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New report on Australian PPPs: lessons for NZ

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A comprehensive report on some of the issues with Australian PPPs provides valuable insights for New Zealand as it moves down the PPP path.

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In May 2010, KPMG provided, to Infrastructure Australia, its report, *PPP Procurement: Review of Barriers to Competition and Efficiency in the Procurement of PPP Projects.*

Australia, with Canada and the UK, are the most mature PPP markets. For this reason, and because many issues faced by Australia apply to New Zealand, the Review provides useful insights, some of which we overview in this note. One reason is that, like Australia, New Zealand's interest in PPPs is driven not by off-balance sheet considerations but by the most suitable procurement model for the circumstances.

Most of the KPMG report is based on qualitative feedback from stakeholders such as suppliers, along with some quantitative and international information. Generally, suppliers have a high level of confidence in Australian PPPs, but with some concerns, including inconsistencies between projects and States.

PPP pipeline

The major recurring theme in the KPMG report is the adverse effect of the lack of a committed pipeline of PPPs. If the pipeline problem is sorted, some of the other issues, such as bid costs, become less significant.

For example, the report notes:[1]

> …compared with some international jurisdictions, the number of PPP projects undertaken in any year and the announced pipeline of future PPP projects in Australia is limited. Hence, bidders are reluctant to expand their teams without a clear pipeline of projects, may withdraw from the market, and will be selective about projects for which they bid, potentially reducing competition.
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> Although process inefficiencies and bid costs are in themselves a barrier to competition, the key issue identified within the Australian PPP market is the

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sporadic nature of the project pipeline and the current limited ability of existing and potential new market participants to undertake an informed assessment of likely PPP projects.

Accordingly, we recommend the implementation of processes that act to improve both the visibility and certainty as to the Australian PPP pipeline, including:

a. as early as possible announcement of potential future PPP projects

b. more consistent and rigorous application of the National PPP Guidelines on the criteria for determining whether PPP procurement is appropriate for a project

c. continued commitment and leadership from politicians and senior bureaucrats within the Commonwealth and each of the various jurisdictions in support of the use of PPPs in appropriate circumstances

d. where possible, continued focus on improving national co-ordination of the release of projects to the market by greater liaison between jurisdictions, acknowledging the difficulties in achieving this.

Pipeline: implications for New Zealand

PPPs are well established in Australia, yet the pipeline problem still exists. International suppliers are reluctant to set up shop in Australia, not knowing whether they can justify having a team based in the territory.

Given New Zealand's smaller size, and the embryonic nature of the market, this may be an even bigger problem in New Zealand, emphasising the need to deal with this pipeline consideration.

Many multi-nationals service the New Zealand market from regional offices in Australia. In this way, it's more likely that international suppliers will enter the New Zealand market.

This highlights the desirability of New Zealand coordinating its pipeline with the Australian pipeline.

Overall, it seems important for New Zealand to coordinate with Australia: for example, Australia also will help alleviate pipeline and scale problems supplemented by New Zealand opportunities. Additionally using similar processes and approaches will assist. The KPMG review points out the importance of consistent and simplified approaches within Australia. Getting uniformity between NZ and Australia seems to be a useful goal.

The KPMG Review, when dealing with the importance of a clear pipeline, emphasized the need for political buy-in. Lack of political support means that it is less likely suppliers will invest in the market.

New Zealand has a particular challenge on this, given that the last prison privatisation sector was terminated by the Labour government. For example, bidding for Wiri will overlap New Zealand's relatively short election cycle, creating further uncertainty for bidders (see below as to funding bidders' costs).

There are a number of court decisions which confirm the ability of Parliament to overturn contracts previously entered by Government (and without compensation as well). That is a risk that bidders will take into account.

One other problem a lack of a pipeline will create in the future is that, even if the odd multinational comes down and wins a particular contract, the government is not going to have additional non-contractual leverage over that provider to sort out problems. For example, given the volume of PPPs in the UK, if a firm doesn't behave on one contract, it is not likely to get another.

Financing bottleneck

Against the background of the global financial crisis, KPMG note that international financiers in the Australian PPP market, generally one of the big 4 national trading banks involved in a bid. Those 4 banks in turn often want to enter a bid along with another of the 4 banks. In effect, this can reduce viable consortia down to 2.

Lack of finance internationally is leading to differing responses internationally ranging from Government enabling finance, through to not requiring consortia to have confirmed funding at the outset, leaving this to debt competitions nearer inking of the contract, once the preferred supplier is selected.

This may be an issue for New Zealand, if not a greater issue, in part because the same banks trade in New Zealand and the same dynamics could apply to a greater extent. At least while the effects of the GFC are felt, the approach may need to take this into account, although it can be expected that Government has already assessed that a project the size of Wiri is not going to be problematic in this regard.

Paying Bidder Costs

The idea of the public sector contributing toward bidder costs is largely unheard of in New Zealand, to the point that to do so is seen as anathema.

But to encourage international players into this PPP market, away from other attractive markets, such lateral solutions may need to be considered. Benefits would amply exceed cost.

KPMG note it as a serious option for Australia, for the same reasons. It is already done in other countries such as Canada (where for some projects a third to a half of the bidder's costs are paid).

Decisions on this would be situation-specific. For example, as to Wiri, and the election cycle noted above, will potential bidders be deterred by the risk of a political reversal, unless a chunk of their costs are covered?

Whether to contribute to costs depends to a degree on the nature of the PPP project in terms of novelty, timing and technical input required to bid. For example, for some projects, upfront design costs are very large as the public sector agency wants a highly innovative and bespoke solution in a short time period. So, bidders might have to carry out significant design work.

There is also a good argument against bid costs in that it compromises the Government negotiating position. The significant upfront costs involved in bidding for PPPs mean that the bidder has a strong incentive to win the bid (not to mention its advisors who are often on contingent deals!).

Each situation can be looked at on its own merits, but benefit will often markedly outweigh cost, particularly in this small and embryonic market.

Interactive dialogue

This key issue is covered in our article, *PPPs: One-to-One Discussions with bidders*.

Skill and expertise of the government team managing the process

KPMG reports the suppliers and other stakeholders noting this as a significant issue, with some government teams lacking adequate skills and experience. This issue is recognised in New Zealand generally as to procurement, as part of MED's initiatives, and also through the establishment, in common with other countries, of a centralised National Infrastructure Unit within Treasury. Procurement specialists can make a huge difference to public sector performance. They should be remunerated and trained, with strong career paths, to foster great skills and experience.

The KPMG report notes its conclusions which equally apply in New Zealand:

> To achieve an efficient process, **it is essential that Governments have strong project teams combined with efficient and decisive governance structures**. (The same also applies to the delivery and operational phases.) The quality of the whole project team is critical to the success of the project, not just the project director. The experience and capacity of project team members responsible for managing the various disciplines required for a PPP project is important. This is often a challenge faced by Governments within standard public service pay scales. Therefore, to the extent that they do not already have them, Governments should consider implementing frameworks to further the:
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> **Q. recruitment, development and retention of high quality Government project team members, in particular the project director and key team members responsible for managing each of the various disciplines.**
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> These frameworks may include paying salaries at commercial rates, either within the public service or, more likely, as consultants. However, pay is not the only issue: other important factors include an appropriate level of empowerment and a clear career path.

To ensure timely decision-making processes, it is important that Governments aim at:

R. ensuring governance structures empower the project team to deliver the project while enabling effective and efficient decision making so as to prevent unnecessarily protracted and uncertain timeframes. …

Independent Reviews

Many high value public sector procurements in New Zealand would strongly benefit from a Gateway or similar independent review at appropriate points. But often this does not happen, often with poorer outcomes as a result. The KPMG report recommends this for Australian PPPs, and Gateway reviews are intended for NZ PPPs.

We welcome your feedback on this article and any enquiries in relation to its contents. This article is intended to provide a summary of the material covered and does not constitute legal advice. We can provide specialist legal advice on the full range of matters contained in this article.

Wigley & Company is a long established specialist law firm. Our focus includes IT, telecommunications, regulatory and competition law, procurement and media/marketing. With broad experience acting for suppliers and customers, government agencies and corporates, Wigley & Company understands the issues on “both sides of the fence”, and helps clients achieve win-win outcomes.

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