Alliance Framework

Table of Acronyms 2
1 Introduction 3
2 Purpose of this document 3
3 Alliance contract overview 4
4 Alliance organisation and governance 7
5 Building and sustaining a high-performance delivery culture 7
Appendix 1: 3-limb compensation model 9
Appendix 2: Outline of ADP scope and terms of a Single-TOC Alliance Development Agreement 12
Appendix 3: Distinctive legal features of the Project Alliance Agreement 15
Appendix 4: Further discussion of alliance structure and management 18

Table of Acronyms

ADA	Alliance Development Agreement
ADP	Alliance Development Phase
AE	Adjustment Event
AEGs	Adjustment Event Guidelines
AF	Alliance Framework
ALT	Alliance Leadership Team
AMS	Alliance Management System
AMT	Alliance Management Team
DCP	Defects Correction Period
FA	Financial Auditor
KPI	Key Performance Indicator
KRA	Key Result Area
MCOS	Minimum conditions of satisfaction
NOP	Non-Owner Participant
PAA	Project Alliance Agreement
SC	Substantial Completion
TCE	Target Cost Estimate (fully detailed build-up)
TOC	Target Outturn Cost (single number)
TPE	Third-party Estimator

1 Introduction

1.1 The Province of British Columbia is procuring some major infrastructure projects using an alliance contracting model in cases where the level of risk and uncertainty is such that conventional risk-transfer contracting is unlikely to achieve the best outcomes.

1.2 Alliances and similar forms of contract have been successful in many parts of the world in circumstances where a conventional contract could limit market participation, drive inefficient risk premiums, or threaten the success of the enterprise when difficulties arise. In a conventional (risk-allocated) contract each party is motivated to protect its own interests, and when risks eventuate the actions required to protect individual positions can easily overwhelm the actions which would improve project outcomes. The central feature of alliance contracting is that most risks are shared, so when difficulties (or opportunities) eventuate, all parties are motivated to optimize the collective outcome because they all 'sink or swim together'.

1.3 An alliance contract would be near the mid-point on a spectrum of fixed price (majority of risks borne by the contractor) to cost-plus contracts (majority of risks borne by the Owner). It allows for a balance of cost and non-cost incentives which aligns contractor objectives with the Owner's objectives. This alignment of commercial interests means the parties will pull in the same direction regardless of the difficulties encountered. Experience in other jurisdictions shows that contractors are more willing to tackle difficult projects under an alliance contract because the probability of good outcomes for all parties is much improved.

2 Purpose of this document

2.1 The purpose of this Alliance Framework (AF) document is to provide a high-level overview of the key principles and typical arrangements for potential owners and industry participants. Specifically, this document sets out Infrastructure BC's thinking on the organizational, legal and commercial arrangements between the Owner[1] and Non-Owner Participant (NOP) entities that would be parties (collectively "Participants") in an alliance contract.

2.2 This AF is generic in nature and not structured around a particular project but an understanding of the concepts outlined in this document will inform decisions regarding specific projects and enable rapid development and execution of the relevant agreements.

2.3 This document does not detail the process for establishing an alliance, which requires a careful approach to establish collaborative behavioural foundations while ensuring value for taxpayers. However, for context readers should understand the following:

(a) There will typically be between two and five Non-Owner Participants in an alliance, depending on the breadth of skills and resources required to self-perform or manage critical elements of the project;

[1] The "Owner" has two distinct roles in an alliance contract: as the client of the alliance (Owner Representative) and as a participant in the alliance Owner Participant (OP). These roles are not differentiated in this Alliance Framework document. Under its role as client, the Owner will perform its obligations and exercise the rights and entitlements reserved to the Owner under the agreements. Under its role as participant, the Owner Participant will act as one team with the NOPs and together be accountable for the performance of the alliance and the alliance works.

(b) The Owner will normally expect the market to form bidding teams prior to entering the selection process;[2]

(c) The Owner will adopt an alliance process that suits the circumstances. The two options are:

- a 'Single-TOC' process in which a preferred proponent is identified on merit and works collaboratively with the Owner during the Alliance Development Phase (ADP) to develop a detailed Project Proposal, including binding Target Outturn Cost (TOC) and other performance targets – and potentially address early works; and
- a 'Competitive-TOC' process in which two shortlisted proponent teams work in parallel during the ADP to develop competing Project Proposals (again including binding targets).

(d) The Single-TOC process is more appropriate when the project features high levels of uncertainty and/or time pressure, requiring a close relationship between Owner and NOPs to progress the optimal solution and offers the potential to maximize market interest. The selection process focuses on the proponent's ability to maximize value over the life of the asset (not simply minimize capital cost), and to manage risk and respond well in the face of uncertainty.

(e) The Competitive-TOC process is more appropriate for projects with lower levels of uncertainty and/or less time pressure, where a more arms-length proposal development process will not prejudice project success.

2.4 This document covers various legal concepts but it is not intended to be legally precise; instead to explain in plain English the key legal and commercial foundations of a project alliance.

3 Alliance contract overview

3.1 The core function of a traditional contract is to set out the respective rights and obligations of the contracting parties. Typically, the contract will prescribe the scope of obligations, form of payment, and commercial or legal consequences where a party fails to fulfil its obligations. The process for establishing and administering such a contract, and the behaviours of the parties, all reflect this context.

3.2 Under an alliance contract most risks and opportunities are shared as illustrated below.

3.3 The key features of an alliance contract are as follows:

(a) The Participants take **collective responsibility** (in the full legal sense) for full delivery of the project, aiming to meet (or exceed) pre-agreed targets which typically cover both cost and non-cost performance aspects.

(b) The agreement establishes **a 'no-blame' commercial environment** in which the Participants have no enforceable legal rights against each other except in the extreme case of a 'Wilful Default' (e.g. insolvency, fraud, criminal conduct, deliberate and reckless misconduct).

(c) The NOPs are paid for their services under a **'3-limb' compensation model** comprising:

[2] As all subcontracts for the Project will be determined on a best for project basis by the Participants after ADA execution, the Participants are not bound to accept any subcontracts or sub-consultancy agreements for the Project entered into by the potential NOPs before the ADA execution.

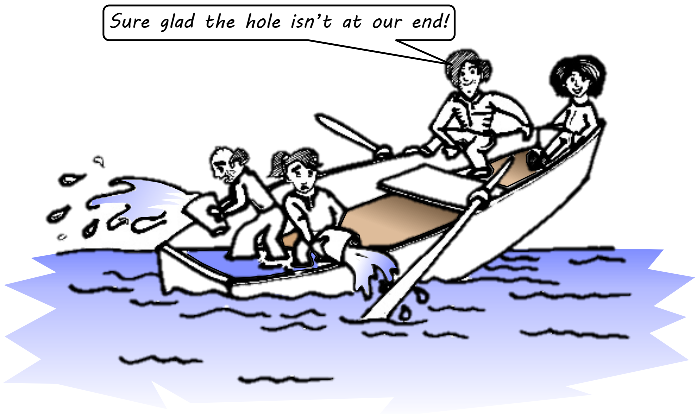
- Limb 1: reimbursement of project-specific costs on a fully open-book basis;
- Limb 2: a fee to cover corporate overheads and normal (risk-adjusted) profit, and
- Limb 3: incentive payments which may be positive or negative, reflecting an equitable share of the 'gain' or 'pain' if outcomes are better or worse than agreed targets.

The 3-limb compensation model is further detailed in **Appendix 1**.

(d) Governance arrangements create **a peer relationship between Participants** with decision-making based on agreed 'Alliance Principles' and requiring unanimity among the Participants, consistent with commercial arrangements in which all Participants 'sink or swim together'.

(e) The project delivery **team is fully integrated** – typically comprising members drawn from each Participant organisation – with each position filled on the basis of 'best candidate' (not on the basis of employer) since the goal is best collective performance rather than protection of individual Participant positions.

3.4 In combination, the arrangements outlined above are designed to create a situation in which the alliance Participants "win together or lose together" – there is no possibility of win/lose outcomes.



3.5 Alliance Participants are typically obliged to act in Good Faith (as defined in their agreements). In addition, they will normally develop and agree the principles to govern their dealings and behaviours, as the process of joint development is important in ensuring commitment and ownership. Typical 'Alliance Principles' are outlined below:

(a) All Participants win, or all Participants lose, depending on outcomes actually achieved.

(b) A peer relationship where all Participants have an equal say (recognising the Owner's unique role in certain decisions).

(c) Collective responsibility for performance, with an equitable sharing of risk and reward.

(d) Full access to 'best-in-class' resources from all Participants.

(e) A focus on innovative thinking and a commitment to achieve outstanding results.

(f) Clear responsibilities within a no-blame culture.

(g) Open and honest communication between all Participants.

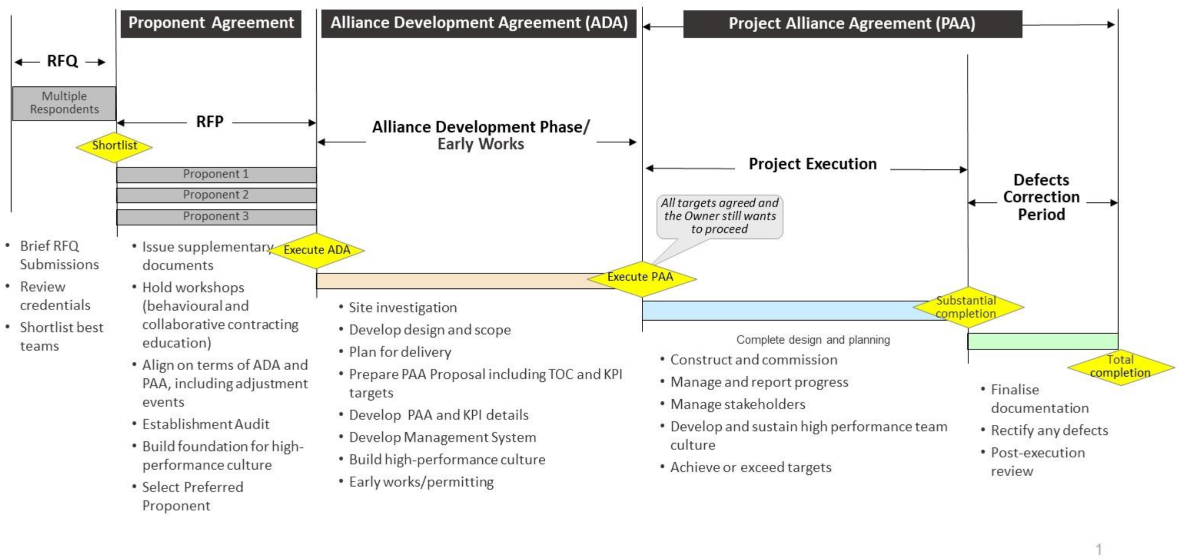
(h) All transactions are fully open-book.

3.6 Alliance activities are governed in two stages under two agreements:

(a) The **Alliance Development Agreement** (ADA) governs the ADP during which the NOP teams will work collaboratively with the Owner to develop a detailed Project Proposal and prepare for project delivery.

(b) The **Project Alliance Agreement** (PAA) governs the delivery phase, commencing once the Owner approves the Project Proposal, and continuing through to the expiry of the Defects Correction Period (DCP).

3.7 The diagram below outlines the alliance lifecycle for a 'Single-TOC' process , including tenure of the agreements and key activities in each phase. A 'Competitive-TOC' process comprises essentially the same phases but with two proponents working in competition during the ADP, prior to selection of the preferred proponent.

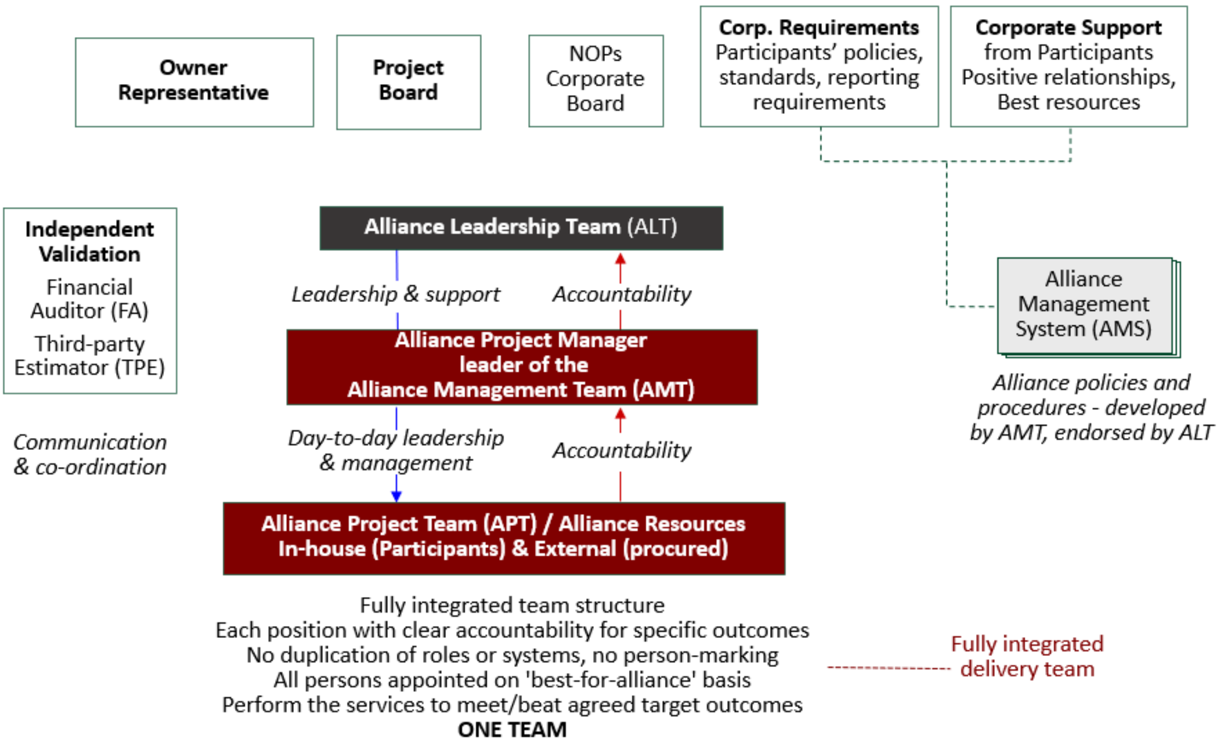


3.8 An overview of ADP scope and ADA terms is shown in **Appendix 2.**

3.9 A summary of distinctive legal features of the PAA is provided in **Appendix 3**.

4 Alliance organization and governance

4.1 The following diagram outlines the typical alliance governance and organizational structures.



4.2 Further details on alliance organizational structures, and roles of the Alliance Leadership Team (ALT), Alliance Project Manager, and Alliance Management Team (AMT) are provided in **Appendix 4**.

5 Building and sustaining a high-performance delivery culture

5.1 Under a traditional contract where obligations and risks are mostly unilateral, although the parties may declare a commitment to shared project objectives, the reality is that their commercial interests are not fully aligned and each party must participate in a way that protects its own commercial position. This underpins the nature of key behaviours on the project, limiting possibilities for close collaboration and in some cases resulting in adversarial relationships and poor outcomes.

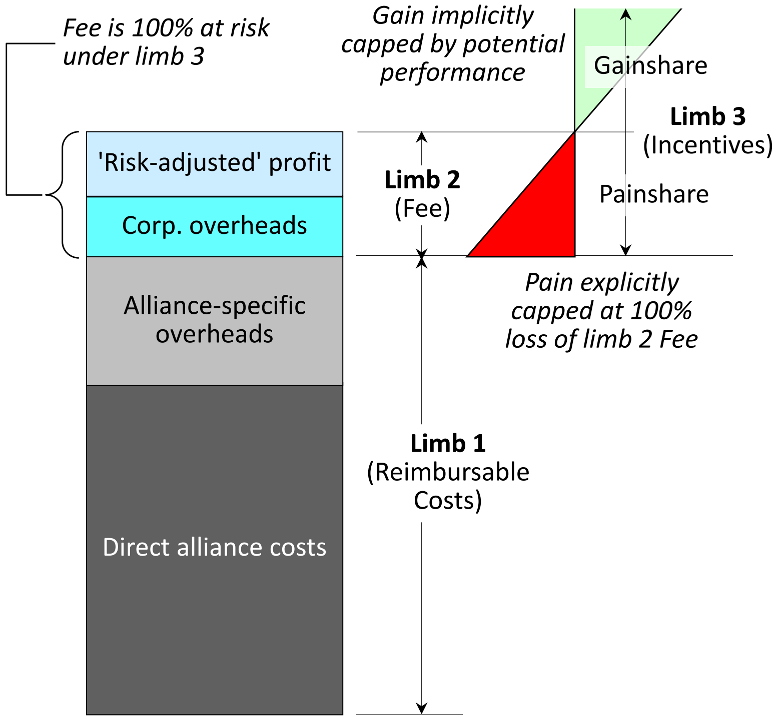
5.2 An alliance contract creates the (commercial) conditions where traditional barriers to cooperation are substantially reduced or eliminated. However, while this creates the potential for genuine collaboration, it does not make it certain. Key individuals may be used to operating in more adversarial contracting environments, and the behaviours that enable strong team performance do not necessarily arise automatically just because the alliance aligns the parties' commercial interests. To maximize this potential there must be a clear intention and a consistent effort to develop true collaboration. Steps to overcome this limitation may include:

(a) Engaging an experienced alliance facilitator to ensure that the Owner is clear about their collaborative intentions, and to help conduct the establishment process in a way that fosters genuine cooperation and trust; and

(b) Introducing behavioural training or coaching – particularly at the leadership levels and during the formative stages of the alliance – to help the Participants build and sustain a high performing collaborative culture.

Appendix 1: 3-limb compensation model

The 3-limb compensation model (illustrated below) lies at the commercial heart of the alliance as it governs how the NOPs are paid and incentivized under the PAA.



The three limbs are as follows:

- **Limb 1 Reimbursable Costs**: Reimbursement of expenditure on the work under the alliance (including mistakes, rework and wasted effort) and project-specific overheads related to the alliance work is reimbursed at actual cost subject to audit;
- **Limb 2 Fee**: A mark-up to cover (risk-adjusted) profit and a contribution towards recovery of corporate (off-site) overheads; and
- **Limb 3 Gainshare / Painshare**: A share of the collective 'gain' arising from out-performing agreed targets or 'pain' associated with under-performing against those targets.

Further details of these three components are provided below.

In relation to **Limb 1**:

- Rules and principles for Limb 1 Reimbursable Costs are defined in detail under the PAA, with the overriding principle being reimbursement of costs specifically incurred for the alliance work (i.e. costs which would not have been incurred if the NOP had not won the contract). This includes reimbursement of costs associated with mistakes and rework (noting that sharing of cost under/overruns under Limb 3 motivates each NOP to minimize wasted effort and rework).
- Limb 1 does not include any recovery of corporate overheads or profit. This means Limb 1 reimbursement 'goes in one pocket and out of the other' – the NOP is financially disinterested in Limb 1 per se.

- In a Single TOC alliance, the Owner appoints a third-party Financial Auditor (FA) to conduct 'Establishment Audits' on prospective NOPs during the procurement process and while still in competition to resolve any ambiguity associated with Limb 1 recovery and prepare for reimbursement of payment claims with minimal fuss.
- Reimbursement of Limb 1 costs is performed on a fully open-book basis. In a Single TOC alliance, the FA will undertake routine audits under the ADA and PAA to verify that payments are in accordance with the agreement.

In relation to **Limb 2**:

- Limb 2 is normally agreed as a simple mark-up percentage applied to actual Limb 1 costs
- If the alliance is being established via a Single-TOC process the Establishment Audits will also provide information on historic actual margins on comparable projects, as well as corporately, to overcome information asymmetry when the Owner and prospective NOPs align on Limb 2. The NOPs will need to present and justify their margin to the owner and come to a point of mutual agreement with the owner on the appropriateness and fairness of the Limb 2 through a commercial alignment process.
- In a Competitive-TOC alliance process the prospective NOPs are free to set their Limb 2 Fee at whatever level they believe appropriate, since the TOC comprises the estimate of Limb 1 plus Limb 2 and overall price competition likely precludes excessive margins. However, best practice is to include information on historic actual margins as part of the Establishment Audit in the spirit of transparency and fairness.
- Regardless of the method of agreeing Limb 2, it is important that Limb 2 is not locked in until the other terms of the PAA are agreed (i.e. once the overall risk profile is clear) – including for example scope of Limb 1 costs attracting Limb 2 mark-up, extent of risk sharing, and rate at which potential painshare / gainshare will accrue.
- It is important that the NOPs see the process for establishing Limb 2 (indeed the overall terms of the agreement) as fair and reasonable, to avoid creating a situation where NOPs need to recover reasonable margin by resorting to adversarial behaviours later in the design and construction phase.

Limb 3 incentives are directly linked to project outcomes, so the NOPs are all highly motivated to ensure the alliance performs as well as possible:

- Performance targets (i.e. performance for which the NOPs accrue neither 'gain' or 'pain') are sometimes referred to as the minimum conditions of satisfaction (MCOS).
  - If aggregate performance is poorer than targets then Limb 3 will be a negative sum ('painshare'), capped in the worst case at a value equal and opposite to Limb 2 (although such an outcome is extraordinarily rare).
  - If aggregate performance is better than targets then Limb 3 will be a positive sum ('gainshare'), with the upside not expressly capped, but implicitly capped by the limits of potential performance.
- Critically, each NOP's gainshare or painshare is (normally) proportional to its Limb 2 in dollar terms, meaning that each NOP feels the same degree of gain or pain relative to their initial commercial expectations.
- If the incentive regime reasonably reflects the 'gain' or 'pain' suffered by the Owner (when actual outcomes diverge from target) than all Participants "win together or lose together" – win/lose outcomes cannot arise – so regardless of how difficult the circumstances, the Participants are united in their efforts to optimize outcomes.

The Limb 3 gainshare / painshare regime may include two components:

Component	Description
1. Cost	Comparing Actual Outturn Cost (AOC) to TOC and sharing under/overrun between Owner and the NOPs collectively (normally on a 50/50 basis)
2. Non-cost KPIs	Incentive payments determined by performance against agreed key performance indicator (KPI) targets within key result areas (KRAs), by applying agreed payment 'rates' for over/under-performance per KPI

These incentive components typically work independently but in parallel, although in some cases there is a degree of linkage to improve overall value to the Owner if performance is very strong – e.g. by diverting a portion of savings against TOC to increase the incentive for out-performing KPI targets.

Other underpinning principles for the compensation model include:

- Because all Participants "win together or lose together" under the 3-limb model, anything which is best-for-project is also best-for-Participants.
- Since Limb 3 is based on collective performance – regardless of which Participant(s) contributed to good or poor performance – there is no need for divisions or competing objectives between Participants.
- The overriding painshare cap provides mutual benefits as follows:
  - The worst possible outcome for a NOP is a negative Limb 3 payment which is equal and opposite to the Limb 2 Fee, leaving the NOP with a guarantee that – unless it commits a 'Wilful Default' – It will always recover costs incurred in continuing delivery (i.e. Limb 1);
  - NOPs are more likely to consider potentially high-value-adding innovations because their self-protecting risk-aversion is moderated by removal of extreme downside risk;
  - Even if the project gets into extreme difficulty, NOPs have no reason to withdraw resources and every reason to strive for better performance. Hence the downside cap – while protecting NOPs from worst-case financial outcomes – also protects the Owner from the extremely poor non-cost outcomes which eventuate all too often in distressed hard-dollar contracts.
- Payment claims (for actual Limb 1 costs plus associated Limb 2 mark-up) are paid "on account subject to audit" so that the NOPs are substantially cashflow-neutral. Typically there are no milestone-related payments or earned value assessments required for payment, which means that the requirement for (and costs associated with) security instruments or reliance on NOP balance sheet strength is significantly reduced under an alliance.
- The timing of payments of Limb 3 (including any interim payments) is normally left to the ALT to determine, noting that there is an obvious need to keep track of actual and forecast performance, and that Participants will prefer a smoother cashflow. If a painshare situation is anticipated, the ALT will typically withhold further payments of Limb 2 (to avoid 'clawback') and as a last resort the Owner may require additional security.

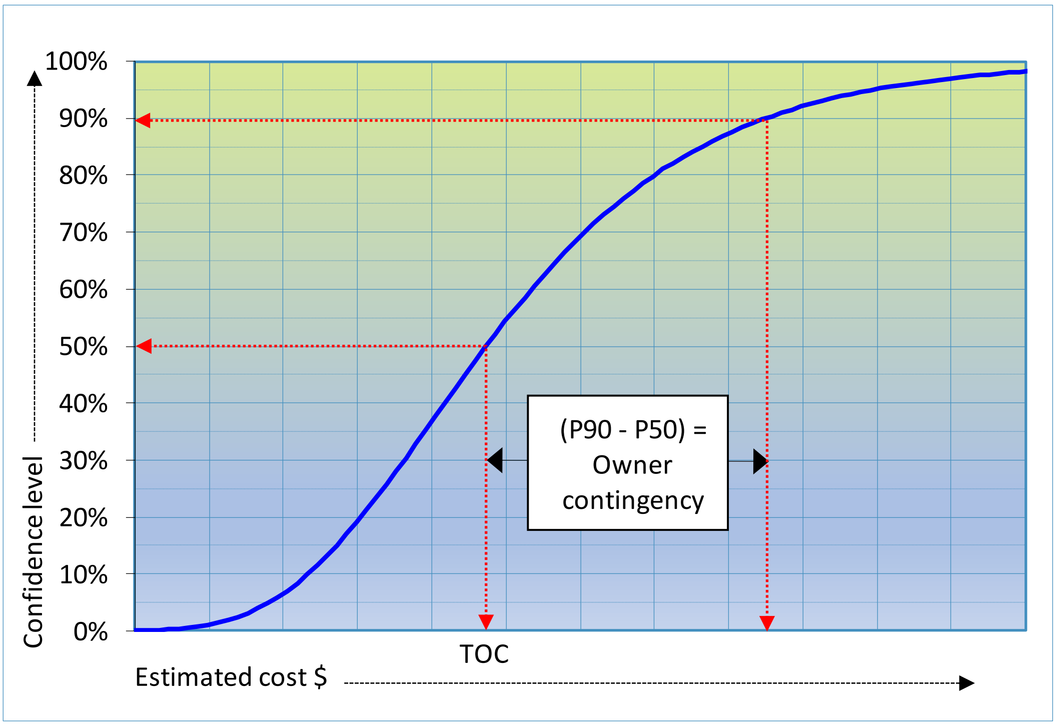
Appendix 2: Outline of ADP scope in a Single-TOC

The purpose of the ADP is for the Owner and the NOP(s) to work as an integrated team to do all the things necessary to develop, prepare and submit a Project Proposal that is capable of being accepted by the Owner because it maximizes value and sets up the alliance for successful project delivery. The Project Proposal will include a fully binding TOC and other performance targets. The typical scope of work during the ADP is as follows:

- mobilize and co-locate personnel to commence the development of an integrated alliance team;
- conduct workshops and other processes as necessary to develop an alliance charter and build a high-performance collaborative culture;
- establish a fully functioning ALT in accordance with the ADA and appoint the Alliance Project Manager and AMT;
- develop the high priority AMS policies, plans and procedures in accordance with the requirements set out in the draft PAA, including a Proposal Development Plan showing how the team will produce a Project Proposal that meets the requirements of the ADA and is capable of acceptance by the Owner;
- undertake various investigations, engineering, cost estimation and other planning activities;
- conduct value management, value engineering, innovation and constructability studies;
- develop a design for the Project in sufficient detail such that the level of uncertainty within the Target Cost Estimate (TCE) is within limits acceptable to all parties;
- perform risk assessments of the various design and construction options and prepare a risk register to inform the contingencies to be included in the TCE;
- develop Schedule 2 Project Description and Alliance Works..
- establish appropriate engagement with third parties in relation to the design;
- establish a detailed critical path schedule for the carrying out of the Alliance Works;
- identify and liaise with organizations (consultants, contractors, suppliers and others) who may be required to supplement the resources of the Participants to perform the Alliance Works;
- undertake preliminary construction activities, which may include Alliance Early Works;
- identify permits and other third-party approvals required for the Project and advance the process of obtaining these;
- secure commitments from insurers for wrap up liability, course of construction and professional liability insurance policies referred to in the draft PAA;
- develop and agree details of the various KPIs, including what will be measured, how it will be measured, performance target values and the rate at with gainshare or painshare will accrue if performance is above or below target;
- review the interim Adjustment Event Guidelines (AEGs) developed during the RFP phase and and align on a final set of AEGs that will form a schedule to the final PAA;
- develop documentation as deemed appropriate by the ALT in support of the Project Proposal; and
- undertake any other works related to the project as directed by the Owner-Representative or the ALT.

Key aspects of **TOC development** include the following.

- The TOC estimate must be based on execution strategies consistent with the achievement of KPI targets (i.e. must not include provisions for out-performance of these targets).
- The TOC estimate will typically include some elements that are best quantified via a Monte Carlo uncertainty analysis, resulting in a cost outturn probability distribution which reflects the level of uncertainty within the estimate, as illustrated below.



- One of the principles governing targets to be agreed during the ADA phase is the 'P50' principle – that there must be a 50/50 probability of out-performing or under-performing targets (at the time when they are established). This principle means that the 'target' for Limb 3 is zero, meaning that NOP Limb 2 represents a fair and reasonable reward for achieving target outcomes.
- Among other things this means that the TOC will not be the same as the Owner's internal budget – which may be set at (say) a P90 level. Differences between the TOC and the Owner's budget are required to allow for alliance cost overruns, and for risks which the Participants agree will be retained unilaterally by the Owner (see item 7 of **Appendix 3**).

The 'right' TOC: In a Single-TOC process the Owner does not have the benefits of direct price competition to satisfy its public sector stakeholders that the TOC represents value for money. Consequently, the 'right' TOC is defined as a TOC that is consistent with the P50 principle and supported by all the Alliance Participants as the 'right number' – i.e. a fair and reasonable target in the prevailing circumstances. If there is genuine alignment on the 'right number' for the TOC, then all Alliance Participants (particularly ALT members) will defend that number if questioned by various stakeholders- and if the actual outturn cost (AOC) is substantially lower or higher than the TOC – will respond with the same clear consistent and compelling explanation of why the TOC was ' right' at the time it was established.

- The Owner will engage a third-party Estimator (TPE) to help verify that the Project Proposal and TCE covers all required scope and is consistent with the requirements of the PAA. Whilst the TPE's duty of care is to the Owner, its brief will be designed to ensure that the TOC is properly constituted – to the benefit of all Participants – so their views and concerns will be shared with all Participants.
- Regardless of whether the Project Proposal and TOC is developed in a Competitive-TOC or Single-TOC process, the Owner will need to test assumptions and conduct due diligence on all aspects of the emerging Project Proposal. Ideally this work will be performed substantially as a collective alliance team, to minimise post-submission concerns. While the Owner is protecting its own interests through this process (and must form its own views) it is also in the NOPs' interests to quantify risks, maximize value, and ensure the Owner will accept the Proposal, so in this sense the parties' objectives are aligned.

Owners normally provide **ADP payments** to the NOPs in consideration for services provided under the ADA. Each NOP will be paid Limb 1 Reimbursable Costs incurred providing the services and associated Limb 2 fee mark-up on a monthly basis, up to a pre-agreed Maximum Development Payment amount. All payments made under this agreement will be included in the TOC for the PAA and in the actual outturn cost calculated under the PAA.

Typical features of an Alliance Development Agreement are shown below.

Area		Main ADA features
1	General obligations	As with any professional services agreement the NOPs are required to provide competent resources, exercise reasonable endeavours etc. and in the alliance context may be required to act in Good Faith (as defined). The NOPs collectively (per consortium) are obliged to provide the ADA services to the Owner and the Owner is obliged to pay for those services.
2	Payment to the NOPs	The NOPs will be paid on a pre-agreed basis, which can take several forms. Typically, Single-TOC ADAs allow for actual costs to be reimbursed (e.g. paying Limbs 1 and 2 under the 3-limb model if those details have been agreed prior to ADA execution) up to a pre-determined amount that the ALT has agreed with the Owner and that will reflect the services and/or scope anticipated to be carried out during the ADP.
3	Intellectual property rights	The Owner retains any intellectual property rights to material developed under the ADA and is free to use whatever it can from that work. However, it releases the NOP from any liability for their ADA product if the Owner does not proceed to execute the PAA.
4	Insurances	One of the key tasks during the ADA is to arrange appropriate insurances for the alliance which will be required promptly upon PAA execution. Until these insurances are in place the Participants normally rely on pre-existing insurances (as with traditional professional services agreements) to cover any liabilities arising out of work under the ADA. If alliance-specific insurance is necessary under the PAA this will typically require professional indemnity insurance to retrospectively cover ADA work.

Appendix 3: Features of a Project Alliance Agreement

	Area	Notable PAA features
1	Collective responsibility	The obligations to perform are generally collective on all Participants, not individual Participants. Risks and opportunities are shared amongst the Participants in pre-agreed proportions through the operation of the gainshare / painshare regime, not by assigning individual responsibilities and individual consequences (or individual legal liability in the event of a failure to perform). Each Participant is commercially exposed to the collective performance of all Participants (except in case of a Wilful Default as outlined below). For the NOPs this exposure is affected by the incentive regime which delivers proportional gainshare or painshare.
2	Good Faith	The PAA typically includes an express commitment to act in Good Faith and on a 'Best-for-Project' basis (as defined) including with mutual respect in relation to the rights of the other Participants, and in accordance with the agreed Alliance Principles.
3	ALT decision-making and Owner Reserved Powers	The PAA formally establishes the Alliance Leadership Team (ALT) – comprising one or more senior representatives from each Participant – and sets out its duties and responsibilities. All decisions of the ALT must be unanimous, except for certain decisions that are inherently Owner's decisions ('Owner Reserved Powers') – for example decisions on functional requirements, suspension of works, etc. Where those Reserved Powers are exercised the decision on any adjustment to TOC or other limb 3 targets rests with the ALT (sometimes subject to Owner endorsement) but not unilaterally with the Owner.
4	Dual role of Owner	In various parts of the PAA a distinction is made between the Owner in its role as Participant (for example bound by unanimous decision-making obligations) and the Owner in its role as client (for example able to exercise Owner Reserved Powers). This concept is further explained in **Appendix 4**.
5	Limitation of rights of action	The ALT deals with any differences that arise between the Participants (where these cannot be resolved at a lower level) and there is no right of arbitration or litigation between the Participants on any matter, except as noted below. Each Participant waives all rights of action against the others whether in contract, under indemnity, in tort including negligence, in equity, under any statute, or otherwise, arising out of any act or omission in connection with the PAA, except in the case of matters defined as 'Wilful Default' which typically include: • bankruptcy / insolvency etc.; • failure to pay moneys due to another Participant; • breach of certain specific warranties expressly provided in the PAA (not general warranties such as adequate skill etc.); • refusal to grant reasonable access to the Financial Auditor (FA), or fraudulent dealings with another Participant; • failure to take out or maintain a required insurance policy; • an intentional act or omission in breach of a material duty, obligation, condition, or stipulation arising out of the PAA, carried out with reckless disregard for the harmful consequences to another Participant, but

	Area	Notable PAA features
		excluding any error of judgement, mistake, act or omission, whether negligent or not, made in Good Faith. Importantly, a non-defaulting NOP is not liable for a Wilful Default committed by another NOP.
6	Payment to NOPs	The NOPs are paid on an open-book basis in accordance with the '3-limb' compensation model described in **Appendix 1**. The terms of compensation are detailed in a comprehensive schedule to the PAA, typically including detailed worked examples covering a range of potential scenarios, to ensure clarity. All financial transactions are subject to audit by the third-party Financial Auditor (FA).
7	Risk allocation and Adjustment Events (including scope changes)	Under an alliance there are only two options for risk allocation: • the risk / opportunity is shared by all Participants; or • the risk / opportunity is borne unilaterally by the Owner. An alliance aims to share almost all risks so that the Participants' instinctive response to unexpected circumstances is to optimize collective outcomes rather than protect their individual interests. However, each shared risk requires a contingency provision within the TOC, and it may be better for the Owner to bear some risks alone, for example high-consequence low-probability events which would inherently require a change in the Owner's budget or program. The PAA default position is that all risks and opportunities are shared unless they are 'Adjustment Events' (AEs) – regardless of whether they were (or reasonably could have been) foreseen or allowed for in the TOC. Where risks or opportunities eventuate – including circumstances which may require a change in scope or approach – there is no change to TOC or KPI targets (hence the risk / opportunity is shared) <u>unless</u> the ALT determines that an AE has occurred, in which case the relevant targets will be adjusted to neutralize commercial impact to the NOPs from that event. In determining potential AEs the ALT must act in accordance with the Adjustment Event Guidelines (AEGs). AEGs are developed via a careful process designed to achieve clear understanding of – and commitment to – sharing / allocation of risks, as follows. During the RFP phase, the Owner participates in a rigorous process (separately with each proponent team) to consider a very wide range of project-specific risks and opportunities, managed so as to reach informed alignment on the types of risk and opportunity that will be retained unilaterally by the Owner. The output from this process forms the interim AEGs attached as a schedule to the draft PAA. During the ADP, the Participants will review the interim AEGs and align on a final set of AEGs prior to locking in the TOC and this final AEGs will be attached as a schedule to the final PAA. The TOC must not contain provision for risks which are agreed to be borne by the Owner alone, and when reviewing the TOC the TPE verifies that this is the case.
8	Completion	The alliance is responsible for the delivery of the full scope of the project through to final completion, including a Defects Correction Period (DCP). In some projects there may be a requirement for progressive handover of the alliance works to the Owner, or for a commissioning process.

Area		Notable PAA features
9	Defective work	The Alliance Participants are collectively responsible for attending to any Defects that arise within the DCP following Substantial Completion – typically two years. The definition of Defects will exclude damage caused by other parties outside the control of the alliance after Substantial Completion (including the Owner in its capacity of asset owner / user). Costs incurred attending to Defects will be reimbursed in accordance with the 3-limb compensation model, so a reasonable allowance for such costs is required in the TOC (as it would in a fixed price estimate).
10	Suspension, termination and default	The Owner has the right to suspend and order recommencement of the alliance works by written notice to the NOPs. The Owner has the unilateral right to terminate the PAA for convenience, in which case it must pay the NOPs for all costs, accrued liabilities, and entitlements up to the date of termination, but not for any loss of prospective profits. NOPs can take comfort in the fact that (assuming the project is still required) the Owner will not terminate arbitrarily or without significant reasons to believe that the alliance is no longer the best way to deliver the project. The Owner has the right to exclude a NOP that commits a defined Event of Default (and fails to remedy it), although the Owner will generally require the consent of non-defaulting NOPs to do so. In most PAAs a NOP will have the right to withdraw where the Owner commits an Event of Default (and fails to remedy it), but NOPs do not have the right to withdraw for convenience.
11	Joint & several liability	NOPs are not required to be jointly and severally liable to the Owner under the PAA. For example if a NOP owes money to the Owner (e.g. under Limb 3) the other NOPs are not liable for that payment. However, the PAA makes all Participants (including the Owner) collectively responsible for performing the work under the alliance – in effect a joint obligation – and actions or failures by any Participant affect the compensation of all NOPs.
12	Resolution of disagreements	The ALT deals with any differences that arise between the Participants (other than a Wilful Default which is not remedied). Many PAAs are silent on how the ALT proceeds if it is unable to reach agreement on an issue – meaning that the ALT must find a resolution – but some PAAs contain processes for non-litigious resolution of ALT deadlocks.

Appendix 4: Further discussion of alliance structure and management

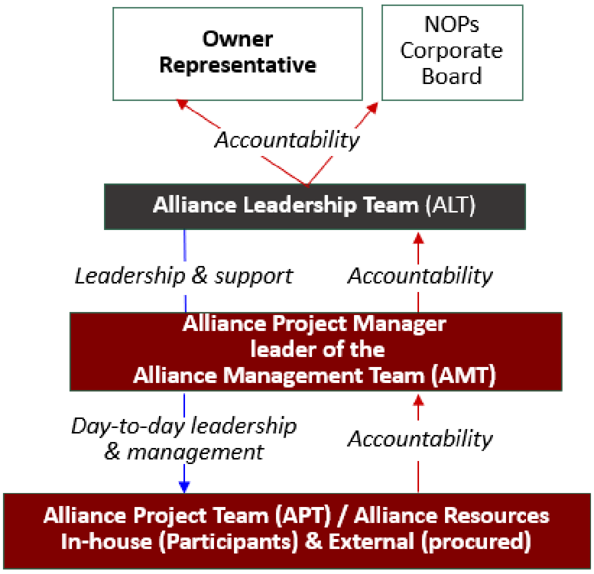
Overview of Alliance Governance

Under traditional forms of contract each party operates within its own leadership and management structure with various processes and protocols to enable communication and decision-making across contract interfaces. Invariably, and appropriately, this entails a significant amount of 'person-marking' where Owner representatives and corresponding contractor personnel 'mark' each other – to communicate their respective expectations, protect their own interests, and to ensure that the other party is fulfilling its obligations.

Under an alliance this type of 'person-marking' is redundant and counter-productive. In the delivery phase (under the PAA) the selfish commercial interests of each Participant will be best served by meeting or exceeding alliance performance targets. The alliance governance and organisational structure (illustrated in section 4) takes full advantage of this empowering context while providing both inspiring leadership and robust governance for the enterprise.

Alliance Leadership Team (ALT)

The ALT is typically accountable to the Owner's CEO (or their delegate) and to equivalent people in the NOP organisations, to ensure that the Participants fulfil their obligations under the PAA, satisfy their respective corporate requirements, and meet or exceed agreed alliance targets.



The ALT typically comprises two senior representatives from the Owner organization and one senior representative from each NOP. Consistent with the general alliance principle of "*a peer relationship where all participants have an equal say*" all decisions of the ALT within the scope of the alliance are required to be unanimous (except for 'Owner Reserved Powers').

The role of the ALT is to provide strategic direction, governance and oversight, and high-level leadership to the alliance. Its governance role is similar to a board of company directors in some respects. However, in the context of an alliance, it also provides direct effective leadership, and will take steps to create and sustain the kind of inspiring environment and culture whereby it becomes inevitable that the alliance achieves (or betters) all of its target objectives.

Key responsibilities and functions of the ALT include:

- Create an inspirational vision for the alliance;
- Establish and 'role-model' the Alliance Principles (often building on the Owner's initial draft principles) and set challenging objectives;
- Review, challenge and approve (or recommend for Owner approval) target cost and other performance targets;
- Endorse policies and delegations, and review / approve the Alliance Management System comprising policies, plans and procedures to effectively control all critical aspects of alliance operations;

- Appoint and empower the Alliance Project Manager and appoint or endorse the structure and appointments in the Alliance Management Team (AMT);
- Provide high level support including influence outside the alliance;
- Harness best resources from Participant organisations;
- Monitor actual and forecast alliance performance and take corrective action when appropriate;
- Confine and resolve inter-Participant conflict within the ALT.

Although the legal and commercial context of the ADP is very different to that under the PAA, the intention is that the ALT is formed early in the ADP to provide high-level leadership and governance under the ADA. The performance of the Participants during that period will determine, for better or worse, the 'DNA' of the alliance and the eventual outcomes achieved by the alliance.

To enable the ALT to function effectively the individual ALT members must possess appropriate attributes, including:

- Knowledge and experience in an enterprise governance role;
- Superior leadership skills – including an awareness of how their leadership style impacts those around them, an ability to challenge their own pre-conceived ideas, and a commitment to further develop their leadership capabilities through the alliance;
- Authority to make the necessary decisions, and willingness and skill to use that authority appropriately – specifically delegated authority to make ALT decisions (and the ability to secure decisions from their parent organisations for ALT matters that exceed delegated authority) – and ability to lead their organisation through the cultural change that is necessary to participate effectively in a successful alliance;
- A long-term perspective on the aspirations and strategies of their respective organisations;
- A high regard for the value of the relationships with other Participants – to ensure that they take proper account of the impact of ALT behaviour on broader interests of their respective organisations;
- Specific skills that will add value to the alliance, and a willingness to personally champion certain aspects of the alliance.

ALT members must also be available. The following table provides a rough guide to the inputs required from ALT members through a typical alliance life cycle.

Type of input	**Days per month in each phase**			
	Pre-alliance	ADA	PAA (pre- SC[3])	DCP
Development and understanding of proposed ADA / PAA	2 – 3			
Establish the alliance & leadership/team development	2 – 3	2 – 3	1	
Prepare for and participate in ALT meetings		2 – 3	1 – 2	0.25
Special meetings reviewing evolving Proposal and TOC		1		
Provide more direct high-level governance & support (being a champion, support on specific issues)		2 – 3	1 – 2	0.25
Typical days per month - total	4 - 6	7 – 10	3 – 5	0.5

[3] Substantial Completion

Alliance Project Manager and Alliance Management Team (AMT)

The Alliance Project Manager leads the AMT, which in turn leads, manages and coordinates day-to-day activities of the alliance.

The Alliance Project Manager reports to the ALT and usually attends ALT meetings, but is not a member of the ALT. Key duties of the Alliance Project Manager (supported by the AMT) include:

- Be accountable to the ALT for ensuring that the alliance meets or exceeds all agreed objectives while operating within the policies and delegations set by the ALT;
- Appoint and empower the wider alliance team (subject to ALT delegation / approval);
- Provide day-to-day management and leadership of the wider alliance team, ensuring duties and accountabilities of each team member are clear (including Participant-employed resources and subcontract resources);
- Monitor actual and forecast performance of the alliance and take corrective action when appropriate, reporting to the ALT as required.

While the Alliance Project Manager is authorized to make decisions within their delegated authority without unanimous support of the AMT, they normally have the kind of leadership skills and empowering management style that ensures full AMT support.

Typically, each alliance Participant is represented on the AMT, but that is not essential and does not take precedence over the principle that each role will be appointed on a 'best candidate' basis. In most cases AMT members are dedicated full time to the alliance, but depending on the role this is not obligatory.

Alliance Management System (AMS)

One of the first priorities of any alliance is to develop and document its policies, procedures and management systems into a comprehensive Alliance Management System (AMS) for review and endorsement by the ALT. Much of the AMS will be drafted during the ADA phase for a Single-TOC process, but a Competitive-TOC process tends to leave some AMS development and approval until after execution of the PAA. The AMS is developed by the AMT under the guidance of the ALT, normally drawing heavily on pre-existing procedures and policies from the Participant organisations.

Among other things the AMS will specify:

- Delegations of financial and general authority and protocols for review and update of delegations;
- Aspects of the AMS that can be amended with the approval of the Alliance Project Manager and aspects that require ALT approval.

The AMS must satisfy the corporate requirements of all Participants, not just the Owner. A well-structured AMS is critical for effective governance, leadership and operations of the alliance and the ALT will normally undertake a robust review of its various management plans and procedures before approval. Typically, individual ALT members review selected AMS elements in their areas of competence, to ensure that the various AMS plans and procedures give the required assurance required by their organization.

In a high-performing alliance the AMS meets a tougher test than merely satisfying the Owner's assurance requirement. In this respect:

5.3 A good AMS is robust, efficient and effective, providing the right information at the right time in a user-friendly form.

- Formal ALT reports will enable the ALT to fulfil its alliance-facing leadership and governance functions and simultaneously enable ALT members to satisfy their individual (outward-facing) corporate responsibilities and provide their parent organisations with assurance that risk and opportunity is being managed effectively.
- Most alliances generate a monthly ALT report which is a comprehensive 'single source of truth', providing all the information required to satisfy each Participant's corporate requirements, including current and forecast performance and associated commercial projections.

Independent monitoring and auditing

In a high performing alliance with a well-functioning AMS there is no intrinsic need for the Owner (or any Participant) to set up a separate audit or performance monitoring function outside the alliance – although there may be statutory or similar Owner-side requirements for specific independent review processes. However, an effective alliance QA function will incorporate appropriate levels of objectivity (including independent verification where required) such that each Participant can rely on the alliance reports. If a Participant feels the need for its own audit and verification function, this indicates failure at the governance level to secure sufficient visibility and confidence through the AMS, weakening the 'one-team' culture that is critical to high performance.

There are some assurance functions that necessarily reside outside the alliance – specifically the third-party Financial Auditor (FA) and third-party Estimator (TPE). These roles are engaged by the Owner, and while they communicate openly with all Participants, they are primarily designed to provide assurance to the Owner as follows:

- The FA is engaged to audit open-book operation and ensure that payments (Reimbursable Costs in particular) are in accordance with the PAA;
- The TPE is engaged to ensure that the TOC and other estimates are soundly constructed, cover all anticipated scope, and represent value for taxpayers. Under a Competitive-TOC process there is a risk that a TOC is lower than the P50 level, which could inappropriately influence the choice of preferred proponent and expose the Owner to unnecessary risks. Conversely, under a single-TOC process, the TOC may risk being higher than the P50 level, resulting in unearned gainshare. These risks can be mitigated through the TPE's review of the TOC. The TPE may also advise on the valuation of any Adjustment Events.