

# VERIFIED VERSION

## PUBLIC ACCOUNTS AND ESTIMATES COMMITTEE

### **Inquiry into Effective Decision Making for the Successful Delivery of Significant Infrastructure Projects**

Melbourne — 21 March 2012

#### Members

Mr N. Angus

Mr P. Davis

Ms J. Hennessy

Mr D. Morris

Mr D. O'Brien

Mr M. Pakula

Mr R. Scott

Chair: Mr P. Davis

Deputy Chair: Mr M. Pakula

#### Staff

Executive Officer: Ms V. Cheong

#### Witnesses

Professor G. Hodge, Director, Centre for Regulatory Studies, Monash University; and  
Associate Professor C. Duffield, School of Engineering, University of Melbourne.

**Necessary corrections to be notified to  
executive officer of committee**

**The CHAIR** — I declare open the Public Accounts and Estimates Committee hearing on the inquiry into effective decision making for the successful delivery of significant infrastructure projects. On behalf of the committee I welcome Dr Graeme Hodge, director, centre for regulatory studies, Monash University, and Associate Professor Colin Duffield, school of engineering, University of Melbourne. Members of Parliament, departmental officers, members of the public and the media are also welcome.

In accordance with the guidelines for public hearings, I remind members of the public gallery that they are not to participate in any way in the committee's proceedings. Only officers of the PAEC secretariat are to approach PAEC members. Officers, as requested by Dr Hodge or Associate Professor Duffield, can approach the table during the hearing to provide information by leave of myself as Chair. Written communication to witnesses can only be provided via officers of the PAEC secretariat. Members of the media are also requested to observe the guidelines for filming or recording proceedings in the Legislative Council committee room, and no more than two TV cameras are allowed at any one time in the allocated spaces. I remind TV camera operators to remain focused only on the persons speaking and that panning of the public gallery, committee members and witnesses is strictly prohibited. As previously advised to witnesses here today, I am pleased to announce that these hearings are being webcast live on the Parliament's website.

All evidence taken by this committee is taken under the provisions of the Parliamentary Committees Act, attracts parliamentary privilege and is protected from judicial review; however, any comments made outside the precincts of the hearing are not protected by parliamentary privilege. This committee has determined that there is no need for evidence to be sworn; however, witnesses are reminded that all questions must be answered in full and with accuracy and truthfulness. Any persons found to be giving false or misleading evidence may be in contempt of Parliament and subject to penalty.

All evidence given today is being recorded. Witnesses will be provided with proof versions of the transcript to be verified and returned within two working days of this hearing. Verified transcripts and PowerPoint presentations will be placed on the committee's website within two weeks following this hearing.

Following a presentation by the witnesses, committee members will ask questions relating to the inquiry. Generally the procedure followed will be that relating to questions in the Legislative Assembly. I ask that all mobile telephones be turned off. I now call on the witnesses to give a brief presentation of no more than 4 minutes if desired.

**Prof. HODGE** — We will make a statement for 4 or 5 minutes. It is a different take on our submission rather than just repeating the submission. Thanks very much to the committee for inviting our input today.

When I look at our submission, Colin and I reckon we made four broad points. Your inquiry is really focusing on competencies and skills, and they are very important. Our submission makes the point that there a whole bunch of skills — a range of professional skills from urban planning and conception through to construction and life maintenance — that are clearly crucial. However, many of those skills are framed in a commercial and technical nature, and our first point through our submission was that proper governance of infrastructure projects matters as much if not more than these narrower project delivery skills.

It seems to us that the capacity for governance of projects needs greater emphasis. To our way of thinking the task of governments has always been to govern well, not just simply deliver infrastructure like smart electricity meters or new food markets. The task is to govern with integrity and in the public's interest — a particularly important point, I suspect, given the air of confidence with which some groups come to the committee announcing that the government should just get on and supply a pipeline of projects, particularly from firms that would no doubt like to see a nice slice of the revenue for either financing or other reasons.

The second point we make is that there has clearly been a longstanding concern about professional skills in government, and the criticism is often made that professional skills are thin; stronger engineering, project management and contract administration skills are required. Clearly for the past two or three decades governments have increasingly tended to buy those skills in, and we agree that that is possible and sensible. But the concern here is not necessarily just about the depth of skills; it is really about the long-term nature of meeting the public interest.

We think there is a potential misalignment between short-term commercial interests at play in the midst of deals and the government's responsibility to pursue the public's interest in the longer term. Whether it is M1 upgrades

or renegotiating desal plants, clearly there is the need for significant professional competence in order to underpin this longer term public interest, and we make a number of comments about transparency and accountability in our submission, which we will not go into.

Colin and I have both travelled extensively internationally, and the third point is that it is heart-warming to see Victoria's PPP guidelines leading international practice and being adopted in many places around the world. I think they have provided not only an ideal but a great model for practices, not only nationally but internationally. They have encouraged improved practices and have provided a benchmark for better project practice; however, the guidelines also leave a range of governance issues up to the government of the day.

The last point that we would make, on page 4, concerns centralisation and decentralisation. We suspect that neither full decentralisation nor full centralisation fits as a kind of one-size-fits-all model for undertaking infrastructure projects. Clearly we need a centralised planning regime with professionals involved to provide optimum strategic benefits for long-term investments. For project delivery we have said governments need strong skills to match those of the private sector so that both sides of the table are equally matched in negotiating the deal. That suggests centralisation is sensible in order to get that critical mass of skills. However, on the other hand we suspect that you do need sector-specific knowledge from professionals out there in particular sectors, and hence you need some degree of decentralisation, because that sector-specific knowledge is greatest at the local level.

This question of centralisation versus decentralisation to us depends on the number of transactions, as well as knowledge management issues. In an area such as roads, where there are many transactions and there is strong local knowledge, it may well be that a good deal of decentralisation is sensible. In an area such as the justice sector, where transaction numbers are low and sector-specific knowledge or, say, building facility availability is thinner, in our view such decentralisation is less needed. Thank you. That completes our opening statement.

**The CHAIR** — Outstanding! Thank you. That is a really succinct summary of some really key issues. I am not sure where to begin, but I will have a crack at the issue about the pipeline. I think I understood you in effect to suggest that the argument that we should just fill up the pipeline of projects to keep everybody busy working is essentially a self-interest sort of view. That is what I understood. If that is not what you were saying, please advise me, but I will go from that to the issue, again, of the parties' interests, which is a fundamental issue about negotiating best outcomes.

If the governance model prescribes that the role of government in delivering infrastructure is to do it cost effectively at the least cost for the taxpayer — in the most efficient manner to get the best value for money for the taxpayer — then clearly we have a real contest in terms of the self-interest of the private sector. No matter what case they plead in terms of it being in the community interest to have all of this activity going on and for us to be your partners, at the end of the day business is in the field of operating at profit. That profit in regard to government projects comes from the taxpayer. We must essentially see that there is a contest around how those contracts are negotiated. It is a major difficulty for this committee to come to a view, which I want you to tease out if you are able to, on the centralised versus decentralised skill set.

You have touched on that ever so briefly, but it is fundamental. The basic measurement is that we do about one-tenth of the infrastructure projects that the UK does. Therefore we have a critical mass issue, so how do you develop a skill set that is competent to match or stand against the interests of the private sector operators who are doing both private and public projects on a continual basis and therefore have a skill set that is generally superior to the public sector?

**Prof. HODGE** — There are multiple questions. I might ask Colin to lead off.

**Assoc. Prof. DUFFIELD** — I will pitch into the pipeline of project one as a starting place — and thank you for letting us come here. Being an engineer by first training I would hold a contra view to some of my colleagues that in fact infrastructure expenditure is all about just spending for the sake of spending. The real fundamental reason for investing in anything is to get return. From a government perspective return comes via productivity, via generating economic growth for my children and my grandchildren, or your grandchildren; therefore some of the big-ticket items in respect to 'Where should we invest?' become paramount. Some recent work by the United Nations and also the World Bank has established that economic growth is most strongly connected to investments in telecommunication, energy and transport.

If you put everything else to rest, those three large-ticket items seem to be driving economies around the world. For our state and our country to remain at the leading edge or at least in the group of countries that are at the forefront, I think strategic investment is far more important than pipeline, and then pipeline becomes the issue in respect to depth in market such that we can efficiently deliver what we are doing, as opposed to the driver as to why we might invest. So I think your question is right in picking up that we think you need sufficient expertise to be efficient in what you do, but I would certainly question whether the drive is just to have a pipeline, which I have heard some suggest is the right answer, but I would like to think that my politicians would think about that strategic outcome.

The best example I use in that is China. When they were talking telecommunications, they did not put copper cables in the ground at all; they jumped technologies, from really no telecommunications to wireless-based communication, to put themselves on a strategic footing for the next dimension of investment. It was not simply a matter of, 'We've got old assets; let's just put some money into them'. It was about 'What do we need to invest in?'

**The CHAIR** — As tempted as I am to ask you a direct question about the NBN, I will not, other than to say I observed in Kenya recently exactly the same model, where it went from zero communications straight to wireless, and there is virtually universal coverage throughout Kenya. In fact even in remote national parks you are likely to find a Masai pull out a BlackBerry and start googling a question that a tourist might ask. Anyway, that is by the way. My point is that we have to think laterally about the knowledge that we apply for solutions.

**Prof. HODGE** — That is exactly right. If I may add something to this question of pipeline, I think there has been a language in the last decade or two from works priorities and needs to pipeline. In some senses it is a dangerous language change. We used to talk about public works priorities and lists and so on. That seems to have disappeared, and we are now at a time when ideas come from all sorts of strange areas: suddenly we need a tunnel that goes from one side of Melbourne to the other because someone made it up. It is as if we are in an age when ministers can walk into a shop and say, 'I'll have one of those and one of those, thanks', and that's our legacy. I think that is dangerous at the same time as business is saying, 'You ought to be providing us with a pipeline of jobs'.

I think, as Colin does, it comes down to needs. You might say 'social return on investment', or you might say 'works priorities', but we ought to be getting back to that language of works priorities as being the driving force here. Part of this has to be, I guess, as well having a dedicated and free and fearless public service that is willing to start talking again about works priorities in complex urban planning and trying to get away from this kind of notion that one magic new large infrastructure project will solve Melbourne's problems. To me one of the good reasons that Melbourne is one of the world's most livable cities is that it has had a highly professionalised urban planning project planning, transport planning history, and you go through complex network models and cost-benefit analyses, as we have done, so more often than not you end up investing in appropriate projects.

**Assoc. Prof. DUFFIELD** — I will lead off on your second question, if I may, which was really talking about competencies within the sectors and what skill sets government needs to match it to not have a symmetry between private sector and government. When we talk large-scale capital investment, if I am honest with you, I hold the view that government officials in this space actually have to be more gifted than private people, insofar as in the private sector, if I go to one of the large construction houses, be it Leighton Contractors or Holland, or Siemens in the electrical industry, or those matters, the focus of their work is about the delivery phase of the job.

In a sense it is all about the dollar and driving the dollar down, whereas the government official has to be cognisant of policy directions and the balance between community outcomes as well as the dollar figure. And they have to actually bring in a community, along with an elected Westminster-type parliamentary system with them to agree with a decision in a timely manner. Therefore I would say their skill set has to include political skills, commercial skills and business acumen, and then into the implementation skills. So the skill set of the gifted people within government, by its very nature, in my view involves the top end of town from multiple different traditional professional disciplines, which makes their job hard.

That is, I think, an underpinning as to why we sometimes do not see the comparable skill sets, as in the private sector we will see the banks cut the deal financially on the private sector, then they will roll over to a big constructor or the like that will go and extract the best dollar figure they can get for their delivery, but then what

they leave behind them is very focused, whereas what government wishes to leave behind is a bit broader than that. Then the outworking of that is in the professional skills of multiple people.

**The CHAIR** — But the question that I was pursuing there is particularly this difficult balance that we have in terms of decentralised sort of project management and delivery versus the need to have a specialist negotiating team to interface, in effect, with the private sector. It is a little bit like somebody who only buys one house in their life: they are not as expert at negotiating the house sale or purchase as is a real estate agent who is in the mix — you know, somebody who does it every day for a living understands the game better. That is really where I am going with this. It is very difficult for me to imagine how it is that we can carry forward a skill set given the constraints that we have currently with the decentralised delivery model.

**Assoc. Prof. DUFFIELD** — I have had a lot of involvement in the public-private partnerships, not only in Australia but also in Canada. I am working at the moment with the European Union on how they actually orchestrate them; I am working on a subcommittee of that group with the European Union and the American government in terms of how much standardisation and how much bringing it together is the right amount before we get to a system where it is all vanilla shaped and we do not get innovation and opportunity. There is a balance between the two to extract the best outcomes.

The example with the Canadian government asking me, probably on behalf of Victoria, as to which model of decentralisation or bringing your skill sets together was raised explicitly in terms of the commercial group within treasury and finance, of which there was a team of people there who were doing the big deals on behalf of government, bringing that expertise together and really acting as mentors to others. But there was a hub of expertise that internationally everybody started to look at and say, ‘Gosh, that seems to be adding real value’. As that group has matured we have started to see repeat business in sectors.

In the health sector you have had a number of health projects that have rolled out one after the other, more or less, and there has been continuity of that commercial team. In talking with the key commercial directors of that team who have decentralised but are reporting back to this group of specialists, they have told me that part of their success is not just the business acumen within the team, but within the team they have got the likes of nurses who actually know how the hospitals operate and can introduce innovations that help everybody and that you then see some of those innovations flow through to the commercial outcome. I think the blend of both — we have seen examples where the decentralised approach seems to get there and there are the transactions, but having a body of expertise at the high level who make sure that naive decisions are not taken and help support and mentor certainly has gone a long way, in that little sector at least, to doing part of what you are talking about.

**The CHAIR** — Any further comment on that?

**Prof. HODGE** — All I would say is that the issue of balancing government intellectual horsepower and firepower over the table from private sector horsepower has been around for a long while. Ten years ago I wrote a book about privatisation. Part of what I did in that was look at half a dozen water projects in Canada and contrast the claims that were made by various parties against the findings. If you go and look at the contracts, in nearly all cases the private sector got a better deal out of their particular Canadian water projects than government, solely because the private sector had greater intellectual firepower. That implies to me that if I apply it to PPPs and alliance projects, as Colin says, there is a need for a centralised hub. Whether or not you include your local regional people with detailed information is perhaps a terrific addition, but you certainly need a strong, centralised force in order to be able to get the best deal for the public.

**Mr PAKULA** — This will be a rather broad question. I invite you to elaborate on something you said in your initial comments — that is, the need for greater transparency. I suppose what I am interested in is in what specific regard are you saying there needs to be greater transparency? Are you talking about post-completion in terms of the capacity, whether it be the Auditor-General or somebody else to review the efficacy of the project? Are you talking about at tender point? At what point and in what manner do you say there needs to be more transparency, and how do you see it making a practical difference to the outcomes of projects?

**Prof. HODGE** — Colin and I have had many a cappuccino over this one. Thank you for raising the question, because it is a perennial one. Let me lead off by saying that I think when Colin and I wrote a chapter in our handbook on international PPPs, one of the comments we made was that Victoria had come a long way.

Over the last decade and a half we have learnt from our experience, and we are now doing things quite differently perhaps to what we did a long while ago. Many people seek this nirvana of full transparency, but we have all got a different version of what exactly that is. I personally probably have different views perhaps to Colin.

Going back to some of my earlier comments, I would say that when we come up with works priorities, one of my early transparency questions is always: where did that come from; what analysis has been done suggesting that this project is a better return for the public than the other perhaps 30 possibilities? What tends to happen is that projects come out of thin air as a result of some advocacy group or some high-profile person suggesting, then getting some currency, then achieving a magic which otherwise is undeserved. My initial question with transparency is: where has the idea come from, how was that compared to the various other possibilities and why is this our new highest priority works project?

The second comment I would make is that if you look at the work of the Auditor-General over the last decade or so, he makes the point repeatedly, and I think correctly, that the amount of evaluation done on projects is pretty thin after the event. I think it is good practice to go and have a look at what was promised initially and compare it to what was delivered. The part of that that could be done much better is having a look at what is promised by way of the public sector comparator, which is part of the initial decision, compared to what is delivered. There is a whole bunch of decisions inside a public sector comparator. It is quite complex. I think government ought to be holding that information close to its chest before the deal is signed, but after the deal is signed, putting out your analysis and your estimations is actually pretty reasonable as a mechanism of accountability. Do you want to add to that, Colin?

**Assoc. Prof. DUFFIELD** — I would see the steps that have happened — and Victoria has been a lead in putting contract documents openly on the web, openly communicating the announcement of projects along with dollar figures and expectations. It is up-front, and if it does not work, there are difficult discussions to be had with all and sundry, so I think Victoria has been at the lead of that. But where I start to see the issue of transparency is not only in what happens after you have held some cards to your chest to get a good commercial deal, which I think is just prudent, but the sharing of that information.

Even whilst the deal is being undertaken there have been numerous examples where, let us say, bidders in good faith have thought they were responding to a government ask, but because of lack of communication of information, lack of ability to get transparent information, have missed the mark, have had to do their deal — their bidding — again and maybe go back and do concept designs again. That is all about the government being caught by the fine line between giving information away and becoming commercially lame versus giving information to actually achieve the benefits.

If I again go back to Canada, which is quite different to Australia, they will table their budget. They will say, ‘We have got this much money’, and they will evaluate the bidders on the basis of what value you are giving them for that money, how you are getting the maximum out of it and how you are leveraging it, whereas we would say, ‘We will keep that figure, and you come and give us the best deal’. You can hold too much information back, but you do not want to be so silly about it that you give it all away.

There are different ways to do that information. I think we have come quite a way. In the industry, the private sector of course is all talk, probably more than government. Every deal you do you go to subcontractors, you get prices. They know the price of about three different groups, so government should be the exemplar and you are not communicating. Others just by the nature of the business, not that they are being devious, do communicate, which puts government at a weakness. So the government should take a bold step and communicate and make it clear that it is expecting great value, great efficiencies, and it will make assessments on that basis, as opposed to maybe simply the dollar that you give me to achieve the outcome. You can sometimes actually extract more from the market by being more transparent rather than being less transparent.

**Prof. HODGE** — Let me just add another dimension that is related to that question of transparency. It is an interesting observation that in Victoria if we do a large infrastructure project, we will go through a tender process and so on, and information will be announced, as Colin said. We had a regulatory regime looking after electricity or water where we appointed regulators to make a decision on the capital and on the returns that will be made in an entire sector, and it is open. I regard that as a transparent way of decision making, so that for the billions of dollars tied up in electricity, for example, citizens know the sorts of returns that are reasonable to

make in that sector. We have got a little idea in projects because we have adopted another kind of tool — the contract tool. We trust the competitive tendering process, hope that that works well, but we really do not know what is being done in that area.

**Mr PAKULA** — I just wanted to follow up on a couple of things. You talked about works priorities and how they are arrived at. My recollection from talking to the newly created Infrastructure New South Wales was that I think the model that they have adopted is that Infrastructure New South Wales will set out both a 20-year plan and a series of 5-year plans. They will convey that to the Premier, the Premier will be free to accept or reject that advice and the Premier will be free to publish or not publish the advice as well. Is that the kind of thing you are talking about where you say there needs to be some transparency about how priorities are created — that is, having some authority that says for the next 5 or 10 years this is what we think the priorities are and have that information made public? Is that what you have in mind or is it something different?

**Prof. HODGE** — For me personally that sounds a more sensible approach than opening up the morning's *Age* and reading about the five priorities because some journalists got hold of the Committee for Melbourne document and it has been published as a newspaper piece. I would much rather see advice coming from an independent body that has gone through some pretty serious planning sums and some pretty serious urban design thinking in coming up with those priorities. I would celebrate the fact that the body is seen to be separate to the government of the day, because I do think it is the government of the day's right, responsibility and mandate to make decisions as it sees fit. It would be nice to have a technically competent assessment of those infrastructure works, and it would be nice to see a list, as I say, of those competing priorities. People can then look at that and say, 'How come there is not this project or that project?'. It is then a consultation tool. It is then a tool for comprehensive discussion rather than choosing the project as if we are in a retail shop.

**Assoc. Prof. DUFFIELD** — If I could put my Australian hat on, I find it to my dislike to see every state government trying to become the biggest port, with Victoria saying that they are more efficient or that they have the facility that has the largest congress or conference centre so that they can say, 'I am the biggest and I am the best'. Australia is such a small nation in comparison to the global events that we now experience, so if one were to start to do the planning in some transparent way, and for the government of the day to have the ugly discussion as to 'Where are we going to back our winners and where are we going to invest good money but not duplicate?', there might be a bit more money to go round to where we really need it. They are difficult discussions, but I think the quicker we can become less parochial at that level and start duplicating, the better off we will be. That is not easy of course.

**Mr ANGUS** — I just wanted to finish off along the transparency line as well, because that was an area of interest to me. On page 4 of your submission you have said:

The degree to which contracting specialists are currently used is also not transparent at present.

I guess that is sort of a narrower view on that. Can I just get your comments in relation to that and what you might see as perhaps some best practice or tangible scope for improvement in that particular area?

**Prof. HODGE** — If I go through our submission, I think the reason we made that comment was that if you are going to talk about some kind of expanded role of consultants or advisory capacities, as a kind of a pragmatic person I would probably need to know what stage we are at at the moment. One of the observations of government in the last couple of decades is that, firstly, it is very hard to know where advice is coming from, and secondly, the degree to which government has been outsourced to private or advisory groups. It is certainly necessary for governments to buy in expertise. I also think the other side of that is that governments have to be clear about what advice they are taking from where and what of that advice is independent of, particularly, transactions for projects and so on.

**Ms HENNESSY** — I am quite interested in noting your expertise in Canada in regard to PPPs. I am wondering what advice you might have around the use of PPPs for social infrastructure.

**Prof. HODGE** — Let me jump in by saying that if you imagine two circles that intersect, Colin and I have differing views on some matters and common views on others.

**Ms HENNESSY** — I had assumed that from some earlier responses around investment priorities.

**Prof. HODGE** — Indeed. When I talk to my colleagues in Canada, particularly my economist colleagues, they talk in somewhat of a disparaging way about Partnerships Canada, it being a body that is simply there as an advocacy group for public-private partnerships. The assessments being done are not truly independent whilst the public sector comparator is claimed and so on. That may well be true to a degree; indeed, if it is government priority in Canada to advocate for PPPs, then why not set up an expert group?

There is another side to this. The same people that make that comment will say to you that, as we have written in our book, there are very few accurate assessments done of PPPs. Simple questions like discount rates that are used are typically quite inappropriate and optimistic for one delivery mechanism over another. So that is perhaps an opening gambit.

**Assoc. Prof. DUFFIELD** — I think PPPs — I would rather not characterise it as a PPP but rather say sensible engagement of the private sector into business that may be government — come in multiple ways. We couch it as opportunities innovations, and I see those innovations sometimes coming via finance, which is probably less the case post the GFC, and sometimes — as the Hong Kong government calls it — efficiency, and really they see the mechanism of sensible engagement of the private sector as a way to gain operational reform that has been too difficult from within government. So we can actually gain real productivity gains by changing how we do things and by having a fresh look by bringing people's private money and private outcomes to the table.

I have actually seen that work itself out really well here at the Royal Women's Hospital. If you have been in there and looked at how the energy use is being used in that particular building, you will see they have three power plugs. They have emergency power that will never go down, normal power and then other power that might be a bit flaky. As the private sector has worked with the operators in the building, they have all changed their culture to being energy conscious. In fact the private sector is saving money, the staff working at the premises are happier because they think they are making a contribution and overall the social infrastructure there is achieving more than I think it otherwise would. So I put that down in the reform box.

Clearly the mechanism can allow you to risk manage better, and a lot of the benchmarking work I have done internationally shows that in the capital spend component to arrange sensibly with hard-nosed contracts — which is what they are — but with clear expectations you can in fact save a lot of cash overruns, which has got to be good for the public purse.

Sometimes in Australia, because we have a very perverse taxation system, government can in fact avail itself of a better commercial deal than doing it itself. So if done properly, and I put that as a caveat, I think you can get excellent outcomes by sensible engagement of the private sector in areas of social events, albeit that they are more on balance sheet for government than, say, some of the demand-driven arrangements, which in Australia at the moment have some problems and need to be solved, in my view.

**Prof. HODGE** — I will just add to that. I had written down here, 'Private sector social investments are perfectly justifiable and perfectly reasonable'. So there is a kind of meeting point between — —

**Ms HENNESSY** — If they work.

**Prof. HODGE** — Let us assume that people do the sums, but what I am saying is: to me private finance — for example, of a road or a hospital — is not the main question. You have to do your sums on both sides, and whether it is social infrastructure or hard infrastructure, I do not think that is actually the central issue. I have seen perfectly reasonable social investments being made.

I think — and again supporting the comments that have just been made — this ideal of working towards getting the best of private ideas and capacities and government ideas and capacities is sensible and will continue. So the ideal, whether it is an alliance, a partnership or any other form of working together, is actually a fantastic and sensible idea. Whether it is applied in hospitals or roads I think is a less relevant question.

There have been some concerns in the UK with hospital financing being unsustainable and so on. I think that their situation is quite different to ours. I suspect that we have learnt a lot from the UK experience and we actually do better projects than they do.



**Assoc. Prof. DUFFIELD** — I will just add to that. I think the first time I stumbled into it was the Berwick hospital, where the private sector when working with the architects to lay out that hospital changed the layout of the nursing stations as they looked down towards the wards so that the nursing station could see more beds at one time. They also had wider corridors. These were very simple design changes, but they were able to change the staffing of the nurses at each station by something like two nurses per station, which over the life of a facility is an enormous savings. It is not the building costs; it is the fact that somebody else has reconfigured how they look at things.

If I expand that to the social housing perspective, at the moment our social housing by design standard requires premises of something like 90 square metres. All the student accommodations are sitting at about 45. We are guilt-edging our facilities because they are the historic standards. There is enormous room for — —

**Ms HENNESSY** — I do not know if all public housing tenants would agree, Associate Professor, that they are living in guilt-edged accommodation.

**Assoc. Prof. DUFFIELD** — No. What I am saying is if you put smart design into place, you can in fact get good outcomes.

**Ms HENNESSY** — I agree with that as a general principle.

**Assoc. Prof. DUFFIELD** — Yes.

**The CHAIR** — I only wish those private sector builders had been around when the La Trobe Regional Hospital was built, because you cannot push two trolleys down a corridor at the same time.

**Assoc. Prof. DUFFIELD** — Yes. That is a problem then.

**Mr O'BRIEN** — I just wanted to pick up on something you said earlier in your submission about this concept of projects coming out of thin air as opposed to projects coming out of a longer term infrastructure plan or infrastructure land-use plan. I think your preference is for projects to be in the longer term plan; is that right?

**Prof. HODGE** — Yes, true.

**Mr O'BRIEN** — There has been some talk in recent times about a pipeline at Major Projects Victoria. In fact Victoria has a pipeline; it has a \$1 billion north–south pipeline which curiously is a project that has also been cited in evidence to this committee as one where there was no business case prepared prior to the decision to build. The criticism is also that the business case that was then conducted, whilst the project may come in around budget, does not properly consider alternatives. You may be aware of that. I am not sure if you have seen the evidence or submissions from other witnesses.

Is one of the problems — and I will ask you to comment generally about that concept of the media announcements, and we also have some evidence from people from the Auditor-General about the problem of retrofitting a business case to an announcement — that steady long-term, planned growth is in fact, say, boring for some media operators or some, more likely, politicians who seek an announcement about a new project, in a sense one that they think no-one has ever thought of before or is not somehow on the plan, or in the case of the north–south pipeline, for example, was the opposite of what they had promised going into the election, which I know upsets some of the regional people, as a specific promise not to deliver such a project? I was wondering if that is part of the lessons learnt in terms of going forward — that long-term, steady planning may not have the same level of headline-grabbing projects out of thin air but may have better long-term consequences for financial investment in the state.

**Prof. HODGE** — I think my point is, and it agrees with what you are saying, that if there is no list, no comprehensive long-term plan, then in the absence of that it is very easy to get projects up — however they are brought to the table. There is clearly a sensitivity between, as you said, the boring, long-term, professionalised planning regime and the kind of headline-grabbing, new idea, sexy projects that are sometimes sought, but I think that is a tension of Western liberal open democracy.

My strong preference is for the existence of strong planning ideals, for the existence of a list of competing projects against which the sexy new ideas can be treated and against which we can have a debate about the east-west tunnel versus these various other priorities. Once projects become part of the public consciousness

and the business consciousness, they get a magic of their own as being a solution to mankind's problems, and that is one of the great things about infrastructure projects: we believe that they are going to solve everything. It is dangerous to have that belief attached to a project in the absence of a professionalised, long-term set of options and set of serious discussions.

**Mr O'BRIEN** — If we are going to have the debate about some of these grander plans — I think the term 'aspirational plan' was used by the Committee for Melbourne — is it better that that debate occur well out into the future, so perhaps in the 20 to 30 years or whenever it be, and of course there always needs to be a change of plan to respond to specific circumstances, than at the immediate level of implementation where there can be, firstly, the most acquisition cost to government, the greatest tension in the community as to who is going to be affected and ultimately the worst ability for government to secure a financially responsible bottom line?

**Prof. HODGE** — Again, there is a tension between those two: long-term and short-term sensitivities. Interestingly enough, if you look back through our history, one of the reasons why we could actually put in projects like EastLink, for example, is precisely because governments did a lot of work 30 or 40 years ago to acquire land and plan several decades ahead.

**Mr O'BRIEN** — Just a quick comment: I think they reserved the land, rather than acquired it, but along corridors et cetera, yes. Please continue.

**Prof. HODGE** — Yes. So you clearly need both a long-term strategic view and a kind of visionary approach, if you like, but also a sensitivity to short-term interests. At the moment we have a habit of just looking at the short term, and I am not sure whether that is a function of the 24-hour media cycle or the invisibility that public servants and planners perhaps have these days, but we need a greater attention to the long term.

The various groups that are around that have ideas as to what Melbourne needs in the long term, I think, is part of a vibrant discussion that needs to be had.

**Assoc. Prof. DUFFIELD** — Putting my research hat on, I suggest that as we start to look into the long term, the vagaries of what it is that we are considering become more and more significant. I reflect on the time I spent at Stuttgart university actually doing the preplanning for Shanghai and other places of development in China. We did in fact model and put out in place where you put your hospital, where you put your freeway, the timing of all the things and that being implemented. At a level you start to model — and this is my criticism of what was happening — assumptions upon assumptions, and you end up with rubbish.

The dynamic effects we deal with where you actually manage the issues of the day are real and, I think, sensible. There is a balance between the two. If I could put my pitch in, there is a need for decision-makers to be brave. Because we have the uncertainty long term in terms of what happens, there is always a propensity to have another inquiry and have another look. We realise the magnitude of the decisions that are taken. They impact long term, because once that decision is taken then that money is gone and you have something in place and you have to make the most of it. I think there is a real tension.

A great colleague of mine talks in terms of water decisions being made. He loves water decisions, because he loves droughts and floods — not because of what they do to the community but because they force a decision to be taken, and he hopes it is a good decision. That is the time when he gets decisions — in the time when you could preplan and you could think about it sensibly. Unfortunately the vagaries of the long-term decision start to make people more conservative about going out and making that call. I suppose I would encourage people to take the bit between the teeth when they have got time to think about it and actually get to the decision point, but because human nature is what it is, that is difficult.

**Mr PAKULA** — Just to follow up, how do you see the interplay between this need to do long-term planning and statistics that defy the trends? In other words, you might make long-term decisions based on long-term forecasts, whether it be drought, spikes in public transport patronage or the impact of 1700 more police, which mean that even this government in its short period of time has now decided it needs to build a prison that it did not anticipate needing to build 15 months ago. How do you see the interplay between, on the one hand, long-term infrastructure planning and, on the other, the need for government to react to circumstances that defy a long-term trend?

**Assoc. Prof. DUFFIELD** — I suppose I see it as their ability to, with greater knowledge, know the impact of what those situations will be. At the moment I know transport numbers have come off. People are saying it is the pure price spiking, it is the global financial crisis and it is the economy coming off, but if I was forecasting road growth at the moment I would not invest in a road. That may just be a little bit of a blip in the ocean, because the growth in roads for the last 50 years has of course been upwards. In relation to those sorts of matters, there is no doubt that you, as major decision-makers, have to confront them and say, ‘Is this just a little blip, and if we don’t invest now we have missed the boat and therefore long-term we have got a bad outcome? Or is it a changing trend?’. They are the things you are saying.

At the moment there is an impact of not investing in respect of, say, transport when there is a little bit of a downturn — is this an opportunity to get more efficiency by doing something smart? I am not sure the modellers are able to give you that informed information. When I think long term I think, ‘If you start projecting long term, you start to be able to model and bring to the table the consequence when you are making that very fine judgement all about what is happening today, and at least you have the information to try to sensibly call it’. I do not think there is a magical answer.

**Prof. HODGE** — My answer parallels Colin’s. My answer to your question is an ‘if and then’ answer — if we take this decision, then we know the full consequences of deciding. I am not talking about a grand plan for Melbourne; they died out long ago. But I think there is a need for us to be more professionally informed about the options for infrastructure as we move forward, compared to the do-nothing option. As we learnt from public transport governance, if you fail to even talk about population growth and steady growth in public transport, to me there is a failure in appropriate infrastructure investment and governance. If we take this decision, then the impacts are this — to me, that is the kind of obvious answer. But it is a difficult one; I am glad you are in the seats you are in.

**The CHAIR** — We have a little bit of time but not much. I wanted to pick up on some commentary which you made earlier in relation to proper governance, integrity and public interest and also a related matter, which I think Colin Duffield particularly spoke to, which is the issue of assessing projects on factors other than price. The tendency here is to see the price — that is, the cost of a project — as the predominant factor in the determination of whether, firstly, the project proceeds and, secondly, who will undertake the work. They are related.

I am interested in the intersect around the issue of the engagement of the private sector in developing proposals and therefore the intellectual input that goes into developing a project relating to how you, from a proper governance perspective, manage the probity issues around that and relating this back to your positing of that price as being not the only determinant of their allocation of the contract. I just cannot quite join all of those bits together, because I think they are central to better value — the fact that we have not found a model where we can fully engage the private sector to help us design the best project and manage our probity risk, in effect, and also get the best financial outcome. The closest that we have seen in discussion with this committee is the WA water department. It is not the water department — —

**Mr PAKULA** — Water Corporation.

**The CHAIR** — It is the Water Corporation which has a competitive alliancing model which is very interesting. I would like you to tease that issue out if you can.

**Prof. HODGE** — I might lead off on it with a comment. When I was talking about the need for proper governance, part of it was the fact that we need a more comprehensive list of project options and a more professionalised approach to choosing potential directions in the future, but part of it was also related to the sense that as Richard Foster, I think it was, said in his submission, to my mind there needs to be a clearer distinction between the initial project investment decision and the decision on how to deliver the project. Firstly, it is about how good is this project; the other is about how exactly are we going to fund this. Is it through users paying, is it going to be through private finance or is it going to be through the government paying? I am not convinced in my own mind that there has been that distinction in the past. I read the state guidelines saying that that happens, but I do not see an equal and opposite set of projects, one of which goes the public way and one of which goes the private financing way. I think in terms of governing, that distinction between the project investment — in other words, the value and worth of the project — and how exactly we are going to deliver that and whether it is going to be privately financed or publicly financed up-front needs to be clearer.

Just on the probity issue, I am less sure about the answer to that, other than saying that the alliance method has become popular. I am less convinced that it deserves all of the accolades that it gets, because it is also a very expensive way of delivering infrastructure. Even the private sector says that. Do you want to comment on that, Colin?

**Assoc. Prof. DUFFIELD** — I will take the question, and I will comment on the question more broadly if I might. From my perspective, the cost of infrastructure relates 1 to the capital cost — this is the straight money which we figure out over time — 5 to its maintenance over its life and 200 to the cost of operating within the facilities that you have. If you go for a straight dollar assessment, you choose the lowest bid and you pick the one. You make your decision on probably the lowest denominator of everything that is going to happen in your facility over its whole of life.

Through some of our contracting mechanisms we try to take whole-of-life consideration. My example for that might be an apartment block. If I get a private developer to do an apartment block, I can guarantee the lifts will fail one year after the warranty period on the lifts. It will put the cheapest, nastiest lifts in, because that is the cheapest outcome it can get, then it is out of there and you do not see it for dust. If you commercially structure that same person to be responsible long term, all of a sudden you have good-quality lifts and they do not have to come back to look at them — funny about that.

Then there is the 5. An example of that is Canadian roads. At the moment you have parallel road systems in Canada — one is being privately financed on these long-term arrangements and one is on public arrangements. The Canadian public works are complaining about the cost of the maintenance on their roads. Their roads are in poor condition, with potholes, patches and whatever, and they are saying, ‘We are paying too much for these P3 contracts that are long term’. You talk to the P3 contractor, and he says, ‘I am not dumb. When I send my people out to do the maintenance, they fix everything they can see and we do not have to go back there for a long period of time’. It is cheaper and they are getting a better product because they are commercially aligned to doing that.

Then if I go to my 200 example, the best example of that is a building that Ove Arup built back in the early 80s, which is the Hong Kong and Shanghai Bank in Hong Kong. You have probably seen it; the structure looks like a coathanger. It is still a glamour building today, 30 years on. In terms of the productivity, the staff happiness and the amount of generation they have had in that building, they now claim it to be just an absolute world beater. At the time they paid double the capital cost. They absolutely knew about it — this was 1, that was the 200. They are recouping and recouping on the 200, and they are laughing

In terms of how you get that value, I think it is opening up to thinking about what we are really delivering. We are thinking long-term facilities, and we are thinking long-term costs commitment. The big commitment to the state budget is — yes, the capital cost is in your face. It is big and it is ugly and the cash flow is horrible, but your ongoing maintenance bills are enormous. The ongoing operation of your department is enormous. That is where the costs just keep going down the plughole if you get it wrong. The first question about value is to think long term. The second thing about value is when you start to look at your evaluations.

Florida Transport were the first to introduce it. They do not assess their tenders on the basis of, ‘This is what I wanted — tick’; this is what you give me; and this is the price — tick, tick, tick’. They get their contractors and say, ‘Okay, we think you are good; that is why you are bidding for the work. Tell us what is going to be hard for you, show us how you are going to manage the bits that are most hard for us and demonstrate to us that you have the management capability to overcome the problems and not cost us more money, and then we will start thinking maybe you are the right one for the job’. They have now put that into IT projects. They started in transport, and they are actually implementing it. Because they are grilling these people, forcing the private sector to think as hard as the government does up-front, they are getting those sorts of outcomes.

You talk about IP, and I will come to your IP. If I see private sector involvement in government affairs, the private sector is motivated by profit — so if I can buy the land and onsell it, there is my profit. If I bring a good idea and I can bank my idea, there is my profit. The long-term what I would call ‘stewardship’ of the outcomes for the community is not wedded with somebody coming with their good idea. I love their good ideas because they have got the juices going — they are going to bring value. That is where I think working with somebody brings more value than either me taking their idea and then trying to shop it around or those sorts of things that would break the law or your alliance concepts done poorly. You have asymmetry of real skill sets, and therefore

you have a private sector that sees opportunity and gouges the opportunity. That is their job. There is nothing wrong with that. You see alliances done properly where you have good commercial people on both sides of the equation sitting sensibly around the table saying, 'If we can make a saving that is good for everybody, we will share it'. They say 'Okay, I would like some of that' and 'I would like some of that', and if it works in that spirit, of course you get magnificent outcomes.

To me it is about not stealing, not sort of trying to pre-empt, but trying to facilitate how we actually grow the cake such that everybody is having a win. How do we make sure people are up to the mark before we select them? How do we change some of that thinking? It is a very much more proactive way of encouraging behaviour that is good for all; it is not being naive and thinking that the private sector will not just look to capitalise on their opportunity if they can get a game. That is my view.

**The CHAIR** — Thank you very much. I regret to say that we are out of time, because I think we could go a bit longer if it were possible. Thank you very much for participating today, Professor Hodge and Associate Professor Duffield. We are sure this has been a useful session. I am not sure that any questions were taken on notice, but we may be in contact with you to follow up with any particular queries at a later date. I am sure you will be interested in following the progress of the committee's examination over the next 24 hours. We will be back in public session later on with the inquiry, and hopefully you will remain engaged with us. Thank you very much for your contribution, and we look forward to being in touch down the track. This closes the hearing.

**Witnesses withdrew.**