The University of Sydney
Faculty of Economics and Business

School of Business

NSW 2006 AUSTRALIA

Linda English
B.A. (Syd.); B.Com. (Monash); CPA
Senior Lecturer, Discipline of Accounting and Business Law
Managing Editor, *Australian Accounting Review*

Economics and Business Building H69
cnr Rose & Codrington Street
telephone + 61 2 9351 3900
facsimile + 61 2 9351 6638
email l.english@econ.usyd.edu.au

Thursday 13 October 2005

Submission to the Legislative Assembly Public Accounts Committee Inquiry into Public Private Partnerships

Evaluation and Monitoring of Public Private Partnerships

Researchers from the University of Sydney (Professor James Guthrie, Linda English and Associate Professor Sue Newberry) and the University of London (Professors Jane Broadbent and Richard Laughlin) are recipients of a large Australian Research Council Linkage Grant to develop a model for the post-project evaluation (PPE) of Australian public-private partnerships (PPP); linkage partners to the project are the Auditors-General of Victoria and Western Australia, CPA Australia, Maddocks Legal and Warringah Shire Council.

Within the broad aim of investigating existing evaluation systems for Australian PPPs and developing a generic evaluation model, the specific research questions to be addressed are:

1. What PPE systems currently exist for Australian PPPs?
2. What can be learnt from international practice concerning long-term PPP evaluation?
3. How can the insights of management and evaluation theory assist the development of a PPP-specific PPE system?
4. What are the features of a generic PPE system that would meet the needs of key stakeholders, and how would this be operationalised?

PPPs involve the financing, design, construction and maintenance of underlying infrastructure assets, as well as the provision of related services, by the private sector. This definition is based on the New South Wales and Victorian policy documentation (WWG 2001, VDTF 2000) and excludes many arrangements that involve some element of partnership between the two sectors for the provision of infrastructure. Reference in this submission to PPPs, unless a contrary intention is evident, is reference to PPPs as described in this paragraph.

There are essentially two types of PPP payment structures. The first, exemplified by tollways, involves the government providing a concession to a private operator for a set period, with consumers paying directly according to their usage. The second involves direct government subsidisation of private sector partners to provide 'public' services in areas such as health and correctional services. This second type of PPP generally involves payment based on specified performance criteria, with the objective of reducing the cost of service provision[1].

Over the past decade Australian governments have entered into PPP contracts worth over $32 billion with projects worth over $55 billion currently in the planning stage (AusCID 2004)[2]. A wide variety of services in areas such as health, detention, utilities and transport, that were previously the sole responsibility of the public sector, are now being delivered through PPPs[3]. The need for inquiry into the nature, purpose and achievements of PPPs has been recognised both in Australia and internationally (Broadbent and Laughlin 1999, English and Guthrie 2003). PPP proponents argue that they provide value for money and superior services for taxpayers by transferring risks to private sector partners and utilising competition to generate efficiencies in service delivery (Broadbent and Laughlin 1999, Heald 2003, English and Guthrie 2003, Fitzgerald 2004, VDTF 2000).

The extent to which PPP arrangements deliver on this potential depends on the pre-decision specification of performance criteria, financial modelling, unanticipated future events and the nature of the relationship between the partners. PPP outcomes can only be effectively assessed through long-term monitoring and evaluation. The negatives of PPPs are frequently the subject of media coverage. Less is known about successful PPPs and why they are successful.

Currently there is little disclosure of reviews of PPPs, either by governments or by private sector partners. There is some evidence that auditors-general have made attempts to monitor and evaluate PPPs. However there has been no systematic monitoring and evaluation of PPPs by any Australian auditor-general. Moreover, there is little evidence in Australia or elsewhere of a systematic attempt to develop a theoretically and empirically informed post period evaluation system capable of capturing, evaluating and reporting on the success of these complicated long-term partnerships.

Although the Australian experience of PPP implementation is complicated by differing approaches in different jurisdictions (federal, state and local), there is a trend towards convergence, with Victoria generally providing leadership in documentation and innovative use of PPP arrangements (English and Guthrie 2003). The Australian approach also borrows heavily from the UK's Private Finance Initiative (PFI)[4].

Steered by policy documentation at the organisational level (English and Guthrie 2003), government agencies must demonstrate, prior to contracting, that the PPP represents value for money and that appropriate risk transfer to private partners will be achieved. Once the PPP is operational, a system of accounting-based monitoring becomes an

---

[1] The payment structure of some PPPs, including many public transport PPPs, contain elements of both direct payment and government subsidisation.

[2] All Australian state, federal and territory governments have PPP policy documentation in place.

[3] In the Australian context, the term PPP refers to "a contract for a private party to deliver public infrastructure-based services", excluding "outsourcing or other service delivery arrangements where no capital investment [by the government] is required" (VDTF 2001).

[4] The UK PFI currently involves 563 projects worth £35.5 billion (Broadbent and Laughlin 2004).

important means of determining whether the terms of the contract (which defines each party's expectations) are being maintained, and hence of calculating payments (or penalties in the case of non-achievement) to contractors. This accounting information is used to monitor the standard of services provided and to determine whether value for money has been attained.

Value for money is, in part, achieved by transferring risk to private partners. The value for money of a potential PPP is measured against the Public Sector Comparator (PSC), a hypothetical benchmark representing the most efficient public procurement option specified at net discounted cost[5]. In the pre-contract stage, the relevant government agency develops an outline business case to justify the project, may conduct a public interest test to consider non-financial impacts, and negotiates with potential bidders (after which the PSC is recalculated to adjust for negotiated changes in costs and risk allocations).

There is clearly a level of uncertainty as to what the risks really are and whether they will remain stable; how they are to be quantified; which ones can and should be transferred; and the characteristics that demonstrate when a risk is actually residing with a particular party. These pre-decision processes, including contractual arrangements in place to specify and monitor performance, are crucial to the decision to take the PPP route, to the ongoing achievement of value for money in any PPP arrangement, and also to the design and implementation of a post project attempt to systematically evaluate their long-term effectiveness in achieving policy and value for money objectives.

In Australia (Partnerships Victoria 2000), as in the UK (Broadbent et al 2003a, 2004), the major focus of ongoing internal government agency monitoring of government-subsidised, welfare-type PPPs is ongoing facilities management rather than post project evaluation. For instance, Partnerships Victoria's *Management Guide* (2000) focuses on various aspects of contract management, such as the timely identification and containment of risks. Post project evaluation is important because it is capable of assessing the merit and worth of the project as a whole, whereas ongoing facilities management takes the project's existence as given and seeks only to optimise outcomes within this framework. Thus, although facilities management is important, it is increasingly understood that it is only one aspect of the set of important issues and concerns relating to financial and non-financial PPP evaluation (NAO 1999, IPPR 2001).

To date the academic research into PPPs has largely concentrated on their nature and purpose, which essentially relates to their financial accounting treatment. Are PPPs a macro fiscal device to reduce government borrowing or a micro procurement process that provides value for money? Risk assessment and allocation is not only important in the decision process, but also in the financial accounting decision concerning asset status and ownership. It is now generally accepted that PPPs are a micro procurement process for the provision of services from the private sector to the public sector which are intended to generate value for money for the latter in the context of risk transfer to the former.

---

[5] The PSC formula includes all capital, operating costs and share of overheads after adjustments for competitive neutrality, retained and transferable risk to achieve the required service delivery outcomes (Partnerships Victoria 2000).

Increasingly, however, this quantitative analysis is seen as needed to be complemented with a more qualitative set of concerns surrounding particular forms of shared risks and benefits analysis. Currently these qualitative concerns are more marginal to the financial quantitative analysis, but Broadbent, Gill and Laughlin (2004) suggest that quantitative analysis should become a key part of the decision criteria and of a systematic method to evaluate PPPs over their lives.

The accurate calculation and allocation of costs and the quantification of transferred risks should be enhanced by consideration of qualitative shared risks and benefits, and their combination in the PPP decision-making process. These are important challenges for management accounting. Accordingly, the nature of the management accounting and control systems that are in place and should be in place are important in the development of a systematic post-period evaluation system.

It is advised that the Committee takes steps to ensure that the New South Wales Auditor-General is given sufficient powers to review the private parts of PPP arrangements and consider developing a parliamentary oversight model to ensure systematic long-term monitoring and evaluation of PPPs.

Linda English
For and on behalf of the research team

Australian Council for Industrial Development (AusCID) (2004), *PPP Database,* available from http://www.auscid.org.au, accessed 26 April 2004.

Broadbent J., Gill, J., and Laughlin R. (2003a), "Evaluating the Private Finance Initiative in the National Health Service in the UK", *Accounting, Auditing & Accountability Journal* 16, 3: 422-45.

Broadbent J., Gill, J., and Laughlin R. (2003b), "The Development in Contracting in the Context of Infrastructure Investment in the UK: The Case of the Private Finance Initiative in the National Health Service", *International Public Management Journal*, 6 (2): 146-172.

Broadbent J., Gill, J., and Laughlin R. (2004), "The private Finance Initiative in the National Health Service: Nature, Emergence and the Role of Management Accounting in Decision Making and Post-Decision Project Evaluation", CIMA Monograph: London.

Broadbent, J., and Laughlin R. (1999), "The Private Finance Initiative: Clarification of a Future Research Agenda", *Financial Accountability and Management,* 15, (2): 95-114.

English, L., and Guthrie, J. (2003), "Driving privately financed projects in Australia: what makes them tick?", *Accounting, Auditing and Accountability Journal* 16, 3: 493-511.

Fitzgerald, P. (2004), "Review of Partnerships Victoria Provided Infrastructure: Final Report", January, available from http://www.partnerships.vic.gov.au, accessed 26 April 2004.

Heald, D., 2003, Value for money tests and accounting treatments in PFI Schemes, *Accounting, Auditing and Accountability Journal* 16, 3: 342-71.

Institute for Public Policy Research (IPPR) (2001), "Building Better Partnerships: The Final Report of the Commission on Public Private Partnerships", London: IPPR

National Audit Office (NAO) (1999), "Examining Value for Money Deals Under the Private Finance Initiative" (HC 739, 1998/99, 13/8/99), London: The Stationery Office.

Partnerships Victoria 2000, "Contract Management Guide", available from http://www.partnerships.vic.gov.au, accessed 27 July 2004.

Victoria, Department of Treasury and Finance (VDTF) (2000), Partnerships Victoria, VDTF, Melbourne.

Working With Government (WWG) (2001), *Working with Government: Emerging PFP Opportunities*, Working With Government Task Force, New South Wales Government Printer, Sydney.