New Zealand Public Private Partnership Model Review

January 2021

New Zealand Government

Contents

About this report

The New Zealand Infrastructure Commission,Te Waihanga (the Commission) was established in September 2019. The Commission will help improve how NZ coordinates and plans its infrastructure, makes the most of the infrastructure it already has, and ensures that investment in infrastructure delivers what NZ needs.

Through its empowering legislation, the Government Procurement Rules and Cabinet Office Circular CO (19)6 one of the Commission's core functions is to advise agencies and local authorities responsible for planning, procuring and delivering major infrastructure projects and any innovative or non-traditional approaches to procurement, alternative financing arrangements, or PPPs. Related to this, the Commission is responsible for maintaining and developing the NZ PPP Model, including:

- developing PPP policy, processes and guidance
- assisting entities with PPP procurement
- maintaining the Standard Form (PPP) Project Agreement
- engaging with potential private sector participants, and
- monitoring the implementation of PPP transactions.

This function was previously undertaken by the former NZ Treasury PPP Unit. The Commission is neither in favour of, or opposed to the use of PPP procurement, but rather acts as a neutral advisor on all forms of procurement, including PPPs, based on what will deliver the best value for money solution in accordance with the articulated benefits and outcomes sought by the procuring agency.

Purpose

The purpose of this Review is to better understand how the NZ PPP Model has operated in practice across the assets and related services procured over the last decade. In doing so, the Review seeks to derive lessons that could be applied to the future procurement of major infrastructure projects as well as the management of the existing PPP projects during their Operating Periods.

Further information on the scope and purpose of the Review is set out on page 12.

Structure

This report is structured as follows:

Executive Summary

Section 1: Introduction and context provides a summary of the origins of the NZ PPP Model and an overview of its key features.

Section 2: The NZ PPP portfolio provides a summary of the eight projects procured under the Model.

Section 3: Outcomes from the Model to date provides a discussion on the extent to which the projects have met their original objectives.

Sections 4-13: These sections set out the key findings of the Review grouped around broad themes.

Sections 14: Future of the NZ PPP Model provides a discussion on next steps.

Acknowledgement and next steps

The Commission welcomes your comments on this report. If you have any feedback or questions, please contact info@infracom.govt.nz.

It is acknowledged that since this report was originally commissioned within the NZ Treasury Infrastructure Transactions Unit (ITU), there have been significant contributions, under the purview of the ITU and subsequently the Commission, in relation to its development and drafting from its consultants including Advisian, Bell Gully , KPMG and Aurecon.

As part of its upcoming work programme, the Commission will consider and perform a prioritisation of the proposed actions set out in this Review, focusing on those that will best support the existing operational PPPs.

Transmission Gully Enquiry

This report was developed over a significant period of time. At the time of writing the Commission has been asked to appoint a reviewer and peer reviewers to prepare a report into the Transmission Gully PPP project. The terms of reference to that enquiry have been included as Appendix B. The outcomes from the

report will be considered by the Commission in terms of supplementing the findings of this Review.

Executive Summary

The NZ PPP Model was developed to achieve better service outcomes from infrastructure procurement…

Internationally, PPP is one form of a public-private risk-sharing framework that is widely utilised. However, there are many other alternative financing variants that can be used for financing publicly owned infrastructure assets whether delivered through a Private Finance Initiative (PFI) procurement route, or otherwise. In the NZ context, however, a PPP is a long term contract for the delivery of a service, where provision of the service requires the construction of a new asset, or enhancement of an existing asset, that is financed from external sources on a non-recourse basis, and full legal ownership of the asset is retained by the Crown. Importantly, the term does not refer to joint ventures or asset privatisation.

The NZ Treasury (the Treasury) began developing the NZ PPP Model (Model) in 2009, with a focus on achieving better service outcomes from Crown procurement of large-scale capital assets for an equivalent or lower whole of life cost to that achieved under conventional procurement methods. At the time, many developed economies, including Australia, the United Kingdom and Canada had already implemented PPP programmes to deliver a significant number of projects, with some version of a PPP model being used internationally for well over two decades. Importantly, and unlike some other jurisdictions, the driving force for the Model was on achieving better service outcomes, not to achieve off-balance sheet financing of capital assets or to minimise cost.

…and over the last decade has been used to procure eight projects, five of which are now operational

The Portfolio of NZ PPP projects is a combination of horizontal (i.e. roading) and vertical (i.e. buildings such as prisons and schools) forms of infrastructure. The eight NZ PPP projects are comprised of:

- three Ministry of Education (MoE) projects, delivering 11 new primary and secondary schools,
- three Department of Corrections (Corrections) projects, delivering c.2000 additional prison beds, and
- two Waka Kotahi, NZ Transport Agency (Waka Kotahi) projects, delivering c.45km of Motorway.

A combined total of $4.2 billion has been committed to these projects, based on the Net Present Cost as at their respective Financial Close (FC) dates. Three of the projects were under construction at the time of this Review.

The above projects all transfer the responsibility for delivery of the design, construction (build), financing, and maintenance of the assets to a private sector partner for a defined period (25 years in all projects to date). The extent to which the private sector partner is also responsible for the delivery of operational services using the assets varies significantly between the projects. For example, the Auckland South Corrections Facility PPP includes the day to day management of the prison services, while none of the school projects include any role for the private sector partner in the delivery of educational services within the assets provided.

At the time of this Review, the Government's position is that PPPs should not be initiated for the procurement of assets in the education, health and correctional sectors[1]. The Model could still be considered in other sectors, such as transport and defence. Notwithstanding the limited PPP pipeline, the Treasury's ITU commenced this Review in 2019 to understand how the Model had worked in practice. The ITU was keen to capture Portfolio performance data and derive lessons to support the existing projects and in the event that future PPPs were considered. Following the establishment of the Commission, the responsibility for maintaining and developing the Model, including this Review, was transferred from Treasury to the Commission.

The Review took the opportunity to draw on the contemporaneous recollections of many of the individuals involved in the projects to date. The Commission conducted interviews with Procuring Entities, successful consortia, major sub-contractors, unsuccessful consortia members, Equity Providers, banks and a range of advisors to the parties including legal, financial, technical and probity auditors and Independent Reviewers. The focus of the Review was not to carry out a comparative analysis of the Model relative to other procurement approaches.

The performance of the Portfolio to date has generally been positive, but not without challenges

The five PPP projects that are now operational have generally been delivered on-time and on-budget (from the Crown's perspective), with each operational PPP project having experienced delays of fewer than six months between the initial market briefing to Service Commencement. As of mid-2019, the total actual Unitary Charge paid by the Crown for the five operational PPP projects was approximately $9.1m lower than that forecast at FC.

With regard to projects still in the Construction Period, the most significant issues have occurred on Waka Kotahi's Transmission Gully and Puhoi to Warkworth projects. On 11 February 2020, Waka Kotahi announced that it had reached a $190.6m financial settlement with the Transmission Gully joint venture builder for the project due to a number of issues, including challenging site conditions, several storm events and the 2016 Kaikoura earthquake. In relation to the Puhoi to Warkworth project, Waka Kotahi have also paid an additional $83m to cover costs and delays to work at the northern end of the route, which have been caused primarily by land purchases taking longer than anticipated.

Covid 19 has also impacted contractual arrangements for the major PPP projects currently in construction, with the major impacts felt by the Waka Kotahi projects:

- Transmission Gully: Agreement was reached between Waka Kotahi, the project contractor (Wellington Gateway Partnership), the builder (CPB HEB Joint Venture), and the maintenance contractor (Ventia), including a compensation payment of $145.5m to the CPB HEB Joint Venture to cover the costs of delays and other impacts resulting from the five-week COVID-19 shutdown, and separate payments to the Wellington Gateway Partnership (WGP) and Ventia to cover their own costs from the COVID-19 delays and associated issues. The agreed payment to WGP is $12.5m and to Ventia was approximately $5m. The settlement included a revised date for the opening of the road, being September 2021; and
- Puhoi to Warkworth: Agreement was reached between Waka Kotahi and the Fletcher Acciona Joint Venture to cover the costs of delays and other impacts resulting from the five-week COVID-

[1] https://dpmc.govt.nz/publications/co-19-6-investment-management-and-asset-performance-state-services, paragraph 80.

19 shutdown. The settlement included a payment of $85m and a revised date for the opening of the road, being May 2022.

In addition to greater cost and time certainty, the original Business Cases for the PPP projects set out a number of other objectives for utilising the Model including improved service outcomes, providing a strong level of risk transfer to the private sector, achieving a whole of life focus for asset management and maximising innovation through harnessing private sector input. As set out in this report, there were a variety of views expressed on the extent to which these broader outcomes had been achieved and how well different aspects of the Model had worked to date.

As part of its ongoing programme of research on the performance of infrastructure procurement models, the Commission intends to maintain regular performance data collection from Procuring Entities, as well as undertaking further comparative analysis across different procurement methods.

The Review findings encompass the development and implementation of PPP projects from the Business Case through to ongoing contract management

The Review findings are structured around the broad themes arising from interviews and other research. In summary, the findings consider the:

- **Determination of the Public Sector Comparator and Affordability Threshold (AT)**, including the role of the AT in the Model and challenges that can arise when it is not set 'correctly'.
- **Procurement phase of PPP projects**, including the level of design specification required from bidders during procurement and the functioning of Interactive Tender Processes.
- **Allocation of risk between parties**, including whether the allocation of certain risks should be reconsidered for future projects and which parties are best able to manage them.
- **Role of the Special Purpose Vehicle (SPV),** including whether SPVs have the resources and capability to manage projects in the way envisaged by the Model.
- **Review procedures,** including the processes for the Procuring Entity to provide design review comments and the role of the Independent Reviewer.
- **Change mechanism and Fit for the Intended Purpose,** including whether the mechanism is working as intended and if further clarity is required on the intention of the Fitness for the Intended Purposes provisions.
- **Performance regimes and the management of disputes,** including whether the design and administration of performance regimes is supporting the delivery of service outcomes.
- **Contract management,** including the level of resourcing and capability required to manage PPP contracts.
- **Refinancing and Change of Ownership,** including experience in implementing these provisions on projects to date.

Finally, the Review also considers additional changes to the Standard Form (PPP) Project Agreement (SFA)[2] not covered in detail in the above sections.

The Review suggests proposed actions for consideration to improve the operation of existing PPPs and for the procurement of new PPP projects in the future

At a high-level, the proposed actions from the Review fall within three broad categories:

- **Development of additional guidance** by the Commission for Procuring Entities to provide greater direction on implementing aspects of the Model and ensure there is consistency of approach across projects.[3]
- **Amendments and updates of the SFA** for future projects to incorporate the lessons identified from the existing projects.
- **Supporting the sharing of lessons across Procuring Entities** to ensure that ongoing on-the-ground experiences in managing PPPs are shared.

A summary table of all specific proposed actions is provided on the following page.

[2] https://infracom.govt.nz/assets/Uploads/Standard-Form-Public-Private-Partnership-PPP-Project-Agreement-v2.pdf

[3] This could, for example, be in the form of published Practice Notes, similar to that recently published by the Commission on consultation requirements regarding certain operational PPP events.

Summary of proposed actions

The following proposed actions emanating from this report will be considered for action by the Commission.

	Proposed Actions	Section Ref.
1	The Commission should update the guidance to Procuring Entities on setting the Public Sector Comparator and Affordability Threshold, including on the level of detail provided during the procurement phase and a framework for adjusting the Affordability Threshold if required.	4
2	The Commission should develop further guidance for Procuring Entities on determining the appropriate level of design specification to include in RFP documents and the appropriate level of design development required (inclusive of relevant management plans for consenting, environmental and construction purposes) from bidders during the procurement process. This guidance should recognise the costs to bidders of extensive design work and subsequent steps that may be required during the Preferred Bidder stage, as well as the importance of keeping desired risk allocations intact.	5
3	The Commission should prepare guidance for Procuring Entities on conducting effective interactive sessions with bidders during the procurement process (both for PPP and non-PPP procurement) in a way that provides value to the Procuring Entity and the bidders and preserves probity.	5
4	The Commission should develop a policy on bid cost contributions for major construction projects, in consultation with relevant agencies.	5
5	The Commission should review the drafting of the Standard Form (PPP) Project Agreement to ensure there is clarity in the allocation and nature of consenting obligations between the parties, including consideration of the inclusion of a 'reasonable endeavours' obligation on the Crown as seen in some PPP projects.	6
6	Procuring Entities should ensure there is sufficient due diligence undertaken on the bidder's proposed strategy and capability in relation to consenting, particularly for horizontal projects. This should include as part of interactive sessions and in bid evaluation.	6
7	Procuring Entities should consider whether the Contractor is best placed to manage all third-party stakeholders and consider amending the risk allocation in the Standard Form (PPP) Project Agreement to reflect this on a project by project and specific stakeholder basis.	6
8	Procuring Entities should seek to ensure that key third party agreements that affect project design, scope and access to land are finalised early (i.e. before entry into the Project Agreement), and where this is not possible, the Project Agreement should state how outstanding risks are to be managed.	6

	Proposed Actions	Section Ref.
9	The Commission should consider amending the default risk allocation in the Standard Form (PPP) Project Agreement in relation to the risk of unforeseeable ground conditions.	6
10	The Commission should consider amending guidance for Procuring Entities on how they can ensure that the major Services and/or Asset Management and Maintenance sub-contractor are involved in design and in key interactive and negotiation sessions.	7
11	The Commission should develop guidance for Procuring Entities on the recommended requirements for the structure and resourcing of the Special Purpose Vehicle, including drawing on lessons from existing projects.	7
12	The Commission should consider amending the Standard Form (PPP) Project Agreement to include an obligation for the Contractor to evaluate whether pass through claims from sub-contractors have merit before sending these to the Procuring Entity.	7
13	The Commission should consider its position regarding Industrial Equity, the level of voting rights and conflict management requirements of major sub-contractors in a Special Purpose Vehicle.	7
14	The Commission should develop guidance on opportunities for both Procuring Entities and Contractors to improve the design review process, including informal engagement. This relates also to consideration of the level of design specification and design requirements for bid submission and ensuring that the major Design and Construction sub-contractor forming part of bid consortia is well aware of the fixed price nature of the PPP model and limited opportunity for variation post Contractual Close.	8
15	The Commission should consider amending the Standard Form (PPP) Project Agreement to include review and comment on the Works Completion Plans in the Independent Reviewer's scope.	8
16	The Commission should consider options for improving incentives for innovation by the Contractor post-Contractual Close including, but not limited to, potential amendments to the Change mechanism.	9
17	The Commission should review the Change mechanism in the Standard Form (PPP) Project Agreement to consider and improve ease of practical implementation.	9
18	The Commission should consider amending the Standard Form (PPP) Project Agreement with regard to the Fit for the Intended Purpose definition to standardise the various positions negotiated across the different projects and provide further detail on the requirement in any contract management guidance.	9

	Proposed Actions	Section Ref.
19	Procuring Entities should ensure that the design of the performance regime is aligned with desired outcomes and incentives and takes account of what would be required to implement the regime in practice.	10
20	Procuring Entities should ensure that the calibration of the breach regime achieves the desired incentives during both the Construction and Operations Periods.	10
21	The Commission should develop guidance on issuing Notices of General Breaches, including on managing instances of minor non-compliance.	10
22	The Commission should consider whether the Standard Form (PPP) Project Agreement should be amended to provide more flexible time bars.	10
23	The Commission should develop and publish contract management guidance for Procuring Entities in relation to the Standard Form (PPP) Project Agreement. This could include recommended strategies to manage handovers between phases and departures of key personnel, such as joint workshops with both the Procuring Entity and SPV personnel.	11
24	The Commission should develop guidance for Procuring Entities on undertaking PPP refinancing, and consider other options for sharing refinancing lessons across projects.	12
25	The Commission should develop guidance for Procuring Entities on dealing with Changes of Ownership.	12
26	The Commission should consider amending the Standard Form (PPP) Project Agreement in relation to the specified (reasonable) timeframe within which the Crown must provide or withhold its consent to a proposed Change of Ownership (subject to the Contractor providing the required information to the Crown).	12
27	The Commission should review and update the Standard Form (PPP) Project Agreement to simplify drafting where possible, incorporate lessons learned from projects executed and address other specific improvements that have been suggested.	13
28	The Commission should consider amending the Standard Form (PPP) Project Agreement to include guidance notes on provisions that may require adjustment for horizontal as compared to vertical projects.	13
29	The Commission should consider amending the Standard Form (PPP) Project Agreement so that the Expiry Date of the Project is either a fixed date or determined from the Planned Service Commencement Date rather than the actual Service Commencement Date.	13

Introduction to the New Zealand PPP Model

1 Introduction and context

1.1 Development of the New Zealand PPP Model

The NZ Treasury (the Treasury) began developing the NZ PPP Model (Model) in 2009. In the NZ context, the Commission defines a PPP as:

> *a long term contract for the delivery of a service, where provision of the service requires the construction of a new asset, or enhancement of an existing asset, that is financed from external sources on a non-recourse basis, and full legal ownership of the asset is retained by the Crown.*

The focus was on achieving better outcomes from Crown procurement of large-scale capital assets for an equivalent or lower whole of life cost to that achieved under conventional public sector procurement methods. It also aligned with broader interests of the government to improve the capital asset management of public assets. At the time, many developed economies, including Australia, the United Kingdom and Canada had already implemented PPP programmes, lessons from which were incorporated into the design of the Model. Importantly, unlike some other jurisdictions, the driving force for the Model was not to achieve off-balance sheet financing of capital assets or to minimise cost.

Under the Model, the Crown and its private sector partner agree a fixed price for the design, construction, maintenance and lifecycle, and if applicable, Operational Service provision of the asset for a defined period (typically 25 years). The Crown makes no payment until construction is complete and the asset is available for service delivery. During the Operating Period, payment deductions are incurred if the asset is unavailable or the services are not delivered to the agreed standards.

The Treasury considered that the benefits of the Model would best be achieved through competitive procurement processes focused on outcomes (with minimised input specifications and constraints), the optimal allocation of risks to parties best able to manage them, and performance-based payment mechanisms that put private sector capital at risk. This would, in theory, provide the incentives and flexibility for the private sector to deliver innovative and effective solutions, and these could act as a catalyst for broader change in the public sector. At the time, there were also drivers of change on specific projects where Procuring Entities were considering new models of operation within their sector (e.g. new approaches to the rehabilitation of prisoners).

It was recognised early in the development of the Model that it would only be suitable for a small subset of capital asset projects. The initial thinking on the characteristics of suitable projects evolved into a set of 'hurdle' criteria that a project would be assessed against as part its Business Case. In summary, the PPP hurdle criteria focus on projects of large scale and long duration where the nature of the asset is specific, services are durable, it is possible to define clear performance requirements over time, and the project is sufficiently complex that innovative design and service approaches may be employed. Finally, there must be sufficient market appetite and depth (including amongst financiers) to ensure a competitive procurement process.

A dedicated PPP Unit within the Treasury was established to assist public sector Procuring Entities to identify PPP candidate projects and prepare policy and guidance. Consistent with other jurisdictions, it was considered that a dedicated team acting as a centre of expertise was necessary to achieve consistency for all parties involved in PPP projects and support information sharing. The team's early work included:

- updating the Cabinet Office Circular CO (10) 2 requiring significant capital projects to consider alternative procurement, including PPP,

- development of, and consultation on, the SFA containing the core commercial principles and structure of the Model, and
- publication of three key guidance documents[4] explaining the framework of the Model, the expected procurement process and more detailed guidance on undertaking the value for money assessment required for a PPP project.

At the time of this Review, the Government's position on the Model is set out in Cabinet Office Circular CO (19) 6. It states that PPPs should not be initiated for the procurement of assets in the education, health and correctional sectors but can still be considered in other sectors, such as transport and defence. The Government had previously made it clear that projects such as the New Dunedin Hospital[5] would proceed under a conventional procurement model (rather than through a PPP as announced by the previous government). The Waikeria Prison PPP reached Financial Close (FC) prior to the Government updating its position given the procurement was already far advanced.

1.2 Purpose of reviewing the Model

The Model is now ten years old and has delivered eight projects, of which five are operational. In 2019, the Treasury's Infrastructure Transactions Unit (ITU) commenced a review of the Model. Apart from the Office of the Auditor General's discussion paper published in 2011[6], no review of the Model had been carried out since its inception, although lessons learned reports were published for the Auckland South Corrections Facility and Transmission Gully projects. The ITU was keen to:

- understand how the PPP Model was working in practice with a view to developing further guidance to support the existing PPPs,
- understand the risk allocation, relationships and processes used by each of the parties throughout the procurement and contract periods as part of wider research on the procurement and delivery of major projects,
- derive lessons that could be applied to alternative procurement models and innovative financing models for the procurement and delivery of future infrastructure, and
- draw on the (still broadly) contemporaneous recollections of many of the individuals involved in the projects.

Following the establishment of the Commission, the responsibility for maintaining and developing the Model, including this Review, was transferred from Treasury to the Commission.

1.3 Review methodology

For this Review, interviews were conducted with participants in all of the NZ PPP projects, including Procuring Entities, successful consortia, major sub-contractors, unsuccessful consortia members, Equity Providers, banks and a range of advisors to the parties including legal, financial and technical advisors, probity auditors and Independent Reviewers.

[4] "The PPP Procurement Process"; "The Public Sector Comparator and Quantitative Assessment" and "The New Zealand PPP Model and Policy: Setting the Scene", NZ Treasury.

[5] https://www.newdunedinhospital.nz/

[6] https://oag.parliament.nz/2011/public-private-partnerships/docs/public-private-partnerships.pdf

The aim of the interviews was to identify and investigate aspects of the Model that are working as intended and those that are presenting challenges for the participants, and for participants to reflect on their involvement in the PPP projects to date. In addition, the Review has drawn on, where appropriate, previous reports on both NZ and international experiences of PPP models. The Review has been further supported by an initial collection of NZ PPP performance data and a small number of targeted research pieces.

The Review recommends some amendments to the SFA for future projects. These comments do not relate to the executed Project Agreements (PAs) for existing projects, which have been drafted, negotiated and priced to reflect the particular context and requirements of each project and the agreed risk allocation between the parties. The references to specific clauses or sections of the PA are to the SFA available online[7].

1.4 Model participants

The Model relies on a relatively complex interplay of incentives and risk allocation among numerous parties that are designed to reinforce each other for the benefit of the Procuring Entity. This means that, for a PPP to function successfully, a large and diverse group of people need to understand their roles and responsibilities and be willing and able to fulfil these roles in a timely and competent manner. The number of individuals interviewed as part of this Review reflects the large range of parties involved in a typical PPP project (see Appendix A).

At a theoretical level, the PPP Model rests on the assumption that the participants have a broadly shared understanding of how the parties must work together and what their respective roles are. In practice, this can take time to develop and expertise comes down to individuals having the knowledge and skills either from working on NZ PPPs or on PPPs internationally.

The NZ PPP market can provide a challenging learning environment for participants due to:

- The relatively small number of PPP projects in NZ providing fewer opportunities for parties in the market (including Procuring Entities) to learn and gain direct experience. NZ's small PPP market, distance from larger markets, and the draw of very large PPP programmes in other markets can also limit the entry and retention of experienced international personnel.
- The learning opportunities at later stages of the PPP lifecycle are even fewer. Of the eight projects to date, there is experience through the commissioning and Operating Period from only five, and in only two of the three sectors that have so far procured using the Model.
- For Procuring Entities, PPP is an exception to their typical procurement and contracting models. While the contract management teams will continue to develop understanding of the Model through their day to day contact with the projects, it will take longer for understanding to penetrate more broadly into their organisation. This is sometimes made more difficult due to the perceived complexity of the Model.
- Participants learn about the Model during the procurement process. However, the high costs of bidding and the intensely busy bidding period may mean that individuals that do have expertise are unable to spend time educating others. The bidding consortia tend to form as a team only as

[7] https://infracom.govt.nz/major-projects/public-private-partnerships/ppp-guidance/

required by the procurement timeline. Furthermore, the people involved on bid teams tend not to carry over into the delivery phase post FC.

This Review is intended to contribute to the evolving understanding of the Model. While there has been a growing maturity in the NZ market as projects have been procured, constructed and begun operations, there are inevitably issues resulting from NZ's small scale and the lack of repetition. The complexity of the Model and requirement for experienced participants is difficult to maintain without an ongoing pipeline of PPP projects. The Commission has a role to fill this information gap, such as through further guidance that is read as a common point of reference accepted by all participants, arranging knowledge sharing among participants and organising other fora to share and build knowledge in the industry.

1.5 Wider commentary on the Model

The Review focused on feedback from participants in the NZ PPP projects to date. It was not intended to be a comparative analysis of different procurement methods. The Commission is, however, aware of broader public commentary on the merits of the Model. Some of this commentary focuses on features of overseas PPP models that are not part of the Model or relate to issues not experienced on NZ PPP projects. Others reflect reasonable critiques of the Model given the trade-offs inherent in its design. This section briefly considers some of this wider commentary.

When considering issues on specific projects, it is important to take account of the inherent complexity of many large infrastructure projects. The PPP projects are relatively high profile and receive a commensurate level of scrutiny, in part due to the increased transparency created by the Model's focus on fixed price and whole of life costing. It is not uncommon for the delivery of other large infrastructure projects to experience significant challenges, regardless of the adopted procurement method. Each procurement method (e.g. PPP, Alliance, Design and Build, Build only, Direct Managed, Early Contractor Involvement[8]) comes with its own set of challenges and trade-offs, with the best approach in any given case driven by the individual project characteristics and objectives. In all cases, the outcome can be subject to circumstances that are at times beyond the control of the project.

Cost of capital

A common criticism of the Model is that it does not represent value for money given that the cost of private financing exceeds the borrowing cost of the government (which was at historically low levels at the time of this Review). While it is true that the government can generally borrow at rates below those of the private sector, a valid comparison should allow for the relative risk to the lenders.

The debt provided for a PPP project is on a non-recourse basis – lenders do not have recourse to any assets or cashflows outside of the project itself. This means lenders provide their capital based on an assessment of the risk of the project alone. Under conventional government borrowing, the Crown borrows against its whole balance sheet with an implicit taxpayer guarantee to support the borrowing almost regardless of the project outcome. The taxpayer backing changes the view of risk from the project-level to the wider government balance sheet-level. This reduces the risk to the lender, making government a 'safe' borrower and reducing the cost at which Debt Providers are willing to lend. While the specific project risks are not reflected in the government borrowing rate this does not mean that the project risks no longer exist in economic terms. Rather, they are made less visible in the cost of capital.

[8] https://www.procurement.govt.nz/assets/procurement-property/documents/developing-your-procurement-strategy-construction-procurement.pdf

For investment decision making purposes on individual projects, the Treasury uses a Crown discount rate[9] (significantly higher than the government borrowing rate) reflecting the risks of different project types, which is a more suitable comparator. As discussed further in section 4, a PPP must be no more expensive than if it were procured under a conventional approach even after taking into account additional financing costs.

Build cost vs NPC

A further criticism is that the building of an asset under a PPP project can be many times the cost of the building the same asset procured under a conventional approach. Commentators often tend to refer to a non-PPP project's cost as being the build cost only rather than the whole of life cost in NPC terms, i.e. inclusive of asset management and maintenance and other costs for the life of the asset. Given that a PPP project's value is usually given in NPC terms, it is important that this is not mistakenly compared with the build only figure.

Off-balance sheet financing

Some commentators argue that part of the appeal of the Model is that it artificially lowers the reported level of government debt. In the NZ context, this is incorrect. The future obligation to pay for the PPP is (and has always been) recognised on the Crown balance sheet and appropriated in advance.

Design and construction issues

Some commentators have highlighted the design and construction issues that some PPP projects have experienced, such as delays in completion and construction quality issues. While these do represent significant challenges for the affected projects, they are not specific to the Model.

At the time of the Review, a number of large infrastructure projects were facing challenges in delivery, such as additional costs and delays associated with COVID-19. New Zealand Standard (NZS) Conditions of Contract and other design and construction contracts did not help address the impact of COVID-19, with the Government issuing guidance to assist parties to reach COVID-19 related settlement agreements. These same COVID-19 related issues have also arisen for the PPP projects still under construction but are more complicated by the fact that the Crown does not pay for the project until after construction is complete. The D&C major sub-contractor must address immediate cost impacts and the delayed completion, both of which require support from its Debt Provider(s). This in turn leads to a longer negotiation period regarding the COVID-19 impacts.

International PPP failures

PPPs have been commonly used in Australia, Canada and the UK over the last several decades. It is common for examples of 'failed' PPP projects from these jurisdictions to be cited in broader commentary on the Model. This Review focuses on the experience of NZ projects procured under the Model, and therefore did not seek to survey international projects in detail[10]. In considering examples of international PPP projects, the Commission believes it is important to consider the following:

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[9] https://treasury.govt.nz/information-and-services/state-sector-leadership/guidance/financial-reporting-policies-and-guidance/discount-rates

[10] A recent Australian study of PPP projects is briefly summarized in section 3.

- As a relatively late adopter, the design of the Model was able to incorporate many of the lessons learnt from early PPP projects undertaken in other jurisdictions and differs from overseas models in many respects,
- The issues faced by some international infrastructure projects are not necessarily unique to PPP and need to be considered in the context of non-PPP projects that have also experienced significant challenges. Further, across the many PPPs procured internationally, there are many successes, which tend not to receive the same level of attention,
- Some international PPPs have struggled when utilisation of the asset has been lower than expected and where this demand risk has been transferred to the private sector (e.g. where revenue is tied to the use of a toll road). All NZ PPP projects are availability-based with no payments contingent on the level of demand, and
- There are many examples where the financial losses incurred by international PPP projects are demonstrations of the risk allocation working as intended, with the private sector bearing the costs of its own miscalculations or underperformance and the public sector continuing to receive the benefits of the delivered asset at the bid price.

High procurement and legal costs

The development of the SFA has achieved a reasonably high degree of consistency across NZ PPP projects, but project specific factors has meant that there have still been significant procurement and legal work required for each project. While there are no accurate comparators on a whole of life basis, it is generally true that the cost of PPP procurement tends to be higher than other procurement methods. It is worth noting that these higher costs are considered in the initial 'value for money' test on whether to proceed with PPP as a procurement method, but the true extent of ongoing legal costs relative to other methods is not measured.

An inherent feature of the Model is that it seeks to achieve whole of life benefits through an integrated 'pay for performance' style contract spanning the design, construction, financing and ongoing maintenance over a defined contract term. This results in a relatively complex initial contracting arrangement that has to consider a broad range of issues that would not typically be required in a simpler procurement method (e.g. performance-based payment mechanism, hand-back conditions at the end of the contract term etc). The trade-off in seeking to achieve these whole of life benefits is higher procurement cost and contract complexity, which must be considered at the Business Case phase in determining whether the Model is suitable for the project. Procurement models that have a shorter contract term naturally require repeated procurement cycles over the period that a PPP would cover, with procurement costs each time.

Lack of flexibility

For similar reasons as those outlined above, it is also generally true that PPPs offer a lower level of change flexibility relative to other procurement methods. The expectations of all parties for the contract term are largely 'locked in' at FC, and changes must generally be undertaken through the prescribed Change mechanism.

The Change mechanism does allow changes throughout the contract term and for the cost to be market tested. There are also mechanisms for minor changes and cost updates to occur throughout the term in the Model, further tailored within some PAs, some of which were developed based on lessons from overseas experiences. The Change mechanism is discussed in more detail in section 9.

Given the above, it is critical that potential PPP projects are subject to robust investment planning to ensure that both the nature of the requirements and the key areas where change may happen are well

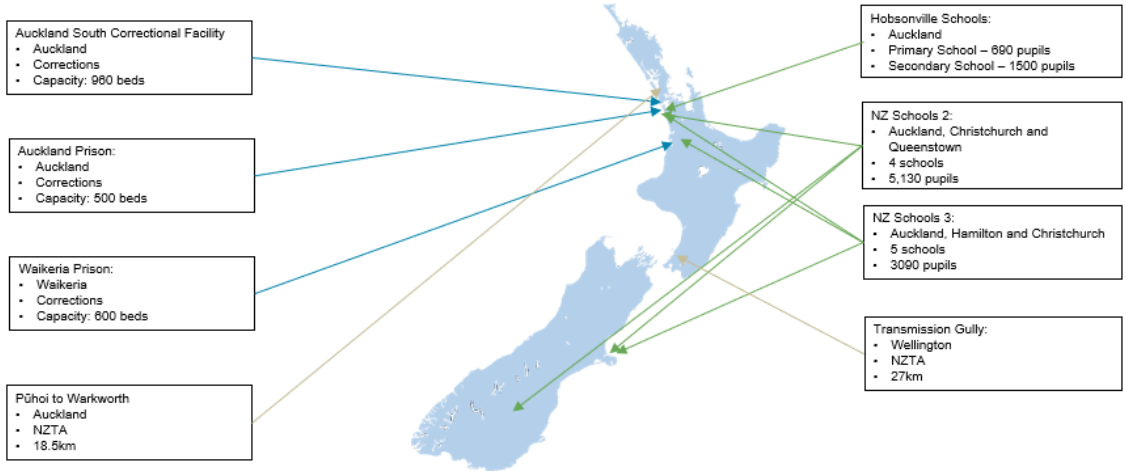
understood. In cases where there are uncertain service requirements, it is unlikely that the Model would be the most suitable procurement method.

2 The New Zealand PPP portfolio

2.1 Summary of the projects

To date, there have been eight PPP projects (the Portfolio) procured over the past 10 years. The Portfolio consists of three Ministry of Education (MoE) projects, three Department of Corrections (Corrections) projects and two Waka Kotahi NZ Transport Agency (Waka Kotahi) projects. Both the Waka Kotahi projects are horizontal infrastructure with the remaining PPP projects being vertical infrastructure[11]. The majority of PPP projects have been in the North Island, particularly in and around Auckland.

Figure 1: NZ PPP Portfolio



The Model utilises two procurement approaches to allocate roles and responsibilities, subject to specific project requirements. In both cases, the Crown retains ownership of the asset at all times:

- Design-Build-Finance-Maintain-Operate (DBFMO), which transfers the responsibility for delivery of the Design and Construction (D&C), financing, maintenance and lifecycle, and Operational Services using the asset, to the private sector partner (Contractor) for a defined period.
- Design-Build-Finance-Maintain (DBFM), which is similar to the above, but the Crown retains responsibility for the delivery of Operational Services using the asset.

For consistency in this document, the ongoing maintenance and lifecycle support of the asset by the Contractor, including for roading projects, is referred to as Asset Management and Maintenance (AMM). The delivery of services using the asset is referred to as Operational Services.

Of the vertical projects, only Auckland South Correctional Facility (ASCF) includes Operational Services (the day to day management of the prison). Both Waka Kotahi projects include some Operational Services, but these represent only a small component of the overall project given the nature of roading assets.

[11] The term 'horizontal infrastructure' typically refers to roads, rail, water and other utility assets, while 'vertical infrastructure' typically refers to buildings.

Table 1: NZ PPP Portfolio – summary details

Project name	Procuring Entity	Asset	Type	Equity Provider	Major D&C sub-contractor	Major AMM and (if applicable) Operational Services sub-contractor(s)
Hobsonville Schools	MoE	2 schools	DBFM	PIP I	Hawkins	Programmed Facilities Management
NZ Schools 2	MoE	4 schools	DBFM	PIP I and PIP II	Hawkins	Programmed Facilities Management
NZ Schools 3	MoE	5 schools	DBFM	PIP II and Pacific Partnerships (CIMIC)	CPB (CIMIC) and Southbase	Spotless
Auckland South Correctional Facility (ASFC)	Corrections	960 beds	DBFMO	Infrared (stake recently acquired by AMP), ACC, John Laing	Fletcher Construction	Serco (with AMM sub-contracted to Spotless)
Auckland Prison	Corrections	500 beds	DBFM	PIP I	Fletcher Construction	Cushman & Wakefield
Waikeria Prison	Corrections	600 beds	DBFM	PIP I, PIP II and Pacific Partnerships (CIMIC)	CPB (CIMIC)	Cushman & Wakefield
Transmission Gully	Waka Kotahi	27.0km Motorway	DBFMO	Infrared, ACC and Pacific Partnerships (CIMIC)	CPB (CIMIC) and HEB Construction	Ventia (CIMIC)
Pūhoi to Warkworth	Waka Kotahi	18.5km Motorway	DBFMO [12]	ACC, PIP II, Acciona Concesiones, Fletcher Building	Fletcher Construction and Acciona Infrastructures	Acciona Concesiones and Higgins

Portfolio timing

The first PPP project commenced procurement in 2010, with the most recent reaching FC in the second half of 2018. Of the eight projects, there are five that are operating at the time of this Review, with the remaining three projects still under construction. There are currently no new PPP projects under procurement.

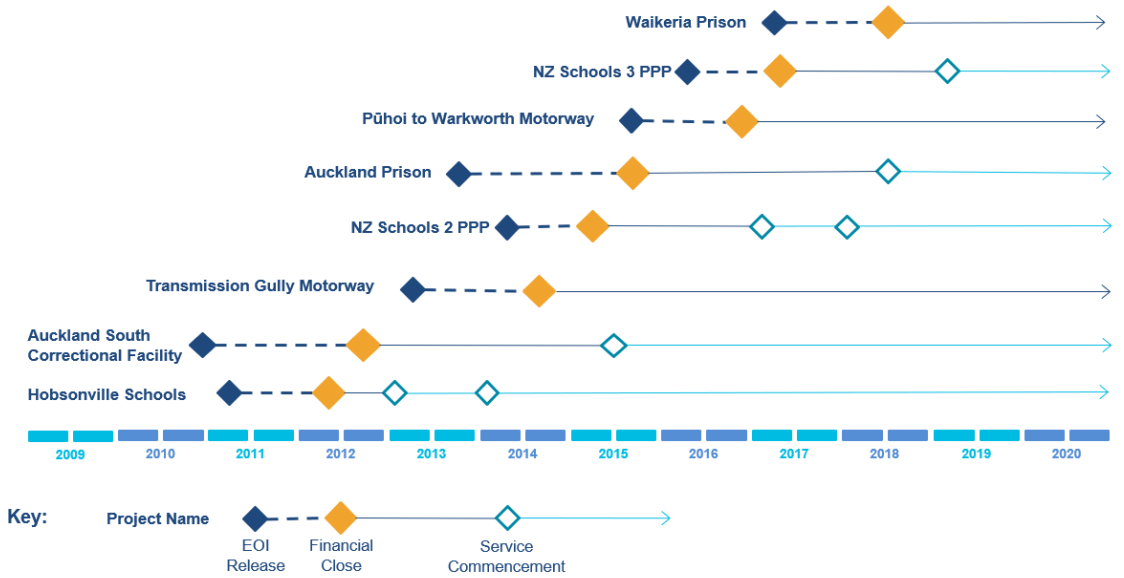
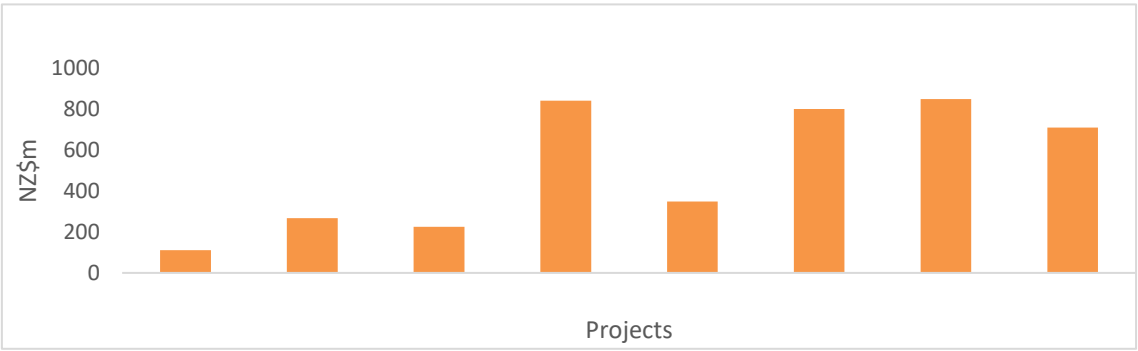


Figure 2: Portfolio timing

Financial value at FC

A total of $4.2 billion has been committed, based on the NPC as at respective FCs, across the Portfolio. The NPC represents the present value of the total value of the projects to the Crown over the contract term.

Figure 3: NPC ($m) at FC for each project

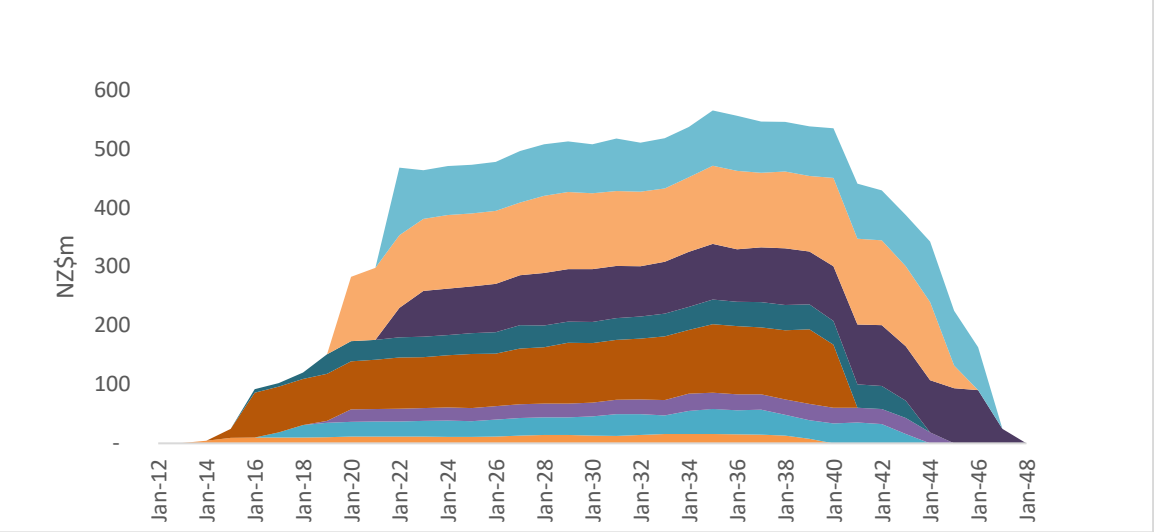


[12] Note that the scope of the 'Operate' component in Pūhoi to Warkworth is more limited than in Transmission Gully.

2.2 Unitary Charge to date

Across the eight projects, a nominal total of $12.8bn is forecast to be paid by the Crown over the contract terms. These payments are in the form of the Unitary Charge (UC) – the regular payment to the Contractor by the Crown during the Operational Period of the project. The forecast profile of the UC is set at FC, with the first payment not occurring until after construction is complete.

Figure 4: Forecast UC profile



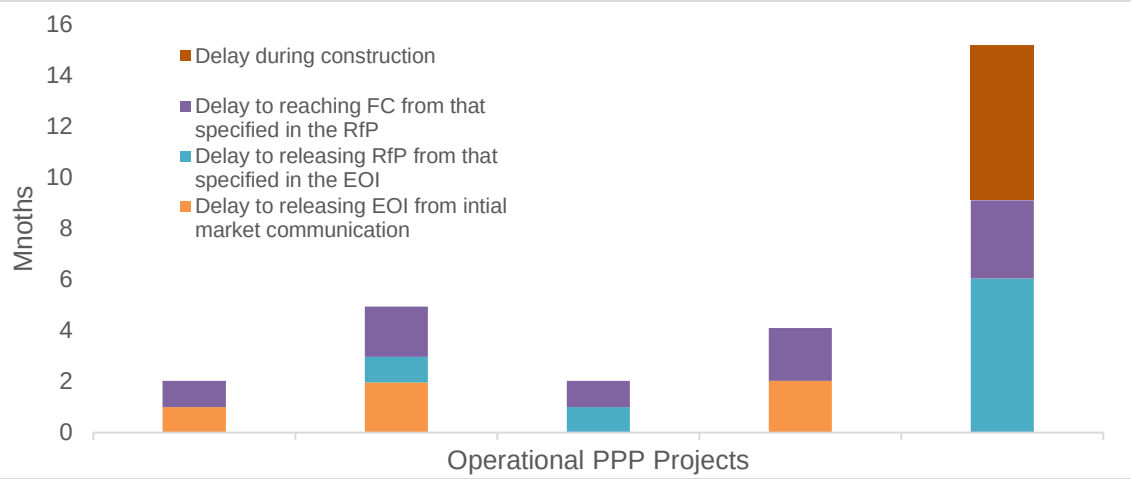
Over the Contract Period, the total UC paid incorporates the payment for the D&C, AMM, Operational Services (if applicable), Special Purpose Vehicle (SPV) management and financing costs. The Model does not provide for adjustments to the forecast UC due to changes in the Contractor's delivery costs except in limited circumstances, for example where a risk has been fully or partially retained by the Crown or where there has been a change in the scope of the project.

As of mid-2019, the total actual UC paid for the five operational projects was approximately $9.1m lower than that forecast at FC. This was due to a number of factors (some of which increased the UC), including changes to base interest rates, Crown initiated Change notices and deductions under performance regimes.

2.3 Delivery timeliness to date

All but one of the operational projects experienced delays of fewer than six months between the initial market briefing to Service Commencement, with the delay most commonly occurring between Request for Proposal (RFP) and FC. During this stage, the Procuring Entity and Preferred Bidder (PB) must agree and finalise project specific details and any derogations from the SFA as a result. Project delays between RFP and FC have generally been one or two months, with the exception of one project which was delayed at this procurement stage due to a change in government.

Figure 5: Delays across the five operational projects by stage



For those projects under construction at the time of this Review, a new completion date had been announced for Waka Kotahi's Pūhoi to Warkworth motorway (delayed from end of 2021 to May 2022)[13] and the Transmission Gully motorway to September 2021[14]. Further details are provided on page 24.

[13] https://www.nzta.govt.nz/media-releases/new-completion-date-for-puhoi-to-warkworth-motorway/

[14] https://www.nzta.govt.nz/media-releases/new-opening-date-and-covid-19-disruption-payments-agreed-for-transmission-gully-motorway/

Review Findings

3 Outcomes from the Model to date

This section provides a high-level commentary on the initial outcomes of the Model to date, based on interviews and other information collected during the Review. It is not intended to draw comparisons across different models. The Commission recognises that a comprehensive understanding of the Portfolio's performance requires a comparison of the Model against other procurement methods, with data required across both PPP and non-PPP projects. That has not been the specific focus of this Review, but the Commission does intend to undertake such research as part of its longer-term work programme.

3.1 Business Case objectives

As with all major government capital projects, the projects were subject to a formal Business Case process prior to approval, including an assessment of the PPP Model relative to conventional procurement methods, such as 'Build only', 'Design and Construct', and more collaborative approaches such as Alliances. Across the Business Cases for the projects, the following were common objectives sought by the Procuring Entity from the PPP Model:

- achieve greater price certainty and a more accurate and transparent assessment of whole-of-life cost,
- provide a strong level of risk transfer and remove the risk that the Crown is exposed to design and construction and related quality risks (e.g. leaky school buildings),
- provide incentives to optimise total whole of life project costs, including design, construction and maintenance,
- incentivise the on time and on budget delivery of the project,
- provide more time for providers of services within facilities to focus on core business, rather than asset management,
- attract major new entrants to the NZ construction and project delivery market,
- develop the Procuring Entity's understanding of planning and delivering complex projects with a whole of life focus, and new asset management techniques, and
- maximise innovation that could be replicated across the broader network of assets.

3.2 On-time and on-budget project delivery

The data available, as presented in the previous section, indicates that the procurement and Construction Periods of PPP projects have generally occurred without significant delay for four of the five projects achieving Works Completion. Further, the five operational projects have generally provided cost certainty to the Crown, with the level of UC paid being marginally lower than forecast at FC.

The most significant issues have occurred on the two horizontal PPP projects. On 11 February 2020, Waka Kotahi announced that it had reached a $190.6m financial settlement with the joint venture builder of the Transmission Gully motorway and a new completion date of December 2020. As stated in the announcement, the settlement was an acknowledgement that construction had been impacted by events that could not have been reasonably anticipated, including challenging site conditions, several storm events and the 2016 Kaikōura earthquake. Following an extensive period of subsequent negotiations

relating to the impacts of Covid-19, Waka Kotahi on 21 August 2021 announced that the completion date had been extended to September 2021.

Similarly, on 1 July 2020, Waka Kotahi announced a new completion date of mid May 2022 for the Pūhoi to Warkworth motorway as a result of COVID-19 impacts.

3.3 Broader outcomes to date

Based on feedback received, the Review makes the following observations:

- Interviewees commented positively on the **benefit of the PPP Model's disciplined approach to risk identification, quantification and optimal allocation**. This results in a more transparent approach to risk allocation and has been subsequently adopted in some non-PPP procurements. While there were comments that the allocation of certain risk types should be reconsidered for future projects, the overall approach was generally seen as a positive feature of the Model. Interviewees did comment more broadly that there are still underlying challenges in the construction market's ability to price and manage risk in large infrastructure projects, although this is not unique to the PPP Model. The Model's risk allocation is discussed further in section 6.

- The **standard of the PPP assets in operations were generally praised by interviewees**. It was also noted that the standard of ongoing maintenance of the assets was often superior to other similar assets managed by the Procuring Entity. In the case of the school projects, the reduced burden on Board of Trustees for property management was seen as a particularly positive feature of the Model as it freed up school resources to focus on education.

- There were a **variety of views on the extent to which the Model led to innovations in design, construction and service delivery**. Interviewees noted examples of innovative construction methods, health and safety approaches, facility operating models and design features, some of which were driven by performance regimes that incentivise meeting long-term availability and performance standards. It was also commented that a higher level of design development was evident through the PPP procurement processes as a way of demonstrating innovation (a key criteria for bid evaluation), although with corresponding higher bid costs. In some cases, the need for PPP assets to fit within a broader network of the Procuring Entities' operations can also limited innovation. Some interviewees stated that they had observed similar innovations on other projects under non-PPP procurement approaches (in particular, Alliance and other more collaborative models) and that PPP innovations largely reflected greater risk taking by the Contractor. Non-PPP procurement approaches can incentivise innovation where contractors are able to pocket associated savings. The lack of this incentive during the Construction Period for PPP projects (through the Change mechanism requiring savings to be returned to the Procuring Entities) was noted by interviewees as counter to the objectives of the Model and is discussed further in section 9.

- The **whole of life focus of the PPP Model was generally praised by interviewees**, although most operational PPP projects are still relatively new and therefore it is generally too early to observe the performance of Contractors in undertaking lifecycle renewals. Neither of the horizontal projects are in their Operating Period. In some cases, the Procuring Entity considered that lower cost materials had been used in some areas of the build, although it was also noted that the Contractor retains the long-term obligation and risk to maintain the asset with those construction materials. For horizontal projects, in particular, interviewees noted that the ongoing AMM and operations were relatively high cost. While the whole of life cost is still capped under

the AT, there is a potential lack of scale efficiencies for some asset types where a single PPP project is managed differently to the broader network of assets/operations in which it sits.

- The **operational PPP projects have generally performed well under their performance regimes, although concerns were raised regarding the breach regime.** As at mid-2019, the number of performance deductions has been modest for the operational PPPs. There were, however, mixed views on the design and administration of the performance regimes, both of which are discussed in further detail in section 10. Interviewees raised a number of concerns with the breach regime, particularly during the Construction Period. This is discussed further in section 10.3.

- There was only **limited feedback that the PPP projects had significantly impacted broader operations and asset management by Procuring Entities**. It was generally considered too early to tell if the PPP projects would materially impact the Procuring Entity's wider approach to capital asset management. Several interviewees commented that the number of PPP projects is very small relative to the broader procurement portfolios of Procuring Entities. This is further compounded by their relative complexity, which can make it harder for lessons learned to be visible to decision makers.

- A number of projects have attracted **international contracting resources** to the market, which arguably increases the competition and knowledge base for the NZ construction sector. Knowledge transfer via joint venture D&C sub-contractors comprising local and international capability is evident on some PPP projects to date.

Case Study: Infrastructure Partnerships Australia – Measuring the value and service outcomes of social infrastructure PPPs in Australia and NZ[15]

Infrastructure Partnerships Australia recently reported the outcome of a study by the University of Melbourne on whether mature social infrastructure PPP projects across Australia and NZ were meeting the service delivery outcomes set out in their contractual agreements, whether service benefits for end users had been achieved and the factors that have driven positive and poor user experiences. The review considered 12 projects that met the criteria for inclusion across the health, justice and education sectors.

At a high-level, the review found that the projects provided a high level of design and build quality and positive overall outcomes. In general, the projects achieved the outcomes at either 100% or slightly below the original Public Sector Comparator (see following section for further details). The report makes a set of recommendations, including on the future use of the PPP approach, the role of parties during the procurement process, and evolving the PPP contractual terms.

[15] https://infracom.govt.nz/assets/Uploads/Infracom-response-to-PPP-report-v2.pdf

4 Determination of the Public Sector Comparator and Affordability Threshold

4.1 Introduction to the PPP Business Case development process

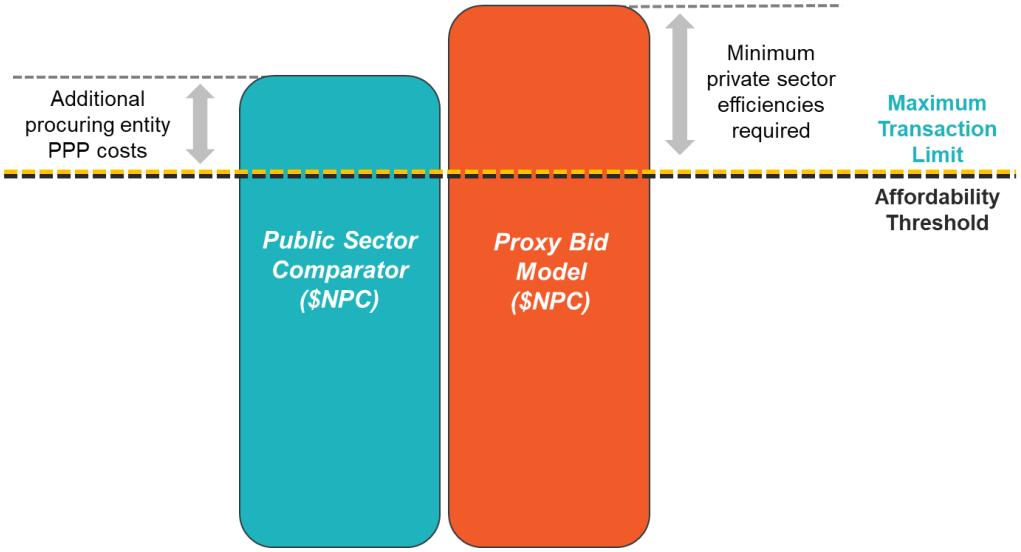
Detailed quantitative value for money assessment

If a project passes the qualitative PPP hurdle criteria (refer section 1.1), as well as any other procurement objectives that a Procuring Entity considers important, the Model is subject to a quantitative value for money assessment relative to a conventional procurement method. The key steps of this are[16]:

- The definition of a **Reference Project,** which is the net present capital and operating costs of the project if it were delivered under a conventional procurement method. The Reference Project is intended to be designed and estimated based on the same scope and quality of services required of the private partner under a PPP over the same time period.
- The definition of the **Public Sector Comparator (PSC).** This is an estimate of the *risk adjusted* NPC of the project using a conventional procurement method. It comprises the costs of the Reference Project, plus the estimated value of transferred risks and a tax adjustment to enable fair comparison with private sector PPP proposals. In other words, it represents the risk adjusted whole of life cost of the project if it were delivered conventionally taking account of the risk allocation between the private sector and Procuring Entity under a PPP.
- The Procuring Entity also develops a **Proxy Bid Model** which represents the estimated NPC that a private sector partner would require as payment for delivering the project as per the PSC, including supporting its own financing costs. It is calculated as the sum of the PSC, plus private sector financing costs and SPV administration costs. Given that the PBM will exceed the PSC, for the project to pass the value for money hurdle, the private sector must be able offset its additional costs (e.g. financing and SPV administration) through construction, operating and/or risk management efficiencies.
- Finally, the **Affordability Threshold (AT)** is the maximum price that a Procuring Entity is prepared to pay for a project. The guidance suggests that this should be equal to the PSC less any PPP-specific costs that the Procuring Entity will incur over the life of the project. During the procurement phase of a PPP, a bidder's price proposal must come under the AT to be considered compliant.

[16] Further details are set out in 'The Public Sector Comparator and Quantitative Assessment: A Guide for Public Sector Entities'.

Figure 6: Comparison of the PSC and PBM[17]



Purpose of the AT in the Model

The AT is a unique aspect of the Model and provides a mechanism to ensure the evaluation is focussed on which bid best achieves the greatest project outcomes (within the AT) rather than which has the lowest price[18]. This is important given that the methodology and weighting for an evaluation sends a signal to the market on the Procuring Entity's relative cost and quality priorities. Further, it impacts the level of interest from market players in participating in the procurement, as well as how they seek to achieve a competitive advantage.

The Model approach can be contrasted with other jurisdictions, such as Australia and the United States, where price can be a significant proportion of the evaluation scoring. Anecdotally, based on comments from interviewees with experience in other countries, the price evaluation approach can drive a focus on cost-cutting rather than quality in the development of bids. The greater focus on quality resulting from the AT in the Model was generally praised by interviewees, with the approach now being used in some non-PPP procurements for large capital projects.

4.2 Setting the Affordability Threshold

Given that the AT is a compliance requirement for bid submission, it is critical that the AT is set at the 'right' level to enable bidders to achieve the Procuring Entity's desired outcomes for the project. The AT aligns with the outcomes focus of the Model but can be problematic if the underlying PSC is not set appropriately. There can be numerous challenges to determining the PSC and AT, typically done during the Business Case stage, including:

- There may only be limited design information available to inform the calculation of the PSC. For some projects, more detailed designs can be costly to produce,

[17] 'The Public Sector Comparator and Quantitative Assessment: A Guide for Public Sector Entities'.

[18] There are limited circumstances where price is considered in the evaluation of bids. In particular, this can occur where quality is considered the same or similar across competing proposals, but there is a significant difference in price.

- The delivery costs and risks for some projects can be significantly impacted by geotechnical and other ground conditions (e.g. contamination, utilities), and site investigations may not yet be complete (or are not practical to complete) at the time of setting the PSC,
- At the Business Case stage, the Procuring Entity has likely not yet developed the performance regime or service specification for the project. Therefore, the PSC is informed by conventional methods focused on design and construction costs, with only limited assessment of whole of life impacts and other performance issues, and
- The quantification of risk transfer is challenging and is often informed by conventional methods, as well as being susceptible to optimism bias from Procuring Entities and their advisors (who may themselves have limited or no experience in project delivery). The final risk allocation may also not yet be fully developed.

Interviewees commented that on some PPP projects, the AT was, in their view, set incorrectly and that this had detrimental consequences for both bidders and the Procuring Entity, for example:

- AT set too low – a bidder pulling out from the process before the Proposal deadline leaving a single bidder. On another project, one of the bidders submitted a bid over the AT (which the bidder calculated to be the cost of meeting the Procuring Entity's requirements) and was excluded accordingly (again leaving only one bidder), and
- AT set too high – causing confusion among bidders about the Procuring Entity's requirements.

Another potential risk noted by interviewees of setting the AT too low is that it drives cost-cutting during the bid that may affect the quality of construction or reduce the Contractor's ability to absorb risks, leading to a greater likelihood of later claims against the Crown. For example, the Transmission Gully PPP – Lessons Learnt Review[19] states that the 'tight' AT on Transmission Gully:

- drove bidders to find alternative options to deliver and document the project (which presented as derogations to the project requirements and documentation), and
- potentially reduced competition.

Case study: Sydney Light Rail

The NSW Auditor-General's Report into the CBD and South East Light Rail Project demonstrates how a project's PSC can change significantly between the Business Case and execution of final contracts.

The cost of the project increased by $549 million and the Auditor-General's Report attributed $517 million of the increase to mispricing and omissions in the Business Case. The Auditor-General's Report concluded that the Business Case underestimated costs and overestimated benefits, because it did not fully assess capital costs and third party agreements with utility providers and local councils, which had not been finalised (which significantly affected the design and scope of the project). NSW allows the PSC to be updated as the project evolves, which it did, including to address an incorrect assumption that management effort and associated interface risks in a PPP would be the same as for a traditional delivery model.

[19] Transmission Gully PPP – Lessons Leant Review, December 2014, section 4.6.1 available at https://www.nzta.govt.nz/assets/projects/transmission-gully/docs/transmission-gully-ppp-lessons-learnt-review-dec-2014.pdf.

Several interviewees commented on the extended period of time that can elapse between the setting of the PSC in the Business Case and the RFP stage in which bids are being developed. During this time, it was noted that there could be significant changes that impact on the cost of the project, such as construction market cost inflation (differing from assumptions used in the PSC), additional information from site investigations, and changes in the Procuring Entity's requirements.

The PPP procurement process guidance states that the PSC and AT can be refined if the scope of the project changes or if new information comes to light that changes the Procuring Entity's estimate of the costs to deliver the project. However, several interviewees commented that there did not appear to be a systematic approach to triggering a review of the AT or a standard method to perform an update. It was also noted that an upward adjustment to the AT could create challenges for the Procuring Entity if the new AT fell outside of the existing budget approvals for the project. In addition, the RFP stage is a relatively short and intense process for bidders and the Procuring Entity, and therefore a late change to the AT could be challenging to adjust to. Procurement rules would also typically not allow adjustments once bids have been submitted to ensure fairness across bidders.

In practice, there may also be challenges in determining whether the AT is genuinely set too high or low, such as if only one bidder raises a concern. Some parties that carry the risk (e.g. major sub-contractors who are more experienced with conventional approaches) may be less familiar with the constraints of the Model, particularly the very limited opportunity for any future cost and time variations and may not raise concerns. Within the dynamics of a competitive bid process it can be difficult for a Procuring Entity to judge these signals about the level of the AT.

Some interviewees also commented that the method of calculating the AT and the assumptions underlying that calculation are not sufficiently transparent and it would be useful if bidders could have an opportunity to test the AT. In previous projects, only the AT dollar amount and discount rate has been disclosed to bidders. Interviewees had a range of suggestions about what should be disclosed, ranging from the full detailed PSC to the key assumptions and escalation rates that have been included. We understand that some Alliance projects have adopted an approach of providing a more disaggregated AT where detailed schedules of costs are shared with bidders.

Proposed Action: The Commission should update the guidance to Procuring Entities on setting the Public Sector Comparator and Affordability Threshold, including on the level of detail provided during the procurement phase and a framework for adjusting the Affordability Threshold if required.

5 Procurement phase

5.1 Introduction to the PPP procurement phase

The procurement of NZ PPPs has typically followed a three-stage process, as follows:

- **Expression of Interest (EOI) stage**: The Procuring Entity openly invites EOIs from interested consortia to deliver the project. The EOIs tend to focus on the respondent's experience and capability to deliver, with short-listed responses proceeding to the RFP stage.
- **RFP stage:** The Procuring Entity invites the short-listed EOI respondents to submit more detailed Proposals (also referred to as bids in this Review) for evaluation. Ultimately, the purpose of the RFP stage is for the Procuring Entity to select a **Preferred Bidder (PB)** with which it will enter negotiations. During the development of Proposals, bidders have the opportunity to participate in face to face meetings with the Procuring Entity as part of the **Interactive Tender Process (ITP).** This is a formal process where bidders can discuss their asset and service solutions and commercial approach against the RFP requirements and desired outcomes with the Procuring Entity and its advisors.
- **PB stage:** The highest scoring bid under the AT is designated as the PB. The PB and Procuring Entity then enter into a period of negotiation on any aspects of the Proposal that the Procuring Entity wishes to amend. Further design work and review can also occur in this period. The conclusion of this stage, where all contractual terms are settled and the PA is executed, is called **Contractual Close.** The final price details (including interest rate setting) are determined separately at **FC**, which in New Zealand has generally been 1 to 2 days after Contractual Close**.** For the purposes of this Review, FC is generally considered synonymous with the end of the procurement phase for a project.

5.2 Level of design specifications

An aspect of the procurement phase that both Procuring Entities and private sector interviewees identified as challenging was determining the most appropriate level of design specification, for the purposes of bid evaluation and for FC.

The Model is intended to be an outcomes-focused approach where the Contractor is responsible for designing and constructing the asset to achieve the outcomes captured in the Services Requirements and the performance regime. To achieve this aim, Procuring Entities must take care to avoid placing undue constraints on the Contractor's freedom to determine the best design solution, however, some participants have struggled with this lack of design specification. This is not unique to PPP projects and potentially reflects an immature D&C market more used to build only contracts. Indeed, some interviewees suggested that PPPs were initially introduced to a NZ market with very limited D&C capability, where clients developed their Reference Projects to well beyond the ability of a D&C contractor to evolve or optimise design, given pressure to achieve construction completion. Good D&C contractors can be penalised for highlighting design issues, while other contractors accept the design as offered and potentially deliver a poorer outcome. The NZ market is changing and through pre-procurement market engagement, D&C contractors are pushing back on highly specified design, untested for constructability and other risks.

In practice, there have been varying approaches to design specifications across different PPP projects, particularly with regard to:

- **different levels of design specification from the Procuring Entity.** Some projects have provided quite detailed specifications to bidders with more of an input focus. This approach has the effect of the Procuring Entity retaining some of the design risk and limits opportunities for innovation but does provide greater certainty for bidders. Other projects have provided only high-level design guidance, which has caused some bidders to struggle to design the asset in a way that meets the agency's operational requirements and constraints, and

- **different levels of design development required from bidders at different stages (i.e. RFP, PB and following FC).** This can be driven by the nature of the project, including whether the private sector will be responsible for Operational Services. Where the Contractor is required to operate the asset, there may be less of a need for the Procuring Entity to focus on asset design details (in contrast to a project where the Crown retains responsibility for the service delivery role and the achievement of outcomes within the specified design).

There are inevitably additional costs to bidders if they are required to prepare extensive designs during the RFP stage, and extensive design requirements may impose an unfair burden on unsuccessful bidders (see also discussion on bid costs below). Private sector interviewees suggested that some of the documents requested by Procuring Entities as part of Proposals were not necessary and added to the bid costs (e.g. full environmental management plans, traffic management plans etc)[20]. At a minimum, bidders need to undertake sufficient design to enable them to have certainty on price and confidence that their preferred design can be delivered within the AT. Ultimately, the level of design needs to provide the Procuring Entity with sufficient detail for bid evaluation and the ability to hold the Contractor to its winning design through the PA, while balancing this against bid costs and the bidder's view on how best to manage its own design risk.

While some private sector interviewees suggested that less design should be required for Proposals, they also acknowledged that further design would therefore be required during the PB stage to obtain a more certain risk adjusted price, essentially implying further price adjustment pre-FC. This additional step to obtain a target outturn cost (TOC) is not an uncommon feature of D&C models, but it is not a feature of the Model.

To manage design risk, some Contractors have sought a longer PB stage and commencement of the Design Review Procedure (refer section 8) pre-FC to obtain some level of endorsement and a clearer basis for Change post contract. The SFA is clear that the Procuring Entity's endorsement of design pre or post contract does not mean that the Contractor is relieved of its obligations to meet the design specification (contractually referred to as the Works Requirements). This means that Contractors will likely seek further negotiation of the Works Requirements in an attempt to shift the design specification to a more input based approach. In effect, the extent of Works Requirements negotiation, pre-FC design work (appended to the contract) and the Design Review Procedure is a way for the Contractor to manage its risk.

The more input based the design specification, the more comfortable the Contractor is likely to be in carrying design risk, having satisfied the Procuring Entity through the procurement process. The Contractor is more confident in meeting the Works Requirements (and the Service Requirements) and in

[20] The Commission has not sought to form a judgement on whether such information requests were required, but notes that in particular for horizontal infrastructure, many of these management plans relate to the method of construction delivery and hence understanding of risk and ultimately price.

the basis for Change. This can also mean a shorter PB stage. A more input-based specification, however, can limit opportunities for innovation in design.

Getting the right balance between the level of design specification, sufficient design to provide price certainty, and the approach to design risk is influenced by:

- the Procuring Entity's confidence in and desire for market participants to bring innovation in design while limiting constraints,
- market participants understanding of the Model and ability to price design risk at bid submission without subsequent adjustment, while also minimising bid costs,
- for a PPP where the private partner is responsible for Operational Services, the extent to which the operator is prepared to underwrite the Contractor's design,
- the extent to which the Procuring Entity is prepared to adjust its Works Requirements to more input based and provide some level of endorsement pre-FC,
- the Contractor's trust in the Design Review Procedure not to increase its risk post contract, and
- the ability of both the Contractor and Procuring Entity to clearly establish a basis for Change under the contract.

Proposed Action: The Commission should develop further guidance for Procuring Entities on determining the appropriate level of design specification to include in RFP documents and the appropriate level of design development required (inclusive of relevant management plans for consenting, environmental and construction purposes) from bidders during the procurement process. This guidance should recognise the costs to bidders of extensive design work and subsequent steps that may be required during the Preferred Bidder stage, as well as the importance of keeping desired risk allocations intact.

5.3 Interactive Tender Processes

An important aspect of the RFP stage is the Interactive Tender Process (ITP) sessions, which provide for interactive discussions between the Procuring Entity and bidders. The ITPs are intended to assist bidders to submit the best Proposal possible by allowing them to "*discuss the development of their commercial and operational approach, concepts and designs and to seek clarification and feedback to improve their understanding of the project and required outcomes*."[21]

Importantly, ITPs are not for the Procuring Entity to offer evaluative feedback on the bidder's solution or to direct the content of their Proposal. It is the bidder's job to develop their own Proposal to meet the desired outcomes which, once submitted, will then be evaluated during the evaluation stage. The target outcomes of the ITP process are that:

- bidders have had, and have successfully taken, the opportunity to fully explore their developing Proposals against the RFP requirements and the desired outcomes of the project,

[21] The PPP Procurement Process: A Guide for Public Sector Entities.

- as a result, the solutions submitted in final Proposals have been improved and better achieve the investment objectives of the Procuring Entity,
- the cost and time burden of the process has been kept to a minimum for all parties, and
- probity has been upheld throughout the process.

The feedback from interviewees is that both Procuring Entities and bidders generally find the ITP sessions to be of critical importance, but the ITPs have not always provided the intended benefits to bidders. Some private sector participants have felt that some ITPs did not provide sufficient feedback and guidance to the bidder, particularly in the design sessions. A number of different potential causes were discussed during interviews for why ITPs have not always functioned openly, as intended:

- **An overly cautious approach to managing probity risks.** It was suggested that Procuring Entities on some occasions have taken an overly conservative approach to ensure that they are not seen to be directing the development of Proposals,
- **Insufficient preparation for an outcomes-based procurement approach.** At the time of the ITPs, the Procuring Entity may not have a settled view on 'what it is looking for' and therefore may not feel confident in providing more detailed feedback during ITP sessions,
- **A lack of experience and maturity from attendees.** Both Procuring Entities and bidders commented that it is important to carefully select the right attendees from both sides to obtain the most benefit from the sessions. Attendees should have sufficient knowledge of the Procuring Entity's requirements and the bidder's Proposal respectively to provide the most valuable input. Appropriate subject matter experts should be included to allow peer to peer interaction on particular topics. All participants should have a good understanding of the ITP process and how to best use the time, either through previous experience or through appropriate training, and
- **Concern that ITPs would be evaluated.** Despite the clear guidance that the ITP sessions do not form part of the evaluation, bidders interviewed expressed a belief that the ITPs are part of a competitive process. This may affect bidders' willingness to ask questions or make comments that they think might place them in a bad light compared to other bidders.

It should be noted that there was significant variation in feedback on the effectiveness of the ITPs across different projects. The ITPs for some projects were consistently well-regarded by interviewees.

Discussion: Observations and lessons learnt from successful ITPs

Based on work conducted during the Review to support the development of revised guidance, the Commission's initial thinking on key features that can support productive ITPs include:

- Successful ITP processes require skill, experience and maturity from participants on both the bidder and Procuring Entity sides. The process occurs within the natural tensions of a competitive process, which can restrict trust and limit interaction (bidder side), and probity concerns, which can also limit interaction (Procuring Entity side). If these tensions are not recognised and appropriately managed, they can stifle achievement of the desired outcomes.
- The Procuring Entity can influence the quality of the interaction and it is appropriate for it to take a good degree of responsibility for this. However, a bidder who lacks experience, is disorganised, or is internally dysfunctional will limit their own potential.

- Successful ITP participants on the bidder side have the confidence to trust the process, share their ideas, and work with the Procuring Entity to understand the purpose of probity, to have a well thought through plan for managing it, and to have confidence in their ability to implement the plan to manage the probity line as it arises.
- Balancing interaction quality against probity requires vigilant attention by the Procuring Entity. All participants on the procuring side should understand probity, but one or two individuals should be assigned the role of managing the interaction and policing probity. All participants should clearly understand their roles including in relation to the leads.
- The Procuring Entity cannot coach the bidder toward its solution, as this would violate probity, but it does have a role in guiding the bidder toward a quality interaction to help the bidder realise its own best solution. Probity requires fairness, so the principle here is that all bidders receive equitable process guidance.
- The ITP process is about people, so behaviours are central. The Procuring Entity has a role both in understanding and managing its own behaviours and in understanding, recognising and adapting to the behaviours of bidders including as these evolve throughout the interactive process.
- Trust is a highly important part of the ITP process and of the procurement process overall. The Procuring Entity should see the ITP process in the broader sweep of the overall procurement process. Trust is to be built for the benefit of the ITPs but also because it will be needed in the negotiation that follows. Trust is set through behaviours.
- The Procuring Entity should be conscious of the interpersonal dynamics in the room and should aim to maintain consistency. Bidders will be aware of the decision hierarchy within the Procuring Entity but will not have visibility of internal process or depth of senior involvement and may misinterpret responses (including body language).
- Innovation is to be encouraged but there can be a tension between bidders exploring innovation and pursuing it too far if it turns out not to best serve the Procuring Entity's desired outcomes. If there are potential innovations that the Procuring Entity is not willing to entertain then these should be identified in the RFP. If they are identified in the ITP process, then this should be communicated to all bidders as early as possible.
- The Procuring Entity's internal preparation and debrief sessions are an important part of the ITP process. Preparation should take account of the bidder's previous ITP sessions and the overall ITP trajectory. Debriefs should consider any intra-ITP communications that are needed (for example, for probity or to manage RFP clarifications) and set preparations for the bidder's next ITP. This could include providing clarifications on issues where bidders may be reluctant to ask a Clarification Question given the competitive nature of the procurement.
- The Probity Auditor is an important role and should be a friend of the process. The Procuring Entity should discuss its ITP approach with the Probity Auditor and provide assurance that it understands and can manage probity in the process.

Proposed Action: The Commission should prepare guidance for Procuring Entities on conducting effective interactive sessions with bidders during the procurement process (both for PPP and non-PPP

procurement) in a way that provides value to the Procuring Entity and the bidders and preserves probity.

5.4 Bid costs

Several interviewees from the private sector commented that PPPs are more expensive to bid than conventional procurement methods, due to the level of design and other documentation sought in the RFP stage. While Procuring Entities can endeavour to minimise bid costs by carefully considering the RFP response requirements and only requesting information necessary to enable it to undertake a robust evaluation, costs are still likely to be relatively high. Some interviewees gave a clear indication that bid costs are likely to be a barrier to market interest in future PPPs, particularly when comparing the value of PPP projects in NZ to the bid costs and to the size of PPP projects in neighbouring countries, such as Australia. Interviewees considered that shortlisted bidders should be given some form of compensation for bid costs, particularly in relation to design work.

The RFP for the Transmission Gully project provided for the unsuccessful bidder to be reimbursed its reasonable design costs up to a cap in exchange for transferring the intellectual property rights in its design to Waka Kotahi. According to the Transmission Gully PPP – Lessons Learnt Review, the bid stipend was seen by bidders as critical in receiving approval to bid and contributed to the quality of the submission.[22] The Pūhoi to Warkworth Project also provided a stipend, which was designed to take into account the level of design fees and the nature of bid-risk expectations amongst thebidding consortia parties, while ensuring that bidders still had 'skin in the game'.

Waka Kotahi has provided bid costs on a limited number of other major construction projects (both PPP and non-PPP) where bidders are asked to undertake significant amounts of design as part of their bids (e.g. the Waterview Connection tunnel project). The payment of bid costs is on the condition that the bidder transfers intellectual property in tender designs to Waka Kotahi. There are also other examples where the reimbursement of bid costs (up to a cap) has been included within RFP documents, such as where the procurement process could be susceptible to a government policy change. (e.g. ASCF, Hobsonville Schools, the Christchurch Social Housing Transfer Transaction).

In Australia, the payment of bid costs (or stipends) is more common than in NZ and both the NSW and Victorian governments have adopted formal bid cost contribution policies. The NSW Government's Bid Cost Contributions Policy[23] provides that the NSW Government will consider contributing up to 50% of the estimated bid costs for unsuccessful bidders on construction projects with an estimated total capital cost over $100 million where:

- the provision of a bid cost contribution has been demonstrated to provide value for money,
- the relevant bidder has submitted an appropriately developed bid but has not been awarded the contract, and
- the bidder has agreed to vest the Intellectual Property in the NSW Government.

[22] Transmission Gully PPP – Lessons Learnt Review (December 2014) https://www.nzta.govt.nz/assets/projects/transmission-gully/docs/transmission-gully-ppp-lessons-learnt-review-dec-2014.pdf, section 4.5.1.

[23] https://www.treasury.nsw.gov.au/sites/default/files/2018-12/ERC%20Submission%20-%20Attachment%20B%20-%20Draft%20Bid%20Costs%20Contribution%20Policy.pdf

The Victorian Government Bid Cost Reimbursement for major Construction Projects Policy[24] applies to major construction projects that meet specified project specific criteria, broader market criteria and conditions, or in certain circumstances, there has been a change to the tender. It does not include a capital cost threshold, although projects must be of "significant scale and complexity". Bid costs are partially reimbursed and the transfer of intellectual property is also a feature of the policy.

Proposed Action: The Commission should develop a policy on bid cost contributions for major construction projects, in consultation with relevant agencies.

[24] https://www.dtf.vic.gov.au/infrastructure-investment/bid-cost-reimbursement-major-construction-projects

6 Allocation of risk between parties

6.1 Introduction to the PPP risk allocation

A key aspect of the Model is that it seeks to drive value through an optimal allocation of risk between the Crown and the private sector partner. In particular, the Model explicitly considers lifecycle and operating cost risks that are usually not a focus of conventional procurement methods. A key principle is that specific risks are identified and quantified, with those identified risks then allocated to the party best able to manage them. This risk quantification and allocation process is typically undertaken during the development of the PSC and Business Case. The impacts of an inappropriate risk allocation include:

- **Lower value for money** for Procuring Entities where a bidder inefficiently 'risk prices' for a risk that it does not have sufficient information to assess or is not well placed to manage,[25]
- **Lower competition** where the risk allocation deters potential market players from participating in a procurement process, and
- **Stress on major sub-contractors**, leading to increased risk of compromised quality or more claims being passed on to the Procuring Entity.

The feedback from interviewees generally praised the transparent and disciplined approach to risk allocation throughout the procurement process that is an inherent feature of the Model. However, there were concerns raised on a small number of specific risk areas, which are discussed further below.

6.2 Consenting risks

Feedback suggests that Contractors have at times struggled to comply with their obligations in relation to the Resource Management Act (RMA), including complying with RMA Designation conditions and obtaining and complying with Consents[26]. Consents are defined under the SFA and, amongst other things, include any required approvals from a government entity to enable the Contractor to meet its contractual obligations. This includes environmental resource consents under the RMA.

Sharing of consenting risk

The SFA (Schedule 6) provides a framework for sharing of Consent compliance. It advises that PAs should divide responsibility for compliance between the Contractor, Crown and Shared Responsibility. Responsibility for complying with RMA Designation conditions and obtaining and complying with Consents is allocated between the Crown and the Contractor on a project specific basis under each PA (known as Crown Consents and Contractor Consents respectively).

Interviewees from both the public and private sector suggested that there should be further consideration of the allocation of roles and responsibilities for obtaining and complying with Consents under the RMA and managing communications with consenting authorities and other stakeholders. For horizontal infrastructure projects, in particular, managing the consenting process involves a significant degree of

[25] Risk pricing is an important aspect of bid pricing in which a bidder rationally prices in a risk premium for certain risks. However, if the quality of information available to the bidder is insufficient, the resulting price may inefficiently reflect the true value of the risk.

[26] Consenting issues are also raised in the Transmission Gully PPP – Lessons Learnt Review.

stakeholder communication and management that the private sector is often less well placed to manage than the Procuring Entity. Stakeholder communication is discussed in more detail below.

As a general principle, consenting risk should be allocated on the basis of who is best placed to bear responsibility for obtaining the Consent and complying with it. In this context, it is important to bear in mind that design is a critical input to the consent process, and design is a Contractor responsibility. Under the SFA, the Contractor is required to use its best endeavours to assist the Crown to obtain all Crown Consents. However, the SFA and most PAs[27] contain no equivalent obligation for the Crown to assist the Contractor to obtain Contractor Consents. Industry standard construction contracts such as NZS Conditions of Contract[28] generally contain a mutual obligation for the Principal and the Contractor to provide all necessary information and documents to enable the other party to obtain Consents that the other party is responsible for obtaining.

It is important that there is clarity in the nature of the consenting risk allocation and obligations between the Procuring Entity and the Contractor. During negotiations, it is vital that this is a focus for all parties. There will, however, likely be occasions where the Crown should assist the Contractor for the benefit of the project with the clear understanding that it is not taking back the risk from the Contractor. Other potential adjustments could also be made, for example, caps on time for obtaining Consents that allow the Contractor extra time and cost where the consenting authority processes take longer than anticipated through no fault of the Contractor.

Case study: Different approaches to RMA Designation conditions

Procuring Entities have adopted different approaches to obtaining Designations for projects, where required. Of particular note, is the different approach taken by Waka Kotahi with the Transmission Gully project compared to that of the Pūhoi to Warkworth project.

The Final Report and Decision of the Board of Inquiry into the Transmission Gully Proposal[29] was published in June 2012, prior to approval of the Business Case in September 2012, and prior to commencing the PPP procurement. Transmission Gully had had a long history of examining different route options. Notices of Requirement (NORs) were initially lodged in 1996, and a designation established in 2002. Further work to refine the design resulted in a modified (and better) alignment, unconstrained by the existing designation, being approved by the Waka Kotahi Board in 2008. An assessment of environmental effects and detailed work to obtain new planning approvals took place between 2009 and 2012 resulting in the Board of Inquiry approval. The Consenting Strategy outlined in the Business Case stated that a total of six different NOR designations had been confirmed along with a total of 16 resource consents with an associated 1643 conditions attached. The Board of Inquiry required that the project should be delivered in general accordance with the detailed work submitted as part of the approval process. This detailed work allowed little room for flexibility and innovation in design and construction.

In early 2012, Waka Kotahi established a Planning Alliance (Further North Alliance) tasked with obtaining consents that could achieve the best outcomes for the Pūhoi to Warkworth motorway project. In anticipation of a potential PPP approach, the consenting strategy aimed to achieve conditions that

[27] A select number of later NZ PPP PAs do include a requirement that the Crown use reasonable endeavors to assist the Contractor in maintaining Consents

[28] NZS 3910: Conditions of contract for building and civil engineering construction

[29] https://www.epa.govt.nz/assets/FileAPI/proposal/NSP000008/Boards-decision/33ecec3074/Transmission-Gully-Final-decision-volume-2-Conditions.pdf

would enable the highest level of flexibility for the design and construction of the motorway so as to support innovation and value for money in its delivery. Waka Kotahi determined that the extent of work carried out for the Transmission Gully project was not a requirement for achieving consents. The Final Report and Decision of the Board of Inquiry into the Pūhoi to Warkworth Proposal[30] published in September 2014 noted that the project was based on an indicative alignment and design. The Further North Alliance was successful in obtaining consent conditions that were more outcomes focused, providing flexibility for innovation, including alignment optimisation.

The consent conditions for the Pūhoi to Warkworth project were significantly different to those on the Transmission Gully project. The Transmission Gully project faced a narrow designation and more challenging consent conditions. It was not consented with a PPP in mind.

It should also be noted that members of the Further North Alliance were retained to assist in the Pūhoi to Warkworth PPP procurement phase. This was not the case with the Transmission Gully project. Consultants involved in the detailed planning work and consenting process were let go prior to procurement commencing.

Proposed Action: The Commission should review the drafting of the Standard Form (PPP) Project Agreement to ensure there is clarity in the allocation and nature of consenting obligations between the parties, including consideration of the inclusion of a 'reasonable endeavours' obligation on the Crown as seen in some PPP projects.

New Zealand consent requirements

A number of interviewees identified that the difficulties some Contractors have faced with obtaining and complying with Consents and complying with RMA Designation conditions may have arisen from a lack of understanding of NZ's resource consent requirements by foreign parties involved in bidding consortia. Some interviewees suggested that, as an example of "bid fever", the advice of local parties involved in the consortia may not have always been heard.

NZ has a specific resource consent regime, which may require Contractors to obtain Consents from multiple consenting authorities, particularly for large horizontal infrastructure projects. This contrasts with some projects in Australia that operate under different arrangements, and some bidding consortia members may have assumed incorrectly that similar arrangements apply in NZ. However, consenting and planning approval requirements are requirements of law, which are necessarily specific to each country or jurisdiction. As with all allocated risks, it should be expected that bidders obtain and listen to advice on local consenting requirements as part of preparing a bid and in project delivery.

[30] https://www.epa.govt.nz/public-consultations/decided/ara-tuhono-puhoi-to-wellsford-road-of-national-significance-puhoi-to-warkworth-section/final-report-and-decision/

Case study: Consenting major projects in Australia

The Commission understands that in some states in Australia, the consenting authority can be the Minister responsible for planning and development rather than local or regional councils. For example, in NSW, the Minister for Planning, rather than a local or regional council approves State Significant Developments, which are certain types of development over a certain value or in specified areas, such as new educational establishments, hospitals and correctional centres, tourist or recreational facilities over a certain value. It is, however, still critical that impacted stakeholders are considered as part of any consenting for major projects.

In Victoria, the Minister also has the power to call-in planning permit applications in certain circumstances, including where the decision has been unreasonably delayed.

Interviewees also raised comments about the capacity of consenting authorities in regional areas to process consents for very large projects such as the PPPs. The level of capability and experience with major projects is likely to differ across consenting authorities, since ongoing and recurring major project work is needed to develop skills and greater consistency to meet the requirements of these projects. Where a local authority is likely to have little capability or track record with major project consenting, this should be a consideration in the consenting risk allocation.

The NSW Public Private Partnership Guidelines 2017 recommend that the ITPs include a session with the Department of Planning and Environment so that bidders can understand the development approval process and any planning conditions likely to be set. Confidential sessions with local consenting authorities during the RFP stage may assist bidders in understanding the likely process and timeframes for obtaining Consents. This approach has been used in some instances for previous NZ PPP projects, including for horizontal infrastructure. However, where such opportunities are provided it is beholden on the bidders to engage with consenting authorities in a proactive and open manner. Some bidders have been reluctant to do so, out of fears for the confidentiality of their emerging design solutions. Given the confidentiality protections in place, such a mindset is counterproductive to the important goal of adequately preparing to mitigate and manage the consenting risk. Given the significant of potential consenting risks, it is critical that they receive sufficient focus by financiers and advisors, and that the D&C major sub-contractor has the capability to understand and manage these risks.

Proposed Action: Procuring Entities should ensure that there is sufficient due diligence undertaken on the bidder's proposed strategy and capability in relation to consenting, particularly for horizontal projects. This should be included as part of interactive sessions and in bid evaluation.

6.3 Third party risks

Both public and private sector interviewees commented that the responsibility and risks in relation to third party stakeholder management should be shared as the Contractor is often not best placed to manage these risks. For many projects, the lengthy site selection and consenting processes that often precede a procurement process can result in established relationships between the Procuring Entity and stakeholders that would take time for a Contractor to take over or replicate. The resources for the Contractor to manage these relationships can also be difficult to judge and therefore difficult to price.

The above issues are generally more complex on horizontal projects given the larger site footprint and more complex consent conditions and therefore generally larger number of stakeholders with which to engage. The Contractor can be required to engage with a range of third-party stakeholders to comply with their obligations, including:

- consenting authorities, including regional and local councils, in relation to Consents,
- affected parties, in relation to the Consent conditions (including, for example, other government entities, interest groups, other submitters to the consent process) and in relation to the effects of the project, particularly during construction (local communities),
- utility providers, in relation to existing utility services (which impact risks relating to ground conditions) and the installation of new utility services (e.g. water, electricity, gas, telecommunications, drainage and sewage). For example, the Transmission Gully alignment intersected in several places with the main gas line between Taranaki and Wellington and an electricity transmission line,
- private landowners, in relation to land acquisition and the impacts of the project on adjoining land. In each of the horizontal PPP projects, a separate mechanism was developed to manage the interaction with private landowners. This recognised that some obligations were not sufficiently well known at FC to simply be transferred to the Contractor, and
- iwi, including mana whenua, where the roles and responsibility of the Crown, as a Treaty partner, cannot and should not be transferred to another party.

The arrangements with these third parties often have a significant effect on the design and scope aspects of the project, and consequently a cost impact. Slow engagement by third parties may also delay construction. The way in which the Contractor manages the relationships with third parties affects the reputation of the Procuring Entity and its relationship with those third parties and with others. If the Contractor manages this relationship poorly or persistently breaches agreements with those third parties (e.g. consenting conditions), there is a risk of damage to the Procuring Entity's long-term relationship with the relevant third party. This may affect other and future projects undertaken by that entity.

The ability of the Contractor to anticipate and manage third party stakeholder risk is also dependent on the level of clarity in the stakeholder arrangements that it inherits. A key finding of the NSW Auditor-General's Report on the CBD and South East Light Rail Project was that Transport for NSW's failure to finalise key third party agreements that would affect the design and scope of works before tendering or before signing contracts, increased complexity and risk and reduced value for money to the State.

Proposed Action: Procuring Entities should consider whether the Contractor is best placed to manage all third-party stakeholders and consider amending the risk allocation in the Standard Form (PPP) Project Agreement to reflect this on a project by project and specific stakeholder basis.

Proposed Action: Procuring Entities should seek to ensure that key third party agreements that affect project design, scope and access to land are finalised early (i.e. before entry into the Project Agreement), and where this is not possible, the Project Agreement should state how outstanding risks are to be managed.

6.4 Unknown risks (ground conditions)

A number of private sector interviewees commented on the allocation of risks related to ground conditions and utilities. In particular, it was suggested that it is not appropriate for the Contractor to bear the full ground conditions risk because:

- the Contractor does not choose the site (the Crown does),

- bidders do not always have the ability to access the site or conduct geotechnical investigations during the RFP or PB stages, and
- depending on the size and nature of the site, there are some ground conditions that no one is in a position to properly pre-assess, as it is not possible or practicable to uncover the full ground conditions through geotechnical investigations alone.

It was noted by interviewees that these issues are exacerbated in horizontal projects. In a vertical project the site is relatively small and contained, which means it is more likely to be feasible for the Procuring Entity and/or bidders to undertake extensive investigations of the ground conditions. In a horizontal project, such as a road, the size of the site and the extensive groundwork that is likely required may make it impractical for either the Crown or the bidders to conduct sufficient investigations along the entire length to fully inform an understanding of variable ground conditions. For example, Transmission Gully is 27 km long and Pūhoi to Warkworth is 18.5km long.

The SFA deems the Contractor to have conducted ground investigations (i.e. prior to execution of the PA) and places the risk of Site Conditions[31] on the Contractor. The Contractor is only entitled to time and cost relief for a Find (e.g. fossils, antiquities, protected objects, protected wildlife, human remains, ordnance), a Māori Claim or Adjoining Crown Site Contamination. The Contractor is entitled to an extension of time, but no additional cost, for Unforeseeable Contamination[32]. There is no provision for either time or cost relief in respect of geotechnical conditions.

Interviewees in the construction sector commented that they are increasingly unwilling to assume ground conditions risk on a project including, in particular, risks relating to in-ground utilities[33]. This is a trend observed in both NZ and Australia. For some projects Procuring Entities allowed bidders to conduct their own geotechnical site investigations and/or the Crown provided geotechnical and utilities reports as part of the RFP. The PA did not provide relief for ground conditions not disclosed in those reports. While such reliance issues are also present in non-PPP forms of procurement, the issues are heightened given the more fixed risk allocation inherent in the Model. Where reports are provided, which can include significant volumes of technical information, there is also a practical challenge of time and cost to interpret them during the bid period.

In two projects, there were early works packages under separate Early Works Agreements before the PA was executed. A potential benefit of such Early Works packages is that they can have a separate price and risk allocation from the remainder of the PA. However, the primary driver for these agreements was to expedite the programme of works while the main PA was being negotiated, rather than addressing ground conditions risk. Only one of these packages of Early Works was paid for by capital contributions by the Crown. The other was incorporated in the Base Case Financial Model once the PA was executed.

There are a number of potential options to provide more certainty where unforeseen ground conditions risk is to be transferred to the Contractor. For example, Procuring Entities could either allow bidders to conduct their own geotechnical investigations during the RFP or PB stages or allow bidders to rely on the geotechnical information provided with the RFP. For the latter, there may be benefit in such upfront

[31] Site Conditions is defined in the SFA and refers to any physical conditions on, under or over the surface, or in the vicinity of the Crown Site.

[32] Unforeseeable Contamination is defined in the SFA and refers to Contamination that would not have been foreseen by the Contractor at the Execution Date if the Contractor had taken a defined set of actions (e.g. examined all information available to it by the Crown).

[33] This was a significant issue in the Sydney CBD and South East Light Rail Project.

investigations being more extensive than they have been in the past given how significant these issues are to the successful delivery of PPP projects. This would require sufficient preparation time ahead of initiating the PPP procurement. Further, such reliance could be structured whereby the Contractor takes the risk up to a certain threshold, with the Procuring Entity responsible beyond that point.

Amending the risk allocation in the SFA in relation to Site Conditions (for example by allowing time and cost relief for certain unforeseeable site conditions) is potentially inconsistent with the generally fixed cost, fixed time nature of the Model (albeit noting the relief that already exists for certain Events, such as those discussed above). However, it is an area that should be investigated further for future (particularly horizontal) projects. Where appropriate, Procuring Entities may need to consider alternative risk allocations in relation to unforeseeable site conditions, depending on factors such as scale of the area and the ability for investigations to be conducted prior to finalising the PA. In circumstances where the risk is of significant scale and cannot be known or efficiently transferred to the Contractor, this should be considered during the Business Case phase in determining whether the PPP Model is the most appropriate procurement method for the project.

Proposed Action: The Commission should consider amending the default risk allocation in the Standard Form (PPP) Project Agreement in relation to the risk of unforeseeable ground conditions.

7 Role of the Special Purpose Vehicle

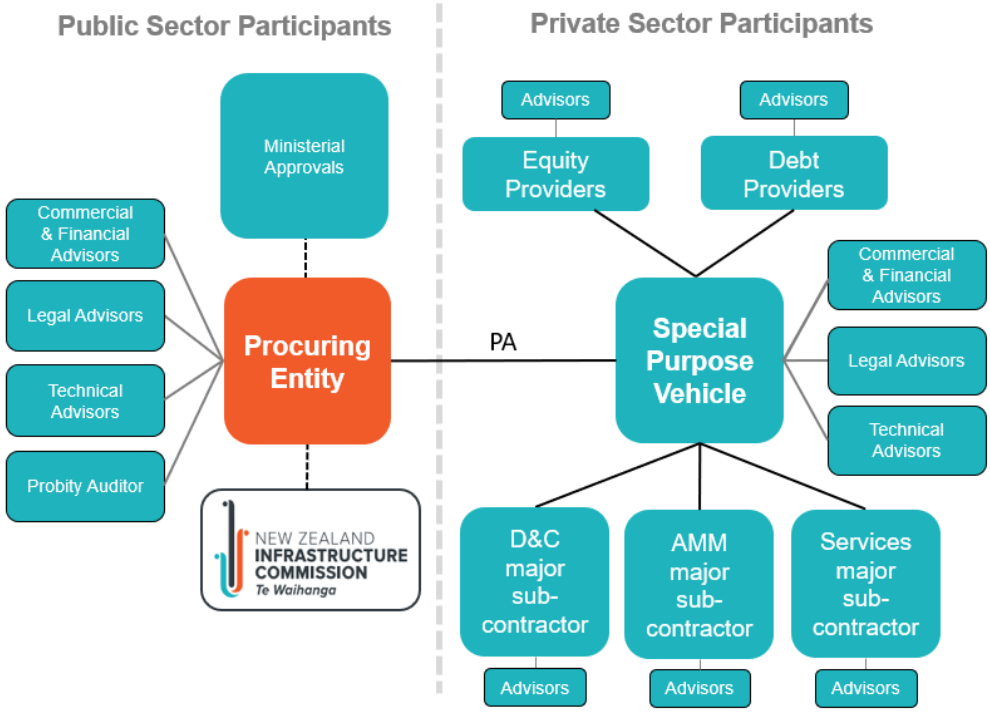
7.1 Introduction to the Special Purpose Vehicle

In practice, the private sector partner of a PPP is a SPV – a separate legal entity established specifically for the delivery of the project (also referred to as the Contractor). The SPV is capitalised on a non-recourse basis, meaning that Debt Providers of the SPV can only be repaid from the project cashflows, rather than any other source (i.e. such as the broader assets of the Equity Providers). In NZ PPPs, the SPV has typically passed the majority of its risks and obligations under the SFA down to its major sub-contractors. The consortium that delivers a PPP therefore typically involves:

- **Equity Providers:** provide capital to the project through a shareholding in the SPV,
- **Debt Providers:** provide the remaining capital through a loan agreement with the SPV,
- **D&C major sub-contractor**: enters into a sub-contract with the SPV to undertake the physical works of the project. In some cases, the major sub-contractor may further sub-contract a portion of its responsibilities to another party or parties,
- **AMM major sub-contractor:** enters into a sub-contract with the SPV to undertake asset and facilities management (e.g. repairs and maintenance) during the term of the contract following completion of construction, and
- **Services major sub-contractor:** enters into a sub-contract with the SPV to operate the asset following completion of construction (DBFMO projects only). In some cases, the Services and AMM major sub-contractors are the same entity.

The SPV is intended to provide a single point of contact for the Procuring Entity and is responsible under the PA for the delivery of the contracted outcomes.

Figure 7: Typical commercial structure of a PPP



7.2 Consortia formation and dynamics

The formation of consortia to bid for a PPP project can begin prior to the initial formal market engagement[34], in particular where there may only be a limited number of specialist providers in the market for some aspects of the project or where the project has been well signalled to the market in advance. This highlights both the value of communication to market about the upcoming pipeline and the need for early market research prior to market engagement to design the procurement in a way that maximises potential competition. One of the benefits of the Model is the involvement of overseas parties in consortia that may result in bringing new participants to the NZ market.

There were a number of comments from interviewees on the intra-consortia dynamics between different parties during the procurement phase. These include:

- The role and style of the financial advisors on a project can significantly impact on the interactions between the other consortium members. In particular, it was commented that financial advisors are incentivised to achieve a success fee from a successful bid, and therefore, in some cases, may be less concerned by the risk allocation that other consortia members are accepting,
- Related to the above point, a potential consequence of this is that the D&C major sub-contractors may not always get a sufficient 'voice at the table' during the procurement phase, despite bearing a significant portion of the project risk, and
- Some interviewees also observed that the D&C major sub-contractor has tended to exert a stronger influence in the consortia over negotiations and design of the asset, rather than the AMM major sub-contractor, who is required to maintain the asset and meet the requirements of the performance regime for the bulk of the term of the PA.

Procuring Entities commented that it is essential that the Services and/or AMM major sub-contractor are significantly involved in design development to ensure that the asset will meet the requirements of the performance regime, and that innovations and potential cost savings are identified. It is important that Procuring Entities are aware of the potential dynamics within an SPV and use their influence to ensure that all members of the consortia are fully engaged at each stage of the process.

Proposed Action: The Commission should consider amending guidance for Procuring Entities on how they can ensure that the major Services and/or Asset Management and Maintenance sub-contractor are involved in design and in key interactive and negotiation sessions.

7.3 Special Purpose Vehicle resourcing and capability

Public sector interviewees commented that SPVs appear not to be sufficiently resourced to perform their intended functions. This is echoed in feedback shared at fora involving public sector contract managers from overseas jurisdictions. Rather than actively managing the project and major sub-contractors, these SPVs had been passing issues through to the Procuring Entity to manage. These so-called 'post-box' SPVs were singled out as points of weakness to be avoided, with the advice being that SPVs need to be sufficiently resourced.

[34] The Commission has published guidance on Market Engagement, which must be complied with under Rule 64 of the Government's Procurement Rules 4th Edition.

In practice, there are a range of issues that can limit an SPV's performance in actively managing the project:

- The majority of Equity Providers (the SPV owners) are often financial parties who do not have specific technical expertise in the delivery fields (e.g. construction, operation, maintenance), although some minority Industrial Equity Providers have been related to the delivery parties (see discussion in section 7.4). This means the SPV does not necessarily have sufficient in-house capability to manage a complex project delivery. In many cases, the SPV board members, and in particular, the representatives of the majority Equity Providers who are ultimately responsible for the project outcomes, do not have technical delivery expertise,

- An SPV is constituted solely for the purposes of the project (by definition, it is specially for that purpose). The boundaries of the SPV's financial resources are defined and limited by the project. In the ordinary course of business, the SPV may not have reach-back to a parent or wider balance sheet for additional resources if the need arises during delivery,

- The PPP contractual framework is such that Procuring Entities will review the agreements between the SPV and the major sub-contractors to ensure the SPV has adequately transferred risks down to its major sub-contractors., The transfer of many of the SPV's obligations to its major sub-contractors is an inherent part of the Model. Afterall, the major sub-contractors are resourced to understand and manage delivery issues. This may lead to a tendency to rely on the major sub-contractors for day to day management and interaction with the Procuring Entity, rather than set aside resources for this itself,

- The competitive procurement process incentivises bidders to minimise overall costs in their offer, which can consequently put limits on the SPV financial resources. The limited resources mean the SPV may only become actively involved when its equity is at risk, which is typically when issues have reached such a serious level that the project may be at risk of failing, and

- PPP procurements tend not to specify the resource requirements for the SPV, assuming that the incentives within the Model will lead the SPV to determine its own requirements for managing its obligations, including ensuring major sub-contractor delivery and risk management. The exception is the Pūhoi to Warkworth project where, based on lessons from the Transmission Gully project, Waka Kotahi specified SPV resource requirements, which it expected would be included in the offer price and maintained throughout the contract term.

The interviews provided a mixed picture on the role of the SPVs in NZ projects to date. Some interviewees commented that they believed SPVs do not actively manage their major sub-contractors, even though they receive a management fee for doing so. Given this, some Procuring Entities have needed to form direct relationships with the major sub-contractor to a greater extent than originally envisaged. The SPV can act as a filter or barrier that provides limited value, especially when solutions needed to be developed. Interviewees stated that this approach meant it was challenging to form close trusting relationships and offered less transparency than in other procurement models. Some interviewees also stated that SPVs have not operated in a collaborative fashion and have been too focused on their relationships with financiers, rather than with the Procuring Entity.

In contrast, the perspective of some private sector interviewees is that Procuring Entities have only paid for thinly resourced SPVs and it was not realistic or efficient for the SPV to duplicate capability that sits within the major sub-contractors. The risk to Procuring Entities from relatively thin SPVs is that additional resources are expended by Procuring Entities to undertake major sub-contractor management and engagement that should be done by the SPV.

Proposed Action: The Commission should develop guidance for Procuring Entities on the recommended requirements for the structure and resourcing of the Special Purpose Vehicle, including drawing on lessons from existing projects.

Event claims pass through

A number of interviewees expressed the view that SPVs have in instances passed on 'flimsy' claims of Events[35] to the Procuring Entity to manage rather than managing them itself. At least one PPP project requires the SPV to pass on all sub-contractor claims, regardless of merit. One potential mechanism to address this risk would be for the SFA to impose an obligation on the Contractor to ensure any claims have some degree of merit or are not frivolous. Some of the later PAs contain a requirement that the Contractor evaluate the factual, technical and legal merits of any claims from sub-contractors to determine whether there are reasonable grounds under the PA before passing the claim to the Procuring Entity and provide a director's certificate that it has done so to accompany the claim. The Commission also understands such an obligation has been included in some PPP projects in Australia and tied to the default provisions, such that a breach of the obligation leads to notification to Equity and Debt Providers.

Proposed Action: The Commission should consider amending the Standard Form (PPP) Project Agreement to include an obligation for the Contractor to evaluate whether pass through claims from sub-contractors have merit before sending these to the Procuring Entity.

7.4 Role of Industrial Equity

Industrial Equity refers to project equity provided by a major sub-contractor or related party (i.e. within the Group) on the same project. Where this has been proposed by bidders, Industrial Equity has often been a minority equity holder only. In theory, the presence of Industrial Equity in the SPV raises the risk that the SPV will to some extent be conflicted in its interactions with the related major sub-contractor, and therefore less likely to act in the best interests of the Procuring Entity. Potentially with greater 'inside knowledge' of the project than other members of the SPV governance, this potential conflict could manifest itself through Industrial Equity participating in the governance of the SPV in a way that prevents it from taking action against the major sub-contractor for performance issues. This could, for example, be achieved through a shareholding and governance structure that allowed the Industrial Equity to veto actions against the relevant major sub-contractor.

On the other hand, some interviewees argued that the potential conflict of interest had not manifested itself in practice to date and that there were offsetting benefits to the project from the presence of Industrial Equity. In particular, that Industrial Equity created greater alignment between parties within the consortium, which was particularly beneficial to a project in distress. Further, the information advantage could benefit the project as the Industrial Equity party had a greater understanding of what was happening on the ground.

While the Commission has not considered the role of Industrial Equity in depth as part of this Review, it has observed examples where Industrial Equity has played a more active role in formulating 'best for project' solutions than institutional forms of equity. A future position on the role of Industrial Equity may also need to consider differences between D&C Industrial Equity and AMM Industrial Equity. Arguably,

[35] Event is defined in the SFA and refers to, amongst other things, an event that may give rise to time extensions or compensation.

there may be a clearer case for the industrial equity from an AMM major sub-contractor given it does not face a conflict during the Construction Period and its interests are more directly aligned with the outcomes of the project.

Proposed Action: The Commission should consider its position regarding Industrial Equity, the level of voting rights and conflict management requirements of major sub-contractors in a Special Purpose Vehicle.

8 Review Procedures

8.1 Review Procedure

The Model has been designed so that the Contractor bears the risk of designing the asset to meet the requirements set out in the PA when it is built. The Procuring Entity is able to influence the design during the procurement process through the specifications it prepares for the RFP and the positions negotiated with the PB that are incorporated in the PA (through the Works Requirements and Service Requirements).

As discussed in section 5.2, the level of design required from bidders has differed across the projects, with bidders not typically required to submit fully detailed designs at RFP stage. Given this, the PB undertakes further design work during the PB stage and after FC. Once the PA has been executed, the Procuring Entity has only limited grounds on which it can review and "comment" on designs. Interviewees suggested that the design review process is not always well understood by either the Procuring Entity or Contractor.

Treatment of review comments

The Review Procedure, covering both the design and operative documents, set out in Schedule 8 to the SFA, allows the Procuring Entity to review design material and either respond with "comments" on specified grounds or "no comments". If the Procuring Entity responds "no comments" or fails to respond within specified timeframes, the design material is finalised, and the Contractor can act on that design material at its own cost and risk.

There was a reported tendency of Contractors in some projects to interpret the Crown's "no comments" response, or failure to comment, as "endorsement or approval" of the design. This suggests a lack of understanding of the risk allocation in the PA (and a tendency to default to positions in other standard form construction contracts). There is clear wording in Schedule 8 of the SFA that the Procuring Entity's comments, or failure to comment, are not a representation that the design material complies with the PA and do not relieve the Contractor from its obligations.

Where comments have been provided, some private sector interviewees considered that in some cases these were in fact changes to the Works Requirements or Services Requirements and should have been addressed through the Change mechanism. Under such circumstances, the Contractor is required to notify the Procuring Entity before complying with the comments and if it does not do so, this constitutes an irrevocable acceptance that compliance with the comments is without cost to the Crown or extension of time[36]. Given this, interview feedback that the cost of implementing comments should have been treated as a Change suggests lack of understanding as to the risk allocation and respective responsibilities of parties under the design review process.

Review process and timeframes

Some private sector interviewees commented that the design review process took longer, and designs and documents went through more review cycles, than expected. Procuring Entity interviewees commented that, even though bidders were notified in the RFP that the design review process would be robust, Contractors did not allow sufficient time in their programmes for multiple cycles of review.

Such design development and review processes are not specific to PPP projects, but the confidence and ability of the Contractor to manage design risk is brought into stark focus in a PPP. As discussed earlier, if

[36] SFA 27.1(f) and Schedule 8.

the design specification and level of design required for the bid is insufficient to give comfort, attention turns to the Procuring Entity's endorsement and approval of design prior to FC. Some interviewees suggested that it was only as they entered the PB stage that they realised the implications of design risk allocation and that, unlike for other procurement models, there would no opportunity for design correction and variation post FC involving further payment by the Procuring Entity.

Most projects commenced the Review Procedure prior to FC, adopting the same timeframes as envisaged under the SFA. The parties agree a Pre-FC Review Procedure including details of Reviewable Design Material[37] and dates for design package submission. Determination of the design packages for submission pre-FC is entirely up to the Contractor in accordance with its design development schedule. Submission pre-FC will depend on the Contractor's approach to managing design risk and the Procuring Entity must be prepared to provide the resource necessary to carry out timely review.

This can place the D&C major sub-contractor's design team under immense pressure to deliver by FC, particularly where there is a desire for a shortened PB stage. In this haste, Procuring Entities often observe errors and inconsistencies or lack of information to support the design, which can stress the process and result in multiple review cycles. While the major sub-contractor is highly incentivised to obtain as much certainty pre-FC as possible, the Procuring Entity is less incentivised, given that its requirements are met via the Works Requirements and Service Requirements. To assist the process, however, Procuring Entities have often included additional informal design engagement between the parties, ensuring that once a design is submitted under the Review Procedure it is more likely to meet the review timeframes and provide confidence.

Proposed Actions: The Commission should develop guidance on opportunities for both Procuring Entities and Contractors to improve the design review process, including informal engagement. This relates also to consideration of the level of design specification and design requirements for bid submission and ensuring that the major Design and Construction sub-contractor forming part of bid consortia is well aware of the fixed price nature of the PPP model and the limited opportunity for variation post Contractual Close.

8.2 Role of the Independent Reviewer

The Independent Reviewer is jointly engaged by both the Crown and the Contractor under a tripartite Independent Reviewer Agreement. The role of the Independent Reviewer in the Model is to act as an impartial independent assessor for the benefit of both the Crown and Contractor. Its key functions under the PA are:

- monitoring the progress of construction against the programme,
- observing works completions tests and issuing the Works Completion Certificate,
- determining the length of any extensions of time for Events, and
- apportioning the delay and change in costs where there are multiple causes of a claim.

The feedback from interviewees is that the Independent Reviewer role has generally functioned well across the projects to date. There were some suggestions that the Independent Reviewer should have a

[37] Includes design drawings, as well as, for example, numerous design reports, data sheets, environmental and construction management plans.

broader role, such as acting as an independent expert to resolve minor issues (e.g. ambiguity in the Works Requirements, similar to the Engineer to the Contract role under the NZS Conditions of Contract). Further, it was suggested by some interviewees that the Independent Reviewer should participate in the design review process (in place of the Crown).

Case study: Independent Certifiers in Australia

The Independent Reviewer role is similar to the role of an Independent Certifier (or Independent Verifier) in Australia. A key difference is that the role of the Independent Certifier in Australia often includes certifying that the design (as well as the construction) is in accordance with the requirements of the contract. Generally the Independent Certifier undertakes independent certification of design at four key stages of the design process (30%, 70%, issued for construction and as-builts after construction) based on evidence provided by the Contractor, which they can rely on - they do not conduct first principles design reviews.[38] Often comments from the Procuring Entity and third-party stakeholders are funnelled through the Independent Certifier, who reviews and consolidates comments to the Contractor. This can raise issues if stakeholders are slow to provide comments, but it is also seen as a way of protecting the Contractor from 'preferential engineering'[39]. Independent certification is separate to the procuring entity's engineering management, design review and assurance processes.

An advantage of engaging the Independent Reviewer to undertake design review, instead of the Procuring Entity, is that the Independent Reviewer may curate comments to ensure only those on permitted grounds are given to the Contractor and to assist in identifying potential Changes early. However, this is likely to have a cost impact on PPP projects and potentially also a time impact. Another potential advantage is that those involved in the design review process are then well informed to conduct the Independent Reviewer activities during construction. There are also other ways assurance on design could be increased in NZ, such as by requiring the Contractor to engage its own design reviewer or imposing assurance requirements similar to those set out in Waka Kotahi's Highway Structures Design Guide.

The Commission considers that the Independent Reviewer should have the opportunity to review the Works Completion Tests prior to finalisation in the PA. Some, but not all, of the Independent Reviewer Agreements expressly require the Independent Reviewer to review and comment on the Contractor's Works Completion Plans.

Independent Reviewers interviewed commented that, in some cases, parties have attempted to refer disputes to the Independent Reviewer rather than to the dispute resolution procedures under the PA. The SFA includes an Accelerated Dispute Resolution process under which disputes should be progressed, although the Independent Reviewer may participate in these as a technical expert. The Commission does not consider it necessary to expand the scope of the Independent Reviewer to dispute resolution.

Proposed Action: The Commission should consider amending the SFA to include review and comment on the Works Completion Plans in the Independent Reviewer's scope.

[38] See for example the Sydney Metro City & Southwest Independent Certification of the Line-wide Works Independent Certifier Deed available here (although this did not relate to a PPP contract).

[39] Preferential engineering refers to changes requested by a client/stakeholder to the designs of a project that are outside the content of the contract.

9 Change mechanism and Fitness for Intended Purposes

9.1 Change mechanism

The Change mechanism within the SFA sets out the approach that the Contractor and Procuring Entity must follow to initiate and respond to a Change Notice. A Change Notice can be initiated by either the Crown or the Contractor and can include any changes to the PA or to the nature of the asset (such as an expansion) or the services.

As of mid-2019, there had been 474 Change Notices across all the projects. Of these, 81% were initiated during the Construction Period, and 47% were issued by the Contractor. For one project, the high number of Change Notices initiated by the Contractor was due to the need for amendments to detailed design drawings to be considered as Changes given the level of design appended to the PA in response to the Works Requirements. These were largely treated as Non-Material Changes.

Change Notices and incentives for innovation

Incentivising innovation is one of the key objectives of the Model. However, the fixed term, fixed price nature of the SFA means that Contractor innovations are generally concentrated in the RFP and the PB stages. Interviewees commented that the Change mechanism in the SFA does not incentivise the Contractor to identify innovation or savings post FC.

On the one hand, it could be argued that where a Change results in a reduction in the UC, the Crown is entitled to receive the full benefit. On the other hand, it could be argued that if the Contractor, through an innovation, can deliver the same outcomes for a lower cost than originally anticipated (and which the Crown considered value for money relative to conventional procurement approaches), then it should be entitled to some of that benefit. While there is a risk that this could lead to a perverse incentive for Contractors to hold back suggestions for innovation until after FC so as to receive a share in the savings, the high stakes competitive nature of the RFP stage and a focus on innovation in the evaluation criteria should mitigate this risk.

Anecdotally, the Commission understands that some projects have been utilising an informal process of keeping a running account of cost increases and reductions and balancing these out, rather than making changes to the UC every time there is a Change. Some projects have also informally allowed the Contractor to keep the benefit of Changes that have resulted in savings, on the basis that the Procuring Entity has received the benefit of the innovation in service improvements.

While recognising that the SFA should be amended to incentivise innovation, the Commission also notes that a number of interviewees commented that AMM major sub-contractors have not always been substantially involved in the negotiation of the PA or the design of the asset. This can represent a missed opportunity to identify design and construction choices that might lead to savings or efficiencies in the operation and maintenance of the asset. This further emphasises the need for the AMM major sub-contractor to be involved in the design process (see earlier recommendation).

Implementation issues with the Change mechanism

In addition to the comments on innovation and savings discussed above, comments from interviewees on the Change mechanism included that the mechanism itself is complex to understand, that the mechanism was more suited for the Construction Period rather than Operating Period and that there was a lack of clarity on how Change in Costs should be calculated relative to the Base Case Financial Model.

The SFA distinguishes between Material Changes and Non-Material Changes. A Non-Material Change is typically defined as one that does not result in a change to the UC, does not change the risk to the Crown and does not increase the likelihood of the Contractor not meeting its obligations. The timeframes and information requirement for a Non-Material Change are less onerous than a Material Change. There is variation across the different PAs as to whether Non-Material Changes can, by definition, only occur after Service Commencement. In some projects, Change during the Construction Period can also be classified as Non-Material. This may have arisen due to the extent of design appended to some PAs and concern (on the part of the Contractor) that relatively straightforward amendments to design drawings would be captured by the Change regime rather than as progression of design captured by the Review Procedure. Some Contractors likely sought to reduce their exposure to design risk by obtaining some level of endorsement from Procuring Entities prior to contract and then by binding the parties to such endorsement through appending documentation, even where the PA makes it clear that the Contractor meeting its Delivery Proposals (and appended drawings) does not relieve it of its obligations to deliver on the Works Requirements.

A later schools PPP project included provisions within the PA for expansion of the facilities and services to accommodate roll growth. In practice, implementation of the expansion provisions has required the Crown and the Contractor to re-interpret the Change mechanism. Commentators in the Australian market have highlighted similar difficulties in extending rail transport networks, originally procured and being managed under a PPP contract.[40]

In addition, feedback from interviewees is that both Procuring Entities and Contractors struggle to respond in the timeframes specified in the SFA and so the timeframes are effectively ignored by both parties.

Proposed Action: The Commission should consider options for improving incentives for innovation by the Contractor post Contractual Close including, but not limited to, potential amendments to the Change mechanism.

Proposed Action: The Commission should review the Change mechanism in the Standard Form (PPP) Project Agreement to consider and improve ease of practical implementation.

9.2 Fit for the Intended Purposes requirement

The Contractor's obligation under the SFA requires it to ensure the asset is and remains Fit for the Intended Purposes. This is effectively a 'catch-all' provision and only applies to the extent it would not impose more stringent or additional standards than those set out in the Service Requirements and other specified documents. This is an enduring requirement for the contract term.

The definition of "Fit for the Intended Purposes" in the SFA essentially requires that the asset:

- meet the Works Requirements,
- be capable of enabling the Contractor to provide the Services in accordance with the Service Requirements, the performance regime and so that availability can be achieved, and

[40] https://www.dlapiper.com/en/australia/insights/publications/2020/02/flexing-ppps/

- be capable of enabling the Crown to provide the retained services (e.g. provide education at a school) in a safe, efficient and effective manner.

It is important that the purpose of the Fit for the Intended Purposes requirement is considered in light of the breach, performance and defects regimes, and some interviewees commented that there is ambiguity in how these concepts work together.

The provisions of the PA state that from Service Commencement, the Contractor must ensure that the asset is available (captured under the performance regime) and that it carries out the services in accordance with the Service Requirements and various asset management and maintenance plans (aspects also captured under the performance regime) so as to ensure that the facility is and remains Fit for Intended Purposes.

From Service Commencement, the failure to remedy issues should, for the most part, be dealt with in accordance with the performance regime. The Fit for Intended Purposes requirement is more closely linked to the defects' regime. Clearly if there are defects in the asset that mean it does not meet the Works Requirements and Service Requirements, for which a remedy is not available under the performance regime, and/or the Crown cannot operate the asset safely, then it is potentially not fit for its intended purpose. The Contractor would in such circumstances be in breach of the PA and the Crown would need to rely on the Fit for Intended Purposes provision.

A number of PAs have varied the Fit for the Intended Purposes requirement from the SFA during negotiation. In some cases, the issue of the Works Completion Certificate is conclusive evidence that the asset was Fit for the Intended Purposes as at the Works Completion Date. This relies on the performance regime providing a remedy for any defect arising subsequent to the Works Completion Date, by either making the area of the asset affected by the defect unavailable, or by raising a maintenance request and requiring timely response to fixing the defect. Where a remedy is not available under the performance regime, failure to meet the Works Requirements and Service Requirements could still constitute a breach. The Contractor is also highly incentivised to address any issues that affect the efficiency and effectiveness of its Services, e.g. by increasing its AMM costs through more frequent maintenance or lifecycle replacements.

There are also differences in the requirement that the asset enables the Crown to provide services in a safe, efficient and effective manner. In some cases, this has been limited to only those services as they are, or anticipated to be, at Service Commencement. Some interviewees commented that there have been issues on projects where the operation by end users of the asset has evolved over time, resulting in disagreement as to whether the asset still met the Fit for the Intended Purposes requirement. Some private sector interviewees identified examples where they had been asked to rectify 'defects' to ensure the asset remained Fit for the Intended Purposes that should actually have been classified as a Change arising from a change in use. Clearly, it was no envisaged that a change in use of the asset would be captured by the Fit for the Intended Purposes provisions.

Proposed Action: The Commission should consider amending the Standard Form (PPP) Project Agreement regarding the Fit for the Intended Purpose definition to standardise the various positions negotiated across the different projects and provide further detail on the requirement in any contract management guidance.

10 Performance regimes and the management of disputes and breaches

10.1 Introduction to PPP performance regimes

A key feature of the Model is the inclusion of a performance regime to provide incentives for the Contractor to meet specified KPIs and other performance outcomes, consistent with the 'payment for performance' concept upon which the Model is based. Performance regimes are based on financial penalties (abatements) and non-financial penalties that the Contractor can incur where the specified KPIs are not met. These are typically:

- **Availability KPIs,** which require that the specified areas of the asset are 'available' for use by the end user of the asset at specified times in the day in a specified condition (e.g. classrooms during a school week). If the area does not meet the standard required to be deemed 'available', the Contractor is subject to penalty under the performance regime. In some projects, there is a Rectification Period that allows the Contractor to remedy the issue within a specified timeframe without penalty.
- **Performance KPIs,** where a specified level of performance must be achieved, such as relating to traffic movement, user satisfaction or reporting accuracy.
- **Charge Events,** where the Contractor is financially penalised for the occurrence (under specified circumstances) of specified events, such as prisoner escapes or road fatalities.
- **Service Failure Points (non-financial),** which the Contractor can accrue (in addition to financial penalties) under the performance regime, which can lead to greater monitoring and, at the extreme, step-in by the Crown.

Case study: ASCF's incentive payment regime

ASCF is the only vertical project in the Portfolio where the Contractor is responsible for the day to day operations of the asset. It is also the only performance regime that provides the opportunity for the Contractor to receive Incentive Payments for exceeding a performance target in a specific area – reimprisonment.

Under the ASCF regime, the Contractor is entitled to an Incentive Payment where the rate of reimprisonment for prisoners released from ASCF is 10% lower than that for similar prisoners released from NZ prisons. A separate payment is also available for achieving a similar objective focused exclusively on Māori prisoners. To qualify for this payment, the Contractor must also have not accrued Service Failure Points beyond a specified level in the same period.

Across the Portfolio, there are 329 KPIs, of which three projects account for approximately 70%. In general, a project with a higher number of KPIs reflects a more outputs-focused approach, while a regime based on fewer KPIs typically reflects a more outcomes-focused approached. An approach based on fewer KPIs can, in some cases, be challenging if the Procuring Entity has not traditionally considered performance on an outcomes basis.

There are five PPP projects in the Operating Period where there is experience as to how the performance regimes are operating in practice. At the time of this Review, there was still relatively limited evidence on the specific impact that the performance regime has had on behaviour and whether it is creating the intended outcomes.

10.2 Design and administration of performance regimes

Design of performance regimes

A number of interviewees commented that performance regimes were overly complicated and esoteric. There was also the view that the number of KPIs made regimes difficult to administer, and that future projects should have fewer but more significant KPIs. There were also comments on aspects of the performance regime for particular projects being unworkable or including contradictory/undesirable incentives (such as the Contractor focusing on limiting abatements rather than overall service delivery). Interviewees also commented that they considered that some components within performance regimes are calibrated such that financial penalties are disproportionate to the impact of the failure. The calibration of the performance regime, including how it relates to the breach regime, is discussed further below in section 10.3.

The role of advisors to Procuring Entities in the designing and calibrating of such regimes was also noted, including that some advisors did not have experience in administering the performance regimes being designed.

Administration of performance regimes

In practice, the administration of currently operational performance regimes is typically managed through a combination of self-reporting by the SPV and the operation of a helpdesk where performance failures are formally reported. The Contractor is also typically required to report periodically and accurately to the Procuring Entity on performance against the performance regime. Failure to do so can itself incur a financial penalty under the regime.

Some interviewees commented that Procuring Entities have not enforced performance regimes to the extent envisaged in the PA. This was ascribed to a number of potential causes, including the regime being too administratively burdensome or that the contract management approach between the parties was for issues to not be formally dealt with through the regime. In some cases, it was considered faster and simpler to resolve issues outside of the formal reporting mechanisms, especially if on-site staff had been experienced in working on other sites that did not require formal reporting through a helpdesk. This approach can create risk for the Procuring Entity if issues are not logged, particularly if the issue is not rectified and no performance abatement can therefore be applied.

The complexity of the design of the performance regimes can also impact how the regime is administered. As stated by some interviewees, the challenge is designing a KPI regime to ensure that the right incentives are achieved, but that it is not overly complex to operate during the Operating Period. In practice, this can be supported by the development of a tool (such as a database or spreadsheet model) that formulaically and consistently calculates performance against the regime from operational data.

Proposed Action: Procuring Entities should ensure that the design of performance regimes is aligned with desired outcomes and incentives and takes account of what would be required to implement the regime in practice.

10.3 General Breaches

Under the SFA, the Crown may issue a Notice of General Breach to the Contractor for any failure to comply with its obligations, except for failures that give rise to remedies under the performance regime (i.e. the same issue should not be captured under both). If there are a number of un-remedied or remedied General Breaches in a specified period (usually 12 months), then this becomes a Persistent General

Breach. The number of General Breaches required to trigger a Persistent General Breach differs across each of the projects.

A Persistent General Breach entitles the Crown to issue a Warning Notice, in response to which the Contractor must propose and implement a rectification programme (for remediable breaches) or a prevention plan (for non-remediable breaches) within specified timeframes. If the Contractor does not do so, then the Crown is entitled to terminate the PA.

Implementation of the General Breach regime

There were some comments from interviewees that the definition of General Breach is too broad, and it should only refer to serious breaches. There is a risk to Contractors that the Crown has a right to terminate the PA where it has issued a series of General Breach Notices for relatively minor technical breaches (that have not been remedied by the Contractor). For example, it is theoretically possible, that where the Contractor repeatedly fails to comply with procedural requirements, such as providing certain information or responding in certain timeframes, and does not remedy the failure, a Termination Event could be triggered. However, it is very unlikely to be a desirable outcome for the Crown to terminate the PA for a series of minor breaches, or to have a major sub-contractor terminated.

There are considerable resources consumed by both the Crown and the Contractor to issue a Notice of General Breach, respond to it, and determine and notify the Crown whether the breach has been remedied. Interviewees noted that the issue of a General Breach Notice is taken very seriously by a Contractor and usually requires them to notify their Debt Providers, which may result in a higher level of monitoring and reporting. The Persistent General Breach threshold (number) that is included in a sub-contract might also be lower than the PA to provide the Contractor a buffer from a sub-contractor's Persistent General Breach. Debt Providers may require those sub-contracts to be terminated if this lower threshold is reached.

It is important that Procuring Entities manage and enforce their rights under the PA to preserve the value of that agreement. An underlying issue identified by Procuring Entities is that for breaches that do not give rise to remedies under the performance regime, General Breach Notices are one of the few tools available to address the Contractor's failure to meet its obligations. In particular, the SFA does not specifically include KPIs in the performance regime to apply during the Construction Phase[41]. This is consistent with standard construction industry contracts, which do not generally include a performance regime for construction. The key incentive in the Model is the Planned Service Commencement Date, by when the Contractor must achieve completion or be subject to liquidated damages charged by the Crown and the Debt Provider.

The comments from interviewees highlight the importance of the calibration of the breach and performance regimes and how these regimes need to work together during different phases of the project. For example, a succession of relatively minor General Breaches (even if remedied) could theoretically lead to a Persistent General Breach more easily than significant underperformance under the performance regime. There is an argument that a different calibration of the breach regime could apply during the Construction Period and/or a wider set of tools be made available to the Crown to manage performance issues during this period.

The Commission is aware that Procuring Entities have in limited cases, where appropriate in the context of the breach and the overall pattern of the Contractor's behaviour, issued non-contractual grace letters

[41] In some of the PPP projects, the PA includes some performance indicators during construction, for example, in relation to compliance with Consent Conditions, environment and heritage protection legislation and reporting.

rather than Notices of General Breach to provide Contractors with an opportunity to remedy breaches. There are breaches for which it would never be appropriate to issue grace letters, such as health and safety breaches or repeated breaches of the same or similar obligations. Given the consequences of un-remedied breaches, it is also important that the Procuring Entities monitor the Contractor's remediation of a breach and notify the Contractor when the Crown considers the breach has been remedied.

Proposed Action: Procuring Entities should ensure that the calibration of the breach regime achieves the desired incentives during both the Construction and Operations Periods.

Proposed Action: The Commission should develop guidance on issuing Notices of General Breaches, including on managing instances of minor non-compliances.

10.4 Time Bars and dispute resolution

The Events regime entitles the Contractor to extra time, relief from the performance regime and in some cases additional costs where specified events occur. However, if the Contractor provides late notice of an Event, any relief is at the absolute discretion of the Crown. These time restrictions are referred to as time bars. The time bars in the SFA are for the Contractor to provide:

- a first notice within 5 Business Days on becoming aware an Event is likely to adversely impact the Contractor, and
- a second notice within 15 Business Days after becoming aware of the Event, which must demonstrate a number of matters to the satisfaction of the Crown, including if the Contractor is entitled to additional costs, the estimated costs and how they will be calculated.

Interviewees suggested that the time bars for relief under the Events regime are too strict, and it is unreasonable to expect the Contractor to provide the required amount of information to make a claim within the specified timeframe. In the context of Events during the Construction Period, 15 Business Days is a relatively short period to provide the level of detail requested, compared to other standard construction contracts. For example, the standard NZS Conditions of Contract generally require notice within one month of an event. The Red Book issued by the International Federation of Consulting Engineers (FIDIC), a standards organisation for engineering and consulting, does include time bars for claims for extensions of time or additional costs, but provides a period of 28 days for the contractor to provide the initial notice and 42 days to submit a full claim.

From the Crown's perspective, a time bar on claims is important to provide certainty that extension of time or costs claims will not be raised in perpetuity. There is also a risk that the more time that passes from an Event the more difficult for both parties to obtain and evaluate accurate information about the Event and its impact.

Proposed Action: The Commission should consider whether the Standard Form (PPP) Project Agreement should be amended to provide more flexible time bars.

11 Contract management

11.1 Capacity and experience

Unlike more traditional forms of procurement where the primary contract is with a build only or D&C contractor for the duration of the construction (and a defined period thereafter), PPP's are long-term contracts for a period of 25 years or more. Given this, many interviewees commented on the importance of ongoing robust contract management by Procuring Entities to achieve the promised benefits of the Model. The Review did not compare the resources required for PPP contract management with resources required to directly manage non-PPP design and build projects or the ongoing resources required to manage operational assets (e.g. asset lifecycle reactive and planned maintenance). Within the Procuring Entities, the team managing the PPP contract tends to be quite distinct from the team managing other assets.

During the Construction Period, the role of the PPP contract management team is primarily to protect the Crown's agreed contractual and risk positions, including monitoring delivery timeframes and Contractor initiated Change requests. During the Operating Period, the contract management team must maintain the ongoing relationship with the Contractor (including stakeholders such as the end users of the asset), monitor the performance under the performance regime, managing any further Change Requests, and other events that can occur during the Contract Period (e.g. refinancing or equity sales). The complexity of PPP contract management and the significant contract management resource required, relative to other contract forms, was mentioned by many interviewees.

Many interviewees considered that there is variable understanding and expertise in contract management on both sides, and some inconsistency in how PPP contracts are managed (including across multiple contracts within the same Procuring Entity). Many interviewees commented on the challenges faced from a lack of continuity of personnel on both the Crown and the private sector sides between the procurement phase, Construction Period and operations' phase. While procurement phase teams on both sides often have previous PPP experience, either in NZ or internationally, it was commented that there was less depth of experience with construction and operations' teams on both sides. It was suggested that embedding the intended contract management and delivery staff in the project team during the RFP stage, rather than bringing them in at FC, would support contract managers to have a stronger understanding of the eventual contract.

There was concern from some interviewees that relative inexperience with the Model creates additional contract management issues and potentially dilutes the benefits of the Model. For example, a tendency in some cases to seek rectification of issues under the Defects' provisions, rather than under the performance regime, or for the performance regime to not be strictly adhered to. There was also a potential tendency to assume negotiating positions under standard industry sector contracts which do not apply in the SFA.

This contract management issue was also addressed in the Transmission Gully PPP – Lessons Learnt Review. That report noted that the Project Manager was a contractor who had previous PPP experience, which was beneficial to the project, but that Waka Kotahi could have done more to ensure the PPP expertise was transferred to Waka Kotahi, as their contract ended after FC. That report referred to a number of steps Waka Kotahi could take to ensure expertise is retained for future projects, including:

- having junior agency staff in project administration roles,
- having senior agency staff working alongside contractors and advisors, and

- greater involvement of governance in key decisions[42].

These measures would be beneficial for all Procuring Entities to adopt.

11.2 Training and formal processes

A lack of guidance and formal training available for agencies was mentioned by many interviewees. Unlike other aspects of the PPP programme, where more detailed documentation has been issued (e.g. PSC quantitative analysis, SFA), only relatively limited guidance has been developed on contract management.

The Australian National PPP Policy and Guidelines provides a high-level description of the key elements of effective PPP contract management such as adequate resourcing, governance, information collection and relationship management. However, a key recommendation is that a detailed contract administration manual is developed that sets out key steps and requirements for effective management of the project and acts as the central source for all relevant information.

While it would not be appropriate for the Crown to produce contract management guidance for private sector participants, the capacity and understanding from private sector participants would also be improved through the publication of the guidance as these would provide standardised information on the intent of how and why the SFA is designed to work as it does.

The Commission has instigated more regular meetings of the PPP Contract Managers Forum for Crown PPP contract managers to promote sharing of experiences and best practice in managing PPPs. Through this Forum, the Commission has identified a few common issues arising for contract managers on which guidance would be beneficial.

Proposed Action: The Commission should develop and publish a contract management guidance for Procuring Entities in relation to the Standard Form (PPP) Project Agreement. This could include recommended strategies to manage handovers between phases and departures of key personnel, such as joint workshops with both the Procuring Entity and SPV personnel.

[42] https://www.nzta.govt.nz/assets/projects/transmission-gully/docs/transmission-gully-ppp-lessons-learnt-review-dec-2014.pdf, section 3.4.

12 Refinancing and Change of Ownership during the contract term

12.1 Refinancing

The financing structure for a PPP is a combination of debt and equity, which provides the necessary capital for the construction of the asset. The debt is provided by agreement between the Contractor and the Debt Provider, with the interest rate being composed of a base floating interest rate plus a credit margin to reflect the relative risk of the project.

A key aspect of the financing structure for a PPP is that the Procuring Entity is protected from market movements in the base interest rate over the contract term. The mechanism by which this is achieved has varied across the projects, but more recent projects achieve this through an initial swap arrangement[43] between the Contractor and its Debt Provider, followed by a separate swap arrangement between the Procuring Entity and a Crown Swap Counterparty for the remainder of the contract term. This arrangement was the result of market evidence that there was not a liquid commercial market for long-term interest rate swaps in NZ or other competitive long-term fixed interest rate finance[44].

A refinancing occurs when the Contractor replaces its existing debt arrangements with a new set of arrangements under different terms. This can include changing to a different Debt Provider, changes to tenor or changes to the credit margin. Typically, the Contractor will run a 'debt competition' in order to secure the most favourable terms.

The Contractor must undertake a refinancing in accordance with the terms of the PA, which requires the consent of the Procuring Entity before the Contractor can finalise a refinancing. Procuring Entities have typically engaged commercial and legal advisors to support a refinancing process, including reviewing financial models, supporting any negotiations with the Contractor and ensuring that the refinancing proposal meet the terms of the PA[45].

As part of its Base Case Financial Model, the Contractor includes a set of credit margin assumptions for the duration of the contract term. These assumptions are used as the basis for determining the profile of the UC at FC. Under the SFA, the Contractor solely bears the risk that the credit margin is higher than that modelled at FC. Where the credit terms are better than those modelled at FC, the SFA provides for a 50% Refinancing Gain share each between the Crown and the Contractor.

The experience of interviewees on refinancing's completed to date suggests that these have generally operated well, but that a number of points have required negotiation between the Crown and the Contractor. In particular, this has occurred where detailed practical aspects of the Refinancing Gain calculation were not stipulated in the SFA and therefore required negotiation and agreement between the parties. Further, Procuring Entities have identified potential improvements in the process through having

[43] An interest rate swap is a contract between two parties in which one party agrees to pay the other party a fixed interest rate in exchange for receiving a floating interest rate.

[44] Long-term fixed rate debt is available to PPPs in other countries, particularly in Europe and North America where financial markets are deeper. Some PPP procurement processes have investigated whether such products could be sold into NZ, but this simply shifts the long-term risk from interest rate to foreign exchange risk.

[45] In particular, a refinancing must not materially increase risks to the Crown or be onerous on the Contractor such that may impact its ability to perform its obligations under the PA.

robust project management and encouraging the Contractor to provide advance warning of its intention to refinance to enable processes to be planned.

Given that it is expected that refinancing will occur in each PPP project approximately every five years, the Commission considers that there should be a consolidation of the lessons learnt from previous refinancing processes to improve efficiency and mitigate the risk of inconsistency across projects.

Proposed Action: The Commission should develop guidance for Procuring Entities on undertaking PPP refinancing, and consider other options for sharing refinancing lessons across projects.

12.2 Change of Ownership

A Change of Ownership generally occurs when an Equity Provider sells its equity share in the SPV to another party. The Change of Ownership provisions of the SFA provide that the Crown must determine that there are no grounds (specified in the SFA) for withholding its consent before a Change of Ownership occurs. This requires Procuring Entities to take positive steps to satisfy themselves that none of the specified grounds exists.

Interviewees commented that the Change of Ownership provisions in the SFA create uncertainty in terms of timeframes and information requirements for investors wishing to sell their shares in an SPV. Interviewees commented that, in their view, the Crown has issued lengthy and potentially burdensome requests for information and taken too long to provide consent to Changes of Ownership. Interviewees commented that Procuring Entities may not understand the impact such delays and information requests can have on a commercial sale process.

From the Crown's perspective, the reputational and operational consequences if an unsuitable party obtains ownership in a PPP project will be ultimately borne by the Crown. Accordingly, it is important for Procuring Entities to undertake appropriate and robust due diligence to ensure that none of the specified grounds for refusing consent exist. However, the potential consequences that delays or unnecessarily burdensome information requests may have on a commercial sale process, including affecting the sale price and the transaction costs and time, should not be disregarded as they may affect investors' willingness to invest in future NZ PPP projects or their cost of capital.

Changes of Ownership may occur on all the PPP projects in NZ in the future, particularly as there are several time limited funds who have invested in the PPPs. There is likely to be benefit for agencies in a consistent, streamlined process for considering proposed Changes of Ownership, including guidance on the information that should be sought from the Contractor. A reasonable timeframe for the Crown to either provide or withhold its consent to a proposed Change of Ownership is likely to assist investors who are either selling interests in or considering investing in NZ PPP projects. It would also be consistent with the approach in Australia, which investors are likely to be familiar with, where PPP contracts set out strict timelines for the State to respond to a proposed change of ownership.

Proposed Action: The Commission should develop guidance for Procuring Entities on dealing with Changes of Ownership.

Proposed Action: The Commission should consider amending the Standard Form (PPP) Project Agreement in relation to the specified (reasonable) timeframe within which the Crown must provide or

withhold its consent to a proposed Change of Ownership (subject to the Contractor providing the required information to the Crown).

13 Other amendments to the Standard Form (PPP) Project Agreement

The SFA was last reviewed and amended in 2013 to reflect lessons learned through the first two PPP projects. The PAs on individual projects have also evolved to some extent through the six projects executed since then. Interviewees commented that there is benefit in having a SFA to aid market understanding and reduce transaction costs (particularly legal costs) by speeding up commercial and legal reviews. A lack of standardisation of PPP contracts is an issue in some states in Australia, which they are intending to address.

In addition to the themes discussed earlier, interviewees also contributed comments on potential improvements to the terms of the SFA for the purpose of future projects. This section focuses on these further suggested improvements.

13.1 Drafting complexity

Some interviewees commented on the complexity of the drafting of the SFA generally, as well as in relation to particular sections (e.g. the Change mechanism and performance regime).

Proposed Action: The Commission should review and update the Standard Form (PPP) Project Agreement to simplify drafting where possible, incorporate lessons learned from projects executed and address other specific improvements that have been suggested.

13.2 Horizontal vs vertical infrastructure

Comments from some interviewees suggest that the SFA may not be optimal for horizontal infrastructure projects in NZ (such as roads) compared to vertical infrastructure (such as schools or prisons). Interviewees suggested several factors that distinguish horizontal and vertical infrastructure and potential measures to improve the SFA to address these. Apart from the risks noted above in relation to consents, third party stakeholders and ground conditions, interviewees also noted:

- the imbalance between the proportionate cost of works and services on a road as compared to social infrastructure, such as a prison,
- a distinction between ground and weather conditions in Australia (where there are a significant number of horizontal infrastructure PPP projects) and NZ, including NZ's mountainous terrain, prevalence of earthquakes and higher rainfall rate, and
- the complexity of environmental issues including run-off, forestry and property acquisitions.

The Transmission Gully PPP – Lessons Learnt Review also identified the difference between roads and social infrastructure in relation to the level of design certainty when the AT is set, as the design of a road often evolves over the Construction Period in response to geotechnical information and consenting requirements.

As also discussed in section 6, the impact of many of these risks (other than the imbalance of construction and operating costs) on a horizontal project as compared to a vertical project should be apparent to bidders and therefore able to be assessed and priced at the RFP stage. They also do not necessarily differ between non-PPP projects and PPP projects. For example, the requirement to engage with multiple

consenting authorities on a road project that passes through multiple council areas. The difference on a PPP project, however, is that a PPP is a fixed cost fixed time model and less flexible.

Partnerships Victoria has a separate Standard Project Deed for linear PPP projects. However, the Victorian Standard Form Project Deed for Linear Infrastructure does not differ significantly from the Social Infrastructure Deed in relation to the risks that interviewees have told the Commission are an issue on horizontal PPP projects in NZ. The key differences relate to equipment and plant, reviewable services and minor works and the assumption in the Social Infrastructure Deed that the State remains the operator.

Proposed Action: The Commission should consider amending the Standard Form (PPP) Project Agreement to include guidance notes on provisions that may require adjustment for horizontal as compared to vertical projects.

13.3 Impact of construction delay on contract expiry date

The SFA provides for the PA to end after a specified number of years (25 years in all projects to date) from the actual Service Commencement Date. Where the actual Service Commencement Date is delayed (e.g. due to construction delays), the end date of the PA will also be later, i.e. the Contract Period becomes longer. This means that payment of the UC also commences and finishes later. This leads to a potential for the SPV to receive a windfall gain at the end of the Contract Period. The windfall gain arises as a result of liquidated damages payable to the SPV by the D&C major sub-contractor to compensate for debt repayments due during the delay and before actual Service Commencement when payment of the UC commences. The UC is calculated to cover interest repayments to Debt Providers, and if it is paid for the full 25 years, will result in the SPV being paid both liquidated damages for debt repayments and the full debt repayments through the UC.

In some projects, the end date of the PA was either a fixed date or determined by reference to the Planned Service Commencement Date rather than the actual Service Commencement Date, which means that even if there is a delay to the Service Commencement Date, the total Contract Period does not change.

Proposed Action: The Commission should consider amending the Standard Form (PPP) Project Agreement so that the Expiry Date of the Project is either a fixed date or determined from the Planned Service Commencement Date rather than the actual Service Commencement Date.

Future of the PPP Model in New Zealand

14 Future of the New Zealand PPP Model

The Commission considers that the Model should continue to be an option for the procurement of major infrastructure projects…

Based on the findings of this Review, the Commission is of the view that the Model should continue to be considered as a procurement option for major infrastructure projects. While there have been challenges on some projects, information to date suggests that the Model has been generally successful in delivering major infrastructure projects with greater time and cost certainty for the Crown. The Commission considers that there are opportunities for non-PPP procurements to consider adopting the transparent and disciplined approach to procurement that that is inherent in the Model, including risk allocation, whole of life considerations and performance.

At the start of the PPP programme, there were a reasonably ambitious set of broader objectives beyond those expected from conventional procurement methods. Evidence as to whether these have been achieved is generally more anecdotal. This does, however, need to be interpreted in the context of the relatively limited number of projects in the Portfolio and that it is still too early to measure the extent to which whole of life benefits will materialise.

…but there are opportunities to improve the Model based on the findings of this Review

The Review has identified numerous areas where the Model has not worked as well as intended and could be improved for future projects. There are also some significant issues that have arisen on specific projects that are still being worked through at the time of this Review. It is likely that further issues will develop over time as the remaining projects enter their Operating Periods.

Some of the issues highlighted in this review are not necessarily unique to the Model and/or are the result of how the Model has been implemented in practice, rather than its underlying design. It is not uncommon for the delivery of major infrastructure projects delivered under conventional procurement methods to experience significant challenges[46], but this does not necessarily point to underlying flaws in the procurement method. Each procurement method is best suited to particular project types, have their own set of trade-offs, and can and do experience difficulties that are inherent in the delivery of large and complex engineering and construction projects.

The current gap in the PPP project pipeline does present a challenge regarding capacity and experience in the market…

While there are currently no confirmed future PPPs in the pipeline, the Model can still be considered under current government policy for projects outside of the education, corrections and health sectors. However, the current gap between projects creates a risk that experience and expertise on both the Crown and private sector side is not retained within the market. This does present a challenge for future projects to ensure knowledge of the Model is retained and lessons from previous projects are incorporated in Model revisions. This risk has been a key motivation for this Review.

[46] For example, the Christchurch Acute Services Building, MacKays to Peka Peka Expressway.

…but the Commission can play an important role in creating an environment for successful infrastructure procurement for both PPPs and other models

A key purpose of the Commission is to provide long-term strategy and planning for NZ's infrastructure sector, as well as procurement and delivery advice for major projects. This includes developing a 30-year infrastructure strategy. In addition to the published Infrastructure Pipeline, this will provide a more aligned forward view of the government's future infrastructure plans.

Many of the factors that will support a robust and competitive PPP market also apply to other procurement models, with key factors including:

- Demonstrating the Model is being updated and refined over time based on the experience of previous projects, such as the amendments and supporting guidance suggested in this Review.
- Providing certainty as to the potential pipeline of infrastructure projects that are being considered for PPP procurement, which will support the 'scaling up' of resources to bid for projects.
- Aiding Procuring Entities through the Business Case process to help ensure that the right procurement model is selected for major projects, and specifically that PPP is applied to projects that it is well suited to.
- Clear messaging on the government's position on alternative procurement models and the use of private financing.

Glossary

Abatement	A reduction in the UC for performance below the standard required by the Project Agreement.
Affordability Threshold (AT)	The maximum price (expressed in Net Present Cost terms) that the Procuring Entity is prepared to pay for delivery of a project. Any Proposal with a Net Present Cost in excess of the Affordability Threshold will be considered non-compliant.
Base Case Financial Model	The financial model agreed (and finalised at FC) for the purpose of, amongst other things, calculating the UC.
Better Business Case (BBC)	A five-case model that provides objective analysis and consistent information to decision-makers, to enable them to make smart Investment decisions for public value. https://treasury.govt.nz/information-and-services/state-sector-leadership/investment-management/better-business-cases-bbc
Business Case	A management tool that supports decision-making for an Investment. A robust Business Case can provide an explicit and systematic basis for decision-making, transparency and accountability, assurance that the proposed Investment optimises Value for Money, and a plan for realising the expected benefits, and for managing costs and risks.
Cabinet Office Circular (19) 6	Cabinet Office circulars complement the Cabinet Manual and CabGuide, providing detailed guidance on central government processes. Cabinet Office Circular CO (19) 6 sets out Cabinet's expectations regarding investment management and asset performance in the state services, including expectations relating to consideration and implementation of PPP procurement.
Commission	The New Zealand Infrastructure Commission, Te Waihanga.
Consortium	A group of private sector parties who work together to bid and, if successful, deliver a project. The bundled services included in the scope of the project will require Consortium members with specialisation in design, construction, asset management, Facilities Maintenance, operational expertise (if applicable), and debt and equity financing.
Construction Period	The period from FC to Service Commencement.
Contract Period	The period from FC to the expiry of the Project Agreement.
Contractor	The entity (a Special Purpose Vehicle - typically a limited liability company, or limited partnership) with which the Procuring Entity contracts (through the Project Agreement) for the delivery of a project.
Contractual Close	The date at which the finalised Project Agreement is signed by authorised representative(s) of the Procuring Entity and Contractor.
Design-Build-Finance-Maintain (DBFM)	A form of PPP procurement that bundles the Design, Build, Finance and Facilities Maintenance components of the project (including associated risks) for delivery by the Contractor. Responsibility for provision of Operational Services (and risk) is retained by the Procuring Entity.
Design-Build-Finance-Maintain-Operate (DBFM))	A form of PPP procurement that bundles the Design, Build, Finance, Facilities Maintenance and Operational Services components of the project (including associated risks) for delivery by the Contractor.
Expression of Interest (EOI)	The stage of the procurement process in which the Procuring Entity conducts an open process to short list a predetermined number of respondents to participate in the Request for Proposals stage.
Financial Close (FC)	The time at which financing obligations (in particular, the final setting of interest rates, the Base Case Financial Model and UC, and the process by which equity contributions will be made to the SPV) are set and agreed between the

	Procuring Entity and the Contractor, in accordance with the FC Adjustment Protocol.
Government Electronic Tenders Service (GETS)	The NZ Government Electronic Tenders Service (GETS) is a free online service designed to promote open, fair competition for NZ government contract opportunities. www.gets.govt.nz
Government Procurement Rules	Standards of good practice for government procurement as published by the Ministry of Business, Innovation and Employment, many of which are mandatory. These include a requirement that agencies considering the procurement of infrastructure with a total cost of ownership over $50 million must consult with the Commission and follow relevant Commission guidance. (Rule 64). The rules apply to all contract types, including PPPs (Rule 10). https://www.procurement.govt.nz/procurement/principles-and-rules/government-procurement-rules/
Handback	At the conclusion of the Operating Period, the asset must be handed back to the Procuring Entity in a pre-defined condition, at no additional cost.
Industrial Equity	Industrial Equity refers to investments made by sub-contractors who are also delivering some or all of the asset and/or services.
Infrastructure	Fixed, long-lived structures that facilitate economic performance and wellbeing. Infrastructure includes buildings and physical networks (principally: transport, water and energy), social assets such as hospitals and digital infrastructure such as mobile and broadband infrastructure.
Input Specification	A level of prescription or direction from the Procuring Entity as to how the asset ought to be designed or function, which may restrict the scope for innovation by RFP respondents and potentially result in greater risk being retained by the Procuring Entity.
Lifecycle Costs	The cost of replacing or refurbishing asset components during the Contract Period.
Net Present Cost (NPC)	The present value of all relevant costs over the asset's life calculated using the relevant discount rate.
Operating Period	The period from Service Commencement to the expiry of the Project Agreement.
Operational Services	The front-line public services delivered using the asset during the Operating Period (which can be contrasted with asset management or facilities maintenance services which keep the asset in the condition necessary to enable the Operational Services to be delivered).
Payment Mechanism	The methodology for applying the Performance Regime to calculate the Unitary Payment for a period (and set out in a schedule to the Project Agreement). The Payment Mechanism and Performance Regime work together to determine the Unitary Payment for a period and therefore incentivise performance of the Contractor's obligations under the Project Agreement and delivery of the project outcomes.
Performance Regime	The performance standards expected of the Contractor, including key performance indicators, and Abatements to the UC for performance below the standard required by the Project Agreement (and set out in a schedule to the Project Agreement). The Payment Mechanism and Performance Regime work together to determine the Unitary Payment for a period and therefore incentivise performance of the Contractor's obligations under the Project Agreement and delivery of the project outcomes.
Preferred Bidder (PB)	The respondent whose Proposal best met the requirements of the project and has been selected to negotiate and execute the Project Agreement with the Procuring Entity.
Procuring Entity	A public sector entity responsible for the procurement of a major infrastructure project; specifically, those staff involved in the development and internal approval of the project Business Case and procurement process. The Procuring

	Entity may refer to multiple entities if the delivery of the Project is a joint mandate or partnership.
Project Agreement (PA)	The contract between the Procuring Entity and the Contractor which sets out each party's rights and obligations in relation to delivery of the project.
Proposal	A Consortium's submission in response to the RFP.
Proxy Bid Model (PBM)	The model used to calculate the estimated UC that a Contractor would require to finance and deliver the Project to the level of performance specified in the Project Agreement. It is comprised of the costs of the risk adjusted Reference Project with third party sector financing, tax and PPP specific costs added to it. It uses the same underlying capital, operating, risk management and tax assumptions as the PSC.
Public Private Partnership (PPP)	In the NZ context, a PPP is a long-term contract for the delivery of a service, where provision of the service requires the construction of a new asset, or enhancement of an existing asset, that is financed from external sources on a non-recourse basis, and full legal ownership of the asset is retained by the Crown.
Public Sector Comparator (PSC)	An estimate of the risk adjusted whole of life cost of a project if it were to be delivered by the Procuring Entity using conventional procurement methods, rather than PPP. The PSC is primarily used as a benchmark against which to assess the net present cost of procuring a project as a PPP.
Reference Project	The whole of life asset and service delivery solution that would be procured using conventional methods if the project was not procured as a PPP. The Reference Project is primarily used as an input to the PSC and PBM. It should be designed, and its costs estimated, such that it is capable of achieving the same outcomes and performance standards that are expected of the private sector under the Project Agreement.
Request for Proposals (RFP)	The stage of the procurement process in which the short-listed respondents develop Proposals (in response to the Request for Proposals document) for delivering the project outcomes required by the Procuring Entity, through an interactive tender process. The Procuring Entity then evaluates the Proposals with the objective of selecting one respondent as the Preferred Bidder.
Risk Allocation	Risks are allocated (through the Project Agreement) to the party that is best able to manage and mitigate those risks, in order to drive delivery of the required service outcomes and Value for Money. All project risks are identified early in the procurement process, and the cost of those risks to the Procuring Entity determined. Risks will only be allocated to the private sector partner where they can manage those risks more effectively or efficiently than the Procuring Entity, and therefore provide a Value for Money solution.
Service Commencement	The date from which the asset is available for use and Unitary Payments to the Contractor begin.
Special Purpose Vehicle (SPV)	The legal entity established for the sole purpose of entering into the Project Agreement with the Procuring Entity and sub-contracting with Consortium members. The SPV will generally be a limited liability company or limited partnership.
Standard Form (PPP) Project Agreement (SFA)	The model contract for PPP projects which forms the basis for PPP projects in NZ. It contains the core commercial principles and structure of the Model. The base agreement, schedules, and contractual framework are available on the Commission website.
Unitary Charge	Means the fee payable by the Procuring Entity during the Operating Period of a PPP.

Value for Money	Value for Money is achieved where PPP procurement delivers better outcomes from a project than conventional procurement methods for the same, or lower, Net Present Cost.

Appendix A: Stakeholder consultation

The Commission wishes to thank the following stakeholders for providing feedback to the Commission as part of this Review.

Organisation/Individual	Role
Ministry of Education	Procuring Entity
Department of Corrections	Procuring Entity
Waka Kotahi New Zealand Transport Agency	Procuring Entity
Northern Express Group	PPP SPV
Wellington Gateway Partnership	PPP SPV
SecureFuture	PPP SPV
Accident Compensation Corporation	Equity Provider
HRL Morrison and Co.	Equity Provider
Infrared	Equity Provider
Pacific Partnerships	Equity Provider
John Laing	Equity Provider
CPB Contractors	D&C major sub-contractor
Fletcher Construction	D&C major sub-contractor
Hawkins (Downer)	D&C major sub-contractor
HEB	D&C major sub-contractor
Southbase Construction	D&C major sub-contractor
Cushman & Wakefield	AMM major sub-contractor
Spotless (Downer)	AMM major sub-contractor
Programmed FM	AMM major sub-contractor
ANZ	Debt Provider
BNZ	Debt Provider
Credit Cube	Debt Provider
MUFG	Debt Provider
Bell Gully	Legal advisor
Anderson Lloyd	Legal advisor
Chapman Tripp	Legal advisor
MinterEllisonRuddWatts	Legal advisor
Simon Ashworth (previously Corrs)	Legal advisor
Herbert Smith Freehills	Legal advisor
MAFIC (members of team previously Macquarie)	Financial/commercial advisor
PwC	Financial/commercial advisor
KPMG	Financial/commercial advisor
Deloitte	Financial/commercial advisor

Organisation/Individual	Role
EY	Financial/commercial advisor
Aurecon	Technical advisors, Independent Reviewer, Financiers' Certifier
AECOM	Independent Reviewer
Audit NZ	Probity Auditor
McHale Group	Probity Auditor

Appendix B: Terms of Reference – Transmission Gully

Transmission Gully Interim Project Review – Expert Reviewer

Terms of Reference

Infracom and responsible Ministers have agreed that Infracom will oversee an Interim Project Review of the Transmission Gully Project.

Process

Infracom intends to directly approach and appoint an independent Expert Reviewer to undertake the Interim Project Review. The Expert Reviewer will be overseen by Infracom and supported by a NZ-based, experienced construction industry professional who will provide peer review support.

The proposed scope and approach to carrying out the investigation is described below.

Scope

The investigation will focus on how the Transmission Gully project agreement was awarded for the price agreed, whether this was a realistic price, and whether the risks identified then were appropriate and appropriately considered and taken into account. Following completion of the project, Infracom will also consider the need for a post completion review to investigate how well the project has delivered on its objectives to date, in order to derive lessons that could be applied to future procurement of major infrastructure projects.

The review will consider the following topics.

Project development and procurement process

1. Business Case
    a. Whether the budget presented was based on reasonable supporting analysis and assessments of costs, including appreciation of the inherent and contingent risks and their associated financial implications. Particular consideration should be given to:
        i. the development of the public sector comparator; and
        ii. the commercial case for selection of the preferred procurement model and the rationale for doing so.
2. Risk Transfer
    a. Whether key risks were appropriately allocated and communicated, with consideration to be given to:
        i. Whether the affordability threshold was sufficient given the nature of the risks transferred to the Contractor, including how was it set, the decision-making pertaining to that process and the authorising environment, and what can be learned from the influence the affordability threshold had on the procurement; and
        ii. Whether the consenting strategy was appropriate, including the allocation of consenting risk and the impact Consenting Authorities may have had on project outcomes.
3. Governance and timeframes
    a. Whether sufficient time was allowed for approvals, commencement, and completion of the tender process so as to allow the tendering parties to fully understand and appraise the project risks and Waka Kotahi to understand the nature of the proposals; and
    b. Whether the project governance structure had the knowledge and experience of delivering PPP construction projects (including the nature of risks transferred to the private sector), to effectively oversee the project and address issues in a timely fashion.

Project implementation and value for money (not in the scope of the Interim Review)

4. Project Implementation
    a. Identify key events and risks that have adversely impacted on project costs and programme.
5. Value for money
    a. Whether the selected PPP procurement model has achieved value for money to date, taking account project outcomes and key risks that have emerged.
    b. Evaluate the likely value for money outcomes if the project had been delivered through an alternative procurement methodology, including the construct-only, design and build, and competitive alliance contracting models. This evaluation should include benchmarking against the performance of analogous projects in the Waka Kotahi investment portfolio.

Indicative Timeline

It is anticipated that the review will take at least three months from the appointment of the reviewer, with the following indicative timeline (subject to agreement with the selected reviewer):

- Week 0-2 – document review;
- Weeks 2-6 – interviews, gather and review evidence;
- Week 6-8 – prepare draft report for consultation;
- Week 9-10 – consultation and comments; and
- Week 11-12– review comments and finalise report.

The final report will be provided to responsible Ministers for consideration and will then be released publicly.

Expert Reviewer

To ensure objectivity in the process, Infracom intends to procure a suitably qualified international advisor to lead the Transmission Gully Interim Project Review. That individual should have significant experience, at a leadership level, of the following:

- Extensive experience with major capital works business cases;
- Review and evaluation of major infrastructure projects of the scale of (or above) Transmission Gully;
- Experience with a range of major infrastructure delivery models including Public Private Partnerships.

Peer Review

The Expert Reviewer will be supported by a NZ-based, experienced construction professional appointed by Infracom. The Peer Reviewer will:

- Have significant knowledge of NZ major projects' procurement practices; and
- Not have been directly involved in the Transmission Gully procurement process.

The Peer Reviewer will provide peer review support to the expert review throughout the life cycle of the review process, including advice as to standard practices in New Zealand and the construction market in general.

Method

Examination of documentation available from Waka Kotahi, the Treasury and the Ministry of Transport.

Interview of those key individuals involved in the procurement and delivery of the Project, including the Wellington Gateway Partnership, the Builder CPB-HEB, Waka Kotahi, the Treasury and the Ministry of Transport.

Governance

Infracom management will oversee the Interim Project Review and provide direction to the Expert Reviewer and monitor the progress of the review and provide monthly progress updates to its Board. Resources from the Major Projects and Advisory Team will be used to support the Expert Reviewer.

Procurement

Infracom will directly appoint the Expert Reviewer and Peer Reviewer. We have prepared a Procurement Plan, including exemption from open advertising and the all of government panel. The Procurement Plan addresses the process for selection and contract award.