

15 November, 2006

Rodney District Council  
Private Bag 500  
Orewa

By email to [Penlink@rodney.govt.nz](mailto:Penlink@rodney.govt.nz)

Dear Sir Madam

## NZCID Submission on Rodney District Council Penlink Tolling Proposal<sup>1</sup>

### Introduction

1. The New Zealand Council for Infrastructure Development is a non profit organisation.
2. Members comprise a diverse range of private and public organisations that seek world class infrastructure developed and provided in New Zealand to help all New Zealanders achieve the standard of living to which we aspire.<sup>2</sup>
3. NZCID shares community and industry concern that there is an urgent need to upgrade access to and from the Whangapararua Peninsula by means of construction of the Penlink project in order to meet existing and future growth needs of the District and the Auckland Region.
4. The Council seeks to work with Rodney District to ensure a balanced and sustainable transport system for the District and it is with that collective vision that NZCID presents this submission on the Penlink Tolling Proposal.

### Key Points of Submission

5. This submission covers the following key points:
  - Support for timely completion of Penlink as a toll road

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<sup>1</sup> Note: This submission represents the views of NZCID as a collective whole, and may not necessarily represent the views of individual member organizations.

<sup>2</sup> Details of NZCID membership and aims and objective can be found on the website [www.nzcid.org.nz](http://www.nzcid.org.nz)

- Recommends an informative rather than prescriptive bid offer to maximise opportunity for private sector innovation
- Opportunities for savings through private sector investment
- Positive international experience with private public partnership procurement option
- The value associated with the transfer of risk as evidenced by the Tauranga Route K and Sydney Cross City Tunnel projects
- Issues to be considered when choosing the best procurement method

NZCID would welcome the opportunity speak in support of its submission at the hearings panel.

### NZCID supports timely completion of Penlink as a toll road project

6. Research undertaken by the Council clearly demonstrates that completion of Penlink will have positive social, environmental and economic outcomes and has broad community support.
7. But it is equally clear that there is insufficient funding available either from local, regional or central government sources to see the timely construction of Penlink within the foreseeable future.
8. For these reasons NZCID supports Rodney Council's initiative to proceed with construction of Penlink by means of the appropriate mix of public or private debt funding supported by tolls
9. NZCID wishes to ensure that the project is a success and delivered in accordance with Council expectations.
10. It has recently undertaken a review of best practice in the delivery of successful Public Private Partnership projects and makes the following recommendations in this regard.

### Recommend an Informative rather than prescriptive bid offer to maximise opportunity for innovation

11. Preliminary estimates of traffic volumes and estimated costs provided in the consultation documents indicate that the offer will need to be made on a negative tender basis and that the full extent of LTNZ subsidy will be required for this project to be viable as a Public Private Partnership.
12. That said, the optimum mix of funding options is best determined through a competitive bid process.
13. For these reasons NZCID does not have a view on the selection toll location points, or toll tariffs and recommends that the bid offer not be prescriptive on these issues, at least within

certain limits (such as maximum toll thresholds established through the consultation process).

14. Rather it is recommended such matters be determined as part of the bid process which in turn will be guided by information provided through the community consultation process regarding toll location preferences, willingness to pay, and relative travel time savings, congestion and diversion impacts as indicated by traffic modelling.
15. Preference is given to providing full information on each of these parameters to prospective bidders.
16. It is then up to bidders to make their own assessment of the risks associated with various levels of toll and location of toll gantries and undertake their own comparative modelling as appropriate.
17. This will maximise the competitive process and encourage innovation in design of both the corridor and the tolling system, including the level of tolls and the location of gantries.
18. The objective of the bid process is to find an optimum tolling strategy that ensures a satisfactory return on investment from the private sector perspective whilst achieving the District Councils goals to:
  - a. Advance completion of the project on or before 2010
  - b. Minimise the public sector financial contribution
  - c. Minimise congestion
  - d. Ensure public amenity and ease of use
  - e. Ensure environmental sensitivity
  - f. Achieve high standards of operation and management of the road corridor
  - g. Ensure that a highly maintained asset is returned to the District at the end of the concession period.
19. NZCID recommends Council clearly specify the project outcomes sought rather than be prescriptive as to how its desired outcomes should be achieved.

## Opportunity for procurement savings through private sector investment

20. Overseas experience has shown the benefit of private sector projects not only in terms of providing the opportunity for additional private sector funding, but also in terms of delivering cost effective procurement and operation of large scale public assets.
21. In addition to the transfer of risk from the public to the private sector, the key benefit of the PPP approach is the incentivisation that private equity investment provides.

22. This encourages innovation, a strong customer service focus to maximize revenues, and commitment to the whole of life of the project.
23. International experience has demonstrated that PPP projects have consistently provided value for money against public sector comparative models.
24. Under the public model, underestimation of project costs and/or the overestimation of traffic volumes and toll revenues can cause significant loss of public funds.
25. On the other hand, private sector involvement can reduce the risk associated with road projects by subjecting toll road proposals to true market assessment.

### Evidence from Overseas on the PPP Procurement Track Record

26. There is a wealth of information available internationally on experience with Public Private Partnerships as a procurement option.
27. Council is referred to a recent report jointly published by NZCID and member law firm Kensington Swan on Infrastructure Development in Comparative Nations. Part F of this report discusses international experience with PPPs in some detail including the relative pro and cons of their use as a procurement option.<sup>3</sup>
28. There is substantial evidence available from both the UK and Australia that demonstrates the PPP procurement track record
29. In a 1999 survey, the UK National Audit Office reports that 73 percent of publicly funded projects exceeded the agreed contract price, and 70 percent were delivered late, whereas 2003 research by the UK Treasury showed that 76 percent of PPP projects were delivered on time or rarely with no cost overruns borne by the public sector.
30. The Australian experience has been similar.
31. Sydney's M2 and Eastern Distributor projects had been sought on a negative tender basis because the New South Wales State Government had evaluated that they would not be commercially viable and sought tenders for the required subsidies that they estimated would exceed \$A60m. In the event, both winning tenders bid zero subsidies.
32. Australian states have used the PPP model to significantly advance major highway projects as listed in the following table. The total length of these corridor developments constructed in the 20 year span between 1988 and 2008 is roughly equivalent to the entire length of the NZ

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<sup>3</sup> A copy of the report is available at <http://www.nzcid.org.nz/infrastructuredevelopmentincomparativenationsinsightsfornz.html>

State Highway network.

### Major Urban Tolls Roads in Australia Built in Much Shorter Time Frames than NZ

Project	Length km	A\$m Value	Start	Finish
Sydney M4	12.5	246	1988	1992
Sydney M5	21.0	380	1988	1992
Sydney Harbour Tunnel	3.0	685	1988	1992
Sydney M2	20.0	644	1994	1997
Sydney Eastern Distributor	6.0	700	1997	1999
Sydney Cross City Tunnel	2.1	680	2000	2005
Sydney Westlink M7	40.0	1,500	2002	2006
Sydney Lane Cove Tunnel	3.6	1,100	2002	2007
Melbourne City Link	22.0	1,780	1996	2000
Melbourne Eastlink	40.0	2,500	2005	2008
Total	170.2	\$A10,215		

33. Of particular note are the very short construction time frames that are being achieved in comparison to smaller projects in New Zealand.
34. One of the key benefits of the PPP procurement option is the incentive it provides to achieve early completion of a project in order gain toll revenues as soon as possible.

#### Lessons to be learned from Cross City Tunnel Project in Sydney

35. Despite the success of these projects, the Cross City Tunnel project has been subject to substantial controversy and has led to some adverse concern about the introduction of PPPs in the NZ context.
36. However it is important to understand the context in which this situation has arisen. A key contributing factor was a decision by the New South Wales Road Transport Authority in 2002 that the project must be delivered at "no net cost" to the State Government. This policy

decision precipitated a number of changes to the project, including changes to the above ground streets to increase traffic volumes and toll revenues thereby increasing the amount of private sector capital that could be introduced into the project. As a result there has been a public outcry at the level of tolls being charged and the closure of local roads to through traffic and usage of the new tunnel has been well below expectation.

37. Notwithstanding the reduced traffic volumes, the project was opened eight months early, and, unlike the Route K situation in Tauranga the full cost of the reduced revenues has fallen on the private sector equity owners, a cost that might well have otherwise fallen on the State Government.
38. Dr Kerry Schott, Executive Director, NSW Treasury to the Select Committee which reported on the project: noted:

"The fact remains that the project delivered a very successful engineering outcome in a more difficult than average construction environment. One cannot find too many projects that require tunneling under a major city with complex interchanges, for example, with existing water structures and pipes, and yet deliver construction before time and on budget." <sup>4</sup>

### Risk Transfer - Tauranga Experience with Route K

39. The risk associated with viability of traffic volumes has been clearly demonstrated in New Zealand with the Tauranga Route K project which has failed to attract the number of vehicles projected when the council sought special tolling legislation to build it.
40. Tauranga City Council debt financed the project with debt repayment being funded from toll revenues.
41. Debt financing provided an apparent advantage at the time in that it attracted a lower rate of interest than an alternative finance package consisting of private sector debt and equity with the financiers accepting the risk of project revenues not reaching predicted levels.
42. In this case, actual toll revenue has not matched projected revenue and the shortfall has had to be met by ratepayers. As of June 2005, toll revenues represented only \$1.3m (34%) of the \$3.8m total cost of service.
43. The consequential loss of \$2.5m represents a negative 5.6% annual return on the original construction cost of \$44.7m – considerably more than any saving on a lower cost of finance.

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<sup>4</sup> Dr Kerry Schott evidence to Select Committee Report on Cross City Tunnel available at <http://www.parliament.nsw.gov.au/prod/parlment/Committee.nsf/v3listreports?open&vw=v3currentreportsbyinquiry>

44. As such, Route K clearly illustrates the potential value of accessing private sector investment and finance in exchange for the mitigation of a key project risk to the public sector.
45. It is difficult to see how the Tauranga Route K project would have proceeded as a private toll project had the proposition been tested in the market, or, if it had, the risk would have been much more clearly exposed at the time.
46. However, the fact that the project is a net cost to rate payers doesn't mean the toll project is a failure.
47. Had it been procured in the traditional sense, without tolling, most of the costs of the project would have still been funded by rate payers.
48. Although the cost of collection of tolls is relatively high at 44% of revenue, toll revenues nevertheless exceed the cost of collection by approximately \$700,000 per annum.
49. This is revenue that otherwise would not be available to offset project costs.
50. Moreover, the overall social and economic benefits of the project must be valued against the costs in order to judge the overall benefits of advancing this project assisted by toll funded debt.

## Conclusion - Choosing the best procurement method

51. Overall, the appropriate procurement structure for a project is that which provides the best value for money for the project.
52. Value for money is a concept embracing efficiency, effectiveness and economy rather than just least cost. The value for money drivers in different procurement structures are:
  - a. An appropriate association of risk between the parties
  - b. A procurement structure which optimizes the whole of life costs over the life of the project
  - c. An output based specification, reducing the complexity and risk for the public sector procurer
  - d. Sufficient flexibility to allow for changes in service requirements over time, while providing sufficient certainty over what is required
  - e. Appropriate incentive structures for the private sector to deliver services in a timely and efficient manner

- f. Risk management expertise through external due diligence or specialist risk management providers
- g. A consideration of the costs of finance and the ability to access revenue to service debt

## Opportunity to be Heard

53. NZCID confirms its desire to address the hearings panel in support of its submission.

Yours faithfully,



Stephen Selwood  
Chief Executive