



Submission to the

Public Accounts Committee

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1.0 Introduction

This paper has been prepared by Leighton Holdings Group to assist the Western Australian (WA) Public Accounts Committee with its 'Inquiry into Project Planning and Funding Applications for Major Western Australian Infrastructure Projects'.

The submission provides information about key areas that the Committee may wish to consider for the inquiry. The key issues, outlined below, are aimed at improving project planning and assessment processes and accelerating project implementation and delivery.

2.0 Summary

Key issues included in this submission include:

- The need for greater certainty around project pipelines.
- The benefits of streamlining procurement and approvals processes.
- The importance of reducing bid costs.
- The need to evolve the Public Private Partnership model from that used in other States if it is to be implemented successfully in Western Australia.

3.0 Key Issues

3.1 Providing greater certainty around project pipelines

One of the challenges facing the infrastructure market in Australia is uncertainty about upcoming projects. Uncertainty stems from not having enough information available about upcoming projects, or abrupt changes. For example, the new Children's Hospital was 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. In addition, the schools PPP was talked about for a long time, but there has been little movement.

Lack of planning and certainty manifests as:

- a boom-and-bust cycle in the construction and development sector;
- overall cost increases, wastage and inefficiency; and
- long term lack of confidence in the sector resulting in underinvestment, particularly in human resources.

There is a clear need for government to work more closely with industry to improve long term strategic planning. Government should also make information readily available, including timelines for future projects, to assist in planning and delivery.

As an example of what works well, the Hong Kong Government (HKSARG) is a leader in infrastructure planning best practice. The HKSARG has implemented a well entrenched, coordinated strategic planning system that underpins economic development. The system is based on the *Hong Kong 2030: Planning Vision and Strategy*, which guides future development and the provision of strategic infrastructure. The HKSARG has endeavoured to support the infrastructure industry through continual review of planning and approval procedures. This approach is more 'contractor friendly' (compared to Australia) and critical in order to develop a vibrant, confident and efficient infrastructure industry.

The HKSARG is continually reviewing its procurement strategies and has recently introduced a Target Cost Contract for challenging projects with significant technical difficulties. This involves selecting three contractors from an initial first round of submissions, then reducing this list to two bidders and going to open tendering from that point. This is effective because it gives contractors an opportunity to evaluate the project before spending money on the tender. The HKSARG is also responsive to industry needs. For example, when the cost of bonds increased during the Global Financial Crisis, the Government amended bonding requirements to ease the pressure on contractors. Dispute resolution is another area where the HKSARG has reformed policy to support contractors. Dispute resolution has increasingly moved away from arbitration. In many Government contracts there is now a built in mediation clause and a mediation process is established early in the project. Some of the terms of mediation included are that: each party bears their own costs despite the final outcome of the case; and mediation is compulsory for most projects.

3.2 Streamlining procurement and approvals processes

One of the primary challenges for the Western Australian Government is to streamline project planning, assessment and approval processes to expedite projects. Currently, these processes are unnecessarily time consuming and costly, and major projects take can take years to be delivered.

Each phase of a project, such as geological surveys, environmental approvals, design and tender, can take a number of years to eventuate. Under traditional delivery methods it can take as long to bid for a project as it does to build. The WA Government could consider streamlining approvals so that these processes can be undertaken concurrently.

Furthermore, the traditional model of procurement is limited in terms of rapid implementation and delivery of projects, as it requires long lead times. Under the traditional procurement model projects are often delivered over budget, late and involve disputes about quality, performance and risk allocation.

There are alternative models of procurement that may be appropriate to adopt (depending on the specific project) that benefit both client and contractor, for example, 'alliance contracting'. Alliance contracting involves bringing the contractor into the early stages of a project – at inception, when the feasibility and qualification studies are being conducted. It means skilled resources are available to public officials when they are scoping the design and throughout the project, supported by strong relationships and underpinned by common goals, trust and cooperation. Alliance contracting allows phases of a project to be undertaken concurrently rather than sequentially, which in turn allows faster implementation and delivery. Furthermore, both the client and contractors share the risks and rewards.

Alliance contracting is one of a range of procurement methods that is well suited to projects that need to commence quickly or have scope that needs to be developed progressively.

There have been a number of excellent projects delivered by alliance contracting. For example, the alliance team working on the \$61 million road rail separation in Middleborough in Melbourne's eastern suburbs has won awards for its innovative approach to project delivery. The project was delivered in four weeks, when similar projects normally take up to 18 months.

It is noted that the WA Government is now seeking delivery of certain select projects via alternative procurement models such as ECI, D&C and Managing Contractor. This approach will greatly assist with the development of better business cases prior to project sign off.

3.3 Reducing bid costs and improving contract conditions

A significant challenge for the Australian infrastructure industry is high bidding costs. High bidding costs limit the range of participants as fewer financiers and constructors are able to bear the risk of losing the bid, and the investment they have put into it. Increasingly, only large companies or joint ventures have the capacity to tender for large projects.

One of the problems is the selection of too many contractors in a bid. For example, in a recent Main Roads WA road/bridge project, there were six bidders, all with proportionately high individual bid costs of around \$600,000 for a \$30 million project. Governments also contribute to high bidding costs by short-listing teams to best and final offers rather than selecting a preferred bidder. Governments should recognise the current capacity limitations of markets and for larger projects and should consider moving quickly to shortlist no more than two bidders, as well as moving to a preferred bidder earlier in order to limit bidding costs.

In addition, lower tier contractors are selected to bid for major work in the building sector with what appears to be no genuine risk analysis. And while it is understandable that the Government will seek to deliver projects at low cost to taxpayers, contracts are awarded to the lowest bidder regardless of other relevant business and capability criteria. This may lead to future problems in delivery such as delays that will ultimately result in higher costs to taxpayers.

Another issue to consider is the inadequate level of cost reimbursement on major alliance contracts. For example, on a current project valued at around \$350 million, the bid will cost around \$7-8 million yet has a reimbursement of only \$1 million for the losing bidder.

Fairer bidding arrangements were implemented in Victoria for the desalination plant project. Under this bidding model, two consortia were shortlisted so collectively no more than \$80-\$100 million was invested by the private sector on tender preparation. There were also arrangements to contribute towards the costs of the losing bid, capped at 50 per cent or \$20 million. This kind of support reduces bidding costs and improves the tender process for bidders.

An additional issue is that the WA Government remains focussed on recruiting their own staff to manage infrastructure projects rather than using advisors as Governments do in the eastern States of Australia – this can impede project delivery.

3.4 Evolving the Public Private Partnerships model

Public Private Partnerships (PPPs) are valuable additions to the provision of national infrastructure. However, it is important to acknowledge the shortcomings associated with PPPs, particularly in relation to the sharing of risk.

Although the community has benefitted from good PPP infrastructure projects in other Australian States, in recent years most of the stakeholders have not. Some of the problems include:

- Investors have lost most or all of their equity.
- Contractors have not received the margins they would like.
- Merchant banks have suffered with debt issues.
- Governments have been criticised about toll levels, concession company failures and traffic calculating costs.

PPPs must evolve nationally so that they become true partnerships that recognise the demands of all the stakeholders. Furthermore, Governments and clients should ensure that processes are not made unnecessarily complicated or adversarial. The National PPP guidelines endorsed by the Commonwealth

Government address these issues, and the WA Government should be credited for using them.

The cost of project finance still presents a significant challenge, and requires Government to engage in a genuine partnership with the private sector to deliver projects. Without an evolution of the model, Government assistance in adding liquidity to the market or providing greater flexibility to sponsors to manage revenue risk, PPPs will struggle to be delivered.

There are a range of options to reduce the risk exposure of financiers and potentially increase willingness to participate in projects. These include:

- Larger upfront contributions from Government.
- Supported Debt Model (e.g. Queensland schools).
- Wrapped Government funding where the Government underwrites liquidity.
- Allowing partial underwriting at bid close.

Another alternative is for the Government to procure the project itself, via a design and construct or alliance model, and possibly sell the mature asset after ramp-up. All new infrastructure projects have an economic worth and make our economy more efficient and Australia more competitive.

The Government could also consider Infrastructure Bonds such as those that were effective during the 1990s in the delivery of the Eastern Distributor in Sydney and Citylink in Melbourne.

4.0 About Leighton Holdings

Leighton Holdings Pty Ltd is one of the world's major project development and contracting organisations, and is also the world's largest contract miner.

Leighton Holdings has its head office in Sydney, Australia. It operates in more than 20 countries including Hong Kong, Malaysia and Dubai.

Leighton Holdings owns six independent companies that directly employ around 45,000 people. These are:

- Thiess
- Leighton Contractors
- John Holland
- Leighton Asia
- Leighton International
- Leighton Properties.

Leighton Holdings provides a corporate governance structure and financial strength to enable these operating companies to compete effectively in the global market place. This structure includes setting policies and operating guidelines, reviewing risk management and performance, and approving of strategic development, acquisitions and investments.

The operating companies offer a broad range of project development and contracting services and skills to public and private sector clients across a wide range of industries and geographic locations. These skills include: engineering and infrastructure construction, infrastructure development (e.g. toll roads), property development and building construction (residential and non-residential), contract mining, and operations and maintenance.