PUBLIC ACCOUNTS COMMITTEE

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

TRANSCRIPT OF EVIDENCE TAKEN
AT PERTH
THURSDAY, 1 APRIL 2010

Members

Mr J.C. Kobelke (Chairman)
Mr J.M. Francis (Deputy Chairman)
Mr A. Krsticevic
Ms R. Saffioti
Mr C.J. Tallentire

Hearing commenced at 3.10 pm

MARNEY, MR TIMOTHY
Under Treasurer,
examined:

The CHAIRMAN: The committee hearing is a proceeding of Parliament and warrants the same respect as the proceedings in the house itself demand. Even though you are not required to give evidence on oath, any deliberate misleading of the committee may be regarded as a contempt of Parliament. Have you completed the "Details of Witness" form?

Mr Marney: Yes, I have.

The CHAIRMAN: Do you understand the notes at the bottom of the form?

Mr Marney: Yes, I do.

The CHAIRMAN: Did you receive and read an information for witnesses briefing sheet regarding giving evidence before parliamentary committees?

Mr Marney: If I say no, do I get to go home? Yes, I did and I have.

The CHAIRMAN: We could give it to you again! Do you have any questions relating to your appearance before the committee today?

Mr Marney: No, I do not.

The CHAIRMAN: I thank you formally for appearing before the committee and assisting us with our inquiry. You would be well aware that the Department of the Premier and Cabinet has provided us with a written submission that pertains to information from the Department of Treasury and Finance. This is a good overview of the processes. I am seeking to get more information about this, how you use it, how it is applied and how effectively and comprehensively it works. The submission says that there are two key areas in which the Department of Treasury and Finance is involved. The first is prioritising public sector capital investment projects in the budget process, and, the second is the strategic asset management framework. We will start with the budget process and prioritising what is obviously a huge demand in a rapidly growing state. The three factors used in that system are importance, benefits and achievability. They are the three level criteria on each area. Give us some more background on that and fill out how it works and how effective you think it has been.

Mr Marney: As you said, there is a lot going on and a lot of demand for infrastructure capital investment across the state. It is, I have to say, extremely 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. I would not for a second want to mislead you that this is a scientific process that is executed within the Department of Treasury and Finance in its processes of providing recommendations to the government, which are channelled through the Economic and Expenditure Reform Committee. Having said that, we need some form of objective criteria by which our analysts can review the capital proposals within the various agencies with which they deal and to try to get some consistency in evaluation, at least in absolute terms of the cost–benefit of individual capital proposals. We must also bring that together for a relative assessment. Having assessed the projects against the criteria outlined in the documents, we conduct forums that moderate projects across the various portfolios. The analysts within the Department of Treasury and Finance will go to the forum, which usually runs for a day, and they present their analysis. The broader executive forum then considers that analysis and sends its recommendations to the EERC on the basis of those presentations and that analysis.

The CHAIRMAN: Do people from the agencies attend those forums, or is it just within the Department of Treasury and Finance?

Mr Marney: It is just within Treasury. Prior to that, the agencies would have submitted their capital proposals. Individual analysts from Treasury spend time talking with them to try to understand the nature of those proposals. Where appropriate, either the director or executive director might get involved in those discussions if it is a particularly complex project and we need to better understand the risks associated with it. As is highlighted in the criteria, deliverability is a critical factor. If it cannot be delivered, there is no point approving it. That plays a part in our analysis as well. That is done internally in the Department of Treasury and Finance. That gives us our relative ranking that we present to the government, and the government makes its decision from there. Usually that is done in consultation, obviously, with the line ministers and the minister's agencies through the open processes—or closed processes; depending on your view—of the EERC.

The CHAIRMAN: You just talked about something being able to be delivered, which I equated to achievability in terms of the criteria. Correct me if I am wrong, but I take it that not equal weight is given to the criteria of importance, benefit and achievability. Is there a hierarchy?

Mr Marney: Obviously the importance of the project to government is a particular factor that weighs fairy heavily. We exist to deliver the government's priorities. That is a significant factor in ensuring that whatever capital expenditure is proposed actually aligns with the government's priorities. Also within that criteria is the importance of the ongoing service delivery of the core critical services of law and order, health, education, child protection and so on. They would rank more highly in those considerations than other projects that might be considered more discretionary.

The CHAIRMAN: So the issue —

Mr Marney: Say of a sporting nature, to be quite direct about it.

The CHAIRMAN: Is it a subjective judgement balance between the three rather than a scoring system?

Mr Marney: 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.

The CHAIRMAN: I want to burrow down on the area of benefits. To what extent are you able to have more scientific—if I can use that term loosely—or objective criteria such as a cost–benefit analysis? Is that just a target that you seek to achieve, or are you able to put that together on all the projects that receive serious consideration?

Mr Marney: It depends on the project and on the planning that an agency has put into it. 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. That, in itself, informs our assessment of the benefits. If the benefits cannot be articulated well and easily, we must question whether there are any benefits. But, again, there is not a process of, if you like, a scientific cost–benefit analysis that brings it down to a single number that we then compare across projects. There is a lot of subjective judgement and qualitative evaluation involved in the process.

[3.20 pm]

The CHAIRMAN: So coming at the same issue in a slightly different way, are you able to tell the committee whether or not a cost–benefit analysis of some substance is the target in terms of all these assessments? Is it the general rule or is it perhaps only in some cases that you actually can have a cost–benefit analysis that gives you some feeling that there has been a robust consideration of the project?

Mr Marney: Our policy settings under the strategic asset management framework require as part of that an articulation of benefits and for that sort of cost–benefit analysis work to be done. So the policy settings certainly require it. It is not always feasible though, whether it be due to data gaps or time frames. So it is the preferred approach to have that cost–benefit work done, but it is not always feasible.

The CHAIRMAN: Perhaps to help other members come in, before I move to questions on the strategic asset management framework, do members want to explore any of those issues regarding priority settings?

Ms R. SAFFIOTI: Yes. In respect of the criteria, importance to governments is one issue that you raised. As I see it, there are some projects which the government has made a decision on in which Treasury has had no involvement in providing advice on whether it should do it, but Treasury's role now is to provide advice on how it should do it; would that be right?

Mr Marney: That is often the case in the circumstances of any government. The government is elected and has a contract with the people, to quote a previous Treasurer, to deliver on its election promises, and our job in those circumstances is not to question the validity of that contract but to help the government deliver on it. So that is what we do. Having said that, if we think something is not in the best interests of the public or is not the best way to meet a certain election commitment or the service delivery outcome, then we certainly will not hold back about saying that. But as you have correctly pointed out, sometimes our job is just to get on and deliver it the best that we can.

Mr C.J. TALLENTIRE: Going back to the issue of benefits, do you look at the quality and strength of verification that has gone into assessing the claimed benefits of different projects?

Mr Marney: Absolutely. I mean, in any proposal to spend public money we always drill down into the quality of the supporting arguments and the validity of the data and the validity of the qualitative analysis as well, tracing right back into the service delivery need that is articulated that requires a particular asset investment; and that is where we start, the analysis. Really if you look at any program of works, whether it is hospitals, schools or prisons, we look at the trend in service delivery need and, therefore, what assets do we need to have in place to support that service delivery need? So we drill right back into that.

Mr C.J. TALLENTIRE: As a follow-up to that, could you comment on how reliable you find the quality of the information that comes forward regarding resources projects and their infrastructure needs? Are there cases where resources projects are presented as being very sure to proceed and therefore needing big amounts of infrastructure only for us to find in years to come that the price of nickel has changed and the mine is no longer viable, or a magnetite deposit is not actually feasible?

Mr Marney: That is probably the greatest area of contention. In evaluating some of those large investments it is actually being able to understand what those, if you like, industrial infrastructure requirements are, because you are essentially taking a bet on what industrial development is going to do. In those circumstances what we tend to do is focus on scenario analysis. So we know what is the worst case and what is the best case in terms of that development path and what does that mean for your asset investment over time? We put that information to government along with our best guess pretty much of what we think the development path will be. So is it scenario 1 or is it scenario 5? Essentially that is what government is elected to do: it is to take those decisions.

Ms R. SAFFIOTI: Can I just go back to priority setting and providing advice to government on projects and whether public funding should be used in some of these projects? In some of the projects that this committee is looking at—for example Oakajee, where the Treasury was asked whether public funding was required—was any cost–benefit analysis undertaken before the commitment and before the announcement to provide public funding?

Mr Marney: We were involved in various stages of evaluation of Oakajee, but that was predominantly handled through the Department of State Development. So in terms of the cost–benefit and so on, I think that is probably a question that is best directed to them.

Ms R. SAFFIOTI: But in respect of DTF's involvement, can I ask whether DTF was party to the decision or the discussion on providing public funding to the project?

Mr Marney: At various points through the EERC process, advice was provided by DTF through to government on that particular project. 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.

Ms R. SAFFIOTI: So, I take it from that that DTF was not consulted significantly in the lead-up to that decision being made to provide public funding into the project.

Mr Marney: Yes, it was more a clearly articulated outcome that the government wanted to achieve, and our work focused on how best to achieve it.

Mr A. KRSTICEVIC: I have just a quick question about your role. Obviously you talk about projects that are on the government agenda, but also I just want to know what role you played in terms of departments, I suppose, establishing contracts for big infrastructure projects and how much of an influence you had in terms of that side of it. Specifically I am thinking, for example, of a number of projects that I could pick, but I will pick the easiest one which is the Perth Arena. So there is an example of a project that has gone hundreds of millions of dollars over budget, which seems to have this open-ended contract that basically BGC can throw as many expenses as they like at us, I suppose, that keep blowing out the cost. How do contracts like that get through and what involvement do you play in advising government of, I suppose, how they have done that or the mistakes they have made or that they have opened up a bottomless pit?

Mr Marney: I think that question is covered fairly comprehensively in the recent Auditor General's report around Perth Arena. At the point at which the Perth Arena contracts were negotiated, signed and so on, those processes were solely the responsibility of the former Department of Housing and Works. That has since changed with this government's reform to the works function within government, and it was partly in response to some of the learnings out of that example, but not purely that. Since then the works segment of the Department of Housing and Works has been moved into Treasury and Finance. The Department of Treasury and Finance now has, if you like, 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.

Mr A. KRSTICEVIC: So I suppose after these changes being made, a lot of those things were not done when infrastructure projects were being put forward.

Mr Marney: To be frank, the same policy settings were in place as in the strategic asset management framework. It would be fair to say that within the Department of Housing and Works, housing being a very large entity, the works side of the business had probably not quite the exposure or prominence that maybe it should have been afforded, but it is the exact same policies and processes. I think what we did learn through how the works activity was running was that we were relying on two fundamental kinds of failures, if you like.

[3.30 pm]

It is no-one's fault. It is just that sometimes you learn these things as you go on in organisational change. The first one was that we were reliant very heavily on external consultants to run projects and contracting processes, and they do not necessarily fully understand or always have the public's interest at the forefront. Secondly, the business model of the then works entity was that it dealt with the agencies of government and considered them to be its primary client. The change we have made since then is that the primary client is the government, and we seek to deliver what the government wants, not necessarily what the agency would prefer. So, if you like, the controls on scope, the controls on contracting and even the capability around contracting are very different from what they were at that point in time. Having said that, we still have a long way to go to build capability in the works business that can deal with those sorts of complex projects.

Mr A. KRSTICEVIC: Do you see cost blow-outs in the future for projects, or do you think there is enough there to be able to do that properly now? Is there still the potential for that to occur?

Mr Marney: There is always potential for cost blow-outs. The question is: what management regime have you got in place to minimise those as much as you can? Whenever anyone is building something, whether it is private industry, public infrastructure or private home renovations, cost blow-outs are not unusual.

Mr A. KRSTICEVIC: No.

Mr Marney: What we are trying to do is ensure that we have the up-front planning as robust as possible, so that we have something to manage back to; you have got your point of reference that is robust. 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, and even just to develop our contracting skills to ensure that we nail those elements whereby private industries, out of the goodness of their heart, feel the need to screw us.

The CHAIRMAN: Could I just follow on from that because, Mr Marney, most, if not all, of what you are covering fits under the strategic asset management framework—correct?

Mr Marney: Yes.

The CHAIRMAN: The issue then is: to what extent has this been changed in terms of the key elements of the strategic asset management framework? Is it an ongoing developmental issue, or has it gone through radical change?

Mr Marney: It has not gone through radical change. It has been finetuned, I would probably say. It is more the implementation. I would have to admit that a key failing in the implementation of the strategic asset management framework is probably on Treasury's part. It actually developed a very good, comprehensive suite of policies, guidelines and requirements, but for whatever reason our implementation of that was not as successful as it needed to be—partly our fault, I guess; partly agencies and their motivations. So we are turning our efforts, having finetuned the policy settings, to doing a much better job at implementing that. Having the works business as part of Treasury and Finance enhances our ability to do that, because we control some of those key steps in the process now that we did not previously.

The CHAIRMAN: Could I just have clarification of that, because I read the document that we have on the strategic asset management framework, correctly or incorrectly, as really putting a lot of that responsibility on the individual agencies, whereas you are saying that Treasury and Finance has to accept a lot of the responsibility for making sure it works better?

Mr Marney: Going forward?

The CHAIRMAN: Yes.

Mr Marney: Absolutely. It is our framework; it is our policy, so we have to make sure it works.

The CHAIRMAN: I am trying to get that interface between the agencies and DTF in terms of who has responsibility for which part to make sure it all works.

Mr Marney: Okay. I can give you a schedule that sets that out, because probably the key challenge when I inherited the works business was to sit down and say, "Well, this is what the strategic asset management framework requires. There are about seven or eight steps in it. Who does what?" So we have mapped that out fairly rigorously and in consultation with agencies. I think the key emphasis now is that agencies were struggling to develop business cases that were robust, going back to your point around cost–benefits and whether the evaluations are based on rigorous analysis in that regard. So we have taken a far greater role in guiding the development of those business cases and, in some cases, writing business cases for them. We are trying to focus agencies on planning their service delivery requirements much better, so they actually model the parameters that are affecting their service demand and plan those seven years out 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, and that is where we tend to get asset decisions that are suboptimal.

The CHAIRMAN: Assuming that the strategic asset management framework is largely the model you want to use—I realise there may still be further refinement—what level of compliance or delivery do you currently have? Are you halfway there or are you still far more than that in terms of getting agencies to work with DTF and DTF being able to help them to come up to the standards that are outlined in the strategic asset management framework?

Mr Marney: It varies considerably across agencies, and that is not surprising, given that some have very large, well-articulated capital programs, such as Health, which has a 13-year program. We know what they want to deliver and when and so on, so we can work very clearly in that space. Other agencies, and sometimes smaller agencies—culture and the arts, for example, gets a new theatre in its program. It is not very often that it has to deal with a project of that magnitude, and it does not necessarily have the capability set to do that. So in those circumstances we now take a much more active role in ensuring that, basically, they articulate the service delivery need to us, and then we try to make everything happen from there. But in those circumstances it is a very close partnership between us and the relevant agency.

The CHAIRMAN: In some cases, with agencies that have experience, are you happy to leave more of the process to them, whereas with others you have to intervene to assist? Is that part of the picture, or is it really one size fits all in terms of agencies?

Mr Marney: No. If agencies have the capability set and we have confidence in their capabilities, then different elements of the process they will take greater control of. But, as you will see from the schedule that I will provide to you, as I have said, there are about eight steps in the process of delivering an asset, and the baton changes a number of times through that, even to the extent that different areas within Treasury and Finance have different roles in different stages of that process. For example, 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. That will then go through a decision process of government, and the Treasury business will come over and critique that and make sure that we have everything covered, that risks are fully identified and that there are strategies in place to mitigate those risks. That is something that we internally are working through as well in terms of who does what at different points in time and who is accountable. I guess the clear accountability, though, is with me, because I cover both those businesses.

Ms R. SAFFIOTI: Just picking up on the member for Carine's comments regarding processes that have changed, two of the big projects that the government is undertaking, the waterfront and the Northbridge hub and Link projects, are probably, in a sense, high risk in respect of capital exposure or possible blow-outs. Do they fall under the works portfolio of DTF—are they brought under that scope or again do they remain with their home agencies?

[3.40 pm]

Mr Marney: We have very close involvement in those projects through the strategic projects business and I think we chair or co-chair some of the supporting committees to those projects. But fundamentally those two projects are the responsibility of the relevant agencies involved, so in the case of the link, PTA and EPRA have the primary carriage of those projects.

Ms R. SAFFIOTI: In respect to the link and hub—I think hub being the public transport component and the link being the urban development component on top of the rail line—was Treasury again consulted before a decision was made to fund those projects?

Mr Marney: We were consulted and we have been given the opportunity to provide advice through to ERC and cabinet in the process, but essentially both the Northbridge project and the waterfront project, again, were articulated priorities of government where our scope in the process was really to assist in identifying factors that need to be taken into consideration and we have a small part in now just getting on and delivering those projects.

Ms R. SAFFIOTI: So again similar to Oakajee, advice is being sought on how to make it happen, rather than if it should happen?

Mr Marney: In the case of those three projects, the scope of our advice was predominantly around what is the best way to make them happen.

Ms R. SAFFIOTI: This sort of again relates to the first list of infrastructure priorities put forward by this new government in, I think, October 2008—the list of five priorities, I think, that was put forward in which Oakajee and I think the hub and link were two components. That list was coordinated by DPC and sent to the Rudd government or Infrastructure Australia. Was Treasury involved in the production of that list of priorities?

Mr Marney: We assisted in gathering the information for the individual projects that were outlined by the government as their priorities for submission into the Infrastructure Australia process.

Ms R. SAFFIOTI: I suppose given your experience, given that you have put in works, given that Treasury now oversees, basically, the capital expenditure and capital prioritisation process of government, were you asked for your advice from DTF on what the infrastructure priorities of the state should be in that submission to the commonwealth?

Mr Marney: From memory, we provided a listing of possible candidates for that process in terms of projects and then those projects were shortlisted by the government as to those that they chose to put forward in that process.

Ms R. SAFFIOTI: Would it be possible to get a copy of the list that you provided to government?

Mr Marney: I am pretty sure we provided that list to cabinet, but I will check.

Ms R. SAFFIOTI: Okay, if we could ask whether Mr Marney could consider whether he could provide the committee with the list of infrastructure priorities submitted as part of the Infrastructure Australia funding round.

Mr A. KRSTICEVIC: With DTF at the moment, obviously, do you now have an understanding of all the projects that are currently out there and their costings and where they are at in terms of the state's finances? The reason I ask that is because I have heard statements made before in Parliament about the fact that Treasury or the government did not know all the projects that were going on, how much money was being spent or overspent; there was no control of the finances—there was lots of money coming in and lots of money going out, but no-one really had a grasp of what was going on in the state. Firstly, was that the case and, secondly, if it was, have we done something to correct that and does someone now know exactly what money is being spent where and how that is affecting the state's finances?

Mr Marney: I think it is fair to say we have always known what money is being spent where—let there be no illusion in that regard. Whether or not we were able to provide a consolidated list at a point in time of the status of each project, the cash flow to that point and the time frames around each project is debatable and remains debatable because the works business covers only a portion of the total asset investment program. As highlighted previously, there are projects that sit outside of

Treasury and Finance's control, if you like, or accountability and that is appropriate—you have Main Roads projects, you have Water Corporation, Western Power and so on. We have a much better consolidation of the projects within the general government sector because we have, I guess, imposed some uniform reporting across those projects. Having said that, it is still not ideal; we still do not have, I think, the supporting systems behind our project management that would be warranted of a capital program that runs into $3 billion to $4 billion per annum. So we have some investment, some work to do, to get our system to a point that are suitable to support the asset investment program.

Mr A. KRSTICEVIC: But you have got a plan to head in that direction?

Mr Marney: Yes, and that is articulated in the works reform plan that was published last year.

The CHAIRMAN: Can I take this up and follow on in terms of the problem of banging into the wall of debt? Clearly, while you may have limited control over some agencies, as you said, the trading agencies, at the end of the day it goes into government debt and then that comes back to you in terms of how the state is going to manage that. So can you make any comments about that? I will just give you a simple example of the recent announcement regarding the Merredin wind farm. Is that an issue where Treasury was able to have input in terms of what impact debt management has into the future?

Mr Marney: I probably know that project by a different name, so I cannot comment on the specific project. But suffice to say, we do have oversight and that relative evaluation process goes across those projects in a comprehensive way. The debt implications associated with projects in the government trading enterprise is taken into consideration in the government's fiscal strategy and its articulated financial targets. Those targets are based on our discussions with the rating agencies over time in terms of their, if you like, tolerance limits around some key parameters like debt and expense growth.

The CHAIRMAN: So the issue is: do those projects have to come back through Treasury to EERC or round to cabinet? How do you handle those government trading—I think the project is called Collgar.

Mr Marney: Collgar Wind Farm. Those projects are usually considered by ERC and advice is then provided from ERC to cabinet as to the best way to proceed or not proceed, whichever the case may be.

The CHAIRMAN: Have any projects actually had the tick off without going through that process?

Mr Marney: In what sense? In terms of not going to ERC or —

The CHAIRMAN: Yes; projects involving expenditure, say, particularly by government trading enterprises, which involve large amounts of money that could impact on state debt, which actually did not go through EERC?

Mr Marney: Not to my knowledge.

The CHAIRMAN: I would like to get a bit of guidance on PPPs. I think the Collgar project is a PPP.

Mr Marney: Of a form, yes.

The CHAIRMAN: Taking it in the widest range.

Mr Marney: Yes.

The CHAIRMAN: So the government clearly has indicated its interest in public–private partnerships, is there supporting documentation in terms of the guidelines that go with that or have they simply rolled over that which was put in place by the last government?

Mr Marney: I do not think we have reissued a suite of policy guidelines. There is substantial work in progress at the moment to clarify the policy settings and processes that are to be followed in the exploration of PPPs.

[3.50 pm]

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.

The CHAIRMAN: With respect to that, if I could use an example such as the wind farm, or even a prison, where a form of PPP is used whereby the government will actually have the prison, or wind farm, built by a private operator. Does that actually equate to a capital cost to government that then becomes a recurrent expenditure as it is paid for each prisoner or for each kilowatt hour? Does the money become due only when the service is delivered?

Mr Marney: Is the kilowatt hour expended on the prisoner? No; we have moved on.

The CHAIRMAN: We have not gone that far yet.

Ms R. SAFFIOTI: Not in this state; not yet.

Mr Marney: 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.

The CHAIRMAN: In terms of how it shows up in your books, the building of a prison would clearly be capital; whereas, if it is a privately run prison, does it show up on the capital side; or does it show up on the recurrent side because you are now paying for the service being delivered in terms of the control and incarceration of so many prisoners?

Mr Marney: It would show up on the recurrent side through service obligations. It gets 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. I think that is AASB 1049, from memory; I can get you further detail on that to give you clarity around it.

The CHAIRMAN: I would appreciate it if you could give us some clarity around that.

Ms R. SAFFIOTI: As I understand it, when it is a PPP and the government is purchasing nearly 100 per cent of the service, then it should be on balance sheet. Is that right?

Mr Marney: That is one of the key criteria. Basically, the accounting standard says that if government is, by far, the majority purchaser of an output of a certain production process—take a wind farm for example—then the accounting standard kind of considers that government is actually buying that asset and the PPP is a financing structure for the purchase of that asset. I think that is the intention of the accounting standard, but I am happy to provide background on that.

Ms R. SAFFIOTI: So many different models are appearing at the moment. For example, Midland hospital has been described as a PPP, but in a sense it is privatisation because that model has been described as the one where, basically, the private sector designs, builds, finances and operates it. But if it does that but only has 50 per cent public patients, does that become an asset that does not appear on the balance sheet but just appears on the operating side? For example, the Midland hospital will be done as a design, build, finance —

Mr Marney: Design, build, own, operate private sector.

Ms R. SAFFIOTI: Yes. Will that appear on the balance sheet or will it appear on the operating side of the equation?

Mr Marney: Yes; I am happy to provide a briefing note on the accounting standard, its application, and how it would apply to various projects. I will give you a spectrum of those sorts of arrangements.

Ms R. SAFFIOTI: I think Princess Margaret Hospital has been described as something a bit different, whereby the government will be operating it, so, again, it is slightly different from the information about the Midland hospital that we have been provided with.

Mr Marney: Midland is complicated further by the fact that, I think, the commonwealth is putting in half the capital cost, so do they own half the asset and whose balance sheet is it on, and so on. I think it is fair to say we have a lot of work to do in both those cases to actually evaluate the best procurement and operational models for those facilities. 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.

The CHAIRMAN: While we are on the accounting treatment, thank you for providing that additional information. It may already be in what you have said you will provide, but if it is not, can you try to give us some idea as to the different models—because there is not just one—and whether you have to enter it into your books at the time you sign the contract, like for a prison; or if it is only actually when you start paying for the services, which might be two or three years later.

Mr Marney: You are right; it does vary. Sometimes it is not until you make your first payment that you end up having to bring those liabilities to book.

The CHAIRMAN: Back to the guiding principles, or the policies that will apply to PPPs, which you are saying are still being developed in terms of nothing actually being set in stone by the government in terms of the guidance for PPPs.

Mr Marney: We have existing policies and processes, but I think 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.

The CHAIRMAN: How important to that process will be some sort of comparator between the private and public model for a particular project?

Mr Marney: In the entire process, the ability to compare it with what it would cost you to do it yourself is absolutely critical, because otherwise how do you know whether or not you are getting a better deal? That is fundamental to the whole process.

The CHAIRMAN: Do you potentially see a range of comparator models or tools that will be used, or is there one that will really be the standard one?

Mr Marney: I think the standard tool is that you figure out what it would cost you to deliver the same outcome. How you estimate that depends on the particular area of service delivery you are dealing with, but 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. That is hard to do and it takes time. To do that well, it 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.

Ms R. SAFFIOTI: Midland hospital has been described as being a PPP. From your perspective, has the decision been made to have it as a PPP, and has the public sector comparison been undertaken, or do you still have to do that public sector comparison?

Mr Marney: As it has been communicated to me, the government is keen to explore the PPP option. I am sure that if it proved to be the case that, 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. 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. You cannot just blanket explore PPPs for every project. The government has articulated to me that Midland is a project that it wants to explore for PPPs.

Ms R. SAFFIOTI: Princess Margaret Hospital on which they had actually, I thought, given an election commitment to do it with public financing, so has that decision been made and do you see that now as Treasury justifying the PPP; or do you believe you still have a role in determining whether it should be public financed or private financed?

Mr Marney: I think we still have 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.

[4.00 pm]

The CHAIRMAN: In respect of projects that the government has currently earmarked as potential PPPs, is there any decision on whether or not a shortlist will be developed and then a couple of proponents, or even one, will be offered some direct financial contribution towards the cost of the project? That has been used on other projects in the past. Is there a policy decision in respect of the ones that are currently earmarked that any of them all go down that road of a reduced number of tenderers and then paying them to work out the cost of an actual deal?

Mr Marney: Not that I am aware of.

Ms R. SAFFIOTI: Still on the PPPs, I think you have a new unit in the DTF that is helping to organise and run the PPPs.

Mr Marney: Yes.

Ms R. SAFFIOTI: I think there was about $4 million to $6 million allocated—I might be corrected on that—in the midyear review document, I think.

Mr Marney: I would have to get back to you on the allocation. Essentially, we ourselves do 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 these things are rigorously planned, evaluated and assessed and that advice given to government is sound, robust and comprehensive.

The CHAIRMAN: I notice that you were involved with the only real PPP done in recent years, which was for the District Courts. I do not know if you know off the top of your head, because you cannot be expected to remember everything, but do you have any idea of how long that took in preparation and doing that preliminary work before there was a sign off?

Mr Marney: It was about 12 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. It was 12 to 18 months from memory.

The CHAIRMAN: Do you think that process was a good and efficient one or that perhaps we could learn from that and do it quite differently?

Mr Marney: The outcome was pretty good. I think the market was happy with the process. We could probably, certainly over time, 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. The District Courts, as far as I remember—I could be corrected—is a pretty vanilla kind of facilities management partnership arrangement. Other areas you might explore—for example, Midland health—could be quite complex in terms of the extent of private delivery and where that crosses the core public delivery, if at all.

The CHAIRMAN: The point of the question that I am getting at is that all governments that make commitments want to deliver on them in a reasonable time line, so although there are advantages in PPPs, if the upfront part of the process is going to take the best part of 12 months before you have got a contract, then there is a real risk that governments will cut that short and you will not have proper assessment, or otherwise they may pay the cost politically if they cannot deliver in time.

Mr Marney: That risk is always there for PPPs or normal, traditional construction. I guess what we have seen over the past decade or so is how planning up front is not as rigorous as it needs to be. 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.

Mr J.M. FRANCIS: Surely, though, if you have got a unit in Treasury now that is dedicated towards evaluating and, I guess, planning PPPs, if they go ahead, you would expect, having those resources, that the time it would take to do the evaluations would come down and the quality of the evaluations would go up if it is a specialist unit.

Mr Marney: You would expect that over time they will gain experience, learning and capabilities, but I would say you will probably have to do four or five of these things to actually start to build that capability so that will take, what, four or five years, if it is a 12-month cycle.

Mr J.M. FRANCIS: It is obviously only new, but has that unit looked at the processes that other states have used in going down the PPP path?

Mr Marney: Yes, we examine that from a number of different aspects, the best of which is poaching people from other states, which we have been reasonably successful at getting some good capabilities in. We have some very good experience from other jurisdictions to help us not only on PPPs but other areas of our works program, and we use the gateway review process is as an opportunity to learn from other jurisdictions in a pretty intensive way. As an example, I have a number of people who will be over east next week doing a gateway review on a health project in Victoria. They will pick up through that intensive review process a lot of learning as to what not to do back here. There are also a number of forums that the heads of Treasuries around the country have pulled together to share learning around PPPs and broader asset investment. I guess all of that recognises the fact that we have got a lot to learn.

Mr A. KRSTICEVIC: On that basis, I suppose from the delivery of infrastructure perspective as well as a financial perspective, do you think that DTF will be strongly encouraging government to use PPPs in the future as a form of delivery of that infrastructure?

Mr Marney: Where it demonstrates better value for money than traditional procurement, yes. 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.

Mr A. KRSTICEVIC: But also I suppose part of it is going to be the balance sheet and the ability to carry debt as opposed to revenue. I know you carry your balance sheet anyway.

Mr Marney: And that is the whole point. 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.

The CHAIRMAN: Thanks very much, Tim. I have just got some brief formalities to close with. I thank you for your evidence before the committee today. The transcript of this hearing will be forwarded to you for correction of minor errors. Please make these corrections and return the transcript within 10 days of receipt. If the transcript is not returned in this period, it will be deemed to be correct. New material cannot be introduced by these corrections and the sense of the evidence cannot be altered. Should you wish to provide additional information or elaborate on particular points, please include a supplementary submission for the committee's consideration when you return your corrected transcript of evidence and, at the same time, if you can provide us with the information that you have either undertaken to give or to have a look to see whether you can provide it to us. Again, I thank you very much for appearing before us and helping us with our inquiry.

Mr Marney: Thank you.

Hearing concluded at 4.08 pm