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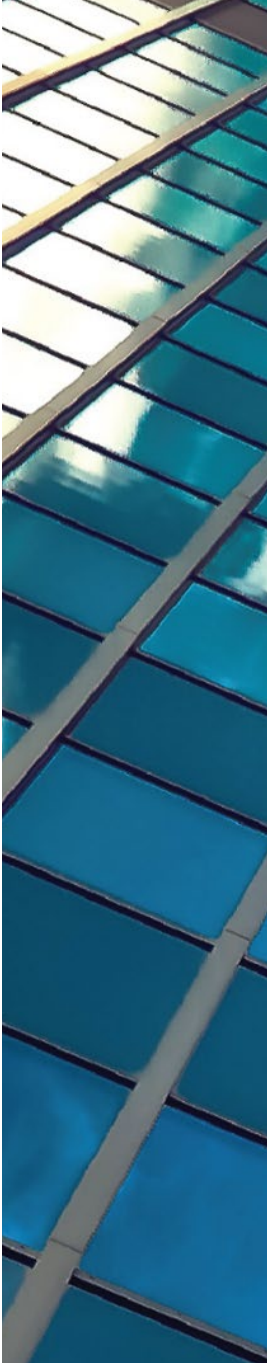


Public Private Partnerships

Optimising PPPs for infrastructure investments in the aftermath of Covid-19



Dr Daphne Freeder | Professor Shankar Sankaran | Professor Stewart Clegg | Professor Martin Locke | Dr Yongjian Ke



Acknowledgements

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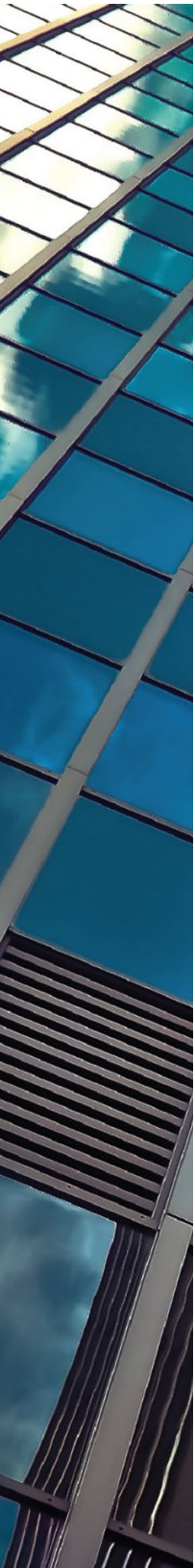
The organising team: Dr Daphne Freeder, Dr Marco Berti, Professor Stewart Clegg, Dr Yongjian Ke, Dr Samuel MacAulay, Professor Martin Locke, Associate Dean Vince Mangioni, Professor Shankar Sankaran.

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Program

9:35 am	Welcome	Associate Dean-Research and Development Michelle Baddeley <i>Professor in Economics UTS Business School</i>
9:40 am	Purpose of the workshop	Professor Shankar Sankaran <i>Professor of Organisational Project Management UTS School of Built Environment</i>
9:50 am	Presentation on PPPs	Adjunct Professor Industry Martin Locke <i>UTS School of Built Environment</i>
10:00 am	Panel Discussion with Q & A	Moderator Emeritus Professor Stewart Clegg <i>UTS Business School</i>
	Panel:	Sonya Campbell <i>NSW Treasury</i> Jeremy Gasparov <i>NSW Treasury</i> Malcolm McIntyre <i>Capella</i> Professor Elizabeth Mossop <i>Dean, UTS Faculty of Design</i>
11:00 am	Break	
11:30 am	Panel discussion with Q & A	Moderator Martin Locke <i>UTS School of Built Environment</i>
	Panel:	Julie-Anne Mizzi, Brian McGlynn - Malpine and Michelle Sichlau (Plenary)
12:30 pm	Close UTS HoS School of Built Environment	Professor Juaneé Cilliers
12:45 pm	Lunch	

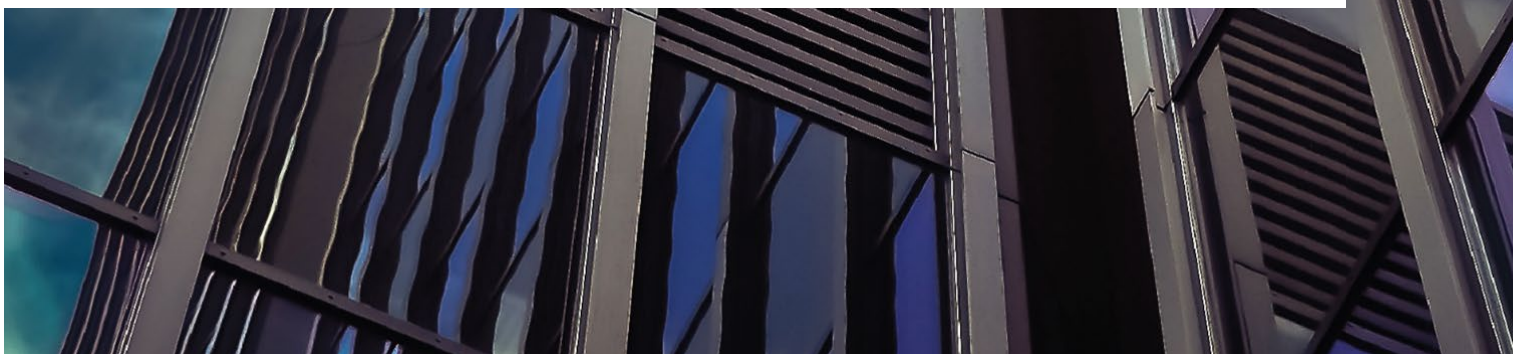


Abstract

With the benefit of multiple decades of experience in Public-Private Partnerships (PPP), it is a perfect time to consider how governments can leverage private finance to realise the opportunities that exist. Although private financing is not a panacea for insufficient government funding capacity, when properly utilised, it can be a highly successful and efficient procurement tool for delivering value to multiple stakeholders. The event brought together key players with real-life practical experience in delivering PPPs from public and private sector perspectives. The symposium sought to identify specific implementation issues that potentially impact PPPs and the ability of governments to leverage private finance in the post-COVID economy, consider solutions and develop courses of action for future acceleration in the use of PPPs. The issues explored included existing constraints against the selection of PPPs, the flexibility of the PPP model to respond dynamically to changing requirements of governments and the capacity to be administered simply. The symposium also surveyed the alignment between PPPs and the need to embed broad social outcomes, build community trust, demonstrate transparency and deliver quality to communities that extends beyond a project's financial targets. In addition, the participants considered the need to develop a more sophisticated model of risk allocation. The scope for developing a pipeline of investable PPP projects supported by investment capital from superannuation funds without compromising the need for robust business cases was also explored.

Introduction

The symposium began with an important question posed by Professor Martin Locke as to whether a fundamental problem exists in the context of PPPs and the potential for complacency in underestimating their value. This was highlighted with reference to the NSW Government's Stations, Systems, Trains, Operations and Maintenance (SSTOM) package proposed for Sydney Metro – Western Sydney Airport project. Despite the NSW Government having signalled that the SSTOM package was to be procured as a PPP, the call for Expressions of Interest (EOI) document indicated that Sydney Metro was open to considering alternative commercial frameworks due to market feedback, which signalled impediments to the traditional PPP model (IPA Newsletter, 4 June 2021). Other indications that PPPs suffer from obstacles include the abandonment of the Outer Suburban Arterial Roads (OSAR) Program and the absence of proposed school or hospital PPPs in NSW. The focus of the symposium was to consider how to avoid the demise of PPPs, as has occurred in the United Kingdom, due to the PPPs being deficient in social legitimacy, having a lack of transparency, comprising inflexible contracts, and over-complicated contract management. That PPPs can both deliver and create value rather than adopting a narrow focus on finance and risk but instead putting the major emphasis on social outcomes was a firm focus of the discussions. Critically, lessons learned from former PPPs need to be shared, and processes must evolve to meet current needs.





Comparing the value of a PPP versus a Design Build Operate Maintain (DBOM)


The traditional procurement process where a contractor is first appointed to build the project with separate subsequent contracting of Operations and Maintenance (O&M) can be replaced by the DBOM method where the same contractor is responsible for both construction and O&M. The DBOM model provides an integrated approach to whole-of-life project delivery but lacks the inclusion of private finance. The advantages of the PPP model compared with DBOM are:

- ▶ The PPP is structured around a capitalised contracting entity
- ▶ The extent of financial liability provides strong financial incentives for performance
- ▶ Financial discipline is introduced through the involvement of third-party financiers
- ▶ The PPP entity provides a single point of contact
- ▶ The PPP entity is responsible for interface contract management

Critical challenges for PPPs

The crucial components to making PPPs operate more successfully include simplifying and introducing more flexibility into contracts and simultaneously making them easier to manage. PPPs are hampered by too many Key Performance Indicators (KPIs), costs associated with variations and augmentation to contracts. These can be mitigated by introducing softer contracts, establishing provisional sums, collaborative contracting provisions, applying regulatory principles and implementing alliances with PPP Special Purpose Entities/Vehicles (SPVs). Improved contractual arrangements are also dependant on informed clients and contractors, embedding a positive and trusting culture.





NSW Treasury Infrastructure and Structured Finance Unit Perspective

Ms Sonya Campbell, Executive Director, Head of Infrastructure and Structured Finance Unit (ISFU) NSW Treasury and Mr Jeremy Gasperov, Associate Director, System and Market Stewardship at NSW Treasury, outlined their advocacy of PPPs and the importance of private financing. They also identified some of the constraints that they are facing. ISFU fully supports PPPs and are extremely mindful of the value that private financing brings. The role of ISFU in the Treasury is as custodian of the PPP guidelines for NSW. The audience was advised that ISFU has been reviewing and updating the current PPP guidelines since mid to late 2020. A consultation document with which industry can engage was issued in 2021 posing key questions from a market perspective directed explicitly at industry participants. Ms Campbell urged those attending the symposium to engage with the process when the draft guidelines are released.

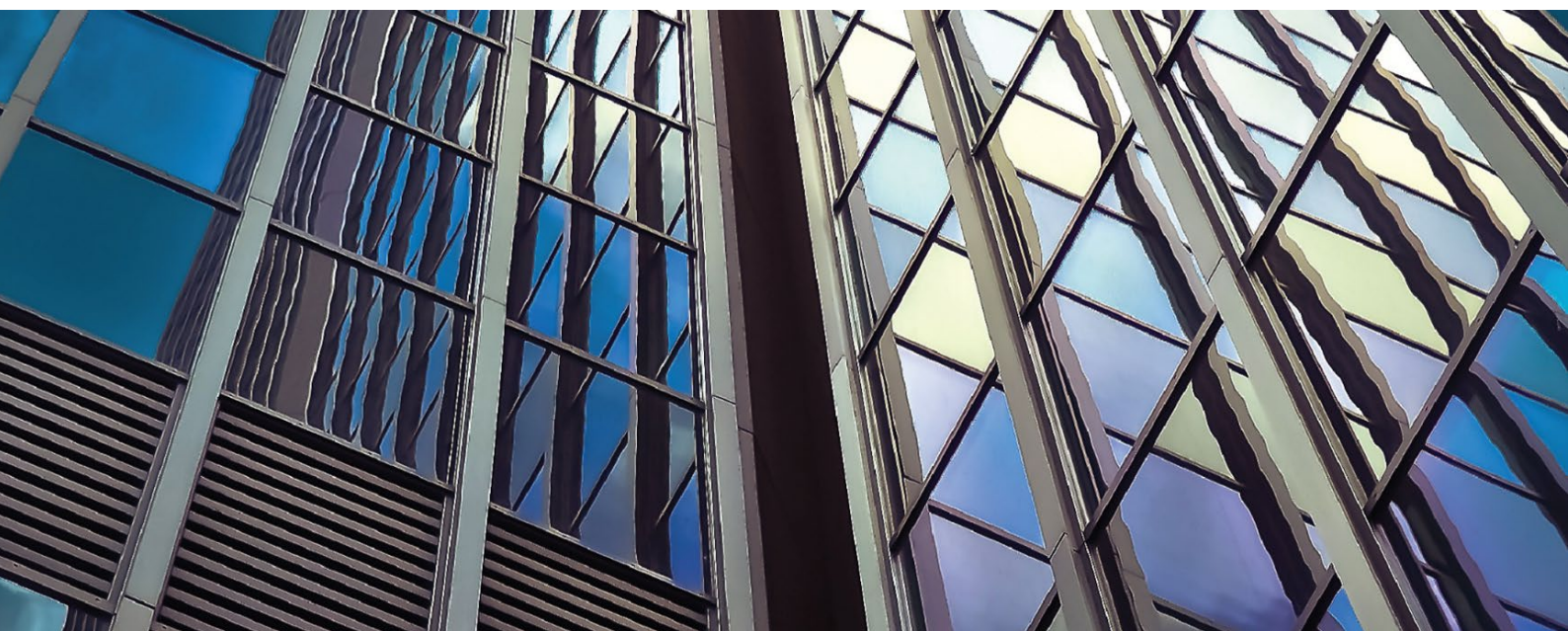
In their regular meetings with industry representatives, ISFU is often asked where the pipeline of projects is for industry members seeking opportunities to engage with the NSW government in PPPs, in areas such as health, schools, and social housing. Ms. Campbell encouraged industry participants to assist ISFU in playing their part as advocates for the

PPP model, particularly in the context of the impact of low interest rates and changes in the political context. The NSW Government altered its accounting standards in 2020, the net effect being the removal of any preferential balance sheet treatment for PPPs. What that means is that the government recognizes the cost of the net effect of a preferential balance sheet in the same way they would if it was state funded through the construction of the PPP. Advocates of PPPs would argue that this does not reflect the value of the PPP. While a PPP does cost more from a capitalised interest perspective, for government post-Covid debt headroom and balance sheet management are important. The question then becomes how can advocacy for the actual value of a PPP be exercised? This links to project outcomes, social outcomes and the certainty that comes with the whole life of such projects and their alignment with new asset-management policies for NSW. Ms Campbell acknowledged that flexibility in PPPs, dealing with changes more efficiently, as well as considering delivery model assessments, are critical components. Although the Western Harbour Tunnel project will be a state-led procurement, considerable work was done regarding PPP options. The tunnel project aligns with the demand risk of a PPP where

project value and project revenues will be higher or lower than expected, and industry has indicated its reluctance for such a model. This highlights the need to bring the market in early and engage with suitable options. Linked to Sydney Metro City & Southwest and Circular Quay Renewal projects, ISFU is working closely on a joint procurement review with Victoria, looking at simplifying processes, facilitating better engagement with the market, outlining the means to increase capability and support in the structuring and delivery of projects with the view of establishing a common approach between the two jurisdictions.

Mr Gasperov outlined how the Circular Quay project in Sydney, which involves a renewal of the three wharves and transport interchange as well as the transformation of the public spaces, has demonstrated the NSW Government's willingness to do things differently in procurement. The typical process

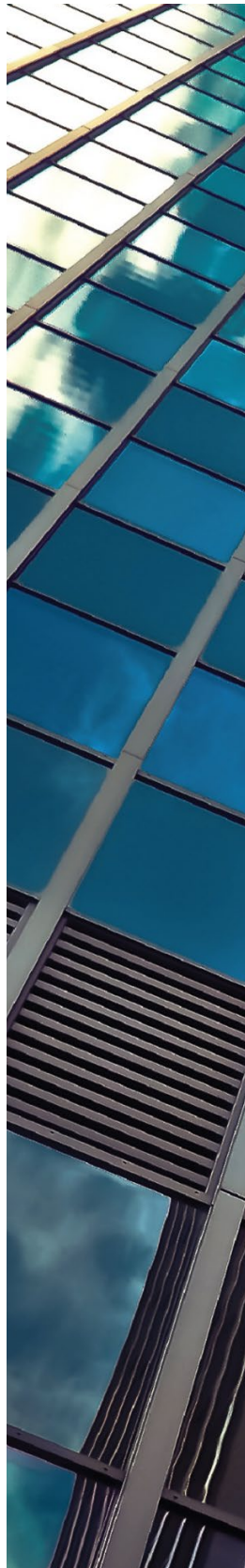
of project development has been that the state develops a concept design in-house and a couple of years later, a business case is produced; then, a final investment decision is made by the government before going to procurement. The consequences of such an approach means the market, competition landscape and regulatory changes alter since the conception of the project and costings will also be inconsistent. In essence, this process entails a lack of live market engagement. By contrast, procurement and business case development are running parallel in the Circular Quay project, and currently no investment decision has been made. It is a market-led procurement process bringing together the expertise and capacity of government and the private sector, focusing on encouraging early innovation for input into the business case with a view to embed greater cost certainty, de-risking through a sharing mechanism and early enabling works.

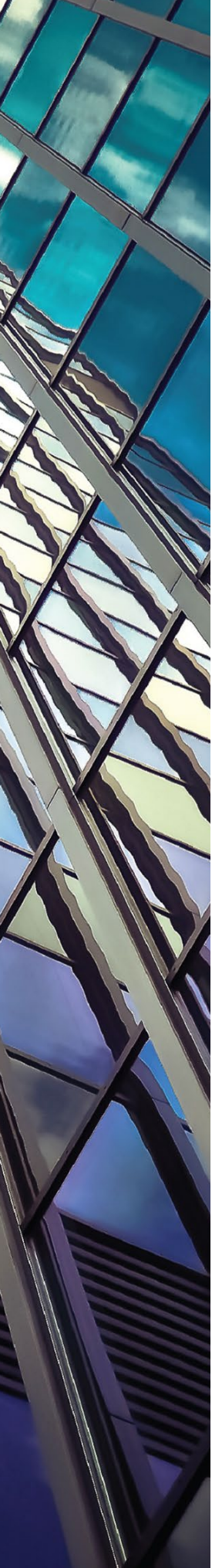




An Industry Perspective

Mr Malcolm McIntyre from Capella Capital concurred that the focus of projects needs to be on social outcomes, not just financial ones. He highlighted that the Darling Harbour redevelopment project, totalling about 5 billion dollars end value, brought together a broad range of experts, such as numerous master planning architects, engineers, convention centre and hotel operators and gave them the opportunity to develop a bid, which meant that the government would be buying an outcome. Putting all of these people in the room over a period of five to six months to come up with a bid, 'that's where magic happens' (McIntyre, 2021), where innovation occurs and the engineers and professionals sitting in that room are not just looking at the three-year delivery phase but how the asset is going to perform over twenty-five years and how the business case for the facility is going to be driven over the twenty-five years. Over the past twenty years, projects have expanded beyond relatively simple availability metrics for a PPP to complex outcomes such as urban renewal, for which the Darling Harbour project stands as an example of value capture. It wasn't just the infrastructure but a whole new precinct that was developed. Mr McIntyre also emphasised that it is vital that those involved in the initial phases of a project and do the deal have 'skin in the game' throughout the delivery of the project.

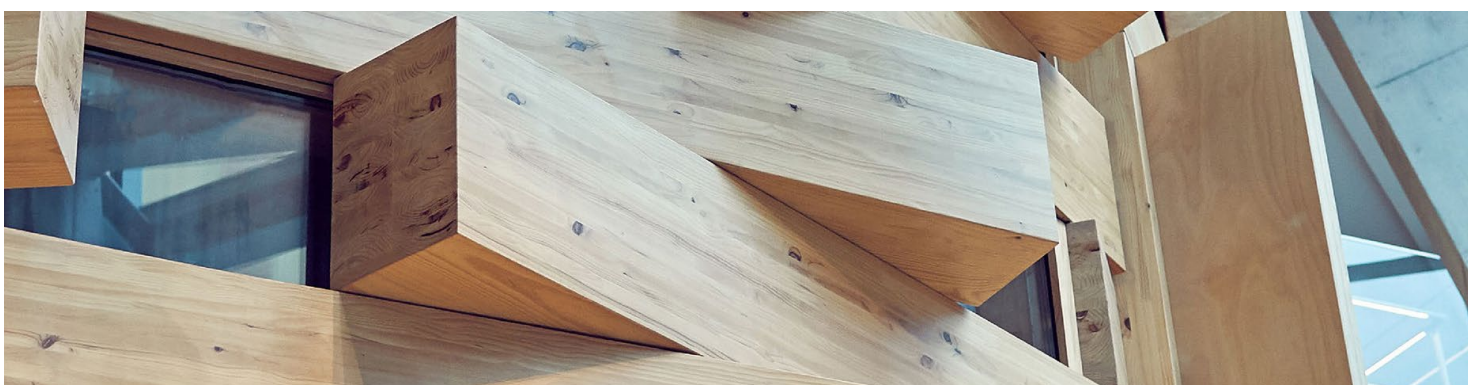




An Academic Perspective

Professor Elizabeth Mossop (Dean, UTS Faculty of Design Architecture and Building) presented an alternative view on key considerations for project outcomes; identifying that the biggest projects that we undertake, particularly in the space of city-making, despite having extremely clever people with diverse expertise, often fall short in the way that such projects are thought of and hence in how these projects are then approached as they are articulated. Legislative constraints and political environments play a hand here. Government, by its very nature has silos, despite attempts to mitigate these; consequently, this has an impact on the stated aims of individual projects and ensuring broader social project outcomes. Professor Mossop urged that all discussions about social effects need to be raised to a higher standard, particularly in relation to how we talk about, define and evaluate public good. Professor Mossop cited the example of building freeways and their implications for enormous parts of the City and while acknowledging that financial questions need to be satisfied as well as efficiencies of car movements and broader considerations. These broader considerations relate to what freeways do or don't facilitate in the context of open space and other kinds of access as well as their physical impacts, including separating areas in communities. Quality of life in Sydney, over the past twenty years, has arguably been massively reduced and there needs to be more thought about radical innovation and change. Factors such as climate considerations and social inequality can no longer just be relegated as political questions and problems outside of project scope. Procurement methods that lend support to these goals beyond a more traditional set of financial KPIs need to be found and a business-as-usual approach cannot be continued. Mr McIntyre responded to the discussion and pointed out that procurements are designed by government. However, as a bidder on projects, he sought to convey that they considered it necessary to win the hearts and minds of the community in any project that they engaged with and thus

focused on ensuring broader benefits. In any major interaction with a big infrastructure project, the focus of government is on how we deliver more, address community expectations and build community commitment. Sustainability targets are also a key focus. Mr McIntyre considered that the Cross City Tunnel project provided an important lesson to everyone in industry because although it was acceptable in terms of a piece of transport infrastructure, it did not satisfy the public good. Decisions made along the way did not take into consideration the impact of road closures on the community. Ms Campbell acknowledged that complications arise in consequence of projects being promised within an election cycle and the associated politics that this entails. However, there are attempts in Treasury to mitigate these factors. Ms Campbell advised that, for the first time, the government will be running an interactive EOI process for a PPP to help inform the tender documents before they come to the market. This will help to understand the risks associated with a project from the early stages and how these might be managed. An audience member commented that when government talks about engaging with the market, feedback is dominated by construction companies. According to his calculation, the range of net present cost of operations versus construction varied between forty and fifty per cent of the total project and yet when government consults with the market about what to do with PPPs, they consult with construction companies notwithstanding that the major problem with construction companies is that they don't know how to manage projects.



What is the value that private equity and finance brings?

Ms Julie-Anne Mizzi saw advantages of PPPs with reference to social outcomes and social benefits. She drew on her experience of running the AMP Community Infrastructure Fund, handling sixteen assets, all operational PPPs, encompassing 1.3 and a half-billion dollars' worth of equity. The projects involved many people within society and Ms Mizzi posited that the benefits achievable through a PPP outweighed those attained through traditional procurement.

She referred to several examples. The Victorian Comprehensive Cancer Centre (VCCC) project, rather than looking like a hospital, is more akin to a high-end hotel. The entryway has a

beautiful organic food cafe and people can sometimes feel like they are lost because they do not realise that these amenities are part of the hospital. The colour of the building is purple, as extensive research identified that the purple colour aligns with providing inspiration. Three research centres from across Melbourne have been brought together in the hospital, allowing cancer researchers in the facility to have direct contact with patients, even serendipitously, through travelling in the lifts, encounters that can directly influence their research. There is a dedicated adolescent space. The hospital offers a full kitchen for families to come in and cook favourite meals for family members who



<https://www.aurecongroup.com/projects/education-research/south-australian-schools-ppp>



Victorian Comprehensive Cancer Centre (VCCC) Project

are patients. Ms Mizzi posed the question as to whether anyone knew of any government procured hospital that offered such amenities.

The South Australia Schools PPP involved the closure of fourteen schools in a relatively low socio-economic area in Adelaide. They were replaced with seven super schools with facilities that extend from day care to Year 12. The largest school has three campuses, one single-sex girl school, one co-educational high school, and the third is a special needs school, with students from the original schools attending these. A principal from one of the former schools reported that seven years ago, the matriculation rate for Year 12 was 57 per

cent but by 2019, this had shifted to 100 per cent.

The Auckland South Corrections Facility, built with a KPI focus on reducing recidivism, has achieved a 37.5 per cent reduction in prisoners reoffending. All prisoners are provided with iPads so that they can contact their families each night to keep the connections. Little children going through the security screening process were encouraged to treat it as a game.

Plenary representative Ms Michelle Sichlau proposed that private finance adds real value because the focus is on outcomes and the whole life of projects and that PPPs offer

process rigour. When asked what should be done differently, Mr Brian McGlynn from Malpine identified, perhaps controversially, that based on his experiences, he would avoid having a construction contractor in the boardroom due to the conflict in using equity to pay for contract variations. KPIs also need to be consistent and realistic to reflect a real partnership and not be gold-plated for the government user. To highlight this, the distinction between what happens in government-run medical facilities was contrasted with an incident in Grafton Correctional Centre. Three among one hundred thousand patients are given the wrong medication to such an extreme extent that these occurrences are officially reported to the Federal Government. However, these figures do not reflect the actual number of instances. By contrast, in the Clarence Correctional Centre, operating under a PPP involving the State Government, significant financial penalties result from errors in medication. Mr McGlynn pointed to the contrast

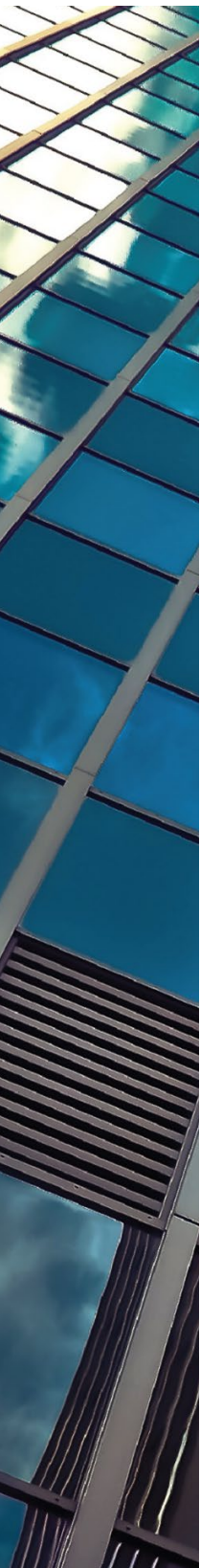
in expectations where a private operator was expected to perform better than every hospital in the state in providing medication to patients.

To facilitate workable contracts, it is necessary to have people from the government who are skilled and know what they are doing negotiating agreements, people with experience who have sufficient delegated authority to deal with the contract requirements.

Ms Mizzi suggested further changes to improve existing issues. Along with the procurement process, there should be a point system to encourage delivery of specific outcomes, some of which link to governance; there should be a limitation on the number of equity partners to simplify governance and, ideally, contractors should be absent. Companies that offer unrealistically cheap construction prices and have a record of trying to win back profit through legal claims should be avoided and not allowed to tender future bids. Longer term debt should be encouraged rather than short-term finance.

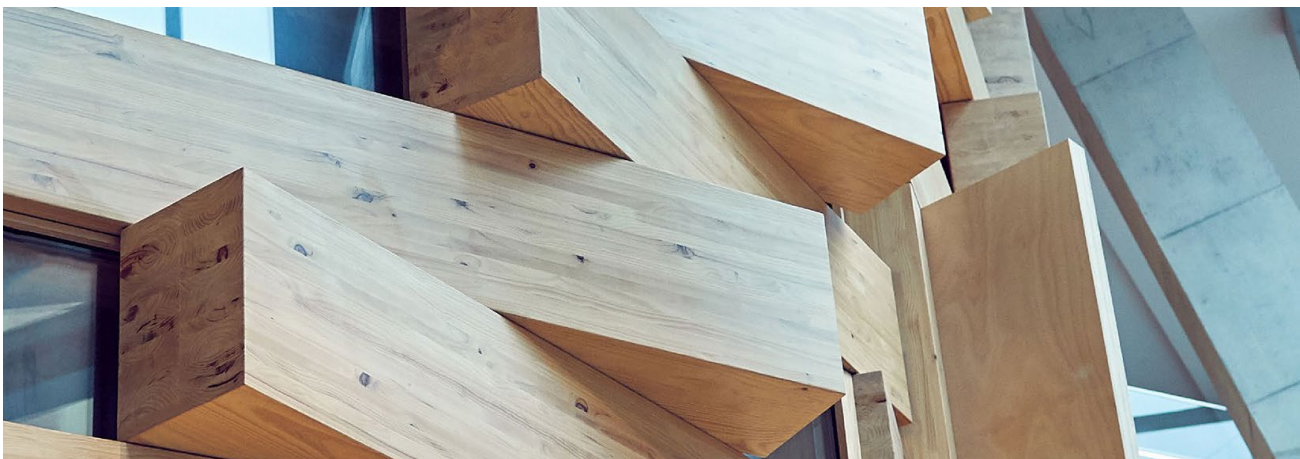


Auckland South
Corrections Facility



Conclusion

The symposium provided an opportunity for a robust discussion of PPPs and considerable networking opportunities. Participants provided specific options to improve PPP practice, identified from both private and public perspectives, to lead to improved partnerships in any projects pursued. Similarly, those present highlighted the value of introducing simultaneous design and procurement processes to reduce risk, embed innovation and establish more realistic financing. A joint narrative between industry and government about the success factors in PPPs also needs to be promoted to avoid the simplistic depiction that the public sector is good and the private sector is bad.



Future Work

The symposium and two subsequent international webinars will also contribute substantially to a new book titled **“Infrastructure Development: A Critical International Perspective on Value in Public-Private Partnerships”** with Edward Elgar Publishing, which will provide a critical international perspective on the public value of PPPs through case studies from a wide range of countries. The chapter contributors are from Australia, Canada, China, Finland, Hong Kong China, India, the Middle East, Netherlands, Norway, Singapore, Spain, the United Kingdom, and the United States.

The book is structured into three sections. The first is a collection of country overview chapters that describe the origin and drivers for governments to adopt PPPs, an overview of PPP development history, PPP-related policies and frameworks, and a current market overview. The second section includes successful case studies, which describe how the projects were planned, procured, and implemented. Achievement of public value and success factors are discussed. The third part contains failed or not-so-successful case studies, which summarise and discuss the reasons behind the failure and areas for improvement in these projects. The extent to which expected public value has been achieved, any observed value conflicts and associated coping strategies are also outlined.

