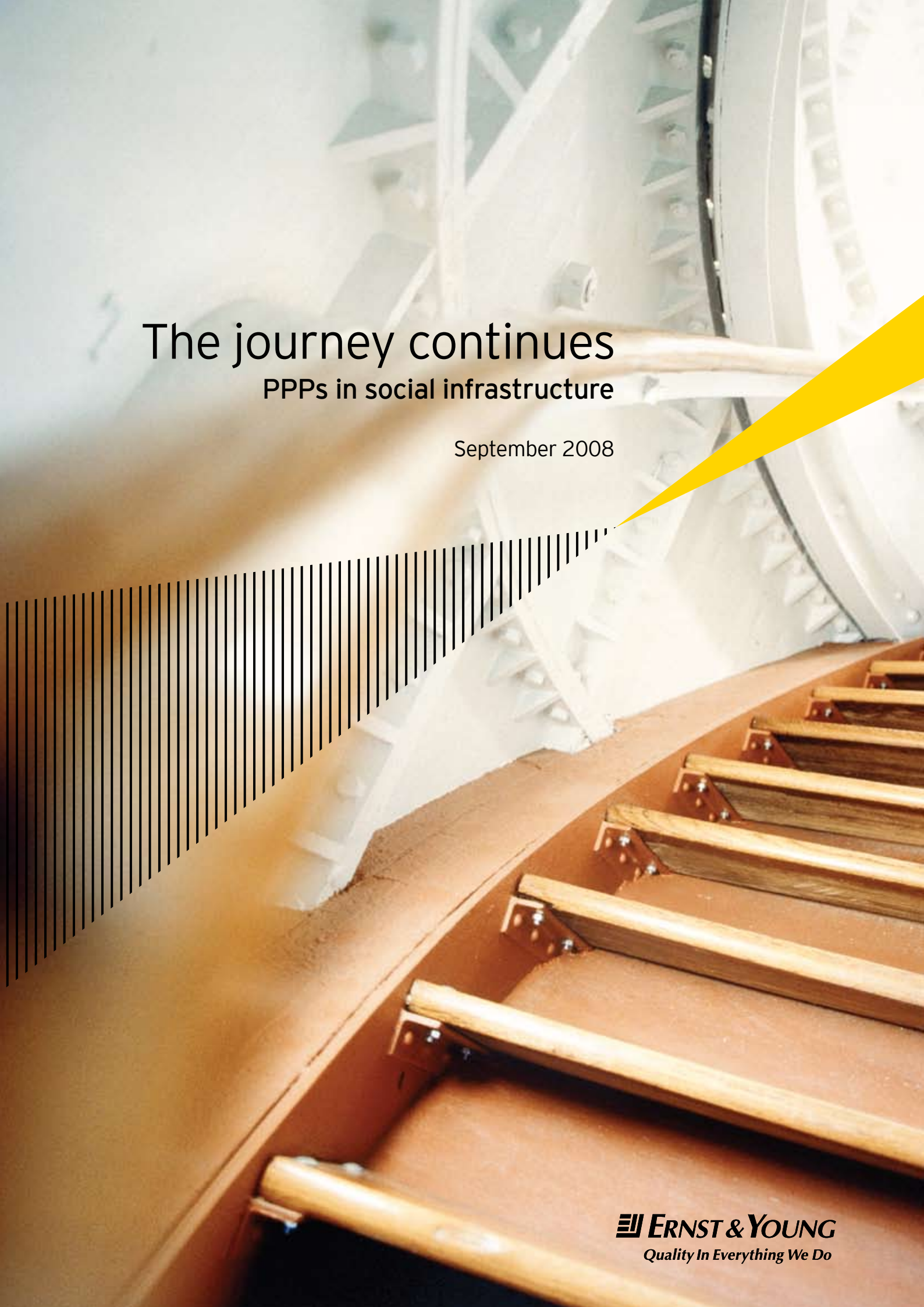


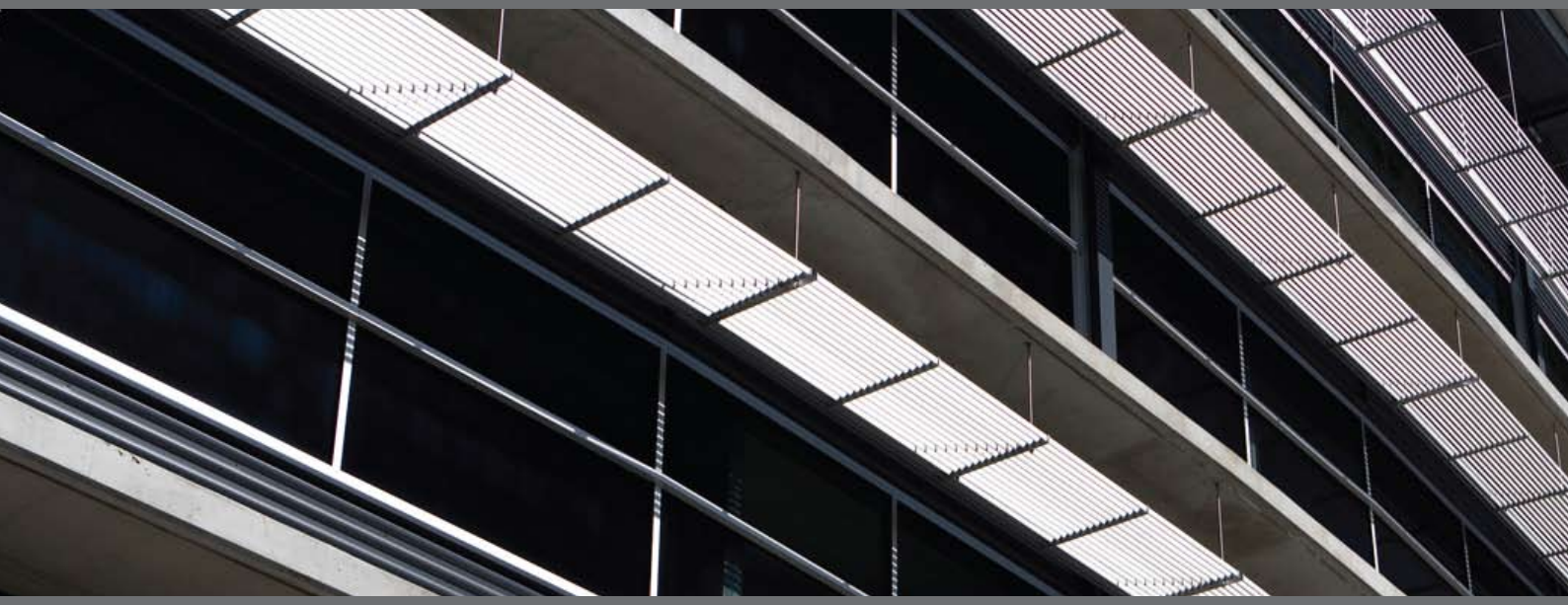
The journey continues

PPPs in social infrastructure

September 2008

Ernst & Young

Quality In Everything We Do



Queensland Southbank Institute of TAFE imagery provided by Spotless

With many early PPP projects now operating, we can examine how the model is performing and identify best practice.

The journey continues
PPPs in social infrastructure

Australian government agencies are increasingly adopting Public Private Partnerships (PPP) to deliver social infrastructure projects. These long-term partnerships with the private sector are addressing the ever-growing demand for services such as: health; education; social housing; corrections; and justice.

The experience of developing and delivering these services has created new disciplines on both sides of the infrastructure industry. Private companies have learnt to deliver the 'user experience', for amenities such as schools, hospitals, courts and prisons, as a long-term service outcome. At the same time, government agencies have developed greater discipline surrounding: services specification; contract design; and project management. With many early PPP projects now operating, we can examine how the model is performing and identify best practice.

To support the industry-wide drive for continual improvement, Ernst & Young surveyed key public and private sector stakeholders participating in operational social infrastructure PPP projects. The survey looked at project effectiveness and examined whether PPPs are delivering value.

In doing so, the survey sought to add to the industry findings on the performance and timeliness outcomes of PPP projects including the report conducted by Melbourne University and the Allen Consulting Group[1]. Thus, the interviews focused on less quantifiable benefits flowing from the projects including: end-user satisfaction; the practicalities of contract management; success of the reporting and communication mechanisms; risk allocation; payment mechanisms; and innovation.

We hope the initial findings from these early PPPs will provide a starting point for collecting more robust information on the operation of PPPs to deliver cost-effective, quality infrastructure to the community.

[1] Melbourne University and Allen Consulting Group, November 2007, "Performance of PPPs and Traditional Procurement in Australia "

Key findings

PPPs delivering on their value promise

With a focus on end-user and government perspectives, the survey revealed PPP projects are delivering value for money to the public sector.

- New infrastructure and facilities were delivered as planned, on time and to government budget requirements.
- The PPPs have enabled public sector personnel to focus their attention on delivering core services, providing confidence that facilities are being monitored and maintained to a high standard.
- Payment and abatement regimes are an effective commercial incentive for the private sector to perform to a high standard.
- The high build quality and level of maintenance of PPP facilities has increased the sense of respect for property.
- Third party use of public sector facilities builds relationships with the community, as well as improving value for money.

PPPs require collaborative and comprehensive planning

Investing time and resources early in the process is critical for project success.

- Investing in developing a robust output specification helps complex contracts to operate smoothly.
- Innovation in infrastructure delivery is not easy; however, freedom of design combined with bundling a wide range of operating services increases the potential for innovation.
- Collaborating with end-users and the public sector during the development phase strengthens the connection between the contract requirements and their practical application.
- Valuable project knowledge is often lost, particularly following the tender process, due to changes in key personnel. Thus, rigorous documentation is required, throughout the project, to safeguard intellectual property.

Effective partnerships are built on relationships

Successfully executing a PPP project depends on a sound relationship between the government agency and private sector partner.

- Contract management is a critical skill for government.
- The contract must provide a supportive framework within which the parties operate in a spirit of partnership to find pragmatic solutions to issues as they arise.

Survey interview panel

Our qualitative survey interviewed industry stakeholders participating in a number of operational social infrastructure PPP projects. The interview panel included the following end-users, government project directors, facilities managers and investors.

Organisation	Contact	Title	Project name
Victorian County Courts	Neil Twist	Chief Executive Officer	Victorian County Court
South Australian Courts Administration Authority	Trevor O'Rourke	Director, Corporate Services	SA Courts Administration Authority
South Australian Courts Administration Authority	John Thrippleton	Senior Project Officer, Corporate Services	SA Courts Administration Authority
Victorian Department of Justice	Johan Top	Senior Program Advisor	Victorian Correctional Facilities
Victorian Department of Justice	Glenn Gunther	Senior Program Coordinator	Victorian County Court
Victorian Department of Primary Industries	John Rickard	Contract Director	Royal Melbourne Showgrounds redevelopment
Infrastructure Funds Management (IFM)	Azhar Abidi	Investment Manager	NSW Schools
NSW Department of Education	Terry Whyte	Project Director	NSW Schools
Plenary	Ray Wilson	Director	Casey Hospital, SA Police & Courts
Royal Agricultural Society of Victoria	Adnan Mansour	Chief Operating Officer	Royal Melbourne Showgrounds redevelopment
Sherwood Ridge Primary School	Jan Marshall	Principal	NSW Schools 1[2]
South Australian Police	Mark Peterson	Principal Contract Manager	SA Police and Courts
Queensland Southbank Institute of TAFE	Norm Jagger	Project Director	Southbank TAFE
Spotless	Geoff Barnsley	Executive General Manager Operations	NSW Schools 1, Queensland Southbank TAFE
Victorian Department of Human Services	John Iliadis	Contract Administrator	Casey Hospital

The following paper includes direct quotations from the interviewees. All views and opinions expressed outside of these statements are the views and opinions of Ernst & Young.

[2] The NSW Department of Education has two PPP projects. This project refers to the first project delivered.

PPPs delivering on the value promise

Project	Planned completion	Actual Completion
NSW Schools 1	January 2005	January 2005
Queensland Southbank TAFE	December 2008	First buildings delivered Jan 2007 Other buildings ahead of schedule
South Australian Police & Courts	December 2006	November 2006 The nine facilities were completed on budget and ahead of time 80 days early across nine facilities
Royal Melbourne Showgrounds	August 2006	August 2006
Victorian County Court	May 2002	May 2002
Casey Hospital	September 2004	August 2004
Victorian Correctional Facilities	Correctional Programs Centre - October 2005 Remand Centre - December 2005	Correctional Programs Centre - February 2006 Remand Centre - March 2006

Value for money is one of the key factors for governments pursuing a PPP model to deliver infrastructure. Not only is value for money achievable through time and cost efficiencies, it can also be gained from: greater certainty of expected financial outcomes; innovation and efficiency; and releasing public sector resources to focus on core service delivery. Our survey captured end-user and government contract managers' observations of whether and how the projects are delivering value for money.

Facilities delivered as planned: on time and on budget

A key benefit of the PPP procurement process is that, once the contract is signed and the design is agreed, the private sector assumes the long-term risk of delivery. The financial incentives to deliver on time and budget under a PPP are significant. This sense of lock down once the contract is signed, gives government agencies security that the costs of the project will not increase further.

Moreover, the PPP model encourages agencies to define and cost the scope of the project in detail at an early stage, reducing the potential for scope creep during the procurement process.

The contractual arrangements of a PPP also help projects stay on schedule, offering incentives for contractors to make up time should projects fall behind. In fact, our interviews identified several projects, driven to tight timeframes by the PPP model, which actually finished ahead of schedule.

"Builders were behind schedule at one of the sites (SA Police & Courts). With the private sector exposed to the consequences of delay and driving the contractual demands, the project was delivered on time. This is a strong example of the benefits of relying on the private sector management over traditional delivery." Ray Wilson, Director, Plenary.

This sentiment is supported by the assessment conducted by Melbourne University and the Allen Consulting Group[3] that identified "traditional projects were likely to be completed later than PPPs relative to the budget. For example, between signing of the final contract and project completion, PPPs were found to be completed 3.4% ahead of time on average, while traditional projects were completed 23.5% behind time." This is demonstrated in the table above, comparing the actual completion date with planned completion date for each of the projects surveyed.

Only one project was delayed. The Victorian Correctional Facilities experienced a small delay in achieving operational readiness that resulted in part from time pressure on commissioning. Prisons are complex environments where security is of paramount importance.

[3] Melbourne University and Allen Consulting Group, November 2007, "Performance of PPPs and Traditional Procurement in Australia "

"Now I have someone with the right knowledge and expertise to take care of the building, so I can focus my time on the students, teachers and parents."

Jan Marshall, Sherwood Ridge Primary School

Proving that they are operationally ready to receive prisoners is essential and in this environment the small delay is not material.

Enhanced core services

Using PPPs in social infrastructure transfers the responsibility for infrastructure delivery, maintenance and support services to the private sector. This allows government employees to focus on delivering their 'core services' e.g., education, medical attention, legal proceedings, custody.

End-user and government stakeholders interviewed were positive about the way daily operations are managed at their facilities. End-users identified staff performance improvements as a result of participating in a modern, innovative environment. While this effect is possible in any newly built facility, the nature of the PPP contracts allows end-users to focus on delivering core services with the confidence that facilities are being monitored and maintained to a high standard. Jan Marshall, Principal of Sherwood Ridge Primary School outlines the importance of this transfer in responsibilities:

"The (PPP) arrangement releases me to be an educational leader. At my old school I would need to spend time sorting out problems with the facilities. Now I have someone with the right knowledge and expertise to take care of the building, so I can focus my time on the students, teachers and parents."

Queensland Southbank Institute of TAFE image provided by Spotless

Long-term approach to service delivery

With ongoing incentives built into its payment mechanism, the PPP model drives a proactive approach to maintenance and refurbishment. All stakeholders within the projects highlighted this as a valuable benefit of the PPP model. Unlike traditional infrastructure management, maintenance within the PPP is not subject to the ongoing government budget process. This focus on long-term service provision is embodied in the performance-based payment mechanism for the private sector.

Victorian County Court image provided by Victorian Department of Justice

John Thrippleton, Senior Project Officer, Corporate Services, SA Courts Administration Authority explains:

"The focus on availability and performance is a great idea. We haven't yet needed to apply any abatement as the payment mechanism provides appropriate incentive for the equity investor to be proactive in addressing failures before they result in abatement."

The survey also revealed evidence of better design and construction quality using the PPP model. Interviewees saw great value in the private sector taking responsibility for long-term maintenance and asset replacement. This drives a whole-of-life approach to asset management, enforcing high quality materials and repairs. The comparison in quality to traditional construction is reinforced by Terry Whyte, Project Director, NSW Department of Education:

"The new schools are of a noticeably better quality build because the provider is responsible for the up-keep of the facilities for thirty years. The equity investor has also encouraged a high standard of maintenance to lengthen the life of resources."

While a PPP contract has a long term period of 25 years or more, the design life of buildings can extend 50 years and beyond. At the end of the contract term the facilities typically revert back to government ownership. The industry is many years away from testing this ownership transfer however, critics argue that the condition of the facilities will not be of a suitable standard to meet the remaining asset life.

It is difficult to predict what will happen with these projects in the next 25 years. This is not an issue that is confined to PPP arrangements. Where an asset is procured using traditional methods, such as Design & Construct, there is still the inherent conflict that arises when the Government creates long life assets that also tend to be reasonably fixed in their form and location. The issue of ongoing functionality exists in all infrastructure projects and there is no evidence to suggest that traditional forms of procurement offer any better long-term outcomes than PPP. Indeed traditionally procured projects are far more likely to encounter chronic back log maintenance in the later years of the asset's useful life that creates an added drain on public funds in addition to the asset perhaps not being functionally efficient.

In these respects PPPs have two major advantages over traditional procurement: firstly there tends to be greater consideration of flexibility in the design and contracts to accommodate changes in the function of the asset over time; and secondly, if maintenance issues do arise then there are very significant financial incentives on the private sector to rectify. Interviewees pointed to the incentives built into the payment arrangements that have to-date encouraged the PPP operators to maintain the facilities at a high standard. These incentives remain throughout the contract term and many believe they are adequate incentives to deliver a well maintained facility with remaining useful design life to Government.

> "The building is made of high quality materials and is well maintained. This contributes to a sense of respect by those using the Court - not just as a building but as an institution. We have seen a marked improvement in people treating the property with care."
>
> Neil Twist, Victorian County Courts

For example, some State governments have included a policy for returning assets to be subject to an independent review that assesses the costs to reinstate the assets to a required condition. An alternative measure used by the Western Australian Government on the Perth CBD Courts project, incorporates a 'bullet payment' that is abated if the assets do not meet the specified standard at the end of the term.

Increased respect for facilities

A previously understated benefit of well designed and managed PPP facilities is their positive impact on end-user behaviour. The survey identified several facilities with reduced graffiti and damage. Interviewees also noted a better user attitude towards cleanliness and tidiness, as Neil Twist, CEO, Victorian County Courts describes:

"The building is made of high quality materials and is well maintained. This contributes to a sense of respect by those using the Court - not just as a building but as an institution. We have seen a marked improvement in people treating the property with care."

While difficult to quantify, this behavioural change is a tangible benefit, reducing ongoing costs and improving the working environment for facility users.

Adnan Mansour, COO, Royal Agricultural Society of Victoria, explains that the PPP has driven Royal Melbourne Showground staff to use the facility more efficiently:

"Staff have a heightened appreciation of the costs associated with providing the facilities. They are now more careful when utilising exhibition and event space to ensure the accommodation is appropriate to the need. This leads to cost savings and reduced wear and tear on the facilities."

This sentiment is supported by Glenn Gunther of the Victorian Department of Justice, Senior Program Coordinator for the Victorian County Courts PPP:

"The PPP has resulted in a shift in culture with users, including judges, being aware of the need for efficient use of the court rooms."

Third party use

The PPP model also opens the door for government to gain value from complementary property development. When such strategies are pursued, critics often denounce the plan as private sector exploitation of community services. Such fears are usually misplaced. For example, while the NSW Schools PPP project makes the facilities available for third party and community use outside of school hours, the school retains ultimate control over the facilities. Jan Marshall, Principal, Sherwood Ridge Primary School, explains:

"It has been suggested that the schools are handing over control of their facilities to the private sector who then allow anyone to use the facilities. This is not true. The principal controls who from outside the school uses the facilities."

Indeed, these commercial opportunities often benefit the government employees and the public using the facilities. For example, Victorian County Courts has relied on an innovative approach to asset utilisation to generate additional value, as CEO Neil Twist describes:

"Using third party bookings for the rooms, while novel, has had the added benefit of introducing the County Court to a wider community audience. It is also an efficient use of the Courtrooms as public spaces when they are not being used for hearings."

Other examples of complementary cross-facility use include:

- Childcare facilities co-located with primary schools in the NSW Schools PPP
- Retail outlets at Casey Hospital
- Student accommodation at Southbank TAFE
- Retail and office precinct at Southern Cross Station, providing an essential link between the Melbourne CBD and the fast developing Docklands area

Outside the PPP model, government agencies are less likely to provide such facilities efficiently. This is a key area where private sector expertise delivers value.

PPPs require collaborative and comprehensive planning

When describing a successful procurement process, both the public and private sector observed the importance of investing time and resources upfront in establishing the State's need and project's objectives. A clearly defined specification helps ensure the contract supports a pragmatic approach to daily operations.

Setting the right specifications

Formulating the right specification for a social infrastructure PPP project is fundamental to the project's success. Interviewees identified cases where detailed specifications led to efficient delivery and smooth running of operations. As Victorian County Courts CEO, Neil Twist, describes:

"The contract shows great foresight, as it sets out in detail how the complex set of relationships between the Court and the business partners should be managed to ensure the smooth operation of the building."

To deliver appropriate standards, service providers require clearly defined output specifications when scoping the project. However, government agencies sometimes focus their limited resources on the facility design specification at the expense of the services specification. This can lead to services standards lacking strong links to measurable key performance indicators (KPIs). Without effective KPIs, payment mechanisms and abatement regimes are less effective at providing the incentives for the private sector to perform.

Project teams are addressing this issue by factoring in longer lead times to allow them to examine specifications thoroughly. The nature of some services means their specifications require greater detail and description for inputs rather than outputs. Government agencies need to determine a balance and avoid being too academic in their approach, as Johan Top, Senior Program Advisor, Victorian Department of Justice explains:

"We have limited flexibility in defining the security requirements for a prison facility. Relying soley on output based specifications could result in unintended outcomes."

John Rickard, Contract Director, Victorian Department of Primary Industries believes procurement can benefit from involving contract managers when finalising specifications and contractual arrangements. This would capture a higher level of practical detail in the contract, providing greater connection between the contract and the practicalities of the day-to-day operations. Some interviewees reported that procuring authorities are finding it hard to resource this requirement, due to the different nature of the skill sets required for transacting and contract management.

Driving innovation

Private sector innovation is often cited as a key value driver for selecting a PPP approach over the traditional model. Our survey captured varied opinions on the degree of innovation achieved on the early PPPs.

"The process helped the Royal Agricultural Society to carry out some deeper analysis of how the Show functions to provide an improved service to patrons. This contributed to some radical and exciting innovation in design."

John Rickard, Victorian Department of Primary Industries

Participants from the Southbank TAFE PPP are positive about the impact of innovation in facilities design. Geoff Barnsley, Executive General Manager Operations, Spotless, notes:

"Innovation was demonstrated through the flexibility of space and resources. Historically TAFEs have struggled with adapting accommodation to meet the variety of class configurations and technical content taught at the college. The design of the new space was testament to innovations developed with assistance from the private sector."

Norm Jagger, Project Director for Queensland Southbank Institute of TAFE, also recognises innovation in managing the construction phase:

"One of the advantages from the PPP framework has been minimal disruption to normal operations. Traditionally during the construction phase, buildings would have been closed and students relocated to another campus. However, the private contractors have worked around normal operations to do what they can to minimise disruptions."

The PPP process has also driven innovation from fresh thinking on the part of the procuring agency as John Rickard, Contract Director, Victorian Department of Primary Industries, highlights:

"The process helped the Royal Agricultural Society to carry out some deeper analysis of how the Show functions to provide an improved service to patrons. This contributed to some radical and exciting innovation in design."

By contrast, other participants observed little innovation outside of project requirements:

"The project achieved some innovation, but not materially different to that which would have been achieved under traditional procurement." Trevor O'Rourke, Director Corporate Services, SA Courts Administration Authority.

"In the first NSW Schools PPP, there was a request to pursue greater freedom of design. However, to meet the extensively reviewed school facility standards and cost effectiveness, few design innovation opportunities were pursued. For the second PPP, the design imposed the New South Wales facilities standards, providing surety of function and minimising design risk for the consortia." Terry Whyte, Project Director, NSW Department of Education."

The survey revealed innovative asset solutions are more likely when the PPP contract bundles a wider range of services. This allows the private sector to consider innovative ways of creating efficiencies by taking a holistic approach to delivering facilities and services. Social infrastructure projects with only a limited range of services constrain the potential for innovation. For example, recent hospital PPP projects in Australia have missed the opportunity to drive innovation by extending services to clinical ancillary areas such as pharmacy and diagnostics.

Interviewees raised the issue of limited incentives for innovation during the operational phase of a project. The standard PPP procurement model is designed to encourage innovation at the tender stage. However, small operational improvements beyond the scope of the tender could create greater efficiencies in the long term. The nature of facilities management sub-contracts can sometimes make the private sector reluctant to invest in more innovative delivery methods than were prescribed in the original bid.

"Incentives in facilities management contracts can conflict with the longer term benefits of life-cycle maintenance. Facilities managers might minimise FM costs in the short term to the detriment of life-cycle maintenance where there is incentive to do so" John Iliadis, Contract Administrator, Casey Hospital.

Procuring agencies and their advisors continue to determine how best to stimulate innovation throughout the term of the contract. Some argue that the current contracts provide for flexibility and technical refresh through change clauses that account for minor works. However, the problem has yet to be solved in terms of creating the right commercial incentives. For example, if a PPP hospital is to take advantage of technological advancements such as mechanised drug dispensing, then the contract needs to include a commercial mechanism to reward the provider appropriately for refreshing technology.

Moving forward, governments should seek to improve on commercial incentive structures to encourage innovation, rather than having to rely on a change mechanism, where the private sector is motivated by reward from taking commercial risk.

Royal Melbourne Showgrounds image provided by Victorian Department of Primary Industries

Interaction during procurement

Through the continuing evolution of PPP procurement approaches, interactive tendering processes are now standard and are becoming more sophisticated as both the public and private sectors gain greater experience with the model. Specific guidance on the interactive tender process has been developed by *Partnerships Victoria*[4], and the other States are adopting a similar approach.

Information sharing and interaction between parties early in the procurement phase is critical to PPP success, particularly in pathfinder projects. While the bidding consortiums have significant experience in construction and facility management, they need an accurate description of the way the public sector operators intend to use the facility to identify the best practice approach for the service. When transferring risks to the private sector, government agencies must allow time to educate the operators on the processes and challenges of the service being delivered.

Equally, the private sector must commit time and resources to understand their client's business. The private sector needs to identify operational risks and develop appropriate measures to mitigate these risks.

"With governments entering into 30 year contracts it is evident that greater government pre-planning and discipline is required for a PPP than a traditional model. The contract drafting could be improved with greater access to end-users throughout the process."
Ray Wilson, Director, Plenary.

In their diligence to be independent, governments risk losing valuable insights to improve services and facilities to the community. Insights from end-users can be invaluable for the private sector in assessing the requirements for the project and preparing their bids. For example, the successful design process for the first NSW Schools PPP gathered insights from teachers and principals. Their knowledge of classroom management and curriculum delivery was fed into the facilities design, providing a material impact. As Geoff Barnsley, Executive General Manager Operations, Spotless explains:

"Sharing information allows us to better understand how the project will function in practice, so we can provide a pragmatic solution. Workshops in the initial stages of planning and development can establish rapport with stakeholders and ensure a high level of understanding and appropriate expectations are established."

... and through construction

Participants in the survey also identified that the project benefits from ongoing discussion with the public sector stakeholders and end-users during the construction phase. Interviewees advocate a framework of formal regular meetings to support the contract and strengthen relationships between parties.

As Norm Jagger, Queensland Southbank Institute of TAFE Project Director explains:

"A general theme of the construction phase is the necessity for contractors to work with the public sector. Even

[4]Partnerships Victoria Advisory Note October 2005, Interactive Tender Process

"Sharing information allows us to better understand how the project will function in practice, so we can provide a pragmatic solution."

Geoff Barnsley, Spotless

though the ultimate decision lies with the contractor, it will save them time and money to take advice from people who have experience in the industry. Throughout the construction phase, Queensland Southbank Institute of TAFE had public sector personnel devoted to working with the contractor to help them interpret and deliver the requirements of the output specifications."

Not only does engaging with stakeholders enhance project delivery, it also serves to manage the expectations of the people involved. Managing community and employee expectations is important to government.

"Where possible, engaging school principals early has been hugely beneficial to the project as they have managed the teachers and communities' expectations of the project." Terry Whyte, Project Director, NSW Department of Education PPP.

Transitioning from tender phase to delivery phase

Interviewees are mindful that the wealth of in-depth project knowledge accrued during the procurement process on both sides of the deal can be lost as soon as the contract is signed. At this point, procurement teams are replaced with project management teams who are tasked with converting the contract and specifications into reality. Procuring authorities are struggling to address this issue, given the different skill sets required for transacting and contract management.

Experience with the early PPPs has demonstrated the importance of managing an effective transition from the bidding process to the project delivery phase. Guidelines and processes need to be established to retain intellectual property in spite of the inevitable turnover in personnel. In particular, knowledge of the intent of contractual arrangements must be captured to maintain expectation levels and provide direction when adopting processes and procedures. John Thrippleton, Senior Project Officer, Corporate Services, SA Courts Administration Authority highlights:

"Rationale for key decisions made during the procurement need to be well documented, as this can save many hours for the contract managers during the later stages of the project. Having this information to hand is invaluable when negotiating issues with the operator."

Equity investors must recognise this potential loss of corporate knowledge as a risk, as Azhar Abidi, Investment Manager, Infrastructure Funds Management explains:

"Over time, you lose corporate knowledge about the intention of the parties at the time of contract execution. This is a risk for equity investors, creating a lack of certainty about the potential breadth of their future obligations."

Effective partnerships are built on relationships

Developing a working partnership is essential for unlocking the value of the PPP model. Strong working relationships that facilitate free-flowing communication produce the greatest efficiencies and smooth issue resolution.

These relationships need not be at the expense of commercial value or end-user resource time. In particular, government agencies have needed to adapt to the different working environment, balancing the demands of being an effective commercial partner, while maintaining the vigilance of probity.

The changing role of government

Once the contract is agreed the public sector should focus on developing policies and procedures that reinforce the transfer of risk to the private operator. Interviewees observed that public sector employees can assume it is easier to simply complete a task themselves rather than push the private sector operator, who has responsibility for service delivery. This is a classic risk take back, where well intentioned action can dilute or blur the responsibilities of the respective parties.

Employees need an 'intentional mindset' to adjust their behaviour. This requires clear communication and instruction within the agencies to educate staff on the division of roles and responsibilities. Furthermore, the specialist skill set for contract management must be recognised and supported in government training and remuneration scales.

To drive performance, government agencies need clear reporting and communication protocols. Interviewees identified reporting specifications and understanding of the type of information required, as areas of concern in some of the early projects. This risk reinforces the importance of establishing structured communication channels in the initial stages of a project, not only to capture information but to develop a positive framework for the relationship. Government is under greater pressure to provide proactive contract management to improve information sharing and timeliness with responses.

"For performance incentives to be effective, the public sector needs to closely monitor operations and services delivery. Projects do not run on auto-pilot. The public sector needs to invest resources in appropriate contract management if projects are to be successful." Azhar Abidi, Investment Manager, Infrastructure Funds Management.

Over the last five years, projects have improved the clarity of information requirements and increased sophistication in measuring performance.

"Knowing what you want is one thing, agreeing on how to define, measure and report it is an entirely different matter. It requires the parties to be specific and develop a strong reporting framework. In recent PPPs the Government has improved the science of specifying and measuring performance outcomes, including a greater emphasis on associated business rules, benchmark standards and improvement processes." John Iliadis, Contract Administrator, Casey Hospital.

The value of relationship

Relationships should develop such that the PPP contract acts as a framework within which the parties work in the spirit of partnership.

Interviewees recognised that having a single point of contact with an interest in the long-term viability of the project is a strong advantage of the PPP approach over traditional procurement. Government agencies value the benefits of dealing with an equity sponsor rather than the design and construction contractor during the development phase.

If the project company doesn't allocate sufficient contract management resources, they may lose the opportunity to develop a long lasting relationship. The interface with government can become strained by confusing and at times inappropriate communication from sub-contractors who do not recognise the nuances of risk allocation under the PPP contract. This issue was raised in the early PPPs, and the market has taken steps to address it by resourcing projects more appropriately at the interface with government.

"The success of the project is driven by good relationships between each of the key stakeholders. Because of these strong relationships, the PPP company operates as a responsive business partner. There is a good balance of adherence to contractual requirements with the flexibility of discussing the best allocation of resources." Neil Twist, CEO, Victorian County Courts.

In many cases, rather than using the change mechanisms in the contract, parties have found practical commercial solutions relying on good working relationships between the client and operator. Geoff Barnsley, Executive General Manager Operations, Spotless explains:

"Knowing what you want is one thing, agreeing on how to define, measure and report it is an entirely different matter. It requires the parties to be specific and develop a strong reporting framework."

John Iliadis, Casey Hospital

"The relationship is flexible enough to assist with 'outside of scope' works. Stakeholders understand that new developments required for the Institute arise and are 'outside of the scope', but it makes sense to use expertise on the ground to get the job done."

Developing working relationships between the parties has reduced the need to use disciplinary actions to manage the contract. Several of the projects surveyed use a degree of reserve in applying abatement regimes, preferring to reach a practical solution between the parties. In these situations it seems that the threat of abatement has the required effect and provides sufficient incentive on the private sector to be responsive and perform in accordance with the contract and specifications.

"A 'softly softly' approach is being taken until the project is fully established. We would rather encourage problems to be resolved to the satisfaction of the client than enforce literal interpretations of the contract that risk the necessary goodwill to produce quality solutions." Norm Jagger, Project Director, Queensland Southbank Institute of TAFE.

Interviewees stressed the importance of creating a cohesive team between the parties. If the relationship falters or is weak, the PPP arrangement can become significantly more restrictive, reverting to the ethos of traditional service contracts. Under such circumstances, contractors execute prescribed tasks in a mechanical yet efficient manner, adhering to the strict wording of a contract.

Casey Hospital image provided by Plenary

This results in a short-term focus, with a reluctance to engage and consider long term benefits for the partnership. Thus, the government agency and the equity investor must invest time and resources in creating a culture of teamwork. Ray Wilson, Director, Plenary reflects on evolving working practices in this area:

"There has been a major shift within the industry in the way companies operate to recognise the difference from being an underwriter of a project to being the client's long term partner: companies have added additional resources to manage relationships more effectively."

The journey continues

The pathfinder PPP projects surveyed demonstrate the value achievable within a supportive partnership model, beyond cost efficiency.

As well as increasing the likelihood of projects being completed on time and on budget, PPP projects can also deliver:

- High quality, well maintained facilities
- Complementary services within the main facilities
- Closer community ties
- Innovative design and management

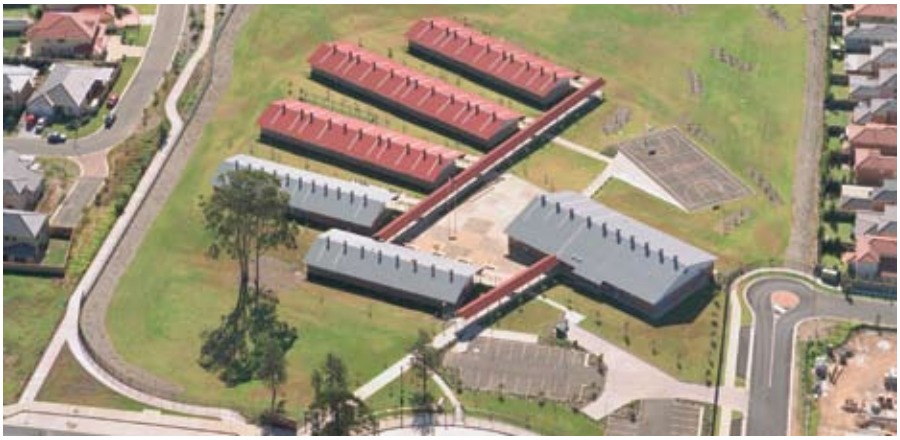
This value is likely to increase as learnings from current projects are incorporated into the next tranche of PPPs. Moreover, the large number of upcoming social infrastructure projects offers the industry an important opportunity to continue to refine the PPP model.

In the next 12 months, a further seven projects will become operational, with six social infrastructure projects in the procurement stage. These projects provide an opportunity for further examination to identify and share best practice. To this end, we recommend:

- Government agency contract managers maintain an issues and innovations log that can be shared in national contract manager forums to promote consistency and excellence.
- State governments commission contract reviews of the projects at two years post completion date and then every five years to capture and integrate best practice.
- Infrastructure Australia (IA) drive the collection of industry insights to further learning in this industry and support a pragmatic framework – this might become part of IA's review of the extent to which governments can better facilitate infrastructure investment.

Proactively building industry-wide best practice requires investment from both sides of the PPP model. We believe that investment will be more than repaid in terms of consistently successful projects that deliver high quality social infrastructure.

PPP project overviews



Kellyville Ridge Primary School image provided by New South Wales Department of Education

Southbank TAFE image provided by Spotless

NSW Schools PPP

Snapshot

- **Core service delivered**: Education. Nine new public schools in Sydney, Wollongong, Shell Harbour and the Central Coast.
- **Government department:** NSW Department of Education and Training (DET).
- **Consortium:** Axiom Education consortium (ABN Amro - sponsor, St Hilliers, Hansen Yuncken - builder and SSL Facilities Management - facilities manager).
- **Contract period:** 30 years.

The first Australian schools PPP project reached financial close in March 2003. This project has delivered nine new public schools in Sydney, Wollongong, Shell Harbour and on the Central Coast. The project was awarded to Axiom Education consortium (comprising ABN Amro, St Hilliers, Hansen Yuncken and SSL Facilities Management), who will also provide non-core services for the 30 year life of the project.

The project received a favourable report from the Auditor General in 2006, which concluded that the contracts "were established and let in a way that greatly assists their potential for delivering value for money". New South Wales Treasury also released its own post implementation review of the first schools project in October 2005. This report [5] claimed that schools "were delivered some two years earlier, on average, than would have been possible had traditional public sector funding been used. PFP delivery has enabled a faster response to demographic needs in urban growth areas."

Given the success of the first New Schools project, it is no surprise that the NSW Government sought to capitalise on the experience, rolling out a second project as part of its plan to accommodate the projected demographic needs in New South Wales' urban growth areas.

Southbank TAFE Redevelopment PPP

Snapshot

- **Core service delivered**: Education. 11 new and four refurbished buildings.
- **Government department**: Queensland Department of Infrastructure and Planning.
- **Consortium:** Axiom Education Queensland Consortium (ABN Amro - sponsor, John Holland - builder and Spotless Facilities Management facilities manager).
- **Contract period**: 34 years.

Southbank Institute is Queensland's leading TAFE, with more than 27,000 Queenslanders and approximately 1,400 overseas students being trained in diploma and advanced diploma courses each year. The redevelopment involves the construction of eight teaching blocks with 11 new and four refurbished buildings. The $550 million project was awarded to Axiom Education Queensland Consortium (comprising ABN Amro, John Holland and Spotless Facilities Management) to construct and maintain the new and renovated buildings over 30 years. Construction of stage one was completed in July 2007, with stage two set for completion by December 2008.

The Southbank TAFE redevelopment project was the Queensland Government's first private sector development partnership. Its success led to the Queensland Government embarking on much bigger projects with confidence.

[5] Privately Financed Projects (PFP) New Schools Privately Financed Project Post Implementation Review, December 2005, NSW Treasury

Mt Barker Police Station image provided by Plenary

South Australian Police & Courts Regional Facilities PPP

Snapshot

- **Core service delivered:** Justice and Law enforcement. Four new courthouses and five police stations in six sites to replace old facilities.
- **Government department:** SA Courts Administration Authority.
- **Consortium:** Plenary Justice Consortium (Plenary Group - sponsor, Deutsche Bank – bond underwriter, Hansen Yuncken – design and construction contractor, Advanced Building Technologies – facilities manager, Walter Brooke and Associates - architects and Connell Mott Macdonald – structural and services engineers).
- **Contract period:** 25 years.

The South Australian Police & Courts Regional Facilities PPP project was designed to construct four new courthouses and five police stations in six sites to replace old facilities well past their useful economic life. The $70 million project reached financial close in June 2005 and was awarded to the Plenary Justice Consortium (comprising Plenary Group, Deutsche Bank, Hansen Yuncken, Advanced Building Technologies, Walter Brooke and Associates and Connell Mott Macdonald). Plenary Group is responsible for maintaining buildings and landscaped areas and providing facilities management services for 25 years.

The South Australian Government did not enter into any hand back conditions with the Project Vehicle (PJSA) holding freehold title of all six sites. However, the State holds the first right of refusal to re-lease the facilities at the end of the term.

Victorian Correctional Facilities Project

Snapshot

- **Core service delivered:** Correctional facilities. Two correctional facilities.
- **Government department:** Corrections Victoria / Department of Justice.
- **Consortium:** Victorian Correctional Infrastructure Partnership (Bilfinger Berger BOT – sponsor, Baulderstone Hornibrook – builder and United Group with Baulderstone Services – facilities manager).
- **Contract period:** 25 years.

The EOI for the project was released in June 2002. It reached financial close in January 2004. The Project was designed to deliver two correctional centres in Victoria: the Marngoneet Correctional Centre, a 300 bed medium security correctional programme centre for male prisoners; and the Metropolitan Remand Centre, a new 600 bed maximum security prison for male prisoners on remand by courts. The $275 million project was awarded to the Victorian Correctional Infrastructure Partnership (a subsidiary of Bilfinger Berger BOT in partnership with Baulderstone Hornibrook and United Group) to design, build and maintain both prisons over 25 years.

Both prisons incorporate innovative and non-institutional designs considered best practice for prisons.

Royal Melbourne Showgrounds image provided by Victorian Department of Primary Industries

Casey Hospital image provided by Plenary

Royal Melbourne Showgrounds Redevelopment

Snapshot

- **Core service delivered:** Primary Industries.
- **Government department:** Victorian Department of Primary Industries - Major Projects Victoria.
- **Consortium:** PPP solutions (Babcock & Brown - sponsor, Multiplex Constructions - builder and Multiplex Facilities Management - facilities manager).
- **Contract period:** 25 years.

The $101 million Royal Melbourne Showgrounds Redevelopment project reached financial close in June 2005. The objective of the project was to restore key historic buildings and build new facilities to create a multi-purpose venue that could be used year-round. The Victorian Government considers the Royal Melbourne Show, which has been held in Victoria since 1853, to be a vital link between urban and rural Victoria.

The project was awarded to PPP solutions (comprising Babcock & Brown, Multiplex Constructions and Multiplex Facilities Management). The Architect for the project was Daryl Jackson. The project was completed on time, with commercial acceptance achieved in August 2006. This meant the Royal Melbourne Show in 2006 was not disrupted.

Casey Community Hospital

(formerly known as Berwick Community Hospital)

Snapshot

- **Core service delivered**: Health. 229 bed community hospital.
- **Government department**: Department of Human Services.
- **Consortium:** Progress Health Consortium (ABN Amro - sponsor, Multiplex Constructions – builder, Silver Thomas Hanley, Daryl Jackson – architects and Multiplex Asset management – facilities manager).
- Contract period: 25 years.

The $120 million project was designed to build a 229 bed community hospital. The project, which reached financial close in October 2002, was secured by the Progress Health Consortium (comprising ABN Amro, Multiplex Constructions, Multiplex Asset Management, Silver Thomas Hanley, Daryl Jackson and Blake Dawson Waldron) to design, construct and maintain the hospital building. The contract is for 25 years, after which ownership is transferred to the State of Victoria. The hospital was opened by the Premier of Victoria on 18 September 2004.

All the building related facilities maintenance was undertaken by the private sector, but the public sector continued to provide soft services, such as clinical services. The hospital is capable of delivering services to 30,000 patients and 25,000 emergency cases per annum.

Victorian County Court image provided by Victorian Department of Justice

Victorian County Court

Snapshot

- **Core service delivered**: Justice.
- **Government department**: Department of Justice, Victoria.
- **Consortium:** Liberty Group Consortium (ABN Amro / NM Rothschild & Sons - sponsors, Multiplex Constructions - builders, Honeywell Ltd – facilities manager).
- **Contract period:** 20 years.

The need for County Court accommodation arose mainly as a result of long waiting times for court appearances. The project reached financial close in June 2000 and was awarded to the Liberty Group Consortium (comprising ABN Amro, Multiplex Constructions, N.M. Rothschild & Sons, Sinclair Knight Merz, Daryl Jackson & Lyon Architects, Corrections Corporation and Interform).

Under the 20 year service contract, the Liberty Group would provide accommodation and essential services including security, maintenance and IT. The $195 million project was completed in May 2002 on time and on budget. The Liberty Group took on the design, construction and commissioning risk, except where the State had specific design requirements. The project is the first major social infrastructure project under the Partnerships Victoria policy and delivered the largest court complex in Australia.

Contacts

Bill Banks

Tel: +61 2 9248 4522
Mobile: +61 402 891 732
Email: bill.banks@au.ey.com

David Larocca

Tel: +61 2 9248 4245
Mobile: +61 439 406 124
Email: david.larocca@au.ey.com

Darrin Grimsey

Tel: +61 3 9655 2519
Mobile: +61 409 090 261
Email: darrin.grimsey@au.ey.com

Mark Wilde

Tel: +61 7 3011 3398
Mobile: +61 404 091 548
Email: mark.wilde@au.ey.com

Gordon Dunfield-Prayero

Tel: +61 2 9248 4435
Mobile: +61 400 486 063
Email: gordon.dunfield-prayero@au.ey.com

David Cochrane

Tel: +61 3 9655 2551
Mobile: +61 419 347 700
Email: david.cochrane@au.ey.com

John Matthews

Tel: +61 3 9288 8830
Mobile: +61 419 887 407
Email: john.matthews@au.ey.com

Amanda Evans

Tel: +61 8 8417 1710
Mobile: +61 424 498 170
Email:amanda.evans@au.ey.com


08

Proactively building industry-wide best practice requires investment from both sides of the PPP model. We believe that investment will be more than repaid in terms of consistently successful projects that deliver high quality social infrastructure.

Royal Melbourne Showgrounds image provided by Royal Agricultural Society of Victoria

Ernst & Young

Assurance | Tax | Transactions | Advisory

About Ernst & Young
Ernst & Young is a global leader in assurance, tax, transaction and advisory services. Worldwide, our 130,000 people are united by our shared values and an unwavering commitment to quality. We make a difference by helping our people, our clients and our wider communities achieve potential.

For more information, please visit www.ey.com/au

Adelaide
Ernst & Young Building
121 King William Street
Adelaide SA 5000
Tel: +61 8 8417 1600
Fax: +61 8 8417 1775

Brisbane
1 Eagle Street
Brisbane QLD 4000
Tel: +61 7 3011 3333
Fax: +61 7 3011 3100

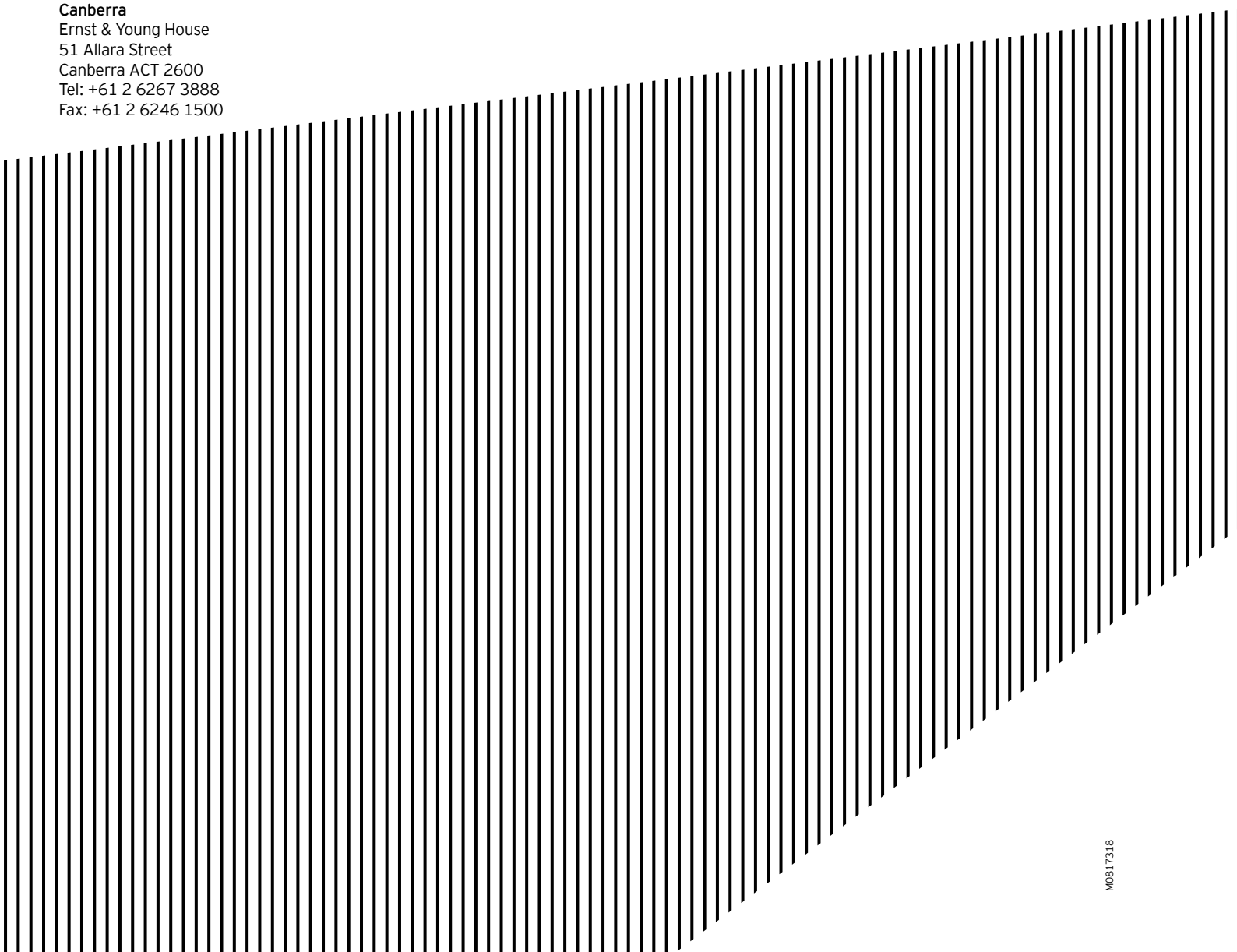
Canberra
Ernst & Young House
51 Allara Street
Canberra ACT 2600
Tel: +61 2 6267 3888
Fax: +61 2 6246 1500

Gold Coast
12-14 Marine Parade
Southport QLD 4215
Tel: +61 7 5571 3000
Fax: +61 7 5571 3033

Melbourne
Ernst & Young Building
8 Exhibition Street
Melbourne VIC 3000
Tel: +61 3 9288 8000
Fax: +61 3 8650 7777

Perth
Ernst & Young Building
11 Mounts Bay Road
Perth WA 6000
Tel: +61 8 9429 2222
Fax: +61 8 9429 2436

Sydney
Ernst & Young Centre
680 George Street
Sydney NSW 2000
Tel: +61 2 9248 5555
Fax: +61 2 9248 5959



M0817318