Australian Government
Productivity Commission

PRODUCTIVITY COMMISSION

PUBLIC INFRASTRUCTURE INQUIRY

MR P. HARRIS, Presiding Commissioner
DR W. MUNDY, Commissioner
MR P. LINDWALL, Associate Commissioner

TRANSCRIPT OF PROCEEDINGS

AT BRISBANE ON FRIDAY, 11 APRIL 2014, AT 10.16 AM

Continued from 9/4/14 in Melbourne

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MR HARRIS: Good morning, ladies and gentleman. Welcome to the public hearings for the National Inquiry into Public Infrastructure. As I'm sure all of you are aware, we released a draft report in March 2014 on this inquiry. My name is Peter Harris, I'm the presiding commissioner. My fellow commissioners are Dr Warren Mundy and Paul Lindwall.

The purpose of this round of hearings is to facilitate public scrutiny of the commission's work so far and to get comment and feedback on the draft report. Following this hearing, hearings will also be held in Sydney on Monday. Then we will be working towards a final report to government at the end of May. Participants in this inquiry will automatically receive a copy of the final report once it is released by the government, but I should point out that the government can take 25 parliamentary sitting days before it responds and that's a fair period in most people's language.

We like to conduct the hearings in an informal manner but I remind everybody that a full transcript is being taken and because a transcript is being taken, we won't be taking comments from the floor. But at the end of the day's proceedings there will be an opportunity for anybody who wants to make a brief additional presentation. Moreover, obviously we're available to take follow-up by email from people. If you hear something said and if you want to provide us with further information, we're happy to take it that way as well.

Participants are not required to take an oath but should be truthful in their remarks. Transcript will be made available to participants and up on the web site following these hearings and all submissions are obviously available there as well, other than those that are rated confidential and we have had some confidential submissions.

I understand the occupational health and safety arrangements require you to follow the green exit signs and proceed out of the building should there be an occupational health and safety issue. There will be floor wardens to advise you according to the venue's requirements, but please speak to one of our people if you're unsure about these arrangements.

I think our first witnesses are from the Board of Professional Engineers of Queensland. Could you please identify yourselves for the record.

MS MURRAY (BPEQ): Clare Murray, registrar, Board of Professional Engineers.

MR CARR (BPEQ): Chris Carr. I'm the chair.

MR HARRIS: Would either of you like to make some basic opening remarks?

MS MURRAY (BPEQ): Yes, we would, thank you. Thank you for the opportunity to make submission today. The Board of Professional Engineers of Queensland administers the Professional Engineers Act 2002. An act has been in place in Queensland for registration of engineers since 1929. Basically the Queensland act regulates the practice of engineering in Queensland with the essence being to protect the health and safety of the community by ensuring that only appropriately qualified and competent people provide engineering services.

It was clearly identified by parliament that it was necessary to have an act in order to protect the health and safety of the community by making sure only competent people provide those services and parliament recognise there is a significant level of risk in the provision of professional engineering services. These include not only risk to the public but also risk of financial loss resulting from construction failure and operating inefficiencies. Those risks exist throughout the whole life cycle of an engineering project from design, construction, production, operation, maintenance, through to the eventual demolition of a project.

There's several examples of recent public disasters, none of which have happened in Queensland, and we believe that is because of the fact we do have a registration system which means only competent people can provide professional engineering services and thereby that mitigates any risk of harm and damage.

MR HARRIS: Thank you for your multiple submissions. It's always a help in this process to get submissions in writing from people so that we can follow up with further analysis. We had this come up in the Melbourne hearings earlier this week from one of the professional officers groups, the same sort of question about registration of engineers and support for the idea of some form of national registration.

I guess the discussion between us rested on the question which, given this is an infrastructure inquiry, it's not an inquiry into every professional standard that might apply across infrastructure, but for us the matter really rests on the degree to which if there is some mandating to take place in our final report of a national standard for engineers, it would be that kind of standard. It would be national in nature rather than what we have currently got, which is, as you have pointed out, Queensland has a legislative based scheme and there are varying schemes in other states which in some cases amount to not a lot.

As a consequence of that, one of the more positive consequences is there is in the case of engineering, unlike in many other professions, relatively little impediment from engineers moving from state to state according to projects, whereas we're quite conscious at the Productivity Commission that there has been a long-term history of standards being used as barriers to entry in markets for professionals moving from one state jurisdiction to another state jurisdiction.

I guess that's the issue we were trying to elaborate on in Melbourne and while it won't be solely the issue that you're interested in, I thought I would start there because it will give us some continuity if you could express a view on the desirability or otherwise from your perspective of there being a single national standard rather than a set of vulcanised standards, as I think we started calling them in the Melbourne discussion.

MR CARR (BPEQ): I think the perceived barrier to entry is just that, a perception. I haven't heard in my professional life anyone talk about as being a barrier to working in Queensland. 25 per cent of the registered engineers reside interstate or overseas. Because you can work under the supervision - and I think that some of the wording in the initial report that I read was incorrect and probably leads to a false impression.

Mandatory registration is a term that's used for different things. In Queensland you either have to be registered or working under the direct supervision of somebody who is, so one registered engineer can supervise up to seven or eight others fairly practically. They can reside in different towns. They can be supervised electronically, over the phone, with occasional meetings. So we don't perceive that - and when I say "we", often I'm talking as an engineer as well - to be a key issue.

The amount of registrations are increasing by 1200 to 1500 a year at the moment. It has been the work of the registrar and the board to go out there and communicate the requirements of the act which the board had previously, prior to 2008, been fairly silent on. As a result of that we're seeing a lot of people getting on board with registrations.

There are a number of different views out there, but the key thing to me is that without a registration scheme or some way of differentiating who is a qualified engineer who continues to develop their skills, anyone can call themself an engineer and provide a service. We don't accept that with airline pilots. We don't accept that with the medical industry. Engineering is talking about the front end of a project, so high quality engineering will prevent what we call, from risk point of view, the low likelihood, high consequence events: when a bridge fails or a road is poorly designed and accidents occur afterwards.

What we seek to do is to have a higher engineering need so the public, who really would find it very difficult to understand who is a competent engineer and who is not if they need to engage one, and that's quite often the domestic building industry - how can they be satisfied that the person that they are engaging or that has built the road that they travel on or the bridge they travel on or the lift - how can they be sure that that person actually knows what they're doing?

We could give you a number of examples where poor engineering practice has led to near fatalities, houses falling apart structurally, a number of emotional consequences, where in Queensland we can hold someone legally to account with our registration scheme, but interstate about the best you could hope for is that somebody is a member of a professional organisation and about the worst they could do is bar their membership.

MR HARRIS: We actually know it does go a little further than that, so in Victoria, for example, if you're a building practitioner there is actually a legal obligation on you, so there are some legal obligations but they are not engineering specific in the way the Queensland legislation is. So we know that there are different approaches in different jurisdictions, but my question to you really was is your advocacy for a national scheme or is your advocacy for a set of state schemes just to ensure that there are some forms of legal qualification that, as you say, mean a person can be held to account for failing to practice appropriately?

That's the reason we're somewhat reluctant, as you have pointed out in your submission and others have pointed out to us - we're somewhat reluctant to mandate the idea of having a registration scheme because of this alternative concern where it has been used in other professions - and this is not a question, therefore, just for engineers. The Productivity Commission does look generally across the economy - has been used as an impediment to the flow of labour between states and the use of qualifications in different jurisdictions.

MS MURRAY (BPEQ): The NERB set up a steering committee, of which I'm a member, for national registration and all the professional associations who are on that NERB steering committee all support basically the Queensland act being rolled out across all of Australia because it is comprehensive registration and it is recognised by all the professional associations that certainly that is what is warranted.

The board is supportive of national registration on the basis it is a comprehensive model, because that has worked very well in Queensland, to allow mobility of workforce, but like we said earlier, the fact is that registration in Queensland is not a bar to working in Queensland. You still can work here but you will need to work under the direct supervision. We have mutual recognition arrangements with other states such as with Victoria, obviously, and Tasmania where people are already registered, so it certainly is not a barrier to labour moving into Queensland.

MR HARRIS: Within Queensland - and we accept - well, I personally accept that there isn't a bar within Queensland. What we're worried about is if we call for a national standard, because this is done jurisdiction by jurisdiction rather than by the Commonwealth because it has no scope to work in this area, we will end up with a multiplicity of jurisdictional differences and those do become barriers to working in one jurisdiction.

MR CARR (BPEQ): That's certainly the case in Canada where you have to register in each province. I think and the board thinks that that would be beyond a lost opportunity. It would be crazy.

MR HARRIS: That's a useful comment, if I could note that.

MR CARR (BPEQ): If the Queensland model works well and that was to be adopted nationally - a number of states have talked about adopting this model - then that would be a way to get through that system so that if you registered in one state, you were automatically recognised in every other state. That's a practical way of going about it if that's what is desired.

MR LINDWALL: Presently if I were a civil engineer, a qualified one, in, say, New South Wales and I wanted to come to Queensland, how difficult would it be for me to obtain registration?

MS MURRAY (BPEQ): If you're already registered with the New South Wales Building Practitioners Board, then you could apply for mutual recognition and that can happen within two weeks. If not, you need to go through the assessment process like any other person and then that can only take three months maximum, depending on - - -

MR CARR (BPEQ): If you were already a chartered professional with Engineers Australia, then the system would be quite easy to work through.

MR LINDWALL: Yes, and normally the people who are registered are also members of a professional association, I guess?

MR CARR (BPEQ): You don't need to be. With the freedom of association laws, anyone can go to Engineers Australia or AusIMM or any of the assessing entities that assesses their particular engineering and pay a fee and be assessed. They do use the same schemes that we use for the chartered professional system. When I say "we", I'm also involved in the AusIMM system.

MR LINDWALL: How do you deregister an individual who has misbehaved or performed poorly or something like that?

MS MURRAY (BPEQ): We can deregister people on health grounds, when they're not physically capable of carrying out engineering work. Otherwise in other instances where it's actually poor performance, we have to go to Queensland Commercial and Administrative Tribunal and then we apply for deregistration. We are at the whim of the member who is sitting, but we do have some cases at the moment where there was one engineer who certified hydraulic equipment being brought into Queensland, certified it as actually complying with Australian standards when it didn't. It collapsed and nearly killed a young mechanic. That person the board is seeking to have deregistered. That person also bought that equipment into New South Wales and there's very little they can do in New South Wales, but we will be able to stop that person working here in Queensland.

So we're sure that we should be able to get him deregistered but with court systems, we are at the whim but we certainly apply when there has been work to a very poor standard for deregistration.

MR LINDWALL: So you're not claiming that registration per se would prevent accidents and bad behaviour. It would discourage the repeat of that I guess because if someone is registered who has a good record in the past would probably be registered and then if they act in a particular job in a substandard way and that causes a major catastrophe, that person is still registered.

MR CARR (BPEQ): But if I could go back. The original point is that you have to demonstrate that you are competent to be registered in the first place. There are a number of people out there who like to call themselves engineers who are not qualified or don't practise enough or don't do professional development and their skills deteriorate or they may not have been qualified in the first place. The first thing this legislation seeks to do is to not let them be registered. Then there's the disciplinary section after that.

MS MURRAY (BPEQ): Yes, but the thing is about registration, it means that you're mandating minimum qualifications and minimum competency which is normally a four-year engineering degree and at least five years postgraduate engineering experience. There's no way, it would be unrealistic to say, that either the Board of Engineers or the Medical Board can ever guarantee that someone once they're registered will be competent for the rest of their life. We don't know where their life and their attitude to work is going to take them.

MR CARR (BPEQ): Exactly.

MS MURRAY (BPEQ): However, the fact is by having a registration system means we can weed out the bad eggs which in other states they're a lot more limited.

MR HARRIS: I see your basic point without a doubt. You referred to a working group I think that was looking at this question of some kind of national acceptance arrangement, so forgive me if it's already in one of your submissions but I don't recall the name.

MS MURRAY (BPEQ): No, it's not. It's the NERB which is made up of Engineers Australia, Consult Australia, Professionals Australia and IPWEA, engineers in local government. They formed a steering committee, of which I'm part of, to look at national registration.

MR HARRIS: Could you perhaps just send us that even by email as a contribution further which says, "This entity is working on the idea," because clearly is we are to go down this path, I think we want to go a bit further than just endorsing a principle because that's the great danger here; that you endorse a principle and leave it to a set of differing jurisdictions to pursue it in differing ways at differing points in time, and you end up with the kind of outcome that has I think, or we envisage could be quite a problem.

The net benefit that might otherwise result from this, in terms of ensuring that better qualified people are the only people allowed to practise or appropriately qualified people are the only people allowed to practise, might become a disbenefit if it becomes a prevention from people moving from one jurisdiction to another, but if you've got a working group on the subject I think that would help us to look at this, "How would you do it?" kind of aspect to this issue which is just as important, I think, as "What would you do?"

MS MURRAY (BPEQ): Yes. I'll send that through.

DR MUNDY: Could I just ask you a couple of questions. It relates to item 3, the Benefits of Mandating Registration. You draw attention to a number of tragic incidents, Piles Creek culvert, the Westralia, the West Gate Bridge collapse. I don't expect you have these documents in front of you but I would be interested if you had any views in relation to the Piles Creek matter, the views expressed by the New South Wales coroner in that where it didn't appear to be that the sole cause was an engineering matter and, indeed, the royal commission of the West Gate Bridge failure and the commission inquiry into the HMAS Westralia because I think the story is a bit more complex than that. But I'd just like to bring you to another matter which is in Queensland, and that is the failure of the bund in Gladstone Harbour which has led to the federal minister for the environment having to order an inquiry into the potential damage to the Great Barrier Reef Marine Park. Abigroup, I understand, undertook this work. Would that work have been undertaken and supervised by an engineer registered by yourselves?

MS MURRAY (BPEQ): It should have been. The engineering workwise, yes, it definitely should have been. We understand there's different views on that inquiry, so it's going to be interesting to see what information comes out. We've certainly received some.

DR MUNDY: But I guess my point is: here is an example where the bund wall has clearly failed. It's likely that the work would have been supervised by a professional engineer and the consequence to the environment have been significant.

MS MURRAY (BPEQ): Yes.

DR MUNDY: It's a bit like an aircraft incident, pilots are registered but plane crashes still happen. So I'm interested in the contributory nature of this claim because it does seem on bald face that you're suggesting that, for example, the West Gate Bridge collapse, where there were a number of highly qualified engineers who weren't registered precisely per se, perhaps because registration wasn't available in Victoria in the 70s - but I think we need to properly understand what this issue is. I very much doubt whether the Public Works Department of Victoria at the time would have not been concerned about the capability, so I'm just interested in: where does this get us? Is it a process that enables us to have a baseline of assurity, accepting that things still go wrong, of medical practitioners are done for malpractice.

MS MURRAY (BPEQ): That's right.

DR MUNDY: Gladstone seems to pop to mind again but I'm interested in a couple of those cases which you've raised. If you'd like to reflect and come back to us in just a couple of paragraphs on what others have said, and with the greatest of respect, I suspect the royal commission into the West Gate Bridge collapse and the coroner in New South Wales will perhaps have brought their minds to these matters in somewhat more detail than you might have.

MS MURRAY (BPEQ): For example, the Canberra Hospital implosion, the coroner there said, "We must have this person, this engineer deregistered," and was horrified to find out that there was no registration system, so the fact is nothing could be done.

DR MUNDY: Yes.

MS MURRAY (BPEQ): The board is actually watching what is happening with Gladstone with the federal inquiry. Certainly we're very aware of that.

DR MUNDY: In the case of the Gladstone matter, in the event that it was - it could have been faulty materials. It could have been anything.

MS MURRAY (BPEQ): Yes.

DR MUNDY: It's prudent to wait for this federal inquiry to be concluded. What process will you go through once those facts become available. I'm not expecting you to prejudge the matter or facts.

MS MURRAY (BPEQ): Yes. If it turns out that there is an engineering issue which is all the board is concerned about then the board will certainly write to the organisations, engineers, involved and ask for an explanation. The board will consider that along with the other information which is gathered by the federal inquiry. If it has got concerns about the level of engineering and the fact that whether or not there was actually proper supervision, if anyone was working on it unregistered, the board will then appoint an investigator who will be an expert in that particular type of engineering to look into the matter.

That investigator will bring a report back to the board and the board will then make a determination. It will then have several options. If the people were unregistered, it will prosecute. If the people are registered and the investigation report shows that there are unsatisfactory professional conduct issues then it will actually take the matter to QCAT where we're obliged to do them..

MR CARR (BPEQ): An alternative is that if somebody lays a complaint about an engineer, a specific complaint, then we may also go through the same process.

DR MUNDY: Presumably the Port of Gladstone and the minister for the environment will have the normal legal avenues available to them under the relevant statutes to deal with contractors and things like that. I just wanted to come back and it was just a tonal thing in your explanation but I take it you are comfortably with the two-phase process where you have to make your case out to QCAT.

Is that something you're comfortable with or is it your view that, and this is a wider question for a national body, if there was a national registration scheme should people who are about to be deregistered be subject to just a determination by the registration body, or should they have to bring that matter to an independent tribunal, such as QCAT or if it was a Commonwealth matter, if there was a Commonwealth registration, presumably the AAT as is the case with pilots' licences or licence for aviation engineers? I just got the sense that you had some frustration in QCAT.

I'm a presiding commissioner on an Access to Justice in Courts. I've got tribunals in my head at the moment but I'm just interested about what the process for deregistration in your mind should be. Should it be something that needs to be put before an administrative or judicial officer or is it something that you believe you should have the power to do yourselves?

MS MURRAY (BPEQ):   I actually do think it should go to - it ends up being my personal point as view - an independent tribunal; that's a matter of ensuring that the people who sit on that tribunal will actually have the appropriate qualifications and competency to hear matters, and engineering is complex.

DR MUNDY: As is aircraft engineering.

MS MURRAY (BEPQ):   Yes.

DR MUNDY: And the AAT seems to be able to be able to deal with these matters.

MR CARR (BPEQ):   Potentially, with natural justice, there needs to be checks and balances and separation of power. I do think that it would be useful if there were a panel of experts that could be made available to the commissioner.

MR LINDWALL: May I ask how long it is between you taking a case to the tribunal and a determination being made, and can an engineer be continuing to practice in between those two periods?

MS MURRAY (BEPQ):   Yes, the engineer can continue to practice, and the period can sometimes easily be 12 months before the matter is finally heard, and that's when lawyers get involved.

DR MUNDY: So you have got no capacity to suspend pending - - -

MS MURRAY (BEPQ):   No.

DR MUNDY: Would you like it? Not in - but in extreme cases.

MS MURRAY (BEPQ):   In extreme cases, yes, that would be very worthwhile, but we don't have a - - -

MR LINDWALL: Did you want to ask anything about skills shortages in engineering?

MS MURRAY (BEPQ):   No, there isn't a skills shortage at the moment. With the decline in the economy, a lot of engineers have been made redundant.

MR CARR (BPEQ):   I would like to make an observation, if I may. I was one of those engineers who was recently made redundant. I was trying to deliver a project, an underground mine, and we saw first-hand the skills shortage. It didn't manifest itself the way that I read in the text of your report. What we found was that there were a number of inexperienced engineers who were over-specifying things to make up for it. I will give you an example of an underground excavation, 140 MPa rock, if that means anything to you, four or five times the strength of concrete, and he wanted this massive slab of 32 MPa concrete, because he didn't trust the rock. I had a number of discussions with him, but he wouldn't change his mind.

I could give you a number of examples about that. So we, as the client, pay a lot of money for these guys to design this stuff and a lot of money and materials to construct it for little good purpose, and then the other part of the skills shortage is with so many supervisors and work crews out there, that the supervisors come from a less and less experienced pool, and on the job they forget to bring certain materials, they don't check that all the risk assessments are done, and it is delay after delay after delay through lack of organisation, basically through a lack of experience. So if you have got three or four times the construction people working at the moment than what we had 10 years ago, the pool of experienced supervisors is dragged so thin, and that's not readily apparent. There are people in every job, but they are not working effectively.

MR HARRIS: Yes, but it's hard to create experience, isn't it?

MR CARR (BPEQ): I don't know anyone who was born with experience. A few guys have told me that had it, but - - -

MR HARRIS: That's the thing and there's no course for experience, so - - -

MR CARR (BPEQ): No, it does take time. These days, with risk assessments and procedures, we can use a lot of systems to help, but there is nothing like personal judgment. That's an area that I've found it would be very hard to put a number on, but it's very real.

MR HARRIS: We have had a number of submissions that talk about this pipeline effect for projects in order to encourage continuity of employment and therefore as a consequence of that to ensure it was a continuous supply of trained expertise, which would certainly cover engineering skills, but it's obviously meant to be wider than that. The difficulty is, who will choose to be where in the pipeline and who will tell somebody that as a consequence of us rather having a smooth supply rather a bunchy of highly cyclical investments, whether your LNG plant should wait for somebody else's LNG plant to ensure there's enough skill base available. It is a reasonably problematic area, nevertheless it is in front of us, and so we will try and deal with that as well.

MR CARR (BPEQ): It's probably as much as the person funding it saying who is going to go first, rather than the people who are going to build it.

MR HARRIS: When it comes to public infrastructure, governments therefore are often the primary funder, and therefore have some capacity to scope projects; and then there's the question of the competition between, again, the jurisdictions and the states.

MR CARR (BPEQ): It is a key risk as a project proponent, trying to build your project when you know a lot of others are being built at the same time. It is a key risk, particularly in very specialist skills.

MR HARRIS: Yes, and presumably delay factors when you lose somebody because they have been poached by another project and you have got to stand down certain parts of functionality until you can replace that particular core skill.

MR CARR (BPEQ): Completion bonuses and all sorts cost tools that come in.

DR MUNDY: Can I just bring you back to the point you made about risk aversion on the part of young engineers, inexperienced engineers at least, and perhaps put it in a different context. The commission regularly hears about risk aversion on the part of regulators. The commission has a very strong view that regulators should adopt a risk management approach to their activities. In the event that there's a problem or an incident where there is always a potential that engineering works will fail or go wrong, and not because someone is being negligent, but because risk management means there's a non-zero likelihood of something going wrong. How do you as a regulator think through that sort of circumspect? I mean, Gladstone could well be a case, particularly in complex environments where geotechnical circumstances are - underground mining, I suspect, is another one. You can't ever know everything.

MS MURRAY (BEPQ): No.

DR MUNDY: I'm just interested in how you as a regulator think about those circumstances.

MS MURRAY (BEPQ): What we do is, when a matter comes to our attention we appoint an investigator. That investigator is an expert. What the do is they sit I the shoes of the engineer with information that they had at the time and say, "Is what they did of a lesser standard than would be reasonable basically in the circumstances by their peers?" So that's how we judge it, because we recognise there's a lot of - - -

DR MUNDY: So your expert would have done the same thing, then you're satisfied that - if you're satisfied that the engineer did the right thing, the fact that - these things could be horrible, no doubt, for the individual concerned.

MR CARR (BPEQ):   An additional test might be, "Did he act on the information he had, or ought he or she have been more diligent in getting further information?" but it's a guess the equivalent of the reasonable person test, was that behaviour reasonable on a peer basis?

DR MUNDY: Thank you.

MR HARRIS: Okay, so I think that's as much as we had for you. Is there anything that we have missed that I would like to cover off?

MS MURRAY (BPEQ):   Did you read my paragraph about impact assessments, the fact that in the report you were of the view that perhaps there hadn't been an impact assessment of the Queensland registration system, in fact there was.

MR HARRIS: We read your statement and we know of three reports actually that have been, not just the one that we had specified from PWC, but we know of three.

MS MURRAY (BPEQ):   Yes.

MR HARRIS: Our problem is in no case was there actually a test made of the benefit versus the counter-factual, in other words what might have happened otherwise; so in a number of them it was assumed that there would be a benefit, a number of the studies. That said, we will be offering that reference in the light of the information you provided. For a start, we went and discovered not just the one that you discovered, but we discovered two others; so we know that there have been assessments made.

MS MURRAY (BPEQ):   Okay.

MR HARRIS: Our problem, it's the one I alluded to at the outset, has always been, at the commissioner level anyway, concern that, generally speaking, professional qualifications have been used not just to ensure that it's only the properly qualified people who practise, they have also been used to restrict labour markets and, generally, we have tried as a commission, over many reports, to discourage that kind of behaviour and historically we have been reasonably unsuccessful, but we persist. In this particular case, were we to do the reverse and alight upon a standard that ought to be imposed, we would certainly be, I think, collectively pretty keen to make sure that it was done in a way that didn't prevent labour skill moving from one jurisdiction to another.

MS MURRAY (BPEQ): Yes, and I think the fact that 25 per cent of our RPQs reside interstate or overseas just shows that that is not a barrier for Queensland.

MR HARRIS: I don't think we doubt Queensland's behaviour. What we doubt is, perhaps, other behaviours.

MR CARR (BPEQ): I fully agree with what you have said. Our intention is to have high-quality engineering and a system that didn't work that way, was dysfunctional, would be a barrier to that, so we would like to see, if it goes forward, to be a practical solution that suits everyone's needs.

MR HARRIS: Which is why, if you can tell us about this working group, we may be able to incorporate something it as well. Okay. Thank you very much for your time today, we really appreciate it.

MR CARR (BPEQ): Thank you.

MR HARRIS: I think, Mr Wallader, are you next up? Please take your microphone. Could you perhaps identify yourself for the transcript.

MR WALLANDER (IFO): Yes. My name is William David Wallander, director of the company Infrastructure Financial Opportunity. We have a product that has been looked at by a few in the Australian area but it has been a 30-year-old concept overseas. My experience is that I was with the Bank of New South Wales and resigned from a level of management some years ago and I have kept my interest up to date. The concept of the financial package that we have come forward with is based on an old taxation ruling, IT 2495, which the Taxation Department brought forward to me, which included the administration of a debt deficiency arrangement. I can elaborate on that later on, if you want.

The history is that the taxation ruling had an effect on the market and it was followed to a point where I wrote a thesis on it and officially cited by ASIC in 1997. I met with the trading platform in the area involving the concept of trading and discounting paper in Europe. However, the level of trading under the minimum entry was US 500 million in the mid-90s, far too large for the Australian market. I kept in touch with the group and then only last year have been given the authority to reduce the level to a minimum trade of 150 million but the preferred minimum level is 200 million. We originally were unable to assist the government of the day due to the fact of their association with the World Bank, IMF and Federal Reserve, because of the fact that governments of the world are supported by these authorities financially and a conflict of interest may come to pass.

Therefore, the trading platform were only interested in the private enterprise to be joined in any financial opportunity. I negotiated again with the trading platform on the fact that our governments within Australia, be they federal or state, were in desperate financial need to keep up with the support needed for financial infrastructure, et cetera. However, they were quite adamant that no financial gain could be considered at any level of military activity. As it may be seen, the supporting financing advanced. Therefore, a further concept was placed before the trading group, as the government of the day do not in most case build the infrastructure; hence the concept was placed before them based on the introduction of the major infrastructure contractors to participate in trade for the benefit of assisting the development of the country, not only here in Australia but where the trading platform is considered worthy of assistance and where the position could be brought into a benefit.

The trade benefit is a contract between two parties; the trade platform who has the trade on a cash basis and can only enter legally into a trade to benefit the growth and employment of the country. The trade platform is not a developer of a project, hence offering a joint venture arrangement between a worthy party who has the backing of substantial assets of their own, a joint venture arrangement brought together for the benefit of creating a profit from a trade of financial commodities within the financial system, a practice that is many years old within the financial system. Our trading platform has been involved in this for more than 30 years. The system is secure, strictly ordered by the world financial compliance authorities at all times within the contract period.

A letter I wrote to the infrastructure commissioner nominates that the concept becomes a debt free opportunity for the government. It's a secure financial opportunity to be considered, focusing on the growth of employment and ensuring participating parties within it are financially rewarded and the awardees are the major infrastructure contractor - he is not doing it for nothing - the major infrastructure contractor's bank - there is a profit area there for them - and the government at federal and state level which, if accepted, could get a majority of the projects built at no cost to the government. It's all done with a guarantee by the infrastructure people who would have to come forward with a bank guarantee based in their own name; their own name not transferable into the trading group. A joint venture arrangement is made and the profits are effectively split fifty-fifty.

It's a financial opportunity, subject to the ordering of the financial compliance authorities which I have just mentioned, which include the World Bank, the International Monetary Fund and the Federal Reserve. The financial opportunity is not subject to currency fluctuations, fluctuation risk, any current fluctuation interest rate or risk of any world stock exchange. The opportunity is considered to be an opportunity above general banking of today, not known too much within the banking arrangements of today. They do it themselves internally, so my presentation really refers back to what is in my presentation per se and where it will affect the government is being able to fund up a lot of infrastructure debt free to the government, if the contractor is willing to participate for a percentage gain. Also the banker receives and will receive a profit margin out of the funding, once you understand how the concept comes into place.

MR HARRIS: So can you explain to me in a cash sense who puts up the money.

MR WALLANDER (IFO): I beg your pardon?

MR HARRIS: In a cash sense, who puts up the money?

MR WALLANDER (IFO): It's the banker overseas. It's the major bank overseas who has a licence to trade and the cash - - -

MR LINDWALL: A licence with the Australian Prudential Regulation Authority.

MR WALLANDER (IFO): A licence to trade within banking instruments on a discount rate. The bank can buy a letter of credit, as I have nominated in my submission, at a discount of 2 to 20 per cent. That's buying a letter of credit to fund up different aspects within banking for the smaller guy, the fellow that imports. From that, what this group do is they buy and sell this particular product, so what they are turning is a letter of credit for trade into a commodity within banking and that's where your profit margin is and that's why such a large profit margin. As you know or would know that commodity trading is very profitable in various aspects.

MR HARRIS: Okay, so - - -

MR WALLANDER (IFO): So what it comes back to is, is the contractor able to support it and is the banker able to support it, so if they want a contract to the government to do a infrastructure project. The government have nothing to do with it at all.

MR LINDWALL: So what are the barriers to this not occurring as at present? What is the barrier to stop it happening now?

MR WALLANDER (IFO): There is nothing.

MR LINDWALL: So why doesn't it occur?

MR WALLANDER (IFO): There is nothing at all. The barriers were that we couldn't do anything for the government because of them being associated with the World Bank and the requirements of the World Bank. It is bringing in a third party - - -

DR MUNDY: Sorry, can I stop you there? Specifically what requirements of the World Bank are we talking bank? To my understanding of the international arrangements, the World Bank isn't central to the international regulatory structure. That is more an issue for other international entities.

MR WALLADER (IFO): That's right. The simplicity of it is - - -

DR MUNDY: Sorry, I do want to understand precisely. What World Bank requirements are you actually talking about, because it is within our capability to make recommendations to the government that it should, as a shareholder of the World Bank, make representations to the other shareholders that these arrangements should be relaxed and indeed that is part of the G20 infrastructure agenda that the treasurer was trying to advance. So it would help us profoundly if you could identify for us with some precision those World Bank requirements that you say are in issue. I am happy for you to take that on notice and come back to us.

MR WALLADER (IFO): I will.

DR MUNDY: But if you say there is a barrier being created through an international arrangement, then it is well within the capability and duty of this commission to make representations to the government to fix it, but without knowledge of what it is, because frankly I don't know what it is - - -

MR WALLADER (IFO): I would have to take it back to the group, sir.

DR MUNDY: Okay. That would be very helpful.

MR WALLADER (IFO): I am willing to do that. It's the simplicity of a bank issuing a guarantee. That guarantee is issued to the contractor in his own name, not transferable in value. It is only confirming that that contractor does have an asset base for the trading platform to support such a transaction. We are talking quite large amounts and effectively we don't just take the word from their balance sheets that they have got whatever. It's the banker coming forward with a guarantee in the contractor's name that is not transferable in value. It is transferable in information but it is not transferable in value, because the trading group does not take security over the asset.

MR LINDWALL: Where do risks lie in terms of things such as exchange rate risk?

MR WALLADER (IFO): It doesn't come into it - no exchange rate risk.

MR HARRIS: How does that happen?

MR WALLADER (IFO): Because it is all done in US dollars. Effectively we are buying and selling a commodity. We are not up and down a commodity purchase.

MR HARRIS: But if the project is in a country where the contract is not paid in US dollars, then you do have an exchange rate risk, don't you?

MR WALLADER (IFO): The contractor will receive the benefit of a profit from the trading group buying and selling within the parameters of what he is allowed to sell under his licence. It's a profit split. It is nothing to do with borrowing. There are no loans involved.

MR HARRIS: I can see that I think. You have got a trading entity which is holding the financial value of this asset but a contractor is creating the asset. If he is creating it in a country where his employees are not paid in US dollars, then there is naturally a currency risk there. There must be some kind of risk that had to be hedged. Otherwise every week he pays a bunch of salaries. Where does he get the money from? I am trying to make this model work in a cash sense. I am sure you can create a lot of financial trading models between various parties in a finance system but we are the infrastructure inquiry and we are only interested in financing things where something is actually built, so we need the built bit of the financing system to work as well as the - - -

MR WALLADER (IFO): I fully understand that.

MR HARRIS: I am trying to work out - when you say there is no currency risk, can you tell me? I can't see how an exchange doesn't take place at some point between the currency in which the financier has provided his guarantee and the currency in which a contractor is paying his employees. That has got to be inherent somewhere.

MR WALLADER (IFO): The guarantee is only a confirmation of the party asset base. It is not secured. They don't take security over that guarantee. They don't transfer the value of the guarantee. It is a method of confirming through their bankers that they do have such an asset base and it becomes a contingent liability to the bank. It becomes a contingent liability to the client; therefore, no interfering with any of their cash flow locally.

MR HARRIS: But it is just a pure financing instrument then. It is not actually concerned with whether something is built or not.

MR WALLADER (IFO): The concern is - - -

MR HARRIS: What I am trying to work out is who pays the contractor then? Can you tell me that?

MR WALLADER (IFO): Who receives the funds?

MR HARRIS: Who pays the contractor?

MR WALLADER (IFO): The contractors receive profits from the trade which go directly to them to pay their infrastructure. They have to apply 80 per cent of that profit to that infrastructure project, of which 20 per cent can be retained for them to cover any other costs and to enhance their business.

MR HARRIS: So would it be correct in saying that this is actually then a subsidy from a finance arbitrage opportunity? Is that correct?

MR WALLADER (IFO): A subsidy?

MR HARRIS: A subsidy, a payment to the contractor from a financial arbitrage opportunity. Is that what you are describing?

MR WALLADER (IFO): The profits that come back from the trading group to the contractor are and earn a profit which they have to pay tax on. It is nothing to do with any loans. It is nothing to do with any risk factor at all within the currency.

MR LINDWALL: So where is the profit created then if there is no risk, there is no activity?

MR WALLADER (IFO): Where is the profit?

MR LINDWALL: There must be arbitrage. I can't see any other source of profit opportunity.

MR WALLADER (IFO): It's simple. Just say you wish to import something from China and you wanted $100,000 worth of goods from China. You have to go to your bank to get them to issue a letter of credit. That letter of credit becomes conditional on what you are supplying, colour, whatever, free on board - whatever. You have to in Australia put up a bank guarantee to support that $100,000 letter of credit. I receive it in China and I am the manufacturer. In China I don't have the financial facilities like we do here in Australia where I can buy the raw material. I go to my bank in China and I ask the group over there will they support a loan against this order, against this letter of credit, and they can't. The letter of credit is in my name. It is not in my bank's name over there.

The bank, under the facility, actually will work out the profit structure that I have. Then they will purchase that letter of credit. It becomes a commodity at a discount. Therefore I say to my bank, "I'm going to make 30 per cent profit out of this job." The bank will say, "Look, you're not going to make that this time. We will put $85,000 in your account today. We're going to buy it at a discount of 15 per cent." The bank now has the letter of credit. That letter of credit becomes a commodity. That profit is where it is split between the major contractor and the bank that comes back to finance the major building. Multiply it by $200 million. We are only talking a hundred thousand.

DR MUNDY: What happens when the letters of credit are exercised, which they must be, because they are effectively an insurance policy? There must be some likelihood of letters of credit being exercised.

MR WALLADER (IFO): A letter of credit can be bought and sold by banks, right down to superannuation funds.

DR MUNDY: I am fully aware of what you can do with letters of credit but letters of credit are also exercised upon banks in the event that the party involved does not make good. It is a form of insurance, so there must be risk involved, and also the banks doing the issuing must be providing capital against the letters of credit which they write or accept because otherwise they are just basically saying, "We will guarantee someone's activity," and not provide capital for it.

The prudential regulators will not wear that and indeed it is likely, and we have had significant evidence, that the Basel III capital requirements that are being tightened are making guarantee products or the acceptance of lower grade credit risk even more difficult. At some point these things are not costless because they come at a cost, if nothing else through the provision of capital on bank balance sheets surely.

MR WALLADER (IFO): You are not saying that a letter of credit bought and sold becomes a commodity.

DR MUNDY: It depends on what your definition of a commodity is.

MR WALLADER (IFO): A commodity is buying something and selling it for a profit.

DR MUNDY: No.

MR WALLADER (IFO): Or making a gain out of it.

DR MUNDY: Sorry. You have just explained to me what a noun is by definition of a verb, so I am not sure that can be right. The fact that a letter of credit remains a claim on a financial institution to perform - that is why people seek letters of credit - - -

MR WALLADER (IFO): That's right.

DR MUNDY: - - - because their customers are not as creditworthy as the bank, but the bank must provide capital for the letter of credit, as do other forms of insurers, as does the Australian Export Finance Corporation.

MR WALLADER (IFO): The client has to provide security to issue that letter of credit in the beginning.

MR LINDWALL: So you think that the letter of credit can be issued ad infinitum effectively; that banks can continue issuing letters of credit at in effect infinite levels without any effect on the financial system. It is like printing money, isn't it? It is going to be inflationary.

MR WALLADER (IFO): I can't quite hear you, sir.

MR LINDWALL: How many letters of credit can be issued?

MR WALLADER (IFO): How many letters of credit?

MR LINDWALL: Yes.

MR WALLADER (IFO): That's an issue between banks on their limitation. They have got a limitation on how much they can do between branches and banks and mainly between banks. They have got a limit as well, just like you might have a limit on your overdraft. They have got a limit on what they can supply to particular banks overseas and then if that limit is there, they can't issue and, say, increase that limit. It's the same thing as you having an overdraft in your bank account. You have got to get permission to increase or trade within your requirements.

MR LINDWALL: So you think that the biggest constraint are these World Bank rules that you were mentioning earlier?

MR WALLADER (IFO): The World Bank doesn't do the trade.

MR LINDWALL: That is the barrier that you are talking about.

MR WALLADER (IFO): The trading group does the trading. They are limited and they are under instructions of what they can do within trading. They can't just go out and do a trade for the love of it and make cash for nothing. They have to support infrastructure, employment and something, except anything to do with the army, navy - - -

MR LINDWALL: And air force.

MR WALLADER (IFO): - - - and air force or any arms. They will do anything else but they can't do anything like that.

MR LINDWALL: I don't have any more questions.

MR HARRIS: Warren, do you have anything else?

DR MUNDY: No. I am done.

MR HARRIS: You have given us a large proposal here which we are also going to have to go through at some depth. Do we have a contact for you if we need to get back to you?

MR WALLADER (IFO): You do have, and the submission is up on the file as well.

MR HARRIS: That is great. Thank you very much for your time today.

DR MUNDY: Thank you.

MR HARRIS: I think we go to the phone next. Is that right? We are a bit early. We will take a five-minute break for everybody. It will only be five minutes while we ensure that we can get the people from the CFMEU on the phone.

MR HARRIS: All right. Dave, with the logistics of phones being such fun, do you want to do any opening remarks? I have been through your submission and so have the others, so if there are some basic things you want to have recorded for the transcript, now is probably the time to list them, otherwise we can ask you questions and go from there.

MR NOONAN (CFMEU): We might just state a couple of brief things. They do I think in general reflect some of our comments in the response to the draft. I should also say I do need to finish by about 10 to 12.

MR HARRIS: You tell us when you're ready to go, so we just hear the beeps then, but just give us 30 seconds notice.

MR NOONAN (CFMEU): One of the major things we have commented on here is where the draft report focuses on a number of matters in relation to industrial relations, and generally we have forcefully put the view that the comments or recommendations in the draft report are not borne out or supported by data or at least by any data that's known to us or replicated in the report. In particular in relation to the Victorian Construction Code we make the point that this is not an economic blueprint to improve productivity. It's a political document which is substantially designed around an ideological view of reducing trade union influence on construction sites.

We can all have a view about whether that is itself a desirable public good or not and you won't be surprised what my view is, and I probably don't need to recount it but to the extent other people have that view, that's fine. What we would say in relation to an important report of the Productivity Commission is that we ought to be dealing with propositions that are supported by some data or some solid analysis and we don't see that thus far in the draft report.

Just for the record, there are a number of other submissions which calls for the Productivity Commission for the reintroduction of the ABCC. Again, you know, that's really a value judgment about industrial relations, in our view, rather than a proposition which is supported by any hard data in respect of productivity. We do, as most people do, most rational people, concur with the comments that the Productivity Commission's draft report made about the failings of the Econtech or whatever they are called now, Economics Are Us or Econometrics Are Us or something like that. We concur with the dismissal of their voodoo sites or voodoo economics.

There are a number of comments about enterprise agreements and we just made the comment there seems to be almost two views here, one is the report at some point is critical of the similarities that exist within and are practised within the sector and obviously there are some similarities. But then there's an attempt to find reason for differences in wages and conditions (indistinct) and we don't think that there is a consistent approach. In that (indistinct) I think that (indistinct) are problematic (indistinct) attempt to (indistinct) and dissect what their (indistinct) in wages and agreements and so on. We point out that the wages and conditions in various agreements are generally reflective of the economic activity in the sector. They also differ very dramatically by region and by the type of project.

There has also been a substantial increase from 1999 to 2014 in the entire workforce of construction of around 70 per cent - 613,000 to 1.037 million - double the increase of the total Australian workforce over the same period. We believe that it's probable that that's going to have some impact on aggregate wage outcomes. The other thing here is that there is I think a suggestion that these enterprise bargaining outcomes are overly generous. Again I suggest that there is some subjectivity in such an assessment. For example, whilst I have met with Mr Tyrwhitt lately of Leightons a number of times - you know, I think he received 14 and a half million dollars or something like that in redundancy. I might regard that as overly generous but I think that we need to come to terms with a couple of things.

There was, rightly or wrongly, through the 1990s and onwards a shift from centralised wage fixing across all industries to enterprise bargaining and bargaining rules are not generally constrained by centralised government policy that tries to set minimum or maximum wage outcomes through that bargaining process. That means that then the market is so hot, as it undoubtedly has in parts of construction over the last few years, the wage outcomes will move upwards.

I think that you will have seen perhaps some reporting in The Financial Review and The Australian this week about some negotiations which are on foot in the construction industry in Western Australia at the moment involving our union. They are not complete negotiations but it is the case that there are negotiations going on for agreements which will be more moderate than those that have existed on some large capital city construction sites.

Our state secretary was quoted that it is a fact that that is reflected by the fact that the heat is coming out of the capital expenditure phase of the resources construction boom and, of course, we are now moving away from that very labour and capital intensive phase of the resources boom into one where the projects are largely - or not all but substantially being completed and moving into production.

Turning to the issue of greenfield agreements, there seems to be an assumption that greenfield agreements are created or demanded or solely the desire of unions. I point out that greenfield agreements have been a feature of major projects for many, many years but our experience is that greenfield agreements generally exist in the major resource projects. They're not commonly used in building and construction. They're used to some extent in road and rail infrastructure but not exclusively. The demand for greenfield agreements often comes from clients of the resources sector who want to be able to prevent their expenditure or their labour costs over very large projects and often over four or five-year sites.

We make a range of comments about productivity and Mr Maxwell might want to supplement what I say there but I think it is a notorious productivity, one productivity that can be very difficult to measure. International comparisons are fraught with problems like conditions that have a dramatic effect on projects and so on. I would say that the trend of productivity, the growth of productivity in Australia, in particular in the construction industry - Australia has tracked closely with the market sector in the last 15 years.

One thing that I think isn't commonly referred to in relation to what we don't deny - in fact we're quite proud of the union - is the fact that we have a high wage economy in the construction industry in Australia. It is our observation on the sites it's actually employers investing in plant and equipment and innovation which has the effect of relatively less labour but it's our contention that those investments and innovations in plant and equipment actually drive productivity much more quickly than intensification of labour exploitation.

We do remain committed to a productive construction industry. We think it's important we do this in the interests of working people in the industry as well, but we are not ever going to be supportive, it won't surprise you to hear if they race to the bottom when wages and conditions are driven down or indeed where what might be strongly and legitimately held views about the role of unions in society of the workplace are provided by arguments that somehow this promotes productivity where it's not supported by hard facts and data. So they are a couple of opening comments. I don't know if Stuart wishes to say any more but perhaps it's useful if we give you some time to, you know, challenge us or talk to us or ask questions and we're happy to do that.

MR HARRIS: No, fair enough. The first thing I would like to say here is we appreciate you putting in a substantial submission. There is - how can I put it - always limitation on the knowledge that we have which can come from the desktop work that we will undertake which we try to make as comprehensive as possible, but there is a limit to what you can actually access via desktop type resources and the rest of our information basically comes from submissions. So getting a submission from you on a comprehensive kind of basis like this is pretty useful.

I just want to start out if I could with EBAs because I want to extend the comment I just made so it just doesn't sound like some kind of platitude. We picked a number of EBAs to go and look at and you've made comments saying you think that they were poor examples or that their analysis was poor and we take the challenge in that so what I think we'd like to be able to do is to obtain a better analysis from you. This is not a question of going through I think you mentioned 35,000 since some time in the 90s and clearly we select what we can select of the current group but I think I'm going to take it from the remarks that you had made in a number of places about these things, so this is not just on wage rates and whether they're overly generous or not but conditions and allowances and big disparities that seem to occur and also training arrangements.

Each of those I reckon you could probably help us with some further analysis of EBAs on. So it wasn't just a platitude at the start, saying we appreciate the comments you've made because some of them will be incorporated and be useful in the current form they're in. But in that EBA area I think there's quite a bit more scope for you to eventually potentially provide us with some advice which would be useful to get.

MR NOONAN (CFMEU): We'd be happy to come back to you with some further comments. Perhaps to give you some idea of the scale of my office at the moment which is that I've got one industrial officer and two legal officers for some administrative support. We also, you might have heard, are subject to a royal commission at the moment and a fairly extensive notice to produce from that commission, I think seven years' worth of documents. The reason I raise that is not to ask for sympathy but just to point out that whilst we will come back to you with some further stuff, we're just a bit strapped for resources at the moment.

MR HARRIS: Yes, we understand.

MR NOONAN (CFMEU): While we're a pretty big union, most of our resources lie in the branches.

MR HARRIS: We understand, but nevertheless I just want to make something of that because there is value in what you've already submitted but we think we can probably extract a bit more and if we can't we'll take what we can get, that's the nature of things.

MR NOONAN (CFMEU): Yes.

MR HARRIS: Before I ask the others to open up, because with the phone I think I'm going to probably run through mine, all of mine as a collective, Warren and Paul, and you each do this. So on the code, we understand your position. We don't necessarily accept every statement that you've made but I don't need to rehearse our judgment said in this area. We did have representations from the ETU in Melbourne the other day on a not dissimilar basis that said basically that code is not productivity enhancing.

What I asked them for, and you may choose obviously not to, you don't need to respond to any of these questions that I'm putting forward either today or subsequently but we said to them we'd be very interested in knowing where the code actually is a negative. It currently applies so we know it applies in Victoria and we know that others are developing codes. I guess it makes no sense for there to be multiple codes if you could have a single code; on the other hand, your position may be there's no need for any codes at all but we're interested in this primarily not to address productivity because we don't actually think these things boil down to that.

As you know a terms of reference for this inquiry was costs of infrastructure and so we're interested in those costs that are potentially addressed by a code and those costs are, I think, much more in the nature of relationships and behaviours that involve not just unions but unions and employers. But you may wish to draw to our attention stuff which you say is more along the lines of the sorts of problems that you've alluded to of a political nature, because we're interested in a code not for political purposes, we're interested in a code for effectively managing better the working relationships that do exist within this industry.

MR NOONAN (CFMEU): A couple of comments on that but we'll come back to you on the code because it's of particular interest to us. I mean, there are things in the code, for example, that say that someone should or shouldn't wear a sticker on their helmet. That's clearly not about productivity, that's about, if you like, a view about whether workers are entitled to promote their position as unionists or so on on a job. So there are some clearly ideological things and it really doesn't take us far in the debate whether the government can improve productivity because most rational people would probably think they won't.

But where we start from, and the union had an internal discussion about this, is that we actually take the view that it is desirable for state and federal governments to set terms and conditions around procurement. I mean, I would've thought that on a pure neo-liberal position it would probably be you let the market sort it out. That's not the position that either Liberal or Labor governments have taken over the last 20 years and we also think that it's quite appropriate for the Commonwealth and for the states as clients to have a view about what should apply to some extent in respect of procurement.

How much they want to micromanage the running of a business is probably a matter of some legitimate debate and whether in fact you should have a set of procurement guidelines which further regulate bargaining behaviour which is perfectly lawful under the Fair Work Act, in other words the act that should set the rules about industrial relations, because the code in a number of places purports to go further than the law, ought to prohibit things which are quite lawful. That's a position that requires some thought.

One of the key things we think in respect of the code is that it doesn't do enough to promote apprenticeship and training and really whether you think unions are good or unions are bad or unions are somewhere in between good and bad, we are strongly of the view and we think that if you talk to a lot of employers, one of the views is that if you want to actually really drive productivity in our industry you build the skill base and in the areas of the trades that we cover, that's best done by improving the number of apprenticeship commencements and completions. I think you've probably seen material elsewhere that tells you that commencements aren't great and they're declining but the other thing is that 50 per cent of apprentices that start don't complete and that's a big drain of productivity.

Some of the other things are we think that there needs to be a much better effort on safety in the industry but then you'd expect us to say that but we've still got an unacceptably high level of fatalities in the industry. Statistics around lost-time injuries are very nebulous and rubbery because companies under-report lost-time injuries and people are kept in fairly meaningless jobs to a point when they're injured to avoid them being reported as lost-time injuries. So there's an under-reporting we think in that area but safety has a big impact on productivity. People getting injured and killed has a big impact on productivity and yet the priorities of the Commonwealth here are a tiny amount of money. When the ABCC was introduced the Commonwealth also, responding to the Cole Commission, introduced the federal safety commissioner. It's basically unfunded. It's almost like a part-time job, it's never been seriously treated and that ought to have a lot more teeth under the code and the Commonwealth ought to be working much harder and putting more resources into that area than it is.

MR HARRIS: Dave, I don't want to take up more time, my colleagues want to speak so just one thing when you got on to training the third thing I was going to ask you is there's a para in your report, para 412 which makes a specific statement because we asked about the National Apprenticeships Program and you say the NAP should not be used at the expense of the recruitment of young people into apprenticeships. I was a bit unclear about this para. It comes at the end of the section where you're defending the training funds so I understand the linkage that might exist there but can you just maybe take a note and see if somebody can elaborate a bit further for us by email or something on para 412 and how this NAP might actually come at the expense of recruitment of young people into apprenticeships.

MR MAXWELL (CFMEU): I could perhaps answer that now. Our understanding is that you can approach a lot of the major infrastructure projects and resource projects. What we tend to find is that the employers on those projects will only take on either mature age apprentices who've worked in the industry previously or people in their third and fourth year. They rarely take on persons (indistinct) my concern is that if the NAP arrangement is one that's promoted in the industry, they would likely take up of young people and particularly first and second year apprenticeships.

MR HARRIS: So it's the word "young" that's the crucial word in that?

MR MAXWELL (CFMEU): It's the basis on which the employer's industry seek to take up apprentices in their later years (indistinct)

MR HARRIS: Okay. Warren, do you want to go next?

DR MUNDY: No, Paul can go first.

MR HARRIS: This is going to be Paul Lindwall. I'll move the thing a bit closer to you to make sure you can hear him.

MR LINDWALL: Gentlemen, my first question I guess is about the federal safety commissioner which you touched on. As far as I understand, there's an Australian Standard 1408, if I'm not mistaken, which also applies and it's a mandatory part of the safety commissioner's regime. The safety commissioner which we spoke to said that they have a higher standard than 1408. Do you see that you could replace one - is there an inefficiency by having both regimes in operation?

MR NOONAN (CFMEU): I think that the federal safety commissioner, with due respect, doesn't know the current job very well, but certainly the first guy wasn't very (indistinct) person. But quite frankly the lack of resources, the lack of enforcement of the position for federal safety commissioner it has no practical impact on the industry at all.

MR LINDWALL: I see, yes.

MR NOONAN (CFMEU): Our view is it's really just there so the Commonwealth can say, "We've got a federal safety commissioner. We're interested in safety." We don't think that position ought to be abolished. We think it ought to given teeth and made a really important part of the industry. I don't want to be dismissive but obviously my general view is that you go through the (indistinct) you have one (indistinct) but that would be the answer to your question. But really our comment on the Federal Safety Commission is that it might as well not be there. We sought to persuade the last government they ought to actually properly fund it and make something that makes a difference to the industry. But I doubt that you will meet a construction worker on a federal or state government construction funded job that would even know the federal safety commissioner existed.

MR LINDWALL: On another issue you mentioned in your submission about the importance of ageing - of course we have a population ageing generally - and the use of older workers in the workforce. Can you comment on that a little bit more, and in particular what age do you expect them to continue. Clearly the roles in which they would be working might change as they get older.

MR NOONAN (CFMEU): I'd like to comment that the workforce is ageing universally, including me. I think this a particular point that we've been trying to articulate a bit lately and it's going to become more relevant as I think inevitably the age of access to the aged pension is pushed upwards and potentially the age of access to superannuation benefits is also pushed upwards. I'm not sure how good the data is to be honest and we would be interested in having a look at it. But as someone who has worked in the construction industry since I was about 20 and I'm now 50 and I've got a lot of contemporaries that started in the industry when I did - I'm not working physically any more, but that's what I started doing - but those of my cohorts that are still working physically are finding it harder and harder to get employment and the employment they get tends to be more irregular in what is already an industry that is notoriously itinerant.

The reasons I think might be it's a product of (indistinct) none of us are as agile, fit or as strong at 50 as we were at 20. This is an industry which still has a lot of (indistinct) which are hard physical labour. Backs get weaker, knees get worse, there's an invitable sort of ageing process. But also when you're engaged in heavy physical work that's accelerated. There's also a reluctance amongst some employers to recognise that workers in about their 50s and beyond have got enormous knowledge and skill which can make a really big contribution to productivity.

I don't (indistinct) that I'll be honest with you, but having done (indistinct) practically I know that that's the case and some smart employers will say that. Insurance companies don't like employers hiring older workers because they're more likely to hurt their back or knees. That's a pressure on employers and it's the case that there used to be historically in the industry a number of the sort of jobs that the older workers would move into. So the effect of steel fixer for me is it's unlikely you're going to make 65 as a steel fixer but you see (indistinct) being the gateman, the lollipop man, working in first aid, working as amenity attendant doing the cleaning, doing these sort of jobs. Those sort of jobs are progressively being contracted out. If you drive around the city of Sydney and look at the people doing traffic control, they are generally under 25, female and Irish. Now, nothing against them having a job, but that is the working holiday visa program which is supposed to be a cultural exchange but used as a labour market program and they're usually being paid like wages.

So that's the sort of comment about that but I'm increasingly concerned that the government end up with a cohort of people who become unemployed or under-employed, out the construction industry and the blue collar trades beyond the age of 50 who aren't going to have a viable means of income, aren't going to have much paid employment and they're going to end up on sickness benefit or if that's restricted, more of them will be drawing down on emergency access to superannuation benefit and they won't have a decent retirement outcome.

MR HARRIS: I might just give Warren a chance to ask a question, Dave, if you've got to go in a minute or two. So, Warren?

DR MUNDY: Dave, we've heard from yourselves and a range of others and it's often debated in the media that the integration of head contractors is creating a circumstance of market power. I think in the draft report we note that there's precious little evidence that the ACCC has done very much about this, presumably because for whatever reason it can't prove, it doesn't have the information or the law doesn't let them get at it but is there any evidence or places you think we should look to find the evidence of where this market power is being used to the detriment of the community?

MR NOONAN (CFMEU): No, I don't have evidence and I don't have the metrics of it and I've been critical of other people for not having facts and statistics to underpin propositions, so I can't - and I'm not going to pretend I have got it. All I can tell you is what I see as a matter of commonsense is that when you have the - essentially you're left with two very, very large companies. You couldn't call it a total duopoly but certainly they have substantial market power. There is just no way around it.

The Lend Lease Group and the Leighton group have substantial market power. We are starting to see some interest again from foreign companies that are involved in some of these projects. I think some of them will require a lot more experience in getting an understanding of the market here, for example. Quite frankly I think Samsung are bidding for the East-West Link in Melbourne, I've got a whole lot of observations (indistinct) now about that project. I don't reckon it's ready to really go. I don't think people understand -

I know it's been developed along with that project but that's another question.

But if Samsung were to win it, I think it would probably be a disaster because I just don't think they know what they're doing. But, you know (indistinct) it just seems to me that having those two big contractors, giants in the marketplace, of course they're going to exercise market power. I know there's a whole stream of fringe - you know, the conspiracy theory that somehow the unions are written off in some (indistinct) cartel with Leightons and Lend Lease driving prices up for (indistinct) school of economics, but it's just not right. It would be a lot easier for us if that was the case. We have good relations with them sometimes and very poor relationships with others, and they have different approaches to their industrial relations affairs around the country, but just the sheer size of them, they probably have an impact on the industry.

MR HARRIS: Yes, fair enough. So, Dave, have you got time for one last question. I wouldn't mind asking you about innovation. In your submission you have suggested that there's inadequate innovation in a sector, and certainly we see practices that are, if you like, late to marked here in Australia versus overseas. Do you have anything more for us on whether to put more effort on your limited research staff, but it's an area where we have been looking for sources of evidence, so even if you haven't got the evidence yourself, just areas where you might have been building industry commentary on innovation. We are quite interested in, you know, we spent a bit of time on BIM and things like that, and prefabricated materials and all that sort of thing. Do you know of sources which we could find on this question of innovation?

MR NOONAN (CFMEU): Have you engaged NATSPEC at all?

MR HARRIS: Sorry, who was that?

MR NOONAN (CFMEU): NATSPEC.

MR HARRIS: No, I don't think so.

MR NOONAN (CFMEU): They (indistinct) these questions. I think we can send you a link to it. They would probably be happy to have talk to you. Look, I think it's a mixing of innovation. I think with both sides, I've looked (indistinct) one survey of innovation.

MR HARRIS: You did. We are just asking for more.

MR NOONAN (CFMEU): Again, sorry, this is only (indistinct) you know (indistinct) jobs sometimes still but I can't for the industry. What I will say is there are areas - and I've talked about the high rate - relatively high (indistinct) environment of the industry here. I took some colleagues from Canada and the US to Melbourne construction sites and I (indistinct) CBD construction and the infrastructure here recently and we've actually got the most advanced formwork construction technology in the world in that high-rise construction area. If you have a look at some of the projects that have been constructed particularly in Melbourne, but also Sydney and Brisbane the interface between - again, I'm getting into construction land here - but the gap between the completed structures and floors and the follow-up (indistinct) fit-out is absolutely lightning fast in this country, and we have actually got some of the best innovation and technology in the world in that area.

I also think that there are some interesting things happening in prefabrication. There are a couple companies in Melbourne that in particular are focused on fabrication process which is actually based on the motor vehicle industry, where they build actual modules, they're completely fitted out in a factory and then can be put into place like blocks. There is some innovation out there. I'm not sure that we are going to be able to produce much more. If we had a bit of a look - I think Stuart had a bit of a look around at innovation and I think the reporting on this is scarce. I think an aspect the (indistinct) construction information might be useful on this.

MR MAXWELL (CFMEU): I can probably send you some links to various web sites that can highlight areas of innovation that then (indistinct)

MR HARRIS: Somebody who you think has credibility I guess is what we were looking for. I think we can all do web searches, but the question is who has got cred that you would see? It's always useful to have somebody who actually works in the industry saying, "These blokes have produced decent stuff in the past."

MR NOONAN (CFMEU): Yes, I think the evidence (indistinct) looked in a practical sense, that's the one I'm talking about. I think Martin Loosemore at the University of New South Wales is interesting on this, an academic, have you see his stuff?

MR HARRIS: Yes, I think we got a submission from him. Certainly, I have seen the name, yes.

MR NOONAN (CFMEU): Yes. He is interesting on this stuff.

MR HARRIS: That's fair enough. I don't want to put you on the spot for the moment, but it's something - - -

MR NOONAN (CFMEU): We will send a link for Richard (indistinct) as well. I actually had a discussion with him about a lot of this stuff yesterday.

MR HARRIS: That's great. Any final things you want to tell us that we haven't managed to pick up or weren't in your opening statement or anything else like that?

MR MAXWELL (CFMEU): No. The only question I had is in termso f time frame, getting things back to you.

MR HARRIS: The next couple of weeks - we need stuff, because I know the next couple of weeks, it means Easter is in the middle of it, which is why I say a couple of weeks, but pretty much by the end of April we will be out of the research phase and into the final construction phase, and there will probably be staff in the audience shaking their heads and saying, "No, no, that's garbage, it's earlier than that," but pretty much that's the plan. So anything that you can let us get access to, even by way, as I said, of emails - you can get mine off the web site, there's nobody else's - that that would be very useful.

MR MAXWELL (CFMEU): Thanks a lot.

MR HARRIS: Thanks very much.

MR LINDWALL: Thank you.

MR NOONAN (CFMEU): Thank you.

MR HARRIS: Sorry to those of you in the audience who found that a bit break up, but I found when two people are on the end of, both on one of these things, that's what you get. So they will have had it the same way. Once you put two of these things on, they are never perfect, and you get the clipped end of sentences and end of words and stuff like that.

I think for us that's going to be a declaration of lunch and we are back here at 5 to 1 to start, which means about 10 to 1 if you want to take your seats, because there is a big demand for seats, as you can tell, so 10 to 1 back here. Thanks very much.

(Luncheon Adjournment)

MR HARRIS: So we will restart the transcript. If you guys could identify yourselves for the purpose of the transcript, that would be great.

MR LYON (IPA): Certainly; Brendan Lyon, chief executive, Infrastructure Partnerships Australia.

MS PETERS (IPA): And Zoe Peters from IPA as well.

MR HARRIS: Do you want to make any opening comments for the record?

MR LYON (IPA): Yes, if that meets with your approval, chairman. Chairman and commissioners, thank you very much for the opportunity to speak with you today, particularly as you move to finalise what will be an excellent report into the infrastructure market. I think it's important to note that your report will be released at a time of substantial political policy and community focus on the nation's infrastructure, meaning that done well, your final report offers us a signal opportunity to start to lead the infrastructure funding and efficiency debate back to the fundamentals.

Obviously, the cost quality and reliability of economic infrastructure services like transport and utilities, telecommunciations and so forth are fundamental to the economy because together with labour capital and other input costs, infrastructure services represent essential aspects of economic production but this is not solely an economic policy issue. Infrastructure policy is of considerable community interest because the cost of living issues played out daily in the media are the domestic sector's reflection of inefficient infrastructure markets. In short, the consequent inefficiencies in key infrastructure sectors accrues to the bottom line of every business in the economy, and each consumer in the community.

I also note that the commission's ultimate report will be fundamentally important in terms of the policy context into which it is released. The commission's report will be released among an architecture of substantive national economic reviews, including the Commission of Audit, Ian Harper's review of competition policy and the review of the nation's taxation system. This means that your inquiry will be released as part of a continuum of reform advice variously considering the efficiency of public expenditure, the adequacy of public revenue and the broad competitiveness of the national economy.

From the outset, I wish to congratulate the commission on the depth and strength of your draft report and I am delighted to join you today to share additional observations as you move to finalise the inquiry. I wish to particularly commend the Commission for the bravery and integrity shown in your contemplation of the real issues that are affecting transport infrastructure in this country. The draft report's user charging recommendations were in my view the most politically complex and therefore the boldest of the commission's recommendations.

As commissioners will be aware, Infrastructure Partnerships Australia recently released a major research project into Road Pricing and Transport Infrastructure Investment. Our report, which forms an annexure to my submission that's before you today, had notable and clear parallels with this inquiry's preliminary report. Both the commission and our study recommended a revenue neutral approach to reform, a frictionless pass-through of revenue to transport investment, large scale technology trials and, most notably, a central role for the motoring clubs in progressing the public debate. Indeed, our report directly addressed that last recommendation, because our study was developed with and actively supported by the Australian Automobile Association, the NRMA, the RACQ and the RACV.

Our central recommendation is for the Commonwealth Treasurer to make a formal referral to the Productivity Commission to consider the structure of the light vehicle road transport market, the structural weaknesses in the existing system of charging and investment and the opportunities and pathways to deliver a more equitable and efficient approach that provides a sustainable revenue base. Our process recommendation should form a basis of consideration for the commission's final report because road pricing is complex and needs to be considered in the absence of day-to-day political priorities; because a full range of options need to be dispassionately and transparently assessed and because driving consensus across the community will require a very detailed and impartial process to analyse the possible solutions and the process to achieve them.

That's why we submit that this issue requires a formal public inquiry process, ideally led by the Productivity Commission, allowing this complex issue to finally advance from a theoretical proposal toward a developed and actionable reform process over time.

I also welcome the Commission's consideration of appropriate roles for the public sector in terms of innovation in financing. There is a substantial factor for Australia's government to be creative in the way that they account and signal for private investment into the capital investment task, particularly in terms of potential interventions around project SPVs and project financing models including the use of public equity investment, the use of marginally lower cost public sector debt within private SPVs, the use of revenue or debt guarantees over private investment and, as is sometimes floated, a public sector national infrastructure bank.

I believe that renewed experimentation to discover a better mix between public and private investment is useful because it will drive innovation and better outcomes, but it is also very important to understand what private finance is, what it does and how private capital structures drive incentives. The draft report found that the capital structure and type of finance deployed conveyed very different incentives to manage different types of risks and the use of approaches like joint equity or public sector intervention and the in debt finance swtructure for project SPVs can serve to undercut the principle reasons for using private finance in the first instance. As the draft report correctly notes, private finance rarely serves as a funding option, in the absence of the creation of a market and revenue stream that signals for and sustains the capital and operating funding requirements.

Examples where private finance can also fund infrastructure might include the creation of a discrete monopoly concession like a road PPP or the creation of a wholly private market structure such as a utility market. In the absence of these types of market creations, it is an error to consider private finance as a funding option because the repayment of the project's debt and equity is sourced directly from the public sector. For the majority of privately financed infrastructure, the finance acts solely as a sophisticated incentive and risk management framework, a structure that neatly aligns private profit to the outcomes sought from public investment. When a government uses private finance to develop an asset, it will typically run a competition around the design costs and potentially whole of life operation between several competitors in the process.

The inclusion of private equity and debt is in my view the most significant reason that private finance options have been reliably shown to deliver public infrastructure more efficiently than traditional public procurement. This is not a reflection of deeper skills or expertise within the private sector but rather a reflection of the powerful incentives created through a private capital structure. In effect, a project SPV brings together the optimism, expertise and profit drive of equity, combining them with the cautious discipline of debt lenders to the SPV. Private debt is important because it tests the assumptions of equity in much the same way that a bank might assess the creditworthiness of a home or commercial borrower. In this way, a PPP or similar financing structure seeks to optimise the competitive process and align whole of life incentives to drive the best value for users and taxpayers.

While different approaches that are able to be structured off budget are naturally and logically attractive to government in a fiscally constrained environment, it is fundamental that any interventions in private capital structures are considered very carefully, given the potential to substantially retard the incentives that are sought by the inclusion of private financing in the first instance. As you have noted in your report, the procurement of the NBN represents a substantial example of an innovative approach to infrastructure finance which has been structured off budget. The substantial cost overruns, delivery interruptions and negative impacts on contractors and taxpayers alike provides us with a good working example of the reduced risk management incentives that can occur.

Another example would occur if the public sector were, for instance, to provide public debt or to guarantee or enhance private debt in a project SPV, particularly during the high risk construction and delivery phase. The exclusion of private debt or its insulation from loss through a guarantee would likely serve to reduce the degree of discipline imposed by the inclusion of debt. Even on its face, it seems unlikely that a Commonwealth or state public servant, however skilled they may be, would have an equal incentive or adequate resources to assess the viability of equity's assumptions underpinning the structure. We agree with both the commission's draft report and the earlier Infrastructure Finance Working Group report, which each cautioned against overly sophisticated approaches based on favourable accounting treatment, noting the substantial and opaque risk of loss or the potential to crowd out efficient existing private investment.

In addition to our strong support to reform the transport markets, the focus on transparent financing and other reforms, we have suggested in our submission four additional areas that would benefit from further development, emphasis or refinement in the commission's final report. These are water market reform, capital recycling, project evaluation tools and the benefit of wider indicators of the efficiency of key infrastructure services markets or key geographic centres over time. I would be delighted to address those areas more closely as we move to questions.

Before moving to questions, I once again wish to congratulate the commission on your excellent draft report. We have appreciated the opportunity to work alongside you in the development and articulation of the draft report and we note the very high level of engagement you have had with the infrastructure industry through this process. As I noted at the start of my remarks, your report comes at a very important time in terms of the context and policy discussion around infrastructure and we would urge you to be bold in terms of the recommendations that you make at the conclusion of the inquiry.

MR HARRIS: Thanks, Brendan. There's a lot in your further contribution to this as there was in your original contribution, including, as you say, the joint study done with AAA and Deloitte. I have a couple of questions for you on that role of equity, if I could just take you to that now. You made a comment which said no matter how gifted or well informed a public servant might be, it's very hard for them to perform the same analysis that I think in your submission you would expect financial market institutions to make of equity's assumptions for an infrastructure project.

We have had a proposition put to us though from superannuation funds for this inverted bid model where effectively it is the proposition to put up equity's case for taking over management of the development of a piece of infrastructure. In that scenario I think, at least in concept, a model that has been put forward by Industry Funds Management and Industry Super Australia, and I think QIC has a model of inverted bid as well - it would effectively be a government entity with presumably whatever professional advice they could get, but nevertheless assessing the proposition of equity to take on effectively almost an alliance arrangement for them running the project collectively.

I don't know whether you're familiar enough with the inverted bid from our own report where we did describe it, but we're very interested in that and, whether it was accidental or deliberate, you have managed to pick a point which is quite important because it would be a government entity one way or another that will be assessing the proposed value that equity saw in a project. So if I could put your comment in that context, did you intend to comment on the inverted bid or is it more of a generalised concept, and if it is a generalised concept, could you do anything about relating it back to the concept of an inverted bid for us?

MR LYON (IPA): It was made in the context of a generalised philosophy of approach out of the public sector. The comment that I would make - and I have seen some discussion around the inverted bid model - one of the reasons that the established PPP model has performed demonstrably well in cost, time and quality measures is because of the level of competition over design and price and to have a number of proponents bidding within that context has been shown to deliver cost risk in particular, but also delivery risk in other things substantially better than established alliance models, so again I would urge caution around adjusting policy frameworks. The default position, particularly for major procurements, should be to look at a competitive outcome first because generally that's the pressure that will drive the innovations and the value gains that you achieve.

MR LINDWALL: Just on the same type of point, what about the UK model of PPPs where they're not required to have a fully funded bid up front and in fact the consortia bid and then this preferred one then has to go and get a competitive bid for the financing?

MR LYON (IPA): Again I don't see the cause for disaggregating the model to that degree because again it means that you have got the assurance of that discipline of the debt providers through the bid process and it means that you're getting a greater degree of cost certainty in terms of the bids that are put in. There's always a question about when do you begin to reduce the degree of competition and how do you keep the process efficient so that you're driving a competitive an outcome as you can without driving inefficient cost into the market, but again I would urge caution in disaggregating what has been a very successful management approach and assurance model for the public sector in terms of the aggregation of skills and leveraging that in terms of the market's aggregation around the outputs that are specified.

DR MUNDY: Why should, as a matter of public policy, we be comfortable about equity supervising the raising of debt for a major airport in the country but we shouldn't be comfortable with them doing it for the building of a new hospital in Bendigo?

MR LYON (IPA): In what, sorry, aspect?

DR MUNDY: You're basically saying that if you allow equity in first without a fully funded bid model, that then reduces the tension. You don't have to line up each bank against each bid. You could let equity, once it is successful, then go and arrange the debt, be it from banks, be it from wherever. It has been put to us that part of the problem with the fully funded bid model is that each equity bidder then has to attach a set of banks to themselves and that leads to a lack of tension going forward.

There are some models which your organisation rightly, in my view, suggests have been very successful at financing public infrastructure and that's in the airport sector where equity out at Brisbane is going to organise all by itself a billion dollars to build a new runway. But what you're saying is that that situation, which I presume you think is acceptable, is somehow different to if - what my colleague Mr Lindwall is I guess alluding to, is that why not just let equity get the right to build a new hospital under a PPP structure without having to turn up to the government and say, "Here are the debt funders"?

MR LYON (IPA): I think the context is quite different because you have got a brownfield operating asset with revenues, with a balance sheet, with an investment committee, with a board and all of these things and you're not contemplating the up-front construction risk aspects that you see in a greenfield PPP procurement, so I would suggest that the risks are somewhat greater during the construction phase of a brand new toll road than they are in laying a new runway at an existing operating capital city airport.

DR MUNDY: When the Commonwealth assessed bids for the privatisation of the first three airports in 1997, when people were bidding on a lease with no corporate structure, you see that different to the building of a new toll road as well?

MR LYON (IPA): Yes. The other thing is you have got the tripartite agreement in the aviation sector also, so there is a degree of contingent guarantee that sits over those assets that's also - - -

DR MUNDY: I think you misinterpret the nature of the tripartite - - -

MR LYON (IPA): Okay. I may well.

DR MUNDY: Anyway, the tripartite isn't an important - - -

MR LYON (IPA): Airports are not my area of specialisation.

MR HARRIS: No, that's fair enough. Let me exemplify it this way then: unsolicited bid proposals have got two policies amongst the two largest jurisdictions.

MR LYON (IPA): Yes.

MR HARRIS: Under those sort of propositions if equity turned up nevertheless with a proposal, I presume you wouldn't go so far as to say, well, you shouldn't investigate and/or even perhaps trial it as a mechanism for determining whether there was validity or not in a particular proposal.

MR LYON (IPA): I'm not against trialing different experiments around the way that we seek to put capital around the delivery of different outcomes and in fact I think that one of the exciting things we're seeing in the market at the moment is a high degree of experimentation between jurisdictions where you have got almost a traditional public works approach being taken in New South Wales with some hybrid equity to the build-out of its motorways, you have got an availability-based, more traditional model being run down in Victoria, so I think there is a good degree of experimentation. Same around the social infrastructure program where we're seeing it used to start to inject benchmark competition into public services. So I'm not sure that we have a concern about the level of expertise or experimentation that's occurring at a state level, but I don't think that those experiments should be systemised if we're not trying to solve an existing problem.

You look at the debt structure. A lot of people have talked about the liquidity of debt markets where they in fact, other than the desalination, are procurements where we saw a specific adjustment and a smart adjustment around the process of acquiring debt for that project, and so I think that we need to recognise that specific projects will have specific features that sit with them but in terms of designing or recommending around structures, I think that the Productivity Commission should be looking at the purest structure of incentives, risks and rewards and making sure that we're harnessing the actual power that you're introducing with a capital structure with private finance and that we're not undertaking or recommending interventions that will lessen those signals in terms of the threat of extinction and the other things that drive better outcomes through a competed privately financed process.

MR HARRIS: But on balance though if we are looking for ways to encourage equity to maintain its interest, there has been a view put which says - - -

MR LYON (IPA): Do we think that there is a lack of interest from equity?

MR HARRIS: I was about to say that there has been a view put which says, "Look, equity will come back. It might have got burnt with a couple of toll roads but they will be back." There is another view which says they won't; it's a greenfields (a) because there are too many opportunities offshore that are even more attractive and then (b) because they would still prefer brownfields to greenfields because they have been burnt. I guess what we are investigating here with this - your point about competence does actually arise in my view because the question is: even if we were to consider an unsolicited bid proposal, and let's face it, that is what it is there for, who does the considering? This is very important in this.

MR LYON (IPA): Yes, it is. I mean, one of the things about the unsolicited bid framework is that they shouldn't be a routine way of sourcing infrastructure. It means that you have a planning or other public administration problem if it is the routine way, but it is a way of insulating unique bids and direct negotiations and making sure that there is a governance and accountability framework about them. I think they are important but we need to recognise the limitations of unsolicited bids. They are not a routine way to signal for investment. They are a process to signal for people to apply new thinking to particular problems. I think it is good discipline.

I think it is good that we have a process to deal with it, and provided those processes are rigorous, it means that you can avoid some of the more unfortunate aspects of infrastructure procurements or outsourcing, things like the Australian Water Holdings issue that is being debated at the moment, because there is clarity and there is probity that sits around even the direct negotiation process. I think that is going to be very important as we move forward because we have got a very substantial degree of change that needs to happen in terms of the mix between public and private provision in public services and a whole range of other things. If we can learn one lesson from the 80s and 90s' reform periods, I think it is important that the community is brought along in terms of the rationale for change and particularly the integrity that sits behind the apportionment of public services out to different providers.

MR HARRIS: Fair enough.

MR LINDWALL: How about we talk now about user charging? Sorry, we will talk about CSOs first, community service obligations. The way I read it, there are two ways of applying this for rural and remote areas, say. You could either the CSO extracted from a cross-subsidy from user charges in cities, for example, or you could have a CSO from general taxation revenue. Do you have a preference one way or the other?

MR LYON (IPA): We don't have a preference only because we haven't gone into the issue down to that level but one of the things I would say about the road user charging discussion is the institutional arrangements are going to be a crucial determinant both of the long-run success of reform if it gets up and also in terms of bringing the states and territories to the table for the discussion.

So certainly one of the things I would urge the commission to do in its final report is to give some consideration to how the allocation of revenues is going to occur and particularly consideration of what happens to that money, once it is distributed down out of the Commonwealth and down into the state jurisdiction.

So I think that discussion around the governance of the allocation of revenues making the CSOs transparent, where they are funded from et cetera are exactly the sort of issue that we would like to see discussed over a detailed public inquiry, including with the inputs of the state and territory road agencies.

MR LINDWALL: For example, the other part of your report was that I think 40 per cent of revenue should be from congestion charges and 60 per cent from road maintenance.

MR LYON (IPA): Access, yes.

MR LINDWALL: Access charges. Now, in principle I would think theoretically the congestion charge should be set exactly at the levels of the externality and then the user charges should be, if you like, a residual that is for your maintenance and new construction and so forth. Do you have any problems with that?

MR LYON (IPA): No, I don't. I mean, we selected that model based on a fairly simple options analysis and we undertook the econometric assessment, really more to have a look at the real world impact on individual users; and that was a recognition we had a number of years ago after we published an earlier work around road user charging that to get this issue to substantially advance, we need to have the users at the table calling for reform, as you noted in your report.

I would like to commend the motoring clubs because this isn't an easy discussion for them to have but one where they have landed in advance of the parliament, in advance of public policy which is really the reason why I think that the commission should be firm in its recommendations around a process to take this forward, because it is very rare that you have an alignment of the sector being reformed wanting the discussion of an independent and respected agency like the Productivity Commission that has got a high degree of understanding of the issue and a general recognition at a state bureaucratic level that the existing system is totally debased and unable to be recovered in any efficient way.

MR LINDWALL: I have got one more question - I have other questions but I don't want to hog the limited time. But does the blue book that you have include an analysis of the ABCC, the Australia Building and Construction Commission, and what would be the IPA's view of the veracity of bringing back the ABCC?

MR LYON (IPA): IR is not an area that we tend to focus on. We tend to look at more the operation of infrastructure markets themselves, but I read with interest the sections of your draft report, both about the lack of information that is available in terms of the impact of labour productivity and I have also obviously read about the industrial disputation that is on around the sector and heard it discussed at some length.

I mean, clearly your numbers find that labour productivity has been slower in construction than it has in other sectors. That would have to point to some sort of problem that can be resolved with a policy intervention. I think that recent examples and very vigorous examples of industrial disputation and other things and the royal commission both point to the benefit of an industrial watchdog in this sector.

DR MUNDY: I will be brief. You do raise on page 6 the commission's 2011 report on urban water. I was a commissioner on that inquiry.

MR LYON (IPA): I left out the word "excellent", commissioner.

DR MUNDY: That is all right. We have healthy egos. I should for the record indicate that I am a director of the Sydney desalination plant. I guess the view that we have largely taken in this space, because of the excellent work that we did in that regard, particularly the work led by Dr Salerian was that we didn't have an awful lot more to say. We had said that we needed to say and we to a large extent had been studiously ignored.

Now, that may well have been because the drought has moved on and there is now an awful lot of capacity particular in desalination within other areas, so perhaps not today - because I am mindful the chairman has some other questions - could you come back to us, even by way of email, with specific matters in which you think we need to do further work in the water space which would significantly add value because it is not clear to me that there is much more for us to say.

MR LYON (IPA): I will. In the briefest of responses, we noted that work because it was very detailed and because it was sent to the jurisdictions for a response and because alongside the road transport market, I would say that urban water and waste water is one of the least scrutinised areas in terms of its operational efficiencies and other things. The other pressure that we are seeing at the moment ties back to the earlier points I made around finance. We know state governments are under a tremendous amount of pressure. They are politically over-committed in terms of the infrastructure they want to build and they are under-resourced in terms of fiscal capacity to pay for it.

We know that a number of jurisdictions have been looking at their urban water and waste water sectors, trying to identify areas where they can cash out some of their chips. The concern I have is that if we haven't resolved what the market structure is going to be, what the most efficient long-run structure for urban water and waste water markets is, then we may find that we have sold sections of different networks that sit right in the middle that either make it impossible or prohibitively expensive to be able to go back and fix those market structures.

I have tried not to focus on the NBN throughout the testimony but one of the points about the NBN was that it was a reaction to a retarded market structure that was created at the start in terms of the vertical integration of the network and retail functions for Telstra.

Telstra exploited those, as you would expect a private company to do and as corporation law requires it to do, but I think in urban water let's start from the start in terms of microeconomic reform.

Let's start a discussion about what the good long-run efficient model might be and then policy-makers can begin to cash out individual sections within the context of knowing where they're going. Let's avoid the Loy Yang experience where part of one of the generators was privatised in the 80s because the government had run out of money. That generating set had to be ring-fenced out of the entire national electricity market until just a few years ago because of the sovereign risk aspects of unwinding all of the guarantees and other things and then it was easier simply to just leave this one generating set outside of the national electricity market.

MR HARRIS: That's a very well-made point and it supports, I think, the contention that we're saying which is you privatise for efficiency reasons. Everything subsequent to that may or may not be - - -

MR LYON (IPA): One of the points I've tried to make is the modest distinction I've made in the submission between the moral hazard that you identify around capital recycling and the reinvestment of released capital is that all of these things should be occurring with an up-front consideration of the market that's been created and ideally that would see things like a separation of the contestable and the network aspects for linear infrastructure, a consideration of contestability or regular sort of mark to market type processes for things where benchmark competition is the best option, but again I think that an up-front consideration is very important for investment certainty, for the general integrity of privatisations and for the long-run efficiency of the economy.

MR HARRIS: Yes, so where we did comment on privatisations we commented in areas where we think enough work has been done to demonstrate that.

MR LYON (IPA): That's right.

MR HARRIS: The efficiency benefits are reasonably clear and the threats as you've identified them from potentially privatising in circumstances where you create a monopoly infrastructure, a taxing point or some other inappropriate intervention in a market minimised so we can see the positives there. We are going to look, as Commissioner Mundy was saying, at further water and that's why we were quite interested in this but at that point we hadn't gone so far but we thought pretty much ports and the remainder of the electricity market, the evidence is reasonably clear.

MR LYON (IPA): I'd say very clear in electricity but the submission has tried to make that distinction that the assets you've recommended are ones that have been privatised into well-articulated competitive markets where the structures are known, but water we don't have that because there is no history of anything other than the most modest of structural reforms and it means that we do run that risk of painting ourselves into a corner in terms of the immediate rush for cash versus a long-run efficiency.

DR MUNDY: Could I just ask you to think and perhaps again just come back to us on what your views might be about the privatisation of Australian Rail Track Corporation and Air Services Australia - - -

MR LYON (IPA): Certainly, I can tell you now on the Australian Rail Track Corporation in terms of where it makes sense to do so, we don't see any compelling reason for network infrastructure that's separated from the above rail operations to be a government enterprise.

Certainly something like the Hunter Valley Coal Chain is worth a substantial degree of money, whether the economics of the interstate track would stack up for privatisation we haven't looked at. Certainly you would have to think the Hunter Valley Coal Chain is a very obvious candidate for privatisation.

DR MUNDY: If you just think about it a bit more and come back to me on both of those, that would be helpful.

MR LYON (IPA): Certainly.

MR HARRIS: There are elements of the ARTC and the way it's developed that might still be relevant. While the state government has obviously committed infrastructure to the ARTC, at a point it's privatised you might find greater difficulty in - - -

MR LYON (IPA): Over the leased sections of the track it gets complex.

MR HARRIS: Yes, but on the other hand you might find that it's not going to occur anyway. There have been suggestions from time to time that segments of urban rail be transferred to the ARTC. Clearly if it was privatised, again that's where you start to look at this as is it a monopoly taxing point for the public transport system at that stage or will priority be given to traffic where a government had an interest in the public transport system, retained that; private enterprise have an interest in the freight, access to that network and you've got - - -

MR LYON (IPA): The Hunter Valley connection doesn't have those same degrees of complexity.

MR HARRIS: I think that's true as far as I'm aware but it would be worthy of examination to be sure that was the case.

MR LYON (IPA): In an ideal world we would have been bringing that forward in conjunction with the port transaction so that you've got a very pure supply chain.

DR MUNDY: Even if you can just flesh out for us what you think the big issues that should be thought about are.

MR LYON (IPA): Certainly.

DR MUNDY: For both of those, because that's really all that's left in the

Commonwealth infrastructure portfolio.

MR HARRIS: My final question, there will be an opportunity for you to add more to this is about institutional reform. So the way that we propose to approach road user pricing was to ensure very much as a way of locking in a future strategy for something we know will take a substantial period of time to implement a model which as you have referred to, would involve both the heavy vehicle industry and roads and motorists representatives, probably through the clubs, the associations, because of the obvious institution but what I call an institutional reform model and we did describe the New Zealand land transport agency arrangements as being a potential guide, without being specific to say that that would be replicated, but we did suggest strongly I think that an institution was required or absent that what you have is a series of idea and no owner for those ideas.

I'd be interested in getting a reaction to that and particularly the question of whether it might be a national institution or a series of state and territory based institutions and any judgments you might have at this point and if you're uncertain at this stage, any further offering of ideas on this maybe by way of a short further submission would be great.

MR LYON (IPA): I'll do both of those. I'll just make a couple of observations and then I'll respond in written form to this, as I will to the other questions that were raised. One of the things that you identify in your report is that the pricing of heavy vehicles has evolved a lot further in terms of the consideration of these kinds of rationalisations and one of the markers that allowed that to happen was the creation of a focused national road transport commission whose specific aim was to begin to look at these sort of things.

In terms of road pricing I suspect, and I'll give this further thought but I suspect your institutional arrangements, the owners of this kind of reform process would probably need to be down at a state level because of the Commonwealth state overlay because of the sensitivities over funding and all of the other issues.

But we will give it further consideration and respond to you with some more considered thoughts, but I agree with the theme of your question which is that these kind of reforms need a champion, need an institutional champion and they need an ability to be able to aggregate the views of different stakeholders. So I agree with the theme of your question and we'll respond in its form in writing.

MR HARRIS: Thanks very much, Brendan.

MR LINDWALL: I note the time is very short so perhaps you could add this to that list and that's the extent to which you think that there's scope for improving the efficiency of the existing road network with technology, for example, better synchronisation of traffic lights or using emergency lanes during peak periods for traffic flow and all sorts of other things that can be done that I would think dramatically would increase or lessen congestion in peak periods.

MR LYON (IPA): There's no doubt that smarter technologies in terms of the management approach to motorways are useful and are important and certainly NICTA have been out in the last couple of days with some discussion around managed motorways and other things but at the end of the day there's a limitation to how efficient those sort of rough-tool capacity management type approaches can be.

We could solve the capacity problem by simply saying if you've got an odd number or an even number you can drive on the following days, but those sorts of very rough-tool type approaches to demand side management are by definition not efficient and there is a substantially greater opportunity in the long run, I think, to use price; to be able to give people efficient choice; be able to close the loop in terms of leakage of funding and start to deal with the real problems that are causing our transport problems.

MR HARRIS: That's great. Anything we missed?

MR LYON (IPA): Just one further point, I noted with great delight the focus that you've taken around project benchmarking.

MR HARRIS: Yes.

MR LYON (IPA): In terms of the preparation of the final report I think the commission should give some further consideration to the development of network-wide indicators about the actual performance of infrastructure markets and potentially some sort of index model around specific geographic centres like capital cities, given that they are such a substantial driver of productivity. We know that more than 2 per cent of GDP will flow into infrastructure but we're not routinely measuring the actual network performance and if we were able to index say capital cities, we were able to index the performance of transport, electricity utility, telecommunications markets and other things over time, it will create I think a much stronger understanding in the community and a much stronger driver on governments to be to be bolder in terms of the types of regulatory interventions they are willing to make and will create more of a discipline not to announce projects but to announce improvements in terms of the upturn in quality of the services those networks provide.

MR HARRIS: Just so that I can get a better feel for that, that index is therefore, if you like, a mashing of the infrastructure quality in, say, a Sydney jurisdiction, so it's almost a rating and shows you the direction infrastructure quality is generally falling in this jurisdiction, rising in this jurisdiction.

MR LYON (IPA): Yes.

MR HARRIS: Rather than the thickness of road pavements is sufficient in a particular jurisdiction.

MR LYON (IPA): Yes, it meant more the costs of quality performance are likely to be the things that you would measure, that that will create a discipline on different jurisdictions in terms of performance of their capital cities and I believe it's more likely in an ongoing sense at some point the public focus will move from infrastructure to other things.

It would be good if this inquiry left a permanent architecture in terms of increasing the diligence of approach and leaves behind an institutional framework that continues to apply discipline around the need to reform and restructure investment in infrastructure markets; and if we move it off a funding battle project by project, street by street and start having a look at the actual performance of the markets that these assets all together provide. Then I think we are starting to leave behind that legacy of accountability for both policy and project interventions and an increased ability to be able to measure the relative performance over time.

MR HARRIS: I see you are creating a competitiveness index between cities.

MR LYON (IPA): I did note that we had collaborative federalism, it seemed to us, between the 2007 election and the first meeting of the Council of Australian Governments.

I think, and this goes to the very heart of the points you make around the vertical fiscal imbalance and the fiscal asymmetry between Commonwealth and state. I think that Australia has always worked best when we recognise that it is a competitive federation and where states are competing with one another to drive up the productivity of their individual states and that's when you start to get the true benefits of being a federation of states, is when we start to see constant and continuous experimentation like we did through the 80s and 1990s toward the sort of reforms that drive this country forward very substantially.

MR HARRIS: Yes, I now see why you would want to make that point. That's been great. I appreciate all of the effort you have made to support this inquiry, multiple submissions and also the coincidences of timing between a very substantial study of your own and ours and your willingness to come back with further information, which we very much appreciate. Thanks for making time available today.

MR LYON (IPA):   Thank you all.

MR HARRIS: So we have K. McGovern and Associates. Good afternoon. If you could state your name for the record, so we know who you are.

MS McGOVERN (KMA): Yes. I am Kerry McGovern and I am with K. McGovern and Associates and I am giving a submission on behalf of EAROPH Australia.

MR HARRIS: Thank you. Did you need to make some opening comments?

MS McGOVERN (KMA): Yes, please. I am a public sector governance financial and asset management specialist at my firm. I am also vice-president for Australia on the Council of the Eastern Regional Organisation for Planning Human Settlements (EAROPH) and president of the Australian chapter of EROPH Australia. EAROPH Australia has a working group that aims to establish a sustainable framework for the managing and investing in physical assets within the context of planning and managing sustainable human settlements. EAROPH is a non-government multisectoral organisation encompassing the private, public and academic sectors. It was established to foster the exchange of insights and experiences among countries in the EAROPH region and it covers countries from Turkey to the Hawaiian islands and includes active chapters in Japan, Korea, Malaysia, Indonesia and the Philippines, as well as Australia. It promotes a better understanding of human settlements and encourages excellence in planning, development and management to improve the quality of life and the sustainability of human settlements.

My background is in whole of government. I have worked in the Australian National Audit Office, the Queensland Treasury, the New Zealand Office of the Controller and Auditor-General, where I developed policies for the audit of the balance sheet of government and various ministries of finance and audit offices through the Pacific, Asia and the middle east. I have designed a whole of government framework for the management of the public assets of the Democratic Republic of Timor-Leste and I have also led a team that established the governance arrangement within the Pacific Association of Supreme Audit Institutions established as a result of our work to include the supreme audit institutions of the northern Pacific, which has enabled it to undertake cooperative performance audits. Those completed include on solid waste management and access to safe drinking water.

I recently partnered with the Australian National University to write a book “Infrastructure Maintenance in the Pacific. Challenging the Build-Neglect-Rebuild Paradigm” which was launched in June last year. I agree with the approach being taken in this report. We think it addresses some of the key issues that must be managed if infrastructure services are to be valued and affordable. EAROPH Australia agrees with the overall approach.

It is sensible and we support the work of the commission.

MR HARRIS: Although it's not actually in your submission - it's something you have just said in your introduction there - so when you were in Timor-Leste, did you know a fellow by the name of Michael Carnahan? He was doing the budget process. He organised the budget structure for Timor-Leste but - - -

MS McGOVERN (KMA): 2005-6?

MR HARRIS: Yes, back at the start with the UN organisation.

MS McGOVERN (KMA): No, he wasn't there when I was there.

MR HARRIS: Okay.

MS McGOVERN (KMA): I was in the Ministry of Finance and I knew the budget guys.

MR HARRIS: It just would have been a total coincidence. He is a former colleague of mine and I am always in awe of the people who go and devote a chunk of their careers to effectively setting up a brand new country, a singularly impressive thing. Back to reality or to today's reality, I guess we haven't really been looking in this infrastructure inquiry at what might be considered to be international aspects but was your interest primarily international? I can see that you have got an international context but we have pretty much focused, as you can see from the report, on the nature of infrastructure investment in Australia, one way or another.

MS McGOVERN (KMA): I think what I want to bring to the commission is the broader picture, more whole of government. I have had the benefit of working with whole states which are unicameral and have been able to see the whole system without the impediment of the federal layers.

MR HARRIS: Right.

MS McGOVERN (KMA): There are three issues I really want to put before you this afternoon: one is in your recommendation you call for the governance arrangements that will enable the effectiveness to be determined by an independent body, for example, the auditor-general or Infrastructure Australia, our recommendation 7.1.

MR HARRIS: Yes.

MS McGOVERN (KMA): We support this and we also encourage you to look at the resource implications of that upon these offices. They often are very stretched for resources but they are doing good work in this area and the New Zealand Office of the Controller and Auditor-General, for example, this year was able to table in parliament a report on the effectiveness and efficiency of arrangements to repair pipes and roads in Christchurch. This report provided assurance to the parliament that "the alliance reinstating horizontal infrastructure in the city is capitalising on its valuable resource of highly trained specialists to develop practical solutions and project scoping is done well. The alliance has sound business systems that create operational efficiencies. When the relevant variables are considered, the alliance's projects seemed to be reasonably priced". Having the auditor-general working in this field provides some assurance at that level.

The Victorian auditor-general also has reported on the longstanding disconnect between planning and funding of transport infrastructure and that it means funding to address the transport needs for flood areas can take more than a generation to materialise. You are probably aware of that report.

MR HARRIS: Me again, yes. We have all got infrastructure backgrounds here, so you just sort of occasionally touch on ones that we own or have owned. Sorry, go on.

MR LINDWALL: Or got wrong.

MR HARRIS: No, that one I got right.

MR LINDWALL: You got that one right.

MR HARRIS: Yes, others I got wrong. Sorry, go on.

MS McGOVERN (KMA): Effectively got wrong.

MR HARRIS: Yes, that's right.

MS McGOVERN (KMA): The auditors-general are supported - I don't know if you're aware but they're supported by an international professional framework for auditing effectiveness. I can bring to the commission's attention a definition of effectiveness. "Effectiveness examination is the overall term applied to the analysis of the impact of government efforts and projects. An effectiveness examination may include an evaluation of goal achievement, impact and the relation between impact and resources. Impact refers to the results of an effort in the short, medium or long term".

So the auditors-general, while they already have the capacity to do this, have the methodologies to support them to implement the recommendations that you have put in your report, I would like you to also take into consideration that any recommendation for them to take on extra work would require extra resources.

MR HARRIS: I think that's a point well made. A number of times we have asked - and in fact you were here for Infrastructure Partnerships Australia just a little earlier and that's why I was asking about the capability of the public sector to, for example, assess bids and things like that. So there are references in various parts of our reports to capability, but your point is well made here in relation to the entity that will own responsibility under our proposed model for creating and assessing, particularly post-investment evaluating, whether we got what we needed in the first instance from this investment but also in aggregating and therefore being able to publish benchmarks of what it's costing across a range of very similar projects, so that you're actually informing the market yourself of the potential expectation for the future, that this benchmark says it roughly cost this much to do a kilometre of pipe or whatever.

As you know, I think by your background, the UK National Audit Office does quite a lot of work in this area too which has been a useful input to this inquiry, but your point is well made. We do actually recognise that whatever independent entity does actually have governance control of this process in the future will have to be one which has the competencies to be able to meet the expectations that inherently are in what we're asking for here. It's quite a difficult task we have outlined in the draft report for an agency like this. I think my colleagues have debated at length which of the current institutions of the Commonwealth, for example, might even be capable of doing this and whether any one of them is actually capable of doing this. I don't know whether you have got a view on that.

MS McGOVERN (KMA): I mean, you're looking at an executive agency. The auditors-general of course is a parliamentary agency, so to keep that separation - - -

MR HARRIS: That's true but we can still draw upon the capabilities of the auditor-general if we wanted to propose that in a governance sense, but we have also looked at the abilities of institutions such as the Bureau of Transport and Regional Economics as being a potential contributing entity in this area as well which would have professional competence without a doubt. The question is, do they have the degree of independence that you actually require as well? So we are conscious of this but it's useful to get a submission that focuses on something that often is crossed over, as you say, and to put it on the record as well.

We are trying to find an answer here, I don't think it's actually so evident and indeed we had given some consideration to whether it must be national.

It's hard to imagine doing it any other way, however, even at the cost of potentially losing some support from state-based jurisdictions by saying there's going to be a national entity to do this. It, nevertheless, appears to be the case that it needs to be national. I don't know whether you have a view on that.

MS McGOVERN (KMA): EAROPH has talked about this issue in terms of developing benchmarks across the Asia-Pacific region and we have just talked ourselves into the ground really because the jurisdictions are so different, the languages are so different, the markets are so different. It's really difficult to get comparable standard costing. When I was in treasury I remember trying to get standard costs and just gave up. You actually have to deal with what's before you and do the best you can with that, drawing on what you can but it's not always comparable.

MR LINDWALL: You were about to make two other points I thought.

MS McGOVERN (KMA): I am, yes.

MR LINDWALL: We should let you do those first I think.

MS McGOVERN (KMA): Thank you very much. The second recommendation I make is about the data and if you're talking about making costing data, I would ask you to think about that slightly differently because the cost of construction projects is a smaller part of the whole of life cost of the asset. What's missing and what is able to be collected is data on maintenance and operation costs. So if you're going to put resources into collecting data, I would invite you to put your attention to collecting more maintenance and operation costs of infrastructure than construction costs which vary, depending on technologies and a lot of other things.

So the report recommends at 8.2 that the Australian government fund the development and ongoing implementation of a detailed benchmark and framework. We agree that data is required but it's the lack of available reliable data of the impact on recurrent budgets of these investment decisions. Maintaining infrastructure is much more than a procurement problem. The LGAQ I think stated in its submission to you that 33 per cent of the council's annual budgets are allocated to maintenance. Budgets for maintenance are usually at the lowest level of an organisation with, for example, health districts being required to fund the maintenance of health assets.

There's a substantial backlog of maintenance of infrastructure estimated to be rising and it's not considered in the report. Estimates vary and the data is not routinely collected but the range is between .7 billion and 1 billion of estimated shortfall on existing infrastructure renewal was proffered by the Regional Australia Institute. It estimated a per capita shortfall of between 44 and 54 dollars per annum. I would like to see some better data on that. I have looked at some of the data in terms of the jurisdictions and, as you know, the Commonwealth has a negative net worth of about $390 billion worth of infrastructure, owing 640 billion in liabilities.

The state of Queensland has got 299.74 billion in assets against liabilities of 137 billion, leaving a net worth of 161, and the City of Brisbane has 21 billion of assets with liabilities of 2.2, leaving a net worth of 18.9. So you can see the infrastructure across various levels of government has quite a different impact in terms of recurrent funding. So I request that the commission consider the whole stock of infrastructure and the funding of its operation and maintenance.

There's a tendency to focus merely on additions to the stock. This avoids the issue of addressing the funding of recurrent budgets to maintain new projects; for example, looking to our neighbours, the Pacific Island countries, the Pacific regional and infrastructure facilities partners alone will be spending about 1.7 billion investing in core economic infrastructure between 2008 and 2017. The World Bank estimates the resources required for infrastructure maintenance range from an average of 5.1 per cent in the middle income countries to about 6.9 per cent of GDP in low income countries. Pacific Island countries, we estimated about $1.2 billion per annum is required to maintain their current stock.

So this puts into perspective the differing sizes of funding required to manage the stock of infrastructure. New project costs account for about 20 per cent of the whole of life costs of that particular asset. So I ask the commission to focus on this area, to request data and to recommend ways that local and state governments can fund their ongoing operating and maintenance of infrastructure under their control, given that the Commonwealth funds the cost of construction but there's no flow-through funding there for maintenance and operations except in the general revenue breakdown.

The best way to ensure this is really to involve the community in decisions that affect the costs, that the residents will have to fund in the future. Countries that have been using participatory budgeting and involving their communities have saved funds. They are avoiding investing in unwanted and unvalued infrastructure. Infrastructure services and the standard that they expect have to be paid for and decisions need to be made with the full knowledge of the impact of the proposals at that early planning stage.

EAROPH Australia was a little concerned by the wording in box 14.3 that infer that local governments are a nuisance and that their requirements are a last minute impost on those designing and constructing infrastructure. Risk is always contextual. Experience indicates that engaging with the local communities that need the service will use it and fund it frequently results in budget savings. Local people also have information that is not immediately obvious to a visiting expert. Without options for respectful engagement this information may not be taken into consideration. So communities are generally less ambitious and more focused on necessary infrastructure. Where the infrastructure is being provided to support new industries, it behoves governments to ensure the industries do not shift cost to the public sector or to the public. EAROPH Australia supports the reports called for collection, collation and reporting of data. We suggest that the priority is to collect data on maintenance and operations. Construction data has many variables, design and innovation affecting costs. It is the annual call on recurrent budgets that needs to be managed and for which reliable data is not yet available.

The third point that I'd like to raise before the commission is the recommendation that waste management infrastructure, which is central to effective human settlement management, be funded and financed to meet emerging challenges. I make this recommendation because while the discussion in the report includes the waste management as funded by the Canada fund, the report avoids discussing the funding and financing of waste management as infrastructure.

Waste management is difficult to manage as it's dispersed amongst three levels of government, operates mainly at the local level and is undertaken by a mixture of private sector, public sector and households. But that doesn't mean we can ignore it. Waste management is more than household refuse. It includes solid waste, liquid waste, marine waste, hazardous waste in addition to waste water and general trade waste.

Much of our waste is imported, making our treatment of it dependent on trade policy. Hazardous waste management requires us to manage health risks as well as possible international reputational risks. The New South Wales parliament in 2010 found that waste generation had grown by an average of 4.3 per cent per year, driven by population grown which was responsible for 3 per cent and increasing per capita consumption of 1.3 per cent per annum.

58 per cent of that has been recycled and 42 per cent is going to landfill. Waste management can provide resources back into the community. I visited a waste management station in Daegu in Korea which is re-cyclying waste to generate gas for heating the city. It returned its initial investment in eight years, so it’s very successful. Efforts to fund and finance waste infrastructure need the commission's support. Waste avoidance and recovery strategies require investment and infrastructure. While local fees are an important part of managing waste, hazardous waste management is in the national interest and requires concerted research effort if we are to minimise waste generation and build a recycling capacity across the nation. The relative neglect of waste

management infrastructure in the report is a weakness and I ask the commission to address this.

In conclusion auditors-general have the capacity to independently report to the various legislatures on the effectiveness of infrastructure and on its financing and funding. The full stock of infrastructure, controlled by public, private and household sectors, needs to be operated and maintained, and this requires annual recurrent funding. Data on the annual expenditure required, including the backlog, needs to be collected as a priority. Waste management infrastructure is central to the health and well-being of human settlements and by treating waste as infrastructure and including funding and financing of it in the report will significantly increase its relevance.

MR HARRIS: Do you have questions, Warren?

MR LINDWALL: On the auditor-general part, I know a few people in the auditor-general's and they tend to say that they focus principally on things that have happened in the past rather than things that are happening in the future or likely to. A lot of what we say, for example, cost benefit analysis, is about analysing a potential project.

MS McGOVERN (KMA): That's right.

MR LINDWALL: If it's done properly by the way it should include a discount of all the costs over the lifetime of the project and the benefits over the lifetime of the project. Whether it has been done well or not is a matter of debate but that's in principle how a cost benefit analysis should be conducted and we will be covering it in more detail in the final report.

On the other parts, I think you mentioned about benchmarking. I take the point about the maintenance, collection for maintenance and operations is an important benchmarking dataset and would be useful to collect that, I would expect, as much for the construction, yes, so we can have a look at all of that too.

DR MUNDY: I think it certainly was the case, certainly in the 90s, that the Commonwealth did actually publish what it spent on what it deemed to be the national highway, both in terms of minor works and in - - -

MR LINDWALL: If wasn't operating then.

DR MUNDY: Yes, it wasn't operating and certainly the late Senator Collins used to regularly request it. I just want to turn to this issue around the auditor-general. I'm not hostile to the notion but I guess what concerns me to some extent is two things. The first is our infrastructure arrangements are increasingly becoming mixed, so that would presumably - particularly to get a national picture and also obviously there are jurisdictional issues but it's probably part of the same problem but you raised issues around operating costs.

Depending upon how an industry is structured, operating costs might be - for example, consider a railway industry. If there's a vertically integrated public rail operator then all those relevant costs lies within the normal remit of an auditor-general but if the rail industry say is vertically separated or today you have a public airport and a pile of private airlines, it ceases to be clear where the relevant operating costs from the point of view of the industry as a whole actually lies.

To develop a circumstance where we have suitable comparisons and jurisdictional comparisons, and we heard from IPA before about the need to start benchmarking city performance, how would you see auditors-general operating in a space where the relevant information that we're interested in may not always sit within the public sector and may not always be accessible by virtue of some form of contract or concession granted by the state? For example, AGL provides the gas services in New South Wales under nothing other than what it has done since 19-whenever.

MS McGOVERN (KMA): Way back when.

MR LINDWALL: Way back when.

MS McGOVERN (KMA): Were you aware that the auditor-general's legislation has been altered to amend it to enable it to do cooperative audits and projects and that it has done one on the Mercy Community Hospital in Tasmania, so it can bring together the different jurisdictions and cooperative audits are now being done right across the region, not just here. So there's a lot of models for cooperative audits.

I would caution you against looking at the auditor-general as an executive agency and remind you that it's a parliamentary agency, so it has really got the focus on the long term, and when auditing effectiveness it can look at the structure of the markets over the long term and report to the house on whether or not they believe it to be in the best public interest. So in terms of an executive agency, if you're looking for someone to actually review the markets and to report on them then you look at something like a commerce commission rather than the auditors-general.

MR LINDWALL: Or a commission such as our own.

MS McGOVERN (KMA): Or indeed a commission such as your own, yes.

MR LINDWALL: But the role the auditor-general has traditionally played and can presumably have even an enhanced role in these circumstances is evaluation because it goes to Paul's point a little earlier. Cost benefit analysis being prospective, the valuation being necessarily a set of circumstances where if we have a transparent cost benefit analysis and a set of objectives that were proposed as a consequence of that and then we have a project and then we build something and it starts operating, the auditor is in a perfect position to do the evaluation because all of the data and information is available against which you could benchmark: did you get what you paid for?

That will contribute very heavily to a benchmarking of asset performance in future, if you did that consistently across a range of similar assets perhaps procured under different models or you can note the differences but this benchmarking thing, we believe is going to be tremendously important. Whoever and however contributes to it, it's probably a thing that will most prove up whether the sort of model for infrastructure development that we've talked about, the pipeline being a pipeline and transparent publications, actually succeeds or not.

If you can't do a benchmarking exercise in five years' time then you haven't developed a pipeline. All you've done is fund a few projects. It would be a summary way of looking at it. Therefore, your point about the auditor is quite important because some entity needs to take responsibility for this which is being an entity which is likely to do both a thorough and an independent job.

MS McGOVERN (KMA): And auditors-general doing effective audits can bring together different people and look at intractable problems with a variety of stakeholder input. We certainly did in New Zealand in effectiveness audits. They can also audit methodologies. That’s a contribution that they can make.

DR MUNDY: I mean, are there things we could do or recommendations we could consider that would assist auditors general when they come to do, because one's expectation as auditors general operate, presumably, on some form of sampling methodology which we wouldn't be expecting auditors general to check off the analyses of every project that was entered into by Queensland Transport.

MS McGOVERN (KMA): It's very costly.

DR MUNDY: Certainly, in a Commonwealth agency, which I used to be a director of, we used to have what were called benefits realisation statements, because it's one thing, of course, to say, well, you know, they have done all of this and they have done this VCR properly, it's another thing to come back, and a very important thing to come back and say, "Well, three years ago you said the benefits were going to be these, and they haven't been. We have actually looked at eight of these, and you have never got the benefit."

Are there things that we can do and recommend to facilitate - because I think there needs to be a framework for learning about - costs are easy, because you have got to write cheques for them usually, or at least the bulk of them, but the benefits, once the thing is built, and there is no feedback and learning, so your experiences in the audit field, are there things that can be put in as almost procedural that required, that would facilitate that sort of analysis?

MS McGOVERN (KMA):   Just for a moment stepping away from the question I think, getting more to your intent, there're a lot of reports being done by auditors general's with recommendations that perhaps could be taken up by the commission. There're very specific recommendations that, if they had a hearing and an advocate in the Productivity Commission, that may well help to actually implement some of these and to achieve some of the objectives, because the audit office is really looking at improving long-term public administration.

DR MUNDY: Yes.

MS McGOVERN (KMA):   The office is often the only advocate for the long term in your whole governance structure; so if the audit office in the various states and the federal government have already done reports, I would encourage you to look at them and have a look at their recommendations and to make sure that you are supporting or, where there're changes, that you can identify where those changes are, because it's the follow-up on the reports that is the thing that most auditors general find frustrating. They do a lot of work with a lot of skilled people, they put a report together and you probably have exactly the same experience.

DR MUNDY: We are familiar with that challenge.

MS McGOVERN (KMA):   So I would suggest that supporting the recommendations that are in a number of reports already could well - - -

MR LINDWALL: I just want to quickly point out, mention that you are quite right that waste management is an important part of public infrastructure such as the Romans recognised 2000 years ago.

MR HARRIS: Okay, on that point, the Romans, it's a good point, as good as any. So thanks very much for your time, effort and contribution here today. We really appreciate it.

MS McGOVERN (KMA): Thank you.

MR HARRIS: Now, I think we have another set of engineers, the Institute of Public Works Engineering Australasia. For the record, could you please identify yourselves.

MS BARNES-GILLARD (IPWEA): Suzanna Barnes-Gillard, Institute of Public Works Engineering Australasia, Queensland division.

MR BANNAN (IPWEA): Joe Bannan, Institute of Public Works board member.

MR HARRIS: Okay, and for today's hearings do you want to make some opening remarks, or can we go straight to questions on your submission?

MS BARNES-GILLARD (IPWEA): Basically, we put in our submission around only the accreditation of engineers, we have just addressed that particular part.

MR HARRIS: Yes.

MS BARNES-GILLARD (IPWEA): The institute is a federated Australasian body, which sounds very strange, but we do advocate a national standard, a national accreditation system, because we believe that that is needed, because of the mobility of people these days, and also the success of the Queensland accredited scheme.

MR LINDWALL: So you would like to see a national scheme based upon the Queensland scheme, basically?

MS BARNES-GILLARD (IPWEA): Most definitely, and we wouldn't like to see any less at all. It's very important to maintain that standard.

MR BANNAN (IPWEA) : In our submission we did reference the need for good professional practice, the risks that exist around provision of infrastructure, the types of things that can fail. Sometimes it's just faulty infrastructure that doesn't work as well. Sometimes it can be the collapse of infrastructure and, as was mentioned in the previous presentation, the long whole of life cost attached to long-life assets, when the initial upfront costs where a practising engineer constructs something, that's only a small part of the costs; so are far as productivity is concerned, considering the whole of life aspect, then the need for good high-quality engineers is an important part; so registration we believe is the mechanism to assist there. We reflect on the need for registration of doctors and solicitors and plumbers, so tradespeople, that's how we decide who was going to do the work for us at home. In a similar way, we would think that that should be the focus of someone procuring engineering services.

MR HARRIS: So we heard this morning from the Board of Professional Engineers, who are strong advocates of something similar, and where we got to effectively in that discussion was this question of if there was to be some kind of standard, can it be national in nature, or are we condemned to repeating the vulcanisation of professional qualifications that has occurred across the other professions and the entrenchment of different standards in different jurisdictions such as would then result in reducing labour mobility between the states. Are you part of any process that's currently looking at this?

MS BARNES-GILLARD (IPWEA):   Yes, nationally we are. The institute is one of the bodies with Consult Australia, Engineers Australia, Professionals Australia, I think as well, and have been looking for some time at how to make a national scheme. Maybe, because of legislative differences and all that sort of thing, it would be necessary to have a scheme that's in a way state-based, but still goes across borders; so a national scheme is ideal because if you're working in Western Australia and you come to Queensland right now, and you have to sign off or supervise people, you have to be registered, you have to go through the process.

We recently have become an assessment body for RPQ. That's not what drives our need to want to have registered engineers, it's the need for good service and quality for the community. I think the other part to remember in anything that we look at is the continuing professional development that when you are registered, registered engineers are subject to audit; so if you have a scheme, whatever that scheme is in any state, at least what you know is people have to do their 150 hours, the same as doctors do and the same in other professions. They have to keep their CPD up, and that forms the basis of a good scheme.

MR HARRIS: So the other issue that came up again this morning, and has come up in a number of areas, but the board - was this engineering skills shortage, and I think you have made some comment or submission on that. Interestingly, we heard this morning that in Queensland, and I guess your focus is in Queensland, that there has recently been a reduction, if not an elimination, of the skills shortages that were previously experienced in engineers. Would that be your own experience currently?

MS BARNES-GILLARD (IPWEA):   There are currently in our sector, which is more the local government and public works sector, there are certainly less positions available. There's probably a couple of reasons for that; people are doing more with less, but I think the skills shortage in Queensland is probably levelled out a bit better than some of the other states and registration of engineers has gone up, which is great.

MR HARRIS: Yes, I think we heard this morning - what was it - a number like 20 per cent anyway. You got a very high increase in - - -

MR LINDWALL: So do you think this is a temporary aberration, that the skill shortages will recur, or is it something that we have had a systemic change and we're now likely to have a reasonably state-equal system? It's speculation, isn't it?

MR BANNAN (IPWEA): It would be just speculation.

MS BARNES-GILLARD (IPWEA): Local government go through peaks and troughs obviously and we have just had some de-amalgamations and that changes how staff operate across that sector. Some of the mining has changed and some of the people who had gone to the mining sector have come back into the local government and public works sector. That's just swings and roundabouts all the time, whether there's mining projects or not. Those changes - when you have a body of people, they go within sectors continually. They go within the consulting industry and within local government and within the mining sector.

MR LINDWALL: Many submitters have requested that there be a better pipeline of projects in Australia and presumably also in Queensland. Have you anything to comment on that?

MR BANNAN (IPWEA): I think where industry can observe a constant flow of infrastructure projects, there's a better ability to prepare and maintain a steady workforce. I think that's fairly commonsense. I think most of our members would consider that.

MS BARNES-GILLARD (IPWEA): Yes, and I think what has happened - if you look at the last few years, you know and we have had some fairly catastrophic events of floods and cyclones and that where sometimes some of the capital works projects that might have been programmed to continue that workflow are put on hold because of flood works and restoration. Then the capital works projects, while they're not shelved, they continue, but what happens - at the same time as the maintenance projects are happening as well. That I think is a big part of it as well.

DR MUNDY: In item 1 in your submission you talk about local government debt and the risk aversion of local governments to debt.

MS BARNES-GILLARD (IPWEA): That's in the national CEO's submissions.

DR MUNDY: Okay. Can I just ask you a couple of questions as it might relate to Queensland?

MS BARNES-GILLARD (IPWEA): Okay, because we hadn't really addressed it.

DR MUNDY: Can I ask you, is it your view that Queensland local governments are risk averse when it comes to debt? I'm merely curious because there seems to be six and a half billion dollars of debt outstanding to them. If you don't feel you're able to answer, that's fine because it may well be that there are different - well, I know there are different arrangement in different jurisdictions.

MR BANNAN (IPWEA): That particular comment, the way I read it, is referring to a local government's perspective around its willingness to borrow or how much debt it holds and - - -

DR MUNDY: Could I perhaps ask if you could ask your colleagues whether they believe that is a nationwide issue or is it confined to certain jurisdictions, because that would be very helpful.

MS BARNES-GILLARD (IPWEA): Certainly.

DR MUNDY: Because, as I say, 6.6 billion at June 30 last year and that was about 800 million higher than June 30 the previous year. There's some interest rate variation issues in there but it doesn't strike me that governments in Queensland and local governments are necessarily running away from debt.

MS BARNES-GILLARD (IPWEA): I don't believe in Queensland they were.

DR MUNDY: I suspect that is the case, but it would be helpful, given your national organisation has made this claim, if they could identify where they think the problems really are.

MS BARNES-GILLARD (IPWEA): Yes, certainly, and back to that same email address?

DR MUNDY: That would be fine, yes. Thank you.

MR LINDWALL: In principle if you had a state-based registration scheme because of the constitutional issues and they weren't referred to the federal government, say, you would want them to be matched to the Queensland one but automatic mutual recognition so that if you are registered in New South Wales, you could automatically work in Queensland without any new work application?

MS BARNES-GILLARD (IPWEA): Yes, and I think it's much like a driver's licence. You know, I have a driver's licence in Queensland and I go to Western Australia and I can go hire a car and drive it.

MR HARRIS: That's an important comment for us from the point of view of this idea of registration, so thank you for making it. Okay. We have nothing more for you so thank you very much for your time today.

MS BARNES-GILLARD (IPWEA): Thank you.

MR HARRIS: In the program we were going to go to afternoon tea, which just means everyone gets a cup of tea 10 minutes early, and I think we have got the Local Government Association of Queensland after that. Cup of tea time.

MR HARRIS: Let's restart now and I think the Local Government Association of Queensland. Thanks for making the time today. If you could identify yourselves for the purposes of the transcript, that would be great.

MR HOFFMAN (LGAQ): My name is Greg Hoffman and I am the general manager of advocacy of the Local Government Association of Queensland.

MS TALBOT (LGAQ): Simone Talbot, manager advocacy, infrastructure, economics and regional development, LGAQ.

MR McMILLAN (LGAQ): Roland McMillan, principal adviser, economics and finance, LGAQ.

MR HARRIS: Do you guys have an opening remarks you would like to make?

MR HOFFMAN (LGAQ): Yes, we do. Thank you for the opportunity to appear at these hearings. As you would be aware, the Local Government Association of Queensland is the peak body for local government in this state. LGAQ provided submissions on both the issues paper and the draft report, reflecting the importance for these matters to local government. By way of brief background, Queensland's 77 councils manage $76 billion worth of non-financial assets with an average of 1.8 billion of assets being added to local government's asset base each year for the past six years.

The quality of these assets, that being local roads, water, sewerage, waste, as well as a variety of community and recreational facilities impact the daily lives of all Queenslanders, as well as contribute to local, regional and state economic outcomes. Over the past 10 years increased local government costs in providing services and infrastructure, including servicing debt, has been primarily met from efforts to increase owned source revenues. Queensland's local government's total general rate revenue has increased by approximately 100 per cent in nominal terms over the past 10 years.

Growth in local government-owned source revenue is limited however, forcing many councils to consider ways to cut costs, defer capital investment and improve the efficiency and effectiveness of key service delivery. For example, key examples include council's leveraging scale in the provision of back office systems, bulk procurement arrangements for materials, plant and services, consideration of alternative institutional arrangements, especially for roads and water, as well as strategies to influence the consumption of assets in order to defer capital expenditure, as well as council's overall asset management strategies.

With respect to the latter, LGAQ suggests demand management initiatives be elevated as a policy priority at both a Commonwealth and state level and further supported and/or incentivised, given that many of the supply site challenges associated with the provision of infrastructure are likely to exist for many years to come. Further exacerbating supply site issues from a local government perspective is the fact that, firstly, council-owned source revenues have been negatively impacted by state government placing a cap on infrastructure charges, with the current charges currently under review and under pressure for further reductions; secondly, funding assistance from the Commonwealth has remained relatively static in nominal terms with Queensland state government funding declining in nominal terms by over 50 per cent over the last decade, based on analysis undertaken by the association using data compiled by referencing budget papers and program information.

Thirdly, in some cases strict environmental legislation and standards have increased operating costs and to a certain degree forced the over-capitalisation of assets, this is especially the case for sewerage treatment plants. Fourthly, certain legislations such as the Trade Practices Act has in the past complicated regional procurement arrangements of large-scale infrastructure projects where considerable costs savings have been achieved. Fifthly, in regional areas service and infrastructure demand for resource sector projects is placing a growing burden on local government, including additional costs associated with increased demand from the transport task and supporting site-based workforces. These costs include capacity, augmentation and additional maintenance due to accelerated depreciation of assets through high rates of consumption. Typically, this is paid for by local governments and their communities and represents a significant opportunity cost to the councils.

Sixthly, cost shifting by other levels of government contributes to local government costs. As a result, Queensland councils provide services and infrastructure that in most other parts of Australia would be provided by state and Commonwealth governments. In some communities, this includes childcare, education, health and housing facilities and services. On the matter of pricing in relation to roads, LGAQ supports the work being undertaken by the Heavy Vehicle Charging and Investment Project, the HVCI.

In an intermediate step towards applying this to light and private vehicles, LGAQ recommends that an increased amount of current taxes charges and excises et cetera collected from road users ostensively for roads be returned to road infrastructure managers at all levels of government according to their respective responsibility for road assets. Qualification is the key element in improving the connection between demand, costs, revenues and provision under existing revenue collection methods for roads, as it improves transparency and accountability and makes politicisation of project selection discussed on page 238 of the draft report more difficult in LGAQ's opinion.

In relation to water, external structural and community characteristics often limit councils' opportunities to implement sound financial strategies, further impacting their ability to reinvest in infrastructure, maintenance or upgrades. Councils, particularly those servicing dispersed communities in remote towns, are often unable to secure sufficient economies of scale to provide a complete range of services at a reasonable cost. The reality is that many small councils cross-subsidise water and sewerage from other revenue sources, as it is rare for a small service provider to be able to fund capital and operational expenditure, let alone depreciation, from water and sewerage revenues.

From a community perspective, the public are generally not aware that traditional pricing levels have mostly not been cost reflective, with communities often angry when asked for pay more for a service that they assume has been provided substantially as a public right for many years. While user charges may provide revenue for some infrastructure, it should be recognised that due to low population density and low usage rates, in many regions, there will always be infrastructure assets that are not financially viable in the direct cost recovery sense. It will remain a core role of government to provide infrastructure to meet a level of public welfare required by communities which is not being provided by the private sector for reasons of insufficient rate of return, scale or other economic reasons.

That being said, the association does believe there is scope for and evidence of public-private partnerships to deliver and operate some significant projects. Elements of water treatment are outsourced in Townsville and Mackay, for example, and beyond a lack of suitable drivers or incentives, there is no reason why this type of service provision could not grow. Private contractors deliver service on behalf of public sector entities, including reticulation, construction and maintenance and meter reading, for example; are prevalent in other states and in New Zealand with clear efficiencies in some instances.

In summary, it is evident that funding from other levels of government to local government to achieve fiscal equalisation and flexibility for local government to generate other revenues will be key if local government is to continue to deliver services and infrastructure for all communities, whether directly or through a service provider. Reform of governance and institutional arrangements must include an examination of the need to change current restrictions placed on local government revenues, including on user charging as well as legislative restrictions on financing and procurement options. Thank you very much.

MR HARRIS: No, that's fine. I think we have got about 20 minutes to ask some questions of you. I guess my primary interest is in areas of benefit capture type of projects in infrastructure. I don't think you referred directly to those but they are in your original submission. Would you say that it's becoming an increasingly accepted concept for local government to at least consider financing some part of the infrastructure by the equivalent of benefit capture and if that's the case, do you have any feeling about the impediments to this? You have mentioned, for example, capping of rates and things like that as being standard practice from state governments, so it would tend to limit you with the most direct mechanism by which you might undertake some benefit capture.

MR HOFFMAN (LGAQ): Let me first make certain I'm understanding your question and the context. Benefit capture being contribution by the beneficiaries that are given a development entitlement which adds value to their investment, primarily?

MR HARRIS: Yes, that's right.

MR HOFFMAN (LGAQ): Okay.

MR HARRIS: Well, in a particular local government area. There have been examples of this in Queensland, so benefit capture applied to the Gold Coast like the rail project, I think, and there were suggestions that it applied to the Ipswich motorway, although I am not myself able to recall them but I know that suggestion was made there and we have been told in the submission from the south east Queensland mayors that they were actually working on a project for this purpose. We thought south east Queensland mayors might be available to be here today but I am treating you as a sort of substitute for them and you may well be familiar with what they have been apparently working on.

MR HOFFMAN (LGAQ): I am familiar with the initiative they are developing, so can make some general observations about it. The principle of benefit capture certainly has been talked about for some time. This state does not have standing legislation or provision for that to occur at a local government level. It certainly was contemplated with the then creation of the Urban Land Development Authority by the previous state government, wherein it envisaged that benefit capture provisions would see the beneficiaries of the expedited development and approval processes in designated areas.

The view is to cover or support in covering some of the costs of the infrastructure provision. There are two aspects of the infrastructure provision, that provided by state government and that provided by local government, and as you are familiar in this state, the issues around water and sewerage have gone through transition in the past five or six years. In short, those objectives have not been realised in those urban land development areas, I would say very much because of the cost implications to the developers themselves.

MR HARRIS: Right.

MR HOFFMAN (LGAQ): Local governments have sought to recover through their development charging regime the reasonable costs of their development and the capping of infrastructure charges and the regime around cost recovery in that respect has in fact denied councils the opportunity to do that in a way in which they see fit. The argument from the proponents of the development is that the revenue generated by increasing value and hence increased rate revenues represents the benefit that is received.

We would challenge that in a number of respects because increased revenues obtained from the land valuation created as a result of the development, or for that matter revenues from water and sewerage service provision, in fact are generated to cover the costs of the services provided. They are not taxes per se. They are in facts costs or revenues to covers costs and one of the most difficult aspects of development for us, particularly in significant and large scale developments creating significant water, sewer, road and stormwater related networks, is that immediately they are built, they come at a cost of depreciation which under regimes now in place require a very significant provisioning for those costs from an early point in time.

So from a local government perspective there is no ready windfall that might be suggested from these developments, and our ability to recover all directly or immediately benefit from those developments if fairly limited. If I could move to your other question about the regime under consideration, hereby the south-east Queensland mayors. I caveat my statements in that I'm not authorised to speak on their behalf but I can explain.

MR HARRIS: No, we thought if you knew about it since they're not here - - -

MR HOFFMAN (LGAQ): It has been developed on the basis of what is known within this aspect of financing of infrastructure as a variant or expansion on the Manchester model developed obviously in the UK where the parties involved at a government level, in this case, the number of local governments, south-east Queensland, and the state government would agree that the increased revenues obtained by way of taxation or other charges that come to government as a result of the development are in a certain form returned to local governments as a means of contributing to their infrastructure and other related costs.

The model requires in general that all of the parties to that agreement, in this case the local councils, the local governments in south-east Queensland are to agree, the state government to agree, and it is in effect a hypothecation of revenue generated to state government being returned to councils. That revenue generation is then used by way of an agreed framework and approach to the prioritisation of infrastructure provision within the area to meet the development that occurs over time.

So it very much relies on a long-term collaborative arrangement between the local governments and the state government for, if you like, the costs and benefits of this process to be achieved over time. I hasten to add that it's probably in sentiment not dissimilar to the offerings or proposals made by the federal treasurer to the state governments in relation to the sale of some of their assets in a recent conversation between the treasurer and the state treasurers in that regard, in a sense to agree to invest in assets or divest in assets and there's a consequential tax or benefit that flows.

MR HARRIS: Thanks.

DR MUNDY: Can I ask you a couple of questions about costs. You alluded to competition issues or issues impeding presumably collective purchasing. Now, I understand that section 4D is long gone. Presumably what you're talking about here is the ability of councils to collectively procure. My understanding is that the ACCC is generally much more relaxed about authorisation and procurement arrangements than it is about authorisation to selling arrangements, so have councils tried and failed or what's the situation?

MR HOFFMAN (LGAQ): No, they haven't tried and failed. We identified it as a hurdle to the process which of itself is a regulatory process requiring time, effort and resource to undertake the required processes, the incidents being or the most significant incidents of where eight councils in central Queensland seeking to aggregate their waste collection and recyclying activities chose to do so but in creating that aggregation then confronted the prospects of market impact that required ACCC engagement.

The issue was a need to demonstrate public benefit as opposed to impact on market. That was done but we simply highlight that as a consideration. Importantly, this was an activity of public sector entities as opposed to private sector entities and therein lies what we think is perhaps a different level of consideration in those instances.

DR MUNDY: Okay. You mentioned issues about water treatment plants or sewerage and I got a sense the regulatory requirements were leading to additional costs. Is that the in sense that it's your view that these legislative standards or the regulatory standards are excessive to what is required? Are they standards that are being imposed and they're not outcomes based and what's the nature of the problem?

MR HOFFMAN (LGAQ): They primarily relate to environmental standards and of course there's conjecture as to what is appropriate or inappropriate in that respect. The point behind the comment is the increase in discharge requirements into riverine watercourses, ocean outfalls and the like have significantly increased and not necessarily wanting to debate the merits or otherwise of that, the implications are that those increased standards from primary, secondary, tertiary and beyond have added significant cost implications to local governments' responsibilities in that regard.

That was happening at a time when the state was withdrawing or was significantly reducing its support, the infrastructure support subsidies and the like, for that to occur. The debate I guess continues as we look to discuss the merits or the relative merits of economic, environmental and social demands. As I said, it occurred at a time when the environmental considerations were on the increase, at the same time the economic supports were on the decrease.

I would suggest then the point that we're making here is that the regulatory impact assessment processes either don't or are built around processes that don't necessarily have enough disclosure or preidentification or presetting of the criteria, the weighting of the criteria and the ability to actually debate in a proper or full sense what those weightings would appropriately or could appropriately be.

DR MUNDY: Just briefly the last thing. I got the impression and I think you and I have discussed development charges more than once - - -

MR HOFFMAN (LGAQ): Along with many others.

DR MUNDY: Along with many others. The sense I get from what you've said to us today is that development charges at least in Queensland are not a vehicle by which councils are generating some sort of rent from developers; that there's not in your sense an issue of over-recovery. Some suggest that councils are using development charges as a device to effectively augment the rate base. It seems to me from your evidence today that that's not the case in Queensland. I just want to be clear about that. And perhaps secondly, if you have evidence of costs and revenues from developer charges, matters, readily available, if you could provide us with that, unless we've already got it, that would be very helpful.

MR HOFFMAN (LGAQ): Thank you for asking the questions. It provides an opportunity to make the point again. We would confidently assert that there is no revenue grab taking place out of infrastructure or developed the charges in this state. The attempts to accurately definitively identify costs against infrastructure needs in a particular local government area, or a niche local government area, on a time frame of three, five, 10 or more years, is an incredibly complex exercise, and the reactions to those efforts are through the late 1980s, more likely the 1990s, not only the cost to undertake those exercises to legitimise the costs, charges, being to councils as high as they were, but also the outcomes of that to developers, when in fact we were looking to identify what it really costs. In fact, the was the development industry that asked for that process to, in their mind perhaps, prove the point that there was being overcharging, in fact produced the opposite result, undercharging.

That process then subsequently saw government intervention, the previous state government, to introduce a system of capped charges, a capped charge regime on a state-wide basis. Inevitably, a regime of that sort was going to see undercharging and overcharging occur, unless councils were of a mind to adjust charging, particularly down, because they didn't have an ability to adjust it up to respond to those circumstances.

The current situation, this issue is currently in debate and decisions from the current state government are pending on further changes to those regimes, but our evidence and our research of late, in contributing to this current discussion has again confirmed that the average charge regime by and large is under-provided for the real costs. I'm happy to provide you with that research material. The policy parameters around which the debate is taking place is what can be done to stimulate development. If reducing costs to, in this case, developers stimulates development that might not otherwise be there, then the policy objective is deemed to have been achieved, given the desire to promote that development, or that aspect of the construction industry.

If that occurs, and it occurs on the basis of under-recovery of costs, it simply transfers those costs to another part of the economic cycle. In this case, to the broader rate base of local governments, effectively then they are obliged to shift or change their priorities from other community needs to enable that other priority set by government to be achieved, and therein lies the policy debate about the importance of communities setting priorities and the community deciding its imperatives and its priorities.

MR LINDWALL: Last year there was a proposal to have a referendum on the constitutional recognition of local government, and you mentioned earlier about cost shifting amongst governments. Is that part of the mix? Is that something that's still important or have we moved on from that particular issue?

MR HOFFMAN (LGAQ): We have moved on from the issue of recognition in the constitution, not that it hasn't been a generation, or several generation long objective, for people in local government; but the issue still remains, recognition or not, as to the role of local government within the federation.

Certainly, there are transfers from federal government to local government, and the key objective of the constitutional based recognition was to remove beyond any doubt the ability of the Commonwealth to make those transfers, directly that is, other than through the states. The doubt still remains of the prospect of High Court action in one particular instance, to that occurring.

The importance of those direct transfers is important because of the efficiencies that a direct transfer can provide, other than through the conduit of the state. I'm not saying that it can't occur, but it adds inefficiencies to the process. It also is the federal government's advantage in a number of respects in that its ability to deliver on its key priorities at a local level is enhanced by way of that direct relationship, so it can be effective and it can be efficient if it is done that way.

Also at a time when there are significant constraints on state revenues, then ensuring a ready and easy transfer in a government or financial relationship between the three partners in government, I think is to the broader community advantage and not to have the constraints of constitutional bars or requirements impeding upon what can and should be done efficiently effectively in a very timely and responsive manner.

MR LINDWALL: Given that you mention then potential for High Court action, which I hadn't been aware of, does that mean that some projects might be at risk because the financing is coming from the federal government and it's uncertain in some way?

MR HOFFMAN (LGAQ): Yes, that is the case. I'm trying to think of the particular programs. I might ask my colleagues. Roads to Recovery is a program that has been in place some 10, 12 years now, longer perhaps, and that sees a direct funding regime between federal governments and every local government in the country. That is one particular program which, based on High Court decisions in the past could well itself be subject to direct action, and that concerns us very much.

DR MUNDY: The issues seems to be whether the Commonwealth has a constitutional head of power. If the head of power exists the problem doesn't seem to exist, but roads doesn't have one.

MR HOFFMAN (LGAQ): Correct.

DR MUNDY: If that's the issue.

MR HOFFMAN (LGAQ): Yes.

DR MUNDY: If it was some other related matter the court, I think, has indicated that that would be okay.

MR HOFFMAN (LGAQ): Yes, that's correct.

MR HARRIS: Perhaps, since we have got a limited amount of time left, can I just ask you about one specific aspect of the draft report where you made some comments, but it wasn't quite clear where you actually stood, which may have been deliberate, but may not have. That's in relation to Project Pipeline, so we have recommended a structure in the draft report which describes the development analysis design work on a continuous publication basis as being the creation of a pipeline, effectively the visibility of each of those reports offering good knowledge to a marketplace, whether it's a public policy of a private investment marketplace of certain developments.

In your comments you say an effective pipeline would require strong design and implementation activity, but it wasn't clear whether you thought what we described was sufficient or not. I must say, when I read the submission, I took it that you thought it was not sufficient, but you didn't say what was required to strengthen it. However, others have read it internally and decided that you probably thought it was sufficient, so can you tell me what you actually thought.

MR HOFFMAN (LGAQ): It's a very good question late on a Friday afternoon.

MR HARRIS: Sorry to be - - -

MR HOFFMAN (LGAQ): Could I defer to my colleague, Roland McMillan, to answer that.

MR McMILLAN (LGAQ): Certainly. On that section they did seem to be more involved in what was being suggested, albeit a brief outline in the draft report. I think we pointed to the state government here having a major projects database, and having undertaken similar work in the past. It has a three-section approach where it talked about under way, approved and planned projects. Perhaps the issue that we would note in our submission was more about pipeline projects requiring longer-term funding certainty, especially for local government, and I think that that would be the main constraint on local government participating in that type of system and that is where you're reliant year to year on a funding program, you just have no way of planning realistically beyond that scope. I think we also indicated that longer funding program commitments would be a reasonable aspect of that initiative.

MR HARRIS: So you're saying effectively it would be good to have a framework from the state which didn't just publicise the planning in a transparent fashion of availability of projects but actually said, "And within this there's a five-year framework for funding," or something with longevity attached to it.

MR McMILLAN (LGAQ): Absolutely, and especially critical to local government.

MR HARRIS: That's great.

MR HOFFMAN (LGAQ): Could I add just another comment to that. In this state we have had over many years varieties of what are called regional plans and those regional plans come in different forms. One of the key points that local government has made to state government in creating this regional plan is that they need to come with a related infrastructure plan.

In other words, if you are looking to promote economic or regional development in a given region of a particular type over a particular period of time, then what importantly is the infrastructure provision to support that? Unless the two come together in a fashion that provides some certainty for investment, whether it's public sector investment, which is what you're significantly talking about here, and the priorities that relate to that, then the potential achievement of the broader objectives of the regional plan are going to be constrained.

That is the point of particular importance at the moment to the Council of Mayors group in south-east Queensland where the south-east Queensland regional plan has been remade and the infrastructure implications of that are of high priority to them. Similar concerns exist obviously in high growth areas where you can't have one without the other, or successfully have one without the other in a way that is meaningful to all parties, public and private sector.

MR HARRIS: Okay. We will need to wrap it up there because we have to go to the phone now for another person who is waiting in Canberra for a call, but I would like to thank you for your contributions in both the initial and - comments on the draft and for your comments today and for the possibility of you providing further information in response to the developer levy question. That would be great. Thank you very much.

MR McMILLAN (LGAQ): Thank you.

MR HOFFMAN (LGAQ): Thank you very much.

MR HARRIS: Now I'm going to try and make the phone work again, which will be tremendously impressive. It's not disconnected anyway.

MR ERGAS: Hello.

MR HARRIS: It's Peter Harris here. Is that Henry?

MR ERGAS: Yes, it is. Hello.

MR HARRIS: G'day. Sorry we're running just a few minutes late here in Queensland, but I have got Warren Mundy with me here and Paul Lindwall.

MR ERGAS: Hello.

DR MUNDY: Hello.

MR LINDWALL: Hello, Henry.

MR HARRIS: You're on the speaker with a small audience but nevertheless a deeply enthusiastic one.

MR ERGAS: Highly expert one.

MR HARRIS: Highly expert one. I'm sure that's certainly the case. We did get a chance to quickly read the supplementary comments that you sent through and I guess if you wanted to speak to the question of capital recycling in any shorthand introduction fashion, that would be great, or indeed other issues, or we could just jump straight into questions.

MR ERGAS: First of all let me apologise for the lateness of my supplementary submission but it wasn't because of any lack of enthusiasm. It was simply time constraints. I should also apologise for the fact that in the version you have I have just noticed - and this is what happens, as I'm sure the three of you know every bit as well as I do, when you set out to write something at 5 o'clock in the morning - some typos have crept in, and so I'm going to be sending in hopefully an intelligible version shortly, so my abject apologies for that.

In essence, before I get to that, let me say that you should be congratulated collectively and to the staff that worked on the report. I think it's a terrific product, very important. It raises and addresses the right questions. It has the additional benefits that it strengthens both my biceps in carrying it around for a couple of weeks as I tried to read through it, so it's mental and physical fitness combined. I think it's a really very good piece of work.

I should say that I have comments that go beyond the simple issue of capital recycling, it's just that I haven't quite had time to write them out but I will. Also it was helpful for me to try to think through the capital recycling issue because you did discuss them and I have raised them, I think not terribly clearly, in my initial submissions, so that's the genesis of the notes you now have. I'm happy to talk to it but I'm also happy to address any other questions that you might have.

MR HARRIS: I think we could probably go on with the questions because we will do a bit of elaboration for everybody present just in the intro so that it's clear where we're coming from. Look, we understand the need, as you say, for swiftness. Getting something in is the vital thing for us because they are pretty short time lines for a complicated inquiry like this, so it's just very good of you to have provided stuff.

My questions weren't going to be on capital recycling. Mine were going to be on the institutional arrangements for road user pricing. You will have noticed in the report that we went quite a long way towards trying to emphasise the need for some institutional structure to take on responsibility for this. Obviously we talked about light vehicles and potential for some form of electronic pricing in the future and that attracted a bit of attention, but the real purpose behind it was to say these things are plausible but need an institutional structure to absorb them and the heavy vehicle charging initiative has languished for a couple of years on the COAG agenda without actually having any implementation and the same thing seemed to us to require some form of institutional structure.

We did combine the two and there are views around which say you should keep them separate, but we found it hard to conceive of an arrangement which would move ultimately towards pricing but which nevertheless was discriminatory between different classes of road user, and I was interested in getting your opinions on that.

MR ERGAS: I found that section of the report very interesting and the discussion of the alternative models I think was a very useful discussion. As you will know from my initial submission, my preference - and I wouldn't put it much more strongly than that - was to try to manage the road access, commercial access, and that seemed to me required a reasonable degree of integration of responsibility for operations, pricing and investment position. I thought that was a useful approach to try to take in terms of integrating responsibility for those in that it meant that you could use the price system not merely to allocate the existing road surface but also to inform management decisions and to inform investment decisions through financial constraints but also by signalling user demand.

I thought something along the lines of the New Zealand approach but with perhaps a bit more explicit corporatisation to it seemed promising and I also thought that it would be important from the point of view of ensuring that efficient decisions were taken and that consumers had confidence in those decisions to move to some form of independent regulation of charging, though I must say I wasn't necessarily thinking of that regulation taking exactly the same form as it takes in public utilities. I think that there can be very good reasons to price-raise on a different basis from the basis on which you price-raise electricity transmission, but the broad model of having an independent regulator review charges seemed to me essential if you were both to provide independence for the organisation but also to provide users with the reassurance that they wouldn't be exploited by what would be a monopoly asset.

That was really my view of that discussion. I fully agree on the need to have an institutional arrangement that can drive or transition more efficient charging. I think that will be a lengthy transition but you would want to put the structure in place and then allow that transition to occur.

MR LINDWALL: Henry, it is Paul here. I just wanted to ask two questions. One is about your capital recycling. In our draft report, if I paraphrase it roughly, we have basically said that the assessment of the privatisation of existing assets should be done efficiently, according to - you would sell it at the right price, with the right market structure, and then the purchase of new infrastructure should be subject to a transparent cost benefit analysis and that the use of recycling as a terminology would be in effect a marketing tool, if you like.

I think that where you have gone further than that is by suggesting - and correct me if I am wrong - that where there is an artificial capital constraint because the government has decided there is a maximum amount of debt to GDP ratio or some sort of such constraint and there is a gap between the social benefits and the private benefits of infrastructure which is wider at the initial period than at the latter period - in other words, when it is greenfield rather than brownfield - there might be specifically a useful recycling.

MR ERGAS: Yes, that's right. My point really is this: if governments face no capital restraint, then effectively they could borrow to undertake all worthwhile projects. If any project had the rate of return that exceeded the essential capital or the social discount rate, whichever approach you want to take, then they should be able to borrow to undertake that, but in reality that is not the case and that is not the case for very good economic reasons and those economic reasons go to whole host of principal-agent problems which (indistinct) the relationship between government and voters on the one hand and essential debt holders on the other.

When you face that situation, then it seems to me not irrational for the user asset to be basically a portfolio and to try to manage that portfolio efficiently. What that may mean is that they invest in assets where the transactions and government cost of securing private finance are high and where the social benefits substantially exceed the appropriate or private benefits. In those situations what you could see is what looks like the government acting as a portfolio manager where it collects projects that in the early stages are difficult and costly to get third party or private finance into and then, as circumstances change, and the transactions and government cost of privatisation fall, in part because it is a private benefit or a private or appropriate benefit becomes a larger share of total benefit, then in those circumstances if it was to sell those assets - now, part of the calculus it makes when it does that, and that is really all I am saying.

Part of the calculus that it makes when it looks at that privatisation is that it relaxes capital constraint, but that doesn't mean that it shouldn't be looking to privatise assets when they are going to be more efficiently managed in the private sector; nor does it mean that you should take investment decisions on new assets without very careful cost (indistinct) on the contrary, the exact opposite is true. What capital rationing means is that it has to be especially careful about what it invests in. That, it seems to me, is an absolutely critical point because it really goes to the heart of the argument that you rightly put about the importance of having proper project scrutiny and having institutions that can guarantee proper project scrutiny.

MR LINDWALL: Thank you.

DR MUNDY: Henry, it's Warren. Henry, you will be aware that the commission has a longstanding scepticism about excessively heavy-handed regulation. It seems to us that there is probably a few hooks in if you went down a traditional rate based particularly DORC-based approach to regulating an extensive road network. You seem to be alluding to a somewhat, dare I say, lighter-handed or perhaps less precise or intensive form of regulation. I was just wondering whether you could give us any steers as to how that regulatory oversight to give the community comfort - because it seems in this case, more than most others, that the search for a perfect set of prices would be indeed a fruitless one.

MR ERGAS: I entirely agree. Let me also say, Warren, that I think the reality of it is that for a host of very good reasons, any transaction to user pays for roads will be a slow one.

DR MUNDY: Agreed.

MR ERGAS: Both for political accountability but also for economic efficiency, there are many elements of the road networks that are difficult to price and difficult to price efficiently. In those cases, what the prices probably look like are shadow tolls where effectively what you would have is some form of what user parties would liken to be a registration charge or whatever else you had by way of a fixed charge that covered the option value of using the road network but a significant share of the funding, particularly for the operating and ongoing costs, would still come from effectively a tax source one way or the other and the allocation of that revenue, it seems to me, should be measured on what would look like shadow tolls would accrue to a road whenever it operated.

Over time the structure of prices that you should have for roads should be based on the marginal cost of using and operating the road network and if the road network operated to approximately constant returns of scale, then appropriate marginal cost price fixing would cover the long-run costs of the road network. Now, whether it will or will not is obviously an empirical question, what the level of the charges would be is obviously an empirical question and how that should be related to investment decisions, both in terms of road capacity and road quality and durability, is also an important and ultimately empirical question.

So the way I would suggest it could operate and I think there's a myriad of ways in which it could do so but a way in which I think it could operate which from reading your report I think has some similarity to the New Zealand structure is for government to have clear statements of expectation that they would give to a road authority, that within those statements of expectation there be a requirement to manage the long-term transition to efficient pricing and that the role of the regulator would be basically to review a corporate plan that was proposed by the road authority. I agree with you it should be as light-handed as possible but it's important for it to be sufficiently clear and transparent as a process that it gives road users confidence that they won't be held to ransom.

MR HARRIS: Yes, that transparency point we think is one of the great advantages of this in terms of making clear to consumers that they have a capacity in this case, particularly if there was some representation on the body from the motorists associations and the heavy vehicle industry and that sort of thing, they have some decision-making role in the allocation of funds so that in some way at least the consumer was reflecting an opinion on willingness to pay. This, we think, in some sense needs to be incorporated in there and no-one has quite cracked that model, the New Zealanders haven't. We think in the design sense we'll have to provide some commentary on that as well. Do you have any views in that area?

MR ERGAS: Look, I agree that you do want to have consumer representation and I think one of the benefits of having the kind of structure that you've discussed in the report is that it would both allow a context in which that user representation could occur but it would also mean that when motorists associations and freight associations and so on were putting their views and proposing changes to road network or changes (indistinct) of that road network, when they're reviewing that they would also face the cost.

MR HARRIS: Yes.

MR ERGAS: I think a problem we have at the moment is that we have a situation where it's in a way been easy for people to say we should undertake these very expensive projects because they don't face the costs that those projects will involve, including the opportunity cost, for costs that if you do that project you won't do other projects and a result of that is that we contribute to the poorer quality of decision-making. So I think it's (indistinct) if we could have real - give a voice in a context where that voice carried with it a responsibility to face the costs of any decision it had.

DR MUNDY: Henry, are you aware of any regulatory models elsewhere where the presence of users or consumers in the decision-making activities of the organisation leads regulators to a view that they can have a degree more confidence in the conduct of the organisation because effectively those who are paying are internalising the consequences of the pricing decisions? So their regulation of UK Nat sort of springs to mind in that regard but I was wondering whether you had any other examples that you're aware of.

MR ERGAS: Look, I must say I don't but I will definitely give it some careful thought and go back to looking at my notes on various models. I haven't really looked at it under that angle but I do have a lot of documentation and notes on these models and I'll take it, however, on notice if I may and I'll get back to you - - -

MR LINDWALL: Okay, I've got one more question given the time, Henry, and that's about project selection again. In our draft report we did write, "Even election commitments to build and/or fund substantial infrastructure should be subject post-election to rigorous project assessment and selection," and as far as I can see we haven't received many submissions that address that point. Have you got any thoughts about how that might be systematised, because it is a political economy issue?

MR ERGAS: Yes. Look, I think that's a very important point because one of the problems with our current arrangements is that political competition, which is a terrific thing, certainly relative to the lack of political competition but political competition needs to focus every time an election approaches on iconic projects, very large-scale projects that will deliver perceived benefits to politically significant areas and the momentum in those projects is that once a project - once that call gets made then it's almost impossible for either party or from indeed any side of politics not to get on that bandwagon and so you end up with the seemingly firm commitment to what may be relatively poorly-judged projects.

Now, it could be that once those commitments have been made locally it's fairly difficult to back off from them, but at least you should have transparent assessment of those projects so that voters will know what they've bought and at the moment we tend to put selection commitments in a separate bag and not come to (indistinct) opportunity costs.

I'm very taken by a model that at least for some years was implemented in Finland which was to require the transport agency to disclose the cost benefit ratio and a bit more information than that about every project above a certain threshold of cost and it not only had to disclose the cost benefit ratio for the project it was undertaking but it also had to disclose the cost benefit project or the major project it had assessed and decided not to undertake and that allowed you to see the opportunity costs of what you were doing and that, it seems to me, really ought to be part of this charter of good infrastructure management that all governments should sign up to and that should have some enforcement made.

MR HARRIS: We'll take that as a challenge as well. Henry, in the interests of time and with the next submitter available to us here, is there anything final that you would like draw your attention to before we close off?

MR ERGAS: No. I do have, like I said, a fair number of more detailed comments I am committed to get to you in a timely way, so again congratulations on an excellent piece of work and thank you for your patience in addressing my late supplementary provision and even later detailed comments which I will get to you as soon as I possibly can.

MR HARRIS: No, like a number of submitters, we appreciate the effort multiple people have made to put in more than one submission. It's very, very helpful to us, so thanks very much for your time today.

MR LINDWALL: Thank you, Henry.

MR ERGAS: A pleasure. Thanks very much, everyone. Goodbye.

MR HARRIS: Aiming to finish on time, he says, so our last submitter is Geoff Edwards from Griffith University. Come on up. Over there. State your name, rank and serial number for the appropriate inquisition. We might notice as you sit down that you are in Public Administration today. There is as an article.

MR EDWARDS (GU): Yes.

MR HARRIS: This arrived on my desk earlier in the week and I thought what a strange coincidence. I just flick it open and there is one of our submitters, straight off.

MR EDWARDS (GU): You have thrown me a challenge, chairman, to say something different today, so that you don't - - -

MR HARRIS: No, I will be able to check out what you say by comparison with this. I will be able to cross-edit the remarks sort of thing. Anyway, please identify yourself for the record.

MR EDWARDS (GU): Geoff Edwards; I'm an adjunct research fellow at Griffith University in the Centre for Governance and Public Policy. I am an independent scholar, so I am here just as a casual scholar. I am also president of the Royal Society of Queensland, which is the oldest scientific society. I am not presenting in that capacity today but that has sensitised me to the benefit cost of alternative uses of public funds and I refer particularly to the Productivity Commission's 2007 report on the benefit cost of research and development and from memory, there was a finding of a typical cost benefit of 40 to one, which I believe is a robust analysis and it's consistent with my own studies and I was in the public service, so I think that's a benchmark that I would like to refer to later on. I'm getting off the track.

MR HARRIS: That's fine. If you have some opening remarks you would like to make generally, that's great. As I said, we are going to try and finish right on 4.30 but please go for it and if not, then we will go to some questions which I have got anyway.

MR EDWARDS (GU): Thanks, gentlemen. I would just like to summarise briefly, perhaps in a different way from my submission, and I can give you a written supplementary submission. Okay?

MR HARRIS: Fine.

MR EDWARDS (GU): I appreciate the opportunity to appear, commend the staff for the very efficient way in which they arranged this, especially my namesake Melissa. I am not going to focus on the positive or the worthy elements of the report. I just want to focus on a couple of what I think are omissions and they are remediable omissions. I think there's three wrecking balls headed towards the model that the draft report outlines. One is climate change and the other is peak oil and they tend to pass beneath the consciousness of some of the business leadership, partly because, as you know, markets don't tend to recognise absolute scarcity.

This is an assumption in market theory; that there's always some resources somewhere else that can be drawn on if the price is right. We are now approaching the limits of the atmosphere's capacity to absorb and the capacity of the earth to yield petroleum fuels. That's in my submission and other people have submitted also, so I won't labour the point. There is a theoretical reason why markets won't handle that and I think any report that deals with infrastructure, especially transport infrastructure, must confront those two challenges, because they will play commercial havoc within the next decade with a lot of projects that would otherwise be seen as having a favourable cost benefit.

The third wrecking ball could be something that would - I support what Mr Ergas said at the end there, that there is an opportunity cost of projects which is not adequately factored into a project by project assessment and I will express that in another way; that there's a lack of a strategic planning element, a public interest planning element, at the beginning of the governance arrangements that the commission has outlined. I'm referring particularly to page 223, where you mention some governance arrangements. Now, I would strongly commend the commission for the first one, being the principle that decisions must be taken in the public interest and I applauded the recognition of this overriding principle, that anything government does ought to be in the public interest.

Unfortunately, I don't think the model that's outlined then gives effect to that and I think there is a missing nexus, because the model then jumps then to what I will call project by project assessment and the cost benefit analysis is a project tool. It's not a strategic planning too, so there is an element there that's missing and the local government people touched on it. Traditionally, what would happen is if someone had an idea for a project, that would eventually go to cabinet after it was assessed in some kind of planning framework. so a transcript project might go through a regional plan, a local government planning scheme, a transport plan, an infrastructure plan, a couple of corporate plans, an enormous amount of time taken and a lot of frustration for the people involved.

Eventually, when it went to cabinet, it would be given approval on its merits but not approval of the funding, so then the proposal for funding would go to cabinet at budget time. That's the traditional way these design and construct projects went, so the cabinet had a decision on its merits without particular regard to cost, which was a public interest evaluation, often sub-optimal but at least in principle that's what it was, but then the financial decision was taken in the context of the budget ranked against the police and hospitals and schools and all the other claims on budget, which allowed opportunity cost to be factored. Those deliberations are not public. They are behind closed doors, so they leave a fair bit to be desired and they are unduly influenced by treasury but at least there was an opportunity to factor in opportunity.

Now, where you have a model that I think the commission perhaps unwillingly is going to give a blessing to is where a project proponent comes along, has a bright idea, comes along to the government and says, "We've got a deal for you. You give us the land between Dandenong and Pakenham and we will build you a brand new corridor. We will double the number of train lines. By the way, just hand over the title to the land," and so the premier will say, "Look, we didn't know about this project but what a fantastic idea. We will get another train line built. It won't cost the public purse anything. We will give them preferred developer status," and then there is no opportunity in there for opportunity costs to be factored in.

My critique of Infrastructure Australia's plan is in the published articles. They have got $16 billion in their top priority projects with a benefit cost of 1.2. How could they get that on the agenda when you have said research 40 to one, libraries nine to one or 11 to one, education generally 15 to one, so if we don't steer projects away from assessment on a cost benefit alone by private initiative, we will see an enormous amount of investment capital diverted to projects that are sub-optimal compared with other projects and that's particularly a problem with transport, where we have peak oil and the policy responses to climate change looming, so I would see a misallocation of capital on a grand scale occurring.

I believe we have seen that already with the tunnels in Brisbane and I think the commission did say we had a favourable result in one sense. Okay, we have got these new roads but the opportunity cost of those billions of dollars of capital has to be factored in, so I would like to answer the question that you put to Mr Ergas later but perhaps I might pause there and say I think there is a strategic public interest planning process that must go ahead of the cost benefit and by all means then kick in the cost benefit analysis that you referred to, transparent, public consultative, et cetera, et cetera, but publish that alongside the cost benefit of alternative uses of public funds.

MR HARRIS: Yes. That's very interesting because we had that discussion about four weeks into this inquiry late December just on this issue of - but I can put it in a far more brutal and succinct way - how do these projects just pop up because combining the Infrastructure Australia list - which is why, as you've seen in our report, we've tried to eschew the idea of endorsing any particular list because lists are all partial and all driven by particular circumstances and, therefore, are not a reflection of any analytical development of, "This is the actual suite of projects that should logically be pursued," and as you point out, there's an opportunity cost.

Every decision that goes towards them and moreover the ones on the Infrastructure Australia list, let's just take that, as you point out, have had relatively low benefit-cost ratios and there's no comparison even inside Infrastructure with alternative options, so as Henry Ergas was saying, the idea that in Finland they have compared these things and required the publication of them, we could do the same thing here. We know that transport authorities actually have information on alternatives that are smaller in scale and perhaps not as ribbon cutting in nature but have much higher benefit-cost ratios. I've managed to work in some of those areas, so I do know they exist.

So I think we will try and draw on your point about opportunity cost in our final report. It's not one that has just been made by you but I think the point is very well made. There's quite a lot to be said for this. The difficulty is identifying that whole of government context in which, therefore, this needs to take place. It's quite hard for an infrastructure inquiry to say, "By the way the whole of government should be analysing whether infrastructure is even the right place to be putting your scarce and limited resources at this point.

I know state jurisdictions do tend to have the idea that we have a capital account and, therefore, we spend it on capital objects and proportions are devoted towards the particular capital objects that states traditionally invest in and that's pretty much how they decide things. It may have improved a bit since I last worked in the state government but that's only five years ago and that's roughly the way capital budgets were determined, so there is an issue inside this. It partially goes to your point about benefit cost. Many of the things that have high benefit-cost ratios that you've outlined are nevertheless treated as recurrent expenditures rather than capital expenditures, so they don't get access to the capital account for again that reason which is a state budgetary issue or budgetary structural issue there too.

It's a very complex area and I doubt whether we'll get a pretty and elegant solution to that front end. Nevertheless, I think we want to comment on it and so we appreciate you and others who can be very helpful.

MR EDWARDS (GU): Mr Chairman, may I respond to that?

MR HARRIS: Sure.

MR EDWARDS (GU): Dealing with one of your latter points first, I wouldn't underestimate the ability of the commission to create orthodoxy. We now have an orthodoxy that economic growth depends upon more throughput and particularly growth in transport as either a precondition or a signal of a prosperous economy. Business has an orthodoxy that environmentalists, fringe dwellers and wreckers and that there's a technological optimism that Peak Oil will be sold and we'll find our way out of that. We'll sequester carbon somehow and so business can continue expanding as usual. I think some of those orthodoxies need to be challenged and I wouldn't underestimate the ability of the commission to nudge a fresh look at some of those orthodoxies.

I would like to comment briefly on your earlier point about how these projects arise. I think one of the secrets is to disaggregate the whole idea of private sector. The classical model of a competitive economy with these firms that had their own money to invest and their own money was at risk, so they were prudent in allocating their own resources, we don't have that situation now with a modern international economy where, say, a private sector proponent might consist of a proposal aggregator or facilitator, a financier, a consultant, the construction companies and others and hedge funds and the super funds that have a stake in it. So to make sense of how these projects arise, it's necessary to disaggregate private sector and realise that there are a lot of players in there and some of them have very different objectives or very different interested stake and the majority of them do not have the public interest as their primary modus operandi or their primary rationale for existence.

This is not casting aspersions on business. It is in the public interest for there to be a prosperous, vigorous, business sector that can exercise entrepeurialship. This is not an anti-business statement. It is just saying that by their essence, even if you take the broadest view of business that is at the centre of a network of stakeholders, not just shareholders but creditors, suppliers, customers, users et cetera, even if you take that broadest view of business then they are still not primarily expected to pursue the public interest. So therefore, if the public interest is to be a central rationale for building public infrastructure, which you've correctly identified, there needs to be a step that will capture business enterprise and initiative but it has to be in the context of a public interest objective or rationale or overriding purpose and it's nonlinenar. It's non-mechanical. It's organic. It's difficult to nail down but that's reality.

MR LINDWALL: Could I cover a few points that you've mentioned. Firstly on benefit-cost ratios. I think caution needs to be treated about that. It's true that when we hear of benefit-cost ratios of 1.2 for infrastructure projects, I probably suspect that they're less than one because of optimism on the benefits and costs blowouts and so forth, but on the other hand benefit costs ratios on research for 40:1 are not over an infinite range.

If we spent the whole GDP of Australia, we don't get 40:1 on research, so on those measured amounts of 40:1 for a limited investment - I don't know. I can't remember exactly what that research report said was the range but it is over a range. I think we have also emphasised in our report about the more efficient use of existing infrastructure which is a very important thing I think when you reflect on opportunity cost and the point you mentioned about the projects that are brought forward from the private sector. They should be subject to a cost benefit analysis, just like any other proposal. Giving away land is certainly not free. It is something that should be reflected as a cost in subsequent analysis.

As for Peak Oil, my (indistinct) is that if and when we reach that stage that the price of gasoline and other products related to that will start rising inexorably, that will have a demand response. In the short term one would expect the price elasticity to be fairly inelastic and it will become more elastic over time as new technologies adjust, so while I can understand the concept of Peak Oil, I'm not afraid of a structural change to an extent that it would cause massive economic damage but I may be wrong.

MR EDWARDS (GU): Can I comment on that latter point first? Yes, it's very difficult to say. I don't regard myself as an expert but I think I did refer in my paper to the BITRE report of 2009 which was not released. I've read a lot about Peak Oil and that is the best official analysis I've read in Australia, so I would recommend that the commission consider commissioning the author of that report to do a chapter or a section in this report for Peak Oil.

It may well be that the time frame for the price signal to take effect is a few years but we must remember that the lifetime, the economic lifetime or the physical lifetime of the structures we're building to cater for growth is much, much longer than even the most optimistic view of Peak Oil. Even if you take the most optimistic view of Daniel - I can't think of his surname - and the other economist who've said 2035, even if you take that view which is at the outer limit of optimism, that's only 20 years away. The freeways that we're building now would have a physical lifetime of more than 20 years. So we need to really think whether it's wise or prudent to commit billions of dollars to these structures when it is quite certain even the most optimistic economist will agree that there is going to be a significant price pressure within a couple of decades.

I would just like to come back to an earlier point you made about not downplaying the relevance of cost benefit. I come from a view that making these decisions or trade-offs, if you like, is a task that is so complex that we elect people to do it on our behalf and you're perfectly right, the cabinet can't sit down and allocate a hundred per cent of the budget to scientific research. It has to balance politics, community feeling, the events that happened last week;

like some bloke shot people at Port Arthur and then the next week gun control is on the agenda. So public policy is a resultant of a whole range of factors, some rational, some non-rational.

The traditional way that we resolved them was to elect parliamentarians to make those decisions on our behalf. They're too non-linear to have other than a human judgment and to support those people with an independent frank and fearless expert, public service. What we're seeing now is - two problems are going wrong with that model, one is that the expertise of the public service is being I think undermined. I don't see the analytical capacity there that I think we need. I think also there's an orthodoxy around that governments can't make sensible decisions and there's an orthodoxy that only business creates jobs. The prime minister has said that recently himself.

So that orthodoxy creates its own vicious circle of lack of confidence in governments to make these multilateral decisions, therefore we outsource them. We outsource them to bodies like Infrastructure Australia that hasn't done a good job of them because it's too complex and too multilateral. So the only way I think is to go back a couple of steps before some of this reform, to strengthen the independent analytical capacity of the public service across portfolios and to strengthen the confidence of government in itself and the confidence of the people in the government. That's a multi-year exercise.

MR HARRIS: Your comments on Infrastructure Australia are also useful to us because I think you already detected from the draft report we are not yet convinced about the Infrastructure Australia model in any of its forms. I'm subsequently on the public record as saying we are going to have to look very closely at where it ends up as a result of the parliamentary process by the time we are finished.

I did read what you said in the article that's in the Institute of Public Administration report but if you're subsequently inclined to send us anything more on Infrastructure Australia, the better model - and that's not a presumption on our part that we actually are going to favour Infrastructure Australia. I think you heard earlier some talk about the role of the auditor-general and I mentioned Bureau of Transport and Regional Economics or whatever it now is - - -

MR EDWARDS (GU):   There's an infrastructure in there as well somewhere.

MR HARRIS: Once upon a time it used to work - it had a real name then. Now it has got some other kind of name, but we're very interested in how to do this and it may end up being a disaggregated version that suits our model. We are I'm afraid at the end of time and I'm particularly concerned to make sure that I don't get commission staff stranded in Brisbane. So can I thank you for your efforts and contributing to us today, and in fact being always the last person who is in a difficult position of - I try to keep time available for everybody but if there is something that we have missed, I'm quite accessible on email, the standard first name dot last name@pc.gov.au. So feel free to send me an email if there are things that we weren't able to get to, particularly on this point about the role of Infrastructure Australia, I'm quite interested in that.

MR EDWARDS (GU): Thanks, chairman. I'm honoured that you have all stayed until the end of my presentation and I'm honoured that you have invited me to submit further comments. There's a couple of points there that I will build in and I will make a supplementary submission.

MR HARRIS: Even by email, as I said. We are not looking for - you heard Henry Ergas. As I say, we will take it in the form we can get it because a lot of people have made a big effort for us.

MR EDWARDS (GU): Thank you, chairman.

MR HARRIS: Otherwise I'm going to declare this adjourned. Anybody who wants to rejoin us in Sydney at 8.30 on Monday morning, feel free. I doubt I will see almost any of you there. Thank you very much.

AT 4.25 PM THE INQUIRY WAS ADJOURNED UNTIL
MONDAY, 14 APRIL 2014