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3/2/06 CO

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INFRASTRUCTURE PARTNERSHIPS AUSTRALIA
Building Australia Together

Opening Remarks from Garry Bowditch to the Joint Select Committee on the Cross City Tunnel - 3 February 2006

Infrastructure Partnerships Australia (IPA) a new industry association consisting of over 70 companies and public sector organizations involved in the planning, construction and operation of infrastructure. Our purpose is to build genuine and enduring partnerships between the public and private sector for the provision of infrastructure.

Firstly, I would like to thank the Committee for the opportunity to participate in this inquiry. There has been a clear demonstration that the Committee is independent and has brought considerable credibility to this matter.

In my opening remarks I would like make some observations in respect of 3 key areas that I believe are pertinent to the Committee's deliberations.

1. Why the private sector has emerged as an important player in infrastructure?
2. Make some brief observations on traffic modeling
3. Comment on up-front payments and contract governance for future transport related infrastructure.

Firstly, why is the private sector now an important player in infrastructure provision?

In the past the community has looked towards the government to provide its infrastructure, but this is less so now with governments facing competing demands for social services, combined with changing attitudes towards running budget deficits and government debt that has led to tighter management of capital budgets and greater efficiency. This has resulted in a general willingness to rely more on the private sector to develop new innovative vehicles such as public private partnerships, to take the burden-off taxpayers.

The benefit to NSWs from private sector involvement in infrastructure has produced world class design and project management. This has resulted in the early delivery of CCT, one aspect that is consistently demonstrated with other PPP projects.

Unfortunately, some of the public debate on PPPs has been based on spurious economic argument. For instance, questions like why the private sector should be raising capital for infrastructure when the government can borrow more cheaply at what is commonly referred as the risk free borrowing rate - comes to mind.

It is a matter of fundamental economics that the risk free borrowing rate is not the end of the story in terms of the capital costs associated with government projects. All projects imply some form of risk, concerning its planning, construction and operation and the burden of that risk is carried by owners of the project in the case of the private sector, and in the case of the public sector it is borne by the government itself and ultimately the taxpayer.

So if a project in government should run foul, the transparency for project risk and who is responsible for it can easily get lost in the complexity of public accounts, but rest assured it is the taxpayer who will carry the final burden.

The notion that there can be a free lunch is a belief based on ignorance and similarly that there is such a beast as a risk-free infrastructure project. The other side of this argument is that when project risk is identified and individuals are held to account then meticulous management of project risk occurs. This is where PPPs have made an important contribution to superior provision of infrastructure.

It is essential that IPA succeeds in its mandate to improve the working and strategic relationships between the public and private sectors, simply because the task of providing infrastructure is so large and important that no government can execute this task alone. It is in that spirit that we appear today – one of improvement and seeking best practice.

For example, over the past five years, tollways worth $3.3 billion have been initiated. Without private investment in these projects, they would have consumed the entire RTA capital works budget for Sydney over the past 10 years. PPPs allow governments to do much more in providing infrastructure and services rather than resorting to the old school of budget management that means chopping back services and doing without.

The massive wall of money sourced from Australian's saving for their superannuation is in need of quality projects for investment. Public private partnerships can and should be a hand in glove fit for ensuring Australia and NSW are equipped with the right infrastructure to grow our economy and living standards sourced from our own pool of savings.

Secondly, I will make some observations about traffic modeling.

I would like to refer the Committee to a recent study undertaken by Standard and Poor's Rating Agency that examines 104 international toll road, bridge and tunnel case studies most of which were project financed concessions. The study has confirmed the existence of over-forecasting asset use (i.e. optimism bias) by comparing predictions of asset patronage before the project is complete with actual patronage in each of the first five years of operation. The key points of the study are interesting:

- On average, across all toll roads, bridges and tunnels, forecasts over-estimated traffic in the first year by 20-30 per cent. There was no dramatic improvement in forecasting accuracy between years 2 to 5.
- The bias was not caused by a failure by forecasters to consider the ramp-up during the very early period of opening.
- Despite allowing for ramp-up the actual numbers were far less aggressive than assumed in predictions and take some years to be fulfilled.

The experience of the CCT in this respect appears to be no worse or no better than the experience of new toll roads throughout the world. I would encourage members of the Committee to take a broader perspective on the CCT and avoid any early judgment as to whether it is underperforming. It is simply too early to tell.

The possible lessons of this analysis suggests that:

1. It is appropriate that the private sector bear the ultimate responsibility for its (potential) optimism on traffic volume and therefore the government got it right to pass all the patronage risk to the concessionaire.
2. On the other hand, the use of up-front payment to defray Government costs of the project has the potential to exacerbate the problems of optimism bias. The capacity of a concessionaire to provide an up-front payment will rely on their estimation of traffic volume and revenue risk.
    a. Clearly, governments need to be level headed and have their own view of traffic volumes, over the ramp-up and life of the project and ensure it has that expertise in-house. This will help to judge the robustness of the concessionaire to withstand a broad range of financial scenarios without risk of defaulting.

Finally, infrastructure – whether it is a road, bridge, tunnel, school or hospital is much more than a series of physical assets scattered around the landscape. Infrastructure is not simply about reinforced concrete but the services that these assets deliver to their customers and stakeholders. It is essential that the CCT continues to explore with its customers what value they seek from the tunnel as a service and that they find the right value proposition to attract and sustain patronage.

Equally, we must see the PPP model as one that will evolve over time, and this inquiry should be a helpful step in that process.

It is essential that we acknowledge that this is a learning experience for government, the consortia and its stakeholders and IPA stands ready to assist with this process in the interest of continuous improvement of government services and the procurement of infrastructure.

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