

26 October 2018

New Independent Infrastructure Body
The Treasury
PO Box 3724
Wellington 6140
New Zealand

Dear Mr Makhoul,

Guardians of New Zealand Superannuation Submission on Treasury's consultation document: A New Independent Infrastructure Body

Thank you for the opportunity to comment on the proposal for a New Independent Infrastructure Body.

1. Background

- 1.1. The New Zealand Superannuation Fund (the Fund) invests money, on behalf of the Government, to help pay for the increased cost of universal superannuation entitlements in the future. The Fund is managed by a Crown entity, the Guardians of New Zealand Superannuation (the Guardians). As at 30 June 2018 the Fund totalled \$39b; of this amount approximately \$6b is invested domestically.
- 1.2. In 2009 the Guardians received a Direction from the Minister of Finance. This Direction, which is still in place, requires the Fund to appropriately identify and consider opportunities to increase the allocation of New Zealand assets in the Fund, subject to the Guardians' duty to invest the Fund on a prudent, commercial basis. The promotion of domestic infrastructure investment is specifically noted within the Direction.
- 1.3. The Guardians sees large scale domestic infrastructure opportunities as having commercial potential and has a current proposal, alongside Canadian institutional investor CDPQ, to explore funding, designing, building, operating and owning the Auckland Light Rail Project.
- 1.4. As at 30 June 2018, around 2% of the Fund's \$6b New Zealand investments was invested in infrastructure. In the context of a restriction on the Fund's ability to control an operating company (s59, New Zealand Superannuation and Retirement Income Act), the Guardians believes it will be challenging to materially increase the Fund's investments in New Zealand without access to large scale infrastructure investment opportunities.
- 1.5. The Guardians has specific expertise in infrastructure investment developed through a range of offshore and domestic investments over the last 15 years. As both an experienced global investor and a significant player in New Zealand's capital markets and investment landscape, we are well positioned to comment on the direction of infrastructure reform in New Zealand. Our submission also reflects our recent experience

in dealing with the Crown as our capacity as a prospective investor in light rail and in the Christchurch redevelopment.

- 1.6. Further information about the Guardians and Fund can be found at www.nzsuperfund.nz.

2. Summary of Submission

- 2.1. We are supportive of the establishment of an independent Infrastructure Body. Reform in this area is critical, given the pressing need to address New Zealand's infrastructure deficit.
- 2.2. It is important that a set of objectives is developed to support and guide the establishment of the Infrastructure Body.
- 2.3. A broader and much more detailed definition of infrastructure than that provided in Treasury's discussion document is needed to provide the basis for decisions to be made on what aspects of infrastructure the new body will cover and what roles it will play in relation to each category of infrastructure. It is also important that significant thinking is given to the scope of the Infrastructure Body and the specific roles it will play, especially in regard to interactions with other Government agencies.
- 2.4. We support the new body leading a workstream to develop a new long-term infrastructure strategy for New Zealand, but care needs to be taken to ensure that this does not become an avenue for re-litigating decisions that have already been made.
- 2.5. In playing a greater role in procurement, the new body has the potential to provide a much needed separation between the functions of procurement and investment partnerships.
- 2.6. We are supportive of the intention for the new body to publish long-term capital intentions, but believe this should be extended to include the identification of funding gaps and potential investment opportunities.
- 2.7. It is important that the body has a central and co-ordinating role in business case development, without creating additional layers of process and bureaucracy.
- 2.8. The roles of the body need to be extended to include responsibility for developing funding mechanisms and the revenue streams necessary to access additional funding sources.
- 2.9. The new body also needs to have a role in considering both the impact of climate change on infrastructure requirements and the effect of infrastructure decisions on climate change.
- 2.10. We are of the view that the body needs to be clearly tied to the Government, with an independent board appointed by responsible ministers through arrangements based on the Crown Entity model. Notwithstanding the need for the new body to be able to speak on behalf of the Government of the day, it is critical that its governance is established in a way that enables it to plan a long-term infrastructure programme for New Zealand. Infrastructure development and ownership horizons are longer than the political cycle and institutional investors are attracted to projects with a high degree of certainty.
- 2.11. In establishing the new body, a clear model needs to be developed for the allocation of risk between delivery and/or investment partners.

- 2.12. Relationships between the new body and local government will need to be carefully defined and agreed between all relevant stakeholders if the reforms are to be successful.
- 2.13. Crucially, any new planning processes the new body gives rise to must be aligned as seamlessly as possible with existing planning processes.

3. Need for Infrastructure Reform

- 3.1. New Zealand's infrastructure deficit, and the level of investment and development required to address it (estimated by Treasury at \$129 billion over the next decade), are among the most pressing economic challenges facing the country. If the infrastructure deficit remains unaddressed it will have a significant, negative and material impact on New Zealand's future economic potential, prosperity and well-being. The compounding impact of under-investment and aging (and aged) infrastructure, alongside the effect of population growth and in particular the concentration of growth in and around Auckland, have come together to result in inadequate infrastructure becoming one of the country's most acute economic constraints and risks. Compounding this, the need to adapt to climate change will place new, and as yet undetermined, pressures on infrastructure ranging from State Highways, to railways, ports, storm water and wastewater systems, flood and river control systems and buildings and structures around the New Zealand coast.
- 3.2. It is our view that current policy settings, funding systems, decision-making processes and the associated institutional structures are neither fit for purpose nor capable of delivering the quantity and quality of infrastructure investment and interventions that are required. Step change reform is needed if we are to deliver the outcomes necessary to provide a modern, robust and flexible infrastructure platform to facilitate and support New Zealand's economic future and address climate change.
- 3.3. For these reasons, the Guardians is, in general terms, supportive of the Government's view that fundamental change is needed in this area and of the thinking behind, and direction of, the proposals for reform. We support both the intent of the proposal and the broad framework on which the discussion document is based.
- 3.4. New Zealand's infrastructure development systems and framework are uncoordinated, complex and inefficient. Due to the lack of an holistic, joined-up and deliberate approach to building a system of infrastructure, New Zealand has the significant infrastructure deficit noted above, along with duplication and systemic gaps in infrastructure.
- 3.5. Unaddressed, New Zealand's infrastructure challenges will only grow more acute and, therefore, more difficult to realistically confront, eventually becoming intractable. The uncoordinated and disjointed infrastructure system under which New Zealand currently labours is, in fact, a major reason that, as a country, we are so far away from where we need to be in having modern, future-focused and integrated infrastructure networks. The public decision-making systems are themselves a key contributor to the deficit that has developed.
- 3.6. In light of this, there is a very real urgency to the type of reform that is being proposed. It is extremely positive and entirely welcome, therefore, that the Government is moving to expedite, as much as is prudent and practicable, the necessary operational, structural and governance reform.

- 3.7. Reform is also necessary and urgent for another reason: that New Zealand is required to compete in an increasingly competitive global market place for the capital, resources, capacity and expertise necessary to deliver its infrastructure requirements (the World's infrastructure deficit has been estimated by McKinsey at US\$21 trillion). Competing successfully for these resources, at the level necessary to deliver appropriate infrastructure outcomes, necessitates the development of a modern, best practice interface with the relevant markets. Such an interface will need to communicate effectively with the international markets and present our requirements and opportunities in a way that resonates clearly with them. This capacity and functionality is a basic prerequisite if we are to attract the necessary resources and expertise, at the best available quality while delivering value for money. As a country, we are far from occupying that space.

4. Objectives

- 4.1. Quality and successful reform programmes tend to be based on a clear set of objectives, agreed at the start of the process. This is particularly important for complex and broad reaching reforms. Such an approach provides a framework and clear guidance as the multitude of decisions involved in complex public policy processes are made, trade-offs determined and judgements made on balancing seemingly conflicting imperatives. It is unfortunate, therefore, that neither Treasury's discussion document nor the available background papers explicitly set out the objectives for the proposal to establish a new infrastructure body and associated reforms. It is our submission that such objectives need to be determined and agreed as a next step priority, and certainly prior to substantive decision making or detailed design of the organisation and its authority.
- 4.2. From our reading of the discussion document, a potential set of objectives for reforms designed to establish the new infrastructure body could involve a primary objective of:
- Developing efficient and co-ordinated structures, systems and practices which contribute to addressing New Zealand's infrastructure deficit through the delivery of quality, best-practice infrastructure outcomes.
- 4.3. The new body will contribute to advancing this overarching objective if it succeeds in:
- streamlining processes at all levels of the infrastructure value chain and decision-making processes;
 - delivering stronger and more integrated infrastructure strategy, planning, investment and delivery;
 - facilitating joined-up investment decisions and decision making;
 - providing an improved evidence and data base for decision making and planning;
 - developing clear, detailed and saleable pipelines of infrastructure projects;
 - improving procurement capability across all levels of governments;
 - providing advice on the need and potential case for different funding arrangements;
 - developing a clear and decisive framework for responding to unsolicited proposals for major projects; and
 - working with the Climate Change Commission to provide advice on the design of infrastructure to adapt to the impact of Climate Change.

5. Defining Infrastructure

- 5.1. If the establishment of the infrastructure body and associated programme of reform is to be successful in addressing New Zealand's infrastructure challenges, a clear, detailed and comprehensive definition of what constitutes infrastructure will be necessary. Such a definition will ensure that the characteristics and requirements of the various components of the types of infrastructure and networks are accurately understood. In turn, this will ensure that differences and specific requirements can meaningfully be factored in to the work that will lead the development and design of the new infrastructure body and the infrastructure development practice and processes that it will give rise to.
- 5.2. Page three of the discussion document includes the following definition of infrastructure:

Infrastructure means fixed, long-lived structures that facilitate economic performance and well-being. Infrastructure includes buildings and physical networks, principally: transport, water, energy, social assets and digital infrastructure such as mobile and broadband infrastructure. Infrastructure is delivered by central government, local government and the private sector.
- 5.3. While this provides a reasonable starting point, a broader and much more detailed definition is needed if it is to provide the basis for decisions to be made on what aspects of infrastructure the new body will cover and what roles it will play in relation to each category. Given the diversity of assets captured by this definition, a detailed understanding of the range of different roles associated with the delivery of each category will need to be developed. Requirements and processes associated with network infrastructure are very different from the drivers and issues relating to social (including cultural and sports) infrastructure and, similarly, a whole different set of issues and industry arrangements are associated with digital infrastructure. For instance, while social infrastructure is and will remain predominantly under public control, digital infrastructure is almost entirely private sector owned and operated and provided on a commercial basis. Cultural and sports infrastructure is a mix of the public and not-for-profit sectors. A one-size fits all infrastructure approach will not work in terms of the new body's roles, responsibilities and functions.
- 5.4. We note that central and local Government thinking predominantly seems to be based on the current understanding of the boundary between public and private involvement and responsibility. The definition needs to be aspirational in terms of questioning current boundaries and evolving thinking about potential roles for the private sector, and private capital in building and owning infrastructure – including questions of roles around the funding, financing and potential regulation of natural monopolies (pricing and return).
- 5.5. For the purposes of this submission, we have not proposed a comprehensive definition of the type we are suggesting as being necessary. In fact, it is our submission that the development of a fit-for-purpose definition is actually a substantial body of work in its own right, and one that will need to be inclusive of input from all of the different categories of players in the infrastructure industry. It is our further submission that this is a piece of work that needs to be completed very early on in the policy process, representing a crucial, 'first principles' building block, if the reform process and resulting infrastructure body is to be successful.

6. Scope/Role

- 6.1. In broad terms, the Guardians supports the potential roles for the new infrastructure body as proposed in the discussion document. In our view, however, the proposed roles need to be extended and, in some areas, be more accurately defined. As discussed earlier in this submission, given the diversity and complexity of the broad infrastructure industry, definitional clarity is essential if the proposed reforms are to be successful. This is equally the case in relation to role definition where clarity will ensure that the reforms improve the effectiveness of the overall system by introducing clear responsibilities and lines of accountability, rather than increasing complexity by adding additional layers of process and bureaucracy.
- 6.2. Sections 7 - 12 of this submission set out the detail of our submissions as they relate to the roles and responsibilities of the proposed new infrastructure body.

7. Strategy

- 7.1. The Guardians supports the proposed function for the new body of working to develop a clear understanding of long-term infrastructure strategy. Each stage of the process through which infrastructure moves, from conception to delivery, will only ever be as effective as the strategy which gives rise to the investment. It is, therefore, imperative that the new body takes a central and leadership role in the coordination and development of the over-arching national infrastructure strategy.
- 7.2. As the body will not necessarily be the primary decision-making body in relation to particular infrastructure investments (which is appropriate), this role does involve the risk of an effective second-guessing mechanism (or avenue for re-litigation) being created in relation to the work and/or decisions of the agencies directly accountable for specific infrastructure plans or projects. To the extent that this eventuates, the new agency will fail to streamline processes and deliver greater efficiency in relation to decision making. In designing the new body, and its interfaces with existing agencies, clear accountabilities and responsibilities, based on principles of subsidiarity, will need to be developed so that the strategy leadership role does not inadvertently impact to impede infrastructure planning.
- 7.3. Given the range of functional areas the long-term infrastructure strategy will touch on, and the layers of specialisation involved, the new body's strategy leadership role does raise issues in relation to the breadth and depth of expertise that will be necessary within it if this function is to be effectively delivered. If not properly resourced, centralised strategy functions can end up delivering lower quality strategies than would otherwise have been the case. In designing and structuring the new body, this risk will need to be an important consideration and adequate resource made available within it to avoid such outcomes. Similarly, in developing its strategy function, the body will need to develop high quality linkages into other agencies in order to make the most of the strategic resource and input that they can provide. An ability to break through existing silos and build inter-agency relationships where they do not currently exist will be crucial, therefore, if the new body is to fulfil a strategy leadership role to the level and standard that is required. We would see the potential, for instance, for the new body to second expertise from existing infrastructure delivery agencies to fill short term expertise gaps.

8. Procurement

- 8.1. The Guardians supports the proposal that the new body will be a key player in improving the quality of procurement practice. Procurement practice is currently inconsistent and of variable quality across the public sector, making it more difficult for potential partners to engage with the Government. As a result, procurement is less efficient, in aggregate, than it potentially could be. The establishment of the new body, and the behavioural change mechanisms and potential for redesign it provides, creates an excellent opportunity for this long standing, seemingly intractable, issue to be addressed.
- 8.2. It is important that, in focusing on robust procurement processes, the new body does not inhibit the potential for collaborative conversations and dialogue with prospective investors and delivery partners. The skills and approaches needed to attract investment capital and innovation are quite different in today's world, given the rapid pace of technological change, compared to a traditional procurement model. There needs to be an openness to (for example) undertaking pilot projects and testing new technologies. Under the current traditional models currently being utilised, opportunities and potential investment partners are being, or at least will be, lost. The establishment of a new body provides a much-needed opportunity to position New Zealand so that it is able to potentially access the full gamut of possible investors, current and future financing options, and innovative technologies.
- 8.3. The creation of the new body provides an opportunity to define and separate the two very different functions of procurement and investment attraction. If the opportunity is not taken to separate these functions and consider investment attraction outside traditional procurement models, the risk is that the reform will simply deliver improved and better co-ordinated procurement capacity. Such an outcome would impact negatively on New Zealand's current and potential capital raising capacity, and detract from the procurement system's ability to perform the functions it was specifically intended to deliver.

9. Capital Intentions

- 9.1. Proposed "Function 5" in the discussion document relates to co-ordinating the development and publishing of a single source of information on long-term capital intentions. The proposed approach that would combine information from across all sources of public and private sector planning documents would be invaluable, demystifying the vagaries and complex layers of the multitude of relevant planning processes. The resulting resource will enable New Zealand to communicate directly and meaningfully with the international infrastructure industry and, importantly, in a way that meets their requirements. Achieving this would represent a significant competitive advantage.
- 9.2. In our view this concept, however, needs to be extended to include the identification of capital or funding gaps and, therefore, potential investment (or co-investment) opportunities. New Zealand operates a complex and unique mixture of funding sources for infrastructure projects and it should not be assumed that the international investment/finance industry understands our systems sufficiently to accurately identify, through analysis of the primary planning and funding documents, where the opportunities exist.

- 9.3. The Guardians, given its international connections and experience, would be well placed to advise the new body on much-needed policy in this area.

10. Business Case Development

- 10.1. It is our submission that the new infrastructure body must have a central and co-ordinating role in the development of infrastructure business cases. A great deal of effort, over many years, has been focused on the improvement of business case development capacity in the public sector. While improvements have resulted, practice remains variable and has a tendency to suffer from an excessively template-based approach being adopted. The establishment of the new body creates an opportunity to leverage a step change in the quality of business case practice.
- 10.2. To achieve this outcome, however, it will be vital that the new body's specific role in this area is clearly defined and structured so as to contribute to improved quality, while avoiding duplication and unclear lines of responsibility. If involving the body in business case practice simply results in an additional set of requirements or a further layer of bureaucracy, it will have failed in achieving its objectives.
- 10.3. It will also be important that flexibility is built into processes so business case work can appropriately be adapted to meet the needs of alternative funding or delivery models and other technological or commercial innovations.

11. Funding

- 11.1. Funding and financing are, in our view, areas that are not adequately explored or covered by the proposals contained in the discussion document and yet these are one of the key challenges that are currently being grappled with by government, both local and central. It is our submission that the functions proposed in the discussion document need to be expanded to include responsibility for developing funding mechanisms and/or revenue streams that will be necessary if realistic access to potential sources and structures of finance are to be brought into play.
- 11.2. The need for this work has been apparent for many years, but continues to drift and to lack focus and immediacy. Given the pressing needs and challenges that New Zealand faces in terms of infrastructure development, it is imperative that this work is progressed as a matter of urgency and in a way that is practically connected, in a meaningful way, to the real-world requirements of global infrastructure investment decision making and drivers.
- 11.3. The development of an infrastructure body provides an opportunity to deliver exactly the type of momentum that is needed in this area. To achieve this, however, policy development will need to be based on the actual imperatives of global capital markets, not the perceived needs, and advice informing the process will need to be structured to deliver this. NZSF is uniquely placed, in terms of New Zealand Government entities, to objectively provide the Government with such insights from a practical international perspective.

12. Climate Change

- 12.1. In our submission, the role of the new infrastructure body needs to be extended to include consideration of the impact of climate change, and associated impacts, on infrastructure requirements. Alongside this, the body needs to be central to thinking and provision of

advice on the extent that infrastructure development and provision is contributing to climate change and the identification of responses to mitigate such effects.

13. Governance/Independence

- 13.1. A key factor to the success of the new infrastructure body will be the level and nature of governance independence it is established with. In terms of government entities, independence ranges from the relatively direct control exercised over ministries and departments to the much greater independence offered by the Crown Entity model (which itself operates with a range of levels of independence).
- 13.2. It is our submission that the governance of the new infrastructure body needs to be clearly and meaningfully tied to the Government in order to give the industry and potential investors the confidence that it can speak for and on behalf of the Government (i.e. material or pure independence from Government is not desirable). The body, as currently proposed, will not directly be bringing capital to the table. If it was also not in a position to bring a demonstrable capacity to tie external proposals into the layers of public sector structures, it will struggle to build the credibility or relevance necessary for it to operate successfully. To achieve this, in our view, it will need to be unambiguously part of the Government's structures. If it is set up to be an independent body, it runs the risk of simply becoming another advocate or ginger-group organisation, and that will further confuse processes rather than clarifying and streamlining them.
- 13.3. The relevant issue is, we believe, a question of from whom the new body is to be independent. It is our view that the new body needs to be independent from all of the Government agencies who are involved in the procurement and delivery of infrastructure, not independent from Government per se.
- 13.4. Having taken this view, the next question is where, on the spectrum of independence that can be achieved within government structures, should the new body be positioned. In our view, if the body is to be effective in delivering across the broad range of intended roles, then some level of actual and perceived independence is desirable. In light of this, it is our submission that a governance model should be adopted that would place the new body at the more independent level of the Crown Entity spectrum. Consistent with this, the body would have an independent, but Government-appointed, Board and report to the Government and Parliament through its responsible ministers.
- 13.5. Notwithstanding the need for the Infrastructure Body to be able to speak on behalf of the Government of the day, it is critical that its Governance is set up in a way that enables it to plan a long-term infrastructure programme for New Zealand. Infrastructure development and ownership horizons are longer than the political cycle and institutional investors are attracted to projects with a high degree of certainty.

14. Allocation of Risk

- 14.1. If the new body is to be successful it is important for there to be a very clear and transparent model developed for the allocation of risk between delivery and/or investment partners. Alongside that, clarity will be crucial with respect to the responsibilities and functions relating to managing that risk. Issues associated with risk and risk allocation are particularly imperative in relation to procurement, construction and any partnership, co-funding or co-investment models.

- 14.2. The topic of risk has not been adequately canvassed in the discussion document and, in our view, this is an area where considerable work is required, representing, as it does, a demonstrable prerequisite to successful reform.

15. Relationships with Other Agencies

- 15.1. The importance of quality inter-relationships with existing agencies has been discussed from a number of perspectives in this submission. On top of that, however, there are some major structural relationships that will require a lot of careful work if the new infrastructure body is to be effective. The most obvious of these are in relation to local government. There will be a number of very difficult issues that need to be worked through and managed in relation to the current roles and responsibilities of local government in infrastructure development. In many ways these issues will be more difficult than those that exist between government departments and agencies. The reason for this is that while local government consists of statutory organisations, they are organisations with established public mandates in their own rights and, therefore, are less straight forward for the government to manage. There are numerous examples of public policy reforms that have been derailed because of the resistance of local government and that is a very real risk here, where the inter-relationships are complex and multi-layered.
- 15.2. At a different level, from our reading of the discussion document, it is unclear how the new body will interact with the existing Infrastructure Advisory Board (IAB) and Unit. It does not appear that the new body is intended to replace the IAB and yet there is seemingly a significant overlap in terms of the intended functions of the new body and the existing advisory board. It will be important, if greater clarity and effectiveness is to result from the reforms, that the demarcation of responsibilities of the two agencies are very clearly defined.
- 15.3. Similarly, if the new body is to effectively deliver an investment attraction and negotiation function (and in our view it must), issues such as how the new body is positioned alongside, and interacts with, agencies such as the Government's Debt Management Office, will also need to be considered and addressed.

16. Relationships with Existing Planning Processes

- 16.1. New Zealand's current infrastructure framework comprises a proliferation of inter-related strategies, funding mechanisms and planning documents and processes. Ideally, the establishment of the new infrastructure body would create an opportunity to rationalise and streamline existing systems – which can be tortuous and difficult to manage and navigate. History and the sheer scale of such an undertaking, however, very much suggest that such an outcome is unrealistic. In fact, if the successful establishment of the new body was in anyway reliant on the rationalisation of existing planning process, the risk would be that the process is effectively, albeit inadvertently, set up to fail.
- 16.2. Given this, it is crucial that any planning processes that the new body gives rise to, are meshed and aligned as effectively and seamlessly as possible with the existing planning structures.
- 16.3. If the effect of the new body is to add additional layers and requirements to the existing planning processes the new body runs the risk of making planning more complex, more unwieldy and less likely to deliver quality and rationale outcomes. This will particularly

be the case if the time frame for any new planning requirements are not aligned with existing time frames.

17. Conclusion

- 17.1. The Guardians supports the Government's view that major reform of New Zealand's infrastructure delivery model is needed and in broad terms supports the development of a new infrastructure industry body. Much work is needed to ensure that this policy process and the establishment of a new organisation is successful. The Guardians looks forward to working with the Government to contribute to achieving such an outcome.
- 17.2. We would welcome the opportunity to discuss our submission with you. The contact point for further information is: Catherine Etheredge, Head of Communications, cetheredge@nzsuperfund.co.nz.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Will Goodwin', followed by a long horizontal line extending to the right.

Will Goodwin

Head of NZ Direct Investment

CC: infrastructure@treasury.govt.nz; Jon Grayson, Joe Sant, John Young – The Treasury; Offices of the Ministers of Finance and Transport.