

Practical ideas to improve procurement for major projects

Submission to the Standing
Committee on Infrastructure,
Transport and Cities on
procurement practices for
government-funded
infrastructure.

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Key points

- The Business Council of Australia welcomes the increasing focus of federal, state and territory governments on improving contracting for major infrastructure projects.
- The scale of Australia's infrastructure pipeline is unprecedented. NSW is leading, committing \$107 billion to 2025, while the Federal Government has committed \$110 billion to 2031. The number and complexity of infrastructure projects has increased significantly in recent years.
- Consistently delivering the 'new normal' of increased infrastructure funding will be crucial to realising Australia's long-term growth and increasing the standard of living for all Australians.
- Urgent action is required to enable the delivery of the infrastructure pipeline. Improving government procurement practices requires greater collaboration with industry.
- Governments and industry must work together to:
 - fix risk allocation on projects. Contractors have increasingly been expected to take on an unreasonable level of risk on projects, creating adversarial relationships during delivery and missed opportunities for communities. Failure to resolve this makes the market less attractive to tier 1 contractors and to new entrants, increases the number of disputes and puts at risk delivery timeframes, resulting in poor value-for-money outcomes.
 - scope projects effectively through early market engagement and allowing time for due diligence. Building collaboration at the start, rather than rushing to announcements and to contract award, will yield better design and value-for-money outcomes.
 - pick the right contracting model for the specific project or programme. Too often government agencies apply a cookie-cutter approach to contracting that relies upon the Design and Construct contracting models. Taking a broader view of available contracting models can lead to selecting the most appropriate model for a specific project. This translates to better value-for-money outcomes and project scopes that better meet community expectations, especially when the risk allocation strikes an appropriate balance.
 - improve the capability and capacity of tier 2 and 3 contractors so that they can undertake more complex projects. The number of tier 1 contractors in the Australian market capable of delivering mega-projects of over \$1 billion has not changed in recent years. Governments can effectively put programmes of projects to market that build the capacity and capability of tier 2 and 3 contractors over time. These programmes should increase in complexity over time, to the point that some tier 2 contractors are bidding for mega-projects in the medium term.
 - smooth the pipeline of mega-projects by coordinating across jurisdictions. An efficient pipeline sequenced across federal, state and territory governments would help to remove peaks and troughs in the availability of key skills and materials, resulting in more certain project delivery timeframes and value-for-money outcomes.
- Over the longer-term, there are structural problems that need to be addressed in the infrastructure system more broadly. Labour productivity in the construction industry has grown at half the rate of other industries. Reform is required. The Business Council proposes a roadmap for reform that builds upon strong collaboration between governments and industry through establishing a shared understanding of the challenges and working together to make change, but this should not distract from the urgent action required on right now to improve procurement practices.

Overview

This is the Business Council of Australia's submission to the Standing Committee on Infrastructure, Transport and Cities on procurement practices for government-funded infrastructure. The development of this submission has been informed by the Business Council's Infrastructure, Housing and Construction Working Group, which includes expertise and applied experience across the whole infrastructure system.

The Business Council welcomes the increasing focus of federal, state and territory governments on improving contracting for major infrastructure projects. Delivering productive infrastructure is essential to securing long-term economic growth, increasing the standard of living for all Australians.

This submission sets out clear, urgent recommendations to unlock bottlenecks in procuring major infrastructure projects and proposes a pathway for reform. At the core of these recommendations is the importance of driving collaboration between governments and industry at each step of the procurement process. Greater collaboration will achieve better outcomes for all Australians.

Taking an infrastructure system view

The Business Council recognises the importance of viewing the infrastructure sector as a system of interacting parts. In the 2019 report, *Australia's Infrastructure System: policy settings to improve the lives of all Australians* we make the case for moving from a project-by-project view of major infrastructure projects to a system-based perspective. The guiding goal of the infrastructure system is to support a productive, competitive and growing economy that enables attractive places to live, study and work, where people realise their potential.

Taking a systems view means every stage of the infrastructure life cycle will be managed well – from planning, funding and delivery through to operation and maintenance. It means that infrastructure projects prioritised for public funding are independently identified and assessed to provide the highest value for the community and for economic growth. In recent times, the benefits of adopting this approach in a spatial context is being demonstrated through focussing on place-based outcomes, rather than being blinkered towards individual projects. Salient recent examples of this important trend are the Western Sydney Parklands and the Parkes Special Activation Precinct.

The infrastructure system does not operate in isolation. It needs to interact seamlessly with the planning system and with systems for skills development, skilled migration, materials supply, security, and so on. There can also be competition for resources with other large private capital projects which can create bottlenecks in skilled labour and materials supply. Mining and energy sector capital investments should of course be factored into systems planning as they draw on a common skills and resource pool. It is only through adopting a system-wide lens that we can shift the dial in the procurement of major infrastructure projects.

Urgent action is required to deliver an unprecedented infrastructure pipeline

The scale of Australia's infrastructure pipeline is unprecedented. NSW is leading on spending commitments, with \$107 billion to 2025, while the Federal Government has committed \$110 billion to 2031. The Grattan Institute has noted that it is 10 years since Australia's first infrastructure project worth over \$5 billion, now there are over nine such projects under construction. Consistently delivering the 'new normal' infrastructure pipeline will be crucial to realising Australia's long-term growth.

Delivering the infrastructure pipeline is challenging given the historically low levels of productivity in the construction sector (the backbone of the infrastructure system). The Australian Constructors Association reports that labour productivity in the construction industry has grown at 1.2 per cent per annum since 1989/90, compared to 2.4 per cent per annum for a basket of other industries. Wide-reaching reform is required in collaboration with governments and industry to turn the sector around.

Achieving wide-reaching reform is a multi-year endeavour. However, urgent action is needed to unlock delivery of today's mega-projects and to better utilise available market capacity. The industry is united in identifying improving the performance of government procurement practices as the way to enable delivery of the infrastructure pipeline.

Increasing collaboration between governments and industry and sharing positive practice across jurisdictions and agencies will shift the dial in delivering the pipeline.

Fixing procurement requires greater collaboration

The following recommendations focus on urgent actions to improve the procurement of projects right now, with examples of positive practice. Greater collaboration between governments and industry is essential.

Risk allocation

Contractors have increasingly been expected to take an unreasonable level of risk on projects, creating adversarial relationships during delivery and missed opportunities for communities. This has been seen through high-profile projects such as Sydney's CBD and South East Light Rail, the New Royal Adelaide Hospital and the Westgate Tunnel.

A reasonable and collaborative approach looks closely at where unknown risks are allocated. Failure to do so makes the market less attractive to tier 1 contractors and to new entrants, increases the number of disputes and puts at risk delivery timeframes, resulting in poor value-for-money outcomes.

Put simply, an unreasonable approach to risk allocation leads to fewer contractors bidding for mega-projects which reduces the competitive tension during procurement, potentially resulting in poorer value-for-money outcomes. Governments need the limited pool of contractors able to deliver the complex, mega-projects to provide the best value-for-money outcome and to maximise innovation.

Regardless of how governments approach risk allocation, the public invariably holds them to account over project delivery. It cannot reallocate the reputation risk around project delivery. As such, unreasonable risk allocations do not fully transfer risk and result in excessive risk pricing and poor value-for-money. They also reduce the sustainability of the construction sector as large unmanageable risks are not supported by the margins expected on public infrastructure projects.

Identifying, avoiding and mitigating risks as early as possible in the procurement process is essential. This relies upon early market engagement, allowing time for due diligence and selecting a contracting model that best suits the project. These points are considered next.

Positive Practice: The adoption of a risk sharing regime for the North East Link primary package in Victoria was a response to market feedback and the nature of the project. It showed an increased willingness by governments to engage with the private sector early and work through the particular risks inherent in the project.

Recommendation 1: Government agencies allocate risks to the party best able to manage them or share the risk where outcomes will impact all parties and are not manageable or assessable. Early engagement with the market will support this approach and foster a collaborative relationship.

Due diligence and early market engagement

Overly prescriptive specifications in procurement remove opportunities to innovate and result in reduced value-for-money. Engaging in early market engagement and allowing time for due diligence are essential.

Allowing time to undertake due diligence in the early stages can improve the project scope and provide a better understanding of cost. It is also important from a risk management perspective, with time spent on identifying, avoiding and mitigating risks. Due diligence can include community engagement on impacts and benefits of a

project as well as identifying latent issues relating to heritage, land contamination, ecology, geotechnical conditions and utility services.

Without due diligence and early market engagement it is impossible to understand the true project cost, or for governments to accurately budget for the project on balance sheets. It also brings confidence to proponents to accurately price the project, setting the stage for a smoother delivery stage and bringing greater certainty to the community.

A barrier to allowing time to undertake due diligence and early market engagement is governments announcing project timings and estimated costs too early, which can set unrealistic expectations within the community. In many cases, governments announce an estimated project cost prior to due diligence taking place. This then acts as a benchmark in the eyes of the public on whether or not the project is effectively procured and delivered.

Positive practice: Infrastructure NSW has published guidance for the NSW public sector on providing reliable project information to the public at different project stages – [*Timely Information on Infrastructure Projects: A Guide*](#). It notes that “the level of reliable detail about community impacts, costs, benefits, and delivery program increases over time and project stages.”

Recommendation 2: Government agencies allow time for due diligence and early market engagement to take place to refine the timing, scope and structure of the project. This is supported by governments avoiding announcing project timelines or cost estimates too early.

Contracting models

Contracting is not a one-size-fits-all approach. Too often government agencies apply a cookie-cutter approach to contracting that relies upon the Design and Construct contracting models. Taking a broader view of available contracting models can lead to selecting the most appropriate model for a specific project. This translates to better value-for-money outcomes and project scopes that better meet community expectations, especially when the risk allocation strikes an appropriate balance.

Alliancing and Delivery Partner approaches have proven successful in the past and should be embraced, where appropriate. Design and Construct models remain very effective approaches but would benefit from greater collaboration during the procurement phase to ensure positive behaviours from all parties during delivery. Using standard documents, where appropriate, would help to reduce uncertainty and streamline procurement processes.

Positive practice: There are examples across Australia of governments successfully selecting and implementing a variety of contracting models best suited to a specific project or programme. This positive practice can be shared across jurisdictions to produce better outcomes:

- **Delivery Partner:** The Woolgoolga to Ballina Pacific Highway Upgrade Project in NSW used a delivery partner model awarding more than 170 work packages. The \$4.9 billion project was delivered early, under budget and recorded an independent staff engagement score exceeding the high performing team threshold.
- **Programme Alliance:** The Level Crossing Removal Project in Victoria is using a Programme Alliance approach to drive longer-term decision-making to development and delivery. A ‘theirs to lose’ approach to allocating work has led to greater efficiencies and better outcomes.
- **Traditional Public Private Partnership:** The New Footscray Hospital is being delivered under a traditional PPP framework with the risk allocation being adjusted to reflect a more balanced allocation of risks between the public and private sectors.

Recommendation 3: Government agencies consider all available contracting models to ensure the approach adopted is fit-for-purpose for the specific project, with central agencies assuring that the best model is utilised.

Pathway for tier 2 and 3 contractors

The number of tier 1 contractors in the Australian market capable of delivering mega-projects of over \$1 billion has not changed in recent years, despite a rapid increase in the number of mega-projects. When combined with a collaborative approach to risk allocation and selecting project-specific contracting models, governments have an opportunity to establish a pathway for tier 2 and 3 contractors while meeting an immediate need to deliver large projects quickly and efficiently.

Governments can effectively put programmes of projects to market that build the capacity and capability of tier 2 and 3 contractors over time. These programmes should increase in complexity over time, to the point that some tier 2 contractors are bidding for mega-projects in the medium term.

Positive practice: The revamped Suburban Roads Upgrade from Major Roads Project Victoria is an example of a deliberate decision to split a project (originally slated as a public private partnership) into a programme of smaller projects targeted at directly engaging the tier 2 and 3 contractor market.

Recommendation 4: Governments procure programmes of projects that are designed to deliver the current infrastructure pipeline and to grow the capability and capacity of tier 2 and 3 contractors.

Sequence infrastructure delivery

An efficient pipeline sequenced across federal, state and territory governments would help to remove peaks and troughs in the availability of key skills and materials, resulting in more certain project delivery timeframes and value-for-money outcomes.

A sequenced pipeline is a reasonable long-term goal, however, in the immediate term, focussing on mega-projects would result in more competitive procurement processes, availability of skills and better value-for-money. This approach would provide industry with greater certainty to invest in building capability and expertise in Australia, growing the overall capacity in Australia to bid for and deliver more projects. There is a role for National Cabinet to play in fostering greater collaboration across jurisdictions to provide pipeline certainty.

Positive Practice: Infrastructure Australia is nearing completion of analyses investigating the market's capacity to deliver the infrastructure pipeline. These analyses have the potential to provide a considered evidence-base for governments and industry to identify sector-wide skills and materials gaps. Adjusting the timing of infrastructure projects will be one way to smooth the pipeline.

Recommendation 5: Federal, state and territory governments, supported by National Cabinet, work together to sequence delivery of mega-projects where it will demonstrably smooth the pipeline and lead to greater certainty for delivery timeframes and better value-for-money outcomes.

Asset recycling

Additional funding sources will be required over time to deliver the 'new normal' infrastructure pipeline. Asset recycling has proven to be an effective approach to bring in private sector investment. Announcing and implementing asset recycling initiatives provides a powerful signal to industry that governments are committed to delivering the infrastructure pipeline over a sustained period of time. This in turn provides industry with greater confidence to invest in building capability and capacity, which leads to better value-for-money procurement.

Positive Practice: The NSW Government announced in the recent 2021-22 Budget that asset recycling will continue to be a key aspect of its fiscal repair strategy. This announcement provides greater confidence to industry of the government's commitment to delivering a strong infrastructure pipeline beyond the forward estimates.

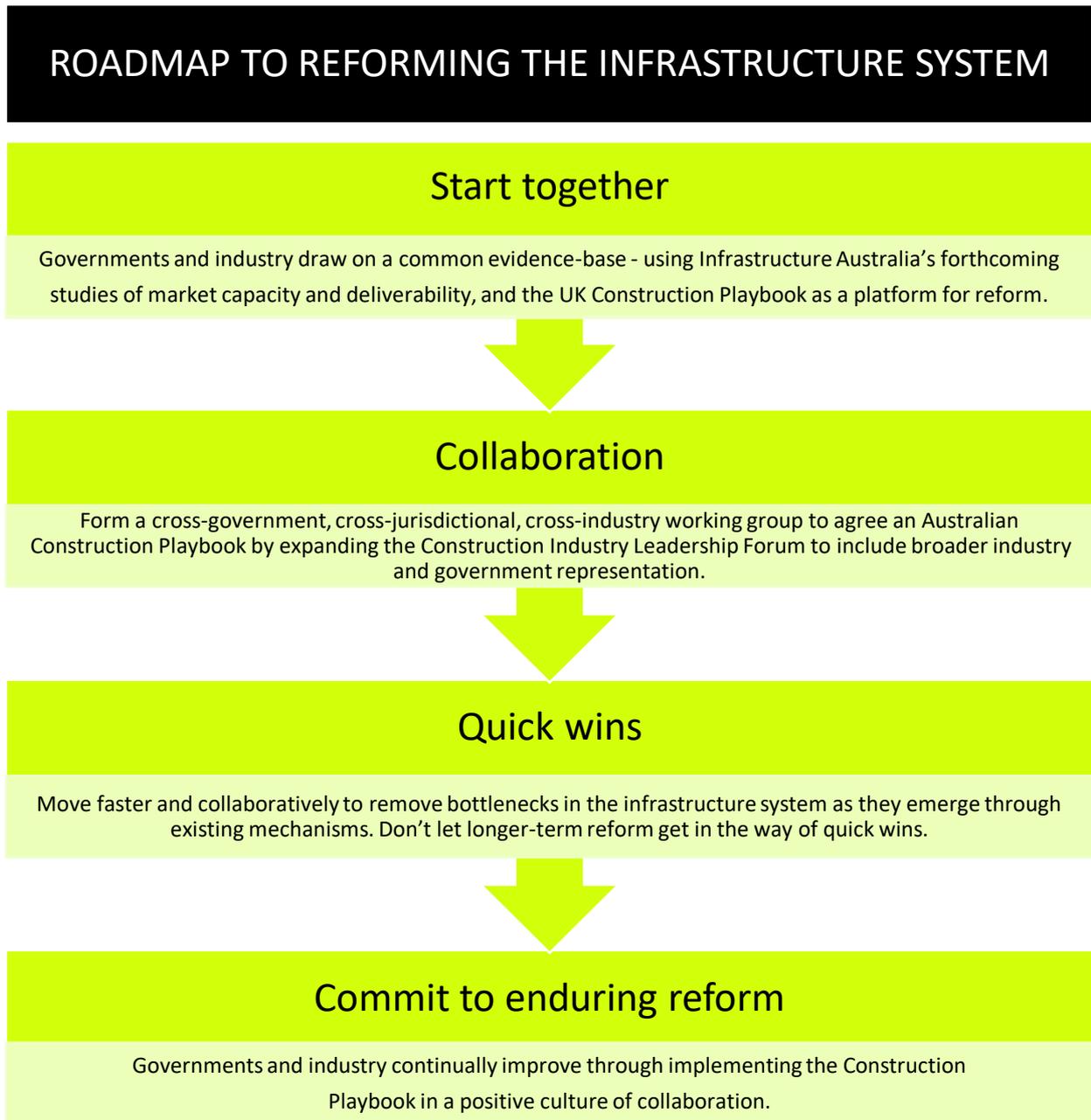
Recommendation 6: Federal, state and territory governments announce and implement asset recycling initiatives to deliver the infrastructure pipeline.

Collaborative Roadmap to Reform

This submission has focussed on short-term wins to deliver today's infrastructure pipeline. However, more substantial and wide-ranging reform of the infrastructure sector is needed to improve performance. There are several initiatives underway across governments and industry that can be aligned to bring reform, such as:

- The Australian Constructors Association idea for an Australian version of the UK [Construction Playbook](#).
- The NSW Premier's Memorandum that introduces an 'if not, why not?' directive for adopting positive procurement practices - [Framework for Large, Complex Infrastructure Projects](#).
- Infrastructure Australia's forthcoming articulation of industry challenges in the *Australian Infrastructure Plan 2021* and further research into the capacity of the infrastructure sector to deliver the infrastructure pipeline.

Underpinning any successful programme of reform will be increasing collaboration between governments and industry. The Business Council proposes a four-step Roadmap to Reforming the Infrastructure System that will shift the dial on delivering the infrastructure pipeline:



Recommendation 7: Governments and industry collaborate to implement the Business Council of Australia's Roadmap to Reforming the infrastructure system.

Protectionism isn't the answer

The Business Council supports sensible efforts to raise the participation of competitive local suppliers in major infrastructure projects. However, adding red tape through local content rules and additional compliance activities is not the answer. The most effective way to increase domestic participation is to ensure Australia is an attractive destination for investment with a competitive business environment.

Introducing an additional regulatory impost on major projects and intervening in efficient business operations would lessen Australia's attractiveness as a place to invest. Australia relies on a level of foreign investment to deliver the infrastructure pipeline.

Global supply chains have proven to be resilient to the impacts of the COVID-19 pandemic. Businesses have been flexible to shocks and continued to deliver. There is no compelling case for governments to intervene in the market under the banner of growing sovereign industry capability. Policy should be aligned to creating a positive investment environment that will grow our economy and create the local employment and supplier opportunities of the future.

The Business Council supports a comprehensive review of existing policies that address information gaps in the market as well as policies that are designed to improve the competitiveness of Australian firms. We support greater consideration of these alternative options:

- Identify and address information barriers experienced by project owners and local suppliers by improving existing programs such as implementing the Modern Manufacturing Strategy.
- Review the effectiveness of policies, such as the Australian Industry Participation Plans, to understand whether they have meaningfully increased participation for Australian businesses than otherwise would have been the case.
- Generally, governments should pursue taxation and regulatory policies that enhance the international competitiveness of Australian suppliers – interventions applied as band-aids mask competitiveness problems that are caused by poor taxation and regulatory settings elsewhere in the system.

Recommendation 8: Governments focus on building the competitiveness of Australian businesses in supporting major infrastructure projects without unnecessarily increasing red tape by starting with reviewing the effectiveness of existing policies and programmes.

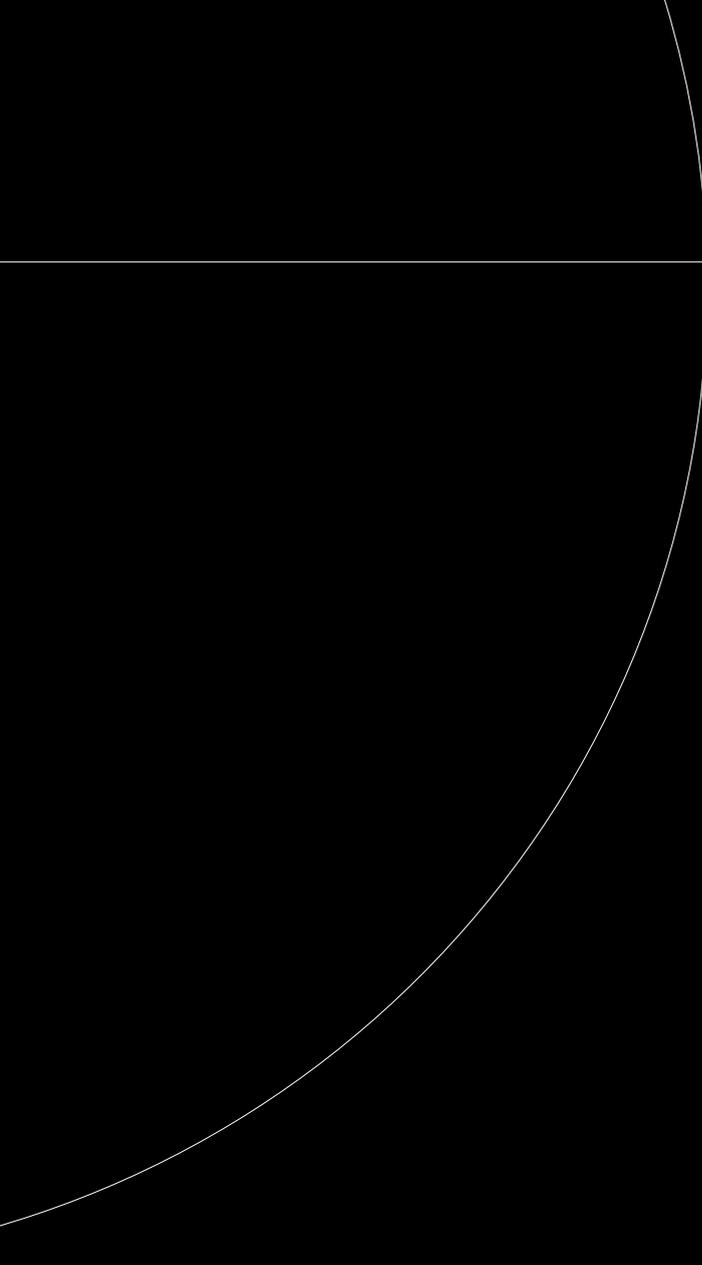
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