PARLIAMENTARY INQUIRY INTO PUBLIC PRIVATE PARTNERSHIPS

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October 2005

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INTRODUCTION

The NSW Public Accounts Committee (PAC) announced on 3 September 2005 that it would be holding an inquiry into 'private sector investment into public infrastructure', considering the following matters:

a. New South Wales, Australian and international legislative and policy frameworks and practices regarding private sector investment in public infrastructure;
b. Government models for evaluating and monitoring private investment in public infrastructure;
c. The framework for risk allocation between the public and private sectors and its application, especially how well risk is assessed, allocated and managed;
d. The extent of opportunities to share knowledge across and between agencies;
e. The extent to which agencies are managing Intellectual Property issues; and
f. Any other relevant matters.

These Terms of Reference are very broad, and in some senses, the listing of items from (a) to (e) suggests (it is hoped, erroneously) that the PAC is more interested in:

- whether NSW policies and practices are *in line with practice in other jurisdictions*; and
- the processes surrounding the implementation of current policies;

rather than:

- whether NSW policy and practice are appropriate and in the interests of the citizens of NSW; and
- whether continuation of those policies is likely to have adverse effects on current and future generations.

This submission commences not with item (a) but with item (f) which is restated as

f. relevant matters, not [directly] identified in the committee's terms of reference.

These 'relevant matters' include the following:

- need for a review of the condition of the State's infrastructure – and what it will cost;
- public private relationships are not new but intensified and changed in recent years;
- PPPs as a form of financial engineering;
- consequences of PPPs.

This submission which has been prepared by Centennial Consultancy (see Appendix A) first addresses these 'relevant matters', followed by a number of the terms of reference set by the PAC.

It should also be noted that the 2005 ALP State Conference called upon the State Government to hold a Public Inquiry to investigate all aspects of PPPs and that such an inquiry should be chaired by a prominent and impartial person having economic and financial expertise and absolutely no vested interest in the outcomes of the inquiry (see Appendix B).

SUMMARY AND RECOMMENDATIONS

1. NEED FOR A REVIEW OF THE CONDITION OF THE STATE'S INFRASTRUCTURE AND WHAT IT WILL COST TO FIX IT

- One of the primary responsibilities of State governments is to manage, upgrade maintain and renew infrastructure, much of which was inherited from the activities of prior governments, and was paid for by previous generations of taxpayers.

- The NSW State sector has infrastructure assets exceeding $80 billion (at book values).

- Accounting practices do not recognise backlogs of infrastructure maintenance as liabilities.

- Possibly because information about emerging needs for infrastructure maintenance, remediation and upgrading have not been compiled and published for public scrutiny, successive State Governments may have failed to provide adequate funding to maintain infrastructure. That, in turn, may have led to increasing deterioration in legacy infrastructure and increasing back-logs of much-needed projects – and a corresponding escalation of the funding required for maintenance and capital expenditure.

- While the State Infrastructure Strategic Plan 2002, that listed a range of potential projects is a start, what is needed is a comprehensive audit of the condition of the State's infrastructure in order to assess what it would cost to at least restore legacy infrastructure to a satisfactory condition.

- NSW pioneered the development of annual assessments of the condition of infrastructure - but only for local government. After a decade of experience with the use of this management tool, local councils appear to be developing more consistent and meaningful estimates of the funds needed to restore and maintain infrastructure to an acceptable standard of functionality. Correspondingly, the availability of this information has been associated with greater allocations of funds to maintenance and remediation of infrastructure systems.

Recommendation 1

It is recommended that the PAC propose that the current NSW Local Government infrastructure condition reporting be extended to all state-sector government agencies.

This will require each agency to prepare estimates of the sums required to bring infrastructure to a satisfactory condition. Reporting these estimates would lead to greater accountability by governments for their management of State finances. It would allow governments as a whole, and individual agencies, to adopt more systematic and rational approaches to resource allocation over time. It would still allow governments of the day to establish priorities in a transparent manner.

2. PUBLIC PRIVATE RELATIONSHIPS ARE NOT NEW

- It has long been recognised that governments cannot do everything and so the need for commercial relationships between the public and private sectors is not new.

- What is new is the increasing intensity of privatisation activities including asset sales and PPPs which incorporate not only the construction and operation of infrastructure but also the delivery of human and other services.

3. PPPs - A FORM OF FINANCIAL ENGINEERING

- PPPs are the currently favoured form of financial engineering or off balance sheet financing.

- PPPs have been devised to avoid treating financing arrangements as government 'debt'.

- But Government debt is not a problem in Australia or NSW. Australia's total general government sector net debt - at 0.6% as percentage of Gross Domestic Product in 2005 and estimated at 0% in 2006 - is among the lowest in the OECD (with averages of 48.3% in 2005 and 49.6% in 2006), and is considerably lower than Europe (57.7% and 58.1%), Japan (81.2% and 82.4%), and the United States (47.2% and 49.6%).

- There is nothing wrong with governments borrowing to finance infrastructure that will be of benefit to current and future generations – especially if the project is also a profit maker.

- Government documents state that Government will only proceed with a PPP arrangement where it is satisfied that this is the best value-for-money and only if it offers 'significant savings'.

- Treasury's record on claims of savings is not a good one. Claims of 20% savings from 'contracting out' is a case in point.

Recommendation 2

It is recommended that the PAC ask NSW Treasury:

- *To provide evidence that PPPs have produced 'significant savings', and explain how those estimates of savings were calculated.*

- *To explain the extent of losses incurred on unsuccessful PPPs, such as the Sydney Airport Rail Link, and what has been learned from that experience.*

4. NSW, AUSTRALIAN AND INTERNATIONAL LEGISLATIVE AND POLICY FRAMEWORKS AND PRACTICES - ACCOUNTING FOR INFRASTRUCTURE

- Though it is denied, it is obvious that the off balance sheet accounting treatment is a prime driver of PPPs.

- The evidence supporting this conclusion is overwhelming. A 2002 Green paper openly stated that accounting standards were a 'strong influence' on 'the way Government does business', and that 'projects in which capital raising is considered a liability on the Government balance sheet could still proceed, but only if the delivery agency is able to bear the capital cost within its budget'. Government guidelines require agencies proposing PPPs to provide details of proposed accounting treatments, supported by references to relevant accounting standards. Particulars of contractual arrangements and associated accounting treatments are to be provided to the Auditor-General for his opinion before contracts are executed.

- NSW Treasury has prescribed that PPPs be treated as 'agreements equally proportionally unperformed', so that they need not be recorded as liabilities. Yet the evidence available from some Victorian PPP contracts that while this may the situation when PPP contracts are signed, the situation changes over time. Once the private sector partner has constructed infrastructure to contractual standards, the agreements are not 'equally proportionally unperformed'. Rather, the public sector agencies that were the contracting parties faced obligations that met standard tests for the identification and recognition of a 'liability'.

- Pending resolution of accounting issues by the International Accounting Standards Board and its committees, it is appropriate to promote high standards of disclosure in order to ensure the highest standard of transparency and accountability.

Recommendation 3

It is recommended that

- *The PAC propose that, in addition to current disclosures of commitments to undertake capital expenditure, the NSW Treasury be asked to calculate and report in notes to the Total State Sector Accounts (consolidated statements):*

  The fees expected to be derived by participants in currently-operating PPPs, from user charges, having regard to the profit-sharing arrangements specified in any base case financial models for those projects.

- *The notes should report this information in conjunction with a separate line showing the amount of financial commitments arising from contracts to pay for the availability of private financed infrastructure.*

- *These disclosures should separately state amounts payable, or expected to be derived by private sector partners*

  not later than one year
  amounts payable later than one year and not later than five years,
  and later than five years

  and should report estimated nominal values of those sums (not present values calculated by discounting).

5. GOVERNMENT MODELS FOR EVALUATING AND MONITORING PRIVATE INVESTMENT IN PUBLIC INFRASTRUCTURE [& AGENCIES' FAILURES TO IMPLEMENT THEM]

- The suite of documents issued by the NSW Government promised a systematic approach to the management of infrastructure, though the devil is in its detail and in its implementation.

- But Government policies have not been implemented:

  - the Infrastructure Council announced in 2001 has met just a couple of times and little is known about its activities, if any;
  - the Infrastructure Plan 2002 promised annually has failed to materialise;
  - the Guidelines which implied a (relatively) open and transparent approach to the disclosure of the case for PPPs (through publication of a 'Public Sector Comparator' or PSC) the Guidelines incorporate three fundamental flaws. They:

    - do not require disclosure of the proposed revenues associated with a project if it is to be a privately-funded;

    - do not require disclosure of what discount rate is to be used to assess the relative merits of the government delivery of projects versus a proposed PPP;

    - instead of requiring disclosure of projected cash flows, propose the calculation of hypothetical costs and questionable adjustments for risk.

Recommendation 4

It is recommended that the PAC inquire:

- *Why the public service has not ensured that Government policy for the publication of the results of PSCs in contract summaries was implemented.*

- *About the extent to which agencies analyse the projected cash flows from the alternatives of government delivery versus PPPs, and the depth in which those analyses are undertaken.*

- *As to when that analysis has been undertaken, vis a vis announcements that specific projects will be considered as possible* *future PPPs (such as were announced in the State Infrastructure Strategic Plan 2002), or when negotiations are undertaken with proponents of PPPs.*

Recommendation 5

It is recommended that the PAC ask agencies that have compiled PSCs to explain whether those PSCs have:

- *incorporated 'risk-adjustments' to the project costs estimated in the PSC – without allowing for similar risks when making comparisons with a PPP option;*

- *utilised the public sector borrowing rate plus a premium, or a high discount rate, supposedly to reflect the risks of the specific project under consideration.*

Recommendation 6

It is recommended that the PAC:

- *Ask NSW Treasury to advise what discount rates it has used (or recommended that agencies use) in (a) cost benefit analyses of program initiatives or capital projects, and (b) PPPs, over the past 10 years.*

- *Ask NSW Treasury to advise whether PSCs calculated by agencies contemplating PPPs have incorporated an allowance for the costs of monitoring compliance with those contracts – and to provide examples of how they were estimated for (say) tollroads or school projects.*

- *Ask the RTA whether sums that it has described as 'reimbursement of development costs' were included in assessments of the 'benefits' associated with prospective PPPs (rather than as reimbursements of past expenditure).*

- *Ask agencies that have compiled PSCs for use in comparison with a PPP proposal, to explain whether those PSCs have been updated before contracts were executed, to ensure that the PSC was then consistent with the PPP proposal (particularly in relation to the cost of potential design changes, the risk of other sources of cost overruns, and the risks associated with government guarantees or commitments to provide ensured revenue or rates of return to the counterparty).*

- *Propose that revised Guidelines for the development of PSC be issued, incorporating the following:*

  (a) the PSC should show the estimated projected cash flows associated with conventional public sector delivery;

  (b) the elements in a PSC should be confined to the cash flows likely to be incurred by the public sector agency from the date on which the PSC is prepared. Notional charges (such as hypothetical land tax or payroll tax) should not be incorporated in these projected cash flows, as they are not cash flows that will actually be incurred by government agencies. Rather, any reference to 'level playing field' adjustments, made in the interests of State compliance with National Competition Policy, should be confined to an accompanying textual analysis of the relative financial merits of the PSC and possible PPPs;

  (c) the discount rate used in the PSC should be disclosed, together with a brief explanation of any variation between this rate and the rates recommended by Treasury for other capital projects or programs within the State sector within the past 12 months;

  (d) the extent of the exposure of State agencies to the risk of failure on the part of the private sector partner should be described, together with references to how the sponsoring agency proposes to avoid or manage such a risk;

  (e) any comparison of the PSC calculation with the effective cost to government of a PPP deal should include an allowance for the costs to Government of monitoring that PPP;

  (f) detailed PSCs showing major categories of expenditure and revenues – not just a brief summary of the PSC calculation - are to be published in contract summaries once PPP contracts are executed;

  (g) detailed PSCs should be accompanied by an explanation of the date on which they were originally compiled, and when they were was subsequently updated.

Recommendation 7

It is recommended that

- *The PAC seek explanations for the inclusion in the NSW Guidelines of a statement that details the likely (risk-adjusted) costs of public sector* *delivery of specific infrastructure projects that might be published for the benefit of prospective tenderers.*

- *The PAC inquire whether any such estimates (or hypothetical costs) have ever been published in tender documents or communicated to prospective tenderers by other means.*

- *If any PSCs have been published in this way, to enquire whether* ***all*** *potentially interested parties were given access to the same documentation, or if the information was published selectively.*

- *If any PSCs have been published to prospective tenderers, to now make them publicly available for scrutiny by external stakeholders.*

Recommendation 8

It is recommended that the PAC propose that

- *Contract Summaries should include*

  a. *particulars of the expected scale of initial investment to be made by private sector partners, and of the value of expected maintenance programs and other operating costs required by the PPP contracts;*

  b. *where a PPP involves the private sector partners deriving revenues from user charges (such as tolls) an outline of the 'base case financial model', and the key forecasts of revenues contained in that model.*

- *That the summary of any cost-benefit analyses presented within a Contract Summary, if those analyses include monetary values attributed to impacts on the community, should:*

  a. *show costs and benefits (and associated indictors, such as benefit-cost ratios) on a consistent basis;*

  b. *detail the items of costs and benefits that were included in the analysis;*

  c. *explain the basis upon which monetary values were assigned to each item;*

  d. *disclose the discount rate used in the analysis.*

6. THE FRAMEWORK FOR RISK ALLOCATION BETWEEN THE PUBLIC AND PRIVATE SECTORS AND ITS APPLICATION

The Guidelines:

- in calculating the PSC provide for risks in their public sector option but fail to make similar adjustments for failure of the private sector partner (including the risk of failure of counter-parties, that often are special entities);

- fail to explore the risks that private sector partners may earn excessive profits which are opportunity costs to the Government;

- disregard the risks to the NSW community of having to pay compensation in the event that there is a need to upgrade public sector infrastructure (even local roads)

- contain no flexibility for adjusting to changed circumstances during the term of the contracts so the Government of the day may lose control of the standard of service to the community.

Some proposals in relation to modification of the Guidelines relating to risk assessment are embodied in Recommendations presented above.

7. THE EXTENT OF OPPORTUNITIES TO SHARE KNOWLEDGE ACROSS AND BETWEEN AGENCIES

Sharing knowledge across and between agencies would be greatly impeded by agreements to keep crucial parts of PPP contracts as 'commercial in confidence'. – and for Contract Summaries to omit relevant information.

The proposal in the NSW Guidelines for the preparation of a post-implementation review of PPPs is applauded.

Recommendation 9

It is recommended that the PAC

- *Seek copies of all of the 12-monthly post-implementation reviews prepared by agencies since the 2001 Guidelines were issued.*

- *Propose that copies of those post-implementation reviews (or summaries of them) be made available on the same Treasury website that reports Contract Summaries.*

8. THE EXTENT TO WHICH AGENCIES ARE MANAGING INTELLECTUAL PROPERTY ISSUES

- If inventions, original designs and practical applications of good ideas are protected through copyright, patents., registered designs, circuit layout rights and trade secrets, public sector managers would have little role in 'managing' intellectual property issues.

- As for so-called trade secrets and proprietary knowledge and 'confidential information', it is noted that, according to an authoritative commentary on the law in this area, 'the law does not regard secret information as property'. Rather, any rights arise from a cause of action based on a duty of good faith or contract or some other cause of action – not property rights.

- The prospect of any such claims being raised could be readily averted simply by establishing (in advance) the ground rules on which PPP proposals will be entertained and handled.

Recommendation 10

It is recommended that the PAC

- *Propose that NSW Government Guidelines be redrafted to give notice to those presenting PPP proposals (whether solicited or unsolicited) that, if successful, the details of the PPP contracts will be publicly available and no regard will be had to prior claims of 'commercial confidentiality'.*

It is noted that the NSW Government Guidelines propose that government agencies may purchase 'intellectual property' from unsuccessful bidders. Hence one useful way of identifying the significance or otherwise of these issues gives rise to another recommendation.

Recommendation 11

It is recommended that the PAC

- *Inquire whether agencies have ever purchased intellectual property from unsuccessful bidders (per NSW Guidelines) – and if so, to explain what that 'intellectual property', and whether those agencies are currently benefiting from the application of that IP – and how?*

9. CONSEQUENCES OF PPPS

The many criticisms of PPPs have been well-documented elsewhere and include claims that they:

- are ideologically-driven;
- have been poorly analysed;
- give rise to a lack of accountability on the part of government for the quality of essential services;
- involve unnecessary secretiveness;
- are often bad financial deals for taxpayers;
- can lead to a loss of services to the community;
- lead to a loss of public sector skills; and
- distort spending and urban planning priorities, since priority may be given to projects that are readily packaged as PPPs, rather than to those which will produce the greatest benefit to the community.

A significant consequence of privatisation and associated policies which has received little attention is the impact on employment and loss of public sector skills.

In particular, there is evidence that these policies since the late 1980s, have led to a significant and sustained decline in apprentice intake.

Recommendation 12

It is recommended that the PAC

- *Note with concern that the wider use of privatisation and related practices has been associated with a decline in the number of apprenticeship positions available in the State to the detriment of the State's economy.*

- *Propose that the Guidelines on PPPs should be*

  - *refined so that the Statement of Economic Development Impacts (Appendix 4) makes specific mention of the impact of available apprentice positions and trade positions during the term of the proposed contract;*

  - *amended to require PPP contracts to contain appropriate minimum apprentice-tradespersons ratios which are in line with trade union and community expectations and needs; and*

  - *amended to require PPP contracts to contain a definition of 'local content' that is tied to local labour content rather than cost content.*

10. THE FUTURE – RESTORING ACCOUNTABILITY AND CONTROL

- The use of public private partnerships as a financing device involves by-passing the legislature's oversight over public sector expenditure on capital projects and service delivery, on a scale hardly contemplated in recent years.

- It is contended that adoption of the recommendations outlined in this submission will go some way towards providing Parliament (and the wider community) with the opportunity to apply greater scrutiny to the substance of PPP arrangements. And perhaps, a brake on PPPs that 'lock in' government to existing modes of service delivery in a time of rapid technological change.

- It is likely that members of the Government and the public sector may not have the technical training and skills to properly evaluate the financial merits of PPP proposals. The recommendations would provide the opportunity for PPP proposals to be scrutinised by a wider range of stakeholders, and hence allow more effective consultation with the community. The community deserves the restoration of accountability.

- The recommendations, if implemented, would provide the Government with the opportunity to (metaphorically) push the chair back from the desk, and reconsider the State's priorities for infrastructure management and development – and even the role of the public sector in the new millennium.

1. NEED FOR A REVIEW OF THE CONDITION OF THE STATE'S INFRASTRUCTURE – AND WHAT IT WILL COST TO FIX IT

1.1 COMMONWEALTH AND NSW INFRASTRUCTURE

One of the primary responsibilities of State governments is to manage, upgrade maintain and renew infrastructure, much of which was inherited from the activities of prior governments, and was paid for by previous generations of taxpayers.

An indication of the relative responsibilities of different levels of government to manage infrastructure is provided in the following Table, which shows 'book values' of the infrastructure assets currently held by different tiers of government.

Table 1.1
Infrastructure Assets

	$m	$m
Commonwealth of Australia: Infrastructure, Plant and Equipment (excluding specialist military equipment) buildings		46,139
State of NSW		
Plant and equipment	10,030	
Infrastructure systems	71,645	81,675

Source:
Commonwealth of Australia consolidated financial statements as at 30 June 2004
NSW 'Total State Sector' consolidated statements as at 30 June 2004.

(It should be noted that the NSW figures are understated because they do not include the value of buildings, as the total state sector consolidated statements do not disaggregate 'land and buildings'.)

1.2 THE COST OF RESTORING OR REMEDIATING INFRASTRUCTURE IS NOT COUNTED AS A 'LIABILITY'

One of the distinctive features of political debate in Australia and elsewhere has been a concern to produce budget surpluses and to reduce government debt.

However political debate about 'debt' or 'liabilities' is to a large extent misplaced. A government may produce a budget 'surplus', and reduce debt or liabilities while still leaving state finances in a desperate situation. That is because ***accounting does not recognise backlogs of infrastructure maintenance as a liability***.

It was not always so. The accounting profession once advocated that financial statements should include ***provisions for deferred maintenance*** (UIG, 1999), and this was echoed in NSW Treasury directives.

Subsequently accounting standard-setters generally have discouraged or banned the reporting of ‘provisions for deferred maintenance’ in statements of financial position on the ground that such provisions do not constitute liabilities in terms of newly-developed tests for the identification and measurement of 'liabilities' (see eg. ASCPA/ICAA, 1992).

It is hard to quarrel with that determination, for ***profit seeking entities in the private sector.*** Such firms are expected to adapt to changing circumstances, and often abandon what were once seen as areas of 'core business' because of those changes.

Governments are in a different position. They are expected to provide a range of services to the community, and can not abandon (say) public transport services, just because they are unprofitable.

Correspondingly, if a government has failed to maintain public transport infrastructure at an appropriate standard, then it faces obligations to either repair or upgrade or replace that infrastructure at some time in the future.

The failure of government financial statements to reflect those obligations is a fundamental weakness of public sector accounting – and has been recognised as such internationally.

It is also a fundamental weakness in the current system of allocating revenues received by the Commonwealth to the States and Territories, via the Commonwealth Grants Commission. The 'older' States, such as NSW, are likely to face far higher obligations to repair or remediate legacy infrastructure than other states where rail track, road bridges and water, drainage and sewerage infrastructure may be more recently-constructed. Yet, the Commonwealth Grants Commission methodology aims to allocate funds between the States and Territories having regard to whether or not they have the capability of funding a common standard of services. One of the implications of this is that the Grants Commission methodology affords privileged treatment to states (like Queensland or Western Australia) which are seeking to construct new infrastructure to serve their populations. It disregards the extent to which other states have to spend equivalent moneys on capital works to maintain or remediate deterioration of their older infrastructure.

Arguably, if NSW and other older states were preparing and presenting evidence about the need for investment in their legacy infrastructure, then they need to be in a position to demonstrate the inequities of the current Grants Commission approach to the redistribution of Commonwealth tax revenues between the States.

1.3 WHAT IS NEEDED: A COMPREHENSIVE AUDIT OF THE STATE'S INFRASTRUCTURE

It is recognised that the NSW Government has published a *State Infrastructure Strategic Plan 2002*, that sets out 'the New South Wales vision for infrastructure opportunities over the next ten years, with around 300 project proposals worth an estimated total capital value of over $29 billion. A Brochure also identified a list of projects each valued in excess of $100 million that were either in the marketplace as PPPs or could be considered as such - and it was claimed that these project proposals 'represent opportunities of over $13 billion in total capital value in the next ten years'.

Arguably most of these projects involve new capital works including extensions of existing infrastructure systems, though the list includes many that represent the upgrading of existing infrastructure systems.

However it is contended that in order to be fully accountable to the community, governments should do more than provide a list of future projects. They should also demonstrate the manner in which they are maintaining existing infrastructure. That requires governments to undertake periodic assessments of the condition of the infrastructure, and to assess (as a minimum) what it would cost to restore legacy infrastructure to a satisfactory condition.

It should be a matter of concern that the Secretary of NSW Treasury has asserted that infrastructure assets are not always 'fully maintained' throughout their life because 'maintenance needs are frequently subordinated to other priorities' (Pierce, 2002). There is no reason to expect that this observation does not also apply to other State Governments.

Possibly because information about emerging needs for infrastructure maintenance, remediation and upgrading have not been compiled and published for public scrutiny, successive State Governments may have failed to provide adequate funding to maintain infrastructure. That, in turn, may have led to increasing deterioration in legacy infrastructure and increasing back-logs of much-needed projects – and a corresponding escalation of the funding required for maintenance and capital expenditure.

Possibly governments – in Australia and elsewhere – have been reluctant to provide such information, for a range of reasons, some political, some technical.

The ***political obstacles*** to compiling such information may be:

- the risk that the 'government of the day' will be blamed for allowing infrastructure to deteriorate and for hefty bills for maintenance and upgrades to accumulate, under its watch;

- the risk that such an exercise may raise expectations that each and every deficiency will be remedied in a short period of time, or that major progress can be made during the term of the current government.

Yet it is in the public interest that this information be in the public domain, and support for such an initiative be bi-partisan, if only because:

- much of our state-based legacy infrastructure – rail track, roads, bridges, water distribution networks and drainage systems – are relatively durable, so that deterioration of those assets would have occurred over long periods – 15 years or more; hence responsibility for any deferral of maintenance and under-funding of upgrades can not entirely be sheeted home to the most recent incumbent government;

- both sides of politics should be anxious to identify risks to the community – for the failure of some kinds of infrastructure can lead to catastrophic consequences (witness the Granville rail disaster).

The ***technical obstacles*** to assessing the condition of infrastructure and the cost of bringing assets to a 'satisfactory condition' are several, but not insurmountable:

- techniques and recording systems are readily available for assessing the condition of some classes of asset (such as roadworks or buildings) but may not be as well developed for other classes of asset (such as telecommunications equipment);

- in that context, those responsible for providing assessments of the funding needed to bring infrastructure to a satisfactory condition may make exaggerated estimates – which are in substance, 'ambit claims' aimed at securing a higher level of funding in future;

- for many classes of infrastructure, there are no agreed standards of 'satisfactory condition'. One can reasonably expect some common standards for certain asset classes (e.g. water treatment and distribution systems should deliver potable water in compliance with World Health

Organisation standards; road bridges should be safe to use under specified loads; there are standards for the illumination of pedestrian crossings). For other asset classes, minimum standards of functionality may need to be established on a case by case basis – so that agency-generated assessments of infrastructure can track whether those minimum standards have been met over time, or whether there have been backlogs in deferred maintenance.

However, as explained below, ***all Federal government agencies in the USA*** are required to ***disclose the extent of deferred maintenance on property, plant and equipment*** (FASAB, 1996).

But Australia lags behind the USA in infrastructure reporting. Hence Commonwealth, State and Territory governments can not be held accountable, from year to year, for how they have managed legacy infrastructure.

1.4 NSW LOCAL COUNCILS ALREADY ASSESS INFRASTRUCTURE CONDITION AND ESTIMATE THE COST OF RESTORING THOSE ASSETS TO A SATISFACTORY CONDITION

It is not commonly recognised that the State of NSW pioneered the development of annual assessments of the condition of infrastructure – but ***only for local government.***

The NSW Local Government Act of 1993 required local councils to prepare an annual assessment of the physical condition of infrastructure, together with estimates of the cost of restoring that infrastructure to a satisfactory condition. Councils were also required to report estimates of what it would cost to maintain infrastructure once it was in a satisfactory condition (a hypothetical 'cost') and what had been budgeted to be spent on infrastructure maintenance or repair in the current year.

These pre-date requirements introduced in the USA for disclosures about infrastructure, or the reporting of information derived from condition assessments. These include the USA's Federal Financial Accounting Advisory Board (FASAB) statement 6 (1996), which establishes reporting requirements for federal government agencies. Similarly, the USA's Governmental Accounting Standards Board, which establishes accounting rules to be followed by states and municipalities, issued rules in 1999 whereby the use of condition assessments was a reporting option[1].

[1] The accounting standard GASB 34 (1999) 'Basic Financial Statements - and Management's Discussion and Analysis – for State and Local Governments' requires that depreciation on infrastructure assets be charged each period or, alternatively, the costs and results of preservation efforts must be included in financial statements as an expense of the period. The latter approach may be used when there is an asset management system in place that provides evidence of the preservation of infrastructure assets at a minimum condition level established by the state or local

While FASAB determined that 'no dollar amount [for deferred maintenance] shall be recognised on the statement [of net costs]', it did require

> Disclosures related to the condition and the estimated cost to remedy deferred maintenance of PP&E [property, plant and equipment] … are to be made as a note to a line item … on the statement of net costs.

It is considered that the introduction of disclosure requirements for deferred maintenance would be better than nothing (no disclosures). However there are inherent limitations of the FASAB requirements. Limitations of disclosing 'deferred maintenance' include:

- the extent of deferred maintenance may depend on what was initially budgeted for maintenance in long-term asset management plans. Hence, two agencies with identical assets that are deteriorating at exactly the same rate could produce significantly different estimates of deferred maintenance;

- there are no objective standards for determining whether certain expenditures (e.g. re-sheeting of road pavements) should be regarded as 'capital' expenditure' or maintenance; hence estimates of the extent of deferred maintenance can be readily manipulated;

- correspondingly, some items of infrastructure (such as wooden bridges, or pumping equipment in waste water treatment systems) may require replacement as they come to the end of their economic life – not maintenance – so that these costs would not be counted as 'deferred maintenance' but rather as planned capital works.

1.5 EXPERIENCE WITH NSW LOCAL GOVERNMENT REPORTING OF INFRASTRUCTURE CONDITION

Application of the 1993 NSW requirements were phased in over time, and it seems fair to state that initial reporting by local councils in NSW varied in quality, with some councils adopting their own individual interpretations of 'satisfactory condition'. These interpretations range from what the preparers of these reports thought was the minimum expenditure necessary to bring assets to a useable

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government. The annual cost to preserve and maintain the infrastructure assets at the predetermined condition level is to be included in the accounts; correspondingly, condition assessments to demonstrate preservation and maintenance of asset functionality are undertaken at least every three years. In effect, the GASB requires either the assignment of values to infrastructure, followed by book entries for 'depreciation', or the preparation of condition assessments; NSW requirements for local government, through the joint operation of accounting standards and the 1993 Local Government Act, require both.

condition with limited functionality, through to a standard representing a significant upgrade of existing infrastructure to support higher functionality than originally designed.

Interpretations of "satisfactory condition"

1	2	3	4	5
After minimum repairs necessary to bring assets to barely useable condition within an existing (limited) functionality	After 'affordable' expenditure which would repair assets to fair condition & minimum desired functionality	After repairs & mtce which would bring assets to a good condition and an acceptable level of functionality	After expenditure which would upgrade or bring assets to 'as new' condition and original (designed) functionality	After expenditure which would significantly upgrade infrastructure to support high functionality required to meet community expectations

Lower range of functionality of existing infrastructure — *Upper range of functionality of existing infrastructure*

Source: R.G. Walker, F. L. Clarke and G. W. Dean (1999).

While acknowledging these limitations (and the fact that not all councils had completed reports on all categories of infrastructure in that year) the data presented by the NSW local government sector in 1996 were alarming.

The information reported by 170 councils for 1996 showed that the ***NSW local government sector estimated that it needed over $6 billion to bring infrastructure to a satisfactory condition.*** Details are as follows

Table 1.2
1995-96 NSW Local Government estimates of expenditure needed to bring infrastructure to a satisfactory condition

Buildings $m	Transport $m	Water $m	Sewerage $m	Drainage $m	Total $m
Panel A: Expenditure required to bring works to a satisfactory standard					
289.8	3,958.0	196.5	352.4	1,231.0	6,028.7
Panel B: Estimated annual cost to maintain works at a satisfactory standard					
97.4	588.2	39.4	53.2	46.9	825.2
Panel C: Maintenance program for 1995-96					
87.3	364.5	39.3	34.8	25.7	549.6

Source: 1995-96 annual reports of 170 councils and the 1994-1995 annual reports of six others.

Note that the planned maintenance program for 1995-96 was only around $550 million, as against an estimated total expenditure 'required' of $6,028 million.

On the face of it, this would suggest that the estimated 'cost to bring to a satisfactory condition' of local government infrastructure would have blown out considerably over time. Why? Because for some classes of infrastructure (such as roads) deferral of spending on maintenance can lead to escalating problems (e.g. if potholes and cracks in roads are not repaired, water infiltration below road pavements can cause greater damage). Underspending on maintenance can accelerate deterioration, and ultimately, leads to higher costs over the life of those assets. Moreover, the estimates are in terms of dollars of the day, and there has been cumulative inflation of around 21% from 1996 to 2004.

Yet later reports from NSW local councils present a somewhat more reassuring picture. The expenditure required to restore or remediate local government infrastructure to a 'satisfactory condition' still tops $6 billion – but has not increased exponentially, as may have been feared.

Table 1.3
2003-04 NSW Local Government estimates of expenditure needed to bring infrastructure to a satisfactory condition

Buildings $m	Transport $m	Water $m	Sewerage $m	Drainage $m	Total $m
Panel A: Expenditure required to bring works to a satisfactory standard					
423.7	3,838.7	339.3	580.3	1,170.4	6,352.4
Panel B: Estimated annual cost to maintain works at a satisfactory standard					
144.7	650.6	61.0	76.7	70.6	1,003.6
Panel C: Maintenance program for 1995-96					
119.3	520.8	55.4	63.2	40.4	799.1

Source: Yet to be published data collected as part of a research project undertaken within the Faculty of Economics and Business, University of Sydney, and jointly funded by the Australian Research Council and the NSW Department of Local Government, being undertaken by P. Edwards, G. Dean. S. Jones and R.G. Walker. The above data reflect what has been reported by NSW councils and have not yet been subject to quality controls. However the figures quoted above are consistent with 2002 data which were subject to an extensive range of tests and follow-up enquiries.

It appears that reported results have been influenced by a combination of factors:

- in recent years councils have spent relatively more on infrastructure maintenance (after the disclosure requirements led elected officials and local government managers to have a better appreciation of the scale of the challenges facing them in managing infrastructure)[2];

- while the NSW local government sector is subject to a regime of rate pegging, several major councils have successfully sought special rate variations specifically to address emerging needs for spending on infrastructure;

- the Department of Local Government has steadily refined its guidelines on the preparation of these reports on infrastructure condition. Hence later estimates from Councils have eliminated some prior overstatements, and are more consistent;

- estimates of the cost of restoring infrastructure to a satisfactory condition have become more refined (e.g. estimates have progressively been based on empirical evidence rather than on desk calculations[3]);

However the data reported presents an alarming disparity between estimates of expenditure needed – and what funds are being allocated to meet those tasks. The big ticket items are 'roads' and 'drainage'.

1.6 FUTURE REPORTING ON PUBLIC SECTOR INFRASTRUCTURE

The NSW local government sector has now had a decade's experience in assessing the condition of infrastructure and what it would cost to restore that infrastructure to a satisfactory condition. Preliminary analysis of these reports suggests that the process has improved and that the data being reported are much more reliable than the figures originally reported.

Research into local government experience has indicated that 'users' of these reports (elected councilors) regard infrastructure reports as helpful in making resource allocation decisions (though there is evidence that there have been shortcomings in information sharing within councils).

Many NSW local councils lack extensive resources to undertake evidence-based assessments, yet have produced data which provides a good indication of needed expenditure. Even if the figures are understated or overstated by a

[2] Some of that funding has come from the Commonwealth Government's 'roads to recovery' program as the Howard Government has distributed some of the proceeds of the sale of shares in Telstra. However the $1 billion allocated to the 'roads to recovery' program throughout Australia can be seen as a relatively trivial sum, when compared with the estimated $3 billion funding required for roads works by the local government sector in just one State.

[3] In 1996 several councils did not undertake physical assessments, but reported data derived from book values for historical cost or replacement cost, and accumulated book values for 'depreciation'. For details, see Walker, Clarke and Dean (1998), at pp. 448-450.

margin of 25%, they indicate the extent of the problem of deferred maintenance and underspending on ***legacy infrastructure.***

It is emphasised that the data cited above relate to legacy infrastructure (not just additional infrastructure that may be required to meet emerging needs in light of increased population and demographic changes).

It is submitted that:

a. Governments fail to be accountable to their constituency if they do not report on how well they have managed legacy infrastructure.

b. Since accounting standards do not permit – indeed, they ***prevent*** – the reporting of 'deferred maintenance' on infrastructure assets as a liability on agencies' balance sheets, political commentary which focuses on debt reduction, or on the need to maintain budget surpluses, often is misguided (and may even be doing a grave disservice to the public interest). Governments may reduce debt and record budget surpluses while allowing infrastructure paid for by previous generations of taxpayers to fall into disrepair and be inadequate to cope with changing needs.

c. The Commonwealth, State and Territory governments have failed to keep up with international developments in reporting on infrastructure condition and deferred maintenance of infrastructure. Even though accounting standards prohibit recognition of deferred maintenance as a liability, all US Federal Government agencies have been required since 1996 to report as notes to their financial statements the dollar values of deferred maintenance. All United States state and municipal governments (including cities like New York) are required to either assign values to infrastructure assets and depreciate them (in terms of standard accrual accounting procedures) OR provide condition assessments and report on whether the assets have been maintained to that standard, consistently applied.

d. Current enthusiasm for private sector financing of public infrastructure is, in part, a symptom of a more fundamental problem - prior neglect of the nation's infrastructure. Combined with pressures from changes in population, and changing demography, governments face a combination of the need to upgrade and enhance legacy infrastructure and also to invest in new capital works.

The PAC could benefit from a study tour to visit offices of both FASAB and the GASB in the USA, in order to learn about these developments and US experience over the past decade.

Better reporting of infrastructure needs is more likely to lead to a more planned and co-ordinated approach to government spending and financing of both infrastructure maintenance and remediation, and emerging infrastructure needs.

1.7 RECOMMENDATION

It is recommended that:

The Public Accounts Committee propose that the current NSW Local Government infrastructure reporting be extended to all state-sector government agencies in NSW.

This will require each agency to prepare estimates of the sums required to bring infrastructure to a satisfactory condition. Reporting these estimates would lead to greater accountability by governments for their management of State finances. It would allow governments as a whole, and individual agencies, to adopt more systematic and rational approaches to resource allocation over time. It would still allow governments of the day to establish priorities in a transparent manner.

2. PUBLIC PRIVATE RELATIONSHIPS ARE NOT NEW

Everyone agrees that governments need to ensure investment in infrastructure. However, there are varying opinions as to the method of creating and the process of financing such investment.

It has long been recognised that governments cannot do everything and so the need for commercial relationships between the public and private sectors is not new.

Private businesses have long provided to government agencies:

- goods and materials;
- services;
- buildings on leases;

and private businesses have been engaged as:

- contractors to government in the construction of physical infrastructure – schools, hospitals, roads, and other public works.

These activities were normally funded from government revenues and/or government borrowings.

Decades later, much of NSW's legacy infrastructure is older, and the population has grown, so that there are greater demands on that legacy infrastructure.

Changing demography, technology and community expectations have collectively established demands for further investment in infrastructure.

But what are the priorities? In the absence of a review of the State's infrastructure as mentioned above, the NSW community does not have a good sense of what should, rationally, be the State's priorities for infrastructure investment.

Parliamentarians have a great responsibility in identifying the long term infrastructure needs of the community. However, this responsibility is hampered by the political cycle and the many temptations to focus spending on short term and obvious projects, issues and achievements.

Moreover, a coalition of politicians, bureaucrats, merchant bankers and others have convinced each other, the media and the community about the evils of public sector debt or the so-called catastrophic effects of a down-graded credit rating. Meantime, the business community has engineered ways of earning high fees for themselves.

The public service, for its part, has been inappropriately politicised. Public servants may fear to provide appropriate advice. There are also concerns that many in senior positions lack the financial skills to adequately analyse proposals put to them by a self-interested private sector.

These developments have given rise to various forms of privatising the public sector.

3. PPPS – A FORM OF FINANCIAL ENGINEERING

'Public Private Partnerships' and 'PPPs' appear to be the currently favoured term and acronym (respectively) for 'off balance sheet financing' and other forms of financial engineering.

The use of financial engineering by Australian governments was once the product of restrictions imposed by a 1920s 'gentlemen's agreement' between the Commonwealth and the States to limit borrowings by States, in the interests of defending the integrity and value in exchange of the national currency (Saunders, 1989).

The NSW Wran Government, to its credit, did not afford much respect to the Gentlemen's Agreement, and its successors. It saw that it was more important to provide infrastructure to meet the needs of current and future generations. The government of the day found that investment in some categories of infrastructure – electricity generation – had been neglected. The community did not take kindly to blackouts. So it set out to invest in new power stations. It wanted them built in a hurry.

These required major investments, that were not affordable from the funds available from current revenues. Possibly the funds could be borrowed – but the Loans Council restricted State borrowings. The Wran Government found a way around these restrictions: it financed the Eraring Power Station through a leveraged lease arrangement. In the process, it found a way to lower the costs of borrowings, by giving private sector partners the benefit of tax deductions (e.g. depreciation on equipment) that were of no value to the NSW Government (since it did not pay income tax to the Commonwealth).

In summary: the antecedents to what we now describe as PPPs (or PFIs or, whatever acronym is thought to be the most benign) were deals that:

- funded ***priority*** infrastructure projects; and
- utilised relatively cheap forms of finance.

In the new millennium, contemporary PPPs are often the opposite.

3.1 WHAT'S DIFFERENT ABOUT PPPs AS A FORM OF FINANCING?

The accompanying table summarises some of the ways in which the private sector has contributed to the financing of physical infrastructure in the past. In some of these, the private sector only contributes to the cost of construction. In others, the private sector meets construction or design costs and receives a guaranteed revenue stream from the government – just as surely as if the government had borrowed the money and was repaying that debt over time (save that the financing arrangements enable government to keep that debt 'off balance sheet').

Table 3.1
Private sector involvement in development of new physical infrastructure and associated services

Form of involvement	Example
Compulsory monetary contributions	Payments towards cost of extending water or electricity services to new property developments
Agreed physical contributions	Property developers construct paths, drains, bus shelters, transport interchanges
Provision of finance for specific projects	Leveraged leases for power stations; pre-commitment finance leases
Construction and management of facilities	Firm constructs a sports facility on government-owned land, and receives all revenues from user charges for the use of those facilities by customers during term of site lease.
Take or pay contracts	Private firms construct pipelines or electricity transmission lines and receive a pre-determined minimum cash flow each year regardless of transmission volumes – thus ensuring an attractive financial return to private sector participant
Ensured revenue agreements	Private firms construct and maintain infrastructure and receive revenues from pre-determined user charges, supplemented by revenues from government to ensure a guaranteed rate of return during term of contract – after which asset is transferred back to the government.
BOOT schemes	Private firms *Build, Own and Operate* infrastructure on government-provided corridor, receive revenues in the form of user charges at pre-set but indexed rates, and then *Transfer* the fully-maintained asset back to government after the later of (a) a specified number of years, or (b) when private sector participants have derived a specified cumulative rate of return on their initial 'investment'.
'New' PPPs	Private firms construct facilities and provide a package of human services traditionally supplied by government (e.g. corrective services, management of detention centres, operation of schools) in return for revenues derived from government and/or customers

The form of these arrangements was progressively modified as State and Territory governments sought to deliver capital projects to their electorates, while avoiding the borrowing restrictions established by Australia's Loan Council. The Loan Council was established after Australia's Constitution was amended by referendum to empower the Commonwealth to 'make agreements with the States with respect to the public debts of the States'. A so-called 'Gentlemen's Agreement' of 1927 (mentioned above) set guidelines for establishing the maximum sums that Commonwealth and State governments could borrow through bond issues or other formal borrowings. This aggregate limit for Commonwealth and State borrowings was set with regard to macroeconomic policy, and the Loan Council allocated that sum between jurisdictions via a formula based on population. In broad terms, States were only allowed to borrow within those allocations (Saunders, 1989).

However during the late 1970s and early 1980s, government agencies sought to use innovative financial arrangements (such as leveraged leases) to circumvent the Loan Council's restrictions. In response, the Gentlemen's Agreement was replaced in 1984 by a Global Approach to public sector financings. Under the latter, the Loan Council controlled all forms of financing by semi-government and local authorities and all companies and trusts that were wholly owned by governments. The annual limit on new money financings was termed the 'global limit', and encompassed non-conventional financings, including finance leases, sale and leaseback transactions, and other modes of financing capital expenditure (Loan Council, 1991).

For a time the Loan Council sought to interpret whether financing arrangements should or should not be considered to fall within the Global Limits, by applying the familiar lease accounting test of whether government 'assumed the risks and benefits of ownership' of infrastructure financed by a variety of mechanisms: cross border leases subject to defeasance arrangements, sale of quasi-equity securities, pre-commitment leases for office buildings, and so forth (see Loan Council, 1991). However this approach of trying to determine which arrangements represented borrowings was abandoned in October 1991. Thereafter individual projects would be reflected in Loan Council Allocations only to the extent of public sector exposure (Walker & Con Walker, 2000).

The pre-1991 Australian institutional arrangements restricting government borrowings may have encouraged experimentation with different forms of financial arrangements, some years before British governments similarly sought to utilise private finance to construct deliver public infrastructure (Broadbent and Laughlin, 1999a).

In many major Australian PPPs, a key element is the construction of physical infrastructure (such as toll roads), while the provision of associated services (such as collecting tolls, maintaining roadworks and street lighting) is a relatively minor component of the arrangement. In other PPPs, such as those involved in the construction and operation of hospitals or detention facilities, the provision of services is of greater significance.

3.2 PPPs DEVISED TO AVOID TREATING FINANCING ARRANGEMENTS AS GOVERNMENT 'DEBT' - BUT WHY?

Undoubtedly the main driver for private sector involvement in capital projects has been financial – the concern by governments to avoid increasing (reported) government ‘debt’. The political theme of advocating debt reduction by government appears to have been imported from Britain, where public sector debt was high, relative to GDP. The Maastricht Treaty (1992) had established ceilings for government borrowings by members of the European Union, on an annual and cumulative basis. A Protocol on the ‘excessive deficit procedure’ called for alarm bells to be rung when a planned or actual government deficit exceeds 3 per cent of gross domestic product, or when government debt exceeds 60 per cent of gross domestic product, at market prices.

It is no surprise that these arrangements also created incentives for the British government to enter into off-balance sheet financing arrangements.

Obviously there are occasions when privatisation through the sale of government trading enterprises (GTEs) may make good sense. Private sector businesses have benefited from selling-off non-performing or non-core assets to meet financial obligations or to fund promising new ventures. But those occasions depend on a careful balancing of the financial and non-financial costs and benefits of a range of options.

In contrast, the arguments disseminated about how privatisation could repair or avert a crisis in government finances have been crude, and often quite misleading.

Indeed, the very idea that there is a crisis in government finances has often been deliberately manufactured to suit the interests of individual governments.

It is on the record that the Coalition Government which first advocated debt reduction in the 1980s had deliberately set out to 'manufacture a sense of crisis' in State finances.

A key element has been the establishment of short-term enquiries into government finances to report on a government’s financial position (and to dump on predecessors). Gary Sturgess, who was a pre-election political strategist to incoming NSW Premier Greiner (and later appointed head of the NSW Cabinet Office) later conceded that it was mainly a 'marketing exercise' to create 'a popular demand for that kind of reform'. He has explained the formation of the 1988 ‘Curran’ Commission of Audit as follows:

> … it was a marketing exercise… In March 1988 there was no great feeling that New South Wales’s finances were in drastic shape, so why would you need a government shake up? … at that point in time people just did not

> see the need for it, people couldn't see the point of user pays. The whole idea of downsizing and putting these things on a commercial basis, there was just no basis for that. Nobody had done it. So we had to create a popular demand for that kind of reform (Interview, December 1994, as reported in Laffin and Painter, p. 9).

The Curran Commission duly reported that

> New South Wales has been living beyond its means!

and the device of having a short-term 'Commission of Audit' talk about a crisis in government finances became a model for incoming governments thereafter – leading to reports in this genre being produced in Tasmania (1992), South Australia (1993), Western Australia (1993), Victoria (1994), Queensland (1996) and the Commonwealth (1996).

The facts are that government debt is not a problem in Australia or New South Wales.

Judging from some political rhetoric, all debt is dangerous. It cannot be emphasised too strongly that such claims would be regarded as nonsense in the private sector, where debt-financing is seen as a fact of life, and the choices about a firm's capital structure can improve returns to shareholders.

International comparisons of debt levels are regularly undertaken as an indicator of the financial standing of governments. The focus of these reports is generally on 'debt' rather than 'liabilities', for the simple reason that data about public sector 'liabilities' has been unavailable for most countries. It has to be acknowledged that, in some jurisdictions, the difference between the two figures may not be significant.

For the purpose of international comparisons, levels of debt are commonly related to the benchmark of Gross Domestic Product – to provide a crude index of 'affordability'. At state level, levels of debt are related to Gross State Product.

It is clear from published international comparisons that Australian public sector debt levels are very low by international standards.

According to the 2005-06 Commonwealth Budget papers, *Australia now has one of the lowest levels of net debt in the OECD* (Organisation for Economic Co-operation and Development) and is expected to fall further. It states that:

> The ratio of Australia's total general government sector net debt to GDP is among the lowest in the OECD and is considerably lower than in Europe, Japan and the United States (Commonwealth of Australia, *Budget Paper No 1, 2005-06*).

The OECD survey, based on figures provided by the various member countries, shows an estimated net debt figure for Australia as a percentage of GDP at 0.6 per cent for 2005 (and a projected 0 per cent by 2006). This compares with 47.2 per cent (2006: 49.9 per cent) for the United States; an average of 48.3 per cent (2006: 49.6 per cent) for the OECD; and an average of 57.7 per cent (2006: 58.1 per cent) in the Euro Area. Details are shown in the table below.

Table 3.2
GENERAL GOVERNMENT NET FINANCIAL LIABILITIES AS A PERCENTAGE OF NOMINAL GDP
Estimates and projections

	1995	**1996**	**2005**	**2006**
United States	57.2	56.3	47.2	49.9
Japan	24.5	29.7	81.2	82.4
Germany	39.7	42.5	61.4	64.4
France	38.9	42.6	44.5	44.3
Italy	101.2	106.5	97.8	98.9
United Kingdom	38.9	40.5	38.7	40.4
Canada	69.3	67.5	29.3	26.9
Australia	**28.2**	**22.4**	**0.6**	**0.0**
Austria	48.0	47.4	39.1	37.6
Belgium	125.6	123.3	90.1	88.3
Denmark	25.9	24.5	2.4	0.9
Finland	-4.1	-6.7	-40.5	-40.0
Hungary	..	..	38.0	38.0
Iceland	40.7	40.5	18.9	16.3
Korea	-17.4	-19.0	-28.4	-28.8
Netherlands	54.1	52.9	37.7	37.8
New Zealand	34.7	30.7	-9.5	-11.7
Norway	-36.5	-41.6	-124.2	-140.1
Portugal	26.4	28.6	45.9	50.1
Spain	47.6	52.4	31.1	28.5
Sweden	25.2	25.7	-5.9	-6.4
Total of above OECD countries	47.3	48.7	48.3	49.6
Euro area	54.7	58.6	57.7	58.1

Source: Organisation for Economic Co-operation and Development, *OECD Economic Outlook 77*, May 2005.
Note: This OECD publication does include a definition of 'net financial liabilities'. However, according to the 1999-2000 Commonwealth *Budget Paper No 1,* 'net financial liabilities' data are for the total general government sector (i.e. the aggregate of all levels of government, including the social security sector but excluding the PTE sector).

The above comparisons and the European benchmarks noted above reveal that comparable Australian government borrowings are close to non-existent and that Australia is not in a public sector debt crisis.

In view of State policies since the late 1980s, the question might be asked:

Does it make sense to base government policies on financial targets rather than on targets for the provision of services to the community?

Thankfully it is noted that the last NSW State Budget for 2005-06 incorporated a change of stance from that adopted in prior years. The 2005-06 Budget provided for new capital works ***to be partly funded by borrowings to the tune of $8.7 billion over the next four years*** (*2005-06 NSW Budget Paper No. 4*, p. 1).

3.3 ARE PPPs THE BEST WAY TO FUND INFRASTRUCTURE PROJECTS?

There are two main government sources of funds for investment in infrastructure:

a. From **current revenues** - paying for these assets out of current year's earnings (for the States, mainly revenues from taxes and charges, and NSW's share of Commonwealth revenues as determined by and controlled by the Commonwealth);

b. From **borrowings** – paying for assets by borrowing, and then repaying borrowings over time.

Of course, it is possible to fund infrastructure from a combination of current revenues and borrowings – by paying for some of it in the current year, and borrowing the balance.

What has been variously described as Public Private Partnerships or 'Private sector investment in infrastructure' essentially involves a combination of funding from current revenues and borrowings – with one important difference. Instead of government doing the borrowing, the arrangement involves ***borrowings by a special purpose entity, on behalf of the government.*** The 'form' of these arrangements is that the special purpose entity will borrow against the security of a stream of future cash flows to be earned from the community (e.g. via tolls) or from government (in the form of 'fees for service'). In substance, the timing and quantum of these cash flows may be underwritten or guaranteed by the public sector.

The form in which government underwrites returns or guarantees borrowings or otherwise sweetens the returns to equity investors, has differed from deal to deal. For example:

- The financial arrangements for the Sydney Harbour Tunnel were based on an 'ensured revenue agreement' which was transparent and embodied in a bill placed before Parliament (albeit in the early hours of the morning). If the revenues produced from tolls did not meet a threshold established by formula, the government would top-up those tolls with revenues from tolls from the Sydney Harbour Bridge.

- Contractual arrangements for the Sydney Airport link were withheld from Parliament in 1994 but a summary was 'leaked'. That summary showed that revenue sharing between the private sector special purpose entity (SPE) and government was to be determined in four steps. In step 1, 100% of the revenues went to the SPE, until investors had recovered all of their initial investment; in step 2, 80% went to the SDPE and 20% to the government, until the SPE had earned a cumulative real rate of return of 15% (presumably, before tax) on its initial, already re-paid investment; in step 3 the consortium would get 20% of any additional surplus cash until it had earned a cumulative real rate of return of 22% on its initial, repaid investment; thereafter the consortium would 10% of any excess revenues. Based on projected traffic volumes, the NSW Government would not recover its investment for more than 23 years, while the private sector consortium would break even in less than 4 years. The NSW Government would only earn an internal 'real' rate of return of 2%, while the private sector consortium stood to earn and internal rate of return of 21% - 25% (in 'real' terms before inflation) over the 30 year life of the project (Walker, 1994). As it happened, the SPE operating the tunnel found itself unable to meet its borrowing commitments. As recently reported, the operating company went into receivership, and the receivers called on a State Government guarantee. The NSW Government eventually had to settle claims for $106 million, payable by 2012 – taking the total cost to Government of more than $800 million (*Sydney Morning Herald*, 14 October 2005).

- Contractual arrangements for the M2 freeway were withheld from Parliament and the Auditor-General in 1994 but were available to potential investors by virtue of the fact that a prospectus had been issued so that foundation investors in Hills Motorway could sell-down their investment. These arrangements were similar to those used for the Sydney Airport link since they established distribution arrangements and the term of the contract by reference to the returns available in a 'base case equity model'. Government support for the project involves deferral of its right to share in revenues from the project, and deferral of rental payments for the tollway corridor (which was acquired through property purchases and use of the Crown's authority for resumptions).

- Arrangements for the construction and operation of prisons in Victoria involved the payment to the private sector's special purpose entity a fee based in part on a facilities availability charge and an accommodation/service charge. The former involved government commitment to make a stream of payments to the SPE for a defined period of years once the facility was available for the accommodation of prisoners. The service charge was linked to the number of prisoners accommodated in the facility, and included complex performance standards and formulae for calculating service fees and fee penalties or discounts if those service standards were not met from period to period

(English and Walker, 2004). The government kept to its side of the bargain by paying availability charges and service charges, but there were disputes over service standards and the quantum of fees payable per 'customer'. The government was compelled to step in and take control of the project. In doing so, it was required to pay sums outstanding in terms of the contract for the construction of the infrastructure.

- Arrangements for the construction and operation of hospitals in Victoria also involved the payment to a special purpose entity of fees based in part on a facilities availability charge, and in part on an accommodation/service charge (Walker and English, 2003). Again, the government was compelled to step in and take control of the project. In doing so, it was compelled to pay sums outstanding in terms of the contract for the construction of the infrastructure.

The fact that some of these arrangements involved the 'bundling' of (say) *infrastructure availability charges* and *fees per unit of service* does not alter the fact that the deals had some common features:

- a series of *special purpose entities* were established by the private sector firms or consortia;
- these private sector special purpose entities *borrowed to fund infrastructure construction*;
- *the financial arrangements promised to generate funds to repay the borrowings of the special purpose entities;*
- the financial arrangements promised high financial returns to investors and project managers – but if the project failed, *the financial burden of failure would primarily be borne by government.*

On the face of it, *the optimum way for government to finance material items of infrastructure in areas of core government business* is through utilisation of the relative strengths of both the private sector and the public sector:

- contracts for the construction of infrastructure can be subject to competitive tendering, supported by substantial financial penalties for shortcomings in performance and delivery. Provided there are a number of firms providing construction services, this provides considerable assurance that government will purchase that infrastructure for a fair price;
- since a key risk on construction contracts is that the private sector construction companies may get into difficulties and not have the financial capacity to incur losses, contractual arrangements should involve substantial performance bonds or readily-enforceable guarantees of performance. It is not appropriate to enter into arrangements with special

purpose entities that may have no underlying substance; nor may it be cost-effective to pursue compensation through litigation;

- governments can obtain debt finance at a lower rate than private sector firms; and private sector participants in PPPs expect a far higher return that the government's cost of capital. Hence it makes sense for government agencies to borrow directly (rather than enter into arrangements with Special Purpose Entities that establish liabilities, that are, 'in substance', borrowings).

The emphasis placed by some politicians in 'reducing debt' is overblown and exaggerated.

There is nothing wrong with governments borrowing to finance infrastructure that will be of benefit to current and future generations. This argument is strengthened if the project is also a profit maker.

However the political reality is that Labor governments are regularly accused in the media of financial irresponsibility if they borrow (even though media empires are themselves founded on borrowings) while Coalition governments somehow escape criticism if they sell inherited businesses and apply the funds for short-term projects that are often of little enduring value to any but sectional interests.

According to the 2005-06 NSW Budget Papers:

> In certain circumstances, PPPs can offer significant savings over conventional procurement options because they combine finance, construction and operational costs and risks in a single package. PPPs are not appropriate where they do not offer significant savings (*Budget Paper No 4*, p. 19).

It is assumed that this statement refers to ‘significant savings’ to the public purse. As such the statement raises a number of questions. For example, how are savings defined? And how are savings measured? To our knowledge, examples of ‘significant savings’ to the public purse have not been publicly documented.

The record on claims of savings in the past is not a good one. Claims of savings from contracting-out is a case in point.

It will be recalled that Prof. Simon Domberger was engaged by NSW Treasury in 1992 to design, perform and evaluate surveys into contracting out in the NSW public sector. His claims that contracting-out produced savings of 20 per cent were an extravagant interpretation of the evidence provided regarding some UK local councils, and the validity of that analysis has been seriously contested by a succession of authors.

Yet the claim of ‘20 per cent savings from contracting out’ was reiterated as fact – notwithstanding the existence of a series of published studies presenting conflicting evidence. For example, NSW Treasury was happy to translate the questionable Domberger claims as a finding from ‘experience’:

> Extensive analysis has been undertaken both in Australia and overseas of the potential for contracting out and the savings and other benefits that can be achieved. Typically, experience shows that savings of the order of 20 per cent can be achieved after account is taken of all transitional (sic) costs (*1991-92 NSW Budget Paper No. 2*).

Then, on the basis of Domberger’s survey work, it was claimed in 1996 that contracting-out across the NSW public sector had produced annual savings of approximately $266 million ‘without sacrificing quality of services’ (*NSW Treasury*, September 1996).

The basis of these claims about savings are in stark contrast with the 1995 findings of the NSW Council on the Cost of Government that the NSW government’s management information systems could not provide basic data about trends in expenditure on ‘line items’ or ‘activities’. Accordingly, sceptical readers might wonder how the respondents to Domberger’s surveys could arrive at estimates of major savings from outsourcing (particularly when overall spending on departmental programs had been steadily increasing).

It seems that respondents to Domberger’s NSW surveys were simply asked to provide their own estimates of savings – at a time when much publicity had been given to claims that savings of around 20 per cent were achievable from contracting out.

In terms of methodology, Domberger’s approach was a textbook example of ‘reactive research’ (*Webb, Campbell, Schwartz and Sechrest*, 1966). Evidence was collected from surveys of senior public sector managers, most of whom would have been on short-term contracts. Managers were asked, in effect, whether they had implemented government policies. Those managers would be unlikely to report that they had defied the government directives, or that their own efforts as managers had been less than successful.

As for the scale of savings secured by their efforts: NSW Treasury was saying that 20 per cent was achievable, and the designer of the survey had already publicly claimed that 20 per cent was an average saving. No one would be surprised if respondents to Domberger’s surveys claimed savings of around 20 per cent. But many researchers would suggest that survey responses collected in these circumstances could have been influenced by external events.

Ideologically-based (rather than factually-based) approaches to contracting out were bound to generate suspicion and resistance from trade unions – which in turn would impede discussions about ways of introducing workplace efficiencies.

A NSW Joint Parliamentary Committee report on its inquiry into *Competitive Tendering and Contracting in the NSW Public Sector* (1998) was highly sceptical about whether the analysis underpinning proposals for more extensive outsourcing was independent**:**

> The Committee remains concerned that the government relies heavily on CTC research obtained through a limited number of consultants. This trend also raises concern about bias and whether researchers have a vested interest in the outsourcing industry themselves.

The observations of this parliamentary committee only highlighted the fact that large-scale contracting out had been undertaken without effective oversight and scrutiny – and that many decisions to outsource had been made on the basis of incomplete, partial, or poor quality information.

On the basis of this past experience, it is not surprising to remain sceptical about Treasury claims of 'significant savings' from PPPs.

The 2005-06 Budget Papers go on to state:

> PPPs are not mechanisms by which the Government expands its available finance. With PPPs, the Government effectively substitutes one form of liability (balance sheet debt) for another (commitment to pay the PPP operator). Irrespective of the balance sheet treatment of PPPs, the Government's credit rating takes into account all forward financial liabilities including commitments to make PPP payments (*Budget Paper No 4*, p. 19).

The statements in this extract are nonsensical and are not based on the facts. The real test is whether the cost of the PPP is shown in the Government's 'balance sheet debt'. As admitted in the above extract, PPPs are not shown in the balance sheet. By definition, this means that they do indeed expand the Government's available finance.

Further the Budget Papers state:

> Therefore, the Government will only proceed with a PPP arrangement where it is satisfied that this is the best value-for-money option, in accordance with its well established guidelines (*Budget Paper No 4*, p. 19).

The claim that *'the Government will only proceed with a PPP arrangement where it is satisfied that this is the best value-for-money option'* is equivalent to the implied claim that the Government will only proceed with a PPP if it offers *'significant savings over conventional procurement options'*. The former implies that detailed analyses are undertaken to assess the options available to government. If that is the case, then such analyses – at least material projects - should be made available to the public.

3.4 CRITERIA FOR EVALUATING PPPs

Governments can not provide every service it wishes to see delivered to the community, on its own. Many elements of government service delivery are undertaken by contracting arrangements with private sector firms, or not-for profit NGOs.

If it is accepted that there is a place for PPPs as a means of supporting governments' efforts to provide services to the community, the following criteria have been suggested (Walker, 2002) for evaluating PPP proposals:

- Whether use of PPPs would permit the construction of infrastructure that otherwise would not be affordable
- Whether PPPs would enable government to benefit from new ideas, or new technologies
- Whether PPPs would enable 'politically difficult' projects to be undertaken (e.g. hospital car parks – given that spending from the health budget on car parking would be likely to attract criticism – provided pricing arrangements do not take advantage of a monopolistic position at a time when patients and their families are most vulnerable)
- Whether PPPs would enable state or local governments to engage in 'cost shifting' with the Commonwealth
- Whether PPPs ensure that risks are borne by the parties best able to manage them
- Whether PPPs enhance competitiveness by enabling benchmarking of performance of private sector operators against public sector operators
- Whether PPPs can utilise waste, or conserve resources
- Whether PPPs can provide additional uses for existing assets.

These criteria are more specific and targeted than generalised statements about securing 'value for money'.

Only some projects undertaken by PPPs in NSW appear to satisfy one or more of these criteria.

3.4 RECOMMENDATION

It is recommended that the PAC ask NSW Treasury:

- *To provide evidence that PPPs have produced 'significant savings', and explain how those estimates of savings were calculated.*

- *To explain the extent of losses incurred on unsuccessful PPPs, such as the Sydney Airport Rail Link, and what has been learned from that experience.*

4. NEW SOUTH WALES, AUSTRALIAN AND INTERNATIONAL LEGISLATIVE AND POLICY FRAMEWORKS AND PRACTICES REGARDING [ACCOUNTING FOR] PRIVATE SECTOR INVESTMENT IN PUBLIC INFRASTRUCTURE

4.1 BRITISH ACCOUNTING TREATMENTS

In Britain, there has been a curious debate about the treatment of public private partnerships in terms of the Blair Government's Private Finance Initiative (PFI). In 1994 the Accounting Standards Board (ASB) issued Financial Reporting Standard FRS 5 'Reporting the substance of transactions', which included statements about the need to reflect 'substance over form'. FRS 5 threatened to create difficulties when the Blair Government resolved to promote PPPs. Indeed, a government-sponsored 'Bates Report' of June 1997 proposed that the accounting treatments to be accorded PPPs needed to be resolved in advance and suggested that the Treasury should issue an interpretation pending resolution of the matter by the Accounting Standards Board.

To external observers, that in itself suggests that a major driver of PPPs was the wish to extend service delivery via privately-financed projects without increasing reported debt or reported liabilities. In due course, the UK Treasury issued its own 'Technical Note' in September 1997. That interpreted FRS 5 and the concept of 'substance over form' in a one–sided way, by focusing not on the total effect of a series of linked transactions, but by raising the question of **whether the exercise involved *the acquisition of an asset*** – and ***ignoring whether a government participant might have incurred a liability***. Along the way, the criteria for identifying 'assets' were also subtly re-interpreted. The definitions of 'asset' adopted by professional bodies generally refer to whether economic benefits are ***controlled*'** by an entity. The Technical Note used a different test**:** whether government had ***access*** to economic benefits.

It has been suggested that PPPs primarily involving the provision of assets should be interpreted in a similar fashion to finance leases. But (as with

Australian BOOT schemes) these arrangements also involve the provision of services. Contractual arrangements typically involve a combination of fixed fees (or service availability charge), and a variable fee, associated with the volume of services provided.

Arguably a key issue was whether PPPs established *liabilities* – an issue which commentators have agreed is of significance when analysing the financial record of governments, if only because of widespread interest in national levels of indebtedness and changes in the Public Sector Borrowing Requirement (see, e.g., Grout, 1997; Broadbent and Laughlin, 1999b). But the Treasury Technical Note focussed on whether a government agency could be regarded as having contracted to acquire an *asset* – and then decreed that if this was the case, both an asset and a liability should be recorded. Conversely – and this was far and away the more significant proposition - if there was no 'asset', there was no liability.

This was a novel way of analysing accounting issues. The common way of applying the concepts in profession-sponsored conceptual frameworks has been to look at a set of circumstances and not simply ask:

> Is there an asset?

but to ask two questions:

> Is there an asset?
> Is there a liability?

Yet the Technical Note only asked the first question, and accordingly only suggested that a liability would arise if there was a contract to acquire an asset. It avoided all discussion of the implications of *recognising a liability*, and the need to then consider whether the corresponding double-entry record should recognise an 'asset' or an 'expense'.

It seems odd that commentary on 'technical' issues associated with the treatment of PPPs also avoided the question of whether PPP contracts establish liabilities, and simply focused on assets. Broadbent and Laughlin (1999b), in a review of 'technical issues', asserted that 'the central question is whether, in accounting terms, PFI involves the purchase … of an asset and other services or only services (even if asset based)' (p.21). Similarly Australian observers, analysing accounting issues for PPPs, asserted that 'the party that bears the majority of the risk should recognise the *asset* on its balance sheet' (Grimsey and Lewis, 2002a, emphasis added). (The same authors, writing elsewhere, conceded that a PPP was 'essentially project financing' – see Grimsley and Lewis, 2002b).

Correspondingly, it seems noteworthy that British analysis of PPPs has interpreted these arrangements by analogy (are they equivalent to finance leases?) rather than from first principles (is there a liability'?).

The contractual arrangements for different PPPs may vary, but a common feature is that governments may be paying cash (or alienating revenues) to meet the cost of constructing infrastructure. That stream of payments ('sacrifices of economic benefits') may also encompass the provision in future periods of a range of services.

Plainly the Bates Report and the Treasury Technical Note put the ASB under some pressure. The Board had previously avoided issuing industry-specific standards, and had not previously been involved in public sector matters. Further, the Blair Government (and possibly many of the ASB's private sector constituency) wanted an answer that would allow PPPs to proliferate. The political processes surrounding the subsequent activities of the ASB thus deserved, and have been accorded, respectful attention (see Broadbent and Laughlin, 1999b; Hodges and Mellett, 2002).

The UK's Accounting Standards Board duly considered the Technical Note, and soon released an exposure draft proposing modifications to FRS 5. The ASB apparently accepted the UK Treasury's characterisation of the issues. Accordingly the 'key question' was 'whether a party to a PFI contract has an asset of the property used to fulfil the contract'. It did not present fundamental analysis about whether PPPs established liabilities, save through analogies with finance leases.

In the event, the Accounting Standards Board ended up proposing a more stringent test to avoid the recognition of PFI assets than that applied in the Treasury Technical Note. The modifications proposed to FRS 5 were mainly confined to explanations of how FRS 5 might be applied to certain forms of PFI contract, such as where there were 'non-separable service elements', or where PFI payments vary with factors such as usage of the property or a specific index that reflects the operator's costs'.

The Board duly amended its FRS 5 in September 1998. Subsequently Treasury issued a revised Technical Note (TN99) which 'appeared to allow most PFI deals to stay off the public sector balance sheet' (Hodges and Mellett, 2002).

The end result is that most PFI contracts were to be viewed as contracts for the provision of services, which may give rise to financial commitments, but those commitments were not to be regarded as giving rise to liabilities except to the extent that services have been delivered and sums are currently owing in terms of those contracts.

Presumably 'services' are to be interpreted in terms of units of service e.g. numbers of students taught in schools, or inmates contained in correctional facilities, or patients provided with medical or surgical treatment. The provision of infrastructure – school buildings, jails or hospitals – was seen as incidental. In that way, the Accounting Standards Board has re-interpreted the 'substance over form' test, by regarding the delivery of infrastructure assets as just another service.

In short, the UK's Accounting Standards Board, despite its claim to support a 'substance over form' approach, has been compelled to devise new notions of 'substance' in order to accept the essence of Treasury proposals that PPPs are to be kept off-balance sheet. One can only speculate what approach might have been adopted by the Board if it had previously endorsed a 'conceptual framework', incorporating a definition of 'liability' (as has been the practice of standard-setting bodies in the USA and Australia). For that reason, the UK's accounting standards and interpretations should not be regarded as providing authoritative guidance in Australia.

4.2 NSW ACCOUNTING TREATMENTS

There are as yet no accounting standards in Australia relating to the treatment of PPPs in public sector financial statements. In the absence of standards, practices vary. Meantime, Heads of Treasuries in Australia have been advocating standards that follow the UK approach, by focusing on whether public sector agencies or private sector partners have 'an asset', and invoking the analogy of lease accounting.

The following statement of accounting policies for the treatment of private sector infrastructure assets was included in the NSW Total State Sector Accounts 2003-04 (the latest available):

> Treasury has adopted the flowing policies pending the development of an accounting standard.
>
> Agreements Equally Proportionately Unperformed arising from private sector financed infrastructure arrangements are generally not recognised as assets or liabilities because there is significant uncertainty as to whether the definitions and recognition criteria in SAC 4 Statement of Accounting Concepts 'Definition and Recognition of Elements of Financial Statements" would be satisfied. Instead, the payments under these agreements are expensed systematically over the term of the agreements. Further, the commitments for future payments under these agreements are disclosed as "Commitments in the notes to the financial statements.
>
> However certain private sector financed infrastructure arrangements provide for a private sector entity to design, construct, operate and maintain certain infrastructure for a specified concession period, after which the infrastructure is transferred back to the State.
>
> The interest of the State in such arrangements is recognised as an asset, being the emerging interest in the remaining service potential to be transferred to the agency. The emerging interest is valued by reference to the State's emerging share in the written down replacement cast of the

> asset at the date of transfer. The emerging interest is progressively recognised from the date of completion of construction over the period of the concession agreement.

In other words, PPP contracts involving hundred of millions of dollars are said to be 'agreements equally proportionately unperformed', so they can be accounted for by treating period payments as payments for services rendered in that accounting period – the same way that businesses might treat rental payments for a photocopier.

Yet evidence available from some recent Victorian PPP contracts from the Kennett era, published by the incoming Bracks Government, suggests that off-balance sheet treatment is inappropriate (Walker and English, 2003). In the Victorian cases, while the execution of a PPP contract did not immediately establish liabilities of the public sector, that situation changed over time. Once a private sector partner had completed construction of infrastructure to contractual standards, that triggered an obligation to pay a 'facilities availability charge' over the life of the contract, with ownership of those facilities to be transferred to the public sector at the end of the contract term. After the construction phase, these arrangements meet all of the standard tests for recognition of liabilities: there is a present obligation arising from past transactions to convey economic resources to the private sector partner, and the quantum of that obligation can be measured reliably.

Accounting treatments remain contentious, though there are signs that rulings from the International Accounting Standards Committee may conflict with contemporary Anglo-Australian practice in accounting for PPPs. The International Financial Reporting Interpretations Committee has issued a series of 'draft interpretations' on the subject of what is now termed 'service concession arrangements'. While these only apply to the accounting treatments adopted by private sector partners (not public sector agencies), one of the proposals suggests that the partners should show as an 'asset' the sums due to be paid over the life of the contract by a public sector agency. A symmetrical treatment of this would be for public sector agencies to record a 'liability' for PPPs. However, in the currently-uncertain environment in which the IASB and its committees produce accounting standards and interpretations, it is difficult to predict whether this stance will be retained.

NSW Government guidelines have claimed that the accounting treatment of PPPs does not determine whether or not they will provide 'value for money':

> The achievement of 'off balance sheet' transactions is not a key driver for the Government in PFPs even though capital projects delivered without appearing on the Government's balance sheet may be financially beneficial (NSW Government, *Working with Government*, November 2001, p. 25)

Indeed, one could only hope that this is the case. Yet the same Guidelines suggest that the accounting treatment is regarded as an important consideration. Government agencies proposing PPPs are required to provide Treasury with details of the project, including a

> summary of [proposed] accounting treatments (p. 24).

and

> Agencies should refer to the relevant accounting standards proposed and, where reliance is being placed on professional accounting opinions, copies of these should be attached to the statement (p. 25).

Further,

> A Treasury determination of the accounting treatment to be adopted must be obtained before the contract is executed (p. 25)

And while the Guidelines go on to say:

> The accounting treatment is subject to audit by the Auditor-General (p. 25)

the Guidelines suggest that efforts are to be made to ensure that the Auditor-General will be consulted to ensure that the transaction will be subject to a particular accounting treatment (i.e. keeping liabilities 'off balance sheet') and thereafter will be committed to that interpretation:

> The Auditor-General should be consulted and advised on the form of the contractual arrangement to be included in the 'call for detailed proposals' as well as the likely accounting treatment for the transaction (p. 23).

For the purposes of the current inquiry, it is simply pointed out that ***if the driver for a PPP was 'value for money' not 'off-balance sheet financing', the question of what accounting treatments were appropriate would not arise before contracts had been executed.***

In fact, the NSW Government Green Paper, *Working with Government: Private Financing of Infrastructure and Certain Government Services in NSW* (November 2000) openly stated that accounting standards were a 'strong influence' on 'the way Government does business' (p. 13). And that 'projects in which capital raising is considered a liability on the Government balance sheet could still proceed, but only if the delivery agency is able to bear the capital cost within its budget' (p. 16).

Frankly, any suggestion that accounting treatment is not a key driver of PPPs ignores the history of these arrangements, ignores the above, previously published statements, and insults the intelligence of the community.

However, given the acknowledgement of NSW Treasury that

> the contractual commitments to pay for the availability of infrastructure are just as real [as borrowings] regardless of how they are accounted for (Pierce, 2002, p.9)

one could only expect that Treasury would not object to the following recommendation, relating to the disclosure of commitments in terms of PPP contracts currently on foot.

Requirements for the disclosure of 'commitments' that are not otherwise recognised as liabilities have been in place in Australia since 1984 amendments to the (then) Companies Act and Codes. Common disclosures made by both public and private sector entities encompass operating leases and the nominal sums payable for finance leases – rather than the 'net present value' of those obligations that are required to be recognised as liabilities in financial statements.

It is noted that the NSW Total State Sector Accounts 2003-04 (the latest available) do report some information about 'commitments', for *some* PPPs. Expenditure commitments for capital expenditure totaling $3.74 billion is described as 'including private sector financed infrastructure assets'. The extent to which that relates to PPPs is not revealed

A further section in these financial statements refers to amounts payable in terms of contracts described as 'major service agreements for filtered water by Sydney Water Corporation'. The sums disclosed are $516 million within five years, plus $443 million for sums payable beyond five years. (The latter sum has been calculated using a present value calculation, and a discount rate of 11.28% - a step which significantly reduces the reported value of those commitments, and is quite contrary to the usual accounting practice of reporting commitments at nominal or estimated nominal values, not present values.)

However these disclosures do not really encompass sums expected to be derived from private sector partners operating PPPs in which revenues are derived from user charges. It is noted that the 2004 accounts for the RTA – the agency responsible for sponsorship of most of NSW's major PPP contracts - do not provide any information regarding commitments to make payments arising from the private sector financing of infrastructure. Arguably, this is because the funds derived from operators come not from the RTA but from 'user charges'.

But disclosure of the sums derived by private sector operators from public infrastructure (under licence from the State) would be important to ensure the accountability of government for their role in entering into past and future transactions of this type.

4.3 RECOMMENDATION

It is recommended that:

- *The PAC propose that, in addition to current disclosures of commitments to undertake capital expenditure, the NSW Treasury be asked to calculate and report in notes to the Total State Sector Accounts (consolidated statements):*

  The fees expected to be derived by participants in currently-operating PPPs, from user charges, having regard to the profit-sharing arrangements specified in any base case financial models for those projects.

- *The notes should report this information in conjunction with a separate line showing the amount of financial commitments arising from contracts to pay for the availability of private financed infrastructure.*

- *These disclosures should separately state amounts payable, or expected to be derived by private sector partners*

  not later than one year
  amounts payable later than one year and not later than five years, and later than five years

  and should report estimated nominal values of those sums (not present values calculated by discounting).

5. GOVERNMENT MODELS FOR EVALUATING AND MONITORING PRIVATE INVESTMENT IN PUBLIC INFRASTRUCTURE [& AGENCIES' FAILURES TO IMPLEMENT THEM]

The NSW Government has issued several documents outlining its approach to future capital projects:

A Green Paper, titled *Working with Government: Private Financing of Infrastructure and Certain Government Services in NSW,* November 2000.

A set of Guidelines, *Working with Government: Guidelines for Privately Financed Projects*, November 2001, which reflected agreed Government policies for the evaluation of PPPs and for subsequent accountability arrangements.

A Strategic Plan – *State Infrastructure Strategic Plan 2002*, December 2002, which detailed a series of projects. As a first cut, it deserves acclamation – particularly as it was to be reviewed on an annual basis.

These promised a systematic approach to the management of infrastructure development – though there are some systemic flaws. While the Guidelines imply a (relatively) open and transparent approach to the disclosure of the case for PPPs (through publication of a 'Public Sector Comparator' or PSC) the Guidelines incorporate three fundamental flaws. They:

- do not require disclosure of the proposed revenues associated with a project if it is to be privately-funded;
- do not require disclosure of what discount rate is to be used to assess the relative merits of the government delivery of projects versus a proposed PPP;
- instead of requiring disclosure of projected cash flows, propose the calculation of hypothetical costs and questionable adjustments for risk.

In summary, they are fundamentally biased in favour of PPPs.

A major element of this submission is to outline the basic components of a more relevant form of PSC that would meet the Government's objectives of ensuring a fair and transparent tender process and a value for money outcome for the Government and community.

5.1 GOVERNMENT POLICIES HAVE NOT BEEN IMPLEMENTED: THE INFRASTRUCTURE COUNCIL

The Government's Guidelines published in November 2001, announced the setting up of:

> a NSW Infrastructure Council, comprising of key Ministers and invited chief executives of private sector organisations representative of those involved in the provision of infrastructure (*Working with Government: Guidelines for Privately Financed Projects*, November 2001, p. 4)

This commitment was repeated in the *State Infrastructure Plan 2002* which referred to:

> The establishment of the NSW Infrastructure Council as a peak forum for considering strategic infrastructure issues with membership of senior Government ministers, senior executives of the private sector and representatives of the union movement (*State Infrastructure Strategic Plan 2002*, December 2002, p. vi, p. 2).

A search of the internet reveals very little information on this Council. The search reveals that:

- Mr Wal King, the Chief Executive Officer of Leighton Holdings Limited has been appointed a Founding Councillor of the Council. This information is on the UNSW website which shows the bios of the Board of Directors of the University of NSW Foundation; and

- Engineers Australia was asked to nominate someone for the Council. This information is contained in an Engineers Australia publication, *Engineers Australia Policy Update 1/04* which states that:

> Sydney division has been asked to nominate a member to form part of the Premier’s Infrastructure Council. This appointment has the potential to enable closer relations with government in the future.

Information about other members (if appointed), and how frequently the Council has met, and with what result are not known. Centennial Consultancy has been advised that Unions NSW was invited to participate in the Council but that the Council has only met a couple of times and not since the last election.

The Council's own website reveals very little information indeed (see Appendix C). It simply states:

> More information on the NSW Infrastructure Council will be available shortly (*Internet site of the New South Wales Infrastructure Council, accessed 26* September 2005).

The website states that it was:

> Last updated 17 March 2004 (*Internet site of the New South Wales Infrastructure Council, accessed 26* September 2005).

These facts compel the conclusion that little progress has been made in implementing the Government's policies in this area.

5.2 GOVERNMENT POLICIES HAVE NOT BEEN IMPLEMENTED: THE INFRASTRUCTURE STRATEGIC PLAN

The NSW Government Guidelines also included a commitment to publish a State Infrastructure Strategic Plan (SISP) annually.

The Guidelines state:

> A State Infrastructure Strategic Plan (SISP) will be published annually (*Working with Government: Guidelines for Privately Financed Projects*, November 2001, p. 4)

The first such Plan was published in 2002 and it contained the following commitments:

> The Plan will hereafter be updated every year in light of changing community needs and priorities (*State Infrastructure Strategic Plan 2002*, December 2002, Premier's Foreword).

And:

> The SISP will be reviewed and updated annually to take into account both changes in the needs of the community and changes in the planning of services and infrastructure by State agencies. As a result, the SISP will be a living document – not one fixed at a point of time (*State Infrastructure Strategic Plan 2002*, December 2002, p. v).

Almost three years later, a revised and updated Plan has yet to be issued.

5.3 GOVERNMENT POLICIES HAVE NOT BEEN IMPLEMENTED: THE PUBLIC SECTOR COMPARATOR

One of the key elements of the NSW Government Guidelines was the proposition that proposals for PPPs would involve the calculation of a Public Sector Comparator:

> the hypothetical risk-adjusted cost of government delivering the required project outcomes

to enable 'true comparisons between service delivery options' (*Working with Government: Guidelines for Privately Financed Projects*, November 2001, p. 4).

The underlying idea is that government agencies should assess what would be the most efficient way for the public sector to undertake a specific project, and to use those estimates as the basis for evaluating other options to ensure that 'value for money' was achieved for taxpayers. The idea of a Public Sector Comparator was introduced by the UK Treasury in what was described as its Private Finance Initiative or 'PFI'. The idea has been copied in Victoria in a document titled *Partnerships Victoria* (2001) and also in Canada (2003). NSW, in turn, has followed the Victorian Guidelines.

To quote from the 2001 NSW Guidelines:

> A PSC:
> - is based on the most efficient likely method of providing the defined output currently available to the public sector;
> - takes into account the potential impact of risks on the costs (and revenues) associated with a proposal over its life
> - is expressed in terms of the net present value (or benefit) to government of providing the output, over the life of the proposed concession
>
> The PSC reference project will be defined and costs to provide the same level and quality of service expected of the private sector (p. 45).

The Guidelines unequivocally indicated that the findings of this form of analysis would subsequently be published in contract summaries, and hence made available to the public.

> The results of the PSC will ultimately be publicly available in the contract summary (p. 46).

This has not happened (see the review of published contract summaries, below) – save for an incomplete presentation from one agency.

As noted above, it is contended that the Guidelines for the PSC were fundamentally flawed. However the idea of providing a full financial analysis of the projected cash flows from the alternatives of government delivery versus PPPs is supported in the interests of accountability.

When the Government Guidelines were initially published in 2001, many in the community (including trade unions, and other stakeholders) were re-assured by these commitments to undertake rigorous and systematic comparisons of the cost of undertaking a project by the public sector, versus the private sector, and the promise of transparent disclosures.

The publication of the PSC was supposed to assure the community that Government had learned from past experience, and was committed to a more open and transparent process.

It is with deep concern that it is noted that these commitments were not met. It is submitted that the reasons for the failure to implement Government policy should be a central focus of the current PAC inquiry.

5.4 RECOMMENDATION

It is recommended that the PAC enquire:

- *Why the public service has not ensured that Government policy for the publication of the results of PSCs in contract summaries was implemented.*

- *About the extent to which agencies analyse the projected cash flows from the alternatives of government delivery versus PPPs, and the depth in which those analyses are undertaken.*

- *As to when that analysis is undertaken, vis a vis announcements that specific projects will be considered as possible future PPPs (such as were announced in the State Infrastructure Strategic Plan 2002), or when negotiations are undertaken with proponents of PPPs.*

5.5 GOVERNMENT POLICIES HAVE NOT BEEN IMPLEMENTED: PROMISED GUIDELINES ON THE PSC HAVE NOT BEEN PUBLISHED

Given that it is NSW Government policy to prepare and compile a PSC for proposed PPPs, it is also disappointing that further details have not been made available concerning how this management tool is being used.

Full details of what would be incorporated in the PSC were not provided in the Guidelines, but further details were to be provided later:

> The structure of a PSC, selection of an appropriate discount rate for comparison of alternatives, and budget treatment of capital and recurrent expenditure are all examples where change is expected as experience is gained. Details of these and other such areas will be promulgated in implementation guidelines and Treasury circulars (p. 5)

A search of the Treasury website indicates that no further details have been published. In particular, Treasury publications such as

> *Economic Appraisal: Principles and Procedures Simplified* (TPP 99-1, 1999)
>
> *Financial Appraisal Guidelines* (TPP 97-4, 1997)
>
> *Guidelines for Economic Appraisal* (TPP 97-2, 1997)

have not been updated since publication of the 2001 Guidelines.

One would expect to find detailed discussion of what costs should be counted, how allowances should be made for risks, and how comparisons were to be made between the PSC and a PPP proposal from a private sector consortium.

For example:

- Should the PSC include estimates of the government's direct costs, or should some element of overheads be included?
- If overheads were allocated – what basis should be used?
- What allowance should be made for unforeseen costs or cost overruns?
- Should risks be handled by undertaking multiple calculations by manipulating key variables, having regard to 'worst case' or 'most probable' or 'best case' scenarios? Or should hypothetical estimates be made of 'the cost of risks'?

Rhetoric about the calculation of a PSC was intended to provide reassurance that PPP proposals would be evaluated systematically and rigorously.

The PAC should be concerned that the claims made about the use of the PSC have not been discarded. Talk about the PSC was of symbolic significance only – it does not appear to have been taken seriously as a management tool. Or, if PSCs have been calculated, they may only have been used to legitimise decisions to enter into PPPs that were not always in the best interests of stakeholders.

5.6 HOW THE PUBLIC SECTOR COMPARATOR MIGHT BE USED (OR ABUSED)

In the absence of detailed guidelines on these issues, the following notes explain what might be expected to be presented if a detailed PSC was published for two basic classes of PPPs:

a. projects involving government paying a consortium (or other private entity) fees for the provision of infrastructure and/or services for the use of those assets;

b. projects in which the private sector constructs public infrastructure and derives revenues from the public.

The following notes will also demonstrate what the PSC statements should include if the Government's promises about disclosure are to be met, for different forms of PPP contractual arrangements.

a. Projects funded by government payments of fees

A valid comparison of the relative merits of a government-funded and operated project versus a PPP would require consideration of both:

- financial factors; and

- non-financial factors (since the role of government is not to 'make a profit' but to provide services to the community).

The following analysis focuses on financial factors.

On the face of it, it would be possible to design a standard format for comparing a government-funded project and a proposed PPP. That format would examine the amount and timing of future cash flows, and the potential variability of those flows, and seek to convert them to a common denominator by converting them to an estimate of 'net present value'.

For simplicity, assume initially that the cash flows associated with such a project – the provision of a school, jail or hospital - are all negative.

Illustration 1:

Government cash flows
Self-funded infrastructure project v. PPP

Year (say)	Main cost elements	Cash flows: PSC	Cash flows: PPP
0	Preliminary scoping	- X	- X
1	Design fees	- X	
2	Tender costs	- X	
2	Contract negotiations		- X
3-5	Construction costs	- X	
5	Ancillary services e.g. utilities	- X	- X
6 onwards	Operating expenses	- X	
6 onwards	Contract monitoring and supervision costs		- X
6 onwards	Facilities availability charge (payable to PPP counterparty		- X
6 onwards	Variable charges linked to usage volumes (payable to PPP counterparty)		- X

In a simple case as in Illustration 1, a relevant 'Public Sector Comparator' could be readily calculated: it would be the Net Present Value of the cash flows from the self-funded project (column 3).

The PSC could then be used to compare the pricing of the provision of similar or equivalent services from a private sector counterparty (as set out in column 4 above).

Illustration 2 assigns some numbers to those various cash flows. The example is necessarily simplified[4], but the selection of elements is based on the structure of a number of actual PPP projects and associated contracts.

One point perhaps deserves mention. As mentioned above, it is a matter of some notoriety that a prior NSW Government advocated 'contracting out', claiming that such an exercise could achieve savings of some 20% per annum. The validity of such claims (and of the evidence on which they were based) was the subject of some contention. However one fact which emerged was that the claims about 'savings' did not take account of the costs of monitoring compliance with those outsourcing contracts.

[4] E.g. It is assumed that all cash payments are made as single instalments at the end of each year.

Hence it is contended that any comparison of the PSC calculation with the effective cost to government of a PPP deal *should include an allowance for the costs to Government of monitoring that PPP*. Such figures have been included in Illustration 2 below.

Illustration 2

Government cash flows
Self-funded infrastructure project v. PPP

Year	**Main cost elements**	**Cash flows: PSC** $m	**Cash flows: PPP** $m
0	Preliminary scoping	- 0.5	0.5
1	Design fees	- 4.0	
2	Tender costs	- 1.0	
2	Contract negotiations		- 2.0
3	Construction costs	- 100	
4	Construction costs	- 100	
5	Construction costs	- 100	
5	Ancillary services e.g. utilities	- 10	- 10
6 -26	Operating expenses	- 40 pa	
6-26	Contract monitoring and supervision costs		- 0.5 pa
6-26	Facilities availability charge		-70 pa
6-26	Variable charges linked to usage volumes		- 39 pa
0	**Net present value r = 19%**	**245.31**	**236.75**

In the above calculation:

- the PSC produces a net present value of projected cash flows of $245.31 million – which is greater than the net present value of the outlays facing government from a PPP of $236.75 million;

- the PPP promises to lower operating costs to government from running the facility from $40 million per annum to $39 million per annum (possibly through employing non-award staff on individual contracts);

- the PPP would also avoid the need for government to borrow in excess of $300 million to fund the capital costs of the project (construction costs $300 million, plus $5 million for design fees and tender costs);

- because of the number of projects competing for funding, the PPP option might also be seen as enabling government to undertake this project sooner rather than later. (Indeed, this claim is commonly advanced by proponents of PPPs – but it is fallacious.)

On the face of it, the PPP deal in Illustration 2 would be a win-win for government and the private sector.

However *the net present value figure in Illustration 2 was calculated using a discount rate of 19%* (which is around what NSW Treasury might argue is an appropriate 'weighted average cost of capital' for a project involving construction and the provision of human services).

For the moment, disregard the relative quality of services provided by public sector agencies and private sector providers – and assume that the services provided would be of equivalent quality. The project is capital intensive, and even though the private sector provider may be able to provide day-to-day costs at a cheaper rate, the cost of providing the infrastructure assets is the key driver of the costs of conventional delivery versus PPP.

If a PPP was adopted in this case:

- the government *would be providing the private sector counterparty a rate of return of 19% per annum, mainly for the use of private sector funding to purchase new infrastructure;*

- rather than providing 'savings' to government, the PPP would actually be far more expensive than public sector service provision – given that a government (such as NSW) has the capacity to borrow funds at rates less than the 'private sector cost of capital' (here assumed to be 19% per annum);

- similarly, the claim that the PPP would allow priority projects to be undertaken 'sooner rather than later' is illusory; if projects deserve to be given priority, then they could be funded from reasonable levels of borrowing (particularly given the strength of the State's balance sheet);

- in any event, while the form of the contractual arrangements commonly entered into PPPs of this structure – requiring a series of payments for 'facilities availability' - do not establish 'liabilities' *at the inception of the contract*, it is inescapable that once infrastructure has been constructed and the government faces an obligation to make those payments, this should properly be regarded as leading to a situation where the government faces a liability, which should be recorded as such. Even if the payments for 'facilities availability' and variable charges for usage (or per student, per inmate, or per unit of service) are bundled together and relabeled, the substance of the arrangement does not change[5].

Consider the impact of the use of a different interest rate on the calculation of the PSC.

Instead of using a high discount figure representing a market-determined private sector cost of capital, the next illustration uses a discount rate that:

- reflects the rate at which governments could borrow, and
- includes an additional risk premium.

Illustration 3 assumes the same cash flows as in Illustration 2, but discounts them at the rate of 8% per annum (not 19% as in Illustration 2).

Illustration 3

Government cash flows
Self-funded infrastructure project v. PPP

Year	**Main cost elements**	**Cash flows: PSC** $m	**Cash flows: PPP** $m
0	Preliminary scoping	- 0.5	0.5
1	Design fees	- 4.0	
2	Tender costs	- 1.0	
2	Contract negotiations		- 2.0
3	Construction costs	- 100	
4	Construction costs	- 100	
5	Construction costs	- 100	
5	Ancillary services e.g. utilities	- 10	- 10
6 -26	Operating expenses	- 40 pa	
6-26	Contract monitoring and supervision costs		- 0.5 pa
6-26	Facilities availability charge		-70 pa
6-26	Variable charges linked to usage volumes		- 39 pa
	Net present value r = 8%	**505.00**	**716.33**

[5] The Secretary of NSW Treasury, Mr John Pierce, has acknowledged this: 'the contractual commitments to pay for the availability of infrastructure are just as real, regardless of how they are accounted for' (Pierce, April 2002, p.9).

The effect of changing the interest rate is to reverse the rankings of PSC versus PPP. In Illustration 3, the PSC would be the preferred option, as the Net Present Value of future payments is less than that for the PPP.

The two approaches are summarised below.

Table 5.1
The impact of different interest rates

Discount rate	Net present value – PSC (government-funded project)	Net present value - PPP	Decision indicated
	$m	**$m**	
19% pa	**245.31**	**236.75**	**Accept PPP**
8% pa	**505.00**	**716.33**	**Reject PPP**

Use of an 8% discount rate (rather than the 19% rate in Illustration 2) totally changes the PSC from being more expensive than a PPP, to the reverse.

That should not be surprising. If government runs a nursing home or hospital or a facility to care for the disabled, it endeavours to do so as efficiently and effectively as possible. When a private sector firm undertakes such an activity. It does so with the aim of making a profit. Hence the private sector may use high discount rates in order to screen potential projects, and to ensure that only the most profitable are entered into. Discount rates of 25% before tax are not uncommon. Anecdotal evidence suggests that some firms have used discount rates as high as 50% in order to ensure that the firm's scarce capital resources were only directed to the most profitable investments.

However the discount rates used by private sector managers in tight capital rationing situations are not at all relevant to evaluations of what investments deserve to be made by government in the public interest. Nor are discount rates calculated by reference to notions of what 'financial returns would be demanded by private sector investors' relevant to decisions made by governments in the interest of the community.

It is noted that the 2000 NSW Government Green Paper on Private Financing of Infrastructure Projects incorporated an extreme view about the choice of discount rates. Under the heading, 'Cost of public versus private finance', it stated:

> That the public sector can generally raise debt at a lower cost than the private sector is an indication of the public sector's superficially lower cost of capital. This would suggest that private financing of infrastructure is relatively inefficient and that the economic benefits would be maximised by public financing. However ***to ensure efficient use of resources, the same cost of capital should be used for both sectors for assets of***

the same risk characteristics when investment decisions are made about public sector projects (pp. 28-29, emphasis added).

(This passage was omitted from the later-published NSW Guidelines, but may still reflect Treasury's thinking and advice to agencies – a matter the PAC is invited to explore.)

b. Projects in which private sector firms construct infrastructure and derive revenues from the public.

Government policy is for the development (and publication) of a Public Sector Comparator for all proposed PPPs, including tollway or tunnel projects.

As discussed further below, published contract summaries have not included details of the PSC previously prepared for those projects. Rather, they have redefined or misrepresented the Guidelines as requiring statements to the effect that the project was beneficial to the sponsoring agency, or that it had a positive 'benefit cost ratio' (without explaining the basis on which non-financial benefits were valued, or the range of costs that were considered.

Even though PPP contracts are not widely available, and considerable efforts have been made to keep their contents secret, some information about the structure of tollway contracts has been gleaned from direct inspection, from contract summaries, from summaries contained in prospectuses, and other sources.

The basic structure of PPP arrangements in which the private sector is to construct public infrastructure and derive revenues from the public, is as follows:

- Contracts and deeds identify the responsibilities of the respective parties during the *construction phase* of the project. For example, the public sector agencies are responsible for providing the 'corridors' in which roads or tunnels are to be constructed, by a certain date, and also to construct ancillary utilities (drainage, power connections etc).

- Further contracts and deeds identify the responsibilities of the respective parties during the *operating phase* of the project. These may include obligations to maintain the infrastructure to a specified standard, or to undertake restoration work (e.g. re-sheeting of road pavements) at specified intervals.

- Documents detailing responsibilities of the parties may cover not only what the respective parties are obliged to do, but may also cover what the government agency is not permitted to do, without paying compensation to the private sector partner (e.g. improve public transport in designated areas, thus affecting the revenues of the consortium).

- Documents specify the basis upon which charges to users of the infrastructure (tollways or other transport infrastructure) will be calculated; commonly these provide for charges to be increased in conjunction with increases in the Consumer Price Index.

- Documents may specify the operator is to make certain payments to the government agency during the life of the project (e.g. rental of the tollway corridor); these payments may be deferred until such time as the operator has recovered its capital investment (e.g. documents regarding the M2 Tollway provided that rental payments to the RTA were to take the form of promissory notes to accumulate to some $400 million before they were payable – a fact not disclosed in a prospectus for Hills Motorway that was published around that time).

- Documents may detail the basis upon which revenues are to be shared between the parties. Such a document – titled the 'base case equity model', 'base case financial model', or similar – is commonly treated as being 'commercial in confidence', probably because it would enable analysts to assess the estimated profitability of the project to the operator. Profit sharing arrangements may involve (say):

  80% of the revenues going to the operator until it had received $x million (representing the operator's estimated initial capital costs);

  thereafter revenues being shared between the operator and the government in the ratio (say) 70% - 30% until (say) returns to the operator represented a return of (say) 12% per annum, cumulative;

  thereafter revenues being shared (say) 60% - 40%, until a 'cap' internal rate of return of (say) 18% was achieved;

  thereafter additional revenues being shared 50% - 50% for the remaining term of the contract (say, 30 years).

  Save that the duration of the contact would be extended until such time as the operator had enjoyed a cumulative rate of return of (say) 18%.

- Contracts provide that at the end of the contract term, ownership and control of the infrastructure assets constructed in terms of the PPP are to be transferred to the government[6].

[6] Some Victorian PPP contracts used a form of words relating to asset transfers that apparently was intended to avoid having to regard the contracts as establishing 'liabilities', and for payments for bundled services not be regarded as including payments for the construction of infrastructure i.e. they provided for land to be leased to the operators, and that possession of the land (only) to revert to the government at the end of the contract term – without any mention of the fact that the land would not have a prison or hospital built upon it (and without any requirements for the operator to bear the costs of demolition of those structures).

There may be variations on these conditions including the following.

Developer's fee: some contracts provide for the private sector partner to provide a fee to the sponsoring agency to compensate the latter for prior costs incurred in developing projects. (e.g. the RTA's accounts for the year ended 30 June 2003 recorded as revenues $290.4 million received from consortia engaged in PPP projects, a sum that was described as 'reimbursement of Development Costs').

Price escalations: the Cross City Tunnel provided that tolls would be increased at the *greater* of 4% or the CPI – thus effectively providing for financial returns to be 'sweetened' during the course of the contract. (Similar provisions were included in Melbourne's Transurban contracts.)

Term of the contract: some contracts may specify a term, but be subject to early termination clauses. Others may provide for the term of the contract to be extended until such time as equity investors have obtained a specified cumulative (and inflation-adjusted) rate of return (during the original term, plus extensions) as specified.

Profit caps: the 2000 NSW Government Green Paper noted that the Government was

> Conscious of the need to maintain a balance between government and private operators equitably sharing in any profits which result from faster than anticipated revenue growth (pp. 29-30)

While recognising that individual contracts may include variations of common arrangements, the following illustrates the basic elements to be considered in a Public Sector Comparator for a BOOT-style PPP.

Government cash flows
BOOT-style PPP

Year (say)	Main cost elements	Cash flows: PSC	Cash flows: PPP
0	Preliminary scoping	- X	- X
1	Design fees	- X	
2	Tender costs	- X	
2	Contract negotiations		- X
3-5	Construction costs	- X	
5	Ancillary services e.g. utilities	- X	- X
6 onwards	Operating expenses	- X	
6 onwards	Contract monitoring and supervision costs		-X
6 – onwards	100% of revenues from tolls – per base case forecasts	+X	
	Minimal percentage of tolls until partners have earned pre-specified cumulative rates of return		+ X

As shown above, these cash flows could be discounted to calculate the Net Present Value of the alternatives. The key elements would be estimates of construction costs and estimates of toll revenues. However the transaction costs in such an arrangement may be considerable – well above the costs of simply calling for tenders for private sector firms to construct infrastructure.

Rather than present hypothetical figures to illustrate a relevant PSC for a BOOT scheme, reference can be made to analysis of draft contract documents for the (failed) Airport Rail Link scheme (as summarised in Walker and Con Walker, 2000). While the scheme failed to achieve target usage volumes (and led the NSW Government to incur substantial costs), the PSC would have shown:

- That had the scheme been retained in government hands, and had the forecast tolls been achieved, the Net Present Value of the self-funded option would have far exceeded the NPV of the PPP option.

- The PPP option, entered into by the Fahey Government, saw the State of NSW incur 79% of the costs of the overall project, incur most of the construction and patronage risks, yet stood to earn an internal rate of return of only 2% pa if forecast traffic volumes were realised.

Had a detailed PSC in the form outlined above been made available for public scrutiny, then the NSW Government may not have proceeded with the project.

While the Airport Link Project failed, it is commonly accepted that many transport-related PPPs involving tollways have promised earnings of the order of 18% pa on funds invested – and have exceeded those targets.

It is contended that the PSC should take the above form.

5.7 NSW GUIDELINES ARE FLAWED AND BIASED IN FAVOUR OF PPPS

Even though they do not appear to be followed in practice, there are concerns that the drafting of the NSW Guidelines is inappropriate, and is systemically biased towards justifying or legitimising PPPs.

Illustration 2 (above) used some simple assumptions about projected cash flows. As noted above, the Guidelines state that the PSC should reflect

> the hypothetical risk-adjusted cost of government delivering the required project outcomes (*Working with Government: Guidelines for Privately Financed Projects*, November 2001, p. 4)

The NSW Guidelines do not illustrate what is meant by a 'hypothetical risk-adjusted cost to government'. However an illustration of this concept is provided in Canadian Guidelines on the preparation of a Public Sector Comparator. The example assumes:

- that a project involves capital outlays of $100 million.
- that there is a 50% probability that the public sector would experience a 20% overrun on costs.

This is then quantified: the hypothetical cost for use in the PSC should not be $100 million, but

Expected cost	$100 m
plus	
Allowance for risk	
Expected cost overrun 20% = $20 m	
Probability 50%	
Allowance for risk = 50% of $20 m	20 m
Hypothetical risk adjusted cost	$120 m

(Source: *The Public Sector Comparator: A Canadian Best Practice Guide*, May 2003)

Plainly such adjustments would make the PSC look expensive.

The validity is also questionable, since the public sector routinely calls for tenders and then contracts out construction projects to the private sector. Arguably many if not most 'cost overruns' are due to design changes during the course of the project.

Accordingly, the allusions to 'public sector cost overruns' are probably equally applicable to PPPs – particularly if contractual arrangements are to provide that the Government (not the private sector) will meet the costs of cover overruns incurred by the private sector partner.

In any event, arguably most 'cost overruns' are attributable to *design changes* in the course of the project. Given that 'Government in principle' approval for PPPs tends to be given in advance of detailed design work, it follows that if PSC calculations are to allow for the public sector to experience an overrun in costs, then there is no point in comparing such a PSC calculation with a PPP proposal if the latter is to incorporate contractual arrangements that require the public sector meet the cost of such changes. The original design for the Cross City Tunnel, for example, had an entry point adjacent to the Sydney Museum (see Contract Summary, p. 6); later design modifications saw the entry point located east of Kings Cross.

Moreover, some contracts have extended the impact of design changes to require additional compensation for changes in maintenance charges and profit margins (see e.g. Contract Summary for the Lane Cove Tunnel, pp. 18-19 under the heading 'Changes to the scope of works').

Further, to be consistent with the PSC, the evaluation of PPP bids should similarly assign a value to the *risk of failure of the project* and what that might cost. It is not known whether such exercises have ever been undertaken by Government sponsors of PPPs. (Certainly the NSW Government Guidelines on the evaluation of PPPs through use of a PSC make no reference to the need for such an assessment to be undertaken and quantified).

But, more importantly, the use in the calculation of a PSC of both:

- 'hypothetical risk-adjusted costs', and

- high discount rates to reflect risks

is fundamentally flawed. It involves *double counting* – further biasing evaluations against the option of public sector delivery of capital projects.

(It is noted that the Canadian Guidelines, which explained 'hypothetical risk-adjusted costs', chose to illustrate the evaluation of PPPs using a discount rate of 6%. Similarly illustrations in the Victorian guidelines on use of a PSC employ a discount rate of 6% when referring to cash flows in 'real terms', or 8.5% if inflation is running at 2.5%).

In any event, one of the questions that has been asked for around 40 years in discussions of business finance is this:

> If a project is viewed as high risk, why should cash outflows and cash inflows be discounted at the same discount rate? After all, we know that there is minimal risk that the cash *outflows* will have to be made – why not discount them at the risk free rate, while discounting cash *inflows* at a higher rate?

The general consensus seems to be that potential variability in financial returns is better handled by standardising the interest rate and undertaking multiple calculations to highlight the range of potential outcomes that might be attributable to variability in revenues, or other variables.

In summary: **the NSW Guidelines for calculations of the PSC are fundamentally *biased against the option of direct public sector investment in infrastructure projects*, by combining the use of 'hypothetical risk-adjusted costs' with the use of high discount rates, supposedly to reflect risks.**

In recent years some have taken an extreme stance in advocating the use of a 'market determined' high discount rate – based on calculations of a private sector's weighted average cost of capital for investment in equivalent projects - when undertaking evaluations of this type in the public sector.

No governments – in Australia or internationally – appear to evaluate public sector projects by using discount rates based entirely on the 'private sector cost of capital' for specific projects. The closest some may come to this stance is by reference to a concept of the Weighted Social Opportunity Cost of Capital (WOSC) – which has regard to the proportion of resources for government projects that comes from displacing private sector investment, by borrowing from foreigners, and from displacing domestic consumption. WOSC is the weighted average of these three rates (one being the private sector cost of capital)[7].

Recently-published Canadian Guidelines explained that 'discount rate' is:

> The rate used to calculate the net present value of future cash flows; usually determined on the basis of the cost of capital used to fund the investment from which the cash flow is expected (p. 39).

Another passage was somewhat equivocal:

> The discount rate to be used should reflect the public sector value of money plus a possible premium for the systematic risk inherent in the

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[7] For a discussion of this and related concepts see Boardman, Greenberg, Vining and Weimer, *Cost-Benefit Analysis, Concepts and Practice, Prentice-Hall,* 2nd ed., 2001, pp. 227-265.

> project. It can be argued that the public sector should use the private sector's cost of capital which takes the risk into account…. (p. 19).

However when these Guidelines came to illustrate the calculation of a PSC, they use an interest rate more in line with the rates traditionally used as reflecting a social discount rate:

> The discount rate (cost of capital) is assumed to be 6% (Industry Canada, *The Public Sector Comparator – a Canadian Best Practice Guide*, May 2003, p. 18.)

The consensus in that literature is that the 'social discount rate' – the discount rate to be used to evaluate the merits of government-funded projects – should be close to the rate at which governments can borrow, subject to adjustments to reflect a modest risk premium (say 2%).

What discount rates are used in practice? Many use 'real' discount rates representing the government bond rate (or similar), adjusted for inflation, and then apply the discounting calculation to projected costs in the future, without any adjustments for future inflation. A standard text on cost benefit analysis describes North American practices in these terms:

> In North American jurisdictions, the prescribed discount rates for federal agencies have tended to be fairly high, but they have been trending lower. For example, in the 1970s and 1980s, the U.S. Office of Management and Budget (OMB), which guides the cost-benefit analyses of all U.S. executive branch agencies, required most agencies to use a real discount rate of 10 percent. This rate was intended to approximate the opportunity cost of capital, measured as the real marginal before-tax rate of return on private investment. In 1992, the OMB revised this real rate downward to 7 percent (OMB A-94). This new rate was based on low-yielding forms of capital (e.g., housing) as well as high-yielding corporate capital.
>
> The General Accounting Office (GAO) and the Congressional Budget Office (CBO), both of which are U.S. congressional oversight agencies, use lower rates that depend on the U.S. Treasury's borrowing rate. The CBO generally favors the use of a rate based on the marginal social rate of time preferences. It has estimated the real historical yield on U.S. government securities at 2 percent and suggests the use of this rate plus or minus two percentage points. Based on the Fisher model of interest rates, the GAO uses the existing average nominal yield on treasury debt maturing between one year and the life of the project, less the forecast rate of inflation. There are a number of exceptions for all agencies.
>
> A recent proposal by the U.S. Panel on Cost-Effectiveness in Health and Medicine recommends the use of a real 3 percent discount rate for cost-effectiveness studies, with sensitivity analysis at rates between 0 percent

> and 7 percent. Similarly, U.S. municipalities that do discount also use a rate around 3 percent.
>
> Since 1976, the Federal Treasury Board Secretariat in Canada has recommended the use of a real discount rate of 10 percent, with sensitivity analysis at 5 percent and 15 percent. The rationale for this rate draws extensively on research by [an advocate of the use of WOSC]. The Treasury Board sometimes allows much lower discount rates (0 percent to 3 percent) for health and environmental cost-benefit analyses, although this is not official policy. Provincial government guidelines in Canada have tended to follow federal guidelines. Currently, the British Columbia Crown Corporations Secretariat recommends a real SDR of 8 percent (Boardman, Greenberg, Vining and Weimer, 2001, p. 250).

And the authors of this text conclude:

> We believe that the appropriate real discount rate ranges between 1 percent and 7 percent. Using 4 percent would not be unreasonable. For impacts that occur far in the future, especially if they have large positive environmental impacts, one could use lower discount rates (p. 250).

In the UK it has been reported that the UK Treasury has recently halved its recommended discount rates to be used for the evaluation of PFI projects from 6% to 3.5%.

> There are a number of key elements in the comparison of the PSC and the PFI. All estimated costs are time valued for the duration of the contract period. Net Present Cost was calculated, originally using a 6% discount rate. Now under the new 'Green Book' (HM Treasury, 2002) rules, 3.5% is used. The change was a reaction to the accusation of 'double counting' of risk – 3.5% being seen as the risk free rate (Broadbent and Laughlin, 2004).

5.8 RECOMMENDATION

It is recommended that:

- *The PAC ask agencies that have compiled PSCs to explain whether those PSCs have:*

  a. *incorporated 'risk-adjustments' to the project costs estimated in the PSC – without allowing for similar risks when making comparisons with a PPP option;*

b. utilised the public sector borrowing rate plus a premium, or a high discount rate, supposedly to reflect the risks of the specific project under consideration.

- *The PAC ask NSW Treasury to advise what discount rates it has used (or recommended that agencies use) in (a) cost benefit analyses of program initiatives or capital projects, and (b) PPPs, over the past 10 years.*

- *The PAC ask NSW Treasury to advise whether PSCs calculated by agencies contemplating PPPs have incorporated an allowance for the costs of monitoring compliance with those contracts – and to provide examples of how they were estimated for (say) tollroads or school projects.*

- *The PAC ask the RTA whether sums that it has described as 'reimbursement of development costs' were included in assessments of the 'benefits' associated with prospective PPPs (rather than as reimbursements of past expenditure).*

- *The PAC ask agencies that have compiled PSCs for use in comparison with a PPP proposal, to explain whether those PSCs have been updated before contracts were executed, to ensure that the PSC was then consistent with the PPP proposal (particularly in relation to the cost of potential design changes, the risk of other sources of cost overruns, and the risks associated with government guarantees or commitments to provide ensured revenue or rates of return to the counterparty).*

5.9 LESSONS FROM PAST EXPERIENCE IN USE OF PRIVATE SECTOR COST OF CAPITAL (SALE OF SBNSW)

Before leaving the subject of the choice of interest rates, we submit that the Public Accounts Committee should be aware of the damage done to State finances by past reliance on the 'private sector cost of capital' in investment evaluations.

Early in 1995 the State Bank of NSW was sold by the Fahey Government for a headline price of $576 million to Colonial Mutual, after the major trading banks were excluded from bidding, supposedly to promote increased competition in the banking sector. One of the conditions of the sale was that the NSW Government would assume most of the risks of bad debts on a $13 billion loan book. After the first $60 million in bad debts, prospective purchasers were to be reimbursed for 90% of any further losses.

Parliament did not agree to the sale proceeding, prior to receipt of a report from the Auditor-General on the merits or otherwise of the sale. The report (costing close to $1 million), when received, recommended that the sale proceed, and independents announced they would vote for the sale. However sections of the report were withheld as 'commercial in confidence'. The former Auditor-General later advised that this condition was attached to the report by consultants he had engaged. As he had a deadline to deliver the report to Parliament, he was unable to argue the point.

Several years later, after the Auditor-General was critical of the withholding of claims that documents were 'commercial in confidence', Centennial Consultancy wrote to the Auditor-General asking if he would now release the unpublished elements of his report on the proposed sale of the SBNSW. He did so in his last report to Parliament before his term of office ended.

The reports that had been withheld included details of the discount rate that had been used to evaluate the options of 'sell' or 'retain' the Bank. It was argued that the relevant discount rate was the private sector cost of capital for the banking industry. It was claimed that this was 'high risk' (a claim that ignored the fact that the NSW Government was itself underwriting most of those risks).

As detailed previously (Walker and Con Walker, 2000), the discount rate selected to calculate the net present value of maintainable earnings from the Bank was equivalent to a rate of return of ***18.9 per cent per annum after tax*.** But Government agencies do not pay corporate tax to the Commonwealth (only notional taxes to the consolidated fund). Accordingly, given that the 1995-96 corporate tax rate was 36 cents in the dollar, this was equivalent to using a ***discount rate of 29.5 per cent per annum before tax***.

Arguably, had there not been claims that elements of the report were ***commercial in confidence***, this discount rate would have been disclosed, and been the subject of widespread ridicule.

Had the full report been provided at the time, and had it contained a meaningful Public Sector Comparator, detailing expected cash flows to government from both the 'sell' or 'retain' options, the extent of potential bad debts on projected cash flows would have been obvious.

Possibly media scrutiny would have dissuaded members of Parliament from voting for the sale to proceed under those terms.

The outcome was a financial disaster for the State of NSW:

- NSW had to reimburse the purchaser for hundreds of millions of dollars worth of bad debts. By 2001 the net proceeds from the sale had fallen from the headline price of $576 million to around *$80 million*.

- The net sale proceeds were less than one year’s profits: in its first year of private ownership, the bank reported a pre-tax profit of $146.9 million.

- Before Colonial merged with the Commonwealth Bank in 2000, an Independent Expert's Report included a valuation of Colonial's banking business – which, (apart from very minor investments in Tasmania and Fiji), was for all intents and purposes the old State Bank of NSW. The valuation, only four years after the State Government's sale of the bank for a net $80 million, was in the range ***$2.5 billion - $2.75 billion.***

In other words, the ***State of NSW lost around $2.5 billion*** from the premature sale of SBNSW – it was sold at the wrong time, for the wrong reasons (to get rid of it before the story of bad debts and maladministration came to light) and on the wrong terms.

The exercise deserves to be regarded as one of Australia's worst financial scandals.

The major mistake was to evaluate the 'sell' or 'retain' options using a discount rate based on market-determined estimates of the private sector cost of capital.

Arguably, NSW Treasury's continued advocacy of use of that methodology has led to similar losses – loss of profits from tollways such as the M2, because they were constructed as a PPP.

5.10 PURPORTED SELECTIVE PUBLICATION OF THE PSC TO POTENTIAL BIDDERS?

If staff of a public sector agency were to disclose details of a private sector firm's tender to another private sector firm, that would be universally condemned. It would be regarded as corrupt conduct.

One of the more extraordinary elements of the Guidelines was the suggestion that the PSC for specific projects might be published for the benefit of prospective tenderers:

> The Government is flexible about disclosing the PSC in tender documents. This is more likely to happen where it is obvious that it would assist the private sector's bid preparation process and result in higher quality and better value bids to the Government (p. 46).

On the face of it, agencies would be able to publish a PSC ***so that tenderers would know what price and conditions they had to beat to win a contract***.

It is difficult to avoid the conclusion that such an approach could have adverse consequences on employment in the public sector, by giving private sector firms a comparative advantage in undercutting service delivery from government agencies.

5.11 PSCs AS MUMBO JUMBO

As noted above, the calculation of PSCs involves not simply estimates of projected costs of conventional government-funded delivery of projects, but adjustments to those costs to allow for 'risks'

In addition, the NSW Guidelines propose that, in order to establish 'competitive neutrality with the private sector', the PSC should add in hypothetical payments

> of Commonwealth and State tax equivalents and other regulation costs equivalent to those faced by the private sector.

Even though the State government agencies may not have made those payments (or would be paying some to the NSW consolidated fund.

The foregoing discussion described these kinds of adjustments as biasing the PSC against conventional delivery and in favour of PPPs.

However the PAC may be interested in the following extract from press reports of comments from England's National Audit Office:

> Government departments and local authorities are relying too much on "spurious" figures to prove whether private finance initiative projects are good value for money, the National Audit Office has warned.
>
> Instead, those who plan projects need to look more carefully at the benefits and risks involved, and not just at their cost, according to Jeremy Colman, deputy controller and auditor-general at the Whitehall spending watchdog.
>
> In demonstrating that PFI deals are value for money, the government relies heavily on "public sector comparators" - desk exercises that work out what a road, hospital or prison would have cost under conventional procurement.
>
> But the NAO's analysis shows that many suffer from "spurious precision", Mr Colman said. Others involve "pseudo-scientific mumbo-jumbo where the financial modelling takes over from thinking", he added. "It becomes so complicated that no one, not even the experts, really understands what is going on."
>
> Some, he said, were "utter rubbish", and were reworked so late in the deal that the comparator had ceased to represent a realistic alternative. That, he said, made them "utterly irrelevant".

The author of these comments has since been appointed to the post of Auditor-General of Wales.

5.12 RECOMMENDATION

It is recommended that:

- *The PAC seek explanations for the inclusion in the NSW Guidelines of a statement that details the likely (risk-adjusted) costs of public sector delivery of specific infrastructure projects that might be published for the benefit of prospective tenderers.*

- *The PAC inquire whether any such estimates (or hypothetical costs) have been published in tender documents or communicated to prospective tenderers by other means.*

- *If any PSCs have been published in this way, to enquire whether **all** potentially interested parties were given access to the same documentation, or if the information was published selectively.*

- *If any PSCs have been published, to now make them publicly available for scrutiny by external stakeholders.*

- *The PAC propose that revised Guidelines for the development of PSC be issued, incorporating the following:*

    a. *the PSC should show the estimated projected cash flows associated with conventional public sector delivery;*

    b. *the elements in a PSC should be confined to the cash flows likely to be incurred by the public sector agency from the date on which the PSC is prepared. Notional charges (such as hypothetical land tax or payroll tax) should not be incorporated in these projected cash flows, as they are not cash flows that will actually be incurred by government agencies. Rather, any reference to 'level playing field' adjustments, made in the interests of State compliance with National Competition Policy, should be confined to an accompanying textual analysis of the relative financial merits of the PSC and possible PPPs;*

    c. *the discount rate used in the PSC should be disclosed, together with a brief explanation of any variation between this rate and the rates recommended by Treasury for other capital projects or programs within the State sector within the past 12 months;*

d. *the extent of the exposure of State agencies to the risk of failure on the part of the private sector partner should be described, together with references to how the sponsoring agency proposes to avoid or manage such a risk;*

e. *any comparison of the PSC calculation with the effective cost to government of a PPP deal should include an allowance for the costs to Government of monitoring that PPP;*

f. *detailed PSCs showing major categories of expenditure and revenues – not just a brief summary of the PSC calculation - are to be published in contract summaries once PPP contracts are executed;*

g. *detailed PSCs should be accompanied by an explanation of the date on which they were originally compiled, and when they were was subsequently updated.*

5.13 CONTRACT SUMMARIES

In the mid 1990s there in the face of political and business opposition to the full disclosure of contracts involving the private sector financing of public infrastructure, the NSW Public Accounts Committee recommended that the essential elements of all projects with private financing 'be made transparent, preferably through contract summaries' (*NSW PAC*, 1994).

Similarly a task force to review infrastructure financing, established by Prime Minister Keating, observed:

> To build public acceptance of private provision of infrastructure, governments should provide contract summaries of major projects to Parliament. They should also give their Auditors General sufficient resources to properly and expeditiously review contentious contracts (*EPAC*, September 1995).

These proposed disclosures were only to be made *after* contracts had been finalised. Mere disclosure of contract summaries *after* deals have been completed is inadequate to ensure appropriate scrutiny and accountability in parliament.

In particular, contract summaries would only tell part of the story about the way in which the risks and rewards of such projects are shared. For a start, they may not reveal all of the government's past and projected expenditure in providing ancillary services to a major project. These can involve new roadworks to feed traffic onto tollways, bridges to enable local traffic to by-pass the tollway route, and the costs of moving wires, pipes and drains in the path of the tollway corridor.

Even then, the spirit of those proposals has not been fully observed. Since 1995, NSW has adopted the practice of preparing contract summaries and associated cost-benefit analyses. After tabling in Parliament that are published in the NSW Treasury website.

Six contract summaries were prepared and examined by the Auditor General between September 1995 and January 1999 (these were reviewed in Walker and Con Walker, 2000). At the time, these contract summaries resided in the offices of the agencies that commissioned them: they had not been tabled in Parliament or even lodged in the Parliamentary library.

As was noted previously (Walker and Con Walker, 2000), those summaries failed to provide basic information about the prospective returns to be earned by private sector partners if base case financial forecasts were met.

The audit reports were *not statements that the deals were likely to be value for money*. Rather, they simply listed the documents examined, stated that the Auditor General had obtained a copy of the *NSW Guidelines for Public Participation in the Provision of Public Infrastructure* (1993), a statement that the information contained in the contract summary had been compared with the recommended disclosure requirements of the Guidelines, and a report that

> Nothing has come to my attention that causes me to believe that the [contract summaries relating to the project]
> (a) does not fairly represent the substance of the contractual arrangements pertaining to the [project….]
> (b) does not comply with the disclosure requirements of the Guidelines.

This audit report was accompanied by a disclaimed from the Auditor-General:

> I disclaim any assumption of responsibility for the adequacy or otherwise of the procedures requested by you [the agency]

Since 2001 it has been Government policy for contract summaries to be published on a Treasury website. However little seems to have changed in terms of disclosure of the details of PPPs.

The following summarises some key features of PPP arrangements that have been executed after the introduction of the NSW 2001 Guidelines. It is limited to those PPPs for which contract summaries are currently available on the 'Working with Government' website. It is noted that the website reports that a contract for an additional PPP (that for the Chatswood Transport Interchange) was signed on 24 June 2005; however a contract summary for this project was not found on the relevant website.

Some features of recent PPPs as disclosed in contract summaries available on Treasury website Oct 2005

Project	**Sponsoring agency**	**Source/ extent of PPP funding**	**PSC shows projected cash flows and NPV of govt funded project?**	**Project undertaken through a special purpose entity?**	**Includes details of profit sharing with Government?**	**Fee paid to government agency?**	**Term of contract**	**Comment**
New Schools Project (May 2003) – construction and operation of 9 school facilities	Dept Education & Training	Not stated	Only shows PSC 'most likely case' as 7.3% more expensive than PPP (but not strictly comparable as PPP was net of 'child care revenues')	Yes (contractor entity); other parties include mtce & cleaning contractor	N/a Net income from third party users to be shared 50% - 50% with the State.	No	To 2033 unless terminated for default	Monthly payments to the contractor comprising a performance based monthly net fee, plus upwards or downwards adjustments. Fees totalling $9.49m pa (at March 2003 prices). Details of how contractor will operate the facilities in document annexed to the Concession Deed (but not publicly available)
Cross City Tunnel (June 2003)	RTA	Debt finance $605 m; equity not stated	No - but discloses PSC for shorter tunnel - projected NPV of risk adjusted RTA's costs $41.93 m	Yes	*'Base case financial model'* not disclosed. RTA to share toll revenues & admin charges if they exceed forecasts by 110% (share 10% - 50% of excess)	Yes - $96.9m plus GST	To 2035 unless terminated for default	The contract summary 'does not disclose the private sector parties' cost structures, profit margins, intellectual property or any other matters which might place them at a disadvantage with their competitors' (p.1)

Project	Sponsoring agencies	Source/ extent of PPP funding	PSC shows projected cash flows and NPV of govt funded project?	Project involves a special purpose entity?	Includes details of profit sharing with Government?	Fee paid to government agency?	Term of contract	Comment
Eastern Creek Alternative Waste Technology Facility (September 2003)	Waste Services NSW	Not stated	No	Yes – Global Renewables (Eastern Creek) Pty Ltd	Operator entitled to share in a specified amount of Waste Service NSW's margin above an agreed hurdle	n/a	25 years after construction completed; may be extended by agreement	Waste Service NSW obliged to pay a performance-based fee for processing waste (initial capacity 175,000 tonnes per annum). Operator must divert a minimum %age of waste from landfilling Different rates payable for different classes of waste.
Westlink M7 Motorway (August 2003)	RTA	Not stated	No	Yes - WestLink Motorway Ltd and WestLink Motorway Partnership	**'Base case *financial model*' not disclosed.** After 6 years, RTA to have %age of toll revenues if > 105% , 110%, 120% or 130% of forecasts in this model (share 10% - 25% of excess)	Yes – $193.3m plus GST(for 'costs incurred and to be incurred')	To 2037 unless terminated for default	Agreement renegotiable if a *competing road project* is completed, or the roadway ceases to be signposted as a National Highway connection. NB *a competing road project* includes widening or upgrading of an existing road (though exemptions). Provision made for dedicated busways and 'other public transport infrastructure'

Project	Sponsoring agencies	Source/ extent of PPP funding	PSC shows projected cash flows and NPV of govt funded project?	Project involves a special purpose entity?	Includes details of profit sharing with Government?	Fee paid to government agency?	Term of contract	Comment
Lane Cove Tunnel, widening of Gore Hill freeway, etc (July 2004)	RTA (and Rail Corporation)	$1,142 m debt $542.8 m equity	No	Yes	**'B*ase case financial model'* not disclosed.** RTA to share escalating %age of toll revenues if > 110% of forecasts (share from 10% - 50% of excess)	Yes – $79.3 m plus GST	To 2037 unless terminated for default.	Instead of a PSC, shows PV of (public sector) costs, compared with PV of benefits [incl. non-financial 'benefits'] to motorists, pedestrians, etc, and benefit/cost ratios. Not clear if costs are gross, or net of development fee.

Of the Contract Summaries obtained from Treasury's Working with Government website, some (those for WestLink and the Lane Cove Tunnel) include a statement that the Contract Summary had been assessed for compliance with the NSW Government's November 2001 guidelines prior to its tabling in Parliament. If that is the case, one would expect that the Auditor-General's reports on whether or not the summaries fairly represented the detailed contracts and did indeed comply with the Guidelines, would have been attached to those same Contract Summaries. The Auditor General's report was not published on the Treasury website.

The Government's *Guidelines* describe the purpose of the Public Sector Comparator as being to assist decisions to be made as to whether 'a private finance arrangement offers superior value for money over traditional methods of government delivery' (p. 45).

Despite statements in the Government's *Guidelines* that Contract Summaries would include 'the results of cost-benefit analyses' (p. 27) and a statement of the results of the Public Sector Comparator (p. 46), the contract summaries have not provided that information.

The only exception is the Contract Summary on the New Schools Project for the Department of Education and Training (DET). This Summary included a Table showing a 'value for money' comparison between public sector and private sector project delivery. The estimated net present value of the financial cost of the project to DET is shown as

PSC best case	$134.3m
PSC most likely case	$141.8m
PSC worst case	$152.6m

As against

Private sector delivery	$131.4m

The differences are obviously fairly marginal over 30 years.

However – far from providing assurance to readers that the PPP provided 'value for money' - the presentation of these figures only casts doubt about the validity of the decision to go ahead with a PPP in this case:

- there is no explanation of how the PSC figures were compiled, since they were described as 'risk adjusted estimates'. Hence the categorisation of 'best case', 'most likely case' and 'worst case' appears to relate to figures which not only represented estimates of capital and maintenance/cleaning costs, but also incorporated adjustments to those estimates to allow for 'risks';

- it is not clear to what extent the PSC costs to DET include allowance for hypothetical costs (such as payroll or land tax) that would be real cash outlays for the PPP option. (It may be that some token recognition must be given to 'competition adjustments' to comply with National Competition Policy, but that policy does not compel governments to pay excessive sums to private firms just for the sake of appearing to take National Competition Policy seriously.)

  Given that the differences between the NPVs of the PSC and PPP options were so marginal, it could be that the differences were largely attributable to a combination of hypothetical 'competition adjustments' and additional 'risk adjustments' to the estimates compiled for the construction and management of those facilities by government.

- while the private sector delivery option is described as

  > Adjusted to ensure discount rate calculated on a consistent basis with the PSC … and to include an estimate of potential child care revenues.

  a critical element of these assessments – the discount rate - is not disclosed;

- the private sector delivery option appears to reflect the cost of that option to DET – without allowing for the cost to DET (and other agencies[8]) of monitoring and managing the PPP arrangement. The PSC costs, on the other hand, would incorporate DET's costs of managing staff and monitoring the condition of the facilities;

- the private sector delivery option is also stated as having included 'an estimate of potential child care revenues'. In other words, the PSC and the PPP options are not comparable, since the NPV of the latter had been reduced by the incorporation of the expected financial impact of a 'good idea' – the construction of revenue-producing child care facilities on school sites.

The latter two points are particularly significant.

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[8] A common failure of financial analyses of this type is to focus on the impact on an organizational unit or department rather that the 'organisation' as a whole. In this particular case, monitoring costs would be incurred not only by DET directly but by the Auditor-General (for reviewing the Contract Summary – though possibly a fee was charged for this service), by the Private Project Branch in the NSW Treasury, and by the Infrastructure Coordination Unit in the NSW Premier's Department (see *Guidelines*, 2001, p. 26).

The PSC – PPP comparison involved comparing apples with oranges.

The Contract Summary for the DET project is the most informative of the five examined. The remainder are notable for their complete failure to provide any form of comparison between the costs and revenues of the project as if they were controlled and operated by the public sector, as opposed to the PPP alternative.

Possibly the Eastern Creek Alternative Waste Technology Facility might be regarded as a virtuous project, since it sought to capture benefits from municipal and green waste, promised to reduce government expenditure, and did not involve the establishment of a monopoly service provider. The contract summary contains assurances from a consultant that the project is likely to be commercially viable (given the fees to be paid by a government-owned corporation for its services), but a PSC is not provided.

Contract Summaries for the three tollway projects do not provide a comparison of the costs and benefits of delivering those projects through public sector tender processes (for capital works) and public sector operating activities, versus the PPP option. Even though the Guidelines require the preparation of a PSC 'as if' the public sector is to finance such a project using a 'commercial capital structure', and if it is to receive revenues (tolls) from the project over its life, the results of such analyses are not provided.

Some features of the information provided follow:

- only one (Lane Cove Tunnel) provides any indication of the scale of the capital investment in the project (debt of $1,142 m, equity investment of $542.8 m);

- two acknowledge that the PPP contracts incorporated a 'base case financial model' detailing revenue forecasts – yet this information was withheld from Parliament (even though such information has and would be regarded as a basic disclosure if the operators sought to raise funds from the public via a prospectus);

- the contracts for the later PPPs reflect a concern with the need to share 'super profits'. The NSW 2001 Guidelines state:

  > it may be appropriate for government (and the community) to share in any windfall gain or super profits received by the private party (p. 40).

  Presumably this reflects concerns about prior experiences. It might be noted that the reference to *super profits* would be to profits in excess of the returns contemplated by foundation investors (anecdotally reported to be 18% - 20%

per annum for tollways with all the features of a local monopoly). Or it could be to returns in excess of those earned by the investors in the M2 motorway project, reported by the then NSW Auditor-General to be in excess of 24.4 per cent per annum if traffic forecasts were valid (Auditor-General of NSW, October 1994).

Hence the Westlink M7 Motorway project and the Lane Cove Tunnel project both provided for the RTA to share in toll revenues if it was greater than as forecast in the 'base case financial model';

- the profit share from these 'super profits' might be regarded as derisory (e.g. only 10% of the revenues in excess of forecasts) – but a more fundamental question is: if public sector agencies believe there is a prospect for the project to produce 'super profits', over and above the very generous returns implicit in the base case financial model, why don't those agencies invest in the whole project, and receive *100% of total profits*?

- the Cross City Tunnel project provides for toll escalations of the *higher of 4% or CPI.* While it is common for commercial transactions to include escalation provisions (linked to CPI or AWOTE) to reflect changes in costs, the commercial justification of increases of the higher of 4% or CPI is inexplicable;

- the Westlink project included requirements for the re-negotiation of pricing and associated financial arrangements if a 'competing road project' was completed. The definition of a 'competing road project' was extraordinarily wide – encompassing 'widening or upgrading of an existing road';

- a common refrain in these Contract Summaries is the statement that they do 'not disclose the private sector parties' cost structures, profit margins, intellectual property or any other matters which might place them at a disadvantage with their competitors'. It is difficult to see how basic financial information about pricing and profit forecasts could possibly disadvantage operators ***after*** they had won a contract – particularly when such information is routinely made available to financial markets;

- instead of a systematic analysis of the cash flows that could be enjoyed by a public sector funded tollway versus a PPP, the contract summaries incorporate statements of 'benefit cost ratios'. In these calculations, the 'cost' is the funding expended by the RTA (though it is not clear if this is gross or net of operators' contributions, or net of the $109 million reportedly committed by the Commonwealth towards scoping and environmental assessments of what became the Westlink project).

  As for 'benefits', it appears that money values had been assigned to such factors as 'saved passenger time' (such much per hour), 'reduced risk of motor accidents' (so many dollars per accident), 'reduced wear on motor vehicles' (so much per kilometre) and so forth. The basis of assigning money values in these calculations is not explained – let alone the dollar values assigned to each component.

In effect, the publication of 'benefit cost ratios' might sound scientific, but it is meaningless without an explanation of how the figures were derived. Without such disclosures, it can hardly be claimed that publication of 'benefit cost ratios' convey any meaningful information, even to those familiar with such exercises.

If the purpose of calculating and publishing 'benefit cost ratios' is to provide assurances that the projects provide 'value for money' to the community, then the elements of those ratios should be on a consistent base – relating '*benefits to the community'* to *'costs to the community'* (not 'costs to the RTA'). For example, if the 'benefits' include savings in motorists' travel time, correspondingly the 'costs' should include the tolls and administration charges that have to be paid by those motorists.

5.14 RECOMMENDATION

It is recommended that the PAC propose that:

- *Contract Summaries should include*

  a. *particulars of the expected scale of initial investment to be made by private sector partners, and of the value of expected maintenance programs and other operating costs required by the PPP contracts;*

  b. *where a PPP involves the private sector partners deriving revenues from user charges (such as tolls) an outline of the 'base case financial model', and the key forecasts of revenues contained in that model.*

- *That the summary of any cost-benefit analyses presented within a Contract Summary, if those analyses include monetary values attributed to impacts on the community, should:*

  a. show costs and benefits (and associated indictors, such as benefit-cost ratios) on a consistent basis;

  b. detail the items of costs and benefits that were included in the analysis;

c. explain the basis upon which monetary values were assigned to each item;

d. disclose the discount rate used in the analysis.

6. THE FRAMEWORK FOR RISK ALLOCATION BETWEEN THE PUBLIC AND PRIVATE SECTORS AND ITS APPLICATION, ESPECIALLY HOW WELL RISK IS ASSESSED, ALLOCATED AND MANAGED

The NSW Guidelines (2001):

- in calculating the Public Sector Comparator (PSC) provide for risks in their public sector option but fail to make similar adjustments for failure of the private sector partner;
- fail to explore the risks that private sector partners may earn excessive profits (which are opportunity costs to the Government and the community);
- disregard the risks to the NSW community of having to pay compensation in the event that there is a need to upgrade public sector infrastructure (even local roads);
- contain no flexibility for adjusting to changed circumstances during the term of the contracts so the Government of the day may lose control of the standard of service to the community.

If agencies were systematically and rigorously compiling a Public Sector Comparator, and comparing that with PPP proposals, then one would expect that efforts would be made to identify the risks associated with ***both options***, that is

- 'public sector delivery'; and
- delivery via a PPP.

Yet the NSW Guidelines (together with discussions in the earlier *Green Paper*) reflect a systematic bias against conventional public sector delivery:

- by double-counting risks from the perspective of the public-sector controlled projects, through use of the private sector cost of capital; and

- by not assigning equivalent values to all of the risks associated with PPPs.

The latter includes *counter-party risk.* Often the consortia that enter into PPPs utilise special purpose vehicles (e.g. $2 companies, or trusts). The consortia may include major enterprises with a strong financial position, but they do not necessarily underwrite the liabilities incurred by the special purpose vehicles used to implement the PPP.

Some proposals in relation to modification of the Guidelines relating to risk assessment are embodied in Recommendations presented earlier in this submission.

7. THE EXTENT OF OPPORTUNITIES TO SHARE KNOWLEDGE ACROSS AND BETWEEN AGENCIES

7.1 SILOS WITHIN GOVERNMENT

Recent research into information sharing within local government in NSW has specifically addressed the extent to which information about the cost of upgrading infrastructure was shared within and between staff and elected officials (Walker, Dean and Edwards, 2004). The study was based on telephone interviews with four respondents from each of a large sample of NSW local councils. In other words, it sought evidence of the perceptions about the extent of information sharing from persons likely to be 'users' of particular reports (the mayor and another, randomly selected, member of the council) and from two senior staff members of the same council (one engineering, one finance).

One of the principal findings of this study was somewhat alarming. The evidence indicated that engineering staff (who, in the main, were responsible for compiling estimates of what expenditure was needed for infrastructure repairs and maintenance) did not engage in much dialogue about these matters with finance staff (who were principally responsible for the formulation of council budgets which determine the pattern of future resource allocations).

In other words, engineering staff and finance staff were found to be operating in 'silos' within the one organisation.

(It is noted that the Department of Local Government has been actively encouraging local councils to share and act on the information obtained by different groups of staff within individual councils, by promoting the development and regular review of integrated management plans.)

The finding that staff operate in 'silos', while disappointing, only confirms what many commentators have suspected when referring to the operations of the public service at state level: that there is a tendency for members of individual agencies to work in their own area, and not work collaboratively with staff of other agencies.

It is also noted that, at a State-sector level in NSW a number of efforts have been made to overcome these tendencies, ranging from the initiatives undertaken by the NSW Premier's Department to establish regular channels of communication between agencies, the establishment of working parties of representatives of different agencies to ensure a 'whole of government' approach to the resolution of specific problems – and, of course, the activities of individual public sector managers to facilitate and support the work of public servants within their organisation, or elsewhere.

However there are major impediments to information sharing 'across and between agencies', in relation to the design, establishment and monitoring of PPPs.

Sharing knowledge across and between agencies would be greatly impeded by agreements to keep crucial parts of PPP contracts as 'commercial in confidence' – and for Contract Summaries to omit relevant information.

The proposal in the NSW Guidelines for the preparation of a post-implementation review of PPPs is applauded.

> A post-implementation review will be undertaken on all private sector infrastructure projects. They should be seen as a valuable tool in refining the processes used in developing private sector infrastructure projects. They will be undertaken by the agency initiating the project and should include:
>
> - project formulation
> - project objectives
> - brief appropriateness *(sic)*
> - design performance
> - approvals process
> - project delivery
> - risk exposure/risk sharing
> - delivery time
> - quality
> - budget performance
> - project management/procedures
> - functional competence of infrastructure, including networking and interfacing
> - project operations, including service delivery and financing
> - industrial relations management
> - environmental management
> - community relations
> - industry development

> The review should be initiated 12 months after implementation although it may be required earlier. So that lessons learned can benefit future projects, a review outcome report should be prepared and copies submitted to the Private Projects Branch in the NSW Treasury and the ICU [Infrastructure Coordination Unit] in Premier's Department.
>
> Service delivery performance will be reviewed periodically throughout the contract.

Plainly the intention of the post-implementation reviews is to enable the public service to learn from experience. Plainly it is also appropriate that a Committee of Parliament should also have the benefit of learning from these experiences. Likewise – given the Government's own concern about risks and 'super profits', and the very scale of current and potential PPPs (as outlined in the *State Infrastructure Strategic Plan 2002)* other stakeholders are entitled to have the opportunity to review these reports of post-implementation reviews.

7.2 RECOMMENDATION

It is recommended that the PAC:

- *Seek copies of all of the 12-monthly post-implementation reviews prepared by agencies since the 2001 Guidelines were issued.*
- *Propose that copies of those post-implementation reviews (or summaries of them) be made available on the same Treasury website that reports Contract Summaries.*

8. THE EXTENT TO WHICH AGENCIES ARE MANAGING INTELLECTUAL PROPERTY ISSUES

8.1 INADEQUATE DEFINITIONS

According to the NSW Government Guidelines, Wo*rking with Government:*

> Intellectual property is an important issue for all PFPs [Privately Financed Projects] including unsolicited proposals. Increasingly, material submitted to the Government is said to represent intellectual property (*Working with Government: Guidelines for Privately Financed Projects*, November 2001, pp 43-4).

The Guidelines define intellectual property as:

> Inventions, original designs and practical applications of good ideas protected by statute law through copyright, patents, registered designs, circuit layout rights and trademarks; also trade secrets, proprietary know-how and other confidential information protected against unlawful disclosure by common law and through additional contractual obligations, such as confidentiality agreements ((*Working with Government: Guidelines for Privately Financed Projects*, November 2001, pp 53).

If 'inventions, original designs and practical applications of good ideas' are already 'protected by statute law through copyright, patents, registered designs, circuit layout rights and trademarks', then it would appear that public sector managers have very little role in 'managing' the intellectual property issues that arise from the use of those inventions, designs and so forth by the parties that are thereby protected.

The remainder of the items in the Guidelines' definition are

> trade secrets, proprietary know-how and other confidential information protected against unlawful disclosure by common law and through additional contractual obligations, such as confidentiality agreements

This element of the definition is questionable.

Dr Robert Dean, author of *The Law of Trade Secrets and Personal Secrets,* states that

> The law does not regard secret information as property *(p. 4)*
>
> If it is always kept in mind that the rights are, or ought to be, merely rights that arise from a cause of action based on a duty of good faith or contract or some other cause of action – not property rights – and that often "property" is used in its possessive rather than its substantive sense, confusion can be kept to a minimum *(*Dean, 2002, p. 5).

It would appear that while parties interested in promoting a PPP proposal may *claim* that certain items constitute intellectual property, the prospect of any such claims being raised could be readily averted simply by establishing (in advance) the ground rules on which PPP proposals will be entertained and handled.

For example, if it is stated at the outset that the content of favoured PPP proposals will be subject to full disclosure to Parliament and others, and if parties continued to put forward those proposals, then it could not be claimed later that disclosing any details of those arrangements breached any duty of confidentiality.

As Dean so succinctly states:

> Once information is used in the market place the owner must risk disclosure and competition (p. 7).

Accordingly, the Public Accounts Committee is invited to consider exactly what 'intellectual property issues' that might arise from Public Private Partnerships are likely to be of such significance as to warrant efforts to keep the terms and conditions of contractual arrangements secret from:

a. Parliament; and

b. the community.

The authors of this submission have examined several commercial contracts that were claimed to warrant the protection of being treated as 'commercial in confidence'.

(Arguably, the most notable were contracts for the M2 Motorway. At the time, the former Coalition Government refused to release contracts for the M2 Freeway to Parliament (and to the Auditor-General). Irritated by this affront to Parliament, Bob Walker attended the offices of Hills Motorway (on the premises of Macquarie Bank) and successfully exercised his rights as a prospective investor (in terms of the then corporations legislation, given that Hills Motorway then had a prospectus on issue), to seek access to 'material contracts'.)

As outlined above, PPP contracts entered into by a later Government have employed a 'base case financial model' – and have again linked profit sharing arrangements to returns forecast in those models.

Similar models have subsequently been described in commentaries on other PPPs and have been described in broad terms in prospectus documents.

The NSW Auditor General in a radio interview (ABC 702, 13 October 2005) volunteered that the structure of many PPP contracts was 'basically the same'.

8.2 WHAT IS THE 'INTELLECTUAL PROPERTY' AT STAKE

What, then, is the 'intellectual property' at stake?

A number of options come to mind

a. The drafting of the contracts and trust deeds?

No doubt some legal firms may wish to charge full fees for preparing such instruments for each new client – rather than simply change the names, numbers and other details on a boilerplate document. However it is believed that the profit sharing arrangements outlined in contracts, trust deeds and associated documents are not unusual or original from a commercial perspective.

b. The manner in which the level of tolls (or other revenues) was to be calculated?

Certainly some contracts have unusual features. But the capacity to negotiate such generous clauses in the contracts can hardly be regarded as 'intellectual property'. Rather, the wish to keep such matters confidential is likely to avoid political furore about provisions that are overly generous to private sector partners (and overly expensive to consumers) – that is, until they are found out.

c. 'Know how' and other confidential information that has been protected by confidentiality agreements?

It is hard to see how 'know how' could be disclosed in PPP negotiations (unless that term was being interpreted in a broad sense to relate to ideas or concepts). The specialised usage of the term relates to trade secrets law:

> …in the majority of cases the courts have used the term "know-how" to define a specific class of information. …in order to protect trade secrets against issue by employees, the courts have evolved principles based on two conflicting policies, namely that employers have a right to keep their trade secrets to themselves, and that there is a public interest in promoting employee mobility, allowing employees to apply the skills and experience gained in one position in another (Dean, p. 18)

In other words, 'know how' could be seen as relating to 'the way in which a skilled man does his job'. One would expect that PPP negotiations involve proposals about design, construction, outputs and pricing – not the detailed way those processes will be carried out. In other words, government agencies need not be concerned about revelations of 'know how', since PPP proposals and contract documents are concerned with outputs not the processes used to achieve those outputs.

As for references to 'confidential information', it is at this point that the Wo*rking with Government* Guidelines fail to provide effective guidance, and actually create 'intellectual property issues' by implying that government agencies will, if requested, keep information 'confidential' *ad infinitum* (regardless of the merits of that request).

To quote Dr Dean again:

> "Confidential information" when used in its specialised sense is simply information which is the object of an obligation of confidence. It is the information with respect to which a breach of confidence action may lie (p. 17)

The NSW Guidelines, rather than asserting

> PPP agreements should not incorporate confidentiality agreements dealing with x or y or z

say (in effect)

> private sector firms are invited to nominate what items of information they wish to regard as commercial in confidence

8.3 RECOMMENDATION

It is recommended that:

- *The PAC propose that the NSW Government Guidelines be redrafted to give notice to those presenting PPP proposals (whether solicited or unsolicited) that, if successful, the details of the PPP contracts will be publicly available and will not have regard to prior claims of 'commercial confidentiality'.*

Further, given that the Guidelines propose that government agencies may purchase 'intellectual property' from unsuccessful bidders, one useful way of identifying the significance or otherwise of these issues gives rise to another recommendation.

It is recommended that:

- *The PAC enquire whether agencies have ever purchased intellectual property from unsuccessful bidders (per NSW Guidelines) – and if so, to explain what that 'intellectual property', and whether those agencies are currently benefiting from the application of that IP – and how?*

9. CONSEQUENCES OF PPPs

9.1 CRITICISMS OF PPPs

The many criticisms of PPPs have been well-documented elsewhere and include claims that they:

- are ideologically-driven;
- have been poorly analysed;
- give rise to a lack of accountability on the part of government for the quality of essential services;
- involve unnecessary secretiveness;
- are often bad financial deals for taxpayers;
- can lead to a loss of services to the community;
- lead to a loss of public sector skills; and
- distort spending and urban planning priorities, since priority may be given to projects that are readily packaged as PPPs, rather than to those which will produce the greatest benefit to the community.

9.2 IMPACT ON EMPLOYMENT AND LOSS OF PUBLIC SECTOR SKILLS

A significant consequence of privatisation and associated policies which has received little attention is the impact on employment and loss of public sector skills.

In particular, there is evidence that the adoption by the NSW Government of micro-economic reform and associated policies since the late 1980s, has led to a significant and sustained decline in the NSW Government annual apprentice intake.

An analysis undertaken by Phillip Toner ('Trends in NSW Government Apprentice Intake: Causes and Implications', *Australian Bulletin of Labour*, Vol. 24, No. 2, June 1998) states that although the decline has occurred in the context of a more general reduction in apprentice intake (especially in traditional trade fields such as building, electrical and metal) in the rest of the NSW economy, the relative decline in State Government intake greatly exceeds the reduction in apprentices intake amongst other (mostly private sector) employers (p. 141).

The trends in the apprentice intake are presented in the following table from the Toner article.

Table 9.1
NSW State Government, Other NSW and Total NSW Annual Apprentice Intake

Year	State	Other	Total
1986	1247	14772	16019
1987	990	14267	15257
1988	874	15421	16295
1989	1058	19079	21147
1990	832	16865	17697
1991	749	13065	13814
1992	475	12442	12917
1993	465	12749	13214
1994	396	14315	14711
1995	311	13647	13958
1996	292	13925	14217

Source: NSW Department of Training and Education Co-ordination (DTEC) (As cited by Toner).

The Table shows that from 1986 (the first year for which data were available from the NSW State Training Authority) to 1996:

- State Government apprentice intake declined from a peak of 1247 in 1986 to 292 in 1996, a decline of 77 per cent;

- from 1989 to 1996, State Government apprentice intake was in continuous decline;

- other NSW intake, composed almost entirely of private sector intake but also including Commonwealth and local government intake, also declined although only by 6 per cent over the same period.

Toner asserts that 'the primary cause of this decline had been the adoption by the NSW Government since 1989 of micro-economic reform and associated changes to the objectives and operation of State Government utilities and trading enterprises (p. 141).

He concludes that the 'very significant decline in State Government apprentice training effort, combined with increasing reliance of SOCs on outsourcing trade skill requirements [through use of contractors], has a number of important implications for the labour market in NSW and possibly Australia' (p. 153), summarised as follows:

- the reduction in State government training effort may have an adverse effect on the supply of skilled trades labour. Although the State government intake only represented, at its peak, 8 per cent of total State intake (in the available data), it was very important in key areas such as the building, electrical, and metal trades;

- the trades have historically been a central element in the teenage labour market. The decline in Government apprentice intake is an important element in the continuing loss of full-time employment opportunities for teenagers;

- there are arguments which suggest that the maintenance of an apprenticeship system depends to a large degree on supportive structures and policies, and that the removal of these structures explains in part the long-term decline of apprenticeship systems in Britain and the United States.

Comparable numbers for more recent years breaking up apprentice intakes between the public and private sectors have not been obtained.

According to the NSW Board of Vocational Education and Training (BVET):

> The total number of apprentices in training in the late 1990s was the same in absolute terms as the total number in training in the late 1970s. Over the 21 years from 1978 to 1998, the number of apprentices in training has never experienced a period of such sustained low levels as in the 1990s. This trend is the outcome of the sustained low annual apprentice intake in most trades over the last decade (*Trends in Apprenticeships and Traineeship Training in New South Wales*, December 2001, p. 44).

The BVET believes that structural changes in the economy can account for almost all of the decline in both apprentice intake and training rates over the last decade. Included in the key structural changes are corporatisation and privatisation of public sector activities, growth of labour hire and outsourcing of trades work, reduction in firm size, and growth of casual and part-time employment.

In relation to corporatisation and privatisation of public sector activities, the BVET states:

> Public sector activities across all levels of government, such as electricity generation and distribution, water and sewerage, railways, roads airlines and certain defence-related functions, have been progressively privatised or corporatised over the last decade or more. Prior to these changes in ownership or legal structure, these activities employed between 10-20 percent of traditional metal, building and electrical apprentices. They now account for less than 5 percent of annual apprentice intake in these fields. The reduction in public sector intake accounts for around one-third of the decline in apprentice intake over the 1990s (*Trends in Apprenticeships and Traineeship Training in New South Wales*, December 2001, p. 45).

The BVET concludes that:

> … the reduction in the apprentice intake is contributing to current and prospective skill shortages in many of the traditional trades *Trends in Apprenticeships and Traineeship Training in New South Wales*, December 2001, p. 44).

There is difficulty in obtaining comparable apprenticeship intake figures for more recent years due to changes in statistical collection methods. The figures below are from the Federal Government's National Centre for Vocational Education and Research and refer to commencements for *'Traditional apprenticeship proxy'.*

It is not clear whether these figures are comparable to those for previous years. There is also uncertainty about the reliability of the estimated figure for 2005. The figures are shown in the Table below.

Table 9.2
Total NSW Annual Apprentice Commencements

Year	Total '000s
2000	13.9
2001	12.4
2002	12.2
2003	14.3
2004	16.3
2005	18.2 (e)

(e) Estimate
Note: Numbers are the 12 months to 31 March and they refer to 'Traditional apprenticeship' proxy.
Source: National Centre for Vocational Education and Research

The apparent increase in the NSW intake in the last three years is due to a number of factors no doubt including a range of innovative policies introduced by the NSW Government making the employment of apprentices more attractive.

However, as the data show, the actual figure for 2004 at 16,300 and also the estimated 2005 figure of 18,200 are still significantly below the peak of 21,147 in 1989.

9.3 PPP GUIDELINES DEFICIENT ON EMPLOYMENT IMPACTS

In light of the trends in the loss of skills and skills training in the public sector, it is surprising to see the little attention devoted to this important matter in the various Government infrastructure documentation mentioned above.

For example, the NSW Guidelines contain just one paragraph related to employment as follows:

> As a general principle the Government does not support forced redundancies. Where public sector employees are affected by a PFP and are offered employment with the new employer, the PFP contract should provide for those employees to receive employment benefits no less than those that would have applied should government employees have performed the work. The NSW Industrial Relations Commission 'no net detriment' test is to apply (p. 41).

They also contain one paragraph on industrial relations as follows.

> The private party will take and manage the industrial relations risk relating to their workforce, in a manner consistent with that party's obligations under employment legislation (p. 37).

The failure to specifically nominate the 'employment legislation' means that it is possible that Federal legislation may be imposed at some future time.

Appendix 2 to the guidelines which refers to 'Public Interest Evaluation' lists employment as one of the Government policy areas with which the proposed project's outputs, service delivery and standard of performance need to be consistent.

It is only when one gets to Appendix 4 to the Guidelines that there is some recognition of the impact of PPPs on employment. This Appendix describes the contents of the *Statement of Economic Development Impacts* which needs to be completed. It includes as part of the project's direct 'short term impacts'

> Additional Employment
> Transfer Employment (from public to private sector) (p. 79)

And as part of its Indirect Impacts:

> Additional Employment in ANZ (p. 79)

9.4 LOCAL CONTENT AND PPPs

The Guidelines to refer to local industry participation as follows:

> The NSW Government recognises the substantial economic benefits flowing from buying Australian/New Zealand (A/NZ) sourced goods and services. It is also aware of the economic benefits of maximising opportunities for local service providers to compete for government business on the basis of value for money.
>
> Bidders will be required to prepare and submit preliminary local industry participation plans identifying how and to what extent they will incorporate A/NZ sourced goods and services (p. 22).

This is a pretty innocuous statement providing little protection for local industry.

9.5 AN EXAMPLE: THE APPLICATION OF THE GUIDELINES IN THE RAIL SECTOR

a. Local content

The adoption of PPPs in the NSW rail sector regarding the designing, building and maintenance of the 498 air-conditioned rail carriages provides an insight as to the impact of some of the Guideline provisions in practice.

The tender documents for the designing, building and maintenance of the abovementioned rail carriages impose only a 20 per cent local content requirement.

Such a low local content requirement is likely to lead to:

- the export of skilled jobs; and
- less investment in training and R & D, compounding the current skill shortages.

This is likely to threaten the viability of the rolling stock industry in NSW, with potential damage to the economy, particularly in regional areas which rely heavily upon the rolling stock industry for employment and training.

Moreover, the lack of a clear definition of the 20 per cent local content requirement means even this requirement is likely to be of little benefit to the local manufacturing sector.

The Local Content Requirement is referred to in clause 29.3 of the rail Project Contract as follows:

a. To achieve the Local Content Requirement, at least 20% of the Assessable Content must be Local Content.

b. Assessable Content is the total cost of the items listed in the Manufacturing Cost Schedule.

c. Local Content is that portion of the cost of each item listed in the Manufacturing Cost Schedule which is accounted for by manufacturing activity carried out by the Rolling Stock Manufacturer in Australia or New Zealand or by the purchase of components manufactured in Australia or New Zealand

Since ‘assessable content’ will be the total cost of manufacturing of the trains, it appears that the ‘20%’ can comprise ***any*** work done in Australia or New Zealand. It need not be skilled work, implying that components could be largely imported, with minor finishing work being undertaken in Australia, such as painting, etc. while still fulfilling contract local content requirements.

As a result, it is believed that this arrangement is likely to do little, if anything, to support the current skills basis, let alone support new apprentices or future skilled tradespeople.

The absence of a clear definition of ‘local content’ or 'local manufacture’ effectively means:

- components purchased locally, but largely or wholly imported can be classified as ‘local content’;

- ‘local content’ can be achieved simply through sub-contracting to local agents, rather than achieving local ***manufacture***;

- effectively, the entire project could be manufactured and assembled overseas, with the ‘local content’ component requirement being satisfied upon delivery, when final testing and commissioning would take place, or else the so-called ‘local components’, which have in fact been wholly imported but sourced locally, could be installed into wholly imported carriages upon delivery.

In any of these circumstances the local content requirement is satisfied, but there is no net benefit to the local economy, local jobs, or local skills. Moreover, because the proportion of apprentices is tied to the number of local jobs, under these conditions, there will be few, if any, jobs created for apprentices.

On the basis of the above, it not surprising that trade unions are concerned that contracts will be written in such a way as to favour overseas companies, or those who largely source overseas.

Following an approach by the NSW Branch of the Australian Manufacturing Workers’ Union to the Government, RailCorp was instructed to issue a statement to all PPP proponents in order to clarify local content requirements.

That statement which is dated 13 September 2005 and issued by the Project Director (Louise Director) states in part:

> I wish to make it absolutely clear that the references to "manufacturing activity" and "manufactured" mean genuine manufacturing activity using local labour. In particular:
>
> - the purchase of a component which has been manufactured outside Australia or New Zealand will not qualify as Local Content, even if purchased from a business located in Australia or New Zealand;
>
> - the purchases of a component which has been manufactured outside Australia or New Zealand, with only trivial finishing work carried out locally, will not qualify as Local Content.
>
> The Local Content Requirement is a pass/fail test for evaluation purposes. Please ensure that your tender response are fully compliant (*RailCorp Statement to All Proponents*, 13 September 2005).

While this is a welcome clarification, this matter needs to be addressed by the Guidelines to ensure that contracts (rather than just circular letters) contain a definition of 'local content' that is tied to *local labour content* rather than *cost content*. Naturally it would be preferable for these requirements to emphasise skilled local labour.

b. Apprentices

In relation to apprentices the tender documents for the rail project state that:

> PPP co's Human Resources Plan (as required under the Contract Management requirements) must demonstrate the PPP co will meet the Apprenticeship Requirement. The Apprenticeship Requirement is that PPP co and its major contractors, the Rail service manufacturer (during the delivery phase) and the Rail service TLS contractor (during the TLS phase) must employ 1 apprentice *for every 9 tradespersons employed locally* on the project at any time.

The proportion of apprentices to tradespeople of 1:9 is very low an according to the AMWU, it should be 1:3 tradespeople.

In any case, the proposed ratio of 1:9 needs to be looked at in the context of the definition of 'local content'. Apprentices are to be employed as a proportion of tradespeople 'employed locally on the project at any time'. Due to the 'local content requirement', there may be very few local people employed. That is, apprentices will be 1:9 of 20% of very few skilled jobs.

c. Industrial relations

Finally, in relation to industrial relations there is the following reference in the tender documents:

> PPP co must comply with applicable legislation but must consult with Rail Corp on any proposed action which might impact on industrial relations affecting its employees.

As noted above in relation to the Guidelines, there is no definition of 'applicable legislation' which leaves the way open for Federal legislation to be imposed.

9.6 RECOMMENDATION

It is recommended that the PAC:

- *Note with concern that the wider use of privatisation and related practices has been associated with a decline in the number of apprenticeship positions available in the State to the detriment of the State's economy.*

- *Propose that the Guidelines on PPPs should be*

    - *refined so that the Statement of Economic Development Impacts (Appendix 4) makes specific mention of the impact of available apprentice positions and trade positions during the term of the proposed contract;*

    - *amended to require PPP contracts to contain appropriate minimum apprentice-tradespersons ratios which are in line with trade union and community expectations and needs; and*

    - *amended to require PPP contracts to contain a definition of 'local content' that is tied to local labour content rather than cost content.*

10. THE FUTURE – RESTORING ACCOUNTABILITY AND CONTROL

It has been observed that 'a system that requires the prior approval of the legislature of all expenditure will be effective only to the degree that it is not by-passed' (CICA, 1980).

The use of public private partnerships as a financing device involves by-passing the legislature's oversight over public sector expenditure on capital projects and service delivery, on a scale hardly contemplated in recent years.

The traditional power of Parliament has been to require government expenditure to be subject to prior approval, through the submission of Budget bills, and their passage through the Parliament. Over time, these requirements have been modified in minor ways (such as through the use of supplementary budgets, or Treasurer's advances). Arguably the greatest change – till recently – was the establishment of public trading enterprises with the power to sell goods or services to the community – thus establishing alternative repositories of publicly-owned assets and enabling those entities to operate under the direction of commissioners or chief executives or boards of directors. But arguably the proliferation of PPPs has constituted the greatest threat to Parliamentary authority and control thus far devised.

Instead of expenditure being subject to Parliamentary scrutiny (through debate over budget bills, and subsequent reviews by Estimates Committees) PPPs often involve the alienation of revenues streams (such as tolls from motorways) to private sector firms.

Instead of expert planners establishing priorities for new capital works in light of emerging needs, the ready availability of tollway projects to be packaged as PPPs has increased reliance on motor vehicles as a means of transport and fundamentally changed the character of the City of Sydney.

Instead of Ministers being held accountable for the performance of government in delivering services to the community, responsibility for delivery of what are commonly seen as basic government services is being assigned to private sector firms, who are not required to publish information about the quality of services they provide to the community.

Instead of governments having the capacity to adapt to changing needs, some PPP contracts effectively place a freeze on the nature and quality of services to be provided to the community for extensive periods. (One need only consider the manner in which at least one recent PPP contract requires re-negotiation – presumably of pricing or profit sharing arrangements - in the event that a future government decides to widen or upgrade a local road, at some time within the next thirty two years.) In areas of health, in particular, the rapidity of technological change makes the idea of 'locking in' hospital management and maintenance for periods of 20 years or more, especially problematic.

It is contended that adoption of the recommendations outlined in this submission will go some way towards providing Parliament (and the wider community) with the opportunity to apply greater scrutiny to the substance of PPP arrangements. And perhaps, a brake on PPPs that 'lock in' government to existing modes of service delivery in a time of rapid technological change.

It is likely that members of the Government and the public sector may not have the technical training and skills to properly evaluate the financial merits of PPP proposals. The recommendations would provide the opportunity for PPP proposals to be scrutinised by a wider range of stakeholders, and hence allow more effective consultation with the community. The community deserves the restoration of accountability.

The recommendations, if implemented, would provide the Government with the opportunity to (metaphorically) push the chair back from the desk, and reconsider the State's priorities for infrastructure management and development – and even the role of the public sector in the new millennium.

Appendix A

Centennial Consultancy

Centennial Consultancy is located in Sydney and its contact details are:

40 Lang Road
Centennial Park NSW

Telephone:	02 9360 4537
Mobile:	0409 360 453
Fax:	02 9360 4538

It undertakes work in both the private and public sectors.

Public Sector Consultancies

Centennial Consultancy (and/or its principals) has carried out work for many Government agencies including the following:

- Audit Office of NSW
- Australian National Audit Office
- Australian Securities Commission
- Australian Accounting Standards Review Board
- Australian Taxation Office
- Australian Government Solicitor

- Commonwealth Director of Public Prosecutions
- Joint Parliamentary Committee on Public Accounts, Parliament of the Commonwealth of Australia
- National Companies and Securities Commission
- National Crime Authority
- National Standards Commission
- NSW Crown Solicitor
- NSW Department of Gaming and Racing
- NSW Prices Commission
- Prices Surveillance Authority
- Prospect Electricity
- Public Accounts Committee, Parliament of NSW
- Public Accounts Committee, Legislative Assembly of the Northern Territory
- Public Accounts and Estimates Committee, Parliament of Victoria
- Sutherland Shire Council
- Treasury, Northern Territory

Private Sector Consultancies

Due to commercial confidentiality private sector consultancies are not listed. Much of the work has been commissioned through accounting and legal firms including:

- Bush Burke & Company
- Dibbs Barker Gosling
- Firmstone and Feil
- Freehills
- KPMG Legal
- McCabes Terrill

- Middletons Moore & Bevins
- Minter Ellison
- Slater & Elias
- T G Hartman & Associates
- Tress Cocks & Maddox.

Other Consultancies

- Local Government & Shires Association
- National Education Union
- NSW Nurses Association
- NSW Teachers Federation.

Work has been in the following areas:

- the finance sector
- the health industry
- the hotel industry
- the resources industry
- the retail sector.

A principal of Centennial Consultancy is:

Betty Con Walker

B. Ec. (Sydney)

Dip. Ed. (Sydney)

Ms Con Walker is an economist with experience in both the private and public sectors. She worked at CSR Ltd (during which she was nominated for the 'Business Woman of the Year Award', and taught part-time at the University of Sydney), and served on various government advisory agencies. They included the Centennial Park Board of Advice to the NSW Premier, the Australian Council on Population and Ethnic Affairs chaired by the Minister for Immigration and Ethnic Affairs, the National Committee on Discrimination in Employment and Occupation reporting first to the Federal Industrial Relations Minister and then to the Attorney-General, and the Australian Institute of Multicultural Affairs reporting to the Minister for Immigration and Ethnic Affairs. She then joined the NSW Premier's Department followed by the NSW Treasury. She has worked with various governments on policy and legislative development, and the preparation of NSW State Budgets. Her employment in government included four years as a financial adviser and spokeswoman for a former NSW Premier and Treasurer. She then set up Centennial Consultancy which provides advice to government and various industries including the education, finance, health, hotel, resources, and retail sectors. Her publications include joint authorship of *Privatisation: Sell off or sell out?* (published by the Australian Broadcasting Commission, 2000), and a chapter in *Economics as a Social Science: Readings in Political Economy,* Edited by George Argyrous & Frank Stilwell (published by Pluto Press, 2003).

The other principal of Centennial Consultancy is Prof Bob Walker.

Dr Bob Walker

B. Com. (NSW)

M. Ec. (Sydney)

Ph. D. (Sydney)

Member, Institute of Chartered Accountants in Australia

Dr Bob Walker is a Professor of Accounting at the University of Sydney.

He is the author or joint author of six books and monographs and more than 60 articles in academic or professional journals or chapters in books. His specialist interests include public sector finances, corporate regulation, and corporate governance. In parallel with academic activities, Bob Walker's professional involvements and community activities include serving six years as the chairman or deputy chairman of the Australian Shareholders' Association. He was a Foundation member of the Accounting Standards Review Board. He has served as a consultant to a range of organisations in the public and private sectors. Public sector consultancies include the National Companies and Securities Commission, the Australian Securities Commission, the Australian Stock Exchange, Treasury Departments in NSW and the Northern Territory, and Public Accounts Committees in NSW, Victoria and the Northern Territory. Many of his activities have involved working with government in policy development. His work with the NCSC led to the most fundamental change in the regulation of corporate disclosure requirements since the 1940s. He was a member of the Companies and Securities Advisory Committee to the Commonwealth Attorney-General, and a member of the advisory committee to the Commonwealth Auditor-General. From 1995-99 he served as Chairman of the NSW Council on the Cost of Government, a standing 'commission of audit' appointed by the NSW Government to review state finances and develop proposals for reform. In that capacity he reported directly to the Premier and the NSW Parliament. From 1993-97 he served as a director of a Commonwealth statutory authority, and is currently chairman of a NSW state owned corporation, Pillar Administration. Maintaining his involvement in research, Bob Walker was (with colleagues from the University of Sydney) recently the recipient of two Australian Research Council large grants.

Appendix B

2005 ALP Conference Resolution

PUBLIC PRIVATE PARTNERSHIPS (PPPs)

This Conference welcomes the commitment by the State Government to spend $30 billion dollars over the next ten years on vital infrastructure development in NSW. We further note that it is the intention of the State Government to use Public Private Partnerships (PPPs) as the preferred method of funding and delivering this infrastructure.

This Conference notes that the use of PPPs has engendered much controversy both in Australia and overseas. In particular, we note the following problems: -

- That a public agency or government is required to underwrite the financial and political risks arising from the project, whilst having no overall control of many important aspects of the overall costs and effectiveness of the undertaking.

- PPP obligations are "*off balance sheet*". That is, the government can use PPP's to understate debt by not recording in the balance sheet the total value of payments to the private sector. There is also a lack of an Australian accounting standard dealing for (*sic)* risk allocation issues associated with PPP's.

- The potential for far higher overall cost to the taxpayer, as a result of funds borrowed by the private entity being raised on private capital markets, which cost more overall than if a government used its far lower risk rating to raise the funds.

- Higher costs of capital lead to a higher overall interest burden, which must be born by the users of the service, as the private entity prices to users must include debt servicing costs as well as a return on funds (profit).

- A funding model which requires return on funds to a private entity must of necessity, increase the incidence and overall burden of '*user pays*' models for the provision of fundamentally necessary services to citizens, thereby decreasing the capacity of governments to ensure equity in access to the necessities of life, such as water, energy, health, education and transport.

Conference calls upon the State Government to institute a Public Inquiry to investigate all aspects of PPP's, including but not limited to the matters outlined above.

Prior to the completion of this Inquiry, conference calls upon the State Government to carefully consider the risk/return characteristics of all PPP's to ensure they are in the public interest and on the basis that they ensure:

- demonstrable value for public money invested in the project;
- the risk allocation is independently analysed and is transparent;
- upfront legal and establishment fees are quantified, transparent, reasonable and in the public interest, and;
- returns on investment are not excessive and unsustainable in the long term to government budgets.

Such an inquiry should be chaired by a prominent and impartial person having economic and financial expertise and absolutely no vested interest in the outcomes of the inquiry. The terms of reference of such an Inquiry should include matters going to international experience of such arrangements as well as Australian experiences and should be tasked with providing the people of NSW with a Best Practise approach to the raising of funds for the provision of services and infrastructure necessary for the next century. Public submissions should be called for and the submissions should be available to any interested person.

Moved:
Seconded:

12th June 2005

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