PUBLIC ACCOUNTS COMMITTEE

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

TRANSCRIPT OF EVIDENCE
TAKEN AT PERTH
WEDNESDAY, 8 SEPTEMBER 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 10.17 am

WARD, MR ROBERT DICKSON
Banker, Royal Bank of Scotland,
examined:

FUNDER, MR HUGH
Banker, Royal Bank of Scotland,
examined:

The CHAIRMAN: Welcome, and thank you very much for your interest and for giving us your time today. I have some standard formalities to go through. The purpose of this hearing is to assist the committee in gathering evidence for its inquiry. Our terms of reference are to look at state infrastructure projects and the decision making that goes into those projects so that we can get the best results, and also to look at whether we can get a better share of federal funding. You have already met the members of the committee. The Public Accounts Committee is a committee of the Legislative Assembly of the Parliament of Western Australia. This hearing is a formal procedure of the Parliament and therefore commands the same respect given to proceedings in the house itself. Even though the committee is not asking witnesses to provide evidence on oath or affirmation, it is important that you understand that any deliberate misleading of the committee may be regarded as a contempt of Parliament. This is a public hearing, and Hansard will be making a transcript of the proceedings for the public record. If you refer to any documents during your evidence, it would assist Hansard if you could provide the full title for the record. Before we proceed to the questions we have for you today, I need to ask you a series of questions. Have you completed the "Details of Witness" form?

The Witnesses: Yes.

The CHAIRMAN: Do you understand the notes at the bottom of the form about giving evidence to a parliamentary committee?

The Witnesses: Yes.

The CHAIRMAN: Did you receive and have you read the information for witnesses briefing sheet provided with the "Details of Witness" form today?

The Witnesses: Yes.

The CHAIRMAN: Do you have any questions in relation to being a witness at today's hearing?

The Witnesses: No.

The CHAIRMAN: Would you please state your full name and the capacity in which you appear before the committee today?

Mr Ward: Robert Dixon Ward. I am executive director, infrastructure advisory, Royal Bank of Scotland.

Mr Funder: Hugh Funder. I am senior adviser, infrastructure advisory, Royal Bank of Scotland.

The CHAIRMAN: I thank you for giving us some documents. We have not had the time to go through them yet. Would you like to make an opening statement, and then we will go straight to questions?

Mr Ward: I will start by explaining who we are and what we do. I will first give you a quick summary of what we do in public infrastructure, and Hugh can give you some of the theoretical underpinnings of some of the major project procurement that we do.

RBS has been operating in Australia for 35 years. We are one of six hubs in Asia–Pacific, and we have approximately 600 staff in Australia. We have a 50 per cent stake in RBS Morgans, which has an office here in Perth. The area in which Hugh and I operate is in the public–private partnerships team within the bank. Earlier this year we brought to a close the peninsula link availability road in Victoria, which was the first such road concluded in Australia, and we are currently bidding on five PPPs nationally that are in the bid process. They include the Royal Adelaide Hospital, the Victorian comprehensive cancer care centre, the Mundaring water treatment plant here in Perth, the Gold Coast light rail project, and the single LEAP 2 defence accommodation project. For probity reasons, we obviously cannot discuss the Mundaring water treatment plant and some of the details of those things that are currently in process and need to be kept confidential for commercial reasons.

Mr Funder: I have brought with me three documents for the committee that I hope will be useful in your deliberations. Two of those documents have a very specific Australian focus, and the other one is from Denmark, of all places. The first document that I will give to you is by a Danish academic with the strange name of Professor Bent Flyvbjerg. It is titled “From Nobel Prize to Project Management: Getting Risks Right”. In this document, Professer Flyvbjerg adapts Nobel Laureate Daniel Kahneman’s work on optimism bias, otherwise known as delusion, to major project procurement. He also introduces another factor that he calls strategic misrepresentation, otherwise known as deception. One of the keys to overcoming delusion and deception in Professor Flyvbjerg’s analysis is getting what he calls an outside view of procurement projections. We believe PPP is one method of not only getting an outside view, but doing it in a competitive environment where the risk of error is passed to the private sector. I also have two Australian-focused studies, both involving the University of Melbourne. One is a 2007 study that compares PPP and traditional procurement and finds that PPP is considerably more reliable in delivering large projects on time and on budget. The 2009 study, in which the Western Australian Department of Treasury and Finance was a member of the steering group, is focused on alliance contracting and includes a comparison between alliancing and PPP. It found that “PPPs provide greatest cost certainty at business case stage, followed by traditional, and then alliancing”. I hope the committee finds those analyses useful.

The CHAIRMAN: Thank you for that. Clearly, your role in bidding for and being a partner in PPPs is one area of expertise that reflects on what we are doing. But I am sure that because of your involvement in that, you also have a broader perspective. So I guess what I am hoping we can elicit from you today is matters central to PPPs as a method of procurement, but also the bigger issue of how you interface with governments when they are developing these projects, so that we can get some sort of outside view as to how we are going in Western Australia with our methodology for development projects. We have had a lot of evidence from government agencies. We have seen that from the inside. My personal comment is that there is lot there that I think we are doing very well. But we are also conscious of the fact that there are better ways of doing things, and other states have managed to get more money from the federal government than we have. So we need to look at whether our own internal systems are delivering best outcomes, and also how we present in terms of trying to get a better share from the federal funds that flow; and then look specifically at PPPs and the things that come off that in terms of the procurement and financing methods. There is a lot in the documents that you have presented to us. Would you like to give us a bit of a thumbnail sketch of where you see PPPs fitting into procurement by a government such as the government of Western Australia, and of what you see as some of the base issues that you look at in terms of whether the government that you are partnering with has got its ducks in a row? What are the benchmarks that you would look at to know whether you are dealing with a government that has got its act together, or one where you think there is a lot more preliminary work that you would like to see before you enter into that sort of partnership?

[10.25 am]

Mr Funder: One of the key things is the structure—in a sense the machinery of government—and we have seen that change here in Western Australia. We have seen a change with sort of an eye to Victoria; and that is, I think, a very good thing in our book. We have been working in Victoria since they introduced their Partnerships Victoria policy in 2000. The other states have come in behind that. We are very happy to bid anything in Victoria. 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. So one thing is the way they are procured, and that is something that has improved in Western Australia—the pipeline—which is perhaps medium in Western Australia. We then look to see that there is in a sense a political champion, and we have seen that change in Western Australia.

Mr Ward: The other thing we look for in the government's approach to PPPs is also that we acknowledge that only some projects are suitable for a PPP. We find that we are a long way from recommending that it be used as a cure-all for project delivery. The other aspect I would note would be scale, in that the generally larger projects as a rule are better suited to PPP 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.

The CHAIRMAN: When you approach a PPP, do you have a fairly standard process, or really is it on a continuum depending on the type of project and a whole range of criteria?

Mr Ward: I think the process itself is reasonably well established and standard, in that following the identification and announcement of a project as a PPP, the expression of interest process is reasonably standard across governments. It is generally a five to six week process, which then narrows the shortlist down to two or three bidders, usually, which is followed by a longer request for detailed proposal process, which may last anything from 13 to 26 weeks before bids are submitted. They are followed by often a second round if the bids are not exactly what the procuring department wishes, with a preferred bidder identified either after the initial bid or after what we call a BAFO, or best and final offer—there are very many acronyms that can be used. So that process itself is reasonably standard. The length of time that is taken by the process will be a factor often of the number of parties involved and the complexity of the project itself. For a school, the PPP will be usually a far more streamlined process than for a major tertiary hospital,

The CHAIRMAN: Just using a hospital as an example, do you have a threshold issue by which you judge in terms of how early you want to get in? A government may come to you and say, "We have got a location, and we want a 600-bed hospital; we have done nothing else; will you help us plan?" That is very different from a government that says, "We have had a report done over the last 18 months, and we have tied down not only the number of beds but also the specialty areas, the style of delivery and all the rest of it, and we have started to look at some of the costings, so we are well advanced". I mean, when you come in, do you want a project to be up to a certain level of definition and scoping, or are you happy to start at the very beginning and work through that with your client?

Mr Funder: I think 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, and then we can go away, price it, and perhaps innovate if we can, and come back to the state. So, in short, the state needs to know what it wants.

The CHAIRMAN: You want a well-defined project, not something that is pretty loose?

Mr Funder: Yes, well defined; and well defined can be defined in a sense in terms of the outcomes and outputs that are desired, and then the higher the level they are, the more opportunity there is for us to innovate around how they are delivered.

Mr Ward: Just to add to that, our experience is 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.

The CHAIRMAN: So you as a partner would be embarking on a risk to yourself in terms of expenditure for a project that you might not get if it is not well defined?

Mr Ward: It is not so much not getting it. When I say “risk transfer”, I mean once a project is under way, in a PPP there is substantial risk transfer to the private sector. The private sector is willing to take that level of risk transfer. But I think a project needs to be well defined in order to take the risks that we are asked to take in a PPP environment. The process itself is more frustrating if the project is not well defined, but that in itself does not necessarily scare us off. It is that getting a value for money outcome requires a level of definition.

The CHAIRMAN: While we are talking about risk, can you give us some indication of the mechanisms that you use to handle risk in a project where, for instance, there may be a lack of environmental clearances, so you do not know what additional costs are going to go into meeting those? So, where you know that there are key areas of risk in a project, they cannot be quantified early on, and to meet time lines you need to actually commit and get started, what are some of the mechanisms by which you handle that risk, and how is that shared between you and the other partner?

Mr Ward: Depending on the nature of the risk, one of our roles as a sponsor of PPPs is to allocate that risk without our consortium to the party that is best able to manage it. If there are site conditions or approvals, that would usually be the design and construction partner that we work with. We would address that risk in two ways. The principal way is extensive due diligence in terms of site conditions or processes that are required to seek approvals; and, secondly, the risk is either one that is able to be taken and priced by the D & C contractor in that sense, or it is something that we need to share with the state, and that is usually where the most interesting discussions and negotiations come into play where risks are less able to be identified and mitigated.

The CHAIRMAN: I think that some of my colleagues have some questions.

Mr C.J. TALLENTIRE: On the issue of projects that are suitable for a public–private partnership, is it fair to say that if a project is in an area in which you could have rapid technological change, that is a project that is therefore less definable, less predictable and perhaps less suitable, compared with a project that is fairly clearly visible—perhaps something like a freeway—where you know there is going to be ongoing maintenance, you know the specifications, and you know there is not likely to be technological change? Is one of the dichotomies the issue of technology or technological change?

Mr Funder: That is an issue however you procure. We procure across fairly long-term concessions, so it is perhaps more of an issue. We have seen that, for instance, in the UK with medical equipment, which is obviously something that changes over time in terms of scanners and so on, they use a concept called technological banding. So, if the best scan today is a 16 cut, and the norm is eight, they can say we want the norm in five years, and then again in five years and in five years from that, or we want the top. So we can handle that sort of stuff, and they are doing so in the UK. If you look at the schools that we have done, we do our best to make sure that they are technologically adaptable over the term of the concession. So that is in a sense getting them all cabled and getting them all ducted and ready for whatever might come along technology-wise, and we have special consultants who come in and do that for us.

Mr C.J. TALLENTIRE: Sticking with your example of hospitals, though, where you are doing this technological banding, it must be very hard to predict what the cost of what might be the best standard will be in five years' time.

[10.35 am]

Mr Ward: That is true. That is probably one of the harder areas of locking in prices in a PPP environment. To stay with the example of a hospital, within the hospital, the equipment is often categorised quite extensively. There are some areas in which it is better for the state to retain ownership and risk et cetera for certain types of equipment, whereas other equipment needs to be maintained and replaced, so the lifecycle is taken on by the private sector. There is quite a lot of extensive evidence of exactly that kind of discussion happening. Ultimately, the existence of technology risk within a project is not prime facie a problem for a PPP. Within a project, quite often there are different items in terms of technology that are best left within the PPP or taken on by the state.

Mr A. KRSTICEVIC: Just to move on from that technology aspect, when you get involved in projects, do you also give advice? I know that sometimes big projects are undertaken, and government departments can have tunnel vision in terms of technology and what they want, and they do not think that far ahead in terms of in two years' time when this project is delivered, it will be ancient. A lot of times we see staff with ancient technology, but they are signed into contracts that are long-term and it is going to take a long time before they can get out of them. That to me is an issue from the technology perspective, because as much as you may say you leave it to the department, do you have that advisory role as well as taking that extra step?

Mr Ward: We certainly offer our views to government in the course of the process. That is true. But the point you raise is one that we would regularly come up with. A tertiary hospital may take five years to construct, and with some of the items that go into the hospital at the end of the process, the equipment et cetera, the challenge we find in the delivery phase is exactly that—where they have specified something at the outset, and then they have changed their mind. That is inevitable. But we do seek to build in flexibility along the way. There are certain prescribed regimes within the project documentation whereby individual pieces of equipment can be changed and adapted and some flexibility can be introduced in that way. So there are ways and means of mitigating that issue. But it will never go away, though, because by its nature it is quite a long concession period, and small variations of that nature happen quite regularly.

Mr A. KRSTICEVIC: Do you find that that flexibility that you have comes at a reasonably big cost? I know that some of these contracts may change, and the cost of changing may be okay in some cases, but it may be twice what it actually costs to do that. I suppose there is a penalty there for the contracting parties not getting it right in the first place.

Mr Ward: In recent PPPs in which we have been involved, that issue has come up early, and prescribed pricing et cetera has been included in the documentation in terms of what margin can be applied to a piece of equipment and what mechanisms to allow the hospital and the state to procure outside the PPP should they not be satisfied with the price.

Mr A. KRSTICEVIC: Thank you.

Mr J.M. FRANCIS: So if you are building a hospital using a PPP, and you are procuring a piece of equipment in five years—it may be a CT scanner—do you just leave the part blank that says it will cost this much in five years' time, and then, when the shell of the hospital is fitted out and they are about to buy that equipment, they then buy a scanner that fits this band and apply so much margin to it?

Mr Ward: No. The price is locked in. If the scanner is in the specifications for the hospital—usually the health department would want to specify that it wants a particular scanner—that will be a fixed item of equipment in the fixed price.

Mr J.M. FRANCIS: Five years in advance, though?

Mr Ward: Five years in advance. Inevitably during that phase there will be elements of those pieces of equipment that they will wish to vary, and there may be savings or costs associated with that, and the difference would be that there is usually a good robust discussion between the private sector and government around what that should cost. There are mechanisms by which, if the pricing is unsatisfactory for whatever reason, they can withdraw that item from the specification and procure it themselves.

Ms R. SAFFIOTI: You have said that some projects are more suitable for a PPP than others. We just heard about the technology angle. Is it a question of big versus small, or are there other issues, such as economic infrastructure versus social infrastructure? Is there any information that you can provide as to whether some projects are more ideally suited to PPPs than others?

Mr Ward: I think the principal response to that would be the earlier comment that I made around it being a well-defined project, not so much in what exactly the project should look like, but more around what the output specifications for that project will be. That would be the first thing I would look at in terms of suitability. There is a question of scale in what is a reasonably busy PPP marketplace, and there are certainly fixed costs in terms of resources and time on both sides—the government and the private sector. I would suggest 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 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. So there is a scale question.

Mr Funder: I think there is fairly good evidence in Australia that the public sector gets good value for money, in both social and economic infrastructure, from PPPs, and has done to date in Australia; that is, over the past 10 years. You have probably read about some of the toll roads in the eastern states—the economic infrastructure—some of which we have been involved in. All those roads operate perfectly well, but the financiers lost a lot of money. So, the infrastructure is there. The risk transfer was definitely there. There was a lot of optimism bias, and perhaps strategic misrepresentation, from the traffic forecasters, which has proved itself not to be a science. But on the schools in New South Wales, we 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.

Ms R. SAFFIOTI: In respect to schools, and both the social and economic infrastructure, nowadays PPP is a term that is used to describe a range of contractual relationships. As I understand it, a classic PPP is one where the management of the asset is held not by the government but by the private sector body. Is that what you would classify as a classic PPP, and one where more advantages flow to government?

Mr Ward: Yes, I would agree with that in terms that 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; and by "core services" I mean the teachers —

Ms R. SAFFIOTI: The nurses.

Mr Ward: Yes, and the prison officers—the actual core delivery of the service. It is intended to facilitate that service but not provide that service within a PPP. 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.

[10.45 am]

The CHAIRMAN: Can I come back to the initiation of the process? Do you have a preferred model of presentation or expressions of interest from government? Would you be happy to embark on a project where you, perhaps, knew there were going to be 10 different proponents and you would have to pay all the up-front costs but you may not know, until you had done a lot of work, what your chances were, or do you like a pre-qualification process; and, if so, can you open up some of those issues for us?

Mr Ward: Certainly. The number of proponents at the expression of interest phase is not a concern to us; we are happy to be one of many at that point in time. As I said earlier, that phase is usually a four to six-week process and we do a substantial amount of work, but it is far from being a detailed proposal process where we engage lawyers, consultants and designers, which is where, I guess, the most resources and money is spent in a PPP process. The number of people bidding during the EOI process is not a concern to us. Traditionally, shortlists after that expression of interest phase are either two or three parties. Any more than that would be of concern to us, because of the level of resources we need to apply to a PPP bid. Furthermore, on the government side, I think the challenge of managing a detailed process with any more than three parties would require a huge dedication of resources, and, perhaps, be very hard to efficiently run.

The CHAIRMAN: Has the GFC changed your operation in any way or changed the availability of funding or the type of projects that you would put funding into?

Mr Ward: Yes, it has. The development of the GFC and how it affected the Australian PPP market has been a movement away from capital markets—bond financing—for PPP transactions, which was the principal provider of debt finance to PPPs prior to the GFC. The bond markets still remain, effectively, closed to PPP and structured project finance transactions. As a result, we have seen the banking sector—the actual project finance bank lenders—fill that role of debt provision. That has meant, I guess, a slightly different set of risk allocations and pricing et cetera for PPPs, and it has meant more parties around the table in the bid process. PPPs are being financed, and we have seen large transactions, such as the Victorian desalination plant, financed entirely by the private sector—albeit with some assistance from the state in the early phase. Two of the bidders on the current bid for the Royal Adelaide Hospital are providing private finance for that project. The availability of finance remains there; it is coming from different parties and it is priced less aggressively than it probably was pre-GFC, but the market remains open.

The CHAIRMAN: Obviously, you have an indicative rate of return; is that, in any way, public, or is that totally confidential, in terms of a general ballpark figure?

Mr Ward: No; that will depend on the nature of the project and who the equity providers are. Each one we work with has different requirements for particular projects; I am afraid I cannot, for commercial reasons, disclose what those parties dictate to be their benchmark.

The CHAIRMAN: Looking at the Western Australian government and your experiences here, you have indicated that having a government that is a willing champion is important, but are there any organisational ways or procedures as to how a PPP is approached by the government that you would like to comment on in terms of how the state has its act together, or things that you would see as, really, basic requirements for being able to do business?

Mr Funder: I think we have had a very good dialogue with the Department of Treasury and Finance, amongst others, over a number of years. Over the past 18 months or so they have changed their machinery of operation, and I think they have recruited—I think they have poached from Victoria and elsewhere. The courts project here was the first PPP, which is now operational and running well, and we are getting ready to bid for some others. I think we are confident that the machinery is there to do it well.

The CHAIRMAN: Part of the work of this committee is to look at how the government has structured itself to actually deliver projects and the decision making around projects. Would you be able to comment on that area, in terms of how you regard that structure from the outside? We have looked at it from the inside, and it would be useful to have a view from the outside about how easy that is to deal with and your assessment of how it is working.

Mr Funder: It was reassuring for us to see the works part of Housing and Works going to Treasury; instead of having two to deal with, there is one to deal with in terms of the old public works function, and we were pleased with that. In terms of the personnel, I think we have been very happy in our dialogue. We were talking to the Department of Treasury and Finance yesterday and updating them on what we are seeing elsewhere, and they updated us on what they are thinking and which projects might be suitable for PPP, and so on. There is good dialogue and good machinery, and we are very ready to go.

Mr Ward: I think we are encouraged by the developments over the past 18 months. For us to be active in a jurisdiction in PPPs—as Hugh, I think, mentioned at the outset—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.

The CHAIRMAN: Coming back to that comment about having a pipeline of projects, what are some of the basic reasons you want the pipeline?

Mr Ward: I think our past experience in some jurisdictions has been that early PPP projects are the most difficult; there were lessons learned on both sides of the fence during earlier PPPs—I am thinking back to the lessons learned in the Spencer Street Station project in Victoria and the New South Wales schools project. As each one is closed and moves on, we find that the processes and the quality of the interaction and outcomes improves as time goes on. An example would be the speed and efficiency of the process in the second New South Wales schools transaction, which I think was probably the fastest, from announcement to close, of any of the PPPs that we have done in Australia. That was as a direct result of the lessons learned and the hard work done in the early PPPs. For us, the knowledge that there will not only be an upcoming project, but a series of them over the coming years, encourages us to do the hard work at the front end and seek to have more efficient and more quality projects as time progresses.

Mr Funder: In your initial remarks you spoke about getting federal funding: one good change we have seen at the commonwealth level is the architecture of Infrastructure Australia and getting in place some common ways of doing things around Australia, and their attempts to get an Australia-wide pipeline. Part of that is what Rob spoke about, but the other part is to attract investors. Investors need to know whether it is worth looking at Australia and doing the due diligence, or whether it is just going to be a one-off project and we do not know what is coming next. I think there is a strong element of getting that offshore investment into these projects, both debt and equity, and being able to show them what is coming up.

The CHAIRMAN: The members of the committee visited the Central Court building, and we prepared a bit of an overview paper on that—I am not suggesting we are conversant with a lot of the details. Would you like to make any comment on how effective or efficient you believe that project was as a PPP? Obviously, it is now in the delivery stage, so it is an ongoing issue in terms of the services that are still being offered as part of that deal.

Mr Ward: I think certainly in terms of the procurement process itself for a first PPP in a state, it was quite a good process. I think we are of the view 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 operation is currently going, although we retain a role in that. For a first PPP, I think it was a very good outcome. From our perspective, if we had any dissatisfaction it would be that we are concerned that, with the passing of time, the lessons learned from that PPP would be lost to PPPs to follow.

The CHAIRMAN: With little knowledge from the outside, it would seem that one of the great success with that project was that it was, basically, built on time and on budget at a time when the state had very high inflation rates. I do not know if you are conversant with that, and how you were able to manage that when other projects—private and government sector—had huge blow-outs.

Mr Ward: I think that 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.

The CHAIRMAN: On the issue of how you deal with government and whether you have any preferences or what you see as advantages or pitfalls, do you have any preference for dealing with a central agency? You mentioned that you saw works being in with Treasury as an advantage, so from your experiences with other states, what are some of the issues you take on board when you are dealing with a particular agency, such as the roads department if you are building a highway, or do you deal with Treasury in a central organisation; what is the mix there and what falls out of the mixes in terms of a service delivery agency as the main proponents you have to deal with, or a central agency, such as Treasury, or the combinations?

Mr Funder: The Victorian model is horses for courses, I think, in that case. Where you have a big department, such as Health or Education, the health need or the education need is best understood there rather than in Treasury, and the technical specifications and so on. I think there we saw Treasury taking a quieter role in the procurement, but the project had already been through the gateway process on how it was going to be procured, so that Treasury, in a sense, have moulded how it was going to be done, and then who actually does it depends on what sort of project it is.

Mr Ward: I would add to that that I think that having a central body that is within government that guides the PPP process is very useful, because lessons learned in one sector—for example, education—can be transferred across efficiently to others, such as health. Because a government department may only procure a very large asset that might be a PPP every few years, it is important to have that central body, such as the Office of Strategic Projects here or Partnerships Victoria, to maintain that PPP knowledge and transfer it from one project to another.

The CHAIRMAN: Turning to a slightly different area: would you like to try to tease out for me, please, the various strengths or weaknesses of PPPs or alliance contracting for different types of projects?

Mr Ward: Certainly. The use of alliance-style contracting, I think, is best suited to projects that are less well-defined and require a further level of interaction with the private sector to establish what it is that the client actually wants, and where there are risks that are so unable to be identified and quantified that there is no meaningful risk transfer and seeking a fixed-price fixed-time delivery. I think it comes down to the level of definition around a project. If it were less well-defined, then alliance contracting would be entirely appropriate; if it were more well-defined, then you would get meaning for the risk transfer, and it would be a better outcome via a PPP process.

The CHAIRMAN: To give you a general hypothetical: how would you deal with a government that says it wants a project built in a very tight time line—because we all have political cycles that we have to meet—and where might you draw the line between saying, “Okay, we will take it on, but you're going to have a higher cost associated with risk", or saying, "Look, I think you'd better go to an alliance on that one because there are just too many unknowns in trying to deliver that project to the time line you're setting"?

Mr Ward: That is a difficult one to answer; I think it is a line of continuum, probably, as to where you would draw the line. I just make the remark that if there is a time-critical element to the project, then it would be more likely for government to achieve that time frame in a PPP environment than it would in alliance contracting. I think the evidence Hugh tabled from studies that have been done in Australia and overseas supports that proposition.

Mr Funder: I think there are generally two schools of thought and two schools of thought in Treasuries—that is, a Treasury-sponsored paper from a number of the state Treasuries. Alliance contracting is very non-conflictual, and it is preferable, I think, for certain types of people who do not engage well in conflict and negotiation. It is cost-plus, and cost-plus is less efficient than fixed time, fixed cost. I think the research, in a sense, indicates that if you are in a real hurry, alliance; but if you can avoid alliance, do so.

The CHAIRMAN: I really appreciate that you have given your time, and I have a few minor formalities to close off, but would you like to make any further comments on the discussion we have had?

Mr Ward: Not from me, thank you.

The CHAIRMAN: I thank you very sincerely for the evidence you have provided to the committee today. A transcript of this hearing will be forwarded to you for correction of minor errors. Any such corrections must be made and the transcript returned within 10 days from the date of the letter attached to the transcript. If the transcript is not returned within this period it will be deemed to be correct. New material cannot be added via these corrections and the sense of your 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.

Thank you again, and I particularly thank you for the written evidence you provided to the committee.

Hearing concluded at 11.02 am