



New South Wales
Government



Working with Government

Guidelines for Privately Financed Projects



November 2001



**New South Wales
Government**

Working with Government

Guidelines for Privately Financed Projects

November 2001

© 2001

This work is copyright. Apart from any use as permitted under the Copyright Act 1968, no part may be reproduced by any process without written permission.

NSW Government
Level 37, Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000

Telephone: +61 2 9228 3200
email: wwg@premiers.nsw.gov.au
web: <http://www.nsw.gov.au/wwg>

ISBN 0 7313 3135 4

Acknowledgement. These guidelines draw heavily on the *Partnerships Victoria* guidance material, particularly Section 5: Risk Management, Section 6: Contractual Issues and Section 7: Public Sector Comparator. Appendix 3: Risk Table, is substantially reproduced from *Partnerships Victoria* guidance material.

The New South Wales Government thanks the Victorian Government for their permission to reproduce extracts from the material and acknowledges the excellent work of the Victorian Department of Treasury and Finance and their team of consultants.

Copyright in the reproduced material belongs to the State of Victoria.

What are these Guidelines about?

These guidelines are about a means of establishing a partnership between the public and private sectors. The aim is to deliver improved services and better value for money, primarily through appropriate risk transfer, encouraging innovation, greater asset utilisation and integrated whole-of-life management.

The guidelines provide a framework that enables both sectors to work together to improve public service delivery through private sector provision of infrastructure and related non-core services. They describe a competitive and transparent mechanism to pursue opportunities that bring together the ideas, experience and skills of both sectors to develop innovative solutions to meet the community's needs, expectations and aspirations.

This does not mean privatisation of public services; the Government will continue to deliver core services. While the distinction between core and non-core services will be determined case by case, it is clear that teaching services in education and clinical services in health for example are core services. All projects covered by these guidelines will undergo an evaluation to ensure they are in the public's interest.

What do the Guidelines cover?

The guidelines specifically cover Privately Financed Projects (PFPs), which are part of the broader spectrum of Public Private Partnerships (PPPs).

PPP is a general term covering any contracted relationship between the public and private sectors to produce an asset or



Photograph courtesy Department of State and Regional Development.

deliver a service. These guidelines cover PFPs only. Other types of PPPs are already covered by the NSW Government Procurement Guidelines.

What distinguishes a PFP?

PFPs, as a specific form of PPP, involve the **creation of an asset through private sector financing and ownership** control for a concession period. The **Government is willing to contribute** through land, capital works, risk sharing, revenue diversion or purchase of the agreed services.

PFPs cover economic and social infrastructure and typically include both a capital component and an ongoing service delivery component.

PFPs are generally **complex** and involve **high capital costs**, lengthy contract periods that create **long term obligations**, and a **sharing of risks** between the private and public sectors. They therefore require careful consideration and approval by the Budget Committee of Cabinet.

Who are the Guidelines for?

- these Guidelines are applicable to all NSW Government agencies, including public trading enterprises and State-owned corporations
- councils are encouraged to follow best practice by adopting similar requirements but local government is not bound by these guidelines
- private sector parties involved in PFPs with the NSW Government.

What's in it for you?

For Government agencies, contracting the delivery of infrastructure and non-core services to the private sector creates opportunities to deliver improved public services more cost effectively. Agencies can focus their own efforts on the delivery of their core services, and use the savings generated to improve or expand other services.

PFPs provide the construction, service and finance industries with opportunities to generate efficiencies and cost-effectiveness in delivery of infrastructure and non-core services through innovation and specialist expertise, and to develop their businesses by doing so.

Contents

- What are these Guidelines about? _____ iii

- 1 Introduction** _____ **1**
 - 1.1 What is a PFP and what do these guidelines cover? _____ 2
 - 1.2 What’s new? _____ 4
 - 1.3 Advantages for all _____ 5
 - 1.4 A national approach _____ 5

- 2 Identifying PFP Projects** _____ **7**
 - 2.1 Projects suitable for PFP _____ 7
 - 2.1.1 Infrastructure planning _____ 8
 - 2.1.2 Coordination _____ 10
 - 2.1.3 Public interest _____ 10
 - 2.1.4 Core and non-core services _____ 10
 - 2.1.5 Value for money _____ 11
 - 2.2 The ground rules _____ 12
 - 2.3 Unsolicited proposals _____ 12

- 3 Project Development** _____ **15**
 - 3.1 Phases in the Budget Committee of Cabinet approval process _____ 15
 - 3.2 Phases in the environmental and planning approval process _____ 15
 - 3.2.1 Provisions relating to Government building projects _____ 15
 - 3.2.2 Provisions relating to Government infrastructure projects _____ 17
 - 3.2.3 Relationship between the environmental and BCC approvals processes _____ 17
 - 3.3 Project definition phase _____ 19
 - 3.3.1 Direct negotiations _____ 20

3.4	Expressions of interest and shortlisting phase _____	21
3.4.1	Call for expressions of interest _____	21
3.4.2	Generic criteria _____	22
3.4.3	Local industry participation _____	22
3.4.4	Evaluation and shortlisting _____	22
3.5	Detailed proposals and assessment phase _____	24
3.5.1	Accounting treatment _____	24
3.5.2	Unbundling financial models _____	25
3.5.3	Purchase of intellectual property from unsuccessful bidders _____	26
3.6	Negotiations and contract phase _____	26
3.6.1	Budget Committee of Cabinet requirements _____	26
3.6.2	Statutory approval under the PAFA Act _____	26
3.6.3	Reimbursement of reasonable bidding costs _____	27
3.7	Disclosure and implementation phase _____	27
3.7.1	Contract summaries _____	27
3.7.2	Progress reports _____	28
3.7.3	Transition _____	28
3.7.4	Post implementation review _____	28
4	Project Management Structure _____	29
4.1	Steering committee _____	29
4.2	Project manager _____	30
4.3	Probity auditor _____	30
4.4	Project team _____	30
4.5	Budget Committee of Cabinet review _____	31
4.6	Treasury Private Projects Branch _____	31
5	Risk Management _____	33
5.1	The risk management process _____	33
5.2	Risk categories _____	34

5.2.1	Site risk	34
5.2.2	Design, construction and commissioning risk	34
5.2.3	Sponsor risk	35
5.2.4	Financial risk	35
5.2.5	Operating risk	36
5.2.6	Market risk	36
5.2.7	Network and interface risk	36
5.2.8	Industrial relations risk	37
5.2.9	Legislative and Government risk	37
5.2.10	Force majeure risk	37
5.2.11	Asset ownership risk	37
5.3	Risk matrix	37
6	Contractual Issues	39
6.1	Payment mechanism	39
6.2	Performance measurement	39
6.3	Dealing with risks that are difficult to allocate	39
6.3.1	Material adverse effect regimes	40
6.4	Benefits of risk	40
6.5	Tenure and access	40
6.6	Variations	40
6.7	Availability	41
6.8	Employment issues	41
6.9	Force majeure	41
6.10	Insurance	42
6.11	Default and remedies	42
6.12	Government step-in	42
6.13	Termination	43
6.14	Dispute resolution	43
6.15	Intellectual property	43

7 Public Sector Comparator	45
7.1 The role of a Public Sector Comparator	45
7.2 Approaches to constructing a PSC	46
7.3 Economic infrastructure	47
7.4 Social infrastructure	48
7.5 Technical issues	48
8 Probity and Accountability	49
Appendices	51
Appendix 1. Glossary	
Appendix 2. Public Interest Evaluation	
Appendix 3. Risk Table	
Appendix 4. Proformae	
Appendix 5. References	
Appendix 6. Contacts	

1 Introduction

The Government is committed to providing the best practicable level of public services to the people of NSW. Key factors contributing to this are the achievement of value for money and the delivery of service solutions that best meet the community's needs and aspirations. To this end, the Government has engaged the private sector in the delivery of services and associated infrastructure to the public.

This is not new; indeed full public sector provision of infrastructure is rare and NSW Government guidelines for private financing of infrastructure have been promulgated since 1989. Projects such as the Olympic facilities, the tollways around Sydney, and the Opera House car park are examples of successful partnerships between the public and private sectors.

The Government is now looking to expand private sector involvement in economic infrastructure into areas of social infrastructure, such as health and education. The goal is to deliver better services and maximise value for money by facilitating innovation, appropriately transferring risk and integrating whole-of-life management.

While the Government will still deliver core services, the distinction between core and non-core services will be determined on a case-by-case basis. Teaching services in education and clinical services in health are clear examples of core services.

These guidelines were developed after an extensive review of current procedures. Following the release of the *Working with Government* Green Paper in November 2000, there was extensive consultation with all interested parties. The aim of these guidelines is to provide a consistent, efficient, transparent and accountable set of processes and procedures needed to select, assess and implement Privately Financed Projects (PFPs).

This NSW Government policy initiative offers new business opportunities for the private sector and new mechanisms by which public sector agencies can deliver better services and infrastructure. Together the Government and the private sector can develop long-term partnerships that combine the skills, experiences and ideas of both to produce innovative solutions to public needs.

1.1 What is a PFP and what do these guidelines cover?

The New South Wales Government engages the private sector in public service delivery in many ways, which may be broadly termed public private partnerships (PPPs). PFPs, the subject of these guidelines, are one type of such engagement.

PFPs create new infrastructure assets and deliver associated services through private sector financing and controlling ownership. Financing and ownership are features of projects covered by these guidelines, distinguishing them from outsourcing of services to the private sector or infrastructure procured by conventional methods such as design and construct.

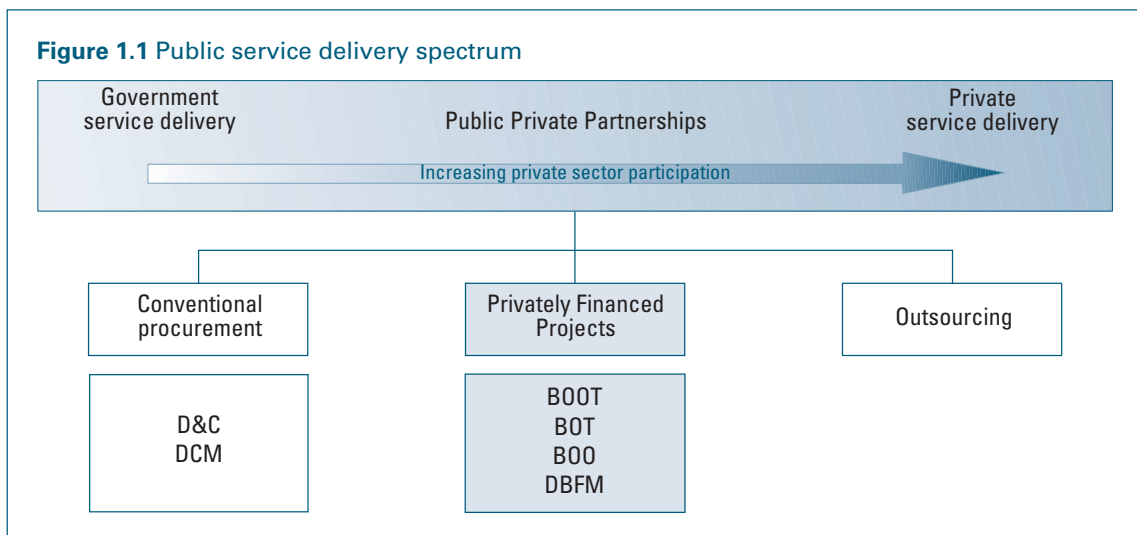
All PPPs can make a very valuable contribution to the delivery of public services in NSW and are therefore

encouraged by government. The challenge to the public and private sectors is to determine the most effective and efficient means of service delivery in a partnership arrangement that is beneficial to both.

The reason for having a distinct set of guidelines for PFPs is that PFPs raise unique issues and risks for government stemming from private sector financing and ownership and the very long-term nature of the commitments involved.

The development and approval of outsourcing and conventional procurement are subject to normal contracting arrangements.¹ They are not subject to **these guidelines, which apply to PFPs only.**

The relationship between PFPs and PPPs is illustrated in Figure 1.1.



¹ Refer to the NSW Government Procurement Guidelines at: <http://www.dpws.nsw.gov.au/DPWS/Policy/Publications/>

The principal features of a PFP to be considered under these guidelines are:

- a service normally provided to the public by government involving the creation of an asset through private sector financing and ownership control
- a contribution by government through land, capital works, risk sharing, revenue diversion or other supporting mechanisms.²

PFPs encompass both the creation of a new asset and the delivery of some services associated with the asset for a defined, but typically very long, period. The balance of total project value between the asset creation and ongoing service delivery components may vary greatly from project to project. In a capital-intensive project, such as a toll road, asset creation is likely to dominate. In projects such as schools, courthouses and hospitals, the long-term service delivery component is likely to be larger, even with the public sector providing core services.

PFPs are typically complex and involve high capital costs, lengthy contract periods involving long-term obligations and a sharing of risks and rewards between the private and public sectors. PFPs differ from

other PPPs in this regard. Because PFPs require careful consideration, the Budget Committee of Cabinet (BCC) will review and progressively approve the projects at each phase of their development.³ Separate environmental and planning approval is required.

These guidelines are applicable to all NSW Government departments and authorities, including public trading enterprises and State-owned corporations.

Infrastructure provided by local government is not bound by these guidelines, but councils are encouraged to follow best practice by adopting similar requirements. At an early stage in all infrastructure proposals involving private sector finance, councils will also have to consider the need to comply with borrowing limits and Loan Council reporting requirements.

Unsolicited proposals from the private sector that include privately owned and financed infrastructure are also considered under these guidelines.

For projects where it is not clear whether the procedures in these guidelines should apply, agencies should contact the Treasury Private Projects Branch for advice.

² See also *Public Authorities (Financial Arrangements) Act 1987*, especially Section 5A.

³ Although PFPs will normally be large projects or bundles of smaller projects with a total contract value of \$20M or more, occasionally a smaller project may be developed as a PFP. For PFPs costing \$5M or less in total, the BCC has delegated approval authority to the Treasurer. Refer to Treasury Circular 98/5, available on the world wide web at: <http://www.treasury.nsw.gov.au/pubs/98tcirc/9805.htm>

1.2 What's new?

In the future, the Government will:

- extend the range of application to include more social infrastructure
- open up opportunities for private partnership in the delivery of services as long as this results in net benefits to the community.

Among the Government's goals are: modern integrated transport systems; schools that provide excellent learning environments; and hospitals that enable high-quality total patient care. In other words, efficient and cost-effective services and infrastructure that meet the current and future needs of the people of NSW.

The aim of these initiatives is to provide long-term value for money by creating more modern, efficient infrastructure. PFPs should support better services and minimise operating and maintenance costs through the innovative application of new technology. As well as new infrastructure, a PFP project can also target the replacement or renovation of ageing infrastructure that is inefficient in delivering services, costly to maintain, or of poor quality.

In considering a project for selection as a PFP, the associated services delivered to the public will be carefully assessed and classified as either:

- core services, which must be delivered by the public sector
- non-core services, which may be delivered by the private sector where it can offer greater value for money.

The specific changes associated with these guidelines are:

- an evaluation of broader public interests to be undertaken before any project is offered as a PFP
- risk management procedures to ensure that all project risks are properly valued and allocated to the party best able to manage them
- the Public Sector Comparator (PSC), the hypothetical risk-adjusted cost of government delivering the required project outcomes, will be calculated to enable true comparisons between service delivery options
- a State Infrastructure Strategic Plan (SISP) will be published annually
- the Director-General of Premier's Department will be the initial point of contact for unsolicited proposals from the private sector
- a Private Projects Branch in NSW Treasury to:
 - ensure application of these guidelines
 - advise the Government and government agencies
 - provide economic and financial expertise in assessing PFPs
 - promote best-practice PFPs
- a NSW Infrastructure Council, comprising key Ministers and invited chief executives of private sector organisations representative of those involved in the provision of infrastructure.

Some details related to the implementation of these guidelines are still evolving and are not included in these guidelines. The structure of a PSC, selection of an appropriate discount rate for comparison of alternatives, and budget treatment of capital and recurrent expenditure are all examples where change is expected as experience is gained. Details of these and other such areas will be promulgated in implementation guidelines and Treasury circulars.

1.3 Advantages for all

This new policy offers outstanding opportunities for agencies to deliver better public services more cost effectively by focussing on delivering their core services, and to use the savings generated to improve other services. It provides the construction, service and finance industries with opportunities to generate efficiencies and cost effectiveness in delivery of infrastructure and non-core services through innovation and specialist expertise, and to develop their

businesses by doing so. It offers investors, including superannuation funds, major opportunities for investment within Australia. Above all, it offers all of us the opportunity to work in partnership to make NSW a better place to live, work and do business.

1.4 A national approach

During the consultation process associated with the *Working with Government* Green Paper⁴ it was strongly suggested that a consistent approach to PFPs in Australia would enhance the development and evaluation of proposals, increase confidence in the processes and reduce transaction costs. These guidelines respond to this suggestion by providing procedural consistency with the recently published *Partnerships Victoria* guidance material⁵, particularly in relation to risk allocation, other contractual issues, and the construction of the PSC. The Government will encourage other Australian states and territories to follow suit.

⁴ *Working with Government—Private Financing of Infrastructure and Certain Government Services in NSW*. NSW Government, 2000.

⁵ The New South Wales Government thanks the Victorian Government for their permission to reproduce extracts from the material and acknowledges the excellent work of the Victorian Department of Treasury and Finance and their team of consultants.

2 Identifying PFP Projects

In considering whether future economic and social infrastructure projects are suitable as a PFP, particular consideration will be given to large projects with clearly definable and measurable service requirements and scope for risk transfer.

2.1 Projects suitable for PFP

Projects likely to have potential to provide value for money using a PFP delivery method are those with some or all of the following attributes:

scale—normally projects with a total contract value of \$20 million or more; a number of small, similar projects that can be bundled; or a regional infrastructure management package

duration—long service delivery periods, possibly up to 25 years or more

service focus—clearly definable and measurable output specifications, suitable for payment on a services-delivered basis

non-core activities—significant non-core services and support activities that currently divert management and skilled staff in the public sector

high maintenance—alternatives to old infrastructure with high operating costs

technology—scope for cost savings and improved services through new technology

risk allocation—capacity to allocate significant risk to the private sector

complexity—complexity and other features that encourage innovative solutions

market appetite—a real business opportunity that will attract a number of competent bidders.

When deciding upon an appropriate form of delivery of particular public infrastructure services, government considers whether:

- the project is consistent with the agency's capital investment strategic plan (CISP)
- the project is of a significant scale or complexity
- the project is in the public interest
- the project relates wholly or partly to the provision of non-core services
- private sector involvement will deliver value for money.

2.1.1 Infrastructure planning

While the BCC approves projects, individual agencies are responsible for planning and providing infrastructure. The Infrastructure Coordination Unit (ICU) in Premier's Department is responsible for inter-agency coordination and the maintenance of a long-term, whole-of-government outlook.

Agency planning

Service delivery strategic planning is an essential part of the NSW Government's planning framework. The framework focuses agencies' planning on achievement of whole-of-government outcomes. In this context, a service delivery strategy turns the broad aims of an agency into the specific service outcomes it plans to deliver. It also provides the initial indication of the resources required to deliver the service. Agencies review and develop service delivery strategies as part of their annual business planning process, examining options for improving value for money in delivering required services to the community.

The planning that leads to new infrastructure should take the following steps:

- define the relevant corporate goals and service outcomes of the organisation and ensure consistency with the overarching government plans, such as transport and metropolitan and regional development. In defining the goals and outcomes, the strategic planning of other agencies should be considered along with opportunities for collaboration and integration to achieve these outcomes
- examine opportunities to improve the performance of existing infrastructure
- consider demand management and non-construction service delivery strategies to refine project objectives, needs and scope
- consider the broad community needs, values and preferences and environmental and economic context in identifying potential output and performance targets to meet the required service outcomes of the organisation
- define the outputs and performance targets of infrastructure needed to meet the required service outcomes of the organisation.

Wherever practicable, an outcomes approach should be adopted by agencies to define their requirements.

The United Kingdom's Defence helicopter pilot training project is a demonstration of the advantages of such an approach.

- the first time the Ministry of Defence involved the private sector in training military pilots they called a tender for the maintenance of the helicopters according to the manufacturers maintenance manuals
- when the contract was renewed the specification was amended to a requirement for 25,000 hours of helicopter flying time per annum, with the contractor being made responsible for supplying the aircraft. Under this PFP approach the number of aircraft involved in delivering the

service was reduced from around 60 to just 47

- the next generation of contract is expected to be based on a specification that requires the delivery of a number of pilots per annum trained to the military’s specifications. Under this approach, which enables maximum innovation, further cost reductions are anticipated through a further reduction in the number of aircraft used and a greater use of simulators.

This demonstrates that for what is essentially the same requirement in terms of trained pilots, the contractor is able to innovatively use aircraft, simulators and other training methods to halve the number of aircraft required and reduce the cost of providing the service significantly.

Agencies should therefore embark on new infrastructure projects only after they have undertaken detailed planning of their requirements and are satisfied that these requirements cannot be met by existing

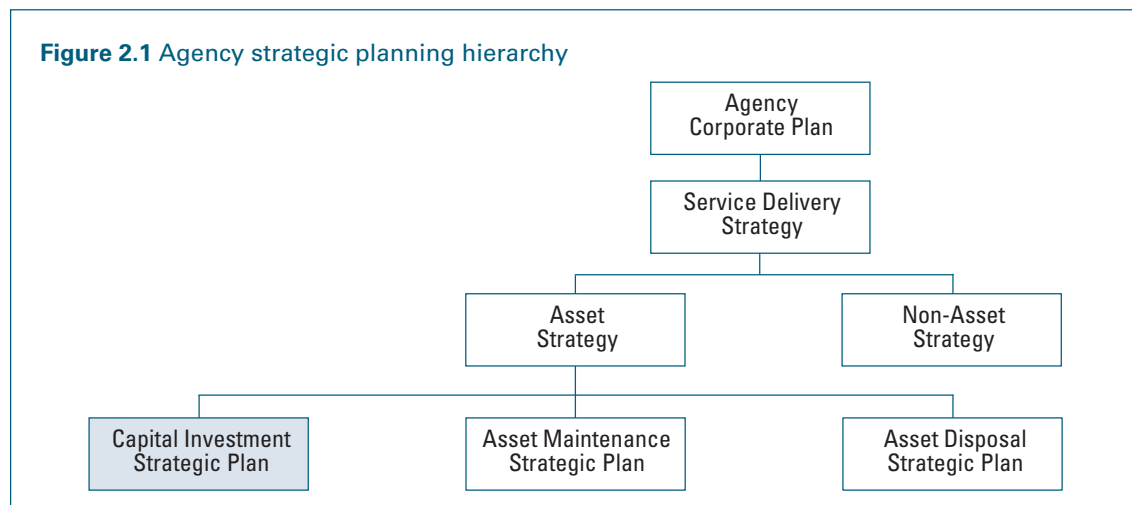
means. The Government is not in the business of building infrastructure for the sake of having infrastructure.

Where new capital works are considered the most cost-effective option for service delivery, the agency will include the requirement in its CISP. As one part of an agency’s asset strategy (of which there are three), the CISP must ensure that its asset portfolio meets its intended service delivery outcomes, now and in the future. Together, the plans provide a whole-of-life picture of construction, ownership and maintenance of public infrastructure.

Agencies will maintain a CISP providing detailed development plans for the first five years and a broad outline for the following five years. Once agencies have identified service-related infrastructure needs in their CISPs, they can proceed to define specific procurement projects.

PFP proposals, including unsolicited proposals, must be consistent with agencies’ service delivery strategies and supporting

Figure 2.1 Agency strategic planning hierarchy



CISPs that are approved during the annual budget cycle. Agencies identify PFPs in their CISPs in partnership with Treasury and ICU.

The NSW Government Total Asset Management Manual⁶ describes agency planning for the acquisition of new infrastructure.

2.1.2 Coordination

The ICU was formed in April 1999 to facilitate better provision of services for the people of NSW by integrating the Government's strategic directions and infrastructure decision-making processes.

It does this by strengthening the links between:

- urban management strategies
- regional development strategies
- infrastructure planning and provision
- the budget process.

State Infrastructure Strategic Plan

Based on the CISPs from each agency, the ICU will develop a consolidated annual SISP for the following ten years for approval by Cabinet. This plan will forecast the Government's infrastructure requirements and identify PFP opportunities throughout the State, including rural and regional NSW. It will assist the private sector to identify commercial opportunities, target its resources and generate proposals. The plan will be updated annually. Because of the

uncertainties of long-term planning, the SISP will contain more specific detail in the early years and broader definition in the outer years.

2.1.3 Public interest

PFPs are assessed against public interest criteria including:

- effectiveness
- impact on key stakeholders
- accountability and transparency
- public access and equity
- consumer rights
- security
- privacy.

The public interest question must be addressed before a project is put to the market. A project can only be considered suitable as a PFP if mechanisms (eg. contractual and regulatory means) can be established to satisfactorily meet the public interest.

See Appendix 2 for guidelines for evaluating public interest.

2.1.4 Core and non-core services

Core services, which must be delivered wholly by government, fall outside the PFP framework. In this context core services relate to the physical delivery of public services, such as clinical services in health and teaching in education. However, even where government retains delivery of core

⁶ Available from the Department of Public Works and Services, or at: <http://www.gamc.nsw.gov.au/tam2000>

services, the private sector may be able to contribute to their efficient delivery. Providing accommodation and supporting services to house core service delivery is an example of how they may do this.

Government will decide the point at which core services finish and private sector service provision starts. This information will be provided for each PFP when expressions of interest (EOI) are sought.

2.1.5 Value for money

All PFPs are to be the subject of a comprehensive economic appraisal.

By working together, industry and government can provide improved service delivery and significant cost savings. The Government aims to maximise the value for money it achieves over the life of PFPs.

The major value-for-money drivers are:

improved risk management—more rigorous risk evaluation and transfer to the private sector of those risks it is best able to manage, including those associated with providing specified services, asset ownership and whole-of-life asset management

ownership and whole-of-life costing—efficiency is improved because design and construction become fully integrated up-front with operations and asset management. Ongoing service delivery, operational, maintenance and refurbishment costs become a single party's responsibility for the length of the concession period



Photograph courtesy Department of Education and Training.

innovation—wider opportunities and incentives for innovative solutions to deliver service requirements. Opportunities may include:

- **bundled services**, through a package deal for all non-core services
- **included upgrades**, of associated and complementary infrastructure
- **packaged information systems**

asset utilisation—reducing costs to government, as a sole user, through more efficient design to meet performance (ie. service delivery) specifications and by creating complementary opportunities to generate revenue from use of the asset by others

whole-of-government outcomes—contained within the objectives and strategies of the NSW Government's Procurement Policy. These include non-asset and non-price related value-adding outcomes of wider interest to the Government, such as socio-economic and environmental outcomes.

Value for money will be determined by evaluating the project's costs and benefits. A key quantitative tool in this evaluation is the PSC (see Section 7). However, to ensure objective evaluation a range of technical, economic and social criteria will also be used (see Section 3.4.2).

2.2 The ground rules

In pursuit of openness and fair dealing, the following principles apply to all PFPs:

- the Government will maintain a competitive and transparent process to provide a fair opportunity for all prospective private sector participants
- no direct negotiations will be considered unless approved by the BCC, whose decision will be made public
- the Government will not guarantee private sector borrowings and will not take an equity share-holding
- the Government may contribute land, capital works or some form of revenue diversion
- information on contracts and tenders will be treated in accordance with the Premier's Memoranda on the disclosure of information on government contracts with the private sector
- delivery of services must be consistent with the National Competition Policy and the Competition Principles Agreement
- the Government is committed to all public projects meeting the obligations of the *Environmental Planning and Assessment Act 1979* (EP&A)
- the Government will require fair and equitable treatment of public employees who may transfer to a private employer as part of a PFP
- maximum Australian and New Zealand industry participation is to be encouraged
- the Government may consider reimbursement of bidders' reasonable bidding costs if, for reasons unrelated to any commercial or technical aspect, a project is prematurely terminated after the call for detailed proposals
- after contracts between the Government and private sector parties have been signed, contract summaries will be prepared, audited, and then tabled in Parliament within 120 days of the contract becoming effective
- these guidelines are to be implemented in a professional, fair, equitable and open manner, ensuring probity and minimisation of tendering costs.

2.3 Unsolicited proposals

Unsolicited proposals can provide a source of innovative ideas about how to improve the delivery of government services. As with all projects, unsolicited proposals must demonstrate an overall community benefit

and be consistent with the Government's plans and priorities. Commercial viability alone will not be sufficient to gain government support.

The Director-General of the Premier's Department is the first point of contact for unsolicited proposals. This will allow opportunities to be captured as they present, and timely and comprehensive feedback to be provided to the proponent. The Director-General will refer single agency proposals to that agency; proposals with a cross-agency element and new initiatives (ie. they are not currently part of the Government's plans or priorities) need wider consideration. The Premier's Department will consult with relevant agencies to assess the merits of a proposal and determine where it fits in the relative priorities of agencies. The SISP will be used to benchmark the proposal against current priorities and gauge its impact on other projects.

The Director-General will advise proponents:

- of the applicability of these guidelines to their proposal
- of additional information required to facilitate further consideration
- of the process and timetable for a preliminary assessment
- about how the ICU might assist them with these processes.

The Director-General will also inform proponents of the outcomes of the preliminary assessment.

The Government will not reimburse any costs incurred by a proponent in developing and presenting an unsolicited proposal.

Where a promising proposal has a broader focus than a single agency, the Director-General will appoint a lead agency to develop it in accordance with Section 3 of these guidelines. During this process, the Government will normally test unsolicited proposals in the market place through competitive tendering. The aim is to maximise both financial efficiencies and effective service delivery.

Requests to bypass the competitive tendering process and negotiate directly with the Government must be approved by the BCC. Approval will only be granted where the proponent can show that it is warranted (ie. the intellectual property or other essential elements of the proposal are significant and beneficial to the public interest). See Section 3.3.1 for further guidance.

3 Project Development

Typical PFPs are complex and involve high capital costs. Lengthy contract periods involving long-term obligations and a sharing of risks and rewards between the private and public sectors are also typical features. They require careful and deliberate consideration to ensure the true benefits of a partnership and the mutual satisfaction of both the public and private sectors.

3.1 Phases in the Budget Committee of Cabinet approval process

Once a project in an agency's approved CISP has been identified as suitable for delivery by PFP, it is developed in a five-phase process, based on progressive approval by the BCC. Table 3.1 on the next page summarises the basic process for project development.

3.2 Phases in the environmental and planning approval process

Environmental and community issues must be considered alongside financial and budgetary factors when developing and planning PFP-type projects.

At an early stage, the project should consider any obligations under local, regional or State environmental plans or policies. Other issues, such as public transport access, should be considered in consultation with the relevant agencies.

Proponents of unsolicited projects must enter into an agreement with the lead agency about the responsibilities for obtaining the relevant environmental approvals under the EP&A Act.

Under the EP&A Act, two separate regimes apply to the environmental assessment and approval of government building and government infrastructure projects. Final environmental and planning approval cannot occur until the preferred project options are finalised and full details of the project are known.

3.2.1 Provisions relating to government building projects

Plans for buildings in which government services are provided (such as correctional facilities, schools and police stations) are generally covered by Part 4 of the EP&A Act. Development applications (DA) for PFP-type projects are usually accompanied

Table 3.1 The five-phase process for BCC approval of project development

Phase	Title	Actions
1	Project Definition	<ul style="list-style-type: none"> • strategic planning • initial project development • public interest evaluation • economic appraisal • financial appraisal • preliminary accounting treatment • public sector comparator • procurement plan • develop project management structure • probity plan • preliminary risk management plan • draft EOI documentation
		<i>BCC approval to proceed</i>
2	Expressions of Interest and Shortlisting	<ul style="list-style-type: none"> • call for EOI • evaluation and shortlisting • draft call for detailed proposals documentation
		<i>BCC approval to proceed if required ⁷</i>
3	Detailed Proposals and Assessment	<ul style="list-style-type: none"> • call for detailed proposals • evaluation and recommendation
		<i>BCC approval to proceed</i>
4	Negotiations and Contracts	<ul style="list-style-type: none"> • negotiations with preferred proponent(s) • contractual agreement
		<i>BCC approval to proceed if significant variations arise in negotiations</i>
		<i>Treasurer's Approval (PAFA Act)</i>
5	Disclosure and Implementation	<ul style="list-style-type: none"> • issue contract summary • implement project • post implementation review

by statements of environmental effect (SEE). The DA and SEE are exhibited and open for public comment.

The local council is normally the consent authority, however the Minister for Urban Affairs and Planning may become the

consent authority if the project or class of projects is of State significance. There should be early consultation with the relevant consent authority to ensure that the proposed PFP is permissible under the relevant planning scheme, and appropriate for the site.

⁷ BCC guidance and approval may be required for very large projects, where there are a large number of bidders, or where there are divergent proposals to consider.

Agencies may seek a variation in zoning if a development is not deemed permissible. In general terms, councils cannot refuse DAs or place approval conditions on developments made by or on behalf of the Crown without the approval of the Minister for Urban Affairs and Planning.

3.2.2 Provisions relating to government infrastructure projects

Infrastructure projects undertaken by or on behalf of a government agency, such as roads, railway, sewerage, pipelines and transmission lines, are generally covered by Part 5 of the EP&A Act.

Agencies should ensure that the proposed activity is permissible under the relevant planning scheme. If it is not, agencies may explore options to amend the planning scheme in consultation with the local council and the Department of Urban Affairs and Planning (DUAP). Key considerations are the surrounding land uses and the appropriateness of the site for the proposed activity.

Agencies must determine whether a proposed project is likely to have a significant impact on the environment based on DUAP's guidelines.⁸ If the impacts are likely to be significant, an EIS is required and DUAP should be consulted about the scope of the EIS. If an EIS is not required, a 'Review of Environmental Factors' should be prepared to assess the environmental implications of the proposal.

An EIS will be exhibited and open to public comment. An updated description of the proposal will also be made public at this time. Issues raised through this public consultation process must be addressed in the request for development approval to the Minister for Urban Affairs and Planning.

If the Minister for Urban Affairs and Planning approves the project, any related determination by the agency's minister must be generally consistent with this approval.

3.2.3 Relationship between the environmental and BCC approvals processes

The requirements of the EP&A Act necessitate careful consideration because they may impact on value for money in PFPs. The timing of private sector involvement in the environmental planning and assessment process is important. There are two likely alternative scenarios.

Scenario 1: An agency gains approval for a project before proceeding to call for detailed proposals. The call for detailed proposals should specify the approved project definition and environmental approval conditions. Any variations to the project proposed by a private party must then be approved under the EP&A Act before implementation. The private party would normally bear the contractual risk and responsibility. This is the preferred scenario.

⁸ 'Is an EIS required?' Available from the Department of Urban Affairs and Planning web site at: http://www.duap.nsw.gov.au/assessingdev/pdf/gu_isaneisrequired.pdf

Scenario 2: When maximum scope for innovation is required, the preferred proponent is selected before the project is defined in detail. A two-stage assessment process is then required:

- first stage—commencing as early as practicable, the sponsoring agency should undertake a preliminary assessment of environmental constraints and opportunities likely to influence the development of preferred options. This should be done in consultation with DUAP and the local council and would usually involve public consultation. The agency should then include the

identified planning and environmental parameters in the call for detailed proposals

- second stage—commences after contractual agreement, which is made subject to environmental approval. Under the EP&A Act, it is preferable for the approval to remain the responsibility of the agency. The sharing of risks and costs relating to the attainment of approval and compliance with any conditions applied to the clearance must be detailed in the contract. See Appendix 3—Risk Table—Site Risks—Approvals.

Table 3.2 Relationship between approvals and environmental assessment scenarios

Phase	Title	Actions
1	Project Definition	<ul style="list-style-type: none"> • strategic planning • initial project development • strategic environmental assessment and consultation
		<i>BCC approval to proceed</i>
2	Expressions of Interest and Shortlisting	<ul style="list-style-type: none"> • call for EOI • evaluation and shortlisting • Environmental Impact Assessment (Scenario 1) • preliminary Environmental Impact Assessment (Scenario 2)
		<i>Approval under the EP&A Act (Scenario 1)</i>
		<i>BCC approval to proceed</i>
3	Detailed Proposals and Assessment	<ul style="list-style-type: none"> • call for detailed proposals • evaluation and recommendation
		<i>BCC approval to proceed</i>
4	Negotiations and Contracts	<ul style="list-style-type: none"> • negotiations with preferred proponent(s) • contractual agreement • Environmental Impact Assessment (Scenario 2)
		<i>Treasurer's Approval (PAFA Act)</i>
		<i>BCC approval to proceed if significant variations arise in negotiations</i>
		<i>Approval under the EP&A Act (Scenario 2)</i>
5	Disclosure and Implementation	<ul style="list-style-type: none"> • implement project • post implementation review

3.3 Project definition phase

Once agencies have identified service-related infrastructure needs in their CISPs, they are able to define specific projects for acquisition.

The essential elements of any proposal for private sector financing submitted by an agency for consideration by the BCC are:

strategic planning:

- consistency with the agency's CISP⁹
- consistency with the SISP
- the cross-agency and environmental, social and economic context.

initial project development:

- all feasible options (including non-capital solutions) identified and evaluated on a whole-of-life basis taking the environmental, social and economic context into consideration
- coordination with all other relevant agencies to take cross-agency impacts into account
- public interest evaluation, including proposed actions
- value management assessment¹⁰
- economic appraisal¹¹

- preliminary financial appraisal¹²
- preliminary statement of fiscal impacts in the format (PSI-2) (see Appendix 4)
- preliminary assessment of Loan Council treatment
- preliminary summary of proposed accounting treatment.

public sector comparator: (see Section 7)

- a reference project identifying the most efficient likely method of public sector delivery
- a PSC identifying the risk-adjusted, whole-of-life cost of the reference project
- identifying PSC information to be disclosed.

procurement plan:

- all feasible options are assessed and the preferred option identified
- identify regulatory issues that may impose constraints on the private sector
- preliminary assessment of opportunities for local industry participation¹³
- proposed project management structure
- reporting mechanisms
- probity plan

⁹ Refer to the GAMC web site at: <http://www.gamc.nsw.gov.au/tam2000>

¹⁰ Refer to the Total Asset Management Manual at: <http://www.gamc.nsw.gov.au/tam2000>

¹¹ Refer to the Guidelines for Economic Appraisal at: http://www.treasury.nsw.gov.au/pubs/tpp97_2/ea-index.htm

¹² Refer to the Guidelines for Financial Appraisal at: http://www.treasury.nsw.gov.au/pubs/tpp97_4/guidline.htm

¹³ Refer to the NSW Government Procurement Guidelines–Economic Development at: <http://www.dpws.nsw.gov.au/DPWS/Policy/Publications/>

- preliminary risk management plan
- community relations plan
- demonstrate the agency's capability to access resources and skills to effectively manage the process according to its timetable.

EOI documentation:

- appoint evaluation panel, including external financial and technical advisers (see Section 3.4.4)
- draft call for EOI document (see Section 3.4.1)
- EOI and shortlisting phase plan showing timings for all elements of the process that have been determined, together with any proposed changes to the standard process
- EOI evaluation plan, including criteria and management of evaluation processes. Any known probity, policy or other issues likely to impact on the tendering or evaluation processes must be disclosed to the BCC. It may be appropriate for agencies to consult with the Independent Commission Against Corruption (ICAC) on these matters. See section 3.4.2 for generic evaluation criteria for infrastructure proposals.

These requirements may seem onerous, but are comprehensive and necessary to ensure the effective use of public funds. Agencies should note that consultation with the Treasury Private Projects Branch is recommended as early as practicable so that advice can be provided on the above matters and the process to be adopted.

3.3.1 Direct negotiations

Where direct negotiation is being proposed the agency must fully demonstrate to the BCC, the reasons for and net benefits of not undertaking a competitive tender process.

The proposal must meet the conditions contained in Section 2 of these guidelines. The agency must have completed the necessary planning (outlined in Section 2.1.1) to specifically demonstrate that the project is consistent with its CISP. The agency also must have thoroughly researched the proposal and have independent evaluations confirming:

- that the proposal contains intellectual property and direct negotiation will preserve considerable benefits for the agency, the Government and the community
- that direct negotiations would provide better value for money than competitive bidding
- that the proponent has the expertise, experience and financial capacity to successfully deliver the project, and that it is not available elsewhere in the market
- the monetary value of the intellectual property.

Where direct negotiation is approved by the BCC, a public statement will be issued outlining the reasons for adopting this approach. The proponent will then be asked to provide a detailed proposal for assessment (see Section 3.5).

3.4 Expressions of interest and shortlisting phase

3.4.1 Call for expressions of interest

Having assessed the various issues of a proposal, the BCC will consider and approve, where appropriate, a call for EOI being issued to invite responses from the marketplace. The call for EOI document must address:

- maximising the scope for private sector innovation. Government's service delivery objectives are to be expressed, as far as practicable, in terms of the essential outcomes and performance-based requirements, without identifying specific solutions
- decision-making processes, including realistic time-frames and stages of the process
- criteria for evaluating EOIs
- the Government's preferred position and requirements together with key issues, such as risk sharing, pricing of services, net community benefits, government contributions and other regulatory aspects
- Australian and New Zealand industry and technology development considerations
- relevant background material, including preliminary market assessment
- environmental and land use planning studies, assessment and parameters and a copy of the approval conditions if the environmental planning and assessment approvals process has been already undertaken by the agency

- limits on the size of EOI responses, to control bidding costs and simplify assessment
- identification of intellectual property.

The call for EOI must specify that the Government reserves the right to withdraw at any time. The Government may also decide not to proceed any further with the process unless the agency receives preliminary proposals from the market fulfilling the stated requirements.

The Auditor-General should be advised of the project and the processes to be followed in seeking a preferred tenderer.

The timing of the call for EOI will depend on the characteristics of the project, agency priorities and other factors, including environmental approval issues:

- if an approval under the EP&A Act is to be based on an agency's preferred site and design parameters, the agency should provide in the EOI documentation, the approval conditions along with the EIS/SEE/REF, technical design and other project information
- if there is no approval under the EP&A Act at this stage, the agency should provide in the EOI documentation, information on strategic planning, preliminary options evaluation and any relevant preliminary environmental assessments and land-use planning studies as well as the outcome of any preliminary community consultation.

3.4.2 Generic criteria

The criteria for evaluation will be clearly stated in the call for EOI. The specific criteria used and their weighting will vary on a case-by-case basis, however, the following generic criteria should be included for each infrastructure project:

- experience in successfully designing, constructing, financing, maintaining and operating major infrastructure
- experience and capacity to undertake the particular project and deliver the required services
- experience and capacity to manage environmental and community relations matters
- financial capacity to meet the likely contractual obligations associated with the project
- design, construction, financing and operational resources available to the proponent
- the proposed approach and evidence of addressing all areas (eg. designing, constructing, operating and maintaining)
- innovative approach, and satisfying specifications, technical feasibility and quality
- net economic, social and environmental benefits and costs

- viability, likely risk to be assumed by government and its probable contribution, if any
- community and other benefits, including local industry participation, technology transfer, and other government programs.

3.4.3 Local industry participation

The NSW Government recognises the substantial economic benefits flowing from buying Australian/New Zealand (A/NZ) sourced goods and services. It is also aware of the economic benefits of maximising opportunities for local service providers to compete for government business on the basis of value for money.

Bidders will be required to prepare and submit preliminary local industry participation plans identifying how and to what extent they will incorporate A/NZ sourced goods and services.¹⁴

3.4.4 Evaluation and shortlisting

Responses to the call for EOI will be evaluated by an agency-established panel and coordinated by the project manager. External financial and technical advisers would usually support the panel. The steering committee will oversee the process, including the attendant considerations of fairness and equity, consistent with the project probity plan.

¹⁴ Refer to the NSW Government Procurement Guidelines–Economic Development at: <http://www.dpws.nsw.gov.au/DPWS/Policy/Publications/>



Photograph courtesy Department of State and Regional Development.

The evaluation panel's brief is to assess whether responses:

- indicate an overall net benefit to the Government and the community, in terms of financial, economic and social factors
- indicate preliminary viability and suitability for private sector financing and delivery of services
- are consistent with the infrastructure strategic plans.

The evaluation panel must objectively assess all proposals against weighted specific selection criteria. All criteria, but not the weightings, will be published in the EOI and 'detailed call' documents, however, the evaluation panel must allocate weightings to each criterion before the closing date for EOI submissions. Consistency in evaluation criteria should be maintained through the EOI and 'detailed call' phases of the project, with some refinement possible in moving from EOI to 'detailed call'.

Shortlisted bidders may also be invited to give presentations of their proposals to the evaluation panel and steering committee. Subject to a favourable outcome, the panel's evaluation would normally lead to a shortlist of about three bidders (but as few as one) from whom detailed proposals could be invited.

The Auditor-General should be consulted and advised on the form of the contractual arrangement to be included in the 'call for detailed proposals' as well as the likely accounting treatment for the transaction.

The evaluation report is submitted by the agency CEO to the responsible minister for endorsement. If supported by the minister, the evaluation report and a draft of the 'call for detailed proposals' document are submitted to the BCC for approval to proceed.

The BCC will consider the panel's report along with the agency's recommendations. Approval will be given to either invite a 'call for detailed proposals' from the shortlisted bidders or terminate the process.

3.5 Detailed proposals and assessment phase

Once the BCC's approval is received the agency may proceed to a 'call for detailed proposals' from the shortlisted bidders.

The agency's evaluation panel will undertake a full assessment of the detailed proposals submitted by the shortlisted bidders and recommend a preferred bidder. If no satisfactory bid is received, the process may be terminated. Subject to endorsement by the responsible minister, the assessment and recommendations will be submitted to the BCC for approval. Updating and finalising studies and analyses commenced at the beginning of the process is an essential element of this full assessment. This would include:

- detailed project description, including financial details
- updated economic appraisal
- updated financial feasibility
- updated value management study
- updated risk management plan that includes the risk of abandonment of the project by the private sector both before and after commencement of the project
- updated statement of fiscal impacts
- environmental impact assessment and planning and environmental approvals
- community relations plan
- updated assessment of net benefits from private sector involvement

- assessment of Loan Council treatment
- assessment of probity, policy and other issues
- assessment of impact on other agencies
- summary of accounting treatment and taxation opinion.

3.5.1 Accounting treatment

Agencies must assess the likely accounting treatment to be adopted for private sector financed projects. A statement of accounting treatment is to be prepared, showing:

balance sheet:

- valuation, treatment and timing of assets to be passed to the agency at the end of any concession period
- treatment and timing of any assets passed over to the private sector
- valuation and treatment of any liabilities assumed
- valuation and treatment of any contingent liabilities.

operating statement:

- treatment of any expenses to be incurred over the duration of the contract
- treatment of any likely revenues to be received from the private sector.

statement of cash flows:

- treatment of any payments likely to be made to the private sector over the duration of the contract
- treatment of any likely receipts to be received from the private sector.

Agencies should refer to the relevant accounting standards proposed and, where reliance is being placed on professional accounting opinions, copies of these should be attached to the statement.

The achievement of 'off balance sheet' transactions is not a key driver for the Government in PFPs even though capital projects delivered without appearing on the Government's balance sheet may be financially beneficial. The Government's key drivers are improved value for money in service delivery and appropriately balanced risk allocation.

The NSW Treasury is responsible for accounting policy guidelines and should be consulted by agencies when the most appropriate accounting treatment is being considered.

An updated statement of accounting treatment must be submitted to Treasury after negotiations have been finalised. A Treasury determination on the accounting treatment to be adopted must be obtained before the contract is executed. The accounting treatment is subject to audit by the Auditor-General.

Treasury is required to report the State's exposure to infrastructure projects with private sector participation when putting forward the annual Loan Council allocation and when making periodic reports to the Loan Council. Exposure is to be estimated as the full contingent exposure measured by the Government's termination liability.

If the termination liability does not include all forms of government underwriting, the sum of the individual liabilities incurred under each clause of the project delivery contract may have to be estimated.

The NSW Treasury will work closely with agencies in preparing an assessment of likely Loan Council impacts from private sector financing. It will use material contained in the statement of fiscal impacts, the economic appraisal and other supporting documentation.

3.5.2 Unbundling financial models

There is a need to analyse cost inputs including those that are part of the financing package, which represent a significant proportion of the total costs of a typical PFP. To enable government to fully understand the private sector's funding package, shortlisted bidders will be required to provide the financial model used to support their bid. Access to the financial model will enhance government confidence in the project by:

- confirming the level of risk transfers and costs
- allowing the full assessment of project affordability
- providing the basis for comparative analyses
- ensuring value for money is achieved
- enabling government to assess project changes, such as interest rate movements and cost changes, prior to financial close.

3.5.3 Purchase of intellectual property from unsuccessful bidders

Bidders must identify the elements of their bids claimed as intellectual property.

Government may seek to negotiate the purchase of intellectual property forming part of an unsuccessful bid.

3.6 Negotiations and contract phase

3.6.1 Budget Committee of Cabinet requirements

When giving approval for the agency to finalise contract negotiations with the preferred proponent, the BCC will need to be assured that it is unlikely that any new issues will be raised that may materially alter the respective positions of the Government and the preferred bidder.

Agencies must remain aware of any potential new issues, particularly relating to other government aspects such as environmental and planning approvals and taxation treatment.

The contract must detail cost and risk sharing relating to the attainment of, compliance with, and delays resulting from, any outstanding or amended environmental and planning approval.

Depending on the degree to which government (a tax-exempt entity) is deemed to have assumed commercial risk and control, Commonwealth taxation legislation may adversely affect PFPs. Because the Australian Taxation Office will only rule on finally developed arrangements, it is the responsibility of the private sector

party to obtain a binding ruling. This will normally be a standard condition of any contract. The NSW Government will not assume nor underwrite risk associated with the denial of tax deductions.

The Auditor-General should be advised of the final form of the agreement to be negotiated.

If there are any significant variations from the detailed proposal approved by the BCC, the negotiated agreement should be referred back to them for consideration and, if favourable, final endorsement. The preferred bidder should not be made public until the BCC has endorsed the final contract.

Progress reports may be required by the BCC for competitively bid projects or those involving exclusive negotiations.

3.6.2 Statutory approval under the PAFA Act

Under the PAFA Act it is the Treasurer's responsibility to give approval for agencies to enter into joint financing arrangements.

In conjunction with Treasury, the sponsoring agency must develop a project-specific 'terms and conditions for negotiations of private sector infrastructure projects' agreement in the PSI-3 format (see Appendix 4). The agreement outlines the scope of the project and areas for final negotiations as well as providing the conditions under which the Government would support the project. This provides formal advice to the Treasurer on the joint financing obligations.

A draft agreement is to be jointly prepared by the agency and Treasury. This should be undertaken before requesting BCC's approval to enter into negotiations with the preferred proponent.

3.6.3 Reimbursement of reasonable bidding costs

The Government may decide to terminate the 'call for detailed proposals' process for reasons other than value for money, commercial or technical considerations.

Under these circumstances, consideration may be given to reimbursing bidders' reasonable bidding costs. Any reimbursement will be based on the quality and quantity of information supplied by the proponent(s). Where reimbursement is paid, the agency will retain the proprietary rights to the bidding material.

3.7 Disclosure and implementation phase

3.7.1 Contract summaries

A contract summary is to be made available to the Auditor-General for audit within 30 days of the contract becoming effective. Within 90 days of receipt by the Auditor-General, the audited contract summary will be tabled in Parliament by the responsible Minister. After tabling, the availability of the contract summary will be advertised in the Public Notices.

The elements in the summary must include:

- the full identity of the private party and its sponsors, including details of cross ownership of relevant companies
- service delivery and quality requirements
- the term of the contract. This information would include details of future transfers of assets of significant value to government at no or nominal cost, and details of the right to receive the asset as well as when this might occur
- what and when assets are to be transferred by the public sector to the contractor
- all maintenance provisions in the contract
- the price to be paid by the public, and the basis for future changes in this price
- provisions for renegotiation
- the results of cost-benefit analyses
- the risk sharing in the construction and operational phases
- significant guarantees or undertakings. This would include loans entered into or agreed to be entered into
- the remaining key elements of the contractual arrangements, if they have not been covered above.

The statement must not disclose:

- the private sector's cost structure or profit margins
- matters relating to intellectual property
- any other matters where disclosure would put the contractor at a commercial disadvantage with its competitors.

The evaluation criteria and weightings used to select the preferred bidder will also be disclosed at this time.

3.7.2 Progress reports

The BCC may require regular progress reports from major projects so that it can monitor implementation. The need for formal reporting to the BCC will be decided on a case-by-case basis.

3.7.3 Transition

After the contract becomes effective, management of the project will normally be transferred to an implementation team and ultimately to ongoing agency service delivery arrangements.

3.7.4 Post implementation review

A post-implementation review will be undertaken on all private sector infrastructure projects. They should be seen as a valuable tool in refining the processes used in developing private sector infrastructure projects. They will be undertaken by the agency initiating the project and should include:

- project formulation
- project objectives
- brief appropriateness
- design performance

- approvals process
- project delivery
- risk exposure/risk sharing
- delivery time
- quality
- budget performance
- project management/procedures
- functional competence of infrastructure, including networking and interfacing
- project operations, including service delivery and financing
- industrial relations management
- environmental management
- community relations
- industry development.

The review should be initiated 12 months after implementation although it may be required earlier. So that lessons learned can benefit future projects, a review outcome report should be prepared and copies submitted to the Private Projects Branch in the NSW Treasury and the ICU in Premier's Department.

Service delivery performance will be reviewed periodically throughout the life of the contract.

4 Project Management Structure

The complexity and scale of PFPs requires a team-based management approach to ensure all the required skills are effectively applied. Teams must have clear lines of accountability and sufficient flexibility to optimise the input of a diverse management team. In this way the public sector will reflect the breadth of skills brought to the project by a private sector consortium.

Experience and knowledge need to be captured retained and shared to enhance the likelihood of success of future PFPs.

This section outlines a suggested project management structure aimed at achieving these outcomes.

4.1 Steering committee

For major projects a steering committee should be established by the delivery agency. The committee's brief should be to guide the development of the project and deal with key issues, including the content of key documentation and the selection of a preferred bidder. Where more than one agency is involved in the project service delivery outcomes, the Director-General NSW Premier's Department will appoint



Photograph courtesy Department of State and Regional Development.

one of them to lead the project and convene the steering committee; the others will be represented on the committee.

The composition of the steering committee will be determined by the delivery agency but a number of key departments will provide input:

- NSW Treasury will provide an experienced officer to contribute to the handling of commercial, financial and process issues in PFPs

- the Department of Public Works and Services will provide central agency oversight of technical contracting and procurement aspects, except where the agency—such as the Roads and Traffic Authority and Sydney Water—has in-house expertise and experience in complex infrastructure projects
- the Cabinet Office will be represented to provide assistance with complex policy issues
- the Infrastructure Coordination Unit will be represented.

4.2 Project manager

The CEO of the delivery agency should appoint a project manager either from the agency staff or on a contract. The project manager should be a member of the steering committee.

The project manager is responsible for delivering the project and managing members of the project team, including external advisers and consultants. The

project manager requires a good understanding of government processes and well-developed commercial skills applicable to developing and negotiating contractual arrangements.

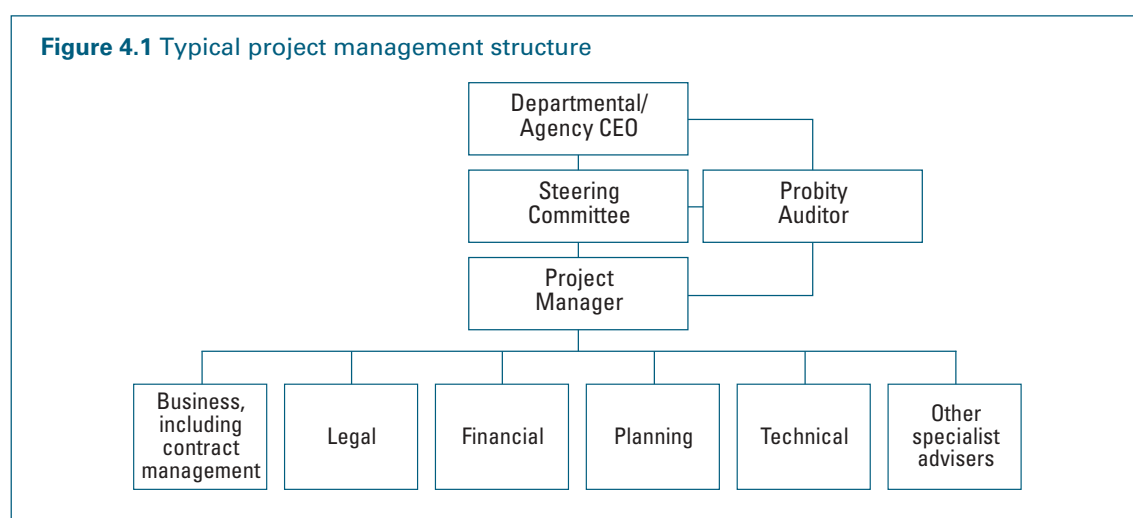
4.3 Probity auditor

A probity auditor should be appointed for large, complex, and unusually sensitive PFPs to ensure that a transparent and robust process is followed. The probity auditor must be objective and also endorse the probity plan, monitor the bid process throughout, and provide advice to the project team, the steering committee and the CEO of the delivery agency.

4.4 Project team

The full team is not brought together until the BCC has given an approval to seek EOI, although some resources will have been devoted to the project definition.

Figure 4.1 (below) provides a typical project management structure, which includes the



project manager and other specialist members of the team. Specialist knowledge required for the project including financial, technical, operational, community relations, environmental, contractual and legal skills will vary with the type of project.

While some specialist roles may be found within the delivery agency and others seconded from other departments, external legal and other specialist skills will be required. The project manager is responsible, through the steering committee, to the CEO of the delivery agency for delivering all critical elements of the project.

4.5 Budget Committee of Cabinet review

The proposed project management structure is to be submitted to the BCC for endorsement when approval is being sought to call for EOI.

4.6 Treasury Private Projects Branch

Treasury's specialist Private Projects Branch will be the focal point for economic and financial assessment and advice on all PFPs and will assist government agencies more generally. The branch will ensure application of these guidelines. It will also promote best-practice PFPs by absorbing and disseminating the lessons of experience and consulting with other governments on their experiences and practices. The branch should be consulted at an early stage in the development of a PFP proposal. It will draw on expertise from across the public sector and the expert advice of private sector consultants when required.

5 Risk Management

Government's aim is to optimise risk allocation so that value for money is maximised in each project on a whole-of-life basis; the aim is not to maximise risk transfer from government to the private sector. A full risk analysis must be undertaken for each PFP. Where possible government will adopt a standardised risk-management approach to minimise transaction costs. However, given the length of contractual arrangements and the likely complexity of issues involved, risks must ultimately be considered on a case-by-case basis.

5.1 The risk management process

The process of risk management should start at the strategic planning stage of the project. The steps involved are:

establish context:

- proposal familiarisation, ie. identify project scope, objectives, assessment criteria, key elements and issues.

risk analysis:

- identify all potential risks

- assess potential likelihood and consequences of each
- screen or grade risks, identifying minor, moderate and major risks.

risk response planning:

- identify feasible responses to risks, including prevention, impact mitigation, transfer and acceptance
- select the best response for each risk
- develop risk action schedules and other management measures, as appropriate.

document planning:

- prepare a risk management plan for large/complex projects; prepare risk action schedules and measures for others.

risk management implementation:

- implement plan, action schedules and management measures
- monitor the implementation
- periodically review risks and evaluate need for additional risk management.¹⁵

¹⁵ For further details on risk management, refer to the Total Asset Management manual at: <http://www.gamc.nsw.gov.au/tam2000/4-7-risk.html>

Optimal risk allocation is the principal driver of value for money in PFPs.

When government focuses on contracting for service outcomes rather than building and maintaining infrastructure, the risks associated with the construction and ownership of the asset can be transferred to the private party, which can design, build, operate and maintain the asset at minimum whole-of-life cost.

Government should retain only those risks that it can manage more effectively than the private sector.

Risks that are outside the control of either party may be shared.

5.2 Risk categories

There are many ways of categorising risk for the development of a risk matrix. The adoption of a standardised approach will facilitate the development of standardised contract clauses and contribute to the minimisation of transaction costs.

Accordingly, these guidelines have adopted the *Partnerships Victoria* risk categories, except that financial and sponsor risks have been categorised separately to better recognise the non-financial elements of sponsor risk.

Appendix 3 sets out a summary of the general position for likely risks, but must not be relied upon as a substitute for detailed analysis. The identification, allocation and management of risks must ultimately be considered case by case.

5.2.1 Site risk

Site risk includes physical suitability, contamination, statutory approvals, land acquisition, indigenous and non-indigenous heritage issues, and native title. It should be allocated to the private party except, generally, where government owns or designates the site.

5.2.2 Design, construction and commissioning risk

Design, construction and commissioning risk is allocated to the private party, except where government initiates a change in design or construction or in some other way interferes in the design and construction process. In these instances, government may share the cost of the changes. Any contract should specify the responsibility for risks associated with any subsequent modification to the proposal and the likely risks associated with obtaining any associated environmental or other approvals.

Except where the purchasing agency is statutorily responsible for design and operating standards, agencies should avoid heavily specifying or formally endorsing a design. This unintentionally takes back some of this risk.

The PFP proposal must determine and allocate all risks associated with meeting environmental and planning conditions and for ensuring that environmental harm is not inadvertently caused by the construction or commissioning of the project.

5.2.3 Sponsor risk

In establishing a project consortium, the sponsor typically establishes the private party in the form of a special purpose vehicle (SPV), which contracts with government. The SPV is simply an entity created to act as the legal manifestation of a project consortium. Because the arrangement is financed through non-recourse debt, creditors have access to the project's cash flows but limited recourse to the sponsors' balance sheets.

Sponsor risk is the risk taken by government that the SPV, or its sub-contractors, will not fulfil their contractual obligations and:

- government will be unable to either enforce those obligations against the sponsors, or recover some form of compensation or remedy from the sponsors for any loss sustained by it as a result of the SPV's breach, or
- the sponsor(s) will prove to be inappropriate or unsuitable for delivery of the project.

The SPV itself has no historical financial or operating record that government can assess. Therefore, in assessing the SPV's ability to fulfil the project obligations, government relies on the individual consortium members' historical performance, as well as any projects they have previously undertaken together.

The project consortium must be carefully assessed for probity, financial viability and competence to deliver the infrastructure

and services required. If there is a likelihood of the SPV not being significantly capitalised after financial close, government should generally seek security before entering into the contract. Security may be in the form of guarantees from the sponsors or parent companies (parent guarantees) or in the form of performance bonds that ensure that the private party is fully committed to delivering the required outputs.

Government needs to lessen sponsor risk by retaining an appropriate level of control over changes to the ownership of the SPV, however, value for money can only be maintained if the benefits of imposing restrictions outweigh the costs.

5.2.4 Financial risk

Financial risk includes the risks that:

- private finance will not be available
- the project will not prove financially robust
- changes in financial parameters will alter the bid price before financial close.

If a project fails to gain finance or fails financially later, government is affected because it must obtain alternative services. These risks may be lessened by requiring bids to be fully underwritten in both debt and equity and by not automatically accepting the lowest bid.

Risks associated with changes in financial parameters before financial close may be assumed or shared by government depending on the circumstances (eg. by agreeing to

accommodate interest rate changes during that period). The financial parameters will normally be fixed in the detailed bid documents, whereupon government takes interest rate risk until financial close.

The private party can benefit by project refinancing but where it receives a premium as a result of lower interest margins (mature markets) or benchmark interest rates, government may seek to share in those benefits in future projects. Arrangements for premium sharing must be clearly established in the contract.

5.2.5 Operating risk

Apart from costs arising from government intervention or interference (eg. changes in output specifications and certain changes in law), risk is borne by the private party.

5.2.6 Market risk

Market risk consists of demand and price risk.

Wherever possible, demand risk is to be borne by the private party. The extent of demand risk borne by them depends on whether government is the only service consumer and value for money questions.

In projects where government pays for the service, price risk is implicitly transferred to the private party by fixing the service charge payable by government for the contract term; this is subject to agreed adjustments. Government substantially controls demand for services in social infrastructure and only part of market risk will generally be related

to facility performance. If the service charge payable by government is so high that price or market variations have little effect on profitability, market risk generally remains with government.

5.2.7 Network and interface risk

Network risk is based on changes to both complementary and competitive sets of connections; the risk that a complementary set of connections on which the contracted services depend will be removed or altered, and the risk that a competitive set of connections will alter demand for the contracted services.

While network risk is often within the control of government, its community obligations can be in competition with the goal of efficient management of the network. Therefore, government generally only accepts network risk where there is a change in a set of connections that actively discriminates against the project and directly affects project viability.

Interface risk is the risk that the contracted services will not be compatible with the delivery of core services and vice versa. Provided that government does not materially change its service delivery, the private party should be responsible for ensuring that the contracted services are compatible with the government's services. Accordingly, the private party should bear the risk that the contracted services are not compatible with the government's services.

5.2.8 Industrial relations risk

The private party will take and manage the industrial relations risk relating to their workforce, in a manner consistent with that party's obligations under employment legislation.

5.2.9 Legislative and government risk

Risks associated with government powers and immunities and changes in law come under the umbrella of legislative and government risk. Government will generally accept much of this risk by:

- warranting its ability to contract
- agreeing to share risks associated with government 'acts of prevention' (ie. government activities impact on the private party's ability to carry out its obligations)
- agreeing to accept the risk of certain changes in law.

With respect to 'change in law' risk, government will generally take back the risk of changes in State law directed specifically or exclusively at the particular project. Other changes in law risk, including the risk of change in Commonwealth law, are generally borne by the private party. Within specified limits, however, government may share the risk of a general or sector-specific change in law that results in the need for significant capital or operating expenditure.

5.2.10 Force majeure risk

Force majeure risks that can be insured on commercially reasonable terms are generally borne by the private party.



Photograph courtesy Premier's Department.

Government may negotiate to share uninsurable force majeure risks, or those to which an unreasonable insurance cost is applied, provided value for money is achieved.

5.2.11 Asset ownership risk

Asset ownership risks are allocated to the private party. This type of risk covers design, technical, maintenance and obsolescence risks, the risk of losing the infrastructure (through a force majeure event or as a result of early termination) and residual value risk.

Government may bear a measure of residual value risk where it will ultimately own the asset. Arrangements, which include a pre-determined life or asset condition, must be made to ensure the asset transfer at the agreed time.

5.3 Risk matrix

All of the significant risks associated with a project are tabulated and categorised in a risk matrix, which also provides a description of the risk and mitigation measures and identifies the preferred risk allocation. The risk matrix can be a useful

mechanism for government and the private sector. During both pre-tender and tender phases, it can assist government practitioners to define relevant project risks and their proposed allocation; whether allocated implicitly through the structure or by way of a take-back by government.

During negotiations, the matrix can work as a checklist to ensure all risks are addressed. After the contract has been signed, it can be a useful summary of the risk allocation effected by the contract. The value and usefulness of the matrix is directly related to the way the risks are treated.

While commonplace in the market, risk matrices have their limitations. If used in

their simplified form, the actual allocation of risk accomplished by both the structure and detail of the contract can be misrepresented. For example, the use of ticks to identify the existence of a particular risk in both government and private party columns gives little indication of the detail of the allocation. The project structure and the contract are the tools by which risk allocation is achieved, not the matrix.

A risk matrix is to be developed and maintained for each PFP and included in the submission to the BCC at each stage of the approval process.

Further guidance on risks and risk allocation is given in Appendix 3.

6 Contractual Issues

The agreed risk allocation must be reflected in the contractual provisions and mechanisms. It is particularly important to align the payment mechanism with the agreed risk allocation and achievement of government objectives. This section provides general guidance on some of the important contractual issues common to most PFPs and the means by which they are often addressed. In practice, all contractual issues will vary on a case-by-case basis.

The contractual issues probably present the most complex part of a PFP and getting them right presents a considerable challenge. It is an area which in itself can generate considerable transaction costs, but it is also an area where all participants should learn quickly from experience to minimise the costs involved and produce an outcome that is reasonable and beneficial to both the public and private parties.

6.1 Payment mechanism

The basis on which government pays for services must align with its service delivery objectives. It is also important that payments are unitised, so that the overall payment can be reduced if services are not

up to standard in terms of quality, timeliness, or other service delivery requirements, or are not delivered.

6.2 Performance measurement

Performance measurement is critical to PFPs because government is procuring a service of stated quantity, quality and availability. Performance measurement may be linked to an agreed set of standards or key performance indicators, which will generally relate to the quality, amount and frequency of service provision. Private party payments will be linked to measured performance in delivery of the contracted service.

6.3 Dealing with risks that are difficult to allocate

Risks clearly identifiable at the time the contract is entered into are allocated in the most favourable way to the party best able to control occurrence and the consequences of their occurrence.

Some risks are difficult to allocate in advance because they may not be controllable or fully identifiable. These risks should be

determined on a case-by-case basis and may be shared or assessed when they occur.

What is important is that their existence is recognised and that their occurrence and their consequences are specified, where possible.

6.3.1 Material adverse effect regimes

Material adverse effect regimes specify those risk categories which, if they materialise, will have a material adverse effect on the project and are to undergo a special process of assessment and allocation between the parties. They offer flexibility and comfort to the private party by specifying the outcome (eg. the restoration of the private party's position before the event) to be achieved through various measures adopted by the parties when a risk in the specified categories materialises.

6.4 Benefits of risk

In each project, risks may materialise to adversely and positively affect either or both parties. In agreeing to share a materialised risk, government should be entitled to an equivalent share of consequences and benefits.

Apart from the above general position, it may be appropriate for government (and the community) to share in any windfall gain or super profits received by the private party.

Government recognises that it should share in benefits of risk—whether on a symmetrical or windfall basis—in a way that does not discourage or stifle private sector innovation.

The terms and conditions for sharing of the benefits of risk must be agreed to in advance and specified in the contract.

6.5 Tenure and access

Private parties need to be assured that they can properly access or use the facility to perform their contractual obligations. The mechanism by which they do this—appropriate tenure—also gives the private party a valuable asset for development, thereby allowing the project to be financed.

Government needs to be assured that it and, where appropriate, the public has adequate continuing rights to enter and use the facility for its intended purposes. For government, this in part means having the access necessary for it to deliver core services and to ensure the delivery of the contracted services. It also needs access during the construction phase to ensure the private party is complying with its contractual obligations, and to inspect the works.

6.6 Variations

Because PFPs are output-based, it is important that agencies clearly and comprehensively specify their service delivery performance requirements, without specifying inputs. This will ensure the government does not need to seek variations to service delivery requirements or modifications to infrastructure, which are often costly and may prejudice the government's risk position.

PFPs usually involve long term contracts during which time circumstances may change. This may occur for any number of reasons, only some of which can be foreseen. The Government therefore requires a flexible contract with suitable mechanisms for achieving necessary operational variations in a transparent, cost-effective way.

6.7 Availability

The provision of contracted services is fundamental to the success of the project. This is particularly so where availability rather than usage is the basis on which payment (wholly or partly) is made.

Because payment depends directly on availability, the definition of availability must be clear and objective in the contract, and the specifications reasonable and easily measurable. The service is unavailable if it is not provided in accordance with the defined availability standards.

The risk of unavailability is to be borne by the private party. Accordingly, payment under the contract must depend on the services being available. The private party is not to be paid, or only paid at a reduced rate, if the service is unavailable. Penalties and/or damages may also be sought.

Failure to earn a payment is not the same as default. If a default clause does not exist and the contract merely states that failure to make a service available will lead to a reduction in payment, unavailability complies with the contract terms; it is not

in breach of them. Non-payment is the only redress available to government. However, continued non-compliance will generally lead to default. This may give rise to the exercise of step-in rights and, in the event of serious default, may result in termination.

6.8 Employment issues

As a general principle the Government does not support forced redundancies. Where public sector employees are affected by a PFP and are offered employment with the new employer, the PFP contract should provide for those employees to receive employment benefits no less than those that would have applied should government employees have performed the work. The NSW Industrial Relations Commission 'no net detriment' test is to apply.

6.9 Force majeure

During the course of a project, an event outside the control of either party—such as a storm, an earthquake, a fire or the outbreak of war—may occur preventing either or both parties from complying with their obligations under the contract to the extent that the future of the project is placed in doubt.

The chance of a force majeure risk eventuating is generally more remote than the chance of most other project risks eventuating. However, the consequences of the force majeure risk, if it eventuates, may be more severe and have a greater impact on the project.

Government needs to ensure that appropriate arrangements are in place to deal with the consequences of force majeure events to minimise the impact on the project and, more importantly, on the delivery of services. The private party should not have access to relief unless it makes temporary or alternative arrangements to replace the affected service; ie. it takes steps to mitigate the effect of the force majeure event.

Contracts should exclude from the definition of force majeure events, those events that could have been prevented, overcome or remedied by the private party exercising a reasonable standard of care and due diligence.

6.10 Insurance

When insurance is taken out before a force majeure risk materialises, the risk is effectively transferred to the insurer. This is one of the few courses of action that can be taken to help with the immediate problem of service interruption caused by a force majeure event. It should provide funds for remediation or reinstatement of the facility in preference to the repayment of debt.

To minimise insurance risk (ie. the risk that cover may not be complete, may not be effective, or that a claim is rejected), the contract should provide that:

- cover is taken out with an insurer subject to the national prudential regulatory regime; for projects involving agencies covered by the Treasury Managed Fund, the fund should be consulted at an early stage
- where possible, government is a co-insured party; it is not sufficient that its interests are merely noted on the policy
- changes cannot be made to insurance by the private party without the approval of the contracting government agency.

To ensure adequate and effective coverage, insurance policies should also be reviewed regularly.

6.11 Default and remedies

The contract includes default and remedy provisions to make risk allocation enforceable. A breach of the contract (ie. a default) occurs when a party fails to fulfil the requirements of the contract, (eg. when a party does not meet its materialised risk obligations). Because the scale and consequences of contractual breaches are at odds, some contractual defaults (ie. material defaults) give rise to a right of termination, and others (ie. non-material defaults) attract an obligation to rectify but the other party cannot, singularly, terminate the contract. However, a non-material default can become a material default when it is not rectified, if progress toward rectification is not satisfactory, or if the default occurs several times or in combination with other defaults within the period allowed.

6.12 Government step-in

Step-in occurs when government elects to assume all or some of the service delivery obligations of the private party for a period of time. Situations in which government

may exercise its contractual rights to step-in include:

- preventing or mitigating a serious risk to:
 - the environment
 - public health
 - the safety of people or property
- guaranteeing continuity of a service
- discharging a statutory duty
- otherwise dealing with a default by the private party under the contract.

Step-in rights are ordinarily included in a package of remedies for private party default. However, a private party does not have to default for government to step-in. Such rights may need to be exercised simply because the private party is unable to deal with a particular situation appropriately (eg. in an emergency). The consequences of risk materialisation may necessitate urgent government intervention because they are beyond the private party's capacity to resolve.

6.13 Termination

Government will make sure that contracts include adequate provisions for ongoing delivery of public services or the implementation of other suitable arrangements to cover for events where termination becomes necessary. These arrangements will require the outgoing private party to cooperate fully with the government during any transition period.

In the event of termination, compensation can be a complex issue. How parties are



Photograph courtesy Department of State and Regional Development.

treated in this situation will necessarily vary between projects.

6.14 Dispute resolution

Appropriate dispute resolution procedures may need to be instituted to speedily resolve any dispute arising over the parties' contractual obligations. This avoids the need for parties to exercise their rights under the default regime. Rather than dealing with disputes through the courts, the implementation of a pre-determined alternative dispute resolution process can have cost saving benefits as well as avoiding delays. In addition, such processes can see disputes resolved at an early stage, which decreases the chances of service interruption and ensures that public benefit and value for money are maintained.

6.15 Intellectual property

Intellectual property is an important issue for all PFPs, including unsolicited

proposals. Increasingly, material submitted to the Government is said to represent intellectual property.

In addressing this issue, it is important that agencies:

- clearly identify intellectual property aspects of proposals
- ensure that the intellectual property of government agencies is protected
- manage intellectual property issues during all discussions
- develop competitive bidding processes, which protect the private sector's intellectual property rights where direct negotiations aren't used (ie. in the majority of cases)
- identify those key phases of a project open to market testing to ensure the government achieves value for money without compromising intellectual property rights.

7 Public Sector Comparator

The essential rationale for the Government's use of private finance arrangements for infrastructure provision is improved value for money. A PSC will be developed for all proposals to assist the Government determine whether a private finance arrangement offers superior value for money over traditional methods of government delivery.

7.1 The role of a Public Sector Comparator

A PSC is a model of the costs (and in some cases, revenues) associated with a proposal under a government financed method of delivery. A PSC:

- is based on the most efficient likely method of providing the defined output currently available to the public sector
- takes into account the potential impact of risks on the costs (and revenues) associated with a proposal over its life
- is expressed in terms of the net present cost (or benefit) to government of providing the output, over the life of the proposed concession.

The PSC reference project will be defined and costed to provide the same level and

quality of service expected of the private sector. The reference project may include elements of private sector provision and risk transfer, such as provision of the facility under a design and construct contract or a maintenance contract, with the private sector. These approaches are consistent with current methods of delivery. However, the PSC will not include private financing of the project over its life.

Because the PSC is a valuable tool for government in determining value for money, it is important that it is prepared carefully and comprehensively. However, the PSC is a quantitative benchmark with inherent limitations because:

- it requires costs (and revenues) to be forecast over the life of the proposed concession. It is difficult, even for the most skilled experts, to make accurate estimates over such a long time-frame
- estimating the impact of risks on costs (and revenues) over the life of an asset is a complex and often subjective exercise.

The PSC, therefore, can provide government with an approximate measure of the range of outcomes it is likely to face in delivering a project under traditional methods.

To maintain its usefulness as a tool, the PSC will be:

- accompanied by qualitative considerations in determining the potential value for money of a private finance arrangement
- subject to sensitivity testing and scenario analysis to determine the robustness of its underlying assumptions, and their impact on the PSC's results
- sufficiently flexible to allow new information to be incorporated as it comes to light, enhancing the integrity of the PSC as a benchmark while maintaining the probity of the project development and tender assessment processes.

The qualitative considerations that will support the PSC include:

- risks not easily or confidently quantified
- the identity, credit standing and proven reputation of the bidder
- differences in the deliverable service not able to be quantified or adjusted for

- any wider net benefits or costs that a private finance arrangement may entail. For example, wider social benefits may include earlier or more flexible provision of important infrastructure services than would be possible under a public procurement, or the establishment of better benchmarks for publicly delivered services.

The Government is flexible about disclosing a summary of a PSC in tender documents. This is more likely to happen where it is obvious that it will assist the private sector's bid preparation process and result in higher quality and better value bids to the Government. The results of the PSC will ultimately be publicly available in the contract summary.

7.2 Approaches to constructing a PSC

The NSW Government is typically involved in the provision of economic and social infrastructure, either as a procurer or facilitator. The key differences between the two types of infrastructure are outlined in Table 7.1.

Table 7.1 Differences between economic and social infrastructure delivery

Economic Infrastructure	Social Infrastructure
Revenues are often from third parties – subject of market-based resource allocation	Usually paid for out of consolidated revenue – subject of Government resource allocation decisions
Infrastructure provider faces genuine market risk	Usually no market risk to provider of infrastructure – payment streams are usually subject to long-term contract or budget allocation
Traditionally delivered through a Government Business Enterprise (including a State-owned corporation)	Traditionally delivered through a general Government agency
Revenue risks are a key driver of financial outcomes	Cost risks are a key driver of financial outcomes



Photograph courtesy Australian Correctional Management Pty Ltd.

The NSW Government will develop each PSC on a basis that is consistent with the nature of the proposed project.

7.3 Economic infrastructure

PSCs for stand-alone economic infrastructure projects (such as road and transport projects, which generate third-party revenue) will usually be developed on a project financed basis, reflecting:

- the importance of revenue, and revenue risk, in determining the financial outcome of the project
- the usual method of delivering such infrastructure (ie. through a stand-alone government business and in accordance with the NSW Government's Commercial Policy Framework).¹⁶

The project delivery vehicle will be assumed to be a special purpose vehicle operating under the *State Owned Corporations Act 1989*.

PSCs for economic infrastructure projects will incorporate the following principles:

- competitive neutrality with the private sector, through the payment of State and Commonwealth tax equivalents and other regulation costs equivalent to those that would be faced by the private sector
- a commercial capital structure, ie. a level of debt and equity that optimises the value of the project, while maintaining an investment-grade credit rating for the project's debt. Prudential constraints will be applied to the project's financial structure, including minimum debt service cover ratios and reserves for debt service
- debt guarantee, reflecting the margin between the project's credit rating and the AAA-rating of the NSW Government

¹⁶ This framework covers financial performance monitoring, financial distributions, capital structure, guarantee fees and social programs. Relevant policy documents are available from NSW Treasury at: <http://www.treasury.nsw.gov.au>

- a commercial level of return on the Government's equity investment in the project, reflecting the project and financial risks borne by equity throughout the project's life.

Constructed in this way, PSCs for economic infrastructure can serve two functions:

- as an initial test of the commercial viability of the project
- as a benchmark for testing bids' value for money.

7.4 Social infrastructure

PSCs for social infrastructure will be constructed as a cash-flow model under traditional delivery methods because, unlike economic infrastructure, social infrastructure is primarily funded by payments from the Government. There is limited or no third-party revenue generated by the infrastructure.

The cash flows for social infrastructure in the PSC will include three core components:

- the base costs of delivering the services specified in the project brief under the traditional funding method

- a competitive neutrality adjustment (if applicable), covering any expenditure-based taxes, fees and charges that the agency is not required to make by virtue of its government-owned status
- an estimate of the expected cost of risks that could potentially crystallise over the life of the project. The PSC should be able to distinguish between the expected cost of risks that would be retained by the Government and those that would be transferred to the private sector.

7.5 Technical issues

Construction of a PSC requires a high level of technical expertise in project costing, financing and risk analysis. NSW Treasury is responsible for advising on the value for money aspects of private financing arrangements, including the development of PSCs. Treasury will assist agencies throughout the project development process and provide advice on technical issues, such as the discount rate to be used in comparing bids to the PSC.

8 Probity and Accountability

The NSW Government is committed to efficiency, fairness, impartiality and integrity in all its dealings.

Probity is an important issue for government as custodian of the community's assets. A comprehensive probity plan is essential in all PFP projects and a probity auditor will be appointed for large, complex and unusually sensitive projects.

By adopting a clear probity process, all parties are assured of the integrity of the awarding process.

The Government will require the publication of a contract summary for privately financed projects with a capital value of more than \$5m. The summary, audited by the Auditor-General, must be tabled in Parliament within 120 days of the contract becoming effective.

To maximise community and business confidence in its tendering practices, the Government has established independent

review mechanisms for complaints about tendering with government agencies. The State Contract Control Board is responsible for issues associated with probity, National Competition Policy and the Australian and New Zealand Government procurement agreement. The ICAC may examine complaints about potentially corrupt conduct in the procurement process.

The NSW Government's Code of Practice and Code of Tendering for NSW Government Procurement¹⁷, together with the Code of Practice and Code of Tendering for the Construction Industry¹⁸, apply to procurement by all NSW Government agencies, and those doing business with and for government. The procurement of services through privately owned and funded public infrastructure are included in this. The codes establish ethical principles and standards of behaviour for all parties involved and will apply to all procurement actions from calling for EOIs through to project completion.

¹⁷ <http://www.dpws.nsw.gov.au/DPWS/Policy/Areas+of+Expertise/Procurement+Procurement+Policy+Documents.htm>

¹⁸ <http://www.cpsc.nsw.gov.au/ethics/>

Appendix 1

Glossary

Acronyms

BCC	Budget Committee of Cabinet	ICU	Infrastructure Coordination Unit
BOO	Build, Own, Operate	LEP	Local Environment Plan
BOOT	Build, Own, Operate, Transfer	PAFA	Public Authorities (Financial Arrangements) Act 1987
BOT	Build, Operate, Transfer	PFP	Privately Financed Project
CISP	Capital Investment Strategic Plan	PPP	Public Private Partnership
D&C	Design & Construct	PSC	Public Sector Comparator
DBFM	Design, Build, Finance, Maintain	SISP	State Infrastructure Strategic Plan
DCM	Design, Construct, Maintain	SPV	Special Purpose Vehicle
EIS	Environmental Impact Statement	REP	Regional Environmental Plans
EIA	Environmental Impact Assessment	SEE	Statement of Environmental Effects
EOI	Expression of Interest	SEPP	State Environmental Planning Policy
EP&A	Environmental Planning and Assessment Act 1979		
ICAC	Independent Commission Against Corruption		

Definitions

Asset A general term referring to a range of resources that represents some value. Assets can be categorised into: financial, such as cash, stocks and bonds; and real, such as land, buildings, machinery and inventory. Intangible assets, such as patents, goodwill and trademarks, have the potential to provide future benefit to the organisation by their use or sale.

Bidder A respondent to a request for expressions of interest or an invitation to submit a bid in response to a call for detailed proposals. Typically a bidder will be a consortium of parties, each responsible for a specific element, such as constructing the infrastructure, supplying the equipment, or operating the business. Government will normally contract with only one lead party (bidder), which is responsible for the provision of all contracted services on behalf of the consortium.

Business case A business case sets out a preliminary view on how the project will be delivered. It also provides an analysis of the various impacts of the project and an indication of the likely level of market interest. The business case provides information, allowing Government to decide whether to support a proposed project before significant resources are spent on its development.

Capital A generic term for an asset. Capital sometimes refers to financial investments and at other times to physical capital, such as land and buildings, earthworks, machinery and vehicles.

Capital expenditure An amount used during a particular period to acquire or improve long-term assets, such as property, plant or equipment.

Commissioning The proving processes involving the start-up of operations to deliver the contracted services as specified.

Competitive Neutrality Removal of any net advantages (or disadvantages) that accrue to a government business simply by virtue of being owned by government.

Default The failure of a party to perform a contractual requirement or obligation, including failures to meet deadlines, to perform to a specified standard, to meet a loan repayment or to meet its obligations in relation to a risk that has materialised.

Demand management The use of pricing mechanisms or other methods to manage demand eg. to delay the need for new infrastructure.

Detailed Proposal A response by a shortlisted bidder to a call for detailed proposals. A call for detailed proposals details government's objectives, service delivery requirements, policy and commercial matters, material background information and the processes for lodging and evaluating submissions. It also sets out government's role and intentions for the infrastructure to be built and explains how checks and balances are observed in the process to ensure impartiality.

Discount rate The rate used to calculate the present value of future cash flows; usually determined on the basis of the cost of capital used to fund the investment from which the cash flow is expected.

Discounted cash flow A stream of future cash flows discounted to calculate a net present value.

Economic infrastructure Fixed assets that support economic activity and development in a fundamental way. Typical examples of economic infrastructure are networks of roads and telecommunications facilities, airports, ports, water storage distribution and sewerage, railways, electric power generation and distribution facilities.

Expression of Interest (EOI) A response to a call by a government department or agency for expressions of interest from the private sector in a project. EOIs are used to evaluate the capability of bidders to deliver a project and may be used to gather some information from bidders on particular approaches that may be accommodated in the call for detailed proposals. Based on the information presented in EOIs, bidders are shortlisted to provide a detailed proposal (see above).

Financial risk Risk of insolvency/default associated with the mix of debt and equity used to finance a business or property. The larger the proportion of debt used, the greater the financial risk. In relation to a PFP, financial risk includes the risks that private finance will not be available, that

changes in financial parameters will alter the bid price before financial close, and that the project will not prove financially robust.

Force majeure Acts of God and other specified risks (eg. terrorism), beyond the control of the parties to the contract, which prevent or delay performance of a party's non-financial obligations under the contract.

Fund A reserve of money or investments held for a specific purpose, such as to provide a pension or pay off a debt. It can be used to denote capital assets, liquid assets, and money in hand or notes and bills.

Government agency For the purpose of these guidelines, the term includes NSW Government departments, statutory authorities, statutory corporations and government business enterprises.

Infrastructure Fixed assets that support economic and social development in a fundamental way.

Intellectual Property (IP) Inventions, original designs and practical applications of good ideas protected by statute law through copyright, patents, registered designs, circuit layout rights and trademarks; also trade secrets, proprietary know-how and other confidential information protected against unlawful disclosure by common law and through additional contractual obligations, such as confidentiality agreements.

Liability In general terms liability refers to the debt of an individual or of a private or governmental organisation.

Loan Council A body with Federal and State representation, which aims to constrain the public sector's call on national savings primarily through the limits it places on borrowing by the public organisations.

Loan Council Allocation (LCA) The LCA is the borrowing allocation to be nominated to Loan Council by the Commonwealth, States and Territories. It is based on the deficit/surplus in addition to some memo items. Final negotiations and endorsement of each LCA are the responsibility of the Loan Council.

Market risk Market risk, which consists of demand risk and price risk, is the risk that market demand and the price paid for services respectively will not conform to forecasts.

Material adverse effect regime The designation of particular categories of risk which, if they materialise, will have a material adverse effect on the project and are to undergo a special process of assessment and allocation between the parties.

Operator The party responsible for operating the business once the infrastructure has been established.

Output specification The output or performance specification sets out the range of services that government is seeking to procure, and the performance levels required for each of those services.

Outsourcing The practice of contracting out government services to the private sector.

Preferred bidder A bidder selected to develop its proposal during the negotiation period in sufficient detail to enable the execution of the final contract.

Privately Financed Project (PFP) A PFP is a PPP (see over) that involves the creation of an asset through financing and ownership control by the private party and private sector delivery of related services that would normally have been provided by government. Government contributes to the establishment of the infrastructure, for example through land, capital works or risk sharing. The services delivered may be paid for by the government or directly by the end user.

Private party The private sector entity with which government directly contracts. Traditionally the private party has been a company, known as a special purpose vehicle, created specifically for the project. The private party is not limited to this form and can be set up under a number of structures, including a joint venture and a trust structure.

Probity Uprightness, honesty, proper and ethical conduct and propriety in dealings. Used by government to mean good process.

Probity auditor An independent expert retained to audit the bidding process at critical stages. The probity auditor will assess and report on whether the process has been conducted according to the required standards of probity. Before a contract is executed, the probity auditor reports to the agency CEO and the project steering committee on the bidding process.

Project manager The project person who has overall responsibility for delivery of the project and leadership of the project team, including external advisers and consultants.

Project team Under the guidance of the steering committee, the project team is responsible for the day-to-day administration of the project until commissioning, to ensure deadlines are met and technical difficulties resolved.

Public interest evaluation An evaluation of the likely impact of the project on public interest, including: effectiveness, impact on key stakeholders, accountability and transparency, public access and equity, consumer rights, security and privacy.

Public Private Partnership Any project, including a PFP (see above), in which there is joint public and private sector participation.

Public Sector Comparator (PSC) The hypothetical risk-adjusted whole-of-life cost of government delivering the project output specifications. As well as adjustments for retained and transferable risks, the PSC includes an adjustment for competitive neutrality. The PSC is used as the benchmark for assessing the potential value for money of private party bids in PFP projects.

Raw PSC The hypothetical whole-of-life cost of government delivering the project output specifications, with no adjustment for risk or competitive neutrality.

Reference project The most likely and efficient form of public sector delivery that could be used to satisfy all elements of the output specification. It forms the basis of the PSC (see above).

Retained Risk The value of those risks or parts of a risk that government proposes to bear itself under a PFP arrangement.

Risk The chance of an event causing actual project circumstances to differ from those assumed when forecasting project benefit and costs, and the impact of that event.

Risk allocation The allocation of responsibility for dealing with the consequences of each risk to one of the parties to the contract, or agreeing to deal with the risk through a specified mechanism which may involve sharing the risk.

Risk assessment The determination of the likelihood of identified risks materialising and the magnitude of their consequences if they do materialise.

Risk category Risk can be allocated into broad categories, such as site risk, network risk, operating risk, market/demand risk, sponsor risk and industrial relations risk.

Risk identification The process of identifying all the risks relevant to the project.

Risk management The identification, assessment, valuation, allocation, mitigation and monitoring of risks associated with a project. The aim is to reduce their variability and impact.

Risk matrix A method of presenting all possible significant risks likely to be encountered in a project, the magnitude and likelihood of the risks occurring, their areas of impact, the allocation of risks between parties and the risk mitigation techniques to be employed.

Risk sharing Risk is shared between parties involved in a venture when more than one party will enjoy the benefits of a desired outcome. The willingness to take on a share of the risk is usually identified with ownership of an equity share in an enterprise.

Risk premium The amount required to compensate an investor for assuming a particular risk attached to an investment proposal.

Social infrastructure Although loosely used, this term generally refers to items of physical infrastructure that aid the provision of social, rather than economic or industrial, services. Hospitals, schools, police stations, day care centres and prisons are examples of social infrastructure.

Special purpose vehicle (SPV) In establishing a project consortium, the sponsor or sponsors typically establish the private party in the form of a special purpose vehicle (SPV). The SPV is simply an entity created to act as the legal manifestation of a project consortium. The SPV itself has no historical financial or operating record that government can assess.

Steering committee A committee that directs the development of a project.

Step-in A right of government to intervene and assume all or some of the service delivery obligations of the private party under the contract for a period of time. Government may have the right under a PFP contract to: step in to prevent or mitigate a serious risk to the environment, public health, or the safety of persons or property; to guarantee continuity of service; to discharge a statutory duty; and to deal with a default by the private party under the contract.

Transferable Risk The value of those risks (from government's viewpoint) that are likely to be allocated to the private party under a PFP delivery method.

Appendix 2

Public Interest Evaluation

Government will develop partnerships with the private sector to deliver infrastructure where the combined ideas and experience of both sectors provide greater value for money and enhanced overall benefits to the community. All projects will undergo a broader assessment of public interest before they are offered as a PFP.

The following is a guide to the types of factors government will consider in looking at the benefits and costs of a proposal. The list is not exclusive or prescriptive and the Government may take into account any other relevant factors to determine whether a proposed PFP is in the public interest.

Effectiveness

Is the project effective in meeting government objectives?

General indicators:

- whether the proposed project's outputs, service delivery and standard of performance are consistent with:
 - the host agency's budget, service objectives and delivery strategy
 - the Government's short and longer term policy objectives for that agency or portfolio

- the Government's legislation and policies relating to the efficient allocation of resources, employment and the environment
- concurrent government initiatives/projects (potential for extra benefits/synergies or detriment/conflicts)
- offers better value for money than the best practicable public sector delivery model.

Impact on Key Stakeholders

Does the project allow for consultation with affected individuals and groups, such as employees, unions, community and action groups, local councils?

General indicators:

- identification of those likely to be affected and the likely social, economic, employment and environmental issues
- impact on the likely affected groups or concerns
- consultation/input processes ensuring participation by affected groups and confidence those views will be taken into account and given fair consideration

- economic and regional development in the area concerned, including investment and employment growth
- compliance of processes with legal requirements, broader policy standards and government commitments to stakeholders.

Accountability and Transparency

Are project processes transparent and do they allow the community to be appropriately informed about the key elements of the project?

General indicators:

- comprehensive probity plan and measures to ensure transparency of process
- clear responsibility and accountability for project reporting.

Public Access and Equity

Are there adequate arrangements to ensure that the public, including disadvantaged groups, can access and use the government service(s) and related infrastructure?

General indicators:

- identification of the likely equity groups and any specific needs that must be met
- identification of the nature and extent of public access needed
- the extent to which the project plans to meet these needs

- third party access to essential major infrastructure and services
- the proposed output/product's compliance with project requirements, specific statutory requirements and government policy standards relating to public use and access
- provisions/mechanisms to address deficiencies.

Consumer Rights

Does the project provide sufficient safeguards for the people who receive the services?

General indicators:

- compliance with project requirements, relevant statutory requirements and government policies relating to consumer rights
- identification of individuals or groups to whom the government has a high level of duty of care
- strategies/mechanisms to meet these needs
- the quality, cost and performance of the proposed project.

Security

Does the project provide assurance that there will be minimum risk to the safety and security of the people who receive the services?

General indicators:

- compliance with project requirements and all relevant statutory public health and safety standards
- provisions to address deficiencies.

Privacy

Does the project provide adequate protection of users' rights to privacy?

General indicator:

- compliance with project requirements and specific legal rights as well as any relevant government policies.

Appendix 3

Risk Table

The risk table on the following pages outlines the risk category, description, consequence, mitigation and preferred allocation in relation to the following areas:

- site risks
- design, construction and commissioning risk
- sponsor
- financial
- operating
- market
- network and interface
- industrial relations
- legislative and government
- force majeure
- asset ownership.

Important note

The risk and preferred risk allocations identified in this table are guides only and should not be considered a substitute for detailed analysis on a case-by-case basis. For example, economic infrastructure projects that do not rely on a government-sourced revenue stream can sometimes accommodate greater risk transfer to the private sector.

Acknowledgment: This appendix is substantially reproduced from *Partnerships Victoria* guidance material with the permission of the State of Victoria. Copyright in the reproduced material belongs to the State of Victoria.

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Site risks				
Existing structure (refurbishment/ extensions)	risk that existing structures are inadequate to support new improvements	additional construction time and cost	private party will pass to builder which relies on expert engineering reports	private party
Site conditions	risk that unanticipated adverse ground conditions are discovered which cause construction costs to increase and/or cause construction delays	additional construction time and cost	private party will pass to builder which relies on expert testing and due diligence	private party
Approvals	risk that necessary approvals may not be obtained or may be obtained only subject to unanticipated conditions which have adverse cost consequences or cause prolonged delay	delay in works commencement or completion and cost increases	prior to beginning the tender process government may seek a planning scheme amendment or environmental impact assessment taking risk of a route diversion or special measures to protect environmental values; for example in the case of linear infrastructure (road, rail, pipeline); during the tender process by means of a Project Development Agreement both government and the private party may achieve a measure of pre-contractual certainty allowing an early start to the approval process and a sharing of costs	private party possibly up to a specific cost amount unless government assumes because of complexity or sensitivity
Environmental (1)	risk that the project site is contaminated requiring significant expense to remediate	clean-up costs and delay (recognising that the ultimate responsibility for clean-up remains with the polluter, if available)	reliance on expert reports and insurance	private party will generally assume the risk. Where knowledge about contamination on a site is insufficient to quantify the risk and the time and cost implications of full contamination investigation and due diligence for each bidder are excessive, some risk sharing may be a cost effective solution particularly using a regime for allocation of cost consequences such as a Material Adverse Effect regime

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Site risks				
Environmental (2)	risk that prior to financial close offsite pollution has been caused from a government site to adjacent land	clean-up liability (recognising that the ultimate responsibility for clean-up remains with the polluter, if available)	government to commission reports; government should also have greatest knowledge of past uses of its site	government may assume responsibility by way of indemnity or obligation to compensate for unidentified offsite pollution pre financial close where the site is a government site
Environmental (3)	risk that prior to financial close (in case of a non-government site) or after financial close (any site) offsite pollution is caused to adjacent land	clean up liability (recognising that the ultimate responsibility for clean-up remains with the polluter, if available)	private party can manage site activity	the private party will be in control of activities on the site post financial close and will be required to assume risk of offsite pollution caused by those activities; also it will take risk of offsite pollution from any site which is not a government site (even if it occurs pre-completion)
Clean-up and rehabilitation	risk that the use of the project site over the contract term has resulted in a significant clean up or rehabilitation obligation to make the site fit for future anticipated use	financial liability on residual owner (recognising that the ultimate responsibility for clean-up remains with the polluter, if available)	private party able to manage the use of the asset and attend to its maintenance and refurbishment; government may require sinking funds if it is to resume the site and its use is liable to result in significant clean up/rehabilitation cost	private party to take risk (whether government is to resume or not) and must demonstrate financial capacity or support to deliver the site in the state required by government

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Site risks				
Native title	risk of costs, delays and compensation or risk of injunction and invalidity of approvals	delay, cost and compensation	search of registers and enquiry if appropriate and take expert advice; <i>mechanisms available</i> under the <i>Native Title Act 1993</i>	government will usually take risk on government preferred sites
Cultural heritage	the risk of costs and delays associated with archaeological and cultural heritage discoveries	delay and cost	search of registers and inquiry if appropriate and take expert advice government will generally take risk on	government on a government preferred site, otherwise private party takes responsibility
Availability of site	risk that tenure/access to a selected site that is not presently owned by government or private party cannot be negotiated	delay and cost	bidders obligation to secure access prior to contract signing	private party, as it makes the decision to bid on a non preferred site

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Design, construction and commissioning risk				
Design	the risk that the design of the facility is incapable of delivering the services at anticipated cost	long term increase in recurrent costs—possible long term inadequacy of service	private party may pass risk to builder/architects and other subcontractors while maintaining primary liability; Government has the right to abate service charge payments where the risk eventuates and results in a lack of service—it may ultimately result in termination where the problem cannot be suitably remedied	private party will be responsible except where an express government mandated change has caused the design defect
Construction	the risk that events occur during construction which prevent the facility being delivered on time and on cost	delay and cost	private party generally will enter into a fixed term, fixed price building contract to pass the risk to a builder with the experience and resources to construct so as to satisfy the private party's obligations under the contract	private party will be liable unless the event is one for which relief as to time or cost or both is specifically granted under the contract, such as force majeure or government intervention
Commissioning	the risk that either the physical or the operational commissioning tests which are required to be completed for the provision of services to commence, cannot be successfully completed	for the private party and its financiers—delayed/lost revenue for government—delayed service commencement	no payment and possible claims for damages by government until all physical and operational commissioning tests have been successfully completed	private party, although government will assume an obligation to cooperate and facilitate prompt public sector attendance on commissioning tests

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Sponsor				
Probity	the risk that after execution of contracts the private party is found to be an improper person for involvement in the provision of the contracted services	possible cessation of service to government, management crisis, and/or forced change in ownership	through assessment of the probity of the private parties and their sponsors. Contractual provisions to allow the Government to ensure continuity of physical delivery of essential services.	government
Financial	the risk that after execution of contracts the private party becomes insolvent or financial demands on the private party or its sponsors exceed its or their financial capacity, causing corporate failure	possible cessation of service to government, forced change in ownership and/or possible corporate failure causing financial loss to private party.	ensure project is financially remote from external financial liabilities, ensure adequacy of finances under loan facilities or sponsor commitments supported by performance guarantees; and due diligence on private parties (and their sponsors). Contractual provisions to allow the Government to ensure continuity of physical delivery of essential services.	government
Technical	the risk that the private party is unable to deliver the required infrastructure and/or operational systems	non-delivery or cessation of service to government	assessment of the experience and technical competence of the private party to deliver the required infrastructure and operational systems. Contractual provisions to allow the Government to ensure continuity of physical delivery of essential services.	government
Operational	the risk that the private party is unable to effectively manage the service delivery operations	cessation or reduced quality of service to government	assessment of the experience and competence of the private party to manage and deliver the required services. Private party to provide performance guarantees during operation phase. Contractual provisions to allow the Government to ensure continuity of physical delivery of essential services.	government

Risk Category	Description	Consequence	Mitigation	Preferred allocation
<p>Sponsor</p>	<p>Change in ownership</p> <p>the risk that a change in ownership or control of the private party results in a weakening in its financial standing or support or other detriment to the project</p>	<p>government assurance of the financial robustness of the private party may be diminished and, depending on the type of project, probity and other non-financial risks may arise from a change in ownership or control which may be unacceptable to government</p>	<p>government requirement for its consent prior to any change in control. Note: private party will seek to limit this control to circumstances where substantive issues are of concern such as financial capacity and probity</p>	<p>government risk as to the adverse consequence of a change if it occurs; private party risk that its commercial objectives may be inhibited by a restrictive requirement for government consent to a change</p>

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Financial				
Interest rates pre-completion	the risk that prior to completion interest rates may move adversely thereby undermining bid pricing	increased project cost	interest rate hedging may occur including under Project Development Agreement	government may assume or share
Financing unavailable	the risk that when debt and/or equity is required by the private party for the project it is not available then and in the amounts and on the conditions anticipated	no funding to progress or complete construction	government requires all bids to have fully documented financial commitments with minimal and easily achievable conditionality	private party
Further finance	the risk that, by reason of a change in law or other event outside the scope of the contract, additional funding is needed to rebuild, alter, re-equip the facility which cannot be obtained by the private party	no funding available to complete further works required by government	private party must assume best endeavours obligation to fund at agreed rate of return with option on government to pay by way of uplift in the services charge over the balance of the term or by a separate capital expenditure payment; Government to satisfy itself as to likelihood of this need arising, its likely criticality if it does arise, and as to financial capacity of private party to provide required funds and (if appropriate) budget allocation if government itself is required to fund it	government takes the risk that private finance is unavailable
Refinancing benefit	the risk (upside) that at completion or other stage in project development the project finances can be restructured to materially reduce the project's finance costs	a beneficial change in the financing cost structure of the project	government will assure itself that likely benefit has been factored into competitive bids to avoid the risk that the private party will be allowed to earn super profits from the project	private party to benefit; government will share in limited circumstances (essentially, in symmetrical risk allocation and super profits)

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Financial				
Tax changes	the risk that before or after completion the tax impost on the private party, its assets or on the project, will change	a negative effect on the private party's financial returns and in extreme cases, it may undermine the financial structure of the project so that it cannot proceed in that form	the financial returns of the private party should be sufficient to withstand such change; with respect to specific infrastructure taxation particularly that relating to transactions with government, the private party should obtain a private tax ruling	private party

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Operating				
Inputs	the risk that required inputs cost more than anticipated, are of inadequate quality or are unavailable in required quantities	cost increases and in some cases adverse effect on quality of service output	private party may manage through long term supply contracts where quality/quantity can be assured; private party can address to some extent in its facility design	private party unless government controls inputs eg. water catchment
Maintenance and refurbishment	the risk that design and/or construction quality is inadequate resulting in higher than anticipated maintenance and refurbishment costs	cost increases where private party has assured whole of life obligation and adverse effect on delivery of contracted services and, in core services model, a corresponding adverse effect on government ability to deliver core services	private party to manage through long term subcontracts with suitably qualified and resourced sub-contractors and through formal or informal consultation processes with government	private party
Changes in output specification outside agreed specification range	risk that government's output requirements are changed after contract signing whether pre or post commissioning	a change in output requirements prior to commissioning may necessitate a design change with capital cost consequences depending on the significance of the change and its proximity to completion; a change after completion may have a capital cost consequence or a change in recurrent costs only; for example where an increase in output requirements can be accommodated within existing facility capacity	government can mitigate this risk to an extent by minimising the chance of its specifications changing and, to the extent they must change, ensuring the design is likely to accommodate it at least expense; this will involve considerable time and effort in specifying the outputs up front and planning likely output requirements over the term	government

Risk Category	Description	Consequence	Mitigation	Preferred allocation
<p>Operating</p>	<p>risk that a subcontract operator may fail financially or may fail to provide contracted services to specification</p>	<p>the failure may result in service unavailability, an inability for government to deliver core services and, in each case, a need to make alternate arrangements for service delivery with corresponding cost consequences</p>	<p>private party must carry out necessary due diligence on all subcontractors; government may carry out due diligence on principal subcontractors for probity and financial capacity and commission a legal review of the major subcontracts including the guarantees or other assurances taken by the private party; if failure does occur the private party may replace the operator or government may require operator replacement</p>	<p>private party is fully and primarily liable for all obligations to government irrespective of whether it has passed the risk to a subcontractor</p>
<p>Technical obsolescence or innovation</p>	<p>risk of the contracted service and its method of delivery not keeping pace, from a technological perspective, with competition and/or public requirements</p>	<p>private party's revenue may fall below projections either via loss of demand (user pays model) payment abatement (availability model) or operating costs increasing; for government –consequence will be failure to receive contracted service at appropriate quantity/quality including adverse effect on core service delivery in core service model</p>	<p>private party may arrange contingency/reserve fund to meet upgrade costs subject to government agreement as to funding the reserve and control of reserve funds upon default; also monitoring obligations in the contract and work on detailed, well-researched output specifications (government) and design solution (private party)</p>	<p>private party except where contingency is anticipated and government agrees to share risk possibly by funding a reserve</p>

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Market				
General economic downturn	in a user pays model, the risk of a reduction in economic activity affecting demand for the contracted service	revenue below projections	where government is the primary off-taker the private party will seek an availability payment element; otherwise the private party will ensure robust financial structure and sponsor/financier support competition	private party except to the extent that government has committed to an availability payment element or agreed to provide redress for impact of government subsidised competition
Competition	in a user pays model the risk of alternate suppliers of the contracted service competing for customers	revenue below projections arising from a need to reduce the price and/or from a reduction in overall demand, because of increased competition	private party to review likely competition for service and barriers to entry	private party except to the extent that government has committed to an availability payment element or agreed to provide redress for impact of government subsidised competition
Demographic change	the risk of a demographic/socio-economic change affecting demand for contracted service	revenue below projections	private party to review likely competition for service, barriers to entry	private party except to the extent that government has committed to an availability payment element
Inflation risk	that value of payments received during the term is eroded by inflation	diminution in real returns of the private party	private party seeks an appropriate mechanism to maintain real value eg. via linkage to CPI; government do concern to ensure its payments do not overcompensate for inflation and to avoid any double payment for after costs adjustments eg. on changes in law	private party takes risk on the methodology adopted to maintain value; government shares to the extent of agreed indexation

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Network and interface				
Withdrawal of support network	the risk that, where the facility relies on a complementary government network, that support is withdrawn or varied adversely affecting the project	negative patronage and revenue consequences	private party will seek financial redress against change which unfairly discriminates against the project particularly on a user pays project where revenue is directly affected; under an availability model private party will seek to avoid abatement if government prevention is cause of unavailability	government where the change discriminates against the project
Changes in competitive network	the risk that an existing network is extended/changed/re-priced so as to increase competition for the facility	negative patronage and revenue consequences	private party will seek financial redress against change which unfairly discriminates against the project by government subsidising competition (existing or new)	private party except to the extent that government provides redress for appropriate, discriminatory changes
Interface (1)	the risk that the delivery of core services in a way which is not specified/anticipated in the contract adversely affects the delivery of contracted services	adverse effect on delivery of contracted service, potential for default by private party and possible need for government to make other arrangements for service provision	government manages core service activities allowing it to influence the materialisation of interface risk and its consequences; other mitigants include an up-front assessment (by both government and the private party) of the likely interface issues, continual review and monitoring and development of a communications strategy in respect of delivery of the two related services; government will also specify in the contract the extent of core services and the way in which they will be delivered so that only manifest and adverse changes and deficiencies can trigger this risk	private party except to the extent that government provides redress for appropriate, discriminatory changes

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Network and interface				
Interface (2)	the risk that the delivery of contracted services adversely affects the delivery of core services in a manner not specified/anticipated in the contract	adverse effect on delivery of core services, default by private party and possible need for government to make other arrangements for core service provision	private party manages contracted service activities	private party

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Industrial relations				
Industrial relations and civil commotion	risk of strikes, industrial action or civil commotion causing delay and cost to the project	cost and time delay	private party or its sub-contractors manage project delivery and operations	private party

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Legislative and Government				
Approvals	the risk that additional approvals required during the course of the project cannot be obtained	further project development or change in business operation may be prevented	private party to anticipate requirements private	party unless government has initiated the change requiring approval
Changes in law (1)	the risk of a change in law of the State Government only, which could not be anticipated at contract signing and which is directed specifically and exclusively at the project or the services and which has adverse capital expenditure or operating cost consequences for the private party	a material increase in the private party's operating costs and/or a requirement to carry out capital works to comply with the change	government may mitigate its liability for such change by monitoring and limiting (where appropriate) changes which may have these effects or consequence on the project and via mechanisms in the contract allowing compensation only above a pre-agreed 'Significant Amount'; also requiring the private party to effect the change in such a manner that the financial effect on government is minimised and, if payment is required, that payment is made in a way and a time best suited to government (eg. pay on a progressive scale); also (in a user pays model) having in place a regulatory regime which allows pass through to end users	government; although the parties may share the financial consequences of capital cost increases in an agreed way, for example by the private party meeting a percentage of the cost up to a specific limit and government meeting any excess
Changes in law (2)	in some cases, the risk of a change in law (at whatever level of government it occurs) which could not be anticipated at contract signing which is general (ie. not project specific) in its application and which causes a marked increase in capital costs and/or has substantial operating cost consequences for the private party	requirement on the private party to fund and carry out capital works or meet a marked increase in operating costs to comply with the change	government mitigates by excluding changes such as tax changes or changes for which the private party is compensated under a CPI adjustment or similar and only allowing compensation above a pre-agreed Significant Amount; also, again mechanisms could be used to minimise and manage financial impact on government and (where appropriate) a regulatory regime to allow pass-through to end users	government; although the parties may share the financial consequences of capital cost increases in an agreed way for example by the private party meeting a percentage of the cost up to a specific limit and government meeting any excess

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Legislative and Government				
Regulation	Where there is a statutory regulator involved there are pricing or other changes imposed on the private party which do not reflect its investment expectations	cost or revenue effects	private party to assess regulatory system and may make appropriate representations	private party
Risk Category				
Force majeure				
Force majeure	the risk that inability to meet contracted service delivery (pre or post completion) is caused by reason of force majeure events	loss or damage to the asset, service discontinuity for government (may include inability to deliver core service) and loss of revenue or delay in revenue commencement for private party	private party given relief from consequences of service discontinuity; if uninsurable, private party may establish reserve funding; Government to establish contingency for alternate service delivery; if insurable, private party must ensure availability of insurance proceeds towards repair of asset and service resumption and government is to be given the benefit of insurance for service disruption costs	private party takes the risk of loss or damage to the asset and loss of revenue, government takes some risk of service discontinuity both as to contracted service and core service subject to insurance availability and will need to arrange alternative service provision the cost of which will be met from redirected service payments and (if insurable) any shortfall made up from insurance proceeds

Risk Category	Description	Consequence	Mitigation	Preferred allocation
Asset ownership				
Technical obsolescence	the risk that design life of the facility proves to be shorter than anticipated accelerating refurbishment expense	cost of upgrade	private party may have recourse to designer, builder or their insurers	private party, but in certain high technology projects costs may be anticipated and shared
Default and termination	risk of loss of the facility or other assets upon the premature termination of lease or other project contracts upon breach and without adequate payment	loss of investment of private party; possible service disruption for government	private party (and its debt financiers) will be given cure rights (time and opportunity) to remedy defaults which may lead to termination including under tripartite deed with financiers; also only serious breaches to lead to termination; if termination occurs pre completion government may (but need not) make payment for value in the project on a cost to complete basis; if occurs post completion government may negotiate a payment, generally based on fair market value less all amounts due to government; government will require step in rights to ensure access and service continuity until ownership/control issues are resolved	private party will take the risk of loss of value on termination
Residual value on transfer to government	the risk that on expiry or earlier termination of the services contract the asset does not have the value originally estimated by government at which the private party agreed to transfer it to government	capital costs incurred to upgrade the asset to the agreed value and useful life or asset demolished or removed	government will impose on the private party maintenance and refurbishment obligations, ensure an acceptable maintenance contractor is responsible for the work, commission regular surveys and inspections; it may also direct funds from the project into dedicated controlled sinking fund accounts to accumulate funds sufficient to bring the asset to agreed condition and/or (if required) obtain performance bonds to ensure the liability is satisfied	government

Appendix 4

Proformae

Statement of Economic Development Impacts PSI-1

The purpose of this document is to identify the direct/indirect and short/long term economic development impacts from this project if it proceeds with private sector participation.

Project Description

Short Term Impacts

Direct Impacts

Private Investment	\$
Additional Employment	No.
Transfer Employment (from public to private sector)	No.

Indirect Impacts

Additional Investment in Australia and New Zealand (ANZ)	\$
Additional Employment in ANZ	No.
Local R&D	\$
Exports	\$

Local Industry Participation

Key elements of the local industry participation plan:	
Local content	%
No. of Agreements (Technology Transfer with ANZ companies)	No.
Value of joint R&D Projects	\$
No. Joint Marketing and Export Arrangements (with ANZ companies)	No.
Other Aspects	
Comment:	

Medium to Long Term Impacts

Global Strategy

Are there any impacts on the global strategies of private sector proponents, over the medium to long term particularly in relation to:

Supply	Yes/No/NA
Investment	Yes/No/NA
Research and Development	Yes/No/NA
Exports	Yes/No/NA
Technology Transfer	Yes/No/NA
Other	Yes/No/NA

If yes please comment:

NSW Treasury Statement of Fiscal Impacts PSI-2

All financial data is to be presented in nominal values

Project Description

Duration of Contract

Pricing Policy

Total Funding Required \$M

Construction Cost

Financing Costs during Construction

Other (including value of assets dedicated to project eg land)

Total Funding Required \$M

Sources of Funds

Private Sector Equity

Project Debt

Public Sector Contributions

Agency Funds

State Budget

Public Sector Loans

Other

Total Funding Required

Government Contingent Obligations \$M

Description of any Government contingent obligations, guarantees, indemnities or underwriting proposed.

Assessment of monetary value of Government contingent obligations

Impact on Sponsoring Agency

	Total	Per Annum
	\$M	\$M
Balance Sheet		
Assets		
Liabilities		
Total		
Operating Statement		
Expenses		
Revenues		
Total		

Residual Assets

Description of any residual assets to be transferred to the sponsoring agency on contract expiry.

Estimate of asset value \$M

Impact on Other Agencies

	Total	Per Annum
	\$M	\$M
Description of impact on other agencies.		
Financial impact for each affected agency:		
Balance Sheet		
Assets		
Liabilities		
Total		
Operating Statement		
Expenses		
Revenues		
Total		

State Budget Impact

	Total \$M	Per Annum \$M
Capital Budget		
Outlays		
Receipts		
Total		
Recurrent Budgets		
Outlays		
Receipts		
Total		

NSW Treasury – Terms and Conditions for Negotiations of Private Sector Infrastructure Projects PSI-3

The Terms and Conditions Agreement jointly completed by Treasury and the relevant agency.

Agency

Private Consortium

Parent Company and Special Purpose company

Private Sector Bankers

Project Costs

Nominal Dollars
\$M

Land Cost

Construction Cost

Capitalised Interest

Financed by:

Government Contribution

Private Sector Equity

Private Sector Debt (List Sources)

Purpose

A full description of the proposed project

Operations & Maintenance

Description of operational costs and revenues

Term

Construction Period

Debt finance term

Franchise period

Proposed Completion Date

Project Construction Contract

Equity Investor Commitment

Costs

The agency should engage consultants and legal counsel normally on the basis of fixed price or capped arrangements. The agency should normally fund from internal sources all related expenses associated with consultants and legal counsel.

Escalation Formula

Description of cost and revenue escalation formula.

Project Cash Flow Model

Agency to develop a Project Cash Flow Model and agree it with Treasury. Its primary purpose would be to calculate the forecast costs and revenues associated with the project and determine the financial risk and rewards to Government

Government and Private Sector Undertakings

Agency to provide a detailed list of those items of the project that would be subject to negotiations before final contract signing.

Benefits to Government

Agency to prepare a financial analysis that shows a net benefit to Government from delivery of the project via private sector financing as opposed to the normal Government delivery process.

Economic Development Impact Appraisal

Agency to provide a description and quantification of the economic development benefits from investing in the project including investment, employment, exports, R&D and other benefits.

Risk Management Plan

Agency to list the major risk aspects associated with the project and the management processes to alleviate those risks.

Loan Council Treatment

Treasury to prepare an assessment of the likely Loan Council treatment of the project.

Events of Default and Compensation

Agency to list default conditions and compensation payments that would be associated with the final contract.

Accounting Treatment

Agency to prepare a statement of the accounting treatment for the proposed project covering balance sheet and operating statement.

Taxation Treatment

Agency to provide preliminary assessment of the likely position regarding tax ruling for the project.

Agency Budget Plan

Agency to prepare a cash flow plan covering the Government costs.

Foreign Exchange Risk

Agency to establish need for foreign exchange coverage.

Conditions Precedent

Agency to list likely conditions precedent to be included in the contract.

Appendix 5

References

Code of Practice for the Construction Industry. NSW Construction Policy Steering Committee, July 1996. Available from the world wide web at:
<http://www.cpsc.nsw.gov.au/publications/>

Code of Practice – NSW Government Procurement. Prepared by the Department of Public Works and Services for the State Contracts Control Board, October 1999. Available from the world wide web at:
<http://www.dpws.nsw.gov.au/DPWS/policy/areas+of+expertise/procurement/procurement+policy+documents.htm>

Code of Tendering for the Construction Industry. NSW Construction Policy Steering Committee, July 1996. Available from the world wide web at:
<http://www.cpsc.nsw.gov.au/publications/>

Code of Tendering – NSW Government Procurement. Prepared by the Department of Public Works and Services for the State Contracts Control Board, October 1999. Available from the world wide web at:
<http://www.dpws.nsw.gov.au/DPWS/policy/areas+of+expertise/procurement/procurement+policy+documents.htm>

Economic Appraisal: Principles and Procedures Simplified (TPP 99–1). NSW Treasury, 1999. Available from the world wide web at:
http://www.treasury.nsw.gov.au/pubs/tpp99_1/prin_pro.htm

Financial Appraisal Guidelines (TPP 97–4). NSW Treasury 1997. Available from the world wide web at:
http://www.treasury.nsw.gov.au/pubs/tpp97_4/guidline.htm

Guidelines for Economic Appraisal (TPP 97–2). NSW Treasury, 1997. Available from the world wide web at:
http://www.treasury.nsw.gov.au/pubs/tpp97_2/ea-index.htm

Implementation Guidelines for the Code of Tendering and Code of Practice for the Construction Industry. NSW Construction Policy Steering Committee, July 1996. Available from the world wide web at:
<http://www.cpsc.nsw.gov.au/publications/>

Implementation Guidelines for the Code of Tendering and Code of Practice – NSW Government Procurement, July 1996. Prepared by the Department of Public Works and Services for the State Contracts Control Board, October 1999. Available from the world wide web at:
<http://www.dpws.nsw.gov.au/DPWS/policy/areas+of+expertise/procurement/procurement+policy+documents.htm>

Infrastructure Partnerships Implementation Guidelines – Version 2. Department of Public Works and Services, 1998

New South Wales Government Capital Works Investment: Capital Project Procurement Manual, October 1993 and updates. NSW Construction Policy Steering Committee. Available from the world wide web at:
<http://www.cpsc.nsw.gov.au/cppm>

NSW Government Procurement Manual, 2000. Prepared by the Department of Public Works and Services. Available from the world wide web at:
<http://www.dpws.nsw.gov.au/DPWS/policy/areas-of-expertise/procurement/procurement-policy+documents.htm>

New South Wales Government White Paper: Construct New South Wales, July 1998. NSW Construction Policy Steering Committee. Available from the world wide web at:
<http://www.cpsc.nsw.gov.au/ConstructNSW/>

Partnerships Victoria – Overview. Department of Treasury and Finance, Victoria, 2001. Available from the world wide web at:
<http://www.dtf.vic.gov.au/dtf/rwp323.nsf/webnav2/Business+and+the+Government>

Partnerships Victoria – Practitioners' Guide. Department of Treasury and Finance, Victoria, 2001. Available from the world wide web at:
<http://www.dtf.vic.gov.au/dtf/rwp323.nsf/webnav2/Business+and+the+Government>

Partnerships Victoria – Public Sector Comparator – Technical Note. Department of Treasury and Finance, Victoria, 2001. Available from the world wide web at:
<http://www.dtf.vic.gov.au/dtf/rwp323.nsf/webnav2/Business+and+the+Government>

Partnerships Victoria – Risk Allocation and Contractual Issues. Department of Treasury and Finance, Victoria, 2001. Available from the world wide web at:
<http://www.dtf.vic.gov.au/dtf/rwp323.nsf/webnav2/Business+and+the+Government>

Probity Auditing: When, Why and How. NSW Independent Commission Against Corruption, 1996. Available from the world wide web at:
http://www.icac.nsw.gov.au/pub/public/pub2_22cp.pdf

Policy Statement, NSW Government Procurement—A whole-of-government framework. Prepared by the Department of Public Works and Services for the State Contracts Control Board, 1999. Available from the world wide web at:
<http://www.dpws.nsw.gov.au/DPWS/policy/areas-of-expertise/procurement/procurement-policy+documents.htm>

Total Asset Management Manual. NSW Department of Public Works and Services, 2000. Available from world-wide web at:
<http://www.gamc.nsw.gov.au/tam2000>

Appendix 6

Contacts

Premier's Department

Director-General
Level 39
Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000

Executive Director
Infrastructure Coordination Unit
Level 37
Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000
Phone: (02) 9228 3200
Fax: (02) 9228 4004
Email: *wwg@premiers.nsw.gov.au*

Treasury

Director
Private Projects Branch
Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000
Phone: (02) 9228 3213
Fax: (02) 9228 4041

Department of Public Works and Services

Group General Manager
Strategic Procurement Services
Level 23
McKell Building
2–24 Rawson Place
Sydney NSW 2001
Phone: (02) 9372 8816
Fax: (02) 9372 8844
Email: *PPF@dpws.nsw.gov.au*

**Working with
Government**
Guidelines for
Privately Financed
Projects

November 2001

Contacts

Premier's Department

Director-General
Level 39
Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000

Premier's Department

Executive Director
Infrastructure Coordination unit
Level 37
Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000
Phone: (02) 9228 3200
Fax: (02) 9228 4004
Email: wwg@premiers.nsw.gov.au
Web: <http://www.nsw.gov.au/wwg>

Treasury

Manager
Infrastructure Assessments
Governor Macquarie Tower
1 Farrer Place
Sydney NSW 2000
Phone: (02) 9228 3213
Fax: (02) 9228 4041

Department of Public Works and Services

Group General Manager
Strategic Procurement Services
Level 23
McKell Building
2-24 Rawson Place
Sydney NSW 2001
Phone: (02) 9372 8816
Fax: (02) 9372 8844
Email: PPF@dpws.nsw.gov.au

Photo Credits

Cover photographs courtesy Department of State and Regional Development (Stadium Australia, Harbour Tunnel approaches); Connex Sydney Pty Ltd (light rail); Sydney Water (water filtration plant)