



## **PUBLIC ACCOUNTS COMMITTEE**

***Inquiry into the Funding of Capital Projects by  
the New South Wales Government***

# **PARRAMATTA RAIL LINK PRE-TENDER PROCUREMENT**

## **A CASE STUDY**



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**Parramatta Rail Link**



# Pre-Tender Procurement: A Case Study

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## Charter of the Committee

The Public Accounts Committee has responsibilities under the *Public Finance and Audit Act 1983* to inquire into and report on activities of government that are reported in the State's Public Accounts and the accounts of the State's authorities.<sup>1</sup> The Committee, which was established in 1902, scrutinises the actions of the Executive Branch of Government on behalf of the Legislature.

The Committee recommends improvements to the efficiency and effectiveness of government activities. The sources of inquiries are the Auditor-General's reports to Parliament, referrals from Ministers and references initiated by the Committee. Evidence is primarily gathered through public hearings and submissions. As the Committee is an extension of Parliament its proceedings and reports are subject to Parliamentary privilege.

## Members of the Committee

The Committee comprises members of the Legislative Assembly and assumes a bi-partisan approach in carrying out its duties.

<b>Chairman:</b>	Joseph Tripodi MP, Member for Fairfield
<b>Vice-Chairman:</b>	The Hon. Pam Allan MP, Member for Wentworthville
<b>Members:</b>	Ian Glachan MP, Member for Albury
	Katrina Hodgkinson MP, Member for Burrinjuck
	Richard Torbay MP, Member for Northern Tablelands
	Barry Collier MP, Member for Miranda

## Committee Secretariat

Secretariat members involved in the Inquiry were:

Committee Manager:	Yael Larkin
Project Officer:	David Monk
Committee Officer:	Stephanie Hesford
Assistant Committee Officer:	Mohini Mehta
Adviser to the Committee:	Rebecca Bishop
Adviser to the Committee:	Christopher Bowdler

## To contact the Committee:

Public Accounts Committee	Telephone (02) 9230 2631
Parliament House	Facsimile (02) 9230 2831
Macquarie Street	E-mail <a href="mailto:pac@parliament.nsw.gov.au">pac@parliament.nsw.gov.au</a>
Sydney NSW 2000	

<sup>1</sup> See Part 4 of the Act – The Public Accounts Committee.



## Chairman's Foreword

This Report, *Parramatta Rail Link Pre Tender Procurement: A Case Study*, focuses on issues relating to the Parramatta Rail Link, a current project of the NSW Government. Lessons from experience with this project are drawn out in order to improve future infrastructure transactions for both the NSW Government and private sector participants.

The Public Accounts Committee has previously considered infrastructure issues in numerous reports including its 1993-94 *Inquiry into Infrastructure Management and Financing in New South Wales*, with two reports: Volume 1: From Concept to Contract – Management of Infrastructure Projects (Report No. 73, July 1993) and Volume 2: Public-Private Partnerships – Risk and Return in Infrastructure Financing (Report No. 80, February 1994).

These reports led to significant changes in the management and financing of infrastructure, with one example being the publication of contract summaries when each infrastructure contract is negotiated.

A second improvement from the Committee's earlier work has been revisions to the Government's *Guidelines for Private Sector Participation in the Provision of Public Infrastructure* (September 1995, revised October 1997). As a result, there is now a clear process for the Government to consider whether and in what ways the private sector may be involved in the provision of infrastructure. It is less clear that the private sector understands the Government's infrastructure planning and procurement processes and the possibilities for its involvement. The Committee believes that further improvements in infrastructure planning and procurement are possible and therefore embarked on the current Inquiry.

The Committee initiated this Inquiry following private sector concern that the path and processes proposed to be followed by the Department of Transport would be too restrictive in such matters as scope, funding options, and construction and design specifications. In turn, concerns grew that such restrictions could preclude the innovative capacity of the private sector to attain a maximum value-for-money from the transaction. Given the scale of the project, the Committee became concerned about this assertion.

Overall, the Committee believes that the Government's processes of planning and eliciting proposals for the Rail Link have been consistent with achieving value for money on behalf of the citizens of New South Wales. The Rail Link has been planned to assist in meeting Sydney's overall transport needs and the private sector has had ample opportunity to contribute its ideas for the construction and financing of the project.

Some areas of improvement are noted. For example, if there are restrictions placed on particular private financing mechanisms in the Registrations of Interest and Alternative Proposals, background reasons may be provided. However, funding decisions are a matter of policy and therefore always remain the prerogative of Government.

The Committee's greatest concern rests with the regular conflicts and strategic political and budgetary interplays that occur between Treasury and the agency proposing the project. Treasury has substantial expertise in scrutinising the economy and value of a public-private partnership deal. Actually, section 8 of the *Public Authorities (Financial Arrangements) Act (1987)* requires such scrutiny and the Treasurer must ultimately consent to the "financial accommodation". Treasury is also the budgetary control or funding approval agency. This



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dual role of Treasury may involve conflicts of interest. Considering the capital funding requirement of the Parramatta Rail Link, the Government needs to be careful in managing the process. Recent initiatives between agencies and Treasury to control this are to be commended.

The Committee wishes to thank all parties who made submissions to the Inquiry and all public officials who provided information and gave evidence.

*Joe Tripodi*

Joseph Tripodi MP  
Chairman



## Recommendations

1. When proponents of infrastructure proposals offer intellectual property involving specialist technologies etc., that are innovative and beneficial, the Government's initial approach should be to manage the tender so that it can capture the intellectual property without disadvantaging its owner. When this cannot occur the Government should consider purchasing the intellectual property for use by all the parties involved in the tender. (Page 17).
2. The approach followed in the Parramatta Rail Link should be continued in future Invitations for Registrations of Interest and Alternative Proposals:
  - the project should be defined by outcome and performance subject to Government policy and processes (especially the Environmental Impact Statement); and
  - future Invitations for large projects should be structured as a dual Invitation for (a) Conforming Packages and (b) Alternative Proposals. (Page 20).
3. Treasury should commission an independent review of the extent and cost implications of suboptimal project construction periods resulting from restrictions in Budget allocations, and make recommendations to prevent this in future. This review should be provided to the Treasurer, and should involve major line agencies, such as the Departments of Education, Health, and Transport, as well as the Department of Public Works and Services. (Page 22).
4. As occurred in the Parramatta Rail Link project, any updates in key information should be provided to interested parties for use in preparing their Registrations of Interest and Alternative Proposals. Sufficient time should be given to proponents after changes to key information in the Invitation. However, these changes should be kept to a minimum. (Page 23).
5. The Government should continue to reserve its prerogative to choose how to finance any project. However, it should define its policy on shadow tolls as a means of financing infrastructure. If there are certain types of projects where shadow tolls could be considered, or where they will not be, this should be spelt out with supporting reasons. (Page 24).
6. The Government should require detailed tender bids to include the financial model used to price the tender, as proposed in its Green Paper "*Working with Government*". (Page 32).
7. The Government should create a centralised source of expert advice in project and service procurement. A special unit within the Department of Public Works and Services should advise agencies on how to structure transactions involving the private sector. The Government should consider current or former staff of the Olympic Coordination Authority for recruitment into this new unit, and it should also create an approved list of private sector project management experts, to introduce contestability in this key role. (Page 37).





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## Introduction

The Public Accounts Committee established its *Inquiry into the Funding of Capital Projects by the New South Wales Government* to address issues which have become evident in both privately and publicly financed infrastructure. Under the Terms of Reference the Committee examined:

1. the funding of large capital projects by the NSW Government, including the impact of legislative requirements and budgeting practices;
2. private sector funding practices for infrastructure projects, including any benefits to arise from the optimisation of project construction and funding periods;
3. an examination of the funding aspects of selected capital projects, including the balance of risks and rewards between the State and private enterprise, the cost of underwriting by the State and accounting/taxation treatments;
4. whether improvements are possible to the funding arrangements for large capital projects, including improved economic benefits and service provision, and any implications for the funding of infrastructure in regional and rural NSW; and
5. any other relevant matters.

The report first summarises briefly the history of the Parramatta Rail Link, then gives an overview of the Government's processes for infrastructure procurement, including consideration of private sector financial involvement. The report then moves on to evaluate concerns expressed in submissions and matters raised in the Hearings.

### Focus of Current Report

Following representations that there were opportunities to achieve greater public value for money in the Parramatta Rail Link project, the Committee decided that the Inquiry would focus on this project.

In focusing on the Parramatta Rail Link the Committee drew on expertise currently involved in this major infrastructure project with the aim of improving future practices. The Committee did not review the Parramatta Rail Link's objectives nor any probity issues. In any case, no issues of probity emerged during the investigation.

The Committee was conscious that because the project is under way there was both an opportunity and a danger in investigating it. The opportunity was that if there were any shortcomings in the Government's approach, improvements could be made and thereby improve the value for money achieved for the citizens of New South Wales. The danger was that if the Committee's investigations gave an advantage to any of the tenderers, this could corrupt the process and jeopardise the outcomes. In this respect, advice was obtained from the Independent Commission Against Corruption (ICAC) (Appendix 1).

The ICAC's advice considered that the scope of the Committee's inquiry was not improper provided that commercially sensitive information was not communicated to competitors and that no advantage was given (or perceived to be given) to any bidder. Furthermore, the Committee was not in a position to make technical judgements concerning risk and value for money, and has therefore focused its inquiry on the processes of procuring the project and not on the content of any party's Registration of Interest or Alternative Proposal.



To strike a balance between airing the views in documents and submissions to the Inquiry and respecting their confidentiality, the report has excerpted relevant material from submissions. The relevant parties have approved these excerpts for public release.

## **Process of the Inquiry**

The Committee placed two advertisements, one in March 2000 seeking submissions in relation to the wider scope of the Inquiry and one in August 2000 particular to the Parramatta Rail Link (see Appendix 2).

In response to the first advertisement, four submissions were received:

- two from private sector infrastructure providers with general suggestions for improvement; and
- two from individuals concerned that past arrangements have not been cost effective – both with a focus on the M2 Motorway. Both parties have previously raised their arguments in other forums (e.g. with the Auditor General) and it was therefore considered unnecessary to review them again.

One of the submissions suggested that shortening the construction schedule from six to four years could reduce the cost of the Parramatta Rail Link, if finance (Budget or private) were available. The considerable potential savings (some \$234 million in nominal dollars) gave rise to the focus of this Report on the Parramatta Rail Link project.

In order to gain other views, a second advertisement was placed focusing on the Parramatta Rail Link. Four submissions were received, of which two were from parties who had responded to the previous advertisement. A list of all submissions is contained in Appendix 3.

To evaluate these concerns, the Committee Secretariat did desk research and interviews. The Committee also wanted to hear directly from the relevant public sector bodies, and in camera Hearings were held on 23 November 2000. A list of witnesses is given in Appendix 4.



## Chapter One

### History of the Parramatta Rail Link

In July 1998 the Government announced in principle approval for the construction of a new commuter rail link from Parramatta to Chatswood via Epping. It is the largest infrastructure project in Sydney since the 1920s when it was first considered as part of Sydney's rail expansion<sup>2</sup>.

The project is included in *Action for Transport 2010*, the Government's strategic plan for the transport sector. The objectives are to:

- support the development of Parramatta as Sydney's second CBD;
- support key educational and employment centres along the route;
- improve public transport access for residents of western, south-western and north-western Sydney and the Central Coast to employment, education and health facilities;
- assist in improving Sydney's air quality;
- increase the benefits of other public transport initiatives such as the Liverpool to Parramatta rapid bus transitway; and
- to improve the efficiency and reliability of Sydney's rail network<sup>3</sup>.

The projected cost in *Action for Transport 2010* was \$1.4 billion (in 1998 dollars) and the full amount has been provided in the forward Budget estimates.

Both the Australian Labor Party and the Coalition were committed to a Parramatta-Hornsby link in the 1995 election<sup>4</sup>. The project had its inception in the amalgamation of this link with separate investigations for an Epping-Chatswood rail link. This resulted in a strategic examination of the corridor from Parramatta through the Macquarie corridor to the lower North Shore<sup>5</sup>.

According to the Rail Access Corporation,<sup>6</sup> there were 11 phases prior to the development of a preferred option and the recommendation to conduct an Environmental Impact Statement. These phases included:

- compilation of a long list of alternatives which would achieve the project objectives;
- establishing their technical feasibility;
- short listing the modes, routes and station/stops based on capital and operational cost, land-use, environmental considerations and projected patronage; and
- more in depth studies of the short-listed options.

Community consultation on the project occurred through the Environmental Impact Statement (EIS) which commenced in September 1998 with the final report published in December 1999. The EIS evaluated 12 route/mode alternatives, and concluded that heavy rail between Parramatta, Epping and Chatswood was the best option to meet the project

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<sup>2</sup> The Hon. Carl Scully MP, Minister for Transport, Second Reading Speech, *Transport Administration Amendment (Parramatta Rail Link) Bill*, 4 May 2000.

<sup>3</sup> NSW Department of Transport, *Parramatta Rail Link Overview Report*, November 1998, page 5.

<sup>4</sup> Bob Carr, Leader of the Opposition, "Labor Plans for NSW-1995 Election Speech", Australian Labor Party March 1995, page 11; and Bruce Baird, Minister for Transport, Media Release 12 December 1994.

<sup>5</sup> Parramatta Rail Link Overview Report, page 1.

<sup>6</sup> Rail Access Corporation Presentation to NSW Treasury, 7 July 1997.



objectives. This was recommended for consideration by the Minister for Urban Affairs and Planning. At the time of this report, the EIS Assessment Report had not yet been completed by the Department of Urban Affairs and Planning and consequently no decision had been made by the Minister.

Concurrent with the EIS, the Government continued developing the procurement and contracting strategy (see Appendix 5 for details and supporting documents).

Following the Government's in-principle approval for the Parramatta Rail Link, the Department of Transport was made responsible for the project management through to the completion of the environmental assessment process. A private company has been established as a vehicle for coordinating the three agencies involved (the Rail Access Corporation, the State Rail Authority and the Department of Transport). The Committee believes there are both advantages and disadvantages in the choice of a private company as the legal entity, and believes that the Auditor-General's June 2001 audit of the Parramatta Rail Link Company will be an opportunity to address these issues.

With the establishment of the Company, public tenders were called for legal, technical and contracting strategy advisers. These tenders were awarded to top level experts in their respective fields, being Clayton Utz, Maunsell and Bovis Lend Lease. In addition, Arthur Andersen was appointed by the Department of Transport in the role of financial adviser<sup>7</sup>.

In March 2000 a workshop was held with the immediate stakeholders which includes the Parramatta Rail Link Company, Department of Transport, Rail Access Corporation, State Rail Authority, and independent advisers with the aim to establish the contracting strategy. This strategy was to be based on the Government's objectives (value for money, innovation, risk with the people who can best bear it, Government input to the design of stations), and restrictions (e.g. no shadow tolls)<sup>8</sup>. The major decision was to be how the Invitation for Registrations of Interest should be structured, as single or multiple contracts and what should be included (design and construct or design construct and maintain). Following the workshop, the Parramatta Rail Link Board asked for this Strategy to be independently reviewed by a team of four private sector experts.

In April 2000, the Government issued the *Invitation for Registration of Interest and Alternative Proposals*<sup>9</sup>. The *Invitation* sought expressions of interest for the 11 conforming contract packages and also permitted alternatives to be offered, if proponents so wished.

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<sup>7</sup> Transcript of Hearings, page 36.

<sup>8</sup> Meeting of PAC Chairman and Secretariat with PRL Project Director, 9 October 2000.

<sup>9</sup> NSW Government, Parramatta Rail Link, *Invitation for Registration of Interest and Alternative Proposals*, 12 April 2000.



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Registrations of Interest were made by 27 proponents of which 17 provided alternatives (including some for the rail link as a whole). The outcome of this stage is expected to be that a small number of parties will be selected to submit detailed tenders.



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## Chapter Two

### Current Government processes for infrastructure provision

#### Infrastructure Planning

Infrastructure planning is carried out by individual Government agencies which plan for individual infrastructure sectors as part of their overall service delivery strategies. Agencies prepare Capital Investment Strategic Plans (CISPs) which show a detailed five-year program and a broad strategy spanning at least ten years<sup>10</sup>. Ministers submit the CISPs of their agencies to Treasury as part of the Budget Cycle on a rolling basis.

Budget submissions must address three criteria to be eligible for funding<sup>11</sup>:

- ❖ Proposals must meet a clear social need. The community's 'true need' for a project can be analysed by such measures as cost-benefit analysis and value management. Such analyses take as their starting point fundamental social and economic factors, such as population growth and future economic growth, which generate infrastructure needs.
- ❖ The project must be consistent with current government strategies and legislation. The Government's strategic policy commitments include:
  - developing economic growth and employment;
  - achieving social justice and livable cities;
  - protecting the environment; and
  - attaining financial responsibility<sup>12</sup>.
- ❖ Projects must demonstrate an excess of benefits over costs. Economic and financial appraisals are submitted to Treasury in advance of (or as part of) agencies' annual Budget submissions for the next financial year. An economic appraisal examines the external benefits and costs of the project for other organisations and individuals. A financial appraisal measures the direct effects on the cashflow of the agency of an investment decision, including any proposed private sector financing.

Satisfying the above criteria does not necessarily mean the infrastructure project will go ahead. There is always an excess of projects which provide a net economic and social benefit and they must be ranked and scheduled by the Budget Committee of Cabinet as part of the Budget process. The Treasury provides advice on all submissions to the Budget Committee to ensure that all potential options and linkages with other agencies have been considered.<sup>13</sup>

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<sup>10</sup> Department of Public Works and Services Notes for the PAC Hearing, 23 November 2000, page 7.

<sup>11</sup> Urban Infrastructure Management Plan, *Volume Two: Tomorrow Planned Urban Infrastructure Investment for 1999/2004*, pages 25-28.

<sup>12</sup> NSW Government, "Working With Government: Private Financing of Infrastructure and Certain Government Services in NSW", 2000, pages 5 and 6.

<sup>13</sup> NSW Treasury, *Economic Appraisal Principles and Procedures Simplified*, March 1999.



This process aims to ensure that those projects which provide the greatest net benefit to the community, in accordance with Government policies, receive priority in the allocation of funds.

## **Guidelines for Private Sector Participation in the Provision of Public Infrastructure**

In planning an infrastructure project, agencies may consider involving the private sector in a number of ways. One is by project management of construction (through construct, design and construct or design, construct and maintain arrangements). In addition, certain projects may warrant financing by the private sector, fully or in part.

Under the *Guidelines for Private Sector Participation in the Provision of Public Infrastructure*, there are two substantive criteria by which the Government will consider private participation in the financing of public infrastructure projects:

- a project must fulfil a community need, consistent with Government priorities; and
- private financial involvement must provide a net benefit to the taxpayer compared with public funding.

Procedurally, an open competitive process will be followed using a two stage tender process. In the first stage, proposals will be invited for delivering the project's objectives and then, assuming one or more proposals demonstrate a net benefit to the community, detailed tenders will be invited from up to three proponents.

In November 2000 the Government released a green paper on infrastructure provision<sup>14</sup>. This paper proposes a broadening of opportunities for public-private partnership, but the two substantive criteria remain.

## **Legislative Requirements**

Legislative requirements specific to infrastructure provision support the above planning processes. The main requirements are in the *Public Works Act (1912)* and the *Environmental Planning and Assessment Act (1979)*. Other general requirements are contained in the *Public Finance and Audit Act (1983)* and the *Public Authorities (Financial Arrangements) Act (1987)*.

The *Public Works Act (1912)* provides that projects over \$1m must be approved by Parliament and that the Public Works Committee of Parliament must review each project. The annual Budget process in which Parliament approves the proposed capital works program for the coming year effectively covers most of the requirements of this Act.

The *Environmental Planning and Assessment Act (1979)* provides the framework for the preparation and exhibition of Environmental Impact Statements (EISs). In the main, EISs are required for infrastructure and other large public capital works because the developing

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<sup>14</sup> NSW Government, "Working With Government: Private Financing of Infrastructure and Certain Government Services in NSW", 2000.



authority is not required to seek development consent via the processes which apply to the private sector. The scope of an EIS should cover both environmental and community impacts, and whether the proposed project will best fulfil the identified community needs<sup>15</sup>.

### **How did the Parramatta Rail Link project comply with this framework?**

The Committee's assessment is that the Government's strategic planning framework was, by and large, fulfilled in the case of the Parramatta Rail Link. This is demonstrated by the inclusion of the project in the overarching strategy *Action for Transport 2010* and provision of the estimated cost in the forward Budget estimates. Further, prior to its being considered by the Budget Committee and included in *Action for Transport 2010*, an extensive process had been undertaken to evaluate the project and its alternatives, as demonstrated by the Parramatta Rail Link Project Director in the Hearing:

**Mr KATZ**<sup>16</sup>: ... The immediate priority, or the immediate strategic reason for proceeding with the Parramatta Rail Link is to satisfy the demand on the main western line out of Sydney. That main western line will reach capacity in about 2006 and it was felt that we need to do something so that the gradually increasing demand can be satisfied. We are also responding to needs for improved public transport in the north-west sector and better utilisation of the existing rolling stock and track. We are also complying with other government documents and government policies such as the *Shaping Our Cities*, *Action for Air* and *Action for Transport 2010*. We did look at a lot of other alternatives.

Over the years a lot of studies have been done. The pre-EIS studies included looking at 66 different options, and they covered a lot of different routes, different modes of transport—light rail, heavy rail, busways, duplication of existing rail line and a whole lot of different routes. They were then short-listed down to 12 different options. After that we called for the private sector and the public to come up with alternatives, and we got 52 different submissions. They were then reviewed and short-listed down to four. The two lots were put together and then again assessed, and the final selected route was the Parramatta Rail Link as it now stands.

**CHAIR**: What were the criteria that were used to evaluate the different alternatives?

**Mr KATZ**: We looked at a whole series of different criteria, and those criteria obviously change as you go through the process. They included things such as looking at maximising public transport access, linking patronage generators so we are likely to increase public transport use. We are trying to provide an integrated transport system so that it links up with the rest of the transport system, improving regional and environmental air quality. We are looking at minimising the land resumptions, and obviously there are things like heritage that are taken into account. Indigenous and non-indigenous heritage all have to be considered.

<sup>15</sup> Department of Urban Affairs and Planning, *"Is an EIS required?"*, *Best Practice Guidelines for Part 5 of the Environmental Planning and Assessment Act 1979*, 1999.

<sup>16</sup> Mr Joseph Tripodi, Chairman and Mr Peter Katz, Parramatta Rail Link Project Director, transcript of Hearings, page 31.





The Department of Transport explained how it tried to improve the planning processes for the Parramatta Rail Link:

**MR ROBINSON<sup>17</sup>:** In terms of the planning process, we have tried to do things on this project in a lot more detail and with a lot more planning than arguably some previous projects. For example, a financial appraisal of the project was done by the Rail Access Corporation in about 1997. That was before the EIS was committed to by the Government.

When the EIS was being progressed, we went out and got some more work done. We talked to the industry, we talked to other jurisdictions about what worked and what did not, and we have tried to keep the economics and the financials, which are two different things, for the project continually under review.

That is one issue. We were keen, I suppose, in terms of the planning approval, not to have the tender process finish before the planning approval because we do not want to have a single private tenderer locked in and have to negotiate changes in scope.

However, a vexed issue is the timing of consultation with proponents of the various options and how it relates to wider consultation with the community through the EIS process. This is considered below under Issues Raised in Submissions and Hearings.

The Parramatta Rail Link *Invitation* document opens the way for proponents to offer solutions involving full or partial private finance. However, it specifies that it is not the first stage of a two stage tender process as envisaged in the Government's *Guidelines for Private Sector Participation in the Provision of Public Infrastructure*. The Committee asked the Parramatta Rail Link Project Director why that was the case:

**Mr KATZ<sup>18</sup>:** Basically, because we did not see it as being the first stage. We did not want to lead the private sector on by saying we would move in the private sector approach. That is why we left it wide open. In fact, I think the Invitation document says that we may proceed in any number of different ways. If somebody came up with an absolutely brilliant scheme that had huge intellectual property, we would have negotiated with them. If the project fell off the rails, we would not proceed with anything. We basically said we were not sure which way we would go; we would look at the alternatives as they came in and then decide which way to go. With the private sector, it is best to give them some guidelines on which way to go. That way we will reduce their costs and give them some direction in which they can aim.

These issues were the subject of comment in the submissions, and are further discussed below.

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<sup>17</sup> Mr Ian Glachan, Committee Member and Mr Ian Robinson, Department of Transport, transcript of Hearings, page 35.

<sup>18</sup> Mr Richard Torbay, Committee Member and Mr Peter Katz, Parramatta Rail Link, transcript of Hearings, page 38.



## Chapter 3

### **Parramatta Rail Link: Issues raised in submissions and Hearings**

We now turn to an evaluation of the issues raised in submissions to the Inquiry, interviews conducted by the Committee, and evidence obtained in the November 2000 Hearing.

Submissions on the Parramatta Rail Link have raised four major concerns:

1. the timing of Budget funding extends the project construction period beyond the optimum, (defined as the most cost efficient construction schedule);
2. although the *Invitation* allowed for alternative proposals, it was biased toward separate design and construct packages;
3. the criteria for evaluating the proposals may be too narrow to accommodate private sector financial involvement and thereby deny the benefits arising; and
4. construction interface risk had not been adequately assessed by the Government.

Further issues raised in the Hearings were:

1. the difficulty of evaluating risk transfer;
2. the need to augment the public sector skill base;
3. the advantages of an 'outcomes-based' tendering process; and
4. the need for protection of proponents' intellectual property.

Each of these concerns is now illustrated and then evaluated with reference to Government documentation, evidence from the Hearings, and interviews with the Project Director. Some of this documentation was confidential to Government and hence the concerns of parties submitting proposals may have arisen from the limited information available to them.

## **PRE TENDER PLANNING**

### **Outcomes-based tendering**

In its recent study tour, Committee members heard that overseas jurisdictions are developing an approach of 'outcomes-based tendering'. In its broadest sense, the Government would request proponents to submit ideas which meet the broad objectives of a project before defining it in any detail. Outcomes-based tendering can also be applied at the stage of calling for registrations of interest for a defined project, and the Committee supports this approach. (Recommendation 2, page 20).



The broader concept was explored in the Hearings:

**Mr COLLIER**<sup>19</sup>: One of the things we came across in our study-tour overseas when looking at public private partnerships was this concept, that rather than have a situation where you say we want to build a rail link from here to Chatswood to Parramatta, the process that seemed to be gaining a lot of favour was say, "We want to move people from Parramatta to Chatswood. What is the best way of doing it?" Do we do that in New South Wales? It could be a bridge, a walkway, a tunnel, a road, whatever.

**Mr OXENBOULD**: I think that is something we are trying to encourage now. So we define the outcomes that we want and I think that is a better way to engage the innovations available within the private sector. So if it is that you want to move this mass of people from Parramatta to the northern beaches or whatever, then put it to the private sector to come forward with a series of alternatives of how that could best be done, and then make judgments on value for money.

**Mr COLLIER**: That was the issue, encouraging innovation and appropriate intellectual property, but are we actually doing that in New South Wales now to your knowledge?

**Mr OXENBOULD**: ... a lot of these issues are under consideration and are part of the Government's public discussion paper that is being launched next week. That is certainly being canvassed.

However, there are difficulties with outcomes-based tendering in this broad sense. The Committee questioned Treasury in the Hearing:

**Mr GRAHAM**<sup>20</sup>: One of the issues there is obviously the raising of how does the private sector provide innovation, ideas and new ways of doing things. I do not know that there is a right answer at any point in time. There are issues that go beyond purely seeking innovation that may be driving the outcome of the project, such as environmental concerns, et cetera, whereby there are certain conditions imposed upon it, and you are tending to lock yourself into a particular outcome because of some of those constraints.

Ideally, one would like to embrace the private sector in terms of their ideas as early as possible without necessarily compromising some of these other factors that government has to take into account. I take the example of environmental planning issues. It is a very complex one because sooner or later major projects confront an EIS process. If we embark upon the EIS process too early, then the private sector responds, "We didn't have a chance to put in our ideas. We didn't have a chance to change the concept." Consequently, do we do the EIS early or late? If we do it too late and are locked in with one bidder and there are major changes and major development

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<sup>19</sup> Mr Barry Collier, Committee Member and Mr Chris Oxenbould, Premier's Department, transcript of Hearings, page 23.

<sup>20</sup> Ms Katrina Hodgkinson, Committee Member and Mr Danny Graham, Treasury, transcript of Hearings, page 20.



approval paths that are changed, then we are locked into the dilemma: how do we get the right price, the value for money from these changes?

It would be better if you had an ability to scan some of those types of concepts earlier to get a refinement of the environmental parameters, getting private sector involvement without necessarily locking them in and without necessarily locking in the Government. It is a difficult trade-off because the private sector does not want to give you too much information too early because it may have expended its competitive advantage over its opponents..., but from the Government's point of view we are looking for certainty of outcome in both price and quality, and there is a bit of a trade-off there ...

...for complex projects like major roads, railways, et cetera, you have got quite a lengthy planning environmental approval stage and development approval stage where both sides are looking for certainty of outcome so that they know the price they are giving is the amount the project is going to cost in the end.

**Ms HODGKINSON:** That is along the road I was thinking and trying to get an answer if you think it is best before the EIS or after the EIS or whatever, but what you are saying is that it depends on the project.

**Mr GRAHAM:** ... the experience we have had is that we have tried it before, after and in the wrong place sometimes. I cannot say that we have necessarily found the correct answer for the current way that the Environmental Planning and Assessment Act is structured and the current way you have to run the process. We have been canvassing a sort of strategic-type assessment framework to clear that first before you get into a detailed corridor analysis, because with the EIS you are canvassing quite a range of issues that have to be debated in the public forum. The EIS might be a road project but you are also canvassing objections: Why is it not a rail project? Why is it not a light rail project? Why is it not a transitway? Now, those things have been considered and dismissed for various reasons but in the EIS you have to open that up to debate again. If we could have that debate earlier and you are concentrating on doing a road, a railway, this type of project, then a lot of that debate does not have to be undertaken during the EIS process. At the moment, the EIS process itself is resulting in a lot of debate about strategic planning, the role of strategic planning and what the Government should be doing strategically investing in this sector, that or some other component.

The Government's Green Paper on Infrastructure recommends that the timing of the EIS be managed on a project by project basis, and the Committee concurs with that.



## Intellectual property

Another concern of the Committee is a lack of protection for intellectual property which can lead proponents to be reluctant to propose ideas.

**MR GLACHAN**<sup>21</sup>: ... If the Government bought the idea from [a proponent], then at least they get paid for what they have done. ... The Government can then go out freely to tender and accept whatever is the best tender from the Government's point of view because it now owns that intellectual property. It does not owe anybody anything.

**Mr GRAHAM**: I understand the principle and from a principle point of view it seems a fair and reasonable approach.

**Mr GLACHAN**: Why do you not do it?

**Mr GRAHAM**: In circumstances that have been produced to us to date in terms of large projects, it has been very difficult to identify precisely what is intellectual property. It is more of the case of, "I want to direct treat. I do not want to sell you the product. I want the final big deal". I can see from your perspective in terms of specialist technologies, specialist ideas, and in those cases, obviously, there could be a case made. We would need from a Treasury perspective to see that costs and benefits were actually attributed, that an expert technical analysis has been undertaken, that truly this is a unique arrangement and the Government by purchasing this will actually end up in the end product getting better value for money from delivery of the government service.

**CHAIR**<sup>22</sup>: But there is no facility for that to occur at the moment...

**Mr OXENBOULD**: But regulations have changed a lot since those days, with the national competition policy—

**CHAIR**: Hilmer reforms have not extended to the bureaucracy's control over large sections of economic activity... There is no gateway, really, for people to contest the dominance that government has in service delivery and they have no payment for those ideas either. ... it is very important to this whole concept of how do we get value for money. It is crucial.

Again, the Committee notes that the Government's Green Paper on Infrastructure addresses this issue. The objective is to protect intellectual property rights in cases where competitive tendering is to occur (the default unless Budget Committee decides that the intellectual property is of such significance and benefit to the public interest that market testing is not warranted)<sup>23</sup>. The Committee supports this approach and believes that an extra incentive to innovation can be provided.

<sup>21</sup> Mr Ian Glachan, Committee Member and Mr Danny Graham, Treasury, transcript of Hearings, page 23.

<sup>22</sup> Mr Joseph Tripodi, Chairman and Mr Chris Oxenbould, Premier's Department, transcript of Hearings page 24.

<sup>23</sup> NSW Government, *Working With Government: Private Financing of Infrastructure and Certain Government Services in NSW*, 2000, page 45.

**Recommendation 1**

When proponents of infrastructure proposals offer intellectual property involving specialist technologies etc., that are innovative and beneficial, the Government's initial approach should be to manage the tender so that it can capture the intellectual property without disadvantaging its owner. When this cannot occur the Government should consider purchasing the intellectual property for use by all the parties involved in the tender.

The Committee heard that the Parramatta Rail Link Project had used the first approach:

**Mr KATZ<sup>24</sup>:** There are two options.

- One, we could pay them for the intellectual property, which has certainly been considered.
- The second one would be to say, for example, "Okay, a slightly different tunnel route between A and B." What we would do then is call a tender to build the tunnel between A and B and let them put in the competitive bid at the tender time, so we would actually broaden that tender document so that they could actually submit their tender bid.

One of the reasons for going out at this stage with our ROIs and alternatives was that we could actually assess these things in a confidential way. When they did it—18 months, two years ago now—it was not confidential, so everyone's ideas were open to everybody, but this allowed the tenderers to put in the ideas confidentially. We would then try to address them in one of those different ways. The preferable way is actually just to modify the tender method so that they can use their intellectual property later.

The approach adopted, of seeking ideas through the tender process, again affirms the benefits of an outcomes-based approach and provides an alternative to purchasing intellectual property if it were hard to define or value, or if there were numerous potentially worthy ideas.

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<sup>24</sup> Mr Ian Glachan, Committee Member and Mr Peter Katz, Parramatta Rail Link, transcript of Hearings page 38.



## Costing of projects

Budgeted capital costs evolve with the scope of a project as it emerges from consultative processes with the public, other agencies and consent authorities. The Committee heard evidence that there may be a significant increase in cost<sup>25</sup>. The Parramatta Rail Link project has increased significantly in cost from \$400m (for a Parramatta-Hornsby link) when it was first announced in 1994<sup>26</sup> to \$1.4 billion in 1998 (and a higher amount in late 2000). This increase can be attributed partly to an escalation in Sydney's general construction costs and the considerable changes in the scope of the project.

These increases in the scope and cost of the project demonstrate the need for continual strategic evaluation of whether a project ranks above other options. However, this is difficult as a project often builds momentum once in the public arena and becomes virtually unstoppable, even if large cost escalations would give it a lower ranking than others. Therefore, Governments should be hesitant to publish projected costs for a project until the project's final form is known definitively. Alternatively, it could publish a range of costs.

In their evidence before the Hearings, parties affirmed that any project with a benefit-cost ratio of less than one should not proceed and that they would so advise the Government<sup>27</sup>. The Department of Transport advised that the project continues to provide an economic benefit to the community, because the benefits had increased commensurately with the costs. The Department will provide this evaluation to the Government for its next decision on whether the project should proceed, and if so, what its structure should be. Regardless of the large increase in cost, it is the Government's prerogative to approve the scope of a project and its associated cost and the Committee accepts the Department's bona fides in keeping the Government informed.

## THE TENDER PROCESS

### Project structure in the Invitation document

A concern was that the *Invitation* was structured in favour of separate contract packages, rather than encouraging proposals for one contractor to supervise the whole project.

AusCID's submission stated:

... the EOI process itself mitigated against optimising taxpayer value. Supporting material for the EOI Process focused on the detail associated with the proposed 14 parcels of subsidiary contracts. Although the documentation briefly addressed the opportunity also to submit non-complying tenders, the weight of material in support of the subsidiary contract approach necessarily promoted responses based on that approach.

<sup>25</sup> Transcript of Hearings, page 17.

<sup>26</sup> Bruce Baird, Transport Minister press release 12 December 1994.

<sup>27</sup> Transcript of Hearings, page 35.



Consequently the submitting parties were more likely to focus on these contract opportunities and to limit any effort involved in producing alternative proposals given the high cost associated with bidding processes. There is also a natural tendency to second-guess governmental and bureaucratic responses to bids and hence an inclination to deliver options more likely to meet with bureaucratic acceptance. Thus the EOI process itself has denied the Government an opportunity to assess objectively all value alternatives. Instead it has, to some extent, prejudged outcomes.<sup>28</sup>

The Committee is not convinced that the process unduly restricted either the number or the substance of alternative submissions. Several of the alternative proposals were for the entire rail link and at least one was for the Epping-Chatswood link. The Committee considers there is a healthy balance between the individual packages (with at least six proposals per contract package) and alternatives for all or part of the rail link.

The Parramatta Rail Link Project Director advised the Committee that the specifications for the 11 contract packages provide the building blocks for any alternative proposal. Therefore, any party making both conforming ROIs and alternative proposals would have a minimum of extra effort<sup>29</sup>. It would also seem difficult for both bidder and evaluator if there were not some level of detail in the specifications.

The *Invitation* may even be seen as being more accommodating of alternatives than might have been the case. The Government's initial report on the proposed tendering process stated that:

... the Project is best suited to be delivered as a DC&M [design, construct and maintain]<sup>30</sup>.

The *Invitation* document went beyond these recommendations and sought alternatives in the broadest terms, within the outcome parameters established by the Environmental Impact Statement and Government policy (major route nodes, finance restrictions).

Further, not all submissions were of the view that the *Invitation* was unduly restrictive. The submission of the Parramatta Chatswood Consortium concludes<sup>31</sup>:

We believe that by choosing these [three] alternatives we have covered a broad range of delivery mechanisms for projects of this type. The alternatives differentiate in the way how value for money is maximised and efficiencies and effectiveness of infrastructure transactions are improved.

<sup>28</sup> AusCID, second submission to the Inquiry, pages 1-2.

<sup>29</sup> Meeting of PAC Chairman and Secretariat with PRL Project Director, 9 October 2000.

<sup>30</sup> Arthur Andersen Corporate Finance, "*Report on the Proposed Tendering Process, Parramatta Rail Link Project*" NSW Department of Transport, March 1999, pages 4, 6.

<sup>31</sup> Parramatta Chatswood Consortium submission to the Inquiry, page 3.





The Committee's conclusion is that once the policy and environmental parameters have been established, there is a tension in specifying the tender between providing guidance on the preferred outcome (e.g. route alignment, preferred structure is Design, Construct and Maintain) and not providing such guidance.

- In the first instance, parties may feel discouraged from offering solutions which potentially provide the best value for money.
- In the second, they may be left wondering what the Government is seeking.

Parramatta Rail Link's approach strikes a balance by providing detail on the project and allowing parties to submit alternatives which meet the fundamental objectives and constraints. This would appear a worthy approach for future projects of any size.

### **Recommendation 2**

The approach followed in the Parramatta Rail Link should be continued in future Invitations for Registrations of Interest and Alternative Proposals:

- the project should be defined by outcome and performance subject to Government policy and processes (especially the Environmental Impact Statement); and
- future Invitations for large projects should be structured as a dual Invitation for (a) Conforming Packages and (b) Alternative Proposals.

### **Mismatch between optimal construction period and Budget funding**

On the basis of information contained within the Environmental Impact Statement, Macquarie Bank believed that Budget restrictions would require the project to be spread over a six year construction period. It argued that if the construction period were reduced to four years, a nominal cost saving of some \$234 million would eventuate<sup>32</sup>.

An examination of the *Invitation for Registrations of Interest and Submission of Alternative Proposals* (the *Invitation*)<sup>33</sup> established that alternative proposals were welcomed and that there was flexibility in both the content of the proposals (technical only, financing only, operations and maintenance or a combination) and the information to be provided.

Staff of the Committee met with the Bank and established that it had, as part of a consortium, submitted its proposals for consideration. The Committee is therefore satisfied this issue has been addressed in the selection process, and this has been confirmed by staff of the Bank<sup>34</sup>.

<sup>32</sup> Macquarie Bank, first submission to the Inquiry, page

<sup>33</sup> Invitation for Registrations of Interest and Submission of Alternative Proposals, Part 2, Schedule C.

<sup>34</sup> Meeting of Macquarie Bank and PAC Secretariat staff, 21 August 2000.



The general issue of budget constraints was raised in the Hearing:

**CHAIR**<sup>35</sup>: This is an issue more for Treasury than yourselves, but what can be done to ensure that the budget allocations made by Treasury and the Treasurer are such that they will fall into line with a construction schedule that minimises the present value of total costs, that is, if the construction cycle is optimal so as to ensure that the cost is minimised? Has this been a problem? ...

**Mr COLLINS**: The answer is obvious that not everything is optimised, and clearly Treasury is going to have to answer some of that, but I do not believe the top of their priority tree is to get those sorts of issues optimised when they make their decisions. Clearly, there are a whole lot of issues about agency requirements that also cut across the point you are making that agencies' different requirements met in various ways may not lead to optimisation of some of these issues either. ...

**CHAIR**: To take as a further example the Pacific Highway, the fact that it is allocated \$200 million a year may not be the best way to fund the whole project over five years.

**Mr COLLINS**: It may well not be. You are quite right. Clearly it might not be.

**CHAIR**: Do you know of other agencies that often clash with Treasury on this matter?

**Mr SMITHIES**: I do not think it is a case necessarily of clashing with Treasury. I will give you a case study example. A few years ago when we were arranging or project managing the construction of Rankin Park Hospital. The contractor... came up with quite an innovative solution in terms of how he was going to build it. Rather than a 30-storey hospital, the design was a long, low-rise hospital.

Basically, he built the car park first. He got all his site organised with the car park to the point that when he built the first floor he could just ramp up and drive up into the first floor. Can you imagine the efficiencies? The project went at 100 miles an hour, much quicker than we had even thought it was going to go. We were caught with a real cash flow problem because of the rate he was going at. All the sorts of information we had given Treasury caused stress, because we were actually trying to hold the project back to match the cash flow. In that sense, that was innovation on the part of the private sector in how they developed this.

**Mr GLACHAN**<sup>36</sup>: Not met by your financial arrangements.

**Mr SMITHIES**: Not met by the cash flow arrangements that had been put in place. That was just because of sheer innovation on the part of the contractor. I think those problems will exist no matter how well you have the system sorted out.

**Mr GLACHAN**: You want innovation in financing.

<sup>35</sup> Mr Joe Tripodi, Chairman, and Mr Tony Collins, Mr Ted Smithies and Mr Norm Johnston, Department of Public Works and Services, transcript of Hearings, page 13.

<sup>36</sup> Mr Ian Glachan, Committee Member.



**Mr JOHNSTON:** That is budget driven....

In theory, the existing Budget process should already provide for the cash flow associated with the lowest net cost option. Agencies are required to advise the Budget Committee of Cabinet of the option with highest net present value (NPV) or, if the scale of the projects were not comparable, NPV per dollar of capital invested, as well as a range of other indicators<sup>37</sup>. However the Committee believes there is sufficient evidence that Budget funding restrictions have caused suboptimal project construction periods to warrant a review of the cost impacts and what could be done to prevent them.

### **Recommendation 3**

Treasury should commission an independent review of the extent and cost implications of suboptimal project construction periods resulting from restrictions in Budget allocations, and make recommendations to prevent this in the future. This review should be provided to the Treasurer, and should involve major line agencies such as the Departments of Education, Health, and Transport, as well as the Department of Public Works and Services.

### **Changes to patronage projections**

Another issue was that projected passenger numbers were revised upwards only days before the closing of the *Invitation* (the lower numbers being a disincentive to private finance solutions)<sup>38</sup>. Two questions arise from this.

- ❖ **Did the late revisions to passenger numbers detract from the quality of the ROI?** The Committee notes that the *Invitation* is expressed in relatively general terms because its objective is to choose several parties for a detailed tender. The *Invitation* sought no financial information, and it would seem that the short notice was not an undue hindrance in meeting its requirements. (Not having access to the proposals themselves, the Committee is unable to test this assumption).
- ❖ **Did the short notice unfairly affect the ROI relative to other bidders?** All parties were in the same situation and hence all were affected equally.

Good management requires that parties are provided with updates in key information, as occurred in the Parramatta Rail Link, and that they have sufficient time to digest the information.

<sup>37</sup> *Financial Appraisal Guidelines*, NSW Treasury Policy & Guidelines Paper TPP 97-4, July 1997.

<sup>38</sup> Macquarie Bank, second submission to the Inquiry, page 2.

**Recommendation 4**

As occurred in the Parramatta Rail Link project, any updates in key information should be provided to interested parties for use in preparing their Registrations of Interest and Alternative Proposals. Sufficient time should be given to proponents after changes to key information in the Invitation. However, these changes should be kept to a minimum.

**Possibility that selection criteria may preclude private involvement**

Three of the four submissions responding to the Committee's separate advertisement outlined their proposals under the *Invitation* for private sector construction and funding. Some were concerned that their proposals would not be seen as meritorious by the Government, and all provided arguments to advocate the benefits of their proposal.

It is not possible for the Committee to judge the relative merit of the proposals nor appropriate for it to comment on this aspect. It is inevitable that only a few of the proposals will be selected for the detailed tender stage. However, it is possible to evaluate whether and how the issues are covered in Government documentation for the project and that will provide an indication of whether the issues will be taken into consideration in any decision. Further, the procedural aspects of the *Invitation* can be examined to establish whether a robust process is being followed. The following discussion addresses the issues raised on a thematic basis.

**Benefits of private financing excluded**

Several parties argued that private financing would provide the greatest benefits to the Government. One party suggested a shadow toll arrangement, and another was concerned that the restrictions on shadow tolls and the like prevented private finance solutions<sup>39</sup>.

A 'shadow toll' is a payment by the Government on a per vehicle or per passenger basis, instead of or in addition to any direct payment by the consumer. Shadow tolls have been used in other jurisdictions, e.g. the UK. However accounting and legal restrictions differ in each jurisdiction and so also would the circumstances in which shadow tolls would be appropriate. There has also been an evolution in the basis on which shadow tolls are paid to align incentives to the operators (e.g. to be consistent with public transport and clean air goals).

Given these developments in other jurisdictions, there may be an advantage in defining more clearly the circumstances when shadow tolls could be considered.

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<sup>39</sup> Submissions by project proponents to the Inquiry.

**Recommendation 5**

The Government should continue to reserve its prerogative to choose how to finance any project. However, it should define its policy on shadow tolls as a means of financing infrastructure. If there are certain types of projects where shadow tolls could be considered, or where they will not be, this should be spelt out with supporting reasons.

A different view was put by the International Association of Public Transport (Australia/New Zealand):

The Parramatta Rail Link has a number of characteristics that make it suitable for the currently envisaged Government funding model ... [these] suggest that all the benefits cannot be collected by the fare box, and indeed if they were, would create inequities between transport provision for eastern and western Sydney ... Efforts for private sector innovation can be sought in contracting to design and build the link<sup>40</sup>.

The range of views expressed indicates confusion on the part of proponents on what would be acceptable financing mechanisms. Procedurally, it would seem good practice to refer to Government policy as a context for restrictions on private finance to assist interested parties in preparing their proposals.

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<sup>40</sup> International Association of Public Transport (Australia/New Zealand), submission to the Inquiry, pages 1 and 2.



To review whether the Government had taken the issues of substance into account, the Committee turned to the March 1999 report of Arthur Andersen Corporate Finance on the structuring of the project. The following extensive excerpts are provided because they illustrate the complexities in the project economics:

The economics of the Parramatta Rail Link are such that a government subsidy would have to be paid to the private sector since insufficient revenues would be generated by the project itself. A full user-pays approach for passengers would not be viable.

The Parramatta Rail Link does not lend itself to differential pricing in the way proposed for the Airport link and the [possible] Bondi Beach Rail extension. If a “user-pays” principle cannot be applied, the privately owned service would require cross-subsidies from the publicly-owned service.

In effect the government subsidy would be paying a return to private sector equity and debt, but for a project where patronage or demand risk effectively remained with government [because the private sector is unlikely to be willing to accept these risks].

Subsidising private sector involvement would be an inefficient use of public funds and against the stated policy and principles of the State.

A justification may exist if the private sector can demonstrate the marginal difference in private financing over state financing delivers greater savings in construction and operating cost.

However the project can be tendered under a competitive D&C [design and construct] process, with full D&C risks being passed to the private sector. It is highly unlikely that a privately financed project could deliver the D&C element for a sufficiently lower cost to compensate for the higher private sector finance cost.

It also seems unlikely that a private operative could operate that section of the network, at less than 30 kms in length, at a cost sufficiently lower than the RAC and SRA, to justify the added cost of private finance.

Private funding and ownership of stations would be subject to the same issues stated above; namely, access charges set to generate a market return would not be competitive with alternate (sic) forms of transport. Subsidies would be required to achieve financial viability.

... there appears to be no reason to exempt the private sector from being involved in most aspects of the construction and delivery. Aspects could include tunnelling, track laying, signalling, maintenance and elements of ongoing operation and interim financing.

Proposals suggesting that the private sector is better placed to capitalise upon the property development potential of stations and hence provide an efficient financing solution have merit for some of the stations, but not all. These opportunities are relatively small in relation to the financial cost of the whole Project.



..... tax benefits for the project are unlikely to be material ... since the patronage risk would effectively remain with the State.. the Project would be deemed to be controlled by the Government. ...

One option does remain ... which is to seek ... tax relief based on the Infrastructure Bond scheme. However, given the size of the project the relief would have to be for a significant value to make private finance more competitive than State originated funds<sup>41</sup>.

The issue of whether and in what ways private finance should be used was also discussed extensively at the Hearings.

**Mr GLACHAN<sup>42</sup>:** ... there is a whole range of things the Government has to do for the benefit of the community. If you talk about roads, for instance, and toll roads, they have to be built all over the State. For some of those roads the Government just has to find the money and build them—there is no other way to get them done—particularly, say, in country areas, but in the city, where there is a high volume of traffic, the Government can pass that responsibility over to the private sector and allow it to charge a toll so that the people actually using the road pay for the benefit. Doing that frees up government money then to build roads in other places where there is no other way of paying for them. My view is that although the Government might take a risk to some extent in having a private company build that toll road, the risk is well worthwhile because it is using private money to build something the Government needs to provide and that frees up government money to build some other project that the Government needs to provide. So I see that sometimes, although there might be a risk involved, the risk is worth taking to get that benefit. What do you think of that?

**Mr SENDT:** I think, Mr Glachan, that assumes there is some restriction on government funding. I do not think there really is. The Government can raise any amount of funding it requires at a moment's notice. I think the restriction is when governments impose upon themselves budget or financial targets that will not allow for major projects. Off-balance sheet deals are then the way around that self-imposed or other form of restriction.

**Mr GLACHAN:** But good financial management would surely mean that you do not just go and borrow without any control or without any limits. Surely good financial managers have to borrow only a certain amount of money.

**Mr SENDT:** True. But in entering into these arrangements, the Government is accepting some degree of liability that at the end of the day may turn out to be just as expensive, if not more so, than having borrowed the money in the first place.

**Mr GLACHAN:** But my point is that maybe the risk is worth it because you free up the money to invest somewhere else. Your view is that you are better to borrow it anyway?

<sup>41</sup> Arthur Andersen, op. cit. pages 30-32.

<sup>42</sup> Mr Ian Glachan, Committee Member and Mr Robert Sendt, Auditor-General, transcript of Hearings page 3.



**Mr SENDT:** Unless there is some specific advantage in having the private sector involved. If it can manage the risks better, if it can bring expertise in respect of project management to the particular project, that is when you want to look to the private sector, but I think that clear delineation of why a particular project is undertaken by the private sector in arrangement with the Government is not always made up-front.

In the Audit Office we undertake a review of the contract summaries that are prepared, but that is an ex-post event. Project summaries are not required to be tabled in Parliament until within 90 days of signing but by that stage, regardless of what we show in our report, it is too late.

Limitations on private finance arising from the nature of the Parramatta Rail Link project were explained by the Department of Transport:

**MR ROBINSON<sup>43</sup>:** We have started, in this process, by trying to be clear as to what the financial position of the project is, and you said it is going to be largely government funded. That is what our view is. It is not all that hard to look at what the patronage is on the line, what the average fare is in Sydney and what is able to be funded. So we have started from that perspective.

It is not a negative view about what the private sector can do. We have tried to be realistic because we did not want to start from a perspective that just continually slipped. That is, hopefully all private sector funded and then have it deteriorate. We think because of the nature of the project, it is wholly integrated with the CityRail network and, for its length, relatively few new stations and in areas that are in Sydney, not for example the airport or a specific destination. The fact of the matter is there is relatively little potential new revenue in it. It is a project that is mostly about the capacity of the whole Sydney rail system, including particularly the west and south west of Sydney. ... we tried to be realistic because we did not want to put an advertisement in the paper that created expectations and wasted everyone's time.

**MR KATZ:** It was felt that the restriction on private sector funding would give the best result because the Government was looking for new ways of getting in finance to pay for this. A shadow tolling arrangement was really just a deferring of cost. We really wanted to see if we could find some new ways of generating income to pay for it, for some real smarts to be shown, not just us pay for every train that goes through, which we thought of, obviously, a long time ago, and we did not see the benefit of reopening that debate.

Given this discussion, the Committee questions whether private finance options should have been invited at all, but is aware that if such a restriction had been placed it is likely that criticism would also have been directed at the Government. The complexity of the issues means that there is no easy answer, it remains an issue of policy and judgement by the Government.

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<sup>43</sup> Mr Ian Robinson, Department of Transport and Mr Peter Katz, Parramatta Rail Link, transcript of Hearings, page 40.





The main procedural issue is whether there was sufficient information for bidders to plan their approach with the greatest potential for success. The Committee notes that the EIS contained information on both costs and revenues (and projected passenger numbers). If this had been explicitly referred to in the *Invitation* along with other relevant sections it may have assisted parties.

## Value for money

Both Macquarie Bank<sup>44</sup> and AusCID<sup>45</sup> explored the concept of ‘value for money’. Macquarie Bank stated:

... the concept of value for money must consider:

- ❖ Whole of life costs and revenues associated with the project – it is the total value delivered over the whole of the project life. Any analysis of value for money should therefore include:
  - all costs incurred during construction including for a private sector funded delivery any costs relating to finance during construction, design and raising of debt, or in the case of a Government funded solution, an appropriate cost of capital and design and management costs;
  - total revenues less all operating costs throughout the project life, recognising that different delivery solutions will have different impacts for ongoing costs, patronage and other revenues. In particular a private sector funded solution may have higher construction costs but this could be offset by lower operating and maintenance cost, as well as higher revenues; and
  - any residual value at the end of the project concession, recognising that the value of the business at that point reflects its locked in revenues at that point in time; and
- ❖ Value of risk transferred from Government to the private sector needs to include:
  - an assessment of the likelihood of a particular risk occurring;
  - the extent to which that risk constitutes an exposure; and
  - the premium that needs to be paid to a third party to divest that risk.

In relation to whole of life revenues and costs, the definitions provided by the Bank are in accord with the Government’s *Financial Appraisal Guidelines* which compare whole of life benefits of all options and therefore permit fair comparisons. A whole of life approach is also used by the Department of Public Works and Services when it assists agencies in infrastructure procurement.<sup>46</sup>

As the Bank notes, the issue of risk is complex because both the likelihood and the impact of the risk are difficult to assess, as is therefore the fair value of a premium for its transfer. The Bank argues [this] “has not traditionally been an area in which Government has developed significant expertise. As a result Government may not be in a position to accurately identify and evaluate the benefits of transferring a risk”<sup>47</sup> (and the Committee would note, the costs).

<sup>44</sup> Macquarie Bank, second submission to the Inquiry, page 3.

<sup>45</sup> AusCID, second submission to the Inquiry, pages 3-4.

<sup>46</sup> Transcript of Hearings, page 10.

<sup>47</sup> Macquarie Bank, second submission to the Inquiry, page 3.



The Committee is in agreement with this as a general proposition, taking account of experience of recent projects in New South Wales such as the Airport Rail Link. However, the **price** of transferring any risk is of fundamental importance, because if the premium is too high it may be beneficial to retain it inhouse. The fact that the Government has chosen to 'contract in' top level private sector advisers on these aspects gives the Committee some assurance that any transactions will be of mutual benefit to both parties and not at an unfair premium.

## Interface risk

Another concern was that the Government may choose separate contractors for the nominated contract packages, thereby imposing an 'interface risk' on itself arising from construction complexities and possibilities of construction cost and time overruns. These risks arise from economies of scale in construction (one set of tunnelling equipment can do all the tunnels), tricky interface between track electrical and signalling equipment in different sections of the line, and the 'domino' effect that if one contractor is running late, it delays the whole project.

The main example cited of interface risk was the UK Jubilee line which had a cost overrun of more than £1 billion and a delay in delivery of 20 months. There were also successful experiences with multiple packages, with Hong Kong cited as an example. The elements of this success were a longstanding inhouse design team which undertook about 30 per cent of the design work prior to the contract being awarded.<sup>48</sup>

At issue is whether there are benefits in transferring interface risk, and if so, how it should be priced. One experienced party maintains that on recent projects, there has been insufficient attention paid to the fundamentals of a project and an overemphasis on financial and legal aspects (with an associated increase in transaction costs)<sup>49</sup>.

The Committee questioned the Parramatta Rail Link Project Director about these concerns and was advised that the Project Team was cognisant of the risks and the issues of delivery and pricing:

**Mr KATZ<sup>50</sup>:** I actually had a copy of the Jubilee Line extension report by Arup, and I was just checking through it... . I was pleased to see when I read it that we had actually addressed at least 80 per cent of their recommendations already.

<sup>48</sup> Macquarie Bank, second submission to the Inquiry, page 5.

<sup>49</sup> Olympic Coordination Authority submission to the Inquiry, page 4.

<sup>50</sup> Mr Peter Katz, Parramatta Rail Link, transcript of Hearings, pages 36-37.



There are some very big differences. To my way of thinking, they made some very big fundamental mistakes. They contracted everything out in relatively small packages and split up the design along those packages. They had different designers without any lead agency and they had huge interface problems. For example, they had 17 electrical and mechanical contracts. In our conforming approach we have one. Very different. No wonder they had interface problems. At their stations they had separate contractors, separate designers for the structural, the electrical, the airconditioning, that sort of thing. Again, we have taken the approach where we have one lead designer who has to coordinate all those different things.

The bottom line is that we have also done a lot of analysis of this and some of the other more successful projects around the world and I guess we have come to a view about one way of delivering it, and that was the conforming approach that we put in our registration of interest [ROI] document. However, we want to take on board more comments from the private sector so we have asked for their comments, and we are reviewing that approach in the light of the comments that have been received. If we do proceed, I imagine we will reduce the number of contracts as a result of the comments.

I think if you read these reports you will see that we have actually addressed most of their issues. They ended up appointing Bechtel as a private sector overseer. Bechtel is a big American project management company. They ended up appointing it to oversee their project. I do not think we need to go there. I think we have the expertise in Australia and we have put together a very good team that can deliver this project.....

As I say, that decision [on single or multiple contracts] has not yet been made. It may well change. It depends on how the project gets delivered and the timing that we stage it. I can give you the reasoning behind the break-up in the conforming tender packages that we went out to registration of interest on. A couple of very important reasons. First of all, we are looking at getting the best value for money, and it was considered that we would get the best value for money if we made the thing very competitive, so we would get experts in tunnels, rail systems and building stations each to do their own thing effectively without paying the huge overheads that a single contractor would have. If we have a single contract, there are a very limited number of contractors in Australia who can tender for such a thing. It is a very big contract, bigger than anything I have seen in Australia.

The Melbourne City Link was smaller than this—but still a very large contract—but the bankers behind that insisted that the winning contractor actually subcontract out huge lumps of it under separate guarantees from the subcontractors. So, effectively, if we did it as one contractor, they would just package it up and send it out anyway and this would be a huge overhead. Another reason is that the experience from Melbourne City Link is that they had problems communicating with those subcontractors. Effectively, the head contractor became a mailbox and meetings became very complex because all correspondence went through a few different levels. We would like to avoid the sort of interface problem that can come if you have a single contractor.



There is also a problem about how quickly we could deliver this project because of the need to design the thing. We could not call tenders for a considerably longer time if we did it all in one contract. We can specify the tunnel design quite quickly and get that moving. In the meantime we can develop up the station. We are quite keen on getting the best possible station designed and we want to specify in a bit more detail what those stations will look like.

In addition to interface risks at the construction stage, there are also operational interface risks if the rail link were operated by a separate operator. The Committee is not aware whether any of the proposed BOOT, BOT etc. proposals include this as an element.

## IMPROVING THE PROCUREMENT PROCESS

### Risk transfer

Risk transfer emerged as the most difficult concept in the evaluation of private financial involvement in infrastructure. The Auditor-General was questioned in the Hearing:

**Mr TORBAY<sup>51</sup>:** On the subject of risks, we saw a little bit of this in a recent study tour. The private-public partnership really talks about risk and where that risk is going to lie. I was just interested to know has there been any inappropriate sharing of risks and are excessive premiums being paid for the transfer of risk?

**Mr SENDT:** Well, I am not sure whether we can provide any answer to the second question. On the first, I think quite often the risk assessment that takes place may assume that the private sector entity continues to operate and can continue to honour its obligations under the arrangement for risks that arise. Whether or not there is a contractual obligation for the private sector party to continue to meet obligations is one thing, but in reality, many of these projects become perceived by the public as a public sector project, as a government project. If the private sector entity were, for example, to become bankrupt, go into receivership or otherwise default, the risk will quite often fall for public policy reasons or revert to the Government.

The Government's Green Paper on Infrastructure proposes that in future, detailed tender bids will include the model used to price the tender.<sup>52</sup> This will allow the Government to assess the nature of the risks and the return which the proponents believe they will achieve – which is (as noted above by the Auditor General) presently impossible to judge. This is a prerequisite for greater public acceptance of private financial involvement in infrastructure and also for transparent and considered decisions.

<sup>51</sup> Mr Richard Torbay, Committee Member and Mr Robert Sendt, Auditor-General, transcript of Hearings, page 3.

<sup>52</sup> Working with Government, page 43.

**Recommendation 6**

The Government should require detailed tender bids to include the financial model used to price the tender, as proposed in its Green Paper “*Working with Government*”.

The Auditor-General continued that the State’s planning and approval processes do not necessarily ensure that projects have a net economic benefit to the community or a financial benefit to the State:

**Mr SENDT<sup>53</sup>:** Given some of the difficulties I have raised about the lack of time for central agency review of those projects, I think it would be difficult to say with a substantial degree of certainty that that is the case. Today’s newspaper article about the Airport Rail Link is a prime example of where the risk assignment might have been disclosed at the time. The implications if the private sector party to the arrangement were to get into financial difficulties were perhaps not sufficiently evaluated. I think that is more looking at the financial arrangements with State Rail than the net economic benefit to the overall community, but it certainly involves a transfer of costs from one sector to another—that is, from the shareholders to the taxpayers.

Treasury was also questioned:

**Mr TORBAY<sup>54</sup>:** ... I would be interested in your view as to what risks you would keep in the public sector and what risks you feel should appropriately be transferred?

**Mr GRAHAM:** I think the first principle is as Treasury and it is in our guidelines on private sector involvement, we have never espoused the transfer of all risks. We are realistic enough to accept that there are only certain risks that the private sector can control. If you try to transfer a risk that they cannot control and manage, they will try to price it and, consequently, you will pay the price. There are some risks that you cannot transfer, for instance, change in State laws. They will not accept that and you will have to take the risk... on the Government’s side, of changing State laws, for instance. A big issue is environmental planning risk. Who takes those risks?

I do not know that there is a clear-cut matrix where you can go down each risk and identify that the appropriate person is the private sector or the appropriate person is the Government. There are some that fall in that category. Design and construction—certain elements of that you can clearly transfer. But some of the other regulatory risk, operational risks fall into a grey area where there has to be a sharing, there has to be an agreement on it, and there has to be some kind of price put on the transfer one way or the other.

<sup>53</sup> Mr Robert Sendt, Auditor General, transcript of Hearings page 2.

<sup>54</sup> Mr Richard Torbay, Committee Member and Mr Danny Graham, Treasury, transcript of Hearings, page 24.



So although people talk about risk transfer and the ability to optimise it, it is not an easy topic. The easy ones are the ones that fall out first. The difficult ones are the ones that get caught up in a lot of complex legal frameworks whereby you are trying to allocate blame, accountability and risk transfer, where it is a difficult area. ... There is a point at which you are going to get optimal risk transfer, and that is what we try to achieve.

Even with access to the financial models of the proponents, the inherent difficulty in evaluating and contracting for risk transfer lends weight to the need for a solid skill base in the public sector.

### Public sector skill base

Sound decision making processes and criteria do not ensure good outcomes unless there is an expert skill base to evaluate value for money and risk. The Committee is of the view that the public sector's existing contract negotiation expertise needs improving and augmenting.

**CHAIR<sup>55</sup>:** Please give a brief summary of the major problems with previous privately funded infrastructure projects....

**Mr SENDT:** ... we have drawn attention to a number of difficulties... the major concerns we alluded to were inappropriate or lack of clear risk assignment in major projects between the public and various private sector parties and, more generally, what appeared to be, quite often, a lack of appropriate skills in the public sector, particularly in the area of contract negotiation.

The existing skill base may be also insufficient if there is an expansion of private involvement in infrastructure (for example through Private Financing Initiatives[PFI]):

**Mr SENDT<sup>56</sup>:** One of the difficulties [of more PFI type projects] may be that if these types of complex arrangements are fairly sporadic or infrequent, the public sector will not within itself build up the skills base. Individuals in the public sector will not build up the skills base. So, perhaps if you reach a critical threshold, you may be able to develop and retain a suitable base of people who have those skills. One alternative is to contract those skills in on behalf of the Government when a particular project is being considered. There may be difficulties with that if most of the firms with whom the Government might want to deal for such advice are themselves involved with one or more of the parties who may be bidding for the project.

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<sup>55</sup> Mr Joe Tripodi, Chairman and Mr Robert Sendt, Auditor-General, transcript of Hearings page 1.

<sup>56</sup> Mr Robert Sendt, Auditor-General, transcript of Hearings, page 6.



The Auditor General outlined two possible approaches:

**Mr SENDT<sup>57</sup>:** ... I was suggesting two possible models. One is a central body with the expertise to get involved in these projects. The other is, if that model does not apply—and some agencies have their own in-house expertise—that there be some central body that itself has sufficient skills, resources and opportunity to review and scrutinise those projects....

**Mr GLACHAN:** So what you were saying was that you think that Treasury is the best agency to review these things and that it needs time to be able to do it properly. That is roughly what you are saying.

**Mr SENDT:** From the financial and risk management perspective, that is the role that Treasury has had and, in that regard, it would be the principal adviser to the budget committee of Cabinet at present. There may be other aspects that the Treasury does not have expertise in, such as project management. Certainly, on the financial side I think Treasury is the right organisation.

Agencies have the ability to contract in the appropriate advice, and the Auditor General has chosen this option because of the difficulty of attracting and retaining staff.<sup>58</sup> For those which prefer to use public sector skills there are currently two options: Treasury and the Department of Public Works and Services.

Some agencies seem not to consult Treasury for advice at the developmental stage because of its pivotal role in advising the Government whether a project should be approved for funding by the budget Committee of Cabinet:

**CHAIR<sup>59</sup>:** Is it your experience that the agencies that are sponsoring the project tend to be secretive and want to control them and possibly keep out, for example, the expertise that Treasury may have to offer?

**Mr SENDT:** The experience from my Treasury time, when the documentation of major projects would quite often arrive in Treasury only a few days before a Budget Committee meeting or Expenditure Review Committee meeting, would seem to indicate a disinterest by the organisations concerned in involving Treasury at an early date. I think when Treasury was involved at an early date, it generally proved advantageous in perhaps providing a different view of what was being proposed.

<sup>57</sup> Mr Ian Glachan, Committee Member and Mr Robert Sendt, Auditor-General, transcript of Hearings, page 7.

<sup>58</sup> Transcript of Hearings, page 6.

<sup>59</sup> Mr Joseph Tripodi, Chairman and Mr Robert Sendt, Auditor-General, transcript of Hearings, pages 1-2.



The Treasurer is required to approve any borrowing greater than \$5m by an agency<sup>60</sup>, and this places Treasury in a pivotal role in relation to any project. On the one hand, it must recommend approval, and when it also provides advice this may create a conflicting role.

**CHAIR<sup>61</sup>:** ...The PRL proponents, whether it is the Minister or the department, know that this is going to be a lot more costly than initially they indicated to you. At the same time, you are performing this other function, because you have a wealth of expertise in how to structure these deals. Given that they anticipate there will be a conflict with Treasury down the road on the issue of how much funding they will receive or when they will receive it, they would be hesitant to come forward with their ideas on how to structure the deal. I just want to get from you whether you believe or acknowledge that there may be a conflict in some situations between the two functions. Yes or no?

**Mr GRAHAM:** I can see with the example you are citing that there may be a conflict. I can cite other examples where there is obviously no conflict. I can cite to you the cross-city tunnel, where we are working cooperatively with the RTA. We are on their evaluation team. We have worked with them from day one on structuring and formulating the project.

**CHAIR:** That is because it is coming in on budget, is it not? That is why there is a good relationship there, because they are not concerned about the budgetary need they have.

**Mr GRAHAM:** There are normally conflicts and tensions between Treasury and agencies.

The Committee believes that the public sector needs an alternative to Treasury as a centralised source of advice. The Committee believes that agencies have on many occasions been in conflict with Treasury over budget funding issues on a project. This conflict has repeatedly caused agencies to evade and possibly even mislead Treasury on the detail of large infrastructure transactions. This agency reaction has prevented Treasury from applying its expert scrutiny to a proposal. Without this scrutiny occurring, the State has entered into agreements where it has left itself open to unanticipated liabilities. The Committee is of the view that Treasury can no longer play the role of recommending to the Budget Committee of Cabinet while also being the adviser to the agency on how to structure these kinds of transactions. The Committee is deeply concerned that, since there have been increases in the projected costs of the PRL project, an inevitable conflict will occur. However, the Committee is confident that the expertise currently employed by the Parramatta Rail Link Company will ensure that the best value for money is secured nonetheless. This conflict between agencies may explain why previous public-private partnership deals have proven costly to the State.

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<sup>60</sup> The Treasurer has prescribed a threshold of \$5m under the *Public Authorities (Financial Arrangements) Act (1987)*, Section 8.

<sup>61</sup> Mr Joseph Tripodi, Chairman and Mr Danny Graham, Treasury, transcript of Hearings, page 27.





The Department of Public Works and Services advised that part of its mandated role in project management includes financial and contract advice:

**Mr SMITHIES<sup>62</sup>:** Under a Premier's memo, [TM]91/7, DPWS has been given the role of acting as the industry interface, if you like, or the intermediary between agencies that are not expert in construction-type matters and the construction industry. We have a list of the sorts of agencies that are, if you like, required to use DPWS in that capacity. Agencies that obviously are not required to use DPWS, such as the RTA and the other major construction authorities, have their own expertise in that area.

... The role that we choose, in fact, impacts on the preparation of contracts because we are about making sure that the risks are allocated appropriately and the Government is not unduly exposed to risk...

**Mr COLLINS:** I do not think we could go quite so far as to say that [agencies] try to get around [the memorandum]. Some are probably ignorant of it. I think when you get into the private sector funding area they may well not make the connection necessarily between what is perceived to be a more construction-oriented memo and the actual consequences. I think that is probably a fairer way of saying it.

The Olympic Coordination Authority (OCA) had a tight mandate to manage provision of the Sydney Olympics infrastructure. One of the keys to OCA's success was that it had a single reporting line to its Minister through its CEO, and it established a 'clean, quick decision making process' with people who were able to operate in this manner<sup>63</sup>. It contracted in advice, from both the public and private sectors, and was successful in operational terms and in remaining within its construction budget. This is similar to the model used in the Parramatta Rail Link.

Larger agencies retain in-house project management expertise and are comfortable with the process of recruiting or buying in the appropriate expertise. However, the Committee believes that the capabilities of smaller agencies need to be enhanced and their lines of accountability made clear in two key roles: as sponsor (managing the procurement process) and as client (managing the various sources of advice). There is currently a plethora of advice and smaller agencies with infrequent projects find it hard to learn the lessons from many previous occasions.

Therefore, the Government should create a centralised source of expert advice in project and service procurement. This will require changes to section 8 of the *Public Authorities (Financial Arrangements) Act (1987)* confining Treasury to determining budget parameters (as contained within the Budget Papers, or possibly involving supplementation) and no longer advising on the deal itself. This expert agency would act as an adviser to the sponsoring agency and would assist it with the planning and contracting strategy for the project. Appropriate legal, financial and technical expertise would be bought in from public or private sector experts. The Government should also create an approved list of private sector project management experts, to introduce contestability in this key role. The Committee believes this

<sup>62</sup> Mr Ted Smithies and Mr Tony Collins, Department of Public Works and Services, transcript of Hearings, page 9.

<sup>63</sup> Submission of the Olympic Coordination Authority to the Inquiry, page 1.



agency is best located within the Department of Public Works and Services and with a structure similar to that of the Olympic Coordination Authority.

This approach separates the project management role and assigns it to a public or private sector body with expertise. It continues the approach successfully used for the Sydney Olympics and subsequently for the Parramatta Rail Link through the PRL Company. It provides the option of buying in relevant public or private expertise (financial, technical, legal) but keeps responsibility firmly with the sponsoring agency. By establishing the project management structure early, it allows industry parties not involved in this aspect freedom to bid on other aspects.

The Committee has been advised that some staff of the Olympic Coordination Authority would be willing and able to continue working in the public sector, if there are suitable roles. The responsibility of working for the principal can be a counterweight to possibly more attractive terms and conditions in the private sector<sup>64</sup>. The Committee believes that this source of public sector expertise should not be lost, and they should be considered for recruitment into the new advisory agency within the DPWS.

As part of these reforms, the Government should also clarify and better define the roles of both DPWS and TCorp and reissue the respective memoranda so that their roles and expertise are clear. Currently, both agencies are able to provide advice on financial aspects of projects and in addition DPWS has a range of other functions.

The Committee believes that in the interim, until the new expert management agency is established, Treasurer's Memorandum TM91/7 and Treasury Circular TC98/07 should be reissued to emphasise the need for agencies to seek early advice on financial aspects in addition to construction, and to outline the contributions of the various agencies available to give advice.

### **Recommendation 7**

The Government should create a centralised source of expert advice in project and service procurement. A special unit within the Department of Public Works and Services should advise agencies on how to structure transactions involving the private sector. The Government should consider current or former staff of the Olympic Coordination Authority for recruitment into this new unit, and it should also create an approved list of private sector project management experts, to introduce contestability in this key role.

<sup>64</sup> Submission of the Olympic Coordination Authority to the Inquiry, page 1.



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## Chapter Four

### Conclusions

New South Wales has been an international pioneer in some aspects of public-private partnerships, like BOOT infrastructure schemes. The Committee's recommendations in this report are designed to build on the strengths of New South Wales' infrastructure procurement systems and the people involved in it.

To encourage innovation, the Committee believes that the approach in the Parramatta Rail Link *Invitation for Registrations of Interest and Alternative Proposals* should be continued in future projects. The project should be defined in accord with policy and planning decisions such as the Environmental Impact Statement, but within these bounds, should be specified in outcome-based terms. This is in addition to a wide canvassing of the project fundamentals earlier in the planning process.

The Government needs to enhance the skill base available to agencies and highlight the risks of not seeking expert advice, to ensure that appropriate decisions are made before community expectations have become built up. The private sector has indicated its preference for a consistent and streamlined approach<sup>65</sup>. Infrastructure planning and procurement will continue to rest primarily with Ministers and their agencies. The Committee's recommendation to create a specialist advisory agency and strengthen the existing centres of expertise should make clear the accountability of the initiating line agencies and strengthen their capacity to be effective. Creation of a new specialist agency should also improve coordination of the process between the key advisory and regulatory agencies.

The Committee is aware that with the release of the Government's Green Paper on Infrastructure, private sector parties are more interested than ever before in fully or partly financing infrastructure projects in New South Wales. At the same time, the general public seems to have a low tolerance for privately financed projects, because of perceptions that some deals (like the Airport Rail Link) have been very unfair to the taxpayer.

To improve transparency and perceived fairness, the Government should require that future detailed tenders include the associated financial model. This is a step toward achieving outcomes which are fair and seen to be fair. However, a contract-based approach alone will never be sufficient to ensure sound and fair outcomes. To move closer toward this objective, all parties need to demonstrate continued goodwill and a commitment to improvement.

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<sup>65</sup> Comment by Mr. M. Phillips, Commonwealth Bank, NSW Infrastructure Forum, 29 November 2000.



## Appendices

### Appendix 1: Letter from the Independent Commission Against Corruption





the Committee should give priority to protecting itself from allegations that such material was deliberately or inadvertently communicated to competitors. Above all, there should be no actual or perceived advantage to any bidder involved in the Committee's enquiry.

Whilst it is outside the Commission's role to advise on issues other than preventing corrupt conduct, it would seem likely that the tendency for each of the bidders to carefully guard their commercial interests may have an effect on the number and nature of any submissions received. Consequently, given that any competitive process has winners and losers, it is difficult to see how some bidders would not be tempted to treat the Committee's interest in the project merely as an opportunity to air grievances.

In any case, if the Committee receives any information about probity concerns it should feel free to forward them to the ICAC.

Yours sincerely

A handwritten signature in black ink, appearing to read 'N. Wolanin'.

Nick Wolanin  
Principal Corruption Prevention Officer



## Appendix 2: PAC advertisements for the Inquiry

*Inquiry Terms of Reference Advertisement:  
Placed 11 March 2000.*

### **Inquiry into the Funding of Capital Projects by the New South Wales Government**

The Public Accounts Committee is to examine and report on:

1. the funding of large capital projects by the NSW Government, including the impact of legislative requirements and budgeting practices;
2. private sector funding practices for infrastructure projects, including any benefits to arise from the optimisation of project construction and funding periods;
3. an examination of the funding aspects of selected capital projects, including the balance of risks and rewards between the State and private enterprise, the cost of underwriting by the State and accounting/taxation treatments;
4. whether improvements are possible to the funding arrangements for large capital projects, including improved economic benefits and service provision, and any implications for the funding of infrastructure in regional and rural NSW;
5. any other relevant matters.

Individuals and organisations are invited to make submission (in writing, typed or on disk) to assist the inquiry. Submissions should be addressed to:

The Committee Manager  
Public Accounts Committee  
Parliament House  
Macquarie Street  
SYDNEY 2000

Alternatively they can be sent by FAX to (02) 9230 2831 or emailed to [alarkin@parliament.nsw.gov.au](mailto:alarkin@parliament.nsw.gov.au)

Further information can be obtained from the Committee Manager, Yael Larkin on (02) 9230 2521.

Closing date for submissions is 14 April 2000.

Joseph Tripodi MP  
Chairman

***Parramatta Rail Link Advertisement****Placed 27 September 2000***Legislative Assembly  
PUBLIC ACCOUNTS COMMITTEE****Evaluation of Funding of Capital Projects  
by the NSW Government****Parramatta Rail Link Project**

The Public Accounts Committee's evaluation of capital funding, which commenced on 11 March 2000, is examining:

1. the funding of large capital projects by the NSW Government, including the impact of legislative requirements and budgeting practices;
2. private sector funding practices for infrastructure projects, including any benefits to arise from the optimisation of project construction and funding periods;
3. an examination of the funding aspects of selected capital projects, including the balance of risks and rewards between the State and private enterprise, the cost of underwriting by the State and accounting/taxation treatments;
4. whether improvements are possible to the funding arrangements for large capital projects, including improved economic benefits and service provision, and any implications for the funding of infrastructure in regional and rural NSW;
5. any other relevant matters.

As part of the evaluation the Committee is seeking submissions from interested parties on capital funding aspects of the Parramatta Rail Link (PRL) project. The Committee is particularly interested in how value for money is maximised through the range of options submitted to government. The Committee is interested in any critical comment that may lead to improving the efficiency and effectiveness of infrastructure transactions for both the NSW Government and private sector participants.

The Committee is taking this opportunity to draw on expertise currently involved in this major infrastructure project with the aim of improving future practices. The Committee is not reviewing the PRL's objectives. The evaluation does not include probity issues, nor have any concerns over probity emerged.

Submissions should be addressed to: The Committee Manager, Public Accounts Committee, Parliament House, Macquarie Street, SYDNEY 2000. They can also be faxed to (02) 9230 2831 or emailed to [pac@parliament.nsw.gov.au](mailto:pac@parliament.nsw.gov.au). Inquiries can be made on 9230 2631 or 9230 2521.

Submissions should indicate if any information is confidential. All sensitive information will be treated with the strictest of confidence. Closing date for submissions is 10 October 2000.

Joseph Tripodi, MP – Chairman



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### **Appendix 3: List of submissions to the Inquiry**

#### **(A) Submissions relating generally to the Inquiry's Terms of Reference**

- Australian Council of Infrastructure Development Limited
- Dr John L. Goldberg
- Macquarie Bank Limited
- the Olympic Coordination Authority (tabled the following day in Hearing)
- North Ryde Residents' Group

#### **(B) Submissions relating to the Parramatta Rail Link**

- ALSTOM Australia Limited \*
- Australian Council of Infrastructure Development Limited
- International Association of Public Transport (Australia/New Zealand)
- Macquarie Bank Limited \*\*
- Parramatta Chatswood Consortium \*\*

\* Commercial in Confidence at the request of the party making the submission.

\*\* Deemed to be confidential by the Committee because it contains material relating to the proponent's proposals to the Parramatta Rail Link Project.





#### Appendix 4: List of witnesses at the Hearing, November 23 2000

<u>Organisation</u>	<u>Representative</u>
Auditor General	Mr Bob Sendt, Auditor General  Mr Phil Thomas, Assistant Auditor General
Department of Public Works and Services	Mr Tony Collins, Group General Manager Project Management Group  Mr Ted Smithies, Group General Manager Strategic Procurement Services  Mr Ed Shestovsky, Acting General Manager Procurement Management Branch  Mr Norm Johnston, General Manager Major Developments Branch
Treasury	Mr Danny Graham Principal Adviser, Infrastructure  Mr Robert Carling, Executive Director, Economic and Fiscal Strategy
Premier's Department	Mr Chris Oxenbould Director, Infrastructure Coordination Unit
Department of Transport	Mr Ian Robinson, Deputy Director General
Parramatta Rail Link Project Team	Mr Peter Katz, Project Director  Mr William Grant, Planning Policy Manager.



## Appendix 5: Major stages in the Parramatta Rail Link decision and supporting documents

Stage	Outcome	Documentation
Strategic planning	<ul style="list-style-type: none"> <li>➤ Establish benefits of major new east-west transport link from Parramatta</li> </ul>	<ul style="list-style-type: none"> <li>➤ Greater Western Sydney Public Transport Strategy, 1997.</li> <li>➤ Greater Western Sydney Planning &amp; Transport Review and Priorities Study, 1996.</li> </ul>
Establish project control group	<ul style="list-style-type: none"> <li>➤ Project Control Group formed from Department of Transport, Rail Access Corporation and State Rail Authority</li> <li>➤ Experienced private sector project manager appointed</li> </ul>	<ul style="list-style-type: none"> <li>➤ Parramatta-Chatswood Rail Link: Economic and Financial Assessment, December 1996</li> <li>➤ Parramatta-Chatswood Rail Link Evaluation Report, February 1997</li> </ul>
Evaluate alternatives	<ul style="list-style-type: none"> <li>➤ Numerous alternatives considered by Project Control Group</li> <li>➤ Parramatta-Chatswood rail link selected as preferred option</li> <li>➤ Decide to conduct EIS</li> </ul>	<ul style="list-style-type: none"> <li>➤ Parramatta Rail Link Overview Report, November 1998.</li> <li>➤ Advertisement calling for comments on proposal as outlined in Overview Report, November 1998.</li> </ul>
Conduct EIS	<ul style="list-style-type: none"> <li>➤ EIS commenced September 1998 and report published December 1999</li> <li>➤ Community consultations December 1998-April? 1999</li> <li>➤ 12 route/mode alternatives discussed in EIS</li> <li>➤ heavy rail between Parramatta, Epping and Chatswood recommended for consideration by Minister for Urban Affairs and Planning</li> <li>➤ EIS Assessment Report not yet completed by DUAP</li> </ul>	<ul style="list-style-type: none"> <li>➤ Environmental Impact Statement, 3 December 1999.</li> </ul>
Call for alternatives	<ul style="list-style-type: none"> <li>➤ Advertisements placed in September 1998</li> <li>➤ 52 alternatives submitted and screened for consistency with project objectives; 12 short listed and evaluated in EIS process</li> </ul>	<ul style="list-style-type: none"> <li>➤ Advertisement 5 September 1998.</li> </ul>
Plan tendering process	<ul style="list-style-type: none"> <li>➤ Framework for tendering process established</li> </ul>	<ul style="list-style-type: none"> <li>➤ Report on the Proposed Tendering Process, Arthur Andersen, March 1999.</li> </ul>
Establish Parramatta Rail Link Company	<ul style="list-style-type: none"> <li>➤ Tenders called for legal, technical and contracting strategy</li> </ul>	<ul style="list-style-type: none"> <li>➤ Advertisement</li> </ul>



Establish project contracting strategy	<ul style="list-style-type: none"> <li>➤ Workshop with main stakeholders, February 2000</li> </ul>	<ul style="list-style-type: none"> <li>➤ Report from Project Risk/Contract Delivery Strategy Workshop, February 2000.</li> <li>➤ Report on Single or Multiple Contract Packaging, Parramatta Rail Link Review Group, March 2000.</li> <li>➤ Parramatta Rail Link Project Contracting Strategy, March 2000.</li> </ul>
Seek proposals from private sector	<ul style="list-style-type: none"> <li>➤ Invitation issued in April 2000, closing date June 2000.</li> <li>➤ 27 conforming proposals and 17 alternatives submitted.</li> </ul>	<ul style="list-style-type: none"> <li>➤ <i>Invitation for Registrations of Interest and Conforming Proposals</i>, April 2000.</li> </ul>
Evaluate proposals	<ul style="list-style-type: none"> <li>➤ Result not yet known: possibly request for detailed tenders from a short list of proponents.</li> </ul>	<ul style="list-style-type: none"> <li>➤ Procedure for Evaluating ROIs and Alternative Proposals, June 2000.</li> </ul>