructing the Highway in 2004. This is obviously a misleading metric because it does not allow for price escalation. MRWA's policies have since changed and all project cost estimates are now completed in outturn dollars.[394] MRWA

390 Mr Leo Coci, Director Major Projects, Main Roads Western Australia, *Transcript of Evidence*, 2 March 2010, p.4.

391 Adapted from evidence provided by MRWA in submission and at hearing.

392 Submission No. 2 from Main Roads Western Australia, 15 January 2010, p.17.

393 Mr Peter Woronzow, Executive Director, Finance and Commercial Services, Main Roads Western Australia, *Transcript of Evidence*, 2 March 2010, p.8.

394 Mr Phil Ladner, Executive Director, Infrastructure Delivery, Main Roads Western Australia, *Transcript of Evidence*, 2 March 2010, p.5.

admits, however, that escalation alone cannot account for the significant increases in the cost of the project.[395] Mr Phil Ladner, Executive Director of Infrastructure Delivery, made the following point about the cost increases associated with the construction of the NPBH:

> *There was a scoping issue. There are lots of reasons. There was probably also the general fact that the start of construction was driven by a commonwealth condition, and it was out of sync with where we were at; where we had the detail. That drove an alliance process, given that an alliance procurement process could be started sooner than if we had gone for a design and construct. That was a procurement debate.*[396]

Working backwards through Mr Ladner's statement it is reasonable to conclude that it was not the alliance contract that resulted in the cost escalations associated with the project. Rather, the issues that drove the cost escalations—the requirement to commence construction early due to funding conditions imposed by the Commonwealth, and the resultant lack of detailed plans or environmental clearances prior to construction commencement—also made an alliance contract one of the few reasonable choices for delivering the project economically.

Furthermore, the use of the alliance contract, given the funding conditions outlined above, was one of the reasonable mechanisms for allowing sufficient community involvement with the project once it was underway. Under a traditional construct only model, variations to road alignment once construction has commenced can lead to significant cost escalations and construction delays. The alliance contract afforded the opportunity for variations to be made in a cooperative environment with both the construction contractors and local communities. Indeed, it is collaboration with this latter group that MRWA highlighted as one particular advantage, given the conditions imposed requiring construction to commence prior to the completion of detailed planning and community consultation:

> *We had an issue with the Tatham Road Landowners Association; the alignment was pretty close to some homes and there were some pretty substantial retaining walls. Together we were able to work to minimise the impact on the community by changing the geometry. That had repercussions on the quantities, but we ended up with a win–win scenario for us and the community. In fact, we were able to win the community over to the point where we were able to work with the community to address some technical issues to do with preloading the approaches to a bridge, where the community was prepared to allow us temporary access to their land while we did some work to make good and enhance the area, which saved the project money.*[397]

The other project examined by the Committee that will be procured through an alliance contracting method is the underground railway works, station modifications and railway systems of the Perth City Link project.[398] Similar to the NPBH, this project will be completed using a competitive alliance.

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395 ibid., p.10.

396 ibid., p.10.

397 Mr Leo Coci, Director Major Projects, Main Roads Western Australia, *Transcript of Evidence*, 2 March 2010, p.12.

398 Public Transport Authority of Western Australia, 'Briefing on the State Asset Investment Plan 2010–2014, 21 July 2010. Available at: http://www.ceiid.wa.gov.au/. Accessed on 18 September 2010.

There are a number of complicating factors in this project, including the need to minimise the impact on the existing train services and the high level of engineering risk associated with keeping the railway tunnel within clearance tolerances. Given the high levels of risk involved, an alliance contract presents a means for government to work collaboratively with alliance partners in a 'no fault, no blame' environment.

Finding 20

Alliance contracts can provide an appropriate delivery model for infrastructure in some circumstances, including where there are:

- a large number of unpredictable risks with complex interfaces; or
- very tight time constraints; or
- there is a need for owner involvement during delivery.

CHAPTER 7 FEDERAL INFRASTRUCTURE FUNDING

At various stages throughout the process of developing infrastructure proposals, agencies must consider how their projects might be funded. The federal government provides a number of avenues for states and Territories to obtain funding for infrastructure projects.

The Department of the Premier and Cabinet (DPC) outlined the range of Commonwealth funding programs as follows:

- *National partnership agreements–where all States receive an allocation based on a variety of criteria;*
- *Commonwealth budget announcements–where one-off major project funding may be made available;*
- *Funding programs–three to four year programs with specified eligibility criteria, such as the Commonwealth National (sic) Building Program (formerly known as Auslink), that may have open competitive funding rounds or be negotiated bi-laterally between Commonwealth and State agencies;*
- *Other mechanisms–such as the Building Australia Fund, which uses a third party, Infrastructure Australia, to assess State submissions and make recommendations to the Commonwealth Government*.[399]

The federal government recognises the potential for confusion with this array of options, and is currently working to resolve some of the different arrangements and rules that govern them.[400]

While there are various avenues available to obtain federal funding, this report focuses on programs that have been variously called AusLink (1 and 2), the Nation Building Program and the Building Australia Fund.

7.1 From AusLink to Nation Building

(a) AusLink

Established in 2004 and administered under the *AusLink (National Land Transport) Act 2005* (Cwth) (the AusLink Act), the AusLink funding program was designed to achieve better national land transport planning, funding and investment decision making, based on improved long-term planning, encouragement of the best ideas and solutions, and targeting investments to achieve the best outcomes.[401]

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399 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.48.

400 Mr Michael Deegan, Infrastructure Coordinator, Infrastructure Coordinator, *Committee Briefing*, 18 August 2010.

401 Department of Transport and Regional Services, *AusLink White Paper*, Commonwealth of Australia, Canberra, 2004, p.15. See also: Department of Infrastructure, Transport, Regional Development and Local Government, *2007–08 AusLink Annual Report*, Commonwealth of Australia, Canberra, 2009, p.2.

Funding arrangements were governed by, and implemented through, a bilateral agreement with the Commonwealth Government, with the Western Australian agreement signed in December 2005.[402]

The agreement provided up to $472 million over the five years from 2004–05 to 2008–09 for construction projects, and approximately $160 million for road maintenance on the National Network.[403]

Initially, AusLink provided for funding through to the 2008–09 financial year, with AusLink 2 developed to provide $22.3 billion for 2009–10 to 2013–14.[404] Amendments to the AusLink Act in 2008 allowed for $70 million of funding of heavy vehicle facilities such as off-road rest stops and decoupling areas through a new Heavy Vehicle Safety and Productivity Package.[405]

AusLink was replaced in 2009 by the Nation Building Program (NBP) and in February of that year a Memorandum of Understanding (MOU) was signed to cover project funding for the period 2008–09 to 2013–14.[406]

The AusLink Act was superseded by the *Nation Building Program (National Land Transport) Act 2009* (Cwth), which primarily reflects the programme name change. Related Commonwealth legislation includes the *Infrastructure Australia Act 2008*, the *Nation Building and Jobs Plan (State Infrastructure Delivery) Act 2009* and the *Nation-building Funds Act 2008*.[407]

(b) Nation Building

In its 2008–09 Budget the federal government announced the creation of a Building Australia Fund (BAF), established through the *Nation-building Funds Act 2008* (Cwth) (the NBF Act).

The NBF Act established the BAF, the Education Investment Fund and the Health and Hospitals Fund. This report is concerned with the BAF component, the main purpose of which is to provide funding in relation to the:

- creation or development of transport, communications, energy and water infrastructure; and

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402 Submission No. 22 from Main Roads Western Australia, 11 June 2010, p.1. See: *Implementation of the AusLink National Land Transport Plan Bilateral Agreement between the Commonwealth of Australia and the State of Western Australia 2004–2009*. Available at: http://www.infrastructure.gov.au/transport/publications/files/ WA_Bilateral.pdf. Accessed on 11 September 2010.

403 Clauses 12 and 13, *Implementation of the AusLink National Land Transport Plan Bilateral Agreement between the Commonwealth of Australia and the State of Western Australia 2004–2009.* Available at: http://www.infrastructure.gov.au/transport/publications/files/WA_Bilateral.pdf. Accessed on 11 September 2010.

404 *Ministerial Statements, Budget 2007–08. Transport: 2007–08 Budget Initiatives. AusLink 2,* Commonwealth of Australia, 2007. Available at: http://www.budget.gov.au/2007-08/ministerial/ html/dotars-31.htm. Accessed on 11 September 2010.

405 Bills Digest no. 13 2008–09 AusLink (National Land Transport) Amendment Bill 2008. Available at: http://www.aph.gov.au/library/pubs/bd/2008-09/09bd013.htm. Accessed on 12 September 2010.

406 Submission No. 22 from Main Roads Western Australia, 11 June 2010, p.1.

407 Department of Infrastructure, Transport, Regional Development and Local Government, *2007–08 AusLink Annual Report*, Commonwealth of Australia, Canberra, 2009, p.2.

- national broadband network matters.[408]

Investment decisions are made by the Future Fund Board, which is established under the NBF Act, and delivered by the Department of Infrastructure, Transport, Regional Development and Local Government (DITRDLG).

The related *Nation Building Program (National Land Transport) Act 2009* (Cwth) (the NBPNLT Act) provides for the funding of projects related to land transport matters, which means that NBP investment carries forward a number of AusLink programme streams and is directed to a range of road and rail projects across the national Land Transport Network.[409]

This NBPNLT Act allows for the approval of projects under various specific programmes, as shown in Table 7.1.

Table 7.1: National Land Transport Nation Building Programs[410]

National Projects: (as defined in Part 3, NBPNLT)	These target high priority projects which will deliver national benefits.
Roads to Recovery Program (Local Roads): (as defined in Part 8, NBPNLT)	A programme to address the problem of local roads reaching the end of their economic life, and their replacement being beyond the capacity of local government.
Black Spots Projects: (as defined in Part 7, NBPNLT)	A programme which aims to improve the physical condition or management of hazardous locations with a history of crashes involving death or serious injury.
Funding for Off-Network Projects: (as defined in Part 6 NBPNLT)	Projects that provide roads, railways and inter-modal facilities that are not part of the National Network.
Transport Development and Innovation Projects: (as defined in Part 4 NBPNLT)	Provides innovation and research funding for land transport research, intelligent transport initiatives and corridor studies.
Heavy Vehicle Safety and Productivity Program:	A $70 million programme to deliver improved safety and productivity outcomes for the heavy vehicle industry.

Main Roads Western Australia (MRWA), a major recipient of AusLink and NBP funding, provided details of its current and future road projects funded in part or in full by grants from the Commonwealth Government. This information (attached at Appendix 5) shows almost $2 billion was allocated to MRWA, with $246 million from AusLink and around $1.3 billion from the NBP.[411] Additional funds of $20 million were provided through the Infrastructure Employment Projects Program and $363 million through the Accelerated Upgrade Package.[412]

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408 Section 11 *Nation-building Funds Act 2008* (Cwth).

409 Department of Infrastructure, Transport, Regional Development and Local Government, 'Nation Building Program', nd. Available at: http://www.nationbuildingprogram.gov.au/index.aspx.

410 Department of Infrastructure, Transport, Regional Development and Local Government, 'Funding Progra', nd. Available at: http://www.nationbuildingprogram.gov.au/funding/. Accessed on 11 September 2010; and *Nation Building Program (National land Transport) Act 2009* (Cwth).

411 Submission No. 22 from Main Roads Western Australia, 11 June 2010, pp.3–4.

412 ibid.

MRWA received Commonwealth funding for the New Perth to Bunbury Highway (NPBH), with $160 million coming from AusLink and $170 million from Nation Building funds.

(c) Nation Building and the Economic Stimulus Plan

In response to the recent global financial crisis the Commonwealth Government invested $42 billion in its Nation Building–Economic Stimulus Plan (the Plan). This two-year Plan was intended to 'support jobs and invest in the long term growth of the Australian economy'[413] through the 'rapid delivery of construction projects in social housing, schools and transport' across Australia.[414] While not the focus of this report, the Plan and its contribution to infrastructure funding needs to be acknowledged, particularly as it appears to be operating under the Nation Building badge.

The infrastructure elements of the Plan include:

- building primary schools, and Science and Language Centres for secondary schools;
- the construction of new social housing, and the repair and maintenance of existing dwellings;
- the construction of 802 defence houses;
- local government, community and transport infrastructure, including major road and rail projects and the East Kimberley Development Package; and
- increasing 'the energy efficiency of Australian homes'.[415]

It is through the East Kimberley Development Package that $195 million of federal funding is being provided for social infrastructure to support Western Australia's Ord–East Kimberley Expansion Project.[416]

413 Department of the Prime Minister and Cabinet, *Nation Building Economic Stimulus Plan. Commonwealth Coordinator-General's Progress Report 3 February 2009–30 June 2009*, Department of the Prime Minister and Cabinet, Canberra, August 2009, p.7.

414 Department of the Prime Minister and Cabinet, *Nation Building Economic Stimulus Plan. Commonwealth Coordinator-General's Progress Report 3 February 2009–30 June 2009*, Department of the Prime Minister and Cabinet, Canberra, August 2009, p.7; and Department of the Premier and Cabinet, 'Nation Building—Economic Stimulus Plan, nd, p.2. Available at: http://www/dpc.wa.gov.au/Pages/WANBJPImplementation.aspx. Accessed on 15 December 2009.

415 Department of the Prime Minister and Cabinet, *Nation Building Economic Stimulus Plan. Commonwealth Coordinator-General's Progress Report 3 February 2009–30 June 2009*, Department of the Prime Minister and Cabinet, Canberra, August 2009, pp.32–50.

416 Department of Regional Development and Lands, *Ord–East Kimberley Development Plan*, Government of Western Australia, Perth, nd, p.30.

7.2 Infrastructure Australia

(a) Establishment and Purpose of Infrastructure Australia

Infrastructure Australia (IA) was established under the *Infrastructure Australia Act 2008* (Cwth) (the IA Act) to provide all spheres of government as well as investors in, and owners of, infrastructure with specific guidance for funding applications, and to provide advice in relation to:

> *(a) Australia's current and future needs and priorities relating to nationally significant infrastructure;*
>
> *(b) policy, pricing and regulatory issues that may impact on the utilisation of infrastructure;*
>
> *(c) impediments to the efficient utilisation of national infrastructure networks;*
>
> *(d) options and reforms, including regulatory reforms, to make the utilisation of national infrastructure networks more efficient;*
>
> *(e) the needs of users of infrastructure;*
>
> *(f) mechanisms for financing investment in infrastructure*.[417]

IA is an advisory body consisting of a Chair and 11 other members, all appointed by the Minister to constitute the Infrastructure Australia Council (IAC). IA's aim to 'drive the development of a long term, coordinated national approach to infrastructure planning and investment'[418] is guided by the set of objectives, strategic priorities and principles detailed in Table 7.2.

In performing its functions, IA is assisted by an Infrastructure Coordinator, who, rather than administering project funding, guides allocations from the BAF through recommendations to the Council of Australian Governments (COAG).[419]

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417 Section 5(1) *Infrastructure Australia Act 2008* (Cwth). Nationally significant infrastructure is defined under s 3 as including transport, energy, communications and water infrastructure 'in which investment or further investment will materially improve national productivity'.

418 Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and Environmentally Sustainable Future*, Commonwealth of Australia, Canberra, May 2009, p.3.

419 Section 5(1) *Infrastructure Australia Act 2008* (Cwth).

Table 7.2: Objectives, Strategic Priorities and Principles for Infrastructure Australia[420]

Objectives	▪ Increased economic standard of living for Australians. ▪ Environmental sustainability and reduced greenhouse gas emissions. ▪ Better social outcomes, quality of life and reduced social disadvantage in our cities and our regions.
Strategic Priorities	▪ Expand Australia's productive capacity. ▪ Increase Australia's productivity. ▪ Diversify Australia's economic capabilities. ▪ Build on Australia's global competitive advantages. ▪ Develop our cities and/or regions. ▪ Reduce greenhouse emissions. ▪ Improve social equity and quality of life in our cities and our regions.
Principles in Analysis and Decision-Making	▪ National perspective to complement State and Territory ambitions. ▪ Triple bottom line approach (economic, environmental and social). ▪ Efficient use of existing infrastructure and resources. ▪ Maximise the productivity of people and assets. ▪ Examine supply and demand side patterns, options and solutions. ▪ A long-term, whole-of-life approach. ▪ Optimise the role of both the public and private sector.

(b) National Infrastructure Audit

Following its establishment, IA undertook a national infrastructure audit—as required under s 5(2) of the IA Act)—to determine the greatest infrastructure challenges nation-wide and allow for the development of an initial Priority List of infrastructure needs. The first national audit of Australia's transport, water, energy and communications infrastructure was conducted in April 2008.[421]

In undertaking this and future audits, IA takes what it describes as a 'long term, top-down approach to infrastructure planning'.[422] According to IA, it:

> *is not seeking a list of projects looking for alternative sources of funding, but instead coherent proposals for a long-term package of reforms and investments, which are the*

420 Meeting Papers for Meeting Four of Infrastructure Australia Council, 1 October 2008, as cited in Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.52. See also: Infrastructure Australia, *A Report to the Council of Australian Governments*, Commonwealth of Australia, December 2008, pp.8–9.

421 Infrastructure Australia, *Outline of* Infrastructure Australia's *Prioritisation Methodology*, Commonwealth of Australia, 24 September 2008; and Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010. This process is explained in detail in these publications, particularly the Australian National Audit Office's performance audit of IA.

422 Infrastructure Australia, *Better Infrastructure Decision-Making: Guidelines for Making Submissions to Infrastructure Australia's Infrastructure Planning Process, through Infrastructure Australia's Reform and Investment Framework*, Commonwealth of Australia, Canberra, October 2009, p.5.

> *direct result of thorough and evidence-based infrastructure planning processes, and which are clearly presented in that context.*[423]

IA called for submissions from state and Territory governments in which core strategic priorities and issues were to be identified, including:

- 'a summary of key infrastructure issues', including any current and/or emerging gaps and bottlenecks;
- general details of the 'approach to developing productive capacity';
- 'major infrastructure priorities';
- 'a sectoral analysis on specific infrastructure sectors; and
- a brief analysis of relevant infrastructure capacities and further requirements of their key regions and cities'.[424]

To assess submissions, the following seven-stage framework was developed and made available to jurisdictions:

- Stage 1: Goal Definition
- Stage 2: Problem Identification
- Stage 3: Problem Assessment
- Stage 4: Problem Analysis
- Stage 5: Options Generation
- Stage 6: Options Assessment
- Stage 7: Solution Prioritisation[425]

Full details of this framework, its components and their rationale are contained in IA's May 2009 report, *National Infrastructure Priorities*.[426] The Australian National Audit Office (ANAO) found

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423 ibid.

424 Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.58.

425 Infrastructure Australia, *Better Infrastructure Decision-Making: Guidelines for Making Submissions to Infrastructure Australia's Infrastructure Planning Process, through Infrastructure Australia's Reform and Investment Framework*, Commonwealth of Australia, Canberra, October 2009, p.10.

426 Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and Environmentally Sustainable Future*, Commonwealth of Australia, Canberra, May 2009, p.5.

that 'overall, Infrastructure Australia's methodology provided a robust framework for the development of the first Infrastructure Priority List'.[427]

The application of this framework allowed IA to identify the challenges faced and the themes through which action was required to meet infrastructure gaps, deficiencies and bottlenecks, and, thus, 'to boost Australia's productivity, protect the environment and enhance Australians' quality of life'.[428]

The audit identified a number of challenges for which it developed seven themes for action:

1. ***transforming our cities*** *– increasing public transport capacity in our cities and making better use of existing transport infrastructure, including the road networks;*

2. ***adaptable and secure water supplies*** *– more adaptable and resilient water systems to cope with climate change;*

3. ***the creation of a true national energy market*** *– more extensive national energy grids to enable greater flexibility and competition in the nation's electricity and gas systems, whilst creating opportunities for the development of renewable energy sources;*

4. ***competitive international gateways*** *– developing more effective ports and associated land transport systems to more efficiently cope with imports and exports;*

5. ***a national freight network*** *– development of our rail and road networks so that more freight can be moved efficiently by rail and by road;*

6. ***a national broadband network*** *– developing a more extensive, globally competitive broadband system; and*

7. ***providing essential Indigenous infrastructure*** *– improved services for Indigenous communities.*[429]

Clearly, the greater number of themes addressed by agencies in their funding applications, the more likely they are to receive federal funding.[430]

(c) Infrastructure Priority List

Following the audit and identification of challenges and themes for action, IA developed its first priority list. IA believed the Priority List projects provide 'solutions that are well developed, can

427 Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.19, p.20 and p.73.

428 Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and Environmentally Sustainable Future*, Commonwealth of Australia, Canberra, May 2009, p.6.

429 ibid., p.7.

430 Mr Michael Deegan, Infrastructure Coordinator, Infrastructure Coordinator, *Committee Briefing*, 18 August 2010.

immediately respond to Australia's challenges and contribute[s] to national productivity'.[431] The first Priority List was required by COAG by December 2008, and was expected to be reviewed 'on an annual business cycle'.[432] Ultimately, IA developed an interim priority list in December 2009 and a final first priority list in May 2009.

The methodology applied to develop the list prioritises projects that:

- support IA's seven themes for action; and
- are of national significance; and
- meet detailed project assessment criteria as contained in the BAF legislation.[433]

Through applying a prioritisation methodology involving profiling, economic appraisal and selection, IA developed a merit matrix against which to assess the projects. The prioritisation categories were 'very high priority', 'high priority', 'moderate priority' and 'no priority'.

Of the 1000 initiatives contained in submissions, IA identified 94 projects as possibilities for the initial priority list.[434] As the information on these projects had been at the 'minimum level', IA worked with the project proponents to develop a comprehensive evidence base to support the projects.

In December 2008, the Infrastructure Coordinator provided an Interim Priority List that recommended 28 high and medium priority projects, six of which were high or medium priority projects for which adequate information, including a robust benefit-cost ratio (BCR), had been provided. The remaining 22 high and medium priority projects were deemed not sufficiently well developed at that time to allow assessment of deliverability risks.

None of the six robustly developed projects were from Western Australia. However, of the insufficiently developed projects, Oakajee Port and Common Use Facilities was assessed as high priority, and the Perth Airport Transport Links and the Northbridge Rail Cutting projects were classified as medium priority.[435]

In December 2008, the Infrastructure Coordinator was required to obtain additional information on the 94 projects originally short-listed, and develop a final Priority List to be published in May 2009.

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431 Infrastructure Australia, *Outline of* Infrastructure Australia's *Prioritisation Methodology*, Commonwealth of Australia, Canberra, 24 September 2008, p.3.

432 ibid.

433 Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and Environmentally Sustainable Future*, Commonwealth of Australia, Canberra, May 2009, p.7.

434 ibid.

435 Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.101. Various iterations of the same project have different names. These are the names that appear in the Auditor General's report.

Diagram 7.1 shows nine projects identified as meeting IA's stringent criteria and a further 28 projects deemed to have met the first two. These formed a 'pipeline' of projects that were required to undergo further project development and analysis.[436] Of these, only 15 had BCRs that could be assessed. Nevertheless, six projects deemed to have insufficient evidence to support their economic viability received federal funding.

While the issue of BCRs and their relevance to funding will be discussed further below, this clearly reinforces the fact that IA fills an advisory role only and that the Commonwealth Government may decide to fund a project that is not on IA's priority list. It is also important to note that IA is restricted to making recommendations for funding from the BAF, and government may decide to fund a less-fully developed project from another source of funds.[437]

One conclusion to draw here is that the political imperative also operates at the federal level with funding decisions sometimes made on that basis. This means that despite a State's best efforts to produce robust funding submissions, some projects may not receive funding due to particular political imperatives. Likewise, some funding submissions that are less well-developed may receive federal funding.

Following this, IA reviewed the 2008–09 submission and prioritisation process, seeking feedback from participants, and while it had released its audit framework to assist jurisdictions prepare their submissions, the review found that the majority of projects submitted 'failed to articulate how this Framework was applied in order to develop the proponent's priorities'.[438]

In particular, the review found that:

- *There was little evidence that the initiatives were the result of robust, top-down infrastructure planning and decision-making processes: indeed there was often no obvious link between individual projects and their context, i.e. prevalent strategies or plans;*

- *Some initiatives did not support Infrastructure Australia's strategic priorities or make a significant impact on national productivity;*

- *There was little attempt to define or quantify the problem that the initiative would solve, so that the case for action was not clear. As a result, it was often not clear why the initiatives submitted to Infrastructure Australia had been prioritised above other potential candidates;*

- *A broad range of options to solve the problems was not considered – in particular many submissions jumped directly to large-scale, expensive capacity*

436 Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and environmentally Sustainable Future*, May 2009, pp.8–9.

437 Mr Michael Deegan, Infrastructure Coordinator, Infrastructure Coordinator, *Committee Briefing*, 18 August 2010.

438 Infrastructure Australia, *Better Infrastructure Decision-Making: Guidelines for Making Submissions to Infrastructure Australia's Infrastructure Planning Process, through Infrastructure Australia's Reform and Investment Framework*, Commonwealth of Australia, Canberra, October 2009, p.6.

enhancements, without any consideration of 'non-build' solutions such as changes in regulations, governance arrangements or introducing demand management measures to make better use of existing infrastructure; and

- *Many initiatives, including those seeking immediate funding, were presented with limited or no supporting economic analysis, with flawed analysis, or with analysis which showed that projects were likely to be economically unviable*.[439]

As a result of these findings, IA determined there was a need for it to better articulate its evidence requirements and to provide 'more detailed guidance on Infrastructure Australia's own top-down planning process – the reform and investment framework – […] to help proponents to demonstrate that they have used the required methodology'.[440]

In October 2009 IA published its guidelines, *Better Infrastructure Decision-Making*, to assist jurisdictions prepare for the 2009–10 round of submissions. In calling for submissions, IA further advised of its intention to 'build a long term pipeline of reforms and investments', which meant that as well as identifying initiatives looking for immediate support, submissions could also 'identify potential future priorities without specifying a precise solution'.[441] This would allow IA to identify emerging challenges and potential solutions, subject them to further analysis and consider including them in the infrastructure pipeline.

In June 2010 IA revealed four new categories that allowed for a 'greater degree of differentiation between initiatives in the pipeline' and thus provided 'greater transparency as to the potential of the initiatives and their stage of development'.[442] Therefore, the infrastructure priorities for 2010 were based on the following categories:

- Early Stage – proposal addresses nationally significant infrastructure challenge, but solution identification and development is at an early stage
- Real Potential – proposal addresses nationally significant challenge and includes considerable solution analysis, although development work is continuing
- Threshold – proposal has strong strategic and economic merit, and only a small number of issues prevents it from being ready to proceed
- Ready to Proceed – proposal meets all of IA's requirements[443]

439 ibid.

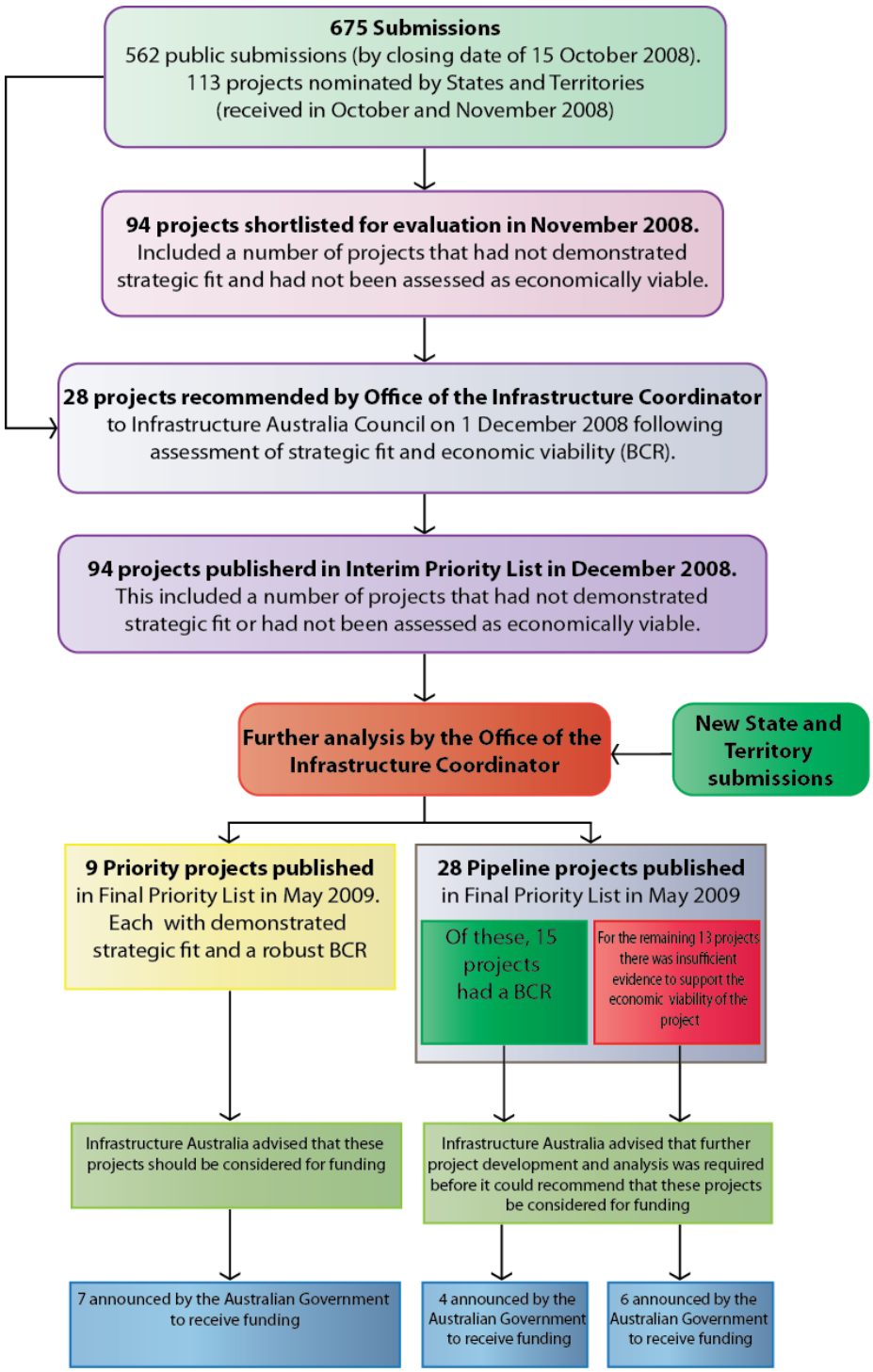
440 ibid., p.3.

441 ibid.

442 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities. An Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010, p.49.

443 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities. An Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010, p.49.

Diagram 7.1: Key Points in the Development of the Infrastructure Priority List[444]



444 Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.18.

As projects are further developed they may move further up the scale. IA works with jurisdictions to ensure that they have clearly identified the problem the proposed project is intended to address, that other options have been considered and that the benefit-cost analysis (BCA) is well developed. Proposals that are less well developed and are in the early stages of planning will require more IA assistance before they have any possibility of proceeding through the pipeline.[445]

The total capital value for the states and Territories (see Table 7.3) includes projects proposed by non-government organisations. For example, the $1,470 million for Western Australia's projects that are classified as having real potential includes $75 million for the Eastern Goldfields Railway—Freight Gateway Upgrade submitted by West Net Rail. Similarly, the $7,000 million North–West Sydney to CBD Rail Link proposal from Australian Infrastructure Solutions is included in the New South Wales early stage capital value figure.

Table 7.3: Capital Value of Infrastructure Australia's Pipeline Projects June 2010[446]

Category	Early Stage	Real Potential	Threshold	Ready to Proceed	Total $ million
WA	7,056	1,470	4,000	–	12,526
VIC	1,500	7,760	–	4,928	14,188
SA	105	1,417	–	418	1,940
NSW	7,200	4,000	2,400	6,000	19,600
QLD	3,663	24,524	3,387	–	31,574
TAS	90	1,150	–	–	1,240
NT	–	–	336	–	336
ACT	–	701	–	220	921
Other	20*	500*	–	–	520
Total ($million)	19,634	41,522	10,123	11,566	82,845

* These projects are research and/or trial projects relating to train control and management systems.

Details of federal government funding of pipeline projects from the 2009–2010 round is yet to be released.

(d) Requirements and Guidelines

At a minimum, IA requires submissions to include the following:

- *'Strategic options' reports*
- *'Feasibility studies' including specialist engineering and environmental assessments and outline economic assessments*
- *Project 'business cases', including demand modeling reports and economic methodology and results reports*

445 Michael Deegan, Infrastructure Coordinator, Infrastructure Coordinator, *Committee Briefing*, 18 August 2010.

446 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities. An Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010, pp.50–51.

- *'Delivery' reports, including specific risk, governance and timing assessments.*[447]

These are detailed in IA's Minimum Information Requirements document, developed following the production of the interim priority list and aimed to assist jurisdictions provide more detailed information for IA assessment.[448]

In addition, IA has produced a number of guidelines[449] to assist proponents prepare submissions that are as well developed as possible, and improve the likelihood of garnering federal funding.[450]

(e) Importance of Cost–Benefit Analyses

IA's three-phase prioritisation methodology clearly places considerable importance on what it refers to as benefit-cost analyses (BCA).[451] This is most evident in the economic appraisal stage where a project's BCR is required to determine its reliability. IA's emphasis on the importance of identifying benefits and costs is shared by Western Australia's DTF, as reflected in SAMF's emphasis on evaluating benefits and cost.

IA's emphasis on BCAs reflects that of the federal government at the time the May 2008 Budget was delivered, which stressed the need for rigorous cost-benefit analyses to be conducted by IA.[452]

(f) Western Australian Proposals to Infrastructure Australia

The Department of State Development (DSD) is the 'lead agency responsible for development and approval of major infrastructure, industry and resource development projects'.[453] DSD also has the lead role in developing the State's submissions to, and liaising with, IA.

IA's December 2008 report to COAG included five proposed initiatives from Western Australia described as requiring further analysis:

- Northbridge Rail Cutting Link
- Perth Airport Transport Links

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447 Infrastructure Australia, Infrastructure Australia Priority List Minimum Information Requirements, nd, p.1. Available at: http://www.infrastructureaustralia.gov.au. Accessed on 14 September 2010.

448 ibid.; and Auditor-General, Australian National Audit Office, Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.112.

449 Infrastructure Australia, 'Publications', nd. Available at: http://www.infrastructureaustralia.gov.au/publications.aspx. Accessed on 14 September 2010.

450 Mr Michael Deegan, Infrastructure Coordinator, Infrastructure Coordinator, *Committee Briefing*, 18 August 2010.

451 The Western Australian Government uses the term cost-benefit analysis, while IA uses benefit-cost analysis. These terms will be used interchangeably in general discussion.

452 Budget Paper No. 1 2008–09, *Budget Strategy and Outlook*, as cited in Auditor-General, Australian National Audit Office, *Conduct by Infrastructure Australia of the First National Infrastructure Audit and Development of the Infrastructure Priority List*, Audit Report No. 2 2010–11, Commonwealth of Australia, Canberra, 2010, p.14.

453 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.49.

- Oakajee Port and Common Use Infrastructure
- Ord River Expansion
- Pilbara Housing and Indigenous Infrastructure[454]

According to the DSD, aspects of the Pilbara Housing and Indigenous Infrastructure project have been included in the 2009 Pilbara Cities project submission to IA. Similarly, the Perth Airport Transport Links project was further developed as Gateway WA for the 2009 round of submissions.[455]

The May 2009 IA report reveals that the following Western Australian projects were assessed as being priority pipeline projects with real potential:

- Oakajee Port Common-user Services
- Perth Airport Multi-modal Links
- Northbridge Rail Link (The Hub)[456]

In November 2009, the state government submitted seven projects to IA for consideration:

- Gateway WA (Main Roads Western Australia)
- Pilbara Cities (Department of State Development)
- Kimberley Supply Base (Department of State Development)
- Mid-West Energy (Western Power)
- Grain Freight Network (Department of Transport)
- Brunswick to Bunbury Port Rail (Department of Transport)
- Port Hedland Inner Harbour (Department of Transport)[457]

In June 2010, IA reported their consideration of the following Western Australian initiatives:[458]

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454 Infrastructure Australia, *A Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, December 2008, p.68, p.70 and p.71.

455 Department of State Development, 'Western Australian Government Proposals. Infrastructure Australia Co-ordination', nd. Available at http://www.dsd.wa.gov.au/7647.aspx. Accessed on 16 September 2010.

456 Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and Environmentally Sustainable Future*, Commonwealth of Australia, May 2009, p.10 and p.11.

457 Department of State Development, 'Western Australian Government Proposals. Infrastructure Australia Co-ordination', nd. Available at http://www.dsd.wa.gov.au/7647.aspx. Accessed on 16 September 2010.

Table 7.4: Western Australian Initiatives Considered in 2009 Infrastructure Australia Round[459]

Project	Capital Cost $ million	Category
Mid-West Energy Stage 2 (330kV Line and Renewable Link)	$795	Real Potential
Gateway WA – Perth Airport and Freight Access	$600	Real Potential
Pilbara Cities	$2,900	Early Stage
Kimberley – Point Torment Supply Base	$550*	nc
Port Hedland Inner Harbour Capacity Enhancements	$3,400	Early Stage
South West Industrial Parks Linkages to the Port of Bunbury	$756	Early Stage
Oakajee Port	$4,000	Threshold
Grain Freight Network	172*	nc
National Managed Motorway projects	na	Real Potential
Brunswick to Bunbury Harbour Rail Bottleneck	$63	nc
Eastern Goldfields Railway Freight Gateway Upgrade Project	$75	Real Potential

* Source: http://www.dsd.wa.gov.au/7647.aspx. nc = not categorised. na = not available

The capital costs in the IA 2010 report to COAG show significant variation from those in the DSD fact sheets for each project, and differ from some of the evidence provided to the Committee. For example, the Pilbara Cities project is shown by IA as having a capital cost of $2,900 million while the DSD fact sheets says that the State has committed $300 million to the Pilbara Revitalisation Plan and is providing a further $350 million for social infrastructure projects in the region. The Pilbara Cities fact sheet also says that the cost of the project is '$471 million for urgent works for airport upgrades, wastewater services, serviced land and some accommodation'.[460]

Similarly, IA lists the Mid-West Energy Project State 2 as having a capital cost of $795 million, while DSD Fact Sheet 4 states that the project cost for Stage 2 is approximately $280 million.

To clarify this confusion, advice was sought from IA in relation to their reported costings. Information received shows that the capital cost figures shown in Table 7.4 represent the capital cost of the whole project, rather than only the cost to government, and where a project consists of different stages, the overall project cost is shown. For example, the Pilbara Cities figure of $2,900 million is made up of $471 million for urgent investment and $2,462 million for medium term

458 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities. An Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010, p.50, p.59, p.61 and pp.63–67. Note that the South West Industrial Park Linkages project was submitted by the South West Development Commission and the Eastern Goldfields Railway Freight Gateway Upgrade Project was submitted by West Net Rail.

459 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities. An Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010. For *, see: Infrastructure Australia, *National Infrastructure Priorities. Infrastructure for an Economically, Socially, and Environmentally Sustainable Future*, Commonwealth of Australia, May 2009, p.10 and p.11.

460 Department of State Development, *Infrastructure Australia Submissions 2009. 2. Pilbara Cities*, nd. Available at: http://www.dsd.wa.gov.au/7647.aspx. Accessed on 16 September 2010.

investment, and IA's data for the Mid-West Energy Stage 2 project actually includes Stage 1 of that project.

DSD used IA guidelines to evaluate and categorise government agencies' infrastructure projects, and grouped proposals into three categories:

1. *Projects which were well developed;*

2. *Potentially suitable projects with strong alignment; and*

3. *Projects which did not align closely with IA priorities.*[461]

The projects DSD assessed as meeting category 1 were provided to Cabinet for consideration. Cabinet endorsed seven for submission to IA.[462] However, as Table 7.4 shows, IA did not agree with DSD's assessment of these projects. Of the seven submitted, none were categorised by IA as either Threshold or Ready to Proceed. Only two received a Real Potential rating, namely Mid-West Energy and Gateway WA, while Pilbara Cities and the Port Hedland Harbour Capacity Enhancements project were deemed to be Early Stage projects. The remaining three—Kimberley Supply Base, Grain Freight Network and Brunswick to Bunbury Port Rail Duplication—were not categorised in IA's 2010 report.

It is a concern that in November 2009, particularly after IA had produced its Minimum Information Requirements document, DSD provided submissions to Cabinet which it believed were well developed, but which IA deemed in some cases needed considerable further work. Furthermore, while IA advised that it understood that previous submissions had been required at a time when Western Australia was in an election period, the submissions listed in Table 7.4 were made on 5 November 2009.

In September 2010 IA was still awaiting the Bankable Feasibility Study (BFS) on the Oakajee Port project, although it was understood by IA that the state government needed to scrutinise the BFS provided by Oakajee Port and Rail (OPR) very carefully and involve Treasury and DSD in that process.[463]

IA acknowledges there have been some issues with the state government's submissions and advised that they were working with the State in a very collaborative and constructive way to prepare for the coming round of submissions. IA informed the Committee that the structure of the Western Australian Planning Commission and the long-term approach to planning in the state are examples of things that this State does well.[464]

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461 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.49.

462 ibid.

463 Mr Michael Deegan, Infrastructure Coordinator, Infrastructure Coordinator, *Committee Briefing*, 18 August 2010.

464 ibid.

Western Australia is learning from other jurisdictions in relation to their planning processes. For example, from Victoria, the state government is adopting a gateway review process[465] and an Investment Logic Mapping tool that is applied prior to producing a business case and which focuses on the service delivery problem to be resolved.[466] Victoria is held in high regard by IA and other organisations such as the Royal Bank of Scotland (RBS). Mr Hugh Funder, Senior Adviser (Infrastructure Advisory) at the RBS, advised that:

> *one thing that the Victorians do very well is that they are consistent in their gateway methodology, in what gets procured in which way. We are confident with that methodology that we can say that if they are going to do a big hospital, it will come out of a PPP, and so on. So we can in a sense imagine a pipeline even if it is not explicit in Victoria.*[467]

Mr Funder noted that the way in which projects are procured in Western Australia is rated as medium, although with the state turning 'an eye to Victoria' this has improved.[468]

(g) Federal Funding as an Equity Injection

As noted elsewhere in this report, the federal government's May 2009 Budget provided for a $339 million equity injection for the Oakajee Port Common Use Facilities project, subject to IA's consideration of a business case to be provided by the state government.[469] According to DSD, this would allow the federal government some 'control and influence over how the dollars are used', and affords them the opportunity to 'track and understand what the rate of return on that investment was and whether they took that to a commercial rate'.[470]

On providing the funding, the Commonwealth Government will have an 'ownership stake' in the Oakajee Port Common Use Facilities and expects this investment to be 'ultimately commercial'.[471] The precise arrangements and the ensuing implications of the equity injection are unknown, and Ms Anne Nolan, Director General DSD, advised 'it is early days in that conversation and we have not come to a complete landing'.[472] In discussing what a possible arrangement might be, Ms Nolan stated:

> *you could envisage that the Geraldton Port Authority could have a subsidiary entity, which it is able to do under the Port Authorities Act, and the shareholders of that subsidiary could be the commonwealth and the state. That would reflect their ownership shares in that vehicle and therefore the commonwealth and the state would have a role in the*

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465 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.12.

466 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.6.

467 Mr Hugh Funder, Senior Adviser (Infrastructure Advisory), Royal Bank of Scotland, *Transcript of Evidence*, 8 September 2010, p.3.

468 ibid.

469 Hon. Anthony Albanese, MP, (Minister for Infrastructure, Transport, Regional Development and Local Government), *Investing in the Nations Infrastructure Priorities*, Media Statement, 12 May 2009. Available at: http://www.minister.infrastructure.gov.au/aa/releases/2009/may/budget-infra_01-2009 .htm. Accessed on 16 September 2010.

470 Ms Anne Nolan, Director General, Department of State Development, *Transcript of Evidence*, 5 March 2010, p.16.

471 ibid.

472 ibid.

> *direction of that company through board membership, for example. That is a potential model. I am not saying that that is where we are at, but that gives you a feel of how that could occur. Appropriate charging and pricing structures would be established for the common-user infrastructure at Oakajee and there would be separate accounting and reporting on that investment.*[473]

One known consequence of a federal equity injection into a state project is the way in which the funding and the project appear in the State's accounts. Rather than the federal funding coming to the State as operating revenue and the State having an asset on its balance sheet, the federal government will want to maintain its equity on its balance sheet. Therefore, both the state and federal governments will show their contributions on their respective balance sheets.[474]

(h) A Strategic Approach

It is clear that Western Australia must endeavour to maximise its opportunities to obtain additional non-state sources of funding for major infrastructure projects. This is particularly so given, first, that IA is reviewing options to attract non-government funds to invest in infrastructure assets[475] and second, there can be no guarantee that the level of federal funding will be sustained over the long-term. One option is for governments to have greater involvement in projects as PPPs (see Chapter 8).

DPC acknowledges that the government needs to be 'both strategic and responsive in identifying projects, and when developing proposals for submission to the Commonwealth for funding'.[476] Such an approach involves using the 'various State planning, priority setting and decision-making mechanisms' to identify projects to be developed for federal funding proposals.[477]

These mechanisms include agency planning strategies, SAMF and/or the State Budget process. According to DPC, a responsive approach 'seeks to optimise the level of Commonwealth funding as and when it becomes available […. taking] into consideration the Commonwealth's stated priorities, timing and funding criteria when developing funding bids'.[478]

Furthermore, DPC states that while the state's highest priority projects may not always receive funding, federal funding will be sought 'where there is alignment with State priorities, a State contribution may leverage additional Commonwealth funds, or where this may release capital for other projects'.[479]

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473 ibid.

474 Mr Anthony Kannis, Executive Director, Infrastructure and Finance, Department of Treasury and Finance, *Transcript of Evidence*, 2 August 2010.

475 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities, An Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010, p.12.

476 Submission No. 3 from Department of the Premier and Cabinet, 12 February 2010, p.48.

477 ibid.

478 ibid.

479 ibid.

Finding 21

In developing a list of funding recommendations Infrastructure Australia assesses funding submissions against a number of criteria, and places particular emphasis on the rigor of the cost-benefit analysis.

Finding 22

Submissions from Western Australia to Infrastructure Australia were assessed by the Department of State Development as being 'well developed' projects; however, Infrastructure Australia did not classify any of the Western Australian submitted projects as being well developed or 'ready to proceed'.

Finding 23

None of the Western Australian projects submitted to Infrastructure Australia in the 2009 round for federal funding were classified as 'ready to proceed', the ratings being 'threshold', 'real potential' or 'early stage'.

Finding 24

Failure to provide well developed and robust submissions to the federal government will decrease the potential for Western Australian projects to receive federal funding.

Recommendation 7

The Department of Treasury and Finance and the Department of State Development should ensure that the funding applications to the federal government are well developed, contain robust cost-benefit analyses and comply with Commonwealth funding submission requirements.

CHAPTER 8 PUBLIC PRIVATE PARTNERSHIPS IN WESTERN AUSTRALIA

Public Private Partnerships (PPPs) have become an increasingly popular method by which Australian governments have sought to procure and provide public infrastructure and associated services.[480] While none of the projects examined for this report were procured via a PPP, the PPP contract model is an option that agencies must consider through the Strategic Asset Management Framework (SAMF) process where appropriate. This procurement model is being pursued by the Western Australian Government for a number of projects.

To provide context for discussing the use of PPPs for Western Australian infrastructure projects, this chapter provides an overview of PPPs, their characteristics, advantages and drawbacks. Following that, the use of PPPs in infrastructure provision in Western Australia is examined.

8.1 The Public Private Partnership Market

According to the World Economic Forum, 'in many developed economies, private finance has been making an increasingly significant contribution to infrastructure development … through public-private partnership (PPP)-type transactions',[481] attributable in part to an acknowledgement that governments have a limited capacity to fund all infrastructure projects from the public purse. Therefore, there will be a gap between the funding needed for infrastructure and the funding that is available via government. This necessarily raises the question of what mechanism might be available to help fill that gap. One possibility lays in the potential for private contributions to the development of infrastructure. While there are other possibilities, such as attracting investment in infrastructure from superannuation funds, for the purpose of this report, the primary option is for projects to be developed as PPPs.[482]

The United Kingdom reportedly has 'one of the most highly developed PPP programs' with government estimates of private-sector investment in infrastructure over the previous 10 years being more than UK£100 billion.[483] In 2002, the Australian Procurement and Construction Council argued that the PPP experience of the United Kingdom was driving Australia's current interest in PPPs.[484] However, the fact that most Australian states 'have been outsourcing construction and certain operating services to the private sector for a number of years' means that the 'the public sector procurement environment in Australia is significantly different to that in the

480 Wettenhall, R, 'The Rhetoric and Reality of Public-Private Partnerships', *Public Organization Review*, vol. 3, no.1, 2003, p.77.

481 World Economic Forum USA Inc., *Paving the Way: Maximizing the Value of Private Finance in Infrastructure*, report prepared in collaboration with PricewaterhouseCoopers, World Economic Forum USA Inc., New York, August 2010, pp.7-9.

482 Infrastructure Australia, *Getting the Fundamentals Right for Australia's Infrastructure Priorities, an Infrastructure Australia Report to the Council of Australian Governments*, Commonwealth of Australia, Canberra, June 2010, p.12. Infrastructure Australia is examining ways in which superannuation funds might be utilised for infrastructure investment.

483 World Economic Forum USA Inc., *Paving the Way: Maximizing the Value of Private Finance in Infrastructure*, report prepared in collaboration with PricewaterhouseCoopers, World Economic Forum USA Inc., New York, August 2010, p.9.

484 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.3.

UK'.[485] One consequence of this is that the efficiencies achieved through increased PPPs in Australia may be less than those obtained in the United Kingdom.[486] Nevertheless, the Allen Consulting Group reports that 'the Australian PPP market is already among the most sophisticated PPP markets in the world, but continues to improve and evolve'.[487] Furthermore, according to (former) State Treasurer Eric Ripper, 'Western Australia has for some time now actively engaged the private sector in the provision of physical infrastructure and ancillary services'.[488]

The exact size of the Australian PPP market is not known. While estimates vary, the 2004 National PPP Forum maintained that 'at that time, over $9 billion in PPP projects were already contracted. This comprised over $4 billion in PPP projects currently in the market and over $5.5 billion of projects being considered for delivery as PPPs'.[489] As will be demonstrated below, Western Australia has a small but growing PPP market.

Whatever the size of the PPP market for infrastructure projects in Australia, Infrastructure Australia (IA) regards PPPs as a 'key element in meeting the Australian Government's commitment to developing Australia's productive capacity and modernising key infrastructure'.[490] Furthermore, for IA, consideration of PPPs is now a 'priority policy issue' due to the potential they offer in accelerating infrastructure provision and thus more quickly 'bridg[ing] critical public infrastructure gaps'.[491] There are, however, advantages and disadvantages to investing in infrastructure via a PPP, and unless a project is stringently assessed and effectively executed, the PPP project may result in adverse economic outcomes for the state (see section 8.4).

It is also important to acknowledge the influence that capital markets have on the prospects of the PPP market, both in Australia and internationally. It has been argued that PPPs are 'heavily dependent on capital markets' on a number of five levels.[492]

Current indications are that PPPs will be placed under pressure due to present market conditions, including capital market volatility and uncertainty.[493] Research suggests that 'future PPPs will be subject to new disciplines — lower leverage, higher reserves, stronger underlying credit credentials, higher debt service coverage criteria and high cost debt', and that these conditions will

485 ibid.

486 ibid.

487 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, p.12.

488 Department of Treasury and Finance, 'Foreword from the Treasurer of Western Australia', *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.1.

489 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, p.12.

490 Infrastructure Australia, *Discussion Paper 2: Public Private Partnerships*, Commonwealth of Australia, Canberra, nd, p.2.

491 ibid.

492 Regan, Michael, Smith, Jim and Love, Peter, 'Public Private Partnerships: What does the Future Hold?' paper presented at RICS COBRA Research Conference, University of Capetown, 10–11 September 2009, p.467. These include: Equity Capital, Debt Capital, Financial Services, Drivers of the Bid Market, Capital Market Innovation.

493 Regan, Michael, Smith, Jim and Love, Peter, 'Public Private Partnerships: What does the Future Hold?' paper presented at RICS COBRA Research Conference, University of Capetown, 10–11 September 2009, p.462.

affect both bid depth and government risk allocation (due to sponsors' expected tougher position on taking delivery and operational risks).[494]

Given current conditions, financial advisers and lenders suggest that while they will remain possible, 'PPP transactions will be harder to do'.[495]

8.2 What is a Public Private Partnership

(a) Defining a Public Private Partnership

The term PPP has been referred to as 'a loose term applied to any venture which embraces both public and private sectors';[496] it might be used in a slightly narrower sense to refer to 'a partnership between the public and private sector for the purpose of delivering a project or service, which would traditionally be provided by the public sector';[497] or it might be used more narrowly to refer to:

> *partnerships between the public and private sectors for the financing, design, construction, operation and maintenance, and/or the provision of assets or infrastructure and associated services that have traditionally been provided by the public sector.*[498]

For IA, PPPs are quite narrowly defined as:

> *contracts for private sector provision of public infrastructure and related services that would otherwise be provided by the Government. PPPs generally involve private sector design, construction, financing, ownership, operation and maintenance of public infrastructure and the provision of related services. PPP contracts are usually for long periods (e.g. 15–30 years) after which the infrastructure is transferred back to public ownership. In some circumstances the private sector owns the infrastructure outright.*[499]

In Western Australia, *Partnerships for Growth*, the State's 2002 PPP policy, defines PPPs as 'the procurement of public infrastructure and ancillary services through a joint arrangement between the public and private sectors'.[500] This policy sees a PPP as a process, 'rather than a readily defined object'.[501]

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494 ibid., p.462 and p.467.

495 ibid., p.467.

496 Jefferies, Marcus and McGeorge, WD, 'Using Public-Private Partnerships (PPPs) to Procure Social Infrastructure in Australia', *Engineering, Construction and Architectural Management*, vol. 16, no. 5, 2009, p.421 of pp.415–37.

497 Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1. Available at: www.newrah.sa.gov.au/downloads/ppp.pdf. Accessed on 30 July 2010.

498 Jefferies, Marcus and McGeorge, WD, 'Using Public-Private Partnerships (PPPs) to Procure Social Infrastructure in Australia', *Engineering, Construction and Architectural Management*, vol. 16, no. 5, 2009, p.421 of pp.415–37.

499 Infrastructure Australia, *Discussion Paper 2: Public Private Partnerships*, Commonwealth of Australia, Canberra, nd, p.2.

500 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.3.

501 ibid.

The policy recognises that while there are similarities between PPPs and other models of infrastructure procurement such as 'Build, Own, Operate' and 'Build, Own, Operate, Transfer', there is one major difference: 'the Government continues to deliver the core services traditionally associated with a facility (such as teaching in schools and medical services in hospitals) while the private sector may deliver the ancillary services which support the infrastructure (such as security and maintenance)'.[502] For the Royal Bank of Scotland (RBS), a classic PPP 'is one in which the design, construction, financing and operation of the infrastructure is provided by the private sector, but with the exclusion of core services'.[503] This means that a PPP cannot be inconsistent with the service delivery and capital investment strategies of the proposing agency.

Rather than deliver core services, a PPP is designed to facilitate them. Furthermore, as Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS, explained:

> *there are a range of variants on that theme, and each PPP we deal with inevitably has a slightly different scope in the operations phase. In the hospital environment, for example, some jurisdictions really only procure via a PPP what we call hard facilities maintenance—that is, the maintenance of the fabric of the building, such as the air-conditioning and that sort of thing, and making the building work—as opposed to the soft facilities maintenance, which includes cleaning, security, pest control and those kinds of things, where most of the people in a hospital are found. There are various approaches in various jurisdictions in terms of the extent to which that soft facilities maintenance actually falls within the PPP.*[504]

8.3 What Types of Projects Suit PPPs

Not all types of public infrastructure projects are suitable for delivery as a PPP, and not all PPP projects have achieved successful outcomes for government and/or project sponsors and operators. While there is significant global interest from governments in procuring infrastructure via PPPs, 'not everyone in the global PPP market is convinced of their value'.[505]

Mr Ward acknowledged that 'only some projects are suitable for a PPP', and advised the RBS 'was a long way from recommending that [the PPP model] be used as a cure-all for project delivery'.[506] Mr Roger Black of Deloitte Corporate Finance echoes this sentiment: 'PPP's have proven to be an effective infrastructure delivery tool – under specific conditions!'[507]

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502 ibid. Core services are those that a particular agency has been established to deliver; for example, nurses, teachers and police officers deliver core services.

503 Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.6.

504 ibid., pp.6–7.

505 Apurva, Sanghi, Sundakov, Alex and Hankinson, Denzel, 'Designing and Using Public-Private Partnership Units in Infrastructure. Lessons from Case Studies around the World', *Gridlines*, no. 27, September 2007, p.1.

506 Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.3.

507 Black, Roger, *PPPs and the Water Sector. Plugging the Infrastructure Hole*, Deloitte Corporate Finance, Infrastructure and Project Finance, March 2009, p.8.

Partnerships for Growth also suggests that in Australia, state government level PPPs are:

- *generally for new infrastructure rather than replacement infrastructure …*
- *more likely to be based around traditional infrastructure assets such as buildings and transport facilities, rather than highly complex defence hardware or civil aviation systems …*
- *in areas where the private sector has a proven track record in the successful delivery of assets and their ancillary service needs.*[508]

The Allen Consulting Group's study found that the size of a project is a significant factor in the effectiveness of the PPP procurement model. It was found that for traditional projects 'size had a marked (statistically significant) negative impact on time over-runs', but this was not the case for PPPs 'whose timeliness of completion were not negatively impacted by size of project'.[509]

RBS also points to project scale as a major factor in project suitability, noting that 'larger projects as a rule are better suited to PPP[s] than the smaller ones, given the process and the resources required on both government and private sector sides to come to the close of a PPP transaction'.[510]

Partnerships for Growth also acknowledges that some forms of infrastructure are better suited for development via PPP arrangements, with the following types of infrastructure considered to be suited to the PPP procurement model:

- transport – road, rail and maritime;
- general purpose accommodation, such as offices;
- health facilities;
- justice facilities;
- schools and training facilities; and
- support and seed infrastructure for industry.[511]

A flexible approach is also important, and governments may consider PPPs in less conventional areas as opportunities arise.

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508 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.3.

509 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, p.1.

510 Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.3.

511 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, pp.6–7.

It is possible to draw from international PPP experiences to learn which factors most impact on the likely success or otherwise of a PPP project. Vickram Cuttaree, writing for the World Bank in 2008, and Roger Black for Deloitte Corporate Finance in 2009 provide a number of reasons for poor PPP outcomes, including:

- poor legal framework and enforcement;
- poor initial design of PPP policies and guidance;
- lack of adequate public sector capacity and PPP strategy;
- inadequate planning, including poor financial and economic analysis;
- lack of clarity and consensus surrounding project outcomes;
- unrealistic revenue and cost estimations;
- inappropriate sharing of risks due to the PPP option chosen;
- lack of procurement competition;
- lack of assessment of the public's willingness to pay for the service; and
- failure to realise value for money, either from imbalance of efficiency gains and costs or from a lack of understanding by government on how to test value for money.[512]

From this, it is possible to list the key success factors for PPPs as including:

1. *Careful planning of PPP project*
2. *Solid revenue and cost estimate*
3. *User willingness to pay and communication plan*
4. *Extensive feasibility study with use of PPP experts*
5. *Compliance with contractual agreement*
6. *Appropriate Legal and Regulatory Framework*
7. *Strong Institutions with appropriate resources*
8. *Competitive and transparent procurement*
9. *Mitigation and flexibility in managing micro-risks*[513]

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512 Cuttaree, Vickram, *Successes and Failures of PPP Projects*, World Bank, Europe and Central Asia Region, paper presented in Warsaw, 17 June 2008, p.6; and Black, Roger, *PPPs and the Water Sector. Plugging the Infrastructure Hole*, Deloitte Corporate Finance, Infrastructure and Project Finance, March 2009, p.8.

In deciding on whether a PPP procurement model will provide the best possible value for money outcome, agencies must thoroughly evaluate and assess their options. The proper allocation of risk, even when future needs are uncertain, is considered achievable when the public sector has a 'strong understanding of the **range** of possible PPP models'.[514]

The Centre for Excellence and Innovation in Infrastructure Delivery's (CEIID's) *Infrastructure Procurement Options Guide* suggests that PPPs provide most benefit in circumstances where there is:

- clearly defined and measurable required outputs, which allows for a structured payment mechanism;
- a competitive market with strong market interest;
- significant opportunity for appropriate risk transfer;
- complexity of project design;
- a whole-of-life approach to the integration of a cost effective package for the design, construction, operation and maintenance of the infrastructure;
- significant scope for innovation in design, construction and delivery of public infrastructure; and
- potential for third-party use of facilities, which would reduce net government costs.[515]

8.4 Benefits and Drawbacks of PPPs

In the right circumstances, PPPs have the capacity to provide significant value for money to taxpayers as a result of cost savings and other efficiencies offered by private sector expertise.[516] The main benefit claimed for PPPs is that they provide value for money through, for example, completing projects on time and on budget, reducing risk to government, improving the quality of services and facilitating innovation.

However, there are also potential drawbacks to PPPs, which can result in higher bidding, finance and transaction costs and barriers to competition. These and other possible benefits and drawbacks are discussed below.

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513 Cuttaree, Vickram, *Successes and Failures of PPP Projects*, World Bank, Europe and Central Asia Region, paper presented in Warsaw, 17 June 2008, p.13.

514 Black, Roger, *PPPs and the Water Sector. Plugging the Infrastructure Hole*, Deloitte Corporate Finance, Infrastructure and Project Finance, March 2009, p.9, original emphasis.

515 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.27–29.

516 Webb, R, and Pulle, E, 'Public Private Partnerships: An Introduction', *Research Paper No. 1 2002-03*, 24 September 2002. Available at: http://www.aph.gov.au/library/pubs/rp/2002-03/03RP01.pdf. Accessed on 31 March 2009.

(a) Potential Benefits of PPPs

(i) Value for Money

One of the most common and overarching benefits claimed for PPPs is that they provide value for money in comparison with traditional procurement models. Supporters of PPPs see them as 'the most cost effective solution',[517] with the PPP cost advantage claimed to be, in absolute terms, both economically and statistically significant. Using publicly available data for 54 PPP projects across Queensland, New South Wales and Victoria, the Allen Consulting Group found superior cost efficiencies for PPP procurement to 'range from 30.8 percent when measured from project inception, to 11.4 percent when measured from contractual commitment to the final outcome'.[518]

The RBS advised that 'there is fairly good evidence in Australia that the public sector gets good value for money, in both social and economic infrastructure, from PPPs' over the past decade.[519] For example, while economic infrastructure in the form of toll roads in the eastern states has received bad publicity and financiers have lost considerable sums of money, those roads 'operate perfectly well … the infrastructure is there. The risk transfer was definitely there'.[520]

Similarly, while acknowledging variations in relation to different types of projects, *Partnerships for Growth* notes the strong evidence that PPPs 'generate synergies through the alignment of design, construction, maintenance and operation phases by forming consortia to get better value for money for the taxpayer's dollar'.[521] However, the degree to which a PPP does generate value for money depends on the degree of rigour that is applied to its planning and implementation. As the Australian Procurement and Construction Council argues:

> *sound preparation and proper interpretation of performance specifications is critical if value-for-money is to be achieved. This may be most challenging for social infrastructure, normally procured through detail specification.*[522]

Likewise, the RBS believes that 'getting a value for money outcome requires a level of definition';[523] the higher the level of definition of desired outcomes and outputs, the better the value for money outcome.

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517 Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1. Available at: www.newrah.sa.gov.au/downloads/ppp.pdf. Accessed on 30 July 2010.

518 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, p.1.

519 Mr Hugh Funder, Senior Adviser, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.6.

520 ibid.

521 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.4.

522 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.3.

523 Mr Hugh Funder, Senior Adviser, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.4; and Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.4 and p.9.

Value for money can also be generated through bundling projects. For example, RBS advised that in New South Wales they 'have done two bundles of schools. They are not particularly complex buildings. But by bundling them up and getting some efficiencies, it has been great value for money for the state'.[524]

(ii) Apportionment of Risk

The apportionment of risk across both the public and private sectors is a significant element of a PPP and represents one of their key attractions to government. Through apportioning some of the risk to the private sector, PPPs limit taxpayers' exposure to commercial activity risks.[525] The joint skills of the public and private sectors manifest in PPPs lead to greater effectiveness in the management of risks that are inherent in large, complex infrastructure projects.[526]

The Australian Procurement and Construction Council discusses risk apportionment in PPPs in terms of optimum risk allocation. It states that:

> *appropriate risk management, especially identifying and valuing risk, and optimising risk allocation underpins value-for-money achieved through PPP procurement. Risk management is continuous throughout a project's dynamic lifecycle and needs to take account of government commitments, expectations and post-concession (contract) interests.*[527]

Similarly, CEIID sees greater transfer of risk to the private sector at each phase of a PPP project, and argues that the 'overall design and fit for purpose risk lies with the private sector party'.[528] For industry to be willing to accept this substantial transfer of risk, amongst other things, the project needs to be well defined.[529]

(iii) Projects Delivered on Time and on Budget

As well as providing value for money, PPPs have delivered projects on time and on budget. In fact, 'early project delivery' has been cited as one of the reasons governments are attracted to this method of procurement.[530]

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524 Mr Hugh Funder, Senior Adviser, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.6.

525 Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1. Available at: www.newrah.sa.gov.au/downloads/ppp.pdf. Accessed on 30 July 2010; and Public Accounts Committee, *Public Accounts Committees and Public-Private Partnerships*, paper delivered at the 2009 ACPAC Conference, Wellington, April 2009.

526 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.4.

527 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.10.

528 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.28–29.

529 Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.4.

530 Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1. Available at: www.newrah.sa.gov.au/downloads/ppp.pdf. Accessed on 30 July 2010.

The Allen Consulting Group reports that Australian governments have 'a very high level of confidence that infrastructure will be available on time and without cost blow-out' when delivered via a PPP, and that PPPs result in 'improved outcomes, by using competitive forces to stimulate creativity, pricing and delivery'. [531] It is also possible that bundling into a PPP a number of 'smaller otherwise unconnected projects' scheduled for delivery years into the future will result in more timely service delivery.[532]

It is reasonable to suggest that the stringent planning requirements for a PPP project should help them to be delivered on time and on budget. This suggestion is supported by RBS, which advised that 'some of the evidence that is there for why a PPP is more accurate in terms of cost and time is because the public sector side has to know what it wants and has to be able to specify that in some detail'.[533] This allows the private partner to price the project, innovate where possible and then provide their bid to government. It had been RBS's experience that:

> *the less well-defined projects will result in a more tortuous and long procurement process, and often there is a point that is crossed where if a project is not able to be sufficiently well defined in terms of its output specification, then that is the kind of project that I would suggest is not suitable for a PPP procurement. In other words, because of the level of risk transfer that is sought and the level of certainty that is required in a PPP, some projects would not meet that threshold if they are not sufficiently well defined.*[534]

Under Treasurer Tim Marney also believes that entering a PPP ensures that government's planning must be more rigorous than it can sometimes be.[535]

It must be noted that full application of SAMF would ensure that many of the benefits purported to accrue from PPP procurement could also be delivered through other contract models.

(iv) Maintenance and/or Improvement of Standards

Another potential benefit of PPPs is an improvement of standards in the ancillary services provided.[536] According to the Australian Procurement and Construction Council, it is through such factors as 'contestability, private sector "know how"… diversity of management skills, integrated

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531 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, pp.1–10.

532 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.10.

533 Mr Hugh Funder, Senior Adviser, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.3.

534 Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.4.

535 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.12.

536 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, pp.9–10; and Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1. Available at: www.newrah.sa.gov.au/downloads/ppp.pdf. Accessed on 30 July 2010.

Facilities Management (FM) services packaging and performance measures/incentives that PPPs improve the efficiency and quality of the ancillary services they provide.[537]

Similarly, the 'bundling of building, maintenance and operations' in a PPP infrastructure project can provide service efficiencies and quality improvements. [538] CEIID suggests that the 'transfer of lifecycle cost risk encourages efficient design and quality construction and finishes – therefore certainty of maintenance standards as agreed and cost certainty as approved for a long term e.g. 25 years'.[539]

Partnerships for Growth also expresses the Western Australian Government's position on PPPs as being able to optimise the quality of infrastructure and services.[540] According to this policy, the agreed maintenance and service standards established through a PPP:

> *provide[s] the opportunity for major public assets to be maintained and preserved to a standard which is higher than has been traditionally possible by the public sector. In the long term this saves on refurbishment costs and makes our public buildings more attractive and safer places to visit, in which to work, and in which to do business.*[541]

Through incorporating maintenance and service standards in a PPP, the whole-of-life asset management is optimised as the infrastructure is supported with 'guaranteed services to ensure its continued usefulness, efficiency and longevity'.[542]

A further benefit is the improvement of up-front planning, which, as the Department of Treasury and Finance (DTF) acknowledges, has not been 'as rigorous as it needs to be' over the past decade.[543] Mr Marney advised the Committee that PPPs:

> *to an extent, force you to do your traditional construction costings and planning much better than sometimes we have done in the past, because you have got to be able to compare like with like. Unless you do your planning well for your internal construct and operate, then you cannot compare it with the external bits. So it does force a degree of rigour that sometimes we find is easily shortcut.*[544]

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537 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.10.

538 Henckel, Timo and McKibbin, Warwick, 'The Economics of Infrastructure in a Globalized World: Issues, Lessons and Future Challenges', Conference Proceedings, Brookings Institution, Washington DC, 4 June 2010, p.6. See also: Chan, Chris, Forwood, Danny, Roper, Heather and Sayers, Chris, *Public Infrastructure Financing: An International Perspective*, Staff Working Paper, Productivity Commission, Melbourne, March 2009, p.143.

539 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.28–29.

540 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.4.

541 ibid.

542 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.4; and Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.10.

543 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.12.

544 ibid.

(v) Innovation

PPPs tend to focus on outcomes and have rigorous performance requirement specifications which, when combined with PPPs' public-private nature, allows them to take advantage of the innovative ideas and technology traditionally developed in commercial environments. This gain from innovation can then be passed on to the users of public infrastructure.[545] The level to which a PPP's private partner can innovate is affected by the level of project definition provided by government.

(vi) Improved Skills Base

Not only do PPPs provide government with access to expert technical and management skills,[546] the public sector can, through their interactions with those from the commercial sector, including commercial negotiators and decision-makers, improve the skills base of its employees. This is particularly so in the development of procurement skills and commercial acumen, and gaining valuable experience in project finance.[547]

DTF expects that over time, possibly four or five years, there will be an increase in PPP capabilities within DTF staff gained through experience and learning from past and current projects.[548] In speaking of the Perth CBD Court Complex, Mr Marney explained that over time, DTF could probably:

> *do better in terms of knowing what to look for and what capabilities we need to assemble to be able to look for it. In time I expect we will be able to do it more efficiently, but a key determining factor is the complexity of the project and how much is factored into service delivery elements in partnerships.*[549]

This view is supported by RBS, which draws from experiences in other jurisdictions, in that 'early PPP projects are the most difficult' and that there were 'lessons learned on both sides of the fence during earlier PPPs'.[550] The lessons learned on one PPP can translate into better processes, and improved quality of interactions and outcomes for subsequent projects in the same jurisdiction.[551] However, RBS also expressed concern that 'with the passing of time, the lessons learned from that

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545 Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1. Available at: www.newrah.sa.gov.au/downloads/ppp.pdf. Accessed on 30 July 2010; Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.4; and Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.28–29.

546 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, pp.9–10.

547 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.4.

548 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.12.

549 ibid., p.11.

550 Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.8.

551 ibid.

PPP would be lost to PPPs to follow'.[552] Hence the importance of having a pipeline of projects that will allow industry to develop confidence in the Western Australian market. This point is discussed further in Chapter 9.

Improvement in agencies' skills base through experience is an important benefit of a PPP as it helps to mitigate some public sector risk in infrastructure provision.

(vii) Financing

The use of PPPs in the procurement of public infrastructure and ancillary services also realises benefits in relation to the financing of the project. Finance-related benefits to government in a PPP arrangement include:

- greater flexibility in arrangements through, for example, better asset utilisation 'including staged development and/or accessing third party revenues'[553]
- assets or services are paid for only when delivered
- providers can be held financially accountable for performance
- access to infrastructure financing without increasing government borrowing[554]

(b) Possible Drawbacks of PPPs

While the abovementioned benefits offer clear incentives to governments to enter into PPPs, there are a number of potential drawbacks that need to be considered. In Australia, PPPs have been subjected to considerable controversy following some high profile 'failures'. Critics have pointed to high bidding costs associated with PPPs, refinancing issues, cost overruns, construction failures, design irregularities, windfall profits and a lack of transparency.[555] Clearly some of these potential drawbacks are also seen by some as potential benefits. This suggests that whether a factor is a benefit or a drawback is largely dependent on the project and the circumstances in and for which it is being developed. The most mentioned drawbacks are high bidding and transactions costs, and the consequences of financing arrangements.

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552 ibid., p.9.

553 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.2.

554 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, pp.9–10; Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.28–29; Department of Health, *Public Private Partnerships*, Government of South Australia, Adelaide, nd, p.1; Public Accounts Committee, *Public Accounts Committees and Public-Private Partnerships*, paper delivered at the 2009 ACPAC Conference, Wellington, April 2009; and Henckel, Timo and McKibbin, Warwick, 'The Economics of Infrastructure in a Globalized World: Issues, Lessons and Future Challenges', Conference Proceedings, Brookings Institution, Washington DC, 4 June 2010, p.6.

555 Allen Consulting Group and the University of Melbourne, *Performance of PPPs and Traditional Procurement in Australia*, Final Report to Infrastructure Partnerships Australia, Allen Consulting Group, Melbourne, 30 November 2007, pp.9–10.

(i) High Bidding and Transaction Costs

High bidding costs are an issue for most private construction enterprises bidding on public infrastructure projects. The evidence suggests that this is also the case for the PPP industry, with contracting and transaction costs held to be high and, at times, excessive.[556]

In fact, for PPP market participants, the very high bidding costs represent a major drawback to participation.[557] A recent review of the procurement of PPP projects reports that for projects of $250 to $300 million capital value, bidding costs are generally around $2.5 million. This increases to $5 to $6 million for a $1 billion project and $30 million or more for a project of $2 billion capital value.[558]

High costs associated with considering a PPP project are not restricted to the private sector. Mr Marney acknowledged that:

> *it takes quite a bit of investment, both for the public sector and for the PPP industry, to actually explore these projects. The bid costs for private proponents, in assembling their consortia and going through the process, can run into multiple millions of dollars, if not tens of millions of dollars.*[559]

The bid phase can require significant public sector resources to evaluate a PPP model, and determining feasibility can also be a lengthy process. Therefore, there is likely to be higher departmental tendering and resourcing costs, particularly as the financial and technical assessments, and the tendering process requires either the appropriate level of skill within the department or the engagement of consultants.[560]

In relation to resource requirements, Mr Marney confirmed that a dedicated PPP unit had been established in DTF as the department does not:

> *have the capability to set around public–private partnerships and the planning thereof, the procurement and the evaluation and negotiation. There is a need for us to augment our resources in that regard both in terms of commercial contracting and legal services. Even as simply as updating and ensuring the policy settings and guidelines are appropriate for the current environment, we have basically come to the conclusion that if we do not resource it, then we will not be doing the right thing by the public in terms of making sure*

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556 Henckel, Timo and McKibbin, Warwick, 'The Economics of Infrastructure in a Globalized World: Issues, Lessons and Future Challenges', Conference Proceedings, Brookings Institution, Washington DC, 4 June 2010, p.6; and Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.3.

557 Infrastructure Australia, *PPP Procurement Review of Barriers to Competition and Efficiency in the Procurement of PPP Projects*, report prepared by KPMG Corporate Finance (Aust) Pty Ltd, May 2010, p.1. These costs necessarily relate to the high transactions costs to government mentioned above.

558 ibid.

559 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.10.

560 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.28–29.

> *these things are rigorously planned, evaluated and assessed and that advice given to government is sound, robust and comprehensive.*[561]

These increased development and bidding phase costs need to be offset against possible lower asset development and service provision costs.[562]

(ii) Barriers to Competition

Bidding costs of the magnitude noted above represent a significant barrier to competition as it limits the number of potential partners willing or able to prepare a tender.[563] Such limited competition in the bidding process leads to 'inefficient competitive arrangements' which, in turn, can lead to bilateral monopolies.[564]

The KPMG review of PPP procurement also found that 'a largely unknown pipeline of projects that is sporadic in nature' is a further barrier to competition in the PPP market.[565]

(iii) Finance Cost and Evaluations

The cost of private sector financing is considerably greater than the financing costs that can be accommodated by the State. Public sector borrowing will always be at a lower rate than the private sector. Given this, and according to the Department of Treasury and Finance, Strategic Projects (DTF-SP):

> *the efficiencies and savings that are generated through outsourcing must outweigh the additional costs of financing on the financial side, there are then obviously social and environment considerations, for example, that need to form part of a public interest test to determine whether we proceed.*[566]

Some note the heavy reliance on financial evaluation as the basis for PPP arrangements and the high dependence of value-for-money assessments on 'key assumptions/inputs and modelling techniques, especially in preparing the Public Sector Comparator'.[567] This is thought to risk marginalising non-financial criteria. The Public Sector Comparator is discussed further below.

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561 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.11.

562 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, pp.28–29.

563 Infrastructure Australia, *PPP Procurement Review of Barriers to Competition and Efficiency in the Procurement of PPP Projects*, report prepared by KPMG Corporate Finance (Aust) Pty Ltd, May 2010, p.2.

564 Henckel, Timo and McKibbin, Warwick, 'The Economics of Infrastructure in a Globalized World: Issues, Lessons and Future Challenges', Conference Proceedings, Brookings Institution, Washington DC, 4 June 2010, p.6; and Chan, Chris, Forwood, Danny, Roper, Heather and Sayers, Chris, *Public Infrastructure Financing: An International Perspective*, Staff Working Paper, Productivity Commission, Melbourne, March 2009, p.143.

565 Infrastructure Australia, *PPP Procurement Review of Barriers to Competition and Efficiency in the Procurement of PPP Projects*, report prepared by KPMG Corporate Finance (Aust) Pty Ltd, May 2010, p.2.

566 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.10.

567 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.3.

While there may be a positive balance sheet impact through PPP procurement, there is a negative impact on the operating statement. Mr Marney noted that the PPP payments from the government to the private sector 'would show up on the recurrent side through service obligations'.[568] This further impacts on the financial flexibility a government has in being able to fund its service delivery, and as these contracts are normally long-term, it also reduces government's ability to prioritise expenditure over the shorter term.[569]

(iv) Transfer of Political Risk

A key drawback in the PPP procurement model is that regardless of the strength of the contract, the political risk cannot be transferred to the private sector. If a project, once delivered, fails to provide the expected services, accountability rests with the government.

8.5 Western Australia's Approach to PPPs

(a) Policies and Guidelines

One of IA's first tasks was to develop a set of best practice PPP guidelines (National PPP Guidelines) to provide a consistent national framework to achieve the following objectives:

- *encourage private sector investment in public infrastructure and related services where value for money for government can be clearly demonstrated;*
- *encourage innovation in the provision of infrastructure and related service delivery;*
- *ensure rigorous governance over the selection of projects for PPPs and the competition for and awarding of contracts;*
- *provide a framework and streamlined procedures for applying PPPs across Australia; and*
- *clearly articulate accountability for outcomes.*[570]

IA has developed a number of key principles to be applied in the consideration of a PPP procurement option:

Value for money: 'achieving the best value for money outcome should be the key consideration at all stages of a project'

Public Interest: procuring and developing the project as a PPP should not be contrary

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568 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.9.

569 Australian Procurement and Construction Council, *Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.3.

570 Infrastructure Australia, D*iscussion Paper 2: Public Private Partnerships*, Commonwealth of Australia, Canberra, nd, p.1; and Infrastructure Australia, *National Public Private Partnership Guidelines*, *National PPP Policy Framework*. Available at: http://my.affinitext.com/viewer/book/?id=5318. Accessed on 21 September 2010.

	to the public interest
Risk Allocation:	optimal risk allocation should be achieved through allocating risk 'to whoever is best able to manage it'
Output Oriented:	maintaining a focus on services to be delivered rather than the method of delivery will maximise opportunities for innovation
Transparency:	information on the use of government resources in PPP projects, as well as disclosure of the processes and outcomes, should be available to Parliament, taxpayers and other stakeholders, taking into consideration the need to protect commercial confidentiality as appropriate
Accountability:	an agency's responsibility for delivery of services cannot be transferred to the private sector
Engaging the Market:	must only occur when there is clear scope for the private sector to deliver value for money and with the government's approval
Policy and Guideline Implementation:	must be carried out in 'a professional, fair, equitable and open manner ensuring probity and minimising of tendering costs'[571]

The National PPP policy and guidelines developed by IA were endorsed by the Council of Australian Governments (COAG) on 29 November 2008, and 'effectively replace previously existing policy and guidelines in those jurisdictions'.[572] All Australian jurisdictions are required to apply the policy to PPP procurement projects.

However, the policy recognises that individual jurisdictions will have different and/or additional specific requirements, and to accommodate these, IA has published a set for each jurisdiction, to be 'read in conjunction with the national guidelines in order to understand how specific jurisdictional practices differ from the national PPP policy and guidelines'.[573]

Mr Mann, DTF-SP, confirmed that Western Australia subscribes to these national guidelines which 'describe PPP selection processes and those PPP value drivers that should be examined early in project development to determine whether it is a PPP candidate'.[574]

The December 2002 *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia* sets out the government policy on, and guidelines for, the

571 ibid.

572 ibid.

573 Infrastructure Australia, *National Public Private Partnership Guidelines, Volume 6 Jurisdictional Requirements*. Available at: http://my.affinitext.com/viewer/book/?id=5325. Accessed on 21 September 2010.

574 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.9.

development of PPP projects. This document states that 'it is the policy of the Western Australian Government not to privatise public assets'.[575]

The June 2009 version of the *Western Australian Requirements* section of the National PPP Guidelines acknowledged that the 2002 *Partnerships for Growth* policy document 'establishes the policy principles for effective contract management'.[576] In April 2010 Mr Marney confirmed that a suite of policy guidelines had not been reissued in Western Australia and that considerable work was being undertaken 'to clarify the policy settings and processes that are to be followed in the exploration of PPPs'.[577] According to Mr Marney:

> *some of the core policy settings of the previous government remain in place, certainly in terms of how we recognise them financially, to ensure that there is transparency and that the financial disclosure or otherwise of the project does not distort the decision making around that project.*[578]

Furthermore, in relation to the policies and processes in operation at the time:

> *it is fair to say that the market has moved substantially from when we initially developed those. We need to update for where the market is, and also update those policies and procedures for what we have learned from experience in other jurisdictions.*[579]

In 2009, CEIID developed a draft Infrastructure *Procurement Options Guide* that described the different public infrastructure procurement methods available to agencies, including PPPs. This draft Guide provided information on the different PPP models, including their advantages and disadvantages. It also provided advice on the circumstances in which a PPP procurement may be most beneficial.

In August 2009, DTF advised that agencies were 'piloting projects in real time using the Guide' and that CEIID, in six months, would 'collect and analyse the feedback and make improvements'.[580] DTF anticipates that when the Guide is released to the public it will provide industry with information on the 'transparent & robust decision making tool used by government'.[581] The Committee is not aware of the outcome of the piloting of the Guide.

Nevertheless, in August 2010, IA published version 2 of the Western Australian Requirements section of the National PPP Guidelines. This latest version is not a detailed document and contains

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575 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.5.

576 Infrastructure Australia, *National Public Private Partnership Guidelines, Volume 6 Jurisdictional Requirements*. Available at: http://my.affinitext.com/. Accessed on 21 September 2010.

577 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.9.

578 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.9.

579 ibid., p.10.

580 Department of Treasury and Finance, *Procurement Matters. Buyers Edition*, Government of Western Australia, August 2009. Available at: http://www.dtf.wa.gov.au.

581 ibid.

several significant amendments to the earlier version. This document does not make explicit the current government's PPP policies, particularly in relation to the provision of core and ancilliary services.

Recommendation 8

The government should publish its Public Private Partnerships policies and processes to ensure their transparent and consistent application, and to improve value for money outcomes.

(b) Public Sector Comparator

According to IA, projects with a capital value in excess of $50 million have potential to provide value for money using a PPP delivery method. Therefore, $50 million is the capital expenditure threshold set by IA at which all Australian state and Territory governments should consider using a PPP.[582] This does not preclude projects with an anticipated capital value of $50 million or less from being suitable for PPP delivery provided 'they exhibit sufficient value for money drivers'.[583]

In accordance with this national policy, for projects to be considered for delivery as a PPP in Western Australia they must typically either have a value of over $50 million or be part of a bundle of projects with a combined value in excess of $50 million.[584] This is also reflected in the Memorandum of Understanding (MOU) between the state and the Commonwealth governments for the Northbridge Link project; clause 22 of the MOU states that 'where the estimated capital cost of a project is greater that $50 million … consideration of public private partnership (PPP) procurement options must be undertaken'.[585]

While IA and the Western Australian Government consider $50 million to be the PPP viability threshold, it seems that industry does not see this as being of sufficient size to justify the considerable bidding and transactions costs associated with PPP tendering. For example, the RBS suggests that:

> *a project needs to be of sufficient scale and value to achieve a really useful process for a PPP. As a rule of thumb, at least $100 million to $200 million would be where I think sufficient parties from the marketplace would be attracted in order to have a competitive process in a PPP environment. There have been PPPs done in the past that are smaller*

582 Infrastructure Australia, *National Public Private Partnership Policy Framework*, Commonwealth of Australia, Canberra, December 2008, p.6.

583 ibid.

584 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.9.

585 Submission No. 6 from Public Transport Authority, 23 March 2010, cl 22.

> *than that range, but as the processes and the resources required to bid for a PPP are substantial going forward, I think that that sort of minimum size is appropriate.*[586]

If the RBS position is representative of the industry, and there is no reason to suggest it is not, clearly there is a marked difference between what government and industry deem to be a PPP threshold value. This makes it increasingly important for government to consider ways in which projects might be bundled to increase its value and make them more attractive to industry.

For projects that meet the $50 million threshold test, a further process must be undertaken to determine whether or not the project is suitable for PPP delivery. Following positive consideration at the business case stage of the project in terms of efficiencies to be gained, public interest, potential for outsourcing services, and real opportunities for optimising risk allocation, the project is subjected to further analysis.[587] This more detailed analysis includes 'financial modelling to compare a proxy PPP contractor's model with a preliminary public sector comparer model. That is, we compare the cost of a contract to deliver a PPP privately financed, as against a publicly delivered project'.[588]

The model used is referred to as a Public Sector Comparator (PSC). A project's PSC 'identifies and quantifies the delivery requirements for the project on the assumption it will be procured as a capital works project, where the asset is designed and developed by public sector processes'.[589] It does this through examining the business case for the project based on the most efficient method of traditional or conventional procurement approaches, and must do this by taking 'into account the potential impact of risks associated with a proposal'.[590] The PSC is expressed as a project's 'net present value to government of providing the output over the life of a proposal'.[591] The feasibility of a potential PPP is then determined by comparing the net present cost of the project as determined by the PSC with that of the 'PPP bids for a range of achievable delivery models'.[592] Together with non-financial factors, these forecasts estimate the value for money achievable under each PPP option. Under the *Partnership for Growth* policy, if value for money can be demonstrated for a PPP bid when measured against the PSC, 'then private sector provision should be pursued'.[593]

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586 Mr Hugh Funder, Senior Adviser, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.6.

587 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, *Transcript of Evidence*, 18 June 2010, p.9.

588 ibid.

589 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.9.

590 ibid.; and Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.26.

591 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.26. The policy states that expressing the PSC 'in terms of net present value over the life of a proposal requires the use of a discount rate and discounted cash flow analysis'.

592 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.9.

593 Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.26.

For the integrity and robustness of each PPP option modelled, the PSC must be calculated using reliable raw data 'on best practice in public sector procurement and hands-on understanding of how the data can be accurately interpreted'.[594] The reliability of the PSC is also 'dependent upon the quality and clarity of the performance specification'.[595] It is also important that the PSC is based upon assumptions that are relevant to the project's jurisdiction, and should be 'sufficiently transparent to enable differentiation between impacts of social, environmental and economic objectives for the project'.[596]

Mr Marney sees the ability to compare the potential public and private models of a project as 'absolutely critical' and 'fundamental to the process' as:

> *ultimately you need to understand what it would cost you to run it yourself and achieve the same outcomes as you are specifying in the procurement documentation that an external must meet.*[597]

Mr Marney acknowledges this is a difficult and time consuming exercise that, when done well, 'probably adds a year to the planning process of a major project, but if you short-circuit that process then it becomes difficult to know whether or not proceeding down a PPP path is actually in the public interest'.[598]

Furthermore, while the Western Australian Government is 'keen to explore the PPP option', it is not possible to 'blanket explore PPPs for every project'.[599] According to Mr Marney:

> *on basis of the evaluation of the public sector comparator and relative to the bids from any private sector parties for whatever spectrum of service, like-for-like, if it was in the state's interest to do it in-house, then that would be the outcome. It is not a predetermined outcome.*[600]

(c) Public Private Partnerships and SAMF

Just as with any public infrastructure project, a potential PPP project must undergo project management and evaluation processes to determine whether a PPP procurement model offers the best value for money outcome. Prior to the evaluation phase, the need must be determined through concept development; the impact of the project on agency performance must be addressed through performance evaluation; and a business case must be prepared, including a financial evaluation,

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594 Australian Procurement and Construction Council, *Key Issues in Procurement through Public Private Partnerships (PPPs), A Discussion Paper*, Australian Procurement and Construction Council, np, November 2002, p.9.

595 ibid., p.10.

596 ibid.

597 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.10.

598 ibid.

599 ibid., pp.10–11.

600 ibid.

economic evaluation and social impact analysis. It is only then that an investment decision can be made and a PPP possibly determined as the most effective procurement option.[601]

However, as PPPs offer a significantly different procurement delivery model, CEIID encourages early determination of feasibility by an expert selection panel which collectively must:

- have knowledge and first-hand experience in the delivery of projects using each of the procurement delivery models under consideration; and
- understand how the assets built as part of the project will be used/operated and maintained.[602]

Early in the life of the project the expert panel can undertake a 'first pass' or 'desktop analysis' of PPP value drivers through addressing questions in relation to the following:

- Sufficient scale and long-term nature
- Complex risk profile and opportunity for risk transfer
- Whole of life costing
- Innovation
- Measurable outputs
- Asset utilisations
- Competitive process[603]

Once a project has been determined to have potential for delivery as a PPP, a more detailed procurement options analysis should be undertaken. This, in turn, is tested, and timing and sequence confirmed during the project definition phase.[604]

Given that only public infrastructure projects that cross the viability threshold of $50 million are considered as potential PPP projects, this generally places them within the jurisdiction of DTF-SP to plan and develop.

According to Mr Marney, DTF still has:

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601 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, p.3; and Department of Treasury and Finance, *Partnerships for Growth Policies and Guidelines for Public Private Partnerships in Western Australia*, Government of Western Australia, Perth, December 2002, p.11.

602 Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, Government of Western Australia, 2010, p.39. There are a number of other desirable qualities that the panel collectively should possess.

603 ibid., p.41.

604 ibid., p.6.

> *a fundamental role in assessing the cost of doing it as a PPP relative to the cost of doing it as a traditional public sector in-house, if you like, project, and informing the government of the difference between those two costs.*[605]

Where PPPs 'demonstrate[s] better value for money than traditional procurement',[606] DTF will be strongly encouraging government to use them as a form of infrastructure delivery. However:

> *if traditional procurement demonstrates stronger value for money, then we will strongly advocate that. It is not the mechanism that is critical; it is the outcome.*[607]

(d) Accounting for PPPs

The complexity of PPPs and the various models that can be pursued raises issues in relation to the treatment of PPP projects in the State's accounts and budgets. The complexity, in accounting terms, is largely because first, there are differences in the accounting treatment of social and economic infrastructure, and second, in addition to the infrastructure asset component, PPPs generally include an 'on-going service delivery' component.[608]

Accounting for PPPs 'tends to mirror this complexity'.[609] As Mr Marney noted, 'essentially, you do not incur an up-front capital cost, or you do to a much lesser extent. The ongoing operating requirement is what you fund, so you purchase a service rather than build an asset and then operate the asset'.[610] This means that accounting for a PPP can be 'pretty technical in terms of accounting standards around how much of a service you purchase as to whether it then has to be disclosed on your balance sheet or not'.[611]

When the federal government's funding contribution is in the form of an equity injection, this makes the accounting possibly more complicated as both the state and federal governments would want to show their asset on their balance sheet. There is also the issue of when the project first appears in the State's accounts, and it is possible that liabilities may not be accounted for until the first payment is made.[612]

This situation is compounded by the fact that commercial arrangements currently contained in the Australian Accounting Standards Board's (AASB's) framework are not mirrored in PPPs.

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605 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.11.

606 ibid., p.12.

607 ibid.

608 Department of Treasury and Finance, 'Accounting for Public Private Partnerships (PPPs)', Briefing Note, attached to Submission No. 29 from Department of Treasury and Finance, 30 April 2010, p.1.

609 Submission No. 29 from Department of Treasury and Finance, 30 April 2010, p.2.

610 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.9.

611 ibid.

612 ibid., p.10.

Furthermore, there is no public sector accounting standard for PPPs.[613] Instead, public sector accounting for PPPs has been informed by:

- guidance from international accounting bodies;
- reference to AASB standards for PPP-relevant concepts;
- guidance issued by the Heads of Treasuries and Reporting Advisory Committee; and
- accounting standard AASB 117 *Leases* as the most relevant for PPPs.[614]

Applying AASB 117—which categorises leases as either finance or operating leases—to PPPs means that:

> *the underlying asset and an associated liability will be recognised on the State's Balance Sheet as a finance lease where the government bears a substantial proportion of the risks and rewards of ownership.*[615]

The categorisation of a lease depends on 'the substance of the transaction rather than the form of the contract .... regardless of which party has legal title'.[616]

Social infrastructure PPPs are generally regarded under AASB 117 as being a finance lease because the State is seen as bearing most of the risk due to:

- the lease term covering the majority of the economic life of the asset;
- the present value of the lease payments representing substantially all the fair value of the asset; and
- asset ownership passing at the end of the term to the State as lessee.[617]

In relation to public sector treatment for concession arrangements—such as toll roads, car park operation—in economic infrastructure PPPs, there is currently no applicable accounting standard. DTF's briefing note advises that in these cases, 'other accounting standards are consulted (such as AASB 117) to determine the accounting treatment that reflects the underlying economic substance of the arrangement'.[618] Particular factors are considered, including:

- *transfer of revenue risk to the private party;*

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613 Department of Treasury and Finance, 'Accounting for Public Private Partnerships (PPPs)', Briefing Note, attached to: Submission No. 29 from Department of Treasury and Finance, 30 April 2010, p.1.

614 ibid.

615 ibid., p.2.

616 ibid.

617 ibid.

618 ibid., p.3.

– *concession period length; and*

– *private operator's rights and obligations.*[619]

Only in circumstances where the private party is deemed to have the majority of risks and rewards associated with ownership will the PPP not give rise to a State asset and liability and, thus, not appear on the State's balance sheet.[620]

Nevertheless, and as Mr Marney stated:

> *whether it shows up on your balance sheet should not determine your procurement process, because at the end of the day it still costs you the same amount of money, which is why the project is approved in concept, regardless of the design procurement strategy, our view is that it should be reflected immediately on the balance sheet.*[621]

(e) Current and Potential PPP Projects

As noted earlier, there is a range of PPP model options, with varying levels of complexity depending upon the outcomes required. None of the projects examined in detail by the Committee were determined by the government to be viable for delivery as a PPP. However, as well as one project that has been procured using a PPP model, namely the Perth CBD Court Complex, there are a number of projects that reportedly have potential to be delivered in the state via a PPP model. Following is a brief outline of the Perth CBD Court Complex as well as some of the potential PPP projects in Western Australia.

(i) Perth CBD Court Complex

At July 2010, the CBD Court Complex was the only contracted PPP project in Western Australia to appear on IA's pipeline list.[622] The project's preparation and preliminary work took approximately 12 to 18 months, 'from the market sounding processes right through to the evaluation of the expressions of interest relative to the public sector comparator and so on'.[623]

The project is seen by DTF and RBS, the private sponsor, as providing a good outcome through a good process.[624] Mr Ward of RBS believes that the 'quality of the infrastructure that has been provided as a result of that process is high. I do not think I can really comment on how the

619 ibid.

620 ibid.

621 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.12.

622 Infrastructure Australia, 'PPP & Infrastructure Pipeline PPP. Projects Contracted as at July 2010', Available at: http://www.infrastructureaustralia.gov.au. Accessed on 18 September 2010.

623 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.11.

624 ibid.; and Mr Robert Ward, Executive Director, Infrastructure Advisory, RBS Group (Australia) Pty Ltd, *Transcript of Evidence*, 8 September 2010, p.9.

operation is currently going, although we retain a role in that [for commercial-in-confidence reasons]. For a first PPP, I think it was a very good outcome'.[625]

This project was built on time and on budget at a time when the state had significant increases in the Building Cost Index. According to RBS, this result was achievable due to the:

> *discipline and the due diligence and the rigour of the fixed price element of the PPP process and the risk transfer of that passed to the design and construct contractor—being Multiplex—showed the benefits of the model, albeit in a difficult environment, and that a clear and well-structured project can still be done on time and on budget.*[626]

(ii) Midland Hospital

In March 2010, Western Australia's Minister for Health, Dr Kim Hames, indicated that the Midland Health Campus, valued at $360 million, would be a PPP, with the model being similar to that used at the Joondalup Hospital.[627] Building Management and Works's (BMW's) list of capital projects for the period 2010 to 2014 includes the Midland Health Campus as a '321 bed replacement of Swan District Hospital', with the principle delivery method to be either DBFO (Design, Build, Finance, Operate) or DBOM (Design, Build, Operate, Maintain).[628] In April 2010 Mr Marney advised that 'the government is keen to explore the PPP option' for this hospital and has articulated this to the Under Treasurer.[629] Mr Marney stated that a PPP has not been predetermined, with the decision to be made following project evaluation. BMW expect the tender to go to market in the last quarter of 2010 and the contract to be awarded in the first quarter of 2012.[630]

The Midland Hospital project is complicated by the fact that the federal government will be providing funding equal to the State's contribution. State Cabinet has approved a PPP model for the hospital, and Dr Hames has said he has 'received confirmation from the federal government to proceed down that path'.[631]

Mr Marney further advised that the federal funding complicated matters, particularly in relation to asset ownership and representation on balance sheets. He believes that 'it is fair to say we [DTF] have a lot of work to do in both those cases [Midland and Princess Margaret Hospitals] to actually

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625 ibid.

626 ibid.

627 Lawson, Rebecca, 'PPP Confirmed for New Midland Hospital', in *WA Business News*, 17 March 2010, p.1.

628 Building Management and Works, Department of Treasury and Finance, *Capital Projects >$10m for 2010 to 2014*, Government of Western Australia, Perth, 2010, p.4.

629 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.10 and p.11.

630 Building Management and Works, Department of Treasury and Finance, *Capital Projects >$10m for 2010 to 2014*, Government of Western Australia, Perth, 2010, p.4.

631 Lawson, Rebecca, 'PPP Confirmed for new Midland Hospital', in *WA Business News*, 17 March 2010, p.1.

evaluate the best procurement and operational models for those facilities'.[632] Mr Marney stated that 'it will be what is best in terms of whole-of-life cost and value for money that drives the recommendations around the way to go, as opposed to what the accounting treatment might be at the end of the day on those'.[633]

On 2 June 2010 Dr Hames advised the Legislative Assembly that the government has:

> *asked for expressions of interest for a build–own–operate model that includes the potential for funding. There are two ways funding can occur. The first involves the private sector putting up the funds. The commonwealth has agreed that its funds could be used a part of the pay-off of the capital cost of the hospital. That is not looking the most promising at present. More than likely the state and federal money will be put in for the capital construction of the hospital. It will be a design–build–operate–maintain model.*[634]

On 6 October 2010. Dr Hames announced that the government expressions of interest were being sought for the new Midland Health Campus and that proposals from private hospital operators would be to design, build and operate the new hospital.[635]

The application of the term PPP to describe this project is inconsistent with the definition contained in the 2002 Guidelines which states that core service delivery remains with government under PPP procurement.

(iii) Mundaring Weir Water Treatment Plant

The Mundaring Weir Water Treatment Plant is one of two PPP projects in Western Australia in the market as at July 2010.[636] On 17 June 2010 the Water Corporation announced the two short-listed consortia for the Request for Proposals (RFP) phase of the project:

- Helena Water, comprising project sponsors Acciona Agua, United Utilities Australia and Royal Bank of Scotland; with design support by GHD; and
- Aquality, comprising project sponsors Commonwealth Bank of Australia, Degremont Australia Ltd, Abigroup and McConnell Dowell; and design support by Worley Parsons and KBR.

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632 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.10. The new Princess Margaret Hospital was originally earmarked as a PPP. However, in June 2010 the government advised that BHP Billiton and Rio Tinto would make a joint one-off payment of $350 million to the government and that this has been allocated to the new children's hospital. See: Hon. Dr Kim Hames, MLA, *Minister for Health, Ministerial Media Statements. New Funds will Help Build WA's New Children's Hospital*. Available at: http://www.mediastatements.wa.gov.au. Accessed on 22 September 2010.

633 Mr Tim Marney, Under Treasurer, Department of Treasury and Finance, *Transcript of Evidence*, 1 April 2010, p.10.

634 Hon. Dr Kim Hames, Minister for Health, Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 2 June 2010, p.218.

635 Hon. Dr Kim Hames, (Minister for Health), *Expressions of Interest called for Delivery of Midland Health Campus*, Media Statement, Perth, 6 October 2010.

636 Infrastructure Australia, 'Potential Projects as at September 2010'. Available at: http://www.infrastructureaustralia.gov.au. Accessed on 18 September 2010. The other project is the QEII Medical Centre Multi-Storey carparks project.

According to the Water Corporation, the RFP process was due to commence in July 2010, submissions due in December 2010 and contract award scheduled for July 2011.[637]

(iv) QEII Medical Centre Multi-Storey Car Parks

According to the Department of Health, the government has 'advertised for EOI from private companies to build, finance and operate two multi-storey car parks at QEII Medical Centre' on a long-term contract that covers all parking at the medical centre site, 'including the existing ground level car parks'.[638] In June 2010 Dr Hames confirmed that the state government had advertised for EOI for a PPP partner for the new car parks.[639] Following the expiry of the long-term contract, all QEII car parks will be transferred to the ownership of the QEII Medical Centre Trust. IA's list of potential PPP projects currently in the market notes that EOIs were expected to be submitted in June 2010, with contractual close expected for early 2011.[640] At a CEIID function, Mr Mann advised that the new multi-level car parking project at QEII Medical Centre has a total estimated cost of $150 million.[641]

It is unclear if strong local community protest has affected the decision-making for this project.

(v) Eastern Goldfields Prison Development

As per the IA list of potential PPP projects as at September 2010, Midland Health Campus and Eastern Goldfields Prison Redevelopment were expected to be released to the market in the next 12 months.[642] This project does not appear on the list of DSD submissions to IA in November

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637 Water Corporation, 'Mundaring Water Treatment Plant Public Private Partnership', nd. Available at: http://www.watercorporation.com.au/. Accessed on 18 September 2010.

638 North Metropolitan Area Health Service, Department of Health, 'Call for private interest in building multi-storey car parks at QEII Medical Centre', nd. Available at: http://www.nmahs.health.wa.gov.au. Accessed on 18 September 2010.

639 Hon. Dr Kim Hames, MLA, (Minister for Health), Ministerial Media Statement, 2 June, 2010.

640 Infrastructure Australia, 'Potential Projects as at September 2010'. Available at: http://www. infrastructureaustralia.gov.au. Accessed on 18 September 2010.

641 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, Procurement Strategy for Delivery of WA Government Major Projects', presentation to CEIID, 21 July 2010.

642 Infrastructure Australia, 'PPP & Infrastructure Project Pipeline, Potential Projects as at September 2010', nd. Available at: http://www.infrastructureaustralia.gov.au. Accessed on 18 September 2010.

2009 provided by the Department of Premier and Cabinet (DPC) in their submission to the Inquiry but is described as a 'new 350 bed mixed security men's and women's prison'.[643] In July 2010, Mr Mann noted that the 350 bed prison has a total estimated cost of $232 million, and the Eastern Goldfields Prison Development's principal delivery method will be a DBFM, or Design, Build, Finance and Maintain, model, with the tender going to market by the end of the first quarter of 2011 and the contract scheduled to be awarded in the first quarter of 2012.[644]

643 Building Management and Works, Department of Treasury and Finance, *Capital Projects >$10m for 2010 to 2014*, Government of Western Australia, Perth, 2010, p.4.

644 Mr Richard Mann, Executive Director, Strategic Projects, Department of Treasury and Finance, Procurement Strategy for Delivery of WA Government Major Projects', presentation to CEIID, 21 July 2010.

CHAPTER 9 OTHER ISSUES

9.1 Reducing and Identifying Project Risks

(a) The Nature of Risk

Throughout the report one of the key themes to emerge has been risk. Risk is 'the uncertainty of outcomes, either positive or negative'.[645] The Department of Treasury and Finance (DTF) has published a guide for risk management entitled, *Risk Assessment and Management: Managing Risks in Contracting*, which outlines a range of risks that may be encountered by government agencies in the delivery of a project or service. Although the publication relates to risks associated with government contracting in general, it has application to the delivery of physical infrastructure, and the categories of risk identified are worth summarising here:

- Planning, preparation and processes – including situations where time and cost targets are not met, delays in approvals are encountered or the procurement method was not appropriate for the project.[646]

- The nature of the product or service – including where the final product or service does not meet expectations or produce the desired outcomes, or technologies associated with the project either fail or become quickly obsolete.[647]

- The environment in which the product or service is to be delivered – including restrictions due to the location of the product or service, delays or damage due to natural events, or restrictions or delays due to planning and zoning requirements.[648]

- Industry – including the possibility of overheated market conditions when the tender is put to the market; too few tender respondents, either through lack of interest or ability in the market; industrial unrest or failures of contractors.[649]

- Stakeholders – including changes in government policy, resistance from community or pressure groups, and adverse media reactions.[650]

- Project Management – including situations where the contract is poorly managed, inexperienced or incapable project teams are appointed or where there is conflict between team members.[651]

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645 Department of Treasury and Finance, *Partnerships for Growth: Policies and Guidelines for Public Private Partnerships in Western Australia*, December 2002, p.22.

646 Department of Treasury and Finance, *Risk Assessment and Management: Managing Risks in Contracting*, August 2010, p.40.

647 ibid., p.42.

648 ibid., p.43.

649 ibid., p.44.

650 ibid., p.46.

651 ibid., p.47.

During the course of the Inquiry, the Committee was made aware of many of the risks outlined above, although broadly speaking, in terms of the projects examined, these could be categorised as having either a negative financial outcome arising from cost over-runs during the construction phase—construction risk; or as having a negative financial outcome arising from incorrect assumptions about the underlying need for the project—demand risk. In both cases, it can be said that adverse outcomes as a result of poor risk management are likely to impact negatively on the value for money outcome achieved by the State. The proper management of risk, therefore, is central to the attainment of value for money. In this light, it can be seen that the processes detailed in the Strategic Asset Management Framework (SAMF)—and the proper selection of an appropriate delivery mechanism (including the consideration of Public Private Partnerships (PPPs))—are intended to reduce risks and maximise the likelihood of achieving value for money.

(b) Demand Risks

Earlier chapters of this report have provided some detail on SAMF's emphasis on identifying the underlying need for the construction of a new piece of infrastructure. If the need for the project is not properly identified there is a risk that, upon completion, the project will:

- be under-utilised due to insufficient demand from targeted sectors; or
- not match the requirements of the targeted sectors and also result in under-utilisation.

In Chapter 2 the Committee provided the example of the Australian Marine Complex (AMC) which was developed after the government identified the need to promote local sourcing of engineering and fabrication for the resources sector and Defence industries. The Committee was informed by the Department of Commerce (DoC) that the initial plans taken to industry were considered too ambitious, and that there was a danger that the original scope of the proposal would exceed demand from industry. [652]

Similarly, Western Power informed the Committee that the Southwest Bulk Transmission Line Reinforcement Project has been delayed following changes to the electricity generator demand forecasts underpinning the need for the project. Western Power noted that should the project proceed prior to confirmation of new electricity generator demand, there was a risk that an investment in new transmission capacity would be under-utilised.[653] There are benefits, however, to proceeding with elements of the project ahead of the establishment of new demand. In particular, Western Power notes that the construction of new transmission lines requires long lead times due to environment and land access approvals.[654] The risks of proceeding with the project early need to be assessed against the likelihood of realising the benefits from doing so. Western Power does this by considering different generator demand scenarios in order to assess optimal cost outcomes.[655]

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652 Mr Ross Holt, Chief Executive Officer, LandCorp, *Transcript of Evidence*, 23 June 2010, p.9.

653 Closed Submission No. 11 from Western Power, 19 April 2010, p.3.

654 ibid.

655 ibid.

By failing to fully identify the need for projects, proponents are denied the opportunity to mitigate against any demand-related risks that might be identified during the assessment process. To some extent this danger is unavoidable when considering projects that, in this report, have been termed 'political imperatives'. These projects are often committed to before the SAMF process has been used to critically evaluate need. The Bunbury to Albany Gas Pipeline is one such case, and when asked if a projection of minimum market demand would be required to allow for the project to go ahead, Ms Gail McGowan, Deputy Director General, Department of State Development (DSD) stated:

> *we have not done the work on that at this stage, as we would ordinarily do in any benefit analysis. We would expect to undertake some of that work and put minimum thresholds. Ultimately, the basis for proceeding will be a policy decision for government.*[656]

If the basis for proceeding with the Bunbury to Albany Gas Pipeline is a political decision, then the government increases the demand risk it is exposing itself to on the basis that demand has not been adequately identified.

(c) Construction Risks

As discussed in Chapter 6, many contract types are chosen in response to the unique challenges posed by the risks associated with each project. For example, Main Roads Western Australia (MRWA) selected an alliance style contract when delivering the New Perth to Bunbury Highway (NPBH) due to the significant risks associated with the project's delivery schedule.[657] A managing contractor model was deemed appropriate for the Fiona Stanley Hospital (FSH) project due to risk posed by scope changes through the early development phase of the hospital.

In an ideal world, projects would not commence unless they had already been subject to the rigorous application of the processes outlined in SAMF. If projects undergo these processes, the likelihood of scope changes once construction has commenced will decrease. This, in turn, will decrease construction risks, particularly the risk of cost escalation as a result of scope creep. That being said, many projects do not always undergo the processes required in SAMF, which can lead to the suboptimal outcomes detailed in earlier sections of the report. In these circumstances, where projects have not been developed through SAMF, the selection of the right contracting method may be one mechanism for mitigating government exposure to the risks associated with the projects.

Table 9.1 below provides an overview of the risk allocation for the various contract types examined by the Committee and provides a simplified break-down of risk allocation and responsibilities between clients and contractors. The table does not allow for the variations that can occur within individual contract types. Nevertheless, it presents a useful overview of the risk allocation for the general contract types. Segments of the table coloured blue indicate risks residing with the contractor, while yellow segments denote risk retained by the client, that is, the

656 Ms Gail McGowan, Deputy Director General, State Initiatives, Department of State Development, *Transcript of Evidence*, 16 June 2010, p.4.

657 Submission No. 2 from Main Roads Western Australia, 15 January 2010, p.14.

government. The table demonstrates that most contracting types result in a distribution of construction related risk types between clients and contractors. The two extremes are represented in the table by PPPs at the ‘least-risk exposure’ end and direct management of projects at the ‘greatest risk exposure’ end.

Some possible risks encountered during the construction phase are outside the control of the government, including delivering the project in an ‘overheated’ construction market or the occurrence of natural disasters. Although there is little that government can do to minimise the risk of these events, if mitigating steps are taken in relation to the risks the government can control, the overall risk profile for the project is reduced.

Table 9.1: Risk Allocation and Contracting Type

Procurement delivery models listed by risk allocation	Predominant Payment Method					Main Decision Maker				
	Concept	Design	Construct	Maintain	Operate	Concept	Design	Construct	Maintain	Operate
Public Private Partnership	FIXED	FIXED	FIXED	FIXED	FIXED	CONTRACTOR	CONTRACTOR	CONTRACTOR	CONTRACTOR	CONTRACTOR
Design & Construct	ACTUAL	FIXED	FIXED	ACTUAL	ACTUAL	CLIENT	CONTRACTOR	CONTRACTOR	CLIENT	CLIENT
Early Contractor Involvement	ACTUAL	FIXED	FIXED	ACTUAL	ACTUAL	SHARED	CONTRACTOR	CONTRACTOR	CLIENT	CLIENT
Managing Contractor	ACTUAL	FIXED	ACTUAL	ACTUAL	ACTUAL	CLIENT	CONTRACTOR	CONTRACTOR	CLIENT	CLIENT
Construct Only	ACTUAL	ACTUAL	FIXED	ACTUAL	ACTUAL	CLIENT	CLIENT	CONTRACTOR	CLIENT	CLIENT
Alliancing	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	CLIENT	SHARED	SHARED	CLIENT	CLIENT
Direct Management	ACTUAL	ACTUAL	ACTUAL	ACTUAL	ACTUAL	CLIENT	CLIENT	CLIENT	CLIENT	CLIENT

Adapted from: Centre for Excellence and Innovation in Infrastructure Delivery, *Infrastructure Procurement Options Guide*, 2009, p.15.

Finding 25

The selection of an appropriate project delivery contract can minimise the level of the State's risk exposure during the construction stages of a project. Many of the possible risks encountered during the delivery stage can be reduced if projects only proceed once they have been fully scoped, thus reducing the risk of costly scope and design changes following the commencement of construction.

(d) Risk Management

Treasurer's Instruction 825 defines risk management as:

> *the culture, processes and structures that are directed towards the effective management of potential opportunities and adverse effects. It is designed to protect the agency, the whole of government and the general community from unnecessary costs and losses.*[658]

The Instruction requires agencies to ensure that:

> *i) there are procedures in place for the periodic assessment, identification, and treatment of risks inherent in the operations of the agency;*
>
> *ii) suitable risk management policies and practices are developed;*
>
> *iii) an appropriate level of security is maintained over money, public and other property of or under control of the agency, including information held and intellectual property developed and controlled by the agency; and*
>
> *iv) these procedures, policies and practices are documented in the financial management manual or other relevant policy manuals.*[659]

Compliance with this instruction can be achieved through the preparation of a risk management plan, which requires agencies to conduct several reviews, including identifying project risks in a structured way and outlining appropriate steps to address the likelihood of this occurring.[660] There are a number of ways in which project risks can be categorised and this will usually depend on the nature and complexity of the project.[661] DSD devised the following risk categories for its Oakajee Port and Rail risk register:

658 Department of Treasury and Finance, *Treasurer's Instruction 825*, October 2007, p.1.

659 ibid., p.2.

660 Department of Treasury and Finance, *Risk Assessment and Management: Managing Risks in Contracting*, August 2010, p.20.

661 ibid., p.24.

- Operational/planning;
- Financial;
- Economic;
- Legal/legislative;
- Timing;
- Political; and
- Engineering;
- Governance.[662]

Agencies must also quantify the risks using subjective assessments of both the likelihood of an occurrence and its consequences. Tables 9.2 and 9.3 below are adapted from DTF's *Risk Assessment and Management: Managing Risks in Contracting*, and outline the methodology used to obtain both likelihood ratings and consequence ratings:

Table 9.2: Likelihood Ratings[663]

Descriptor	Definition
Almost Certain	Extremely high probability of occurring, or likely to occur frequently (several times per year) during the contract
Likely	High probability of occurring, or likely to occur several times (once per year) during the contract
Moderate	Moderate probability of occurring, or likely to occur (once) during the contract
Unlikely	Low probability of occurring during the contract (once in one hundred years)
Rare	Extremely low probability of occurring during the contract (once in one thousand years)

Table 9.3: Consequence Ratings[664]

Objective				
Descriptor	**Time**	**Cost**	**Quality**	**Others**
Catastrophic	Cancellation of the contract	Cancellation of the contract	Product or service can't be used	Insert appropriate wording depending on the nature of the objective
Major	Significant time overruns	Significant cost overruns	Significant modifications required to make product/service useable	
Moderate	Some time overruns	Some cost overruns	Some modifications required to make product or service useable	
Minor	Some inconvenience	Some inconvenience	Some inconvenience	
Insignificant	No noticeable effect	No noticeable effect	No noticeable effect	

662 Closed Submission No. 32 from the Department of State Development, 3 September 2010.

663 Department of Treasury and Finance, *Risk Assessment and Management: Managing Risks in Contracting*, August 2010, p.26.

664 ibid.

Once risks have been quantified they must then be prioritised to ensure that the most urgent risks are dealt with first. DTF's *Risk Assessment and Management: Managing Risks in Contracting* suggests rating the specific risks depending on the combined ratings of the likelihood and consequence.[665] This can be done through the use of a risk prioritisation matrix, which is reproduced in Table 9.4 below:

Table 9.4: Risk Prioritisation Matrix

Risk Prioritisation Matrix					
Likelihood	**Insignificant (1)**	**Minor (2)**	**Moderate (3)**	**Major (4)**	**Catastrophic (5)**
Almost certain (5)	Moderate	Significant	High	High	High
Likely (4)	Moderate	Significant	High	High	High
Moderate (3)	Low	Moderate	Significant	High	High
Unlikely (2)	Low	Low	Moderate	Significant	Significant
Rare (1)	Low	Low	Moderate	Significant	Significant

Following the prioritisation process, agencies are required to 'treat' or control the risks by taking action to:

- reduce the likelihood of the risk occurring;
- reduce the consequences of the risk should it occur;
- transfer or share the risk with another party;
- accept the risk if the likelihood and consequence are both low; and
- avoid the risk—by ceasing the activity—if the risk is unmanageable or too costly to manage.

Finally, agencies are required to develop an action plan that provides detail of the risks, their likelihood and consequences, overall risk rating and the steps that should be taken to address them.

9.2 The Importance of Project Pipelines

One issue that emerged during the Committee's discussions with private sector infrastructure providers and financiers was the importance of 'project pipelines', which are understood to be

665 ibid., p.27.

publicly available plans outlining the government's upcoming infrastructure projects. These plans may include the projects' estimated costs and likely procurement methodologies. Infrastructure Australia (IA) has established a pipeline which provides contractors with an overview of the national PPP infrastructure market, including potential projects, those already in the market and those already contracted.

In its submission, Leighton Holdings addressed the importance of having access to information about planned government infrastructure projects, expressing particular concern about the uncertainty surrounding upcoming projects:

> *Uncertainty stems from not having enough information available about upcoming projects, or abrupt changes.*[666]

Mr Chris Palandri of Brookfield Multiplex expressed similar sentiments when he noted the following:

> *In the middle of boom times in Western Australia, before the GFC I guess, there were issues around supply and subcontractors and delivery of projects, so having a pipeline of projects out that is somewhat regulated and having as much notice as we can around that pipeline gives the industry as a whole the opportunity to prepare itself.*[667]

Mr Palandri also outlined the importance of certainty for contractors and the role it plays in allowing contractors to send resources to locations where they are needed:

> *But certainty is probably the most important thing, because the industry will react to whatever the opportunities are. I think you will find that the workforce is somewhat mobile. It is not ultimately 100 per cent mobile. But the workforce will move in some respects to where the work is. You will find that, from our national business point of view, there is more work in Western Australia at the moment than there is in New South Wales. So we have a lot of people from New South Wales working on our projects in Western Australia. We have a lot of subcontractors, and we have a lot of supervisory staff and the like, working on our projects. So certainty of time frame and certainty of projects, and the sort of presentation that Richard [Mann of DTF-SP] did, really gives the opportunity to the industry to prepare for upcoming opportunities. In that regard, I think certainty is probably more important than having a steady flow, because when the certainty is there, people can build their businesses around what the opportunities are.*[668]

Project sponsors in the PPP market share similar sentiments to those expressed above. The Royal Bank of Scotland (RBS) is a leading infrastructure project sponsor which has delivered over 25 projects in Australia and New Zealand.[669] Its representatives advised the Committee that:

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666 Submission No. 33 from Leighton Holdings, 13 August 2010, p.3.

667 Mr Chris Palandri, Regional Managing Director, Brookfield Multiplex, *Transcript of Evidence*, 18 August 2010, p.7.

668 ibid.

669 Royal Bank of Scotland, 'RBS - Infrastructure Advisory & PPPs'. Available at: http://www.rbs.com.au/default.aspx?page=17. Accessed on 29 September 2010.

> *for [RBS] to be active in a jurisdiction in PPPs […] it is about having a pipeline, or a prospect of repeated transactions, sufficient to attract bidders. It is about having sufficient scale on those projects and having a delivery capacity, and we have seen those things over the past 18 months in, we think, an appropriate structure and manner.*[670]

Both Leighton Holdings and Brookfield Multiplex also noted the confusion in relation to the delivery of projects in Western Australia through the use of PPPs. These companies cited the procurement of the new children's hospital as one project that had created considerable confusion for industry.[671] This situation arose as the hospital was originally:

> *promoted as a future Public Private Partnership (PPP), but was changed with little notice to a design construct and maintain (DCM) procurement model without engagement with the industry, causing confusion, frustration and uncertainty for stakeholders.*[672]

Leighton Holdings also reported that 'the schools PPP was talked about for a long time, but there has been little movement'.[673] This situation does not allow industry to develop confidence in the continuity of both the supply and procurement methodology of infrastructure projects in Western Australia.

The previous government had commenced development of a State Infrastructure Strategy in late 2005. The Strategy aimed to:

- *engage the wider community and all tiers of government to identify existing and emerging infrastructure pressures throughout WA;*
- *prioritise infrastructure requirements to provide greater certainty for private investors;*
- *outline a plan for delivering major projects to allow for better-informed decisions in both the public and private sectors;*
- *encourage the Commonwealth and local government to take responsibility for their fair share of infrastructure provision; and*
- *ensure proposals for future investment are affordable and based on an appropriate mix of skills from both the public and private sectors.*[674]

The final report on this infrastructure strategy was delivered to the government in June 2008, which was shortly before the calling of the state election.[675] To date, while the current government

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670 Mr Robert Ward, Executive Director, Infrastructure Advisory, Royal Bank of Scotland, *Transcript of Evidence*, 8 September 2010, p.8.

671 Submission No. 33 from Leighton Holdings, 13 August 2010, p.3; and Mr Chris Palandri, Regional Managing Director, Brookfield Multiplex, *Transcript of Evidence*, 18 August 2010, p.3.

672 Submission No. 33 from Leighton Holdings, 13 August 2010, p.3.

673 ibid.

674 Hon. Dr Geoffrey Gallop, MLA, (then Premier of Western Australia), *State Infrastructure Strategy to Drive Jobs and Investment Growth*, Media Statement, Perth, 29 October 2005.

675 Beyer, Mark, 'State Infrastructure Strategy Finalised', *WA Business News*, 26 June 2008, p.3.

has committed to its Works Reform Program, it does not appear to have made any announcements on the implementation of the *State Infrastructure Strategy*.

There are important issues that arise from the industry evidence quoted above. First, and perhaps most importantly, is the value that private sector participants in infrastructure delivery place on the certainty of the supply of future projects. Secondly, RBS clearly identifies its preference to bid on a project in a jurisdiction where there is an ongoing market for PPPs, rather than projects proceeding on an intermittent supply basis. This probably relates to the expenses associated with bidding for a PPP, an issue examined in Chapter 8.

The Centre for Excellence and Innovation in Infrastructure Delivery (CEIID) organises regular briefings for industry representatives during which public sector agencies—including Government Trading Enterprises (GTEs)—provide information on planned infrastructure projects. The most recent took place in late July 2010 and was described as providing very useful information to industry participants.[676]

CEIID's industry presentations fulfil a key aspect of keeping industry advised of the state government's infrastructure investment plans. There are several advantages that may arise from the publication of project pipelines, including:

- an increase in the number of construction market participants in Western Australia, and, therefore, an increasingly competitive tendering market for major projects.
- lower costs for projects arising from contractors' ability to better plan for major projects and manage their resources appropriately.

Finding 26

Industry welcomes the Centre for Excellence and Innovation in Infrastructure Delivery briefings outlining proposed infrastructure projects as this assists potential bidders to prepare for upcoming opportunities.

While CEIID's industry briefings are clearly beneficial to all participants, the development of the state's infrastructure would be further enhanced by the creation, maintenance and regular publication of a 10-year Government Sector Infrastructure Plan that details all medium to large infrastructure projects being considered. The information necessary to develop this Plan is currently provided to DTF by agencies in the form of their Strategic Asset Plans (SAPs). The development of the Plan would require the collation and assessment of this information so that, ultimately, it provides to both industry and government accurate indications of the stages of development of each project. It also needs to provide information on the projects' readiness to proceed, possibly through the use of a classification system similar to that used by Infrastructure Australia (IA). The benefits to be gained from the Plan would be increased if GTEs were required

676 Mr Chris Palandri, Regional Managing Director, Brookfield Multiplex, *Transcript of Evidence*, 18 August 2010, p.2.

to provide information on their potential projects. Once developed, the Plan would need government approval prior to its publication and, in effect, would become the state's infrastructure pipeline.

Recommendation 9

The government should develop, maintain and publish a Government Sector Infrastructure Plan that details all medium to large infrastructure projects being considered, and provides an assessment of each project's stage of development.

9.3 Post-project Assessment

Throughout this report, the importance of value for money in relation to the delivery of new infrastructure assets has been emphasised. Until now, the emphasis has been on achieving value for money during the project development, evaluation and delivery stages. The effectiveness of these measures can only really be assessed once the project has been successfully delivered and is in operation. There are a number of measures of value for money against which a project can be assessed once it is in operation, although it is noted that most often, political and media attention is focussed on the extent of cost and time blow-outs, rather than the extent to which the project meets the objectives on which construction has been justified.

Post-implementation reviews are included in SAMF, and require agencies to determine the extent to which the project is meeting its aims, examine cost variations (including instances where operational costs are not consistent with the originally planned costs) and identify value opportunities for implementation on future projects.[677] Evidence suggests that the post-project evaluations tend not to be carried out or, if they are carried out, tend to not be done particularly well.[678] This was for a number of reasons, including the over-reliance by government on project management contractors, who tend to depart a project once it has been delivered, taking project knowledge with them.[679]

DTF's Gateway Review Process includes a 'gate' specifically dedicated to the provision of what it describes as a 'benefits analysis', which is undertaken in order to:

- *Assess whether the business case justification for the project is still realistic*
- *Confirm there is still a business need for the investment*
- *Assess whether the benefits anticipated at this stage are actually being delivered*

677 Department of Treasury and Finance, *Capital Investment Policy for Project Proposals*, August 2005, p.18.

678 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

679 ibid.

- *Assess the effectiveness of the ongoing contract management processes*
- *Confirm the client-side continues to have the necessary resources to manage the contract successfully*
- *Confirm continuity of key personnel involved in contract management role/s*
- *Where changes have been agreed, check they do not compromise the original delivery strategy*
- *Assess the ongoing requirement for the contract to meet the business need. Ensure that if circumstances have changed, the service delivery and the contract are adapting to the new situation*
- *Check there is ongoing contract development to improve value for money*
- *Confirm there are plans to manage the contract to its conclusion*
- *Confirm the validity of the exit strategy and arrangements for re-tendering/new tender*
- *Assess lessons learned and communication of these lessons to others.*[680]

The number of issues identified for review in the Gateway Process indicates the extent of the lessons that can be learned from examining completed projects. It is not clear, however, what is done with the information once it has been collected and reviewed. Nor is it clear if the results of the reviews are reported to a responsible authority. Given that the application of post-project reviews has been sporadic in the past, it is to be hoped that their proper application in future will assist agencies in improving the quality of the asset acquisition process, although this outcome may depend on the manner in which the information is used once it has been collected.

Recommendation 10

The Strategic Asset Management Framework requirement for a post-project assessment should be universally applied and involve an independent party.

9.4 Staffing Challenges

Among the key problems Works Reform is intended to address are:

- *poor strategic asset planning across government;*

[680] Department of Treasury and Finance, *Gateway Benefits Evaluation*, Government of Western Australia, Perth, p.9.

- *poor business case development for capital investment; [and]*
- *loss of project management skills and experience within government.*[681]

As discussed throughout this report, SAMF is an integral element of Works Reform, with the framework currently being reviewed, and improved agency compliance with SAMF being the foundation of the reforms undertaken.[682] It is generally understood that SAMF provides a robust infrastructure delivery framework, but that agency compliance has been low.

Each stage of the SAMF process requires appropriately experienced staff with a requisite skill mix. Writing on PPP projects, Roger Black of Deloitte Corporate Finance cites a lack of internal capacity as a reason for poor project outcomes. While some tasks can be outsourced, others cannot, 'and often the agency does not have the skill sets internally to manage complex PPPs or the dedicated team required to address the time intensive upfront structuring needs'.[683] It is also reasonable to suggest that it is likely that one reason for high non-compliance with SAMF is that agencies do not have staff with the necessary skill sets to allow them to complete the processes as effectively and fully as required by the framework. This is not a criticism of the agencies as the delivery of core non-building services is their primary focus.

Agency staffing issues were also compounded by staff shortages in times of high wages growth in the private sector. This necessarily impacts on the level of experience within the public sector. In discussing the day-to-day expertise of agency staff, Mr Peter Conran, Director General, Department of the Premier and Cabinet, confirmed that:

> *one of the problems that Western Australia has—it is a consequence of the boom as well—is that it lost a lot of good people because they got snapped up there. One of the things that I think is missing, in part—although with some exceptions—is really strong policy experience. I think that is one of the focuses of the Premier, who wants to rebuild that capacity. I certainly want to do that and I think everyone wants to do that because we need it, especially at this time. It is a bit tough.*[684]

This Inquiry has drawn attention to the positioning of the Building Management and Works (BMW) function within DTF, and the further delineation of that function into BMW and Strategic Projects (DTF-SP). The referral of projects to BMW (or DTF-SP if the Under Treasurer so directs) is no longer optional for agencies. The two DTF business units are delivery focused and work with agencies to articulate and draft business cases for proposed assets. Prior to this, some agencies tried to work through the entire process themselves, without the requisite skills to apply the SAMF or manage projects well.

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681 Department of Treasury and Finance, *Works Reform Business Solution Plan*, Government of Western Australia, Perth, June 2009, p.6.

682 ibid., p.13.

683 Black, Roger, *PPPs and the Water Sector. Plugging the Infrastructure Hole*, Deloitte Corporate Finance, Infrastructure and Project Finance, March 2009, p.9.

684 Mr Peter Conran, Director General, Department of the Premier and Cabinet, *Transcript of Evidence*, 23 March 2009, p.4.

The division of labour resulting from Works Reform allows for the development of staff with specialist project planning and management skills. However, DTF recognises the difficulties associated with attracting and retaining skilled staff, and has a number of responses to the challenges posed. First, DTF can redeploy skilled staff from other agencies to their works business units and/or provide suitable professional development opportunities. Second, DTF can attract expertise from the private sector. However, for either of these strategies to be effective, it will be necessary for salaries and conditions to be competitive with those on offer in the private sector.

Recently, DTF has received approval from the Public Sector Commission to recruit 12 new project directors at senior public service levels, including Level 9, Class 1 and above. The annual salary for a Level 9 position currently ranges from $124,000 to $133,000; the salary for a Class 1 public servant is $141,000 per annum.[685]

685 Western Australian Industrial Relations Commission, Public Service General Agreement 2008 No PSAAG 10 of 2008, Schedule 2 General Division Salaries.

CHAPTER 10 CONCLUSION

10.1 Risk and Political Imperatives

The Strategic Asset Management Framework (SAMF) should be seen as a series of policies intended to reduce risks and maximise the likelihood of achieving value for money. It does this by requiring agencies to plan in response to clearly identified need, and to then implement an infrastructure project using a rigorous, staged analysis of the best options for both the form of the project and the manner in which it is delivered.

Governments are required to respond to a wide range of demands and community expectations. Often commitments are made on infrastructure projects that have not progressed through the detailed processes required in SAMF. Such commitments may be made due to unforseen circumstances creating a change in service delivery needs or decision-making driven by purely political imperatives. Risks associated with commitments arising from unforseen circumstances can be avoided if agencies implement proper planning procedures.

In relation to the risks arising from political decision-making, the nature of politics means that from time to time political leaders will give commitments to projects on the basis of their popularity, even if a more thorough analysis may show that the project is hard to justify as a value for money project. The proposed $2 billion water canal from the Kimberley to Perth was a commitment during the 2005 election campaign made without preliminary planning analysis by government. A study conducted by Professor Reg Appleyard concluded the project would cost at least $14.5 billion[686] and had a high risk profile. The commitment to building a new sealed road from Tom Price to Karratha was a commitment made in the 2001 election with a cost of $100 million.[687] Two of the four stages of the road have been completed at a cost of approximately $180 million.

Projects that arise as a result of political imperatives and which have not been subjected to SAMF processes increase the risk that projects will be developed without giving proper consideration to the:

- service delivery need underpinning the demand for the new asset;
- other solutions, including non-asset solutions;
- scope of the work to be undertaken;
- procurement model; and, therefore,
- funding implications.

686 Hon. Alan Carpenter, MLA, (then Premier of Western Australia), *WA Premier Rules Out Kimberley Water Canal*, Media Statement, ABC News, 2 May 2006.

687 Hon. Dr Sally Talbot, MLC, Western Australia, Legislative Council, *Parliamentary Debates* (Hansard), 25 June 2008, p.4348.

These issues were broadly categorised in Chapter 9 as either demand or construction risks. Projects developed in response to political imperatives necessarily increase the State's exposure to these risks as they limit the application of the asset planning and the concept development and evaluation stages of SAMF.

One way to reduce the risks associated with political imperatives is through the development of a publicly available infrastructure project pipeline. This will afford the government of the day the opportunity to make project announcements drawn from a pipeline of projects that have a clearly identified need and, in some instances, have progressed through to further stages of SAMF. The public availability of the pipeline of projects would also assist other parties at election time to promise projects with real and identifiable benefits.

However, even in situations where SAMF is rigorously complied with by agencies, there will be occasions when, for reasons of state development or the development of a new specific industry, commitments will be made to major infrastructure projects. Such circumstances necessarily involve a high level of risk for government. For example, when the government committed to the CY O'Connor water pipeline to the goldfields, it was judged that the State should take on significant risk to supply water to an arid part of the state where gold mining was driving the state's economic development. Similarly, the 1970s commitment to underpin the Woodside gas development building a pipeline and contracting to buy gas for the metropolitan area placed the State at considerable risk. More recent commitments of this type include the Australian Marine Complex, which was intended to secure a developing industry, and the Oakajee Common Use Infrastructure, which aims to provide port facilities that would support the development of diversified value-adding industry in the Mid-West. These state development projects are high-risk projects, with risks including high reliance on strong commodity prices, anticipated industry development not being realised or not being sufficiently advanced to justify the project, expected demand not eventuating and construction risks associated with unproven technology.

In light of the risk attached to these types of projects, it is incumbent on the government to ensure, to the greatest extent possible, that they are subject to full risk assessment and that plans are implemented following SAMF processes in order to mitigate risks as far as possible.

There is generally an expectation that political decision-making will lead to governments embarking on projects for the benefit of the state. However, rather than being made on a purely political basis, state development projects should only be made after very thorough assessment of the respective benefits and costs, and the risks involved.

10.2 Progressing SAMF

SAMF provides a robust and progressive system for planning, developing and delivering Western Australian infrastructure. It was intended to improve the quality of asset management through its application to assets at each stage of their lifecycles, from planning and delivery through to ongoing maintenance and, finally, to asset disposal. It is generally acknowledged that SAMF is a solid framework and represents a significant step towards improved decision-making in relation to

the commitment to building infrastructure. However, it is only in recent years that it has been developed to its present level, and implementation by agencies has been

The Works Reform Program (Works Reform) aims to achieve a better alignment between how SAMF is implemented and how it is intended to be implemented.[688] Through the sound processes of SAMF and the restructuring that has occurred through Works Reform, Western Australia is well on the way to having a system that is capable of delivering better infrastructure outcomes. However, there is still much progress to be made by government in recruiting and retaining staff with the right skill sets to implement the processes.

SAMF continues to undergo refinement and Works Reform is not yet fully implemented. As more projects are completed through a rigorous application of SAMF procedures supported by Works Reform, the Department of Treasury and Finance (DTF) will be better placed to assess the benefits derived from the implementation of Works Reform. While internal assessment is an integral part any reform process, and in this instance would be expected to be conducted by DTF, there is also the need for external assessment of these processes and the extent and effectiveness of their implementation.

As it is important that Works Reform and SAMF are judged in accordance with their impact on the quality of the state's infrastructure outcomes, the Committee intends to examine a small number of infrastructure projects each year to determine whether anticipated outcomes are being achieved. The Committee will report the results of these investigations in its annual reports.

> The Public Accounts Committee will determine which infrastructure projects it may assess with a view to determining the degree to which the Strategic Asset Management Framework is being successfully applied. Reports on any such assessments would be provided in the Committee's annual reports to the Legislative Assembly.

Hon. John Kobelke, MLA
Chairman

688 Mr John Tondut, Executive Director, and Ms Margaret Sharpe, Director Review and Reform, Building Management and Works, Department of Treasury and Finance, *Briefing*, 2 September 2010.

APPENDIX ONE

SUBMISSIONS RECEIVED

List of Submissions received for the inquiry.

No.	Date Received	Name	Position	Organisation
1	13 January 2010	Mr P Evans	Private Citizen	
2	15 January 2010	Mr D Snook	Acting Commissioner of Main Roads	Main Roads Western Australia
3	12 February 2010	Mr P Conran	Director General	Department of Premier and Cabinet
4	2 March 2010	Mr R Waldock	Chief Executive Officer	Public Transport Authority of Western Australia
		Mr T Morgan	Chief Executive Officer	East Perth Redevelopment Authority
5	23 March 2010	Mr M Henneveld	Commissioner of Main Roads	Main Roads Western Australia
6	23 March 2010	Mr R Waldock	Chief Executive Officer	Public Transport Authority
7	23 March 2010	Mr T Morgan	Chief Executive Officer	East Perth Redevelopment Authority
8	23 March 2010	Mr R Waldock	Chief Executive Officer	Public Transport Authority
9	29 March 2010	Ms A Nolan	Director General	Department of State Development
10	20 April 2010	Closed Evidence		Western Power
11	20 April 2010	Closed Evidence		Western Power
12	20 April 2010	Mr P Rosair	Director General	Regional Development and Lands

No.	Date Received	Name	Position	Organisation
13	22 April 2010	Mr T Narvaez	General Manager Strategy and Business Development	Verve Energy
14	30 April 2010	Mr M Henneveld	Commissioner of Main Roads	Main Roads Western Australia
15	27 May 2010	Closed Evidence		Verve Energy
16	31 May 2010	Mr R Mann	Executive Director Strategic Projects	Department of Treasury and Finance
17	28 May 2010	Mr P Stubbs	Director, Ord-East Kimberley Expansion Project	Department of Regional Development and Lands
18	1 June 2010	Closed Evidence		Western Power
19	3 June 2010	Ms A Nolan	Director General	Department of State Development
20	3 June 2010	Ms A Nolan	Director General	Department of State Development
21	10 June 2010	Closed Evidence		Western Australia Police
22	11 June 2010	Mr M Henneveld	Managing Director of Main Roads	Main Roads Western Australia
23	2 June 2010	Mr B Bradley	Director General	Department of Commerce
24	31 May 2010	Mr T Marney	Under Treasurer	Department of Treasury and Finance
25	15 April 2010	Mr T Marney	Under Treasurer	Department of Treasury and Finance
26	13 July 2010	Mr F Marra	A/Chief Executive Officer	Western Australian Land Authority (LandCorp)
27	16 July 2010	Mr B Bradley	Director General	Department of Commerce
28	14 July 2010	Mr P Robb	Private Citizen	
29	30 April 2010	Mr T Marney	Under Treasurer	Department of Treasury and Finance
30	18 August 2010	Mr R Waldock	Chief Executive Officer	Public Transport Authority

No.	Date Received	Name	Position	Organisation
31	9 September 2010	Ms A Nolan	Director General	Department of State Development
32	9 September 2010	Closed Evidence		Department of State Development
33	13 August 2010	Ms C Fitzpatrick	Manager, Government Relations and Sustainability	Leighton Holdings Limited

APPENDIX TWO

HEARINGS

List of hearings for the inquiry.

Date	Name	Position	Organisation
2 March 2010	Mr Phil Ladner	Executive Director, Infrastructure Delivery	Main Roads Western Australia
	Mr Michael Cosson	Manager, Project Programming	Main Roads Western Australia
	Mr Leo Coci	Director, Major Projects	Main Roads Western Australia
	Mr Peter Woronzow	Executive Director, Finance and Commercial Services	Main Roads Western Australia
2 March 2010	Mr Reece Waldock	Chief Executive Officer	Public Transport Authority of Western Australia
	Mr Marko Martinovich	Executive Director, Infrastructure Planning	Public Transport Authority of Western Australia
	Mr Anthony Morgan	Chief Executive Officer	East Perth Redevelopment Authority
5 March 2010	Ms Anne Nolan	Director General	Department of State Development
	Ms Gail McGowan	Deputy Director General	Department of State Development
5 March 2010	Mr Menno Henneveld	Commissioner of Main Roads	Main Roads Western Australia
	Mr Michael Cosson	Manager, Project Programming	Main Roads Western Australia
	Mr Robert Arnott	Engineer/Project Director	Main Roads Western Australia

Date	Name	Position	Organisation
1 April 2010	Mr Timothy Marney	Under Treasurer	Department of Treasury and Finance
5 May 2010	Mr Tony Narvaez	General Manager, Strategy and Business Development	Verve Energy
5 May 2010	Mr Paul Rosair	Director General	Department of Regional Development and Lands
	Mr Peter Stubbs	Director, Ord-East Kimberley Expansion	Department of Regional Development and Lands
7 May 2010		Closed Hearing	Western Power
16 June 2010	Ms Gail McGowan	Deputy Director General, State Initiatives	Department of State Development
	Ms Gemma Brown	Senior Project Manager	Department of State Development
18 June 2010	Mr Dominic Staltari	Assistant Commissioner, Professional Standards	Western Australian Police
	Mr Greg Italiano	Executive Director	Western Australian Police
	Mr James Lord	Director, Asset Management	Western Australian Police
	Mr Michael Webster	Assistant Director, Land and Building Services	Western Australian Police
18 June 2010	Mr Richard Mann	Executive Director, Strategic Projects	Department of Treasury and Finance
23 June 2010	Mr Brian Bradley	Director General	Department of Commerce
	Ms Julie De Jong	Acting Executive Director	Department of Commerce
	Mr John O'Hare	General Manager, Marine and Defence	Department of Commerce
	Mr Ross Holt	Public Servant	LandCorp
	Mr Luke Willcock	General Manager	LandCorp

Date	Name	Position	Organisation
18 August 2010	Mr Chris Palandri	Regional Managing Director	Brookfield Multiplex
8 September 2010	Mr Robert Ward	Executive Director, Infrastructure Advisory	RBS Group (Australia) Pty Limited
	Mr Hugh Funder	Senior Advisor, Infrastructure Advisory	RBS Group (Australia) Pty Limited

APPENDIX THREE

BRIEFINGS HELD

List of Briefings to the Inquiry

Date	Name	Position	Organisation
Briefings provided to the Committee			
8 June 2010	Mr Brian Bradley	Executive Director	Department of Commerce
	Mr John O'Hare	General Manager, Marine and Defence, Oil and Gas	Australian Marine Complex
	Mr Luke Willcock	General Manager Metropolitan	LandCorp
	Mr Bill Adlam	Business Manager Western Trade Coast	LandCorp
18 August 2010	Mr Michael Deegan	Infrastructure Coordinator	Infrastructure Australia
Briefings provided to the Committee Secretariat			
2 August 2010	Mr Anthony Kannis	Executive Director, Infrastructure and Finance	Department of Treasury and Finance
10 August 2010	Ms Josephine Quealy	Program Manager, Economic Audit Implementation Unit	Department of Treasury and Finance
2 September 2010	Mr John Tondut	Executive Director, Building Management and Works	Department of Treasury and Finance
	Ms Margaret Sharpe	Director Review and Reform, Building Management and Works	Department of Treasury and Finance

APPENDIX FOUR

LEGISLATION

List of Legislation (or other relevant information) used in the Inquiry.

Legislation	State (or Country)
Infrastructure Australia Act 2008	Commonwealth
AusLink (National Land Transport) Act 2005	Commonwealth
Nation Building Program (National Land Transport) Act 2009	Commonwealth
Nation Building and Jobs Plan (State Infrastructure Delivery) Act 2009	Commonwealth
Nation-building Funds Act 2008	Commonwealth

APPENDIX FIVE

Government of Western Australia

mainroads WESTERN AUSTRALIA

ABN: 50 860 676 021

Our Ref: 05/5523-03 (D10#108881)

Hon John Kobelke, MLA
Chairman
Public Accounts Committee
Parliament House
PERTH WA 6000

Dear Mr Kobelke

PUBLIC ACCOUNTS COMMITTEE INQUIRY
COMMONWEALTH FUNDING FOR WA ROAD PROJECTS

Thank you for the Committee's letter of 17 May 2010 seeking additional information regarding projects submitted with my letter dated 22 April 2010.

Main Roads is pleased to provide this additional information to assist the inquiry and in this regard please find attached a spreadsheet which outlines for each project:

- the grants program under which the funding was provided;
- the dates that the funding was allocated by the Commonwealth Government; and
- the dates by which the funds had to be spent.

You will note from this spreadsheet that the funding is provided under one or a combination of the following four Commonwealth programs:

- AusLink Investment Program;
- Accelerated Upgrade Package;
- Nation Building Program; and
- Infrastructure Employment Projects (IEP) Program.

The first of these programs, the AusLink Investment Program (AIP), was an integral part of the so-called AusLink White Paper which was announced in a letter from the then Minister for Transport and Regional Services on June 7 2004. This letter included cash flows for projects to be funded under the AIP over the period 2004/05 to 2008/09. The AIP was subject to a Bilateral Agreement that was jointly signed by the Commonwealth and State Ministers on 8 December 2005. Either date could be used to indicate when funding was allocated by the Commonwealth to AIP projects, however, the latter date has been adopted and is reflected in the attached spreadsheet. Other than the New Perth Bunbury Highway project, no dates were prescribed in the Bilateral Agreement by which the funds had to be spent, however, the intention was for all funds to be spent by the end of the five year period ie by 30 June 2009.

Australian Business Excellence Awards
Bronze Award 2007

Infrastructure Delivery Directorate, Waterloo Crescent, East Perth or PO Box 6202, East Perth Western Australia 6892
Telephone: 138 138 Facsimile: (08) 9323 4567
Email: enquiries@mainroads.wa.gov.au Website: www.mainroads.wa.gov.au
D10#85385

The second of these programs, the Accelerated Upgrade Package (AUP) was announced in a letter from the then Minister for Transport and Regional Services on 2 May 2006. The AUP is subject to a Memorandum of Understanding (MoU) that was jointly signed by the Commonwealth and State Ministers on 27 June 2006. This is the date adopted in the attached spreadsheet to indicate when funding was allocated by the Commonwealth for AUP projects. The dates by which funds for AUP projects are required to be spent are also indicated in the spreadsheet and are based on the dates for projects to be completed as set out in the MoU.

Projects funded under the third of these programs, the Nation Building Program (NBP), were announced in the lead up to the 2007 Federal election. The only exception to this is the Heavy Vehicle Safety and Productivity Project (HVS&PP) which was announced separately. The NBP is subject to a Memorandum of Understanding (MoU) that was jointly signed by the Commonwealth and State Ministers on 5 February 2009 and 27 February 2009 respectively. The latter date has been adopted to indicate when funding was allocated by the Commonwealth for NBP projects, other than the HVS&PP, and is reflected in the attached spreadsheet. No dates were prescribed in this MoU indicating when the funds had to be spent, however, the intention was for all funds to be spent by the end of the five year period ie by the end of 2013/14. This date has been adopted to signify when the funds had to be spent for NBP projects other than a number of projects for which agreement was subsequently reached with the Commonwealth Government and for which the relevant dates have been included on the spreadsheet.

The final program, the Infrastructure Employment Projects (IEP) Program, applies to only one project, the Hopetoun-Bremer Bay Road. Commonwealth funding for this project was announced in a media release from the Minister for Infrastructure, Transport, Regional Development and Local Government on 17 December 2009. An Implementation Plan for the project has since been prepared and is in the process of being forwarded to the Commonwealth and State Ministers for their signature. This does not set out a date by which the funding has to be spent but indicates that the project is scheduled for completion by April 2012. This is the date that has been adopted in the spreadsheet to indicate when Commonwealth funding has to be spent.

I trust this information will be of assistance for your enquiry.

Yours sincerely

Potter

Menno Henneveld
MANAGING DIRECTOR OF MAIN ROADS

9 JUN 2010

Enc.

Asset Investment Program

Projects With Commonwealth Contribution - Funding Information as at 2 June 2010

Auslink:
- On June 7 2004 the Australian Government released the AusLink White Paper detailing its new land transport plan.
- The AusLink Bilateral Agreement was signed between WA and Australian Governments in December 2005. It detailed projects and funding for the five years to 2008/09.

Nation Building Program (NBP):
- NBP Memorandum of Understanding (MOU) was signed in February 2009 (replacing the AusLink Bilateral Agreement) and covers projects and funding for the period 2008/9 to 2013/14.

Accelerated Upgrade Program (AUP):
- The State was advised of additional funds under the AUP in May 2006 and the MOU was signed in June 2006. $323m was paid to State in June 2006 with all projects to be completed or best endeavours made to complete by Decmber 31 2009.

Infrastructure Employment Projects (IEP) Program:
- The Australian Government announced its contribution to upgrade roads within the Fitzgerald National Park (Hopetoun-Bremer Bay Road) by a media release in December 2009. Completion of the project is expected by April 2012.

Asset Investment Program	Cwlth Program	Cwlth Allocation $000	Date that Funding was allocated by Commomwealth Government	Date by which the Funds had to be spent
Projects with Commonwealth and State funding contributions:				
New Perth Bunbury Highway (Kwinana Freeway Extension & Forrest Highway)	AusLink	160,000	AusLink Bilateral Agreement signed Dec 8 2005.	Project to be opened to traffic by December 2009
	NBP	170,001	NBP MoU signed Feb 27 2009	
Mandurah Entrance Road	NBP	77,500	NBP MOU signed Feb 27 2009	project to be completed by Dec 2010
Bunbury Port Access Stage 1	NBP	17,367	NBP MOU signed Feb 27 2009	project to be completed by Dec 2009
Bunbury Port Access Stage 2	NBP	65,774	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Bunbury Outer Ring Road Stage 1	NBP	52,858	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Great Eastern Highway - Kooyong Rd to Tonkin Hwy	NBP	179,999	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Reid Hwy & Alexander Dr Interchange	NBP	10,000	NBP MOU signed Feb 27 2009	project to be completed by April 2011
Great Eastern Highway - Roe Hwy Interchange	NBP	74,034	NBP MOU signed Feb 27 2009	project to be completed by Jan 2012
Leach Highway (High St) Improvements	NBP	33,993	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Roe Hwy Midland/Kewdale to Fremantle Port ITS Management System	NBP	7,162	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Kwinana Freeway ITS Management System	NBP	8,876	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Kwinana Freeway Freight Management System	NBP	29,436	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Kwinana Freeway - Additional lanes Leach Hwy to Roe Hwy	NBP	22,166	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Tonkin Highway Leach Highway to Roe Highway	NBP	15,610	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Tonkin Highway Roe Highway Interchange Improvements	NBP	3,009	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Tonkin Highway Leach Highway Interchange	NBP	24,902	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Tonkin Highway Kewdale Road (Horne Miller Drive) Interchange	NBP	32,395	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Tonkin Highway Incident & Congestion Management System	NBP	3,770	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Tonkin Hwy Abernethy Road Interchange Stage 2	NBP	8,088	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Kewdale Intermodal Terminal Network - Rail	NBP	26,776	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Nation Building Program 1	NBP	134,681	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Coolgardie-Esperance Hwy - Esperance Port Access Corridor	NBP	60,000	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Dampier Highway Stage 1B	NBP	4,392	NBP MOU signed Feb 27 2009	project to be completed by Dec 2009
Dampier Highway Stages 2-6	NBP	75,609	NBP MOU signed Feb 27 2009	project to be completed by June 2012

Asset Investment Program	Cwlth Program	Cwlth Allocation $000	Date that Funding was allocated by Commonwealth Government	Date by which the Funds had to be spent
GNH - Pinga & Wallwork Intersections & Dual C'Way	NBP	6,000	NBP MOU signed Feb 27 2009	project to be completed by late 2009
Great Northern Hwy - Port Hedland Upgrade	NBP	154,000	NBP MOU signed Feb 27 2009	project to be completed by 2013/14
Heavy Vehicle Safety and Productivity Program Stg 1	NBP	2,705	Funding approved by Commonwealth Minister on April 6 2009	project to be completed by 2009/10
Great Northern Hwy Muchea to Wubin	AusLink	65,100	AusLink Bilateral Agreement signed Dec 2005	project to be completed by 2008/09
	AUP	57,600	AUP MoU signed June 2006	Best endeavours to complete works by 31 December 2009
Great Northern Hwy Lennard St to Muchea	AusLink	21,200	AusLink Bilateral Agreement signed Dec 2005	project to be completed by 2008/09
	AUP	64,000	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Daddow Road Bridge	NBP	14,700	Included in revised AusLink Bilateral Agreement - signed Jan 2007.	project to be completed by 2008/09
Hopetoun to Bremer Bay Road Stage 1	IEP	20,000	Media announcement of Commonwealth contribution towards project in Dec 2009	project to be completed by April 2012
Projects with Commonwealth funding contribution only:				
Eyre Hwy - Balladonia East	AUP	29,290	AUP MOU signed June 2006	Complete works by 31 December 2009
Eyre Hwy - Heart Break Ridge	AUP	34,246	AUP MOU signed June 2006	Complete works by 31 December 2009
Eyre Hwy - Ciaguna East/Balladonia	AUP	47,516	AUP MOU signed June 2006	Complete works by 31 December 2009
Great Northern Hwy Big Mabel Creek Bridge	AUP	17,929	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Great Northern Hwy Bow River Section	AUP	46,322	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Great Northern Hwy Elvire to Sandy Creek Section	AUP	11,419	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Great Northern Hwy Fitzroy to Gogo	AUP	4,999	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Great Northern Hwy Telegraph Creek Bridge	AUP	14,838	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Great Northern Hwy Fletcher Creek Bridge	AUP	25,878	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009
Victoria Hwy Kununurra Heavy Haulage Route	AUP	9,001	AUP MOU signed June 2006	Best endeavours to complete works by 31 December 2009

PROJECT PLANNING AND FUNDING APPLICATIONS FOR MAJOR WESTERN AUSTRALIAN INFRASTUCTURE PROJECTS

MINORITY REPORT

Mr Joe Francis, MLA **Mr Tony Krsticevic, MLA**

1.1 Background

This Minority Report has been submitted by Joe Francis, MLA and Tony Krsticevic, MLA in order to address what we believe is a significant omission from, and incorrect conclusion drawn in, the Public Accounts Committee's report into this Inquiry.

While the majority of the information and findings outlined in the report were unanimously supported, the issue of public funding for the development of Oakajee Port was not.

There has been much political debate over the merits of public funding for the Oakajee development, and this Minority Reports seeks to impartially outline the case for part public funding.

(a) State Investment in the Oakajee Port Common Use Infrastructure

It is understood that Oakajee Port and Rail Pty Ltd (OPR) submitted a draft Bankable Feasibility Study (BFS) to Government on 29 March 2010 and that the State is now in the process of conducting an extensive review on the information presented in this study. This review is intended to ensure that the final decision committing the government and its funding contribution to the project is made on a sound basis and with due respect for any associated risks.

The estimated cost of the Common Use Infrastructure (CUI) is $678 million. It is understood this initial estimate was based on information obtained during the Request for Proposal process (RFP). The government is currently reviewing the cost estimates provided. These costs should be further refined as OPR continues to refine the costs and implementation plan; the final cost should be better known once OPR provides its final BFS and a further due diligence process is completed.

The $339 million 50/50 share of the CUI costs between the Western Australian and Commonwealth Governments is based on the initial estimate of $678 million. The Commonwealth Government announced it would set aside $339 million towards the CUI and this was included in the *2009–10 Federal Budget*, subject to further work and consideration by Infrastructure Australia (IA). State funding for the CUI is currently allocated for the 2010–13 financial year.

The federal government recognises the unique long-term economic benefits this project will produce for Western Australia and the nation, and is offering bi-partisan support. Recognising the potential, the federal government is an enthusiastic partner in this project. Premier Colin Barnett highlighted this to Parliament on 18 March 2010 when he informed the House that:

> *I again remind members that my good friend … Hon Kevin Rudd is a strong advocate of Oakajee, and a strong advocate of the state and commonwealth governments joining together to build that key piece of infrastructure, the common-user port facility.*[689]

This echoed the support affirmed by former Prime Minister Rudd during a visit to Geraldton in May 2009. Mr Rudd stated that the Oakajee port was a very good project, and that 'the whole nation should pause for a moment and reflect on where this great project takes not just the great state of Western Australia, [but also] Australia itself in the decades ahead'.[690]

There are two main partners in the Oakajee Port and Rail consortium, being Mitsubishi Corporation and Murchison Metals. The plan by the consortium to invest heavily in Oakajee Port is clearly driven by the principle that more product on rail equals more product through the deep water port. The potential of Oakajee has been further endorsed by Sinosteel Midwest Corporation, Karara Mining Ltd and Crosslands Resources Ltd all coming on board as the three foundation customers.

1.2 Rationale for Government Funding of the Oakajee Common Use Infrastructure

Oakajee will be a multi-user, multi-function port. This is clearly different from other ports being developed in Western Australia, which are largely single-product and single-user, or have a defined small number of users.

There is solid precedent for part or wholly State-owned ports in Western Australia, including: Port Headland, Broome, Dampier, Geraldton, Fremantle, Albany and Esperance.

Furthermore, Cape Preston—the state's only essentially private port, which comes under operational control of Dampier Port Authority—is, as a result, limited in expansion to further export organisations, driving the requirement to develop a further port at Anketell.

Therefore, it is a natural conclusion that without State investment and the resultant leverage that occurs from such investment, there is a very real risk that third-party exporters may be excluded from or hindered in their access to facilities at Oakajee Port.

Additionally, government has traditionally owned CUI infrastructure at multi-user, multi-function ports (including Geraldton).

The Mid-West iron ore industry is characterised by a number of smaller operators. Unlike other port developments, such as iron ore ports in the Pilbara, none of the companies or mining projects are sufficiently large or commercially robust enough to justify investment in the port in their own right.

Government investment in, and control of, the CUI provides the opportunity to ensure the development is designed to cater for the longer-term needs of the state and the region.

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689 Hon. Colin Barnett, Premier, Western Australia, Legislative Assembly, *Parliamentary Debates* (Hansard), 18 March 2010, p.898.

690 (Former) Prime Minister Kevin Rudd, cited in 'Oakajee to Help Rebuild "Economic Prosperity"', *ABC News*, 21 May 2009, p.1. Available at: http://www.abc.net.au/news/stories/2009/05/21/2577217.htm. Accessed on 8 November 2010.

The development of the Mid-West also includes a world-class heavy-industry site that will require Panamax size berths in the longer term. Developing Oakajee Port as an 'iron ore only' port would not facilitate the industrial estate and the longer term economic development benefits which the Estate will provide for the region and the state.

1.3 Conclusion

The federal Labor government and state Liberal-National government in Western Australia have both committed a total of $678 million towards 50/50 funding for Oakajee Port CUI. This project is forward thinking. It has bi-partisan support from the federal government. Rather than attempt to catch up once the next upward trend in the mining sector has started, this anticipates the needs of the mining industry and will underpin the broader development in the Mid-West region of Western Australia. It is predicted that by 2020, 100 million tonnes of iron ore will be shipped through Oakajee. The project will generate thousands of direct jobs during the construction and development phase, as well as being the keystone to the growth of the local iron ore industry.

Finding 1

There is a clear risk that without State investment and the resultant leverage that this provides government as a part-owner of Oakajee Port, future access for other exporters may be excluded or hindered. Government investment in part of the port, in particular the Common Use Infrastructure, allows the State to control fair access to the development into the future.