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# WHAT'S NEXT FOR MARKET-LED PROPOSALS IN AUSTRALIA?

MARCH 2017

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## MARKET-LED PROPOSALS IN AUSTRALIA – WHAT’S NEXT?

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A market-led proposal or unsolicited bid (MLP) can provide a range of benefits for governments and the private sector. By inviting the private sector to submit MLPs, governments can deliver infrastructure more quickly than other forms of government procurement and access technology or innovation which would otherwise be unavailable. A market-led proposal can also assist government to provide services, or achieve policy objectives, in a faster and more dynamic way. For example, there may be economic or other constraints which impact on the government’s ability to deliver a particular project or service without private sector involvement. MLPs can overcome these constraints.

Whilst MLP policy frameworks in each State are an excellent step in the right direction, there is room for the policies to be improved to maximise the benefits to governments, and the private sector, flowing from MLPs. These improvements include:

- expanding and clarifying the MLP assessment processes and certain key components of the policy frameworks to achieve certainty for both proponents and State governments;
- clarifying the relationship between an MLP and other forms of procurement (eg competitive procurement methods); and
- clarifying how the MLP processes operate in relation to projects which form part of government policy but are in a very preliminary stage.

### CONTEXT

While MLP policies have been in place in some states for many years, there are now formal MLP policies in each Australian state and territory.<sup>1</sup> High levels of infrastructure and service delivery policy development activity in State government agencies and bodies like Infrastructure Australia has created keen interest in the MLP process.<sup>2</sup> However, as with any policy framework, a number of challenges arise.

Current key challenges for the States include:

- managing the process where a proponent may be seen to have a structural advantage (for example by managing or owning an asset with little or no competition);
- controlling submission of proposals which cut across a procurement in its preliminary stages; and
- balancing the benefits of flexibility against the need for policy certainty.

To date, relatively few proposals have reached contract close across Australia under the latest version of the MLP policy frameworks in each State. MLPs which are progressing or have reached completion include a microbrewery, tourism centres, new and upgraded road infrastructure, the implementation of 4G across a train system, a driver training centre, a hospital car park, transport interchanges, a cruise terminal, the long term lease of a poles and wires network, a ferry line and a new police headquarters.

The following questions are considered below:

- How is uniqueness assessed?
- How can the threshold stages of the policies be refined?
- What is the relationship between an MLP process and a competitive process?
- How do you test whether an MLP aligns with government policy?
- What are the future trends for this form of delivery?

### How is uniqueness assessed?

An MLP must contain an element of uniqueness. However, this is a subjective assessment and must be considered in the context of the entire proposal. Statistically speaking, this criteria appears to create a huge headache for many proponents. Since the NSW Policy was issued five years ago, 117 proposals have been submitted, mostly in the transport or real estate sectors. The vast majority didn't pass the first stage and almost half failed the uniqueness criteria.<sup>3</sup> The policies give examples of what might be considered to be unique:

Example	Qld	NSW	SA	Tas	Vic
Unique idea	√				√
Exclusive access to or ownership of strategic assets integral to proposal	√		√	√	√
Unique financial arrangement		√	√		
Improvement of value to State by reference to timeframes, service delivery, risks not borne by State or other advantages					√
Combination of attributes create and constitute a unique idea and an innovative departure from previous practice or service delivery	√		√	√	
Ownership of land, intellectual property (eg technology or software) or other legal rights	√	√	√		√
Where there are no competitors or if there are, those competitors would not be able to deliver the same outcome	√	√	√	√	√
A solution which is otherwise unlikely to be defined and put to market		√			
Proponent has unique ability to deliver an outcome supporting government's strategic priorities.			√		

A common policy thread is a form of 'but for' test. Essentially, the relevant government will ask 'Can this proposal be delivered by competitors?' If the answer is 'yes', then it will ask what justification is there for the State to seek value through a competitive tender process?

Uniqueness must also be considered in the context of other benefits the proposal might achieve. According to the NSW Policy, it must apply to both the proposal and the proponent.

The Victorian Policy says 'it is not sufficient to only demonstrate the presence of unique characteristics in a proposal. It must also be demonstrated that these characteristics provide value-for money and other benefits for government that could not be achieved through a traditional government competitive procurement process outside the guidelines within acceptable timeframes'.

The relationship between innovation and uniqueness is also interesting. Not all unique proposals will be innovative. However, the ACT Government requires a proposal to be both unique **and** innovative. It has recently been suggested that the concept of uniqueness could more usefully be replaced with a simpler test of 'benefit' to the State in question.<sup>4</sup>

The uniqueness test can perform an important function as a useful, legitimate and defensible justification for not testing the market. However, if the high watermark of uniqueness is to be the fundamental test for assessing an MLP, then a failure to meet this requirement should not necessarily result in the proposal failing to progress.

Rather, it should then call up a competitive market process, provided of course that other relevant criteria (innovation, policy alignment, some value for money being shown) are met. As explored below, most states do not permit a competitive process as part of their MLP policy which is arguably an inherent constraint on both the process and the ideas which are submitted as part of that process.

Finally, the NSW Policy provides a list of the types of proposals which will not meet the uniqueness test, which includes proposals:

- seeking to directly purchase or acquire a government owned entity or land;
- where proponent holds an existing government licence or approval to provide goods or services and is seeking to bypass a tender process or to significant extent an existing contract on the basis that the contractor is 'on site' or has some other advantage;
- seeking to develop land not owned by government or the proponent; or
- to provide widely available goods and services to the State (eg office supplies).

Whilst most proposals will seek government funding in some form, a critical question for government will increasingly become the extent to which an MLP based on a value capture model could be categorised as sufficiently unique or offering value for money.

### **How can the threshold stages of the policies be refined?**

Whilst the MLP process has many objectives, the key objective should be to achieve robust policy outcomes for the State through an appropriate balance between:

1. competition and value for money including in the absence of market testing;
2. the need for certainty and the desire for flexibility in the process; and
3. achieving government objectives whilst enabling innovation.

There are four areas where further refinement may be helpful:

#### *Pre-submission meeting*

Most MLP policies envisage a pre-submission meeting with the Department responsible for managing the policy. This meeting is generally optional but strongly recommended.<sup>5</sup> The purpose of the meeting is to test the attitude of the government to, and obtain initial feedback on, the proposal.

Whilst these meetings are intended to be informal, there may be advantages to having the meeting held on a more structured basis. Although it is critical that these meetings do not become an exercise in pre-supposing the outcome or success of any particular proposal, mandatory meetings would likely prevent the submission of proposals with no prospects of proceeding any further.

It follows that whilst it may impose a burden on personnel, the preliminary meeting should be compulsory. If the meetings were held with the same person or persons, messages as to timing, content of any proposal, policy alignment and potential improvements could be delivered on a consistent basis. Clarity as to with whom this meeting should be held (does a meeting with a Minister or Department Secretary constitute such a meeting?) would also be useful.

#### *Form of proposal*

Most Policies take a light touch to the form and content of a proposal. The SA and NSW Policies require a template 'Schedule of Information Requirements' and a pre lodgement checklist to be completed by all proponents. The Queensland Policy imposes similar requirements. These templates require proponents to identify costs to Government, risks, organisational details, intellectual property, validity of proposal period and an explanation of how the proposal meets the assessment criteria contained in the policy. The Victorian policy includes a submission checklist and list of information to be included in a proposal.

This approach reverses the usual parameters for a government procurement which tend to specify in great detail the form in which any offer or bid should take. Whilst this is to some extent driven by the need to compare like with like and manage probity risks, the MLP process could maintain flexibility whilst at the same time requiring the provision of more detailed and structured information at an earlier stage.

If proponents are required to provide a more detailed, structured and well thought through proposal, this will minimise wasted government time and resources assessing proposals from 'tyre kickers'. However, at the same time, the requirement to provide detailed information at an earlier stage should not be so onerous that private sector proponents become required to invest a large amount of time and money in preparing an early stage proposal.

Another threshold restriction which could be considered, is the imposition of a financial threshold for any proposal. The SA Policy

contains a threshold of \$3 million for construction proposals and \$1 million for non-infrastructure proposals, and the ACT and Tasmania also have dollar thresholds.

### *Cost of proposal preparation and review*

The financial and other costs to both parties of preparing and assessing a proposal are often significant. Australian MLP policies specify that participation in the MLP process is at the proponent's risk.

However, it may be appropriate for a proponent to recover some of its costs (for example capped direct costs) if a project does not proceed due to a change in government policy.<sup>6</sup> Or, it may be that costs could be reimbursed in other circumstances.

Parallels may be drawn between the process project alliance participants follow under an alliance development agreement (for which they may be reimbursed specified costs) and the stages of a market-led proposal process. While total cost recovery is not realistic, reimbursement of a component of costs may result in a more detailed initial proposal and more robust participation in the various stages. This is particularly important where design refinement or detailed technical input is expected.

It remains to be seen whether reimbursement of costs would result in better quality proposals, or more MLPs being submitted or some other outcome.

Conversely, for some proposals it may be necessary to require a proponent to submit a bid bond or a fee for proposal review.<sup>7</sup> Again, the fee charged could never achieve full cost recovery but may:

- cover some of the resources the State expends in assessing proposals; and

- deter poor quality proposals.

### *Timeframes for assessment*

A number of jurisdictions specify a timeframe for assessment of the proposal at each stage. Specified timeframes have the advantage of providing certainty for proponents (and policy makers) and can also provide a guide as to the likely costs to be incurred at each stage of the process. This is particularly so for the preliminary stages. It may be more challenging to provide certainty around the final stages, as the timing will vary considerably depending on the nature and cost of the infrastructure of services and the stakeholders involved.

Subject to having sufficient resources to meet any timeframes, it may be appropriate to specify general timeframes for the progress of a proposal through the relevant stages.

### **What is the relationship between an MLP process and a competitive process?**

Every MLP process will commence on an exclusive basis. For a proponent, exclusivity is a key advantage. The policies vary significantly in terms of how the exclusive mandate will be assessed and how (and if) this might 'revert' to a market process.

Under the SA Policy, exclusivity is granted for a specified period but if the government has received multiple proposals on the same subject matter, then it may proceed to negotiate with all proponents.<sup>8</sup> Of course, it is most unlikely that the State would receive two or more proposals on the same subject matter at a similar time. What is more likely is that once one MLP is publicly disclosed, another party may seek to take advantage by also submitting a proposal for a similar subject matter. In this case,

government will be required to invest resources in assessing the later MLP even as the first MLP is progressing.

The Queensland Policy states that for a proposal to be accepted on an exclusive basis, the government must be satisfied that a proposal addressing a similar need is not already being considered by government, and there are no competing proposals addressing the same or similar need already under active or advanced consideration. Once this has been assessed, the negotiation may proceed on an exclusive basis. The only other option is that the proposal does not proceed at all.

The NSW Policy adopts a similar approach with the refinement that projects which do not meet the policy requirements 'may' be offered to the market, but not under the MLP policy framework.<sup>9</sup> Victoria is the only State with a policy framework which expressly enables a market-led proposal to revert to a competitive process.<sup>10</sup> Stage 2 of the Vic Policy permits the proposal to proceed to one of the following:

1. a tailored competitive process which may involve:
  - a. Swiss challenge (a competitive process is conducted and if the original proponent is unsuccessful it is given an option to match the winning bid); or
  - b. development manager (a competitive process is conducted by the proponent and paid a fee from the successful bidder);
2. exclusive negotiation; or
3. standard competitive process in accordance with the relevant agency's procurement rules.

A tailored competitive process will be used where the uniqueness criteria has been met but there is a need, or the opportunity, to test value for money via a market process. As suggested above, a tweak on this approach could be the use of a competitive process where the uniqueness criteria has not been met, but all other relevant criteria have been.

Achieving a level playing field if the competitive option is selected remains a significant challenge, which is apparent when one considers the potential imbalance between a proponent who may have spent years developing a proposal and parties who will be given a few months to develop a competing bid.

Numerous other jurisdictions have policies which support a reversion from exclusivity in certain (or all)<sup>11</sup> circumstances whilst still recognising the value provided by the original proponent:

Jurisdiction	Recognition of original proponent value
Chile <sup>12</sup> and South Korea <sup>13</sup>	The original proponent is entitled to participate in an open tender process and given a bonus in a specified form (for example a value applied to its offer for evaluation purposes only). The original proponent is automatically shortlisted but given no other advantage
Argentina	The original proponent is given a bonus and a right to submit a best and final offer depending on the bid differentials
South Africa <sup>14</sup>	Several rounds of tendering are held and the original proponent has an automatic right to participate in the last best and final offer round
Costa Rica <sup>15</sup>	A public tender is held for an unsolicited proposal which is accepted, the original proponent can participate on same terms as others, and is reimbursed its costs if it does not win the tender

Reversion to competition gives government more flexibility in the process, enables a proposal to be tested and arguably maximises the chances of at least some version of the proposal achieving contract close. By maximising the chances of a proposal achieving contractual close, governments will encourage the private sector to submit more MLPs and invest more time and resources putting together ideas for solving government priority challenges.

A detailed framework around reversion to competition should be considered by States other than Victoria.<sup>16</sup>

### How do you test whether an MLP aligns with government policy?

Important questions arise for major infrastructure projects which are unfunded but strongly supported by the relevant government agency or a policy development body like Infrastructure Australia.

For example, to what extent is a government able to consider an MLP for a project or service which has preliminary funding only (for example for development of a business case, or preliminary design)? Should a business case take account of the possibility that an MLP might be submitted? At which point in the procurement process should an MLP be excluded?

The NSW Policy provides that a proposal for a project *'where a tender process has formally commenced, whether published or not'* will be unlikely to progress. Does this enable a savvy proponent to 'jump the queue' for a project with wide government support which has only progressed through internal feasibility stage?

The Victorian Policy says a proposal is unlikely to be progressed or will otherwise not be considered if it:

- seeks to circumvent existing government approval processes for a project;
- has been developed in consultation with a government agency; or
- relates to a project which government has already decided or announced will be released to the market.

More complications arise when the project is one which forms part of a network (whether transport, telecoms or electricity). Incumbent operators or providers have a unique knowledge of the asset or service and ability to connect that asset with the existing network. It is often not possible for this advantage to be overcome. There is a question as to the extent to which this kind of proponent might fall within the 'existing licence or approval holder' exclusion set out in the NSW Policy.

It might be appropriate to regain some control over the process by formally briefing potential proponents en masse for key early stage projects with significant market interest.

Rather than requiring a proposal to align with 'government policy', another approach could be for government to develop and issue a standalone market-led proposal strategic plan which identifies strategic project and investment opportunities in respect of which a market-led proposal will be considered, eg, a road from A to B.<sup>17</sup> An approach like this is used in Italy (for example the Bre. Be.Mi toll road in northern Italy).<sup>18</sup> This has the benefit of providing structured guidance by actually telling the market what project government seeks to deliver via an MLP process. It also addresses the policy alignment risk and avoids an MLP intruding upon a procurement process which is already on foot. The difference between this model and a standard PPP model is that in the first stage the market is asked to offer proposals, one of which then forms the basis of a formal procurement process.

## What are the future trends for MLP delivery?

We anticipate activity in the following areas:

- Further refinement of the various Australian policies to include:
  - more structure as to the form and content of proposals;
  - more definitive timelines for assessment;
  - externally formalised guidance for the value for money assessment (like PPP guidance);
  - a move away from the concept of 'uniqueness' and towards an assessment of innovation and benefit to government or taxpayers;
  - some best practice guidance for risk allocation to assist proponents to revise and finalise their proposals;
  - some degree of harmonisation across the Policies; and
  - a reversion to competition in certain prescribed circumstances.
- The PPP and MLP frameworks will become more closely aligned. In US states like Ohio, the Department of Transportation's P3 legislation specifically permits it to receive, consider, evaluate and accept unsolicited bids for a P3 project. It may then solicit competing bids under the unsolicited proposal process or terminate the process and procure the project through its regular tender process. In South Africa, an unsolicited proposal is either considered to be a PPP or it is not. If the former, the relevant agency must also comply with the relevant PPP regulations in performing the assessment. Some current

Australian policies (for example NSW and ACT)<sup>19</sup> also require an MLP which seeks to enter into a PPP to comply with the applicable guidelines.

- More detailed public reporting – there are three types which have been proposed – annual aggregated data,<sup>20</sup> information about the nature and scope of MLPs which are submitted and a proposal's progress through each stage, and once a proposal is closed, a PPP style contract summary.
- Development of standard documentation and tools to support the process and guide proponents (for example a process deed which can govern confidentiality, probity, reimbursement of government costs (if applicable), IP and refinement of a proposal in the mid stages or a template of the Participation Agreement required at Stage 2 of the NSW Policy).

Some MLP Policies are currently under review, and we may soon see some refinement both as to the specific requirements and the structure of the process in order to maximise benefits for both the State and proponents.

1. There are now policies in each State - Market-Led Proposals Guideline issued by Department of Treasury and Finance dated November 2015 (**Victorian Policy**), Unsolicited Proposals Guide issued by NSW Government dated February 2014 (**NSW Policy**), Guidelines for the Assessment of Unsolicited Proposals issued by the Department of Premier and Cabinet, SA Government on November 2014 (**SA Policy**), Project Assessment Framework (Guidelines for the assessment of market-led proposals) dated July 2015 (**Qld Policy**) and Unsolicited Bid Guideline (Limited to Land Sales) issued by the Department of Lands of the WA Government (**WA Policy**) and the Unsolicited Proposals Policy and Guidelines issued by Department of Treasury and Finance on 1 January 2015 (**Tas Policy**). The Department of Treasury in the ACT issued an Unsolicited Proposal Guideline in March 2015.
2. The concept of a private sector initiated proposal to government is not new. Many countries enable the submission of unsolicited proposals although the formality of the policies governing such submission vary. In Australia, Queensland has had an MLP policy in place since 2001, and the Sydney Harbour Tunnel was constructed following an unsolicited proposal submitted in 1986 by Transfield \ Kumagai Gumi.
3. It has been reported in the media that in Queensland, since the current Qld Policy was launched in July 2015, more than 100 projects have been presented to government, including 37 formal proposals, but only one has progressed to Contractual close.
4. Queensland Opposition party policy announced in February 2017 states that its revised MLP policy would commit to a four month assessment period for proposals, publish more detailed information about proposals, relax the uniqueness test and emphasise delivery ability and value for money.
5. Qld Policy, Victorian Policy, NSW Policy.
6. This could mirror the contractual rights a party is sometimes given has if a contract is terminated for convenience due to a policy change. The Pakenham Cranbourne Rail Capacity Upgrade MLP was cancelled when the new Victorian Government implemented its (differing) policy of level crossing removal. It was reported that the consortium was paid an amount for design work completed.
7. The Arizona Department of Transportation charges two fees –for \$15,000 for the initial evaluation and then a sliding scale based on capital cost for any detailed evaluation. ADOT reserves the right to waive the fee if it considers this in the best interests of the state.
8. The implication is that it will only do so if the proposals are received before it commences to negotiate with one proponent.
9. The NSW Auditor General has suggested that this avenue needs to be made clearer in the Policy.
10. The ACT Guidelines also permit this.
11. Many US states will automatically commence a competitive process once a MLP has been evaluated and 'accepted'.
12. In Chile, the bonus may also be sold to another tenderer. Ministry of Public Works, Regulations of MOP Statutory Decree no 164 of 1991 made under Supreme Decree no 294 of 1984 and Supreme Decree no 900 of 1996 in relation to Private Initiative Ideas.
13. *Private Participation in Infrastructure Act 1998*
14. This express right is provided only in relation to roads (Policy of the South African National Roads Agency in respect of unsolicited proposals May 1999, and National Treasury Republic of South Africa Practice Note No 11 of 2008/2009 on Unsolicited Proposals)
15. *Public Works Concession Law 1998*
16. This forms part of the Queensland Opposition party's revised MLP policy framework.
17. This also forms part of the Queensland Opposition party's revised MLP policy framework.
18. Under this two phase model a Prior Information Notice describing the project is put to the market, the best proposal is selected and that is then put back out to tender. The proposals are then evaluated and a 'promoter' selected. Then a tender for the concession is issued and a concessionaire selected. The original promoter is given the opportunity to match the best offer.
19. For example only, although the ACT has two Guidelines for PPPs and Unsolicited Proposals, the framework envisages the application of both guidelines to an unsolicited proposal for a PPP. Applicability of an MLP for a PPP delivery will be undertaken in Phase 2.
20. The Audit Office of NSW provided detailed data in its Performance Audit on Managing Unsolicited Proposals in NSW dated 10 March 2016

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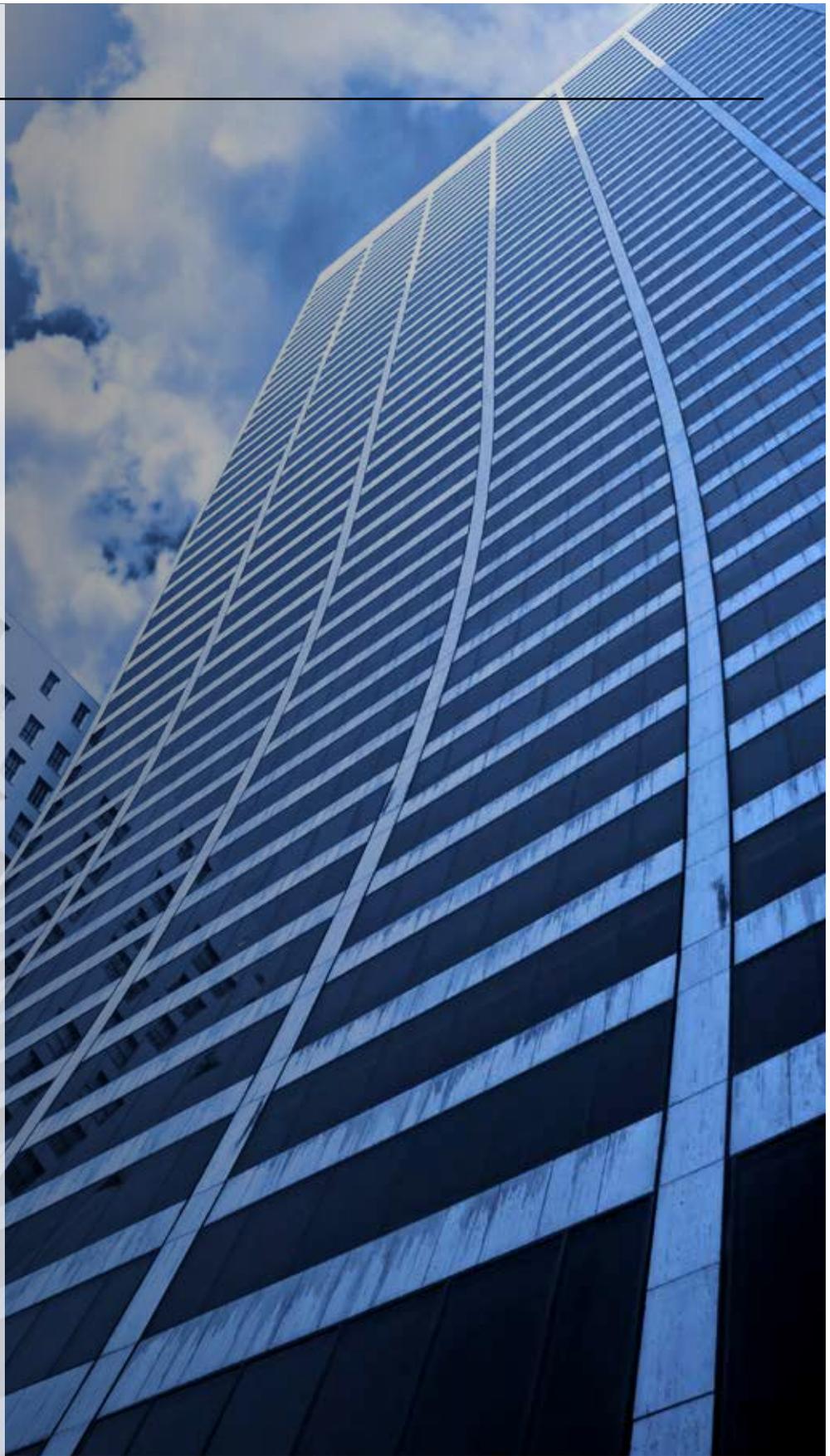
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