

Jackie Ohlin  
Senior Committee Officer  
Public Accounts Committee  
Parliament of New South Wales

22 November 2005

Dear Ms Ohlin

Re: Public Accounts Committee Inquiry into Public Private Partnerships  
Sewerfix Pumping Stations Alliance

I am writing in response to your request, on behalf of the Public Accounts Committee (PAC), for information on Sydney Water's Sewerfix Pumping Stations Alliance.

By way of background, and bearing in mind the PAC's terms of reference, I would like to explain Sydney Water's approach to procurement.

Sydney Water uses a broad range of procurement strategies to execute its capital investment program. Each strategy is aimed at delivering the key project objectives so that optimal value is delivered to our customers and stakeholders. The majority of the program is delivered by conventional design and construct contracts but various other methods such as Build, Own and Operate (BOO), Design, Build, Own and Operate (DBOM) and Alliances have and are being used.

The contracting method selected for each project is based on an assessment of a number of factors including time, complexity, size, opportunities for innovation and risk. As such, it is difficult to compare one contract method with another as each is tailored to meet the particular mix of factors associated with that project. It would be even more difficult to compare an alliance contract with a Privately Financed Project (PFP) due to the fundamentally different issues to be managed and risk allocation between the parties.

Alliance contracting is relatively new in Australia and the art of alliancing is still evolving whereas design and construct contracting is in a very mature stage of development and consequently better understood by the market and the general community.

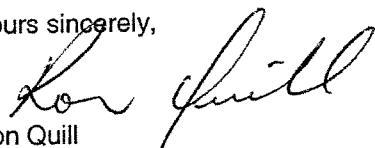
Currently about 25% of Sydney Water's capital program, in dollar terms, is delivered via Alliance contracts.

Sydney Water was one of the first NSW government agencies to use a PPP form of contract to deliver four privately owned and operated water filtration plants were built via BOO contracts which were progressively let from 1993. These contracts operate over a 25 year time frame. These four water filtration plants collectively treat about 90% of Sydney's water supply.

The SPS Alliance and other projects Sydney Water has delivered via alliancing, have all been successful, delivering the required outcomes on or before time, within budget and in an environmentally responsible manner. However, various other contracting methods have also been successful but have experienced more failures because they are more numerous and have been used over a much longer time frame.

I trust the attached information assists the committee in its deliberations.

Yours sincerely,



Ron Quill  
General Manager, Asset Solutions  
Sydney water Corporation

## **Public Accounts Committee Inquiry into Public-Private Partnerships (PPPs) - Submission by Sydney Water Corporation**

### **Introduction**

Sydney Water understands that the focus of the Committee's inquiry into PPPs is private sector investment in public infrastructure projects or what is generally known as privately financed infrastructure projects. These projects generally involve the creation of infrastructure assets via private sector financing, long-term ownership and control. However, it is also possible to have private sector involvement in the financing of existing infrastructure assets.

Private sector investment in Sydney Water infrastructure projects to date includes the creation of the Blue Mountains Sewage Transfer Tunnel Scheme, and the four Water Filtration Plant projects. These projects were delivered via private sector financing, ownership, design, construction and operation over a long-term concession period. The Blue Mountains Tunnel Scheme, commissioned in 1996, involved private sector capital investment of \$80 million while the Water Filtration Plant projects, which were commissioned between 1995 and 1997, required upfront private capital investment of over \$500 million.

While the availability and provision of private financing for large-value infrastructure projects in the face of competing demands on limited internal funding, may be a benefit of private sector involvement, the objectives behind private sector participation in Sydney Water's infrastructure projects to date were much more than gaining access to private financing. Sydney Water wanted to utilise innovative private sector technical solutions, particularly for the delivery of these complex, greenfield projects, private sector management expertise and cost-effective provision of services.

### **Forms of Private Sector Investment**

Private sector investment in infrastructure projects could be provided through a number of structures and may include the following:

- **BOOT/BOO** – the private sector could be involved in full Build, Own, Operate and Transfer (BOOT) schemes as was the case for the Blue Mountains Sewage Transfer Tunnel Scheme or Build, Own and Operate (BOO) arrangements as for the Water Filtration Plants. Under BOOT/BOO arrangements, financing as well as operational expertise is provided by the private sector. The implication of this is that upfront capital expenditure that would have been required by Sydney Water is replaced by ongoing operating expenditure in the form of tariff payments.
- **Sale and Leaseback** – involves the sale and leaseback of existing assets to the private sector. This transaction releases capital tied up in existing assets in return for making lease payments to the private investor over time. Sydney Water's motor vehicle and computer fleet were initially outsourced through these arrangements.
- **Joint Venture** – Sydney Water may enter into Joint Venture arrangements with the private sector for the development of specific projects. Sydney Water could

contribute equity, expertise and/or resources to the project. Tax implications and risk sharing would need to be properly considered under this arrangement. In practice, Sydney Water has not been involved in any joint venture arrangement with the private sector for the delivery of infrastructure projects.

### **Policy and Evaluation Framework for Private Sector Investment**

It is Sydney Water's policy to encourage private sector investment in infrastructure projects where it can be shown that private participation provides clear commercial benefits for Sydney Water and meets its strategic objectives. The regulatory framework within which Sydney Water operates means that all private financing proposals must follow the NSW Government's guidelines with respect to privately financed projects, including approval processes.

The latest update of the Government guidelines, entitled "Working with Government Guidelines for Privately Financed Projects" (the Guidelines), was released in November 2001. As a state-owned corporation, Sydney Water is covered by these guidelines. However, since the Water Filtration Plants, Sydney Water has not undertaken any privately financed project and therefore has had no occasion to bring about a project under the updated guidelines.

The guidelines are considered to be comprehensive with respect to the various phases of project development, the risk management framework and major contractual issues.

In addition to core requirements for economic and financial appraisals of the project, the Guidelines require the preparation of a Public Sector Comparator to enable comparison of the costs of the project under a traditional, government-financed mode of delivery and the cost using private finance.

A full risk assessment is also required for privately financed projects. In principle, risk should be allocated to the party best able to manage the risk and should be considered on a project-by-project basis. However, the Guidelines contain a risk table outlining the risk areas, specific risks, consequence, mitigation and preferred allocation of risks, which would be a useful starting point for future privately financed projects.

### **Opportunities to Share Knowledge Across Agencies**

Sydney Water is of the view that opportunities to share knowledge across and between agencies should be maximised. The Guidelines also promote inter-agency participation, particularly from the Department of Commerce for oversight of technical contracting and procurement aspects where the agency lacks in-house expertise and experience, and the NSW Treasury for advice on PPP projects.

Under the Guidelines, agencies are required to consult the Private Projects Branch in NSW Treasury in the development of a privately financed project. The Private Projects Branch has the role of ensuring the application of the Guidelines and advising Government and government agencies. It may also provide economic and financial expertise in the assessment of privately financed projects.

## **Potential benefits of Private Sector Investment**

There are a number of potential benefits from private sector financing, including:

- private sector financing can provide real financial benefits from off-balance sheet funding;
- private sector funding can allow infrastructure projects to be delivered earlier than would otherwise be the case - private sector funding can supplement Sydney Water's capital funding and defer large capital expenditures;
- private sector ownership can lead to technical and commercial innovation in construction and long-term operation by focussing on the desired outcomes rather than traditional approaches and using financial structuring
- the involvement of the private sector can allow benchmarking with the way Sydney Water manages the provision of services (assuming there is transparency of the private sector's costs)

## **Future for Private Sector Investment in Sydney Water**

Although private sector investment can release resources for other projects, the availability of funds will not be the major driver of potential private sector investment in the foreseeable future. The primary drivers for Sydney Water for future private sector investment will be the continuing goal to focus on core business, customer service, regulatory compliance, cost-effectiveness, innovation and management of risk.

While there have been no recent approaches from the market for the financing of existing infrastructure, there are potential opportunities for the financing of new infrastructure projects, such as:

- packaging of renewable energy generation projects at various sewage treatment plants; and
- non-infrastructure assets, including the development and long-term leasing of Sydney Water's proposed Head Office accommodation at Parramatta.