Public private partnerships guidance material

Overview

Queensland the Smart State

Queensland Government
Department of Infrastructure and Planning

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Introduction

In September 2001, the Queensland Government released its policy on public private partnerships, joining governments throughout the nation and around the world in exploring smarter ways to develop and maintain assets which serve the community.

From major transport links to educational facilities, there are constant demands on government to deliver infrastructure which meets the needs of a 21st Century community, focussed on the development of knowledge and wealth through learning, interaction and exchange.

A partnership approach creates the opportunity to apply the respective skills of the public and private sectors to deliver effective infrastructure services in a timely manner, extracting the best possible value for money on behalf of taxpayers.

This guidance material describes the tasks involved in implementing Queensland's public private partnership policy. It sets out a comprehensive framework for analysing and delivering all major infrastructure projects that support the government's strategic objectives. The framework provides for rigorous analysis of the best available infrastructure delivery options through either the public or private sector. It proposes a fair process for applying competitive forces to drive innovation and cost effectiveness.

By applying the approaches within the guidance material, the government can ensure that all opportunities for private sector involvement are appropriately examined. Why should the private sector get involved in public infrastructure? A critical issue in the delivery of infrastructure is the broad range of risks and exposures that government confronts.

Through design, development and a lifetime of operation of infrastructure services, there are a range of 'risk' events that could occur which may add to cost or impede the delivery of public services. The perennial issue for government is how best to prevent these sorts of 'risks' from happening, or if they do happen, how best to manage that eventuality.

If the private sector is better able to manage risks involved in a project, it makes sense for government to utilise those skills. But experience has shown that some risks continue to be best managed by government. By constructing a public private partnership, risks can be allocated to those best able to manage them, rather than expecting the private or public sectors to carry the full exposure by themselves.

The public private partnership approach can thereby help government to contain costs, and help to ensure that the infrastructure underpinning important community services continues to serve its purpose throughout its planned effective life. It enables government to harness the capabilities of the private sector, while maintaining an ongoing control over the performance of infrastructure in meeting community needs.

Public private partnerships encompass a broad spectrum of project delivery options. This policy applies to projects involving design, build and operate; design, build, finance and operate; and equity sharing arrangements. Further, there are numerous variations on these concepts, including build, own, operate and build, own, operate, transfer structures. Queensland's public private partnership policy encompasses the full spectrum of these options.

While this guidance material is applicable to the full range of public private partnership delivery options, it is principally focussed on the privately financed public private partnership model that entails equity risk transfer. This option incorporates the options termed 'design, build, finance and operate' and 'project finance initiative' (named after the UK approach) type transaction. The privately financed public private partnership delivery model represents what is likely to be the most variant from traditional procurement. Some of the principles and positions presented will not be applicable to all public private partnership delivery options and only those that are relevant to the specific option being proposed should be utilised.

After identifying the service requirements of the project, this guidance material focuses on exploring the range of delivery options to determine which mechanism or combination of mechanisms will deliver value for money for government. This analysis will range from the traditional options available to government (agency delivery and management, through D&C or government owned corporation delivery) through the range of public private partnership delivery options that are available.

Many of the project structures within this spectrum are not new to Queensland. This guidance material builds upon that history to present a coherent process for engaging the private sector in infrastructure delivery, the application of which will be consistent across government.

In dealing with large and costly infrastructure services, responsible government requires careful assessment of the delivery options which can offer the best value for money – meeting the service requirement in the most cost effective way. A public private partnership may not always be the answer, so it is important to closely investigate the technical and policy issues, the costs and the risks involved before choosing a delivery approach.

This guidance material aims to guide government and private sector personnel on the process and issues they are likely to confront in analysing and developing major infrastructure proposals, and where appropriate, delivering public private partnerships. It is not a 'how to' manual. Circumstances differ widely between each infrastructure proposal, and specialist expertise is required to ensure the analysis is comprehensive. Rather, the purpose of this guidance material is to give people a working knowledge of the methods and issues that arise in infrastructure analysis, so they are better placed to interpret and analyse technical and specialist advice.

Principles

The aim of this guidance material is to support the objectives of Queensland's public private partnership policy, namely:

- to deliver improved services and better value for money through appropriate risk sharing between public and private sector parties;
- to encourage private sector innovation;
- to optimise asset utilisation; and
- to promote integrated whole of life management of public infrastructure.

Queensland's public private partnership policy has been developed to support the government's ongoing priorities of:

- More jobs for Queenslanders.
- Safer and more supportive communities.
- Community engagement and better quality of life.
- Valuing the environment.
- Building the regions.

A key characteristic of the policy initiative is its flexibility, which ensures that there is the ability to respond to the changing needs of our communities in an evolving social and economic environment.

The guiding principles which underlay this policy framework include:

- **Clarity and certainty of process** to provide the private sector with the confidence to invest in the development of high quality, cost-effective and efficient project solutions.
- **Value for money** focus, to ensure the objectives of the government are delivered by the mechanism best able to deliver value for money.
- **Competitive process** to drive value for money and innovation.
- **Consistency** with government policies, objectives and planning principles, and with the public private partnership policies being developed in other jurisdictions.
- **Analytical rigour** which focuses on objective, whole of life, risk-adjusted costing as part of a thorough investigation of available delivery options.
- **Effective risk allocation** which allocates risk to the party best able to manage it.
- **Protection of genuine intellectual property** to encourage development of innovative solutions.

- **Transparency and accountability** through clear definition of the process and of the respective roles and responsibilities of the government and private sector parties.
- **Clear definition and understanding of project outcomes** through constructive information exchange with potential proponents. This will be undertaken through a structured process which ensures that all proponents are treated in a fair and equitable manner.

The scope of the public private partnership policy encapsulates the delivery of 'hard' and 'soft' infrastructure facilities and related non-core services, such as operation and maintenance of the assets.

This guidance material is consistent with the objectives of the State Purchasing Policy, that is to:

- advance government priorities;
- achieve value for money; and
- ensure probity and accountability for outcomes.

The guidance material comprises a framework document which sets out a process for analysing and, where appropriate, implementing public private partnership Proposals, together with a range of supporting documents which provide further detail on specific aspects of the public private partnership process, including:

- risk management
- project resourcing
- probity and process governance
- contract development and management
- business case development.

This guidance material will be supplemented over time through the release of further supporting documents.

Process framework

The proposed process to be used in delivering a service under the public private partnership framework consists of six separate but interdependent stages:

1. Service identification
2. Preliminary assessment
3. Public private partnership business case development

4. Expression of interest
5. Binding bids
6. Contract management

Stage 1—Service identification

Departments will use their existing strategic planning and service review programs to identify the need for specific service developments. If the expected net present value of a strategic service priority will exceed a whole-of-life project cost of $100 million, then the Department must notify the Department of Infrastructure and Planning. The Strategic Infrastructure Procurement Division of Department of Infrastructure and Planning, with whom responsibility for the public private partnership policy and the framework sits. will then assist the agency to identify the initial scoping and output requirements of the project. The portfolio minister may write to Cabinet Budget Review Committee seeking to exempt from the framework a project which lies above the threshold, or include a project that lies below the threshold, having first consulted with the Deputy Premier, the Minister for Infrastructure and Planning, and the Treasurer.

Any unsolicited proposal will be assessed for priority against existing planning frameworks.

Stage 2—Preliminary assessment

The work undertaken in the preliminary assessment stage must be sufficient to enable Cabinet Budget Review Committee to assess the priority of the project based on affordability and value for money. During this stage, initial qualified estimates are generated on policy, environment, economic and financial impact. These provide the foundations for the public private partnership business case.

At this stage an initial government project team and steering committee will be formed.

The Preliminary Assessment Stage will determine if it is likely that the solution will provide value for money through public private partnership delivery as a result of analysis to determine the risks that could be better managed by the private sector. At the end of the Preliminary Assessment Stage, Cabinet Budget Review Committee will decide whether the project has sufficient priority to warrant further investigation using the framework

Stage 3—Public private partnership business case development

During this stage, a government project team and steering committee will be formalised. The principal purpose of this stage is to investigate the options and prepare a business case by comparing the delivery of the required services using best practice traditional procurement processes with alternative private sector delivery.

Detailed analysis of the project during this stage presents the government with a detailed case upon which to make a decision to take the project to the private sector if it is likely to represent a value for money delivery option.

This includes the development of the public sector comparator model and a hypothetical partnership model. The public sector comparator model represents Government's best estimate as to the whole of life cost of delivery for the project via traditional delivery. The partnership model represents an estimate of the delivery option that the private sector is likely to adopt for the project. The partnership model forms a key piece of information by which government can determine the likelihood of value for money through public private partnership delivery. It is also used to assist in the interpretation and analysis of private sector bids at a later stage.

Fundamental to this stage is the identification of all risks confronting the project, and the allocation of those risks to the party (private or public) best able to manage those risks. The proposed risk allocation, and the service performance requirements, will form the basis of the contractual conditions government will specify in seeking to invite bids.

At the end of this stage, Cabinet will decide on the priority and affordability of the proposal, the preferred delivery model and allocate any necessary budget funding.

Stage 4—Expression of interest

If Cabinet agrees to pursue a public private partnership delivery option, expressions of interest will be called to develop a shortlist of proponents which have demonstrated, in their expression of interest, that they have the technical and financial capabilities to deliver the service requirement on a value for money basis.

At the end of this stage, Cabinet Budget Review Committee will be asked to confirm the selected shortlist and approve going to the next stage, that is, the binding bid stage.

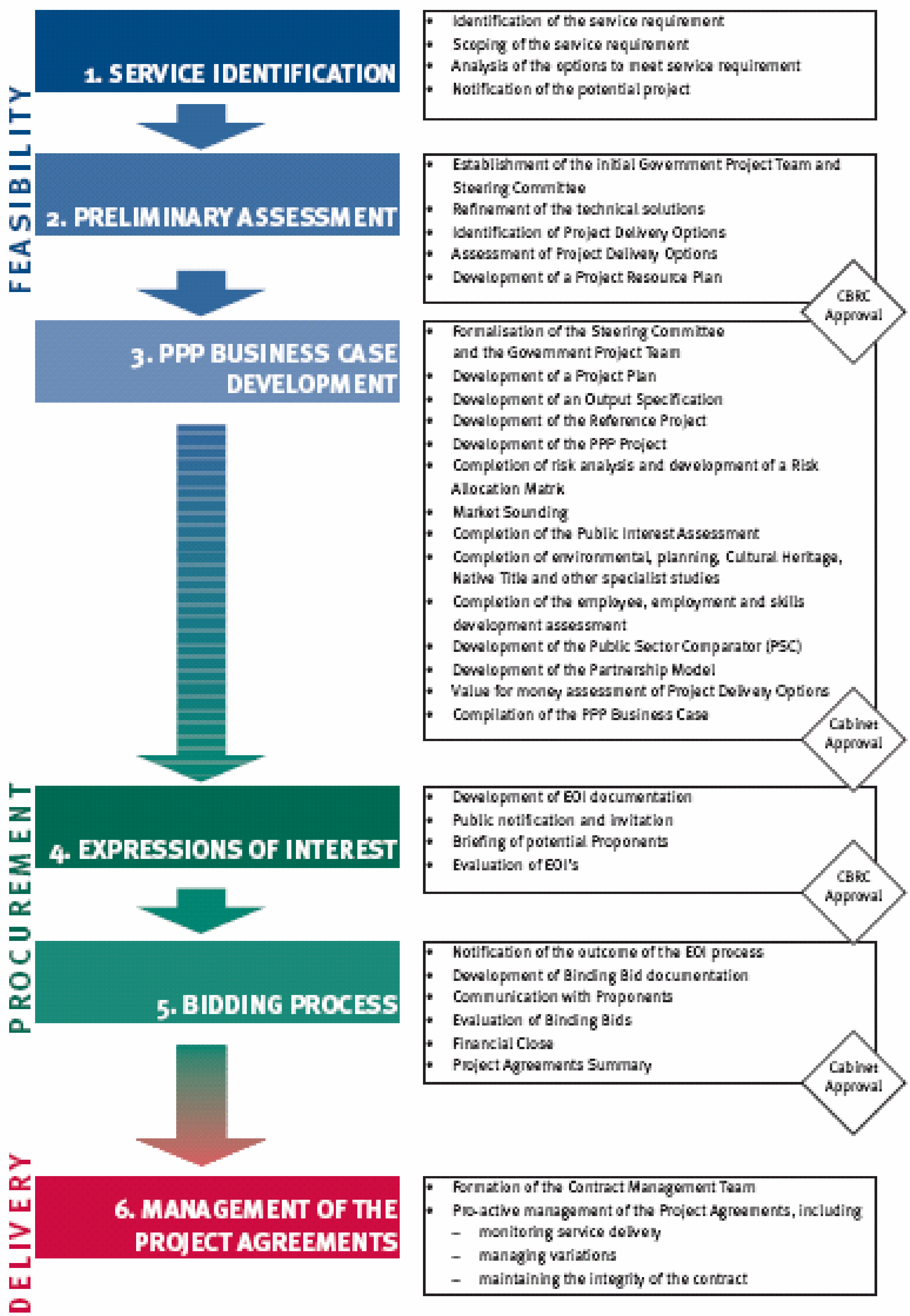
Stage 5—Binding bids

This stage commences with the invitation to submit binding bids and concludes with signing a contract to deliver the project, provided that value for money has been demonstrated. A recommendation to Cabinet of the preferred proponent will be based on an assessment of all bids and identify that most likely to deliver the best value for money. A series of legal agreements will encapsulate the details of government requirements through the delivery and operation of the infrastructure service. Those agreements will also identify mechanisms to deal with contractual events such as imposition of performance standards, termination and/or transfer.

Stage 6—Management of the contract stage

Management of the contract is critical to ensuring that the public private partnership delivery option achieves value for money in the delivery of the service over the term of the project. A specialist contract management team within the line agency will generally manage the contract. They will have responsibility for implementation of the partnership project and managing the ongoing relationship to ensure service delivery is maintained to the required standard.

STAGES OF THE VALUE FOR MONEY FRAMEWORK



Unsolicited proposals

If an agency receives an unsolicited proposal from a private party addressing a service requirement identified by that party, the proposal will be assessed for priority against the relevant agency's strategic plan and the South East Queensland Infrastructure Plan and Program. If the proposal is considered by the agency to be a priority, it will be progressed either:

- within this framework in the same manner as agency-generated outputs or
- pursuant to an exclusive mandate to analyse the project's feasibility. (For further detail on exclusive mandates, refer to appendix 1 of the framework).

Any unsolicited proposal seeking to place any risks, costs or payment obligations on government must, if pursued, be subject to a competitive bidding process to ensure that it represents a value for money outcome to government.

In progressing unsolicited (and all other) proposals, the government will take all reasonable steps to protect genuine Intellectual Property of the private sector. This can be achieved through use of an output based specification during the competitive process.

Risk

"Risk is the chance of an event occurring which would cause actual project circumstances to differ from those assumed when forecasting project benefit and costs". [1] Because management of risks holds the key to project success or failure, "projects are about risks, about their evaluation and their subsequent acceptance or avoidance".[2]

The 'science' of risk management seeks to identify, prevent, contain and mitigate risks in the interests of the project.

Typical risk categories for infrastructure and service delivery projects (in general) and in public private partnership projects (in particular) are:

- site risk
- design, construction and commissioning risk
- sponsor and financial risk
- operating risk
- market risk
- network and interface risk

[1] Chris Furnell, Risk identification and risk allocation in project finance transactions, Paper presented at the Faculty of Law, The University of Melbourne, May 2000, p. 1.
[2] Allen & Overy, from Furnell, ibid., p.7.

- industrial relations risk
- legislative and government policy risk
- force majeure risk
- asset ownership risk.

The Risk management supporting document aims to:

- identify all major risks relevant to public private partnership projects and outline the commercial issues associated with them;
- increase agencies' understanding of risk allocation and the likely objectives of public and private parties when negotiating risk allocation; and
- indicate the government's likely preferred position on allocating major risks and offer guidance to government practitioners on how each of these risks may be best addressed in their particular project, recognising that each project has unique features.

Probity

In pursuing partnerships with the private sector for the provision of infrastructure services, the Queensland Government is committed to a process which is transparent and accountable and which ensures that all proponents are given fair and equitable treatment. In this regard, the public private partnership process will be underpinned by probity practices that ensure that the procedural integrity of the process is maintained. This is consistent with the objectives outlined in the State Purchasing Policy.

It is the responsibility of the government and its representatives to ensure that probity is maintained. This includes:

- ensuring conformity to processes;
- facilitating accountability;
- ensuring that proponents are treated in a fair and equitable manner;
- encouraging commercial competition on the basis that all bids will be assessed against the same criteria; and
- preserving public and proponent confidence in government processes.

The Probity and process governance supporting document provides a detailed outline of how agencies can meet their probity responsibilities as they investigate public private partnership opportunities.

Project resourcing

Successful implementation of the public private partnership process requires the establishment of a dedicated government project team which has an appropriate mix of skills and experience across key disciplines relevant to the project, including technical, commercial and financial. The government project team will also be supported as necessary by specialist external advisers in the areas of legal, financial, technical, planning, industrial relations and communications.

A project steering committee should be established to oversee the development of the project and to deal with key commercial and policy issues.

A project director will have overall responsibility for the day to day management of the project, including responsibility for management of the government project team and external advisers. The project director will be required to have highly developed project management and commercial skills and a knowledge of government processes.

A probity auditor should be engaged to observe and review the competitive bid process and establish whether the procedures have been administered fairly and impartially to all parties.

The project resourcing supporting document aims to assist agencies in assembling resources, including the procurement of specialist advisers, and to develop a project structure for a public private partnership project. It is advisory rather than mandatory, providing guidance on good practice.

Business case development

Development of the business case represents a key aspect of the feasibility stage of the public private partnership process. The business case provides the analytical rigour that allows for effective government decision making and value for money procurement.

During the development of the business case, the agency undertakes a detailed analysis of the delivery options that may provide value for money.

The business case will include significant analysis of the risk and issues surrounding the project and will include the undertaking of significant studies to identify, quantify and where appropriate mitigate risks that the project may experience. This analysis may include the examination of environmental, planning and geotechnical matters as well as the allocation of risk to the party best able to manage it.

A detailed hypothetical financial model of the traditional delivery option (the reference project) is developed on a risk adjusted, whole of life basis. This model, known as the public sector comparator, becomes the benchmark against which value for money assessment is made.

A similar model, known at the partnership model, is developed to allow the government project team to better understand the private sector's key drivers and possible solutions to the project (ie: the likely private sector's delivery option). The partnership model is based upon the allocation of risk to the party best able to manage it.

The business case development supporting document provides the next level of detail on the steps required to complete the public private partnership business case as outlined in the framework document in stage 3.

This supporting document provides significant additional information on all aspects of business case development including:

- reference project
- output specification
- public sector comparator
- partnership model
- business case analysis including value analysis, sensitivity and scenario analysis, bankability etc.

It also provides information regarding the administration and outputs from the business case development stage of the public private partnership process.

Contract development and management

The nature of privately financed public private partnership projects requires a number of contractual mechanisms that may be new to some agencies. An understanding of these mechanisms and how they allow for risk allocation, mitigation and management are important elements for the development of the draft contract. While this work would be undertaken by the legal advisor, an understanding of the contractual mechanisms is required to assist in the development of the public private partnership business case.

The draft contract is then provided to potential proponents during the binding bid stage. This allows for government to discuss specific contractual issues during the competitive process in line with probity requirements.

Following the selection of preferred bidder and financial close, the project moves into the implementation phase. For government, this presents the contract management phase. Given the long term nature of the contracts associated with public private partnership projects, effective contract management is required to ensure ongoing success of the project.

The Contract development and management supporting document provides detail on the type and nature of contracts that will be developed and utilised during the development and delivery of a public private partnership project. The range and scope of contractual documents in a public private partnership project will be familiar to line agencies. What may be foreign territory is the fine detail of the contracts and the interrelationship between the various documents.

The supporting document provides a guide as to the parties involved and their roles within the ongoing partnership. It gives an understanding of the relationships between the various parties including government, financiers, special purpose vehicles, contractors and subcontractors. It identifies the issues that may arise between the parties and possible solutions.

The contract management section of the document explains the key contract management implications, including the main pitfalls and suggested ways of avoiding them. This includes the various mechanisms for monitoring and encouraging optimal performance.

For further information:

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