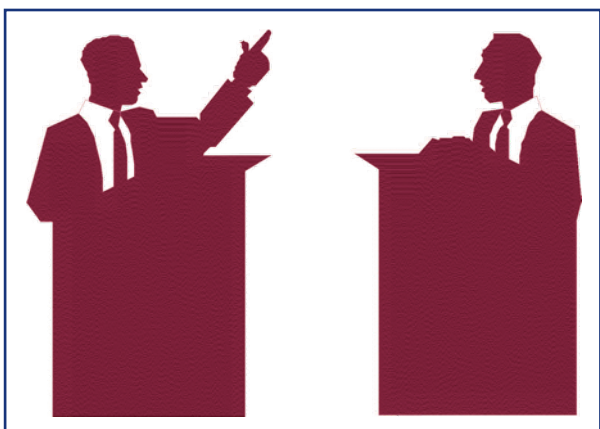


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For Practitioners, Policy Makers and Planners in Public Infrastructure



## The Right Debate

“On time and on budget!” Great, but what did you DO? And was it what you said you would? Is it what we want?

These questions go to the core of NON-financial asset management performance reporting. It is this reporting, according to the New Zealand Auditor-General, Kevin Brady, that after 15 years of experience, we have yet to get right and in the section ‘The Right Debate’ in his review of council performance in the 2006-16 Long Term Council Community Plans, he gives examples. (see p.\*)

The Auditor-General is speaking of non-financial performance in general but it applies very much to asset management performance.

For ‘right’ read ‘can be understood by the intelligent lay person who is prepared to inform himself a little and apply effort’, and ‘accountable’ meaning that if the performance is not going in the direction intended, this can not only be recognised but corrected.

This requires commitment across the board - operators, top management, elected members. In this issue I look at why prescriptive regulation is unlikely to get us there.

Enjoy - debate!

Penny

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## Editorial: The Right Debate

In the last issue I argued that long run goals are necessary for setting direction but they don't work so well for motivating current action. I also argued that it was not sufficient to simply quote the numerous benefits that good asset management brings - more efficient resource usage, knowing where to get the most bang for the buck, no surprises, etc. - these had to be *illustrated*. We had to make the claims come alive, be meaningful for people. When I read Kevin Brady's speech, referred to on page 1, I began to understand why we all find this so difficult. It is the poor quality of non-financial performance information.

Whether we are trying to see whether outsourcing has brought us the benefits claimed, or whether external events - floods or drought, for example - are sufficient to account for the fact that what we thought we were going to get, we didn't, the source of the problem is the same. We have no clear statements of future performance intent framed in a way that we can track whether the intent was achieved. And we don't have good tracking information.

This not only means that outsiders cannot judge performance - insiders can't either! As the Auditor-General says, we would look askance at any business that said it did not use its financial performance to improve, but the non-financial performance equivalent for non-commercial government organisations is not being used to improve management; it is so poor it cannot be.

Can we impose good non-performance information by regulation? Here is what the AG has to say

“For financial statements, their structure, composition, measurement, and disclosure are heavily prescribed by financial reporting standards. There are no such standards for non-financial performance statements, which need to be customised to reflect the nature of the reporting entity. Therefore judgements need to be made about which outcomes and outputs are most relevant and significant for the purpose of external reporting. It is these judgements that seem to create many of the issues and problems – both for preparers and users.”

Kevin Brady's speech can be accessed at the Audit NZ website. It is worth reading, particularly for those of you who are involved in your professional associations and have a say in developing national policy. <http://www.oag.govt.nz/2008/speeches/forecasting-and-reporting-performance/?searchterm=accountability>



## To Regulate or Not to Regulate

In the light of the NZ Auditor-General's comments it is good to see that the IPWEA, who have just released a draft policy statement for comment, have stayed away from suggesting prescriptive legislation.

Nevertheless, in the ensuing discussion on the IPWEA's Asset Mates website, a number of the comments were inclined to stronger regulation.

Why?

### One argument runs like this.

**Premise 1. Long run infrastructure sustainability is a good thing.** Without this focus our children and grandchildren are either left to pick up the costs for what we have enjoyed during our lifetimes, or else they are forced to endure the lower services and life styles that come with a poorly maintained, degraded, asset stock.

**Premise 2. Elected Members are not focussed on future communities;** their focus is the needs and wishes of the current community whose votes put them into office and can either keep them there or toss them out. Long run sustainability provides benefits to future communities and future administrations - but at the expense of current communities and *their* administrations.

**Conclusion 1:** It's a no-brainer, Elected Members will choose to focus on short run goals unless forced to do otherwise,

**Conclusion 2:** The only way to get a long run focus is to this is to mandate/ regulate/ legislate good long run practices and introduce national, even global standards.

Now I am prepared to concede Premise 1. I am also prepared to concede Premise 2.

But I have trouble with both of the conclusions. I do not believe that they really follow so inexorably from the premises.

**On Conclusion 1** I will grant that elected members have a natural pre-disposition to consider shorter run goals and objectives, but encouragement of many kinds, and greater understanding may be more effective.

**Conclusion 2** is an example of the 'this or that' thinking so common today that I find quite objectionable, namely the assumption that there are only ever two approaches - total freedom or complete control. Or in Bush's words on Iraq "You are either for us or against us". This is nonsense. The world is not and never has been so black and white.

And in a world where grey, not to mention the entire colour spectrum rules, there are many options. As asset managers we should have the imagination and ability to seek out these many options and weigh up the benefits and costs.



### Another argument for Mandating

There is also another strand to the argument for mandating. It runs like this:

The people who turn up for asset management training are always the implementers and not the managers. We need the managers to know what we are doing so that we can get clear directions and guidance from them.

We, the implementers, don't need or want mandated practices because we know that they will be just more checkboxes to be filled in mindlessly. But perhaps some legislation to make the managers take asset management seriously would be a good thing?

(Of course, an alternative explanation for why senior managers don't turn up is that the courses on offer are designed for implementers and not for managers. In the very early days of asset management - about 20 years ago - I can remember sending my young assistant to a course on 'asset management'. She reported back that they spent over an hour explaining where to stick barcodes on telephones so that they could not be idly picked off by bored public servants during long conversations! I am not kidding. And while I am not suggesting for a moment that this is the current focus, the point is that there are different levels of interest and we should respect that in terms of different levels of instruction for different groups.)

### The Common Element and Assumptions of both Arguments

The common element in both of the above strands, is that we operational asset managers don't want/ need to be regulated but that **regulation is needed for others** - the managers and for elected members who won't take asset management seriously without it.

Both strands implicitly assume

1. That there are no other options or not such good options, and
2. That mandating /regulation actually works.

This raises a number of questions.

Regulating what?

Does Regulating work?

What are the costs of Regulating?

Are there alternatives?

What criteria should we use to evaluate the benefits/costs of all alternatives?

### Regulating What - Practices?

We can't get very far into a discussion of mandating or regulating before we begin to notice that just about everybody spoken to has a slightly different idea of what is involved.

Some have suggested that we should standardise (ie regulate) our practices, perhaps on a national, even a global basis. But we maintain, operate and renew our assets in order to meet the service level requirements of our community. That is why



local government exist - to give the local community a voice. *Standardisation would negate the whole rationale for the existence of local government.*

### **Regulating Outcomes?**

OK, if not our practices, what about our outcomes? Can we regulate outcomes?

This is what is proposed in the IPWEA policy statement, that we regulate broad *performance* outcomes - such as accountability, transparency, long term sustainability - but without prescribing the methods by which such outcomes are to be achieved. In this way, the policy avoids the danger of freezing best practice at the current moment. Councils are free to continue to innovate and improve their asset management practices.

There is, however, the problem of how outcomes are to be audited. If the auditors develop a set of practice 'checklists', as they have done in NZ to audit the Long Term Council Community Plans, then no matter how good the checklists are, this is really introducing practice regulation 'in through the back door', as it will not take very long for councils to realise that they can improve their audit 'score' by adhering to standard practices.

If outcomes are to be audited free of the checklist approach, then they need to be stated in a clear form that enables tracking and good quality non-financial performance information needs to be available to do the tracking. That takes us back to the AG's issue.

### **What are the costs of prescriptive regulation?**

The costs are not only the resource and dollar costs of compliance and the lost opportunity to do other things. It is something worse! It takes the fun out of asset management. Mary Bourke, the Mayor of South Taranaki District in New Zealand expresses it this way. It turns an 'adventure' into an 'obligation'. That means it takes the fun out and puts the stress in. (Not a good prescription for attracting new staff!)

### **Does Regulation work?**

Depends what you want to do. If you want to improve the quality of the produced asset management plans, then, yes, it probably does work.

If you want to use the plans to improve asset management - then the answer is it probably does not.

Here again, it is worth turning to the Audit work in New Zealand. After about ten years of broad outcome regulation but no prescription as to practice - much along the lines of the IPWEA proposal - they moved to a more formal, complex, regulated environment with the 2002 Local Government Act. There is the possibility that this can have the effect of dragging up the bottom of the rungs to the level of regulated good practice, maybe. On the other hand, there are the possible problems I have listed above.

What did the Auditor General find when he reviewed the performance of the Long Term Council Community Plans recently? This is what we turn to next.

New Zealand is a leader in asset management and the observations below are of a mature asset management economy - they are thus more demanding than those new to the field may wish to apply. Nevertheless, I find the observations interesting in the light of the question we are asking ourselves here - does mandating asset management practices lead to greater commitment and better outcomes?



## The Right Debate

### The early years of Asset Management - till 2002

Between about 1993 and 2002, New Zealand Councils were required to prepare ten year forward cash flow statements. It was recognised that in order to do this ten year asset management plans would be necessary but they were neither mandated nor prescribed.

As a result the early Asset Management Plans were of extremely variable quality, but the Audit Offices' approach of 'letting a thousand blossoms bloom' yielded a number of dividends. Councils were challenged to determine for themselves what constituted a good asset management plan. This generated a great deal of enthusiasm amongst the better councils who were keen to learn from each other. The middle rung were brought up the learning curve by the work done by the better ones, and the bottom rung? Well, as an auditor said at the time 'there will always be the basket cases'. Overall, however, NZ learnt quickly and interest was high.

### Since 2002, LTCCPs

With the new Local Government Act 2002, this rather laissez-faire approach changed. councils are now required to prepare Long-Term Council Community Plans (LTCCPs) under the Act, and requirements for these LTCCPs are detailed and quite complex.

The emphasis on long-term planning in the Act reflected the concern of the Parliament and the Public that there should be an accountability framework *for sustainable long-term service delivery, informed by an understanding of community needs and views.*

### Does Prescription work better than the Laissez Faire Approach?

According to the Auditor General "While other countries have adopted long-term planning requirements for local government, auditing the reasonableness of the LTCCP and issuing an audit opinion is unique to New Zealand". In his recent review of the performance of the LTCCPs, the Auditor General does not address this comparison question directly (It would almost surely be ultra vires his mandate!) but his observations are useful, and particularly his concern with "the Right Debate".

### What did Audit find?

The results show an improvement in the quality of asset management planning



Progress is being made but there is ‘a long way to go before the LTCCPs become strategic and user centric planning documents that are a strong expression of the purpose of local government.’

“A particular concern was that many LTCCP Statements of Proposal did not appear to encapsulate the “right debate” - they did not focus on the crucial issue facing each local authority and how the authority was addressing these issues”

Because of the amount of required information the LTCCPs are large and complex. It was the intention of Audit that they would validate the detail providing the assurance to allow councils to use the summary document for general consultation.

But the Summaries were not being used in this way. Audit found that many of the Summaries were prepared late, ‘almost as an afterthought’ and ‘without a focus on the important issues that needed to be addressed - a consequence of not having identified the ‘right debate’ in the first instance.

### Compliance rules

The Expert Reviewers reported to Audit that “councils focused on complying with the requirements of the Act, and have improved the quality of the underlying information to ensure that they meet audit expectations, but are still at an early state in effectively using the integrated information to enhance their own decision-making processes and the quality of the planning process for all stakeholders.”

The Auditors noticed that while most local authorities were well into updating their asset management plans since the previous review “many had not prepared much of the underlying information on which future planning for asset management is based. This included not identifying and reviewing their relevant policy and strategic objectives, and not reviewing current and intended levels of service.”

This may be simply a feature of time constraints as the LTCCP requirements are quite extensive. But it is symptomatic of authorities completing the LTCCPs *as an audit requirement* rather than engaging wholeheartedly in them for their value in helping to manage the LR sustainability of their councils. The following comment is also in the same mould.

“During this work, my auditors frequently observed that changes to capital expenditure budgets did not result in changes to forecast levels of service, suggesting weak relationships between financial and service performance forecasts for infrastructure assets ... Many local authorities were therefore preparing asset management forecasts without having formed deliberate objectives in terms of the nature and condition of assets required

### Overall

Audit found that improvements had been made in the development of performance frameworks but it was still the area where greatest deficiencies lay.



Local authorities, it was observed, were more experienced at assembling financial statements than other sets of LTCCP information (presumably including life cycle cost information as well as the above mentioned service objectives.)

### **And of value to all councils (and other organisations) within New Zealand and beyond these shores**

- Local authorities should explain the financial prudence of its annual forecast surplus or deficit position in the light of its future service intentions and the funding of these.
- Long-term management of local authority finances remains a crucial issue.
- Financial forecasts in the later years of the 2006- 16 LTCCP show similar weaknesses to the 2004 -14 LTCCPs. Investment and cash balances significantly increase in later years, while capital expenditure substantially reduces. This suggests that capital expenditure forecasts may not be complete, and that local authorities need to reconsider whether their current approaches to capital planning remain appropriate.

(Australians 'of a certain age' may recall the former Prime Minister Keating's "J" Curve which always showed things getting worse in the immediate term but then miraculously improving after that. This is a common pattern with just about every long term plan that I have seen. On paper, the future is always rosy.)

Reference: "Matters arising from the 2006-16 Long-Term Council Community Plans" Report of the Controller and Auditor-General. <http://www.oag.govt.nz/local-govt/ltccp/>

This report of the Controller and Auditor- General may also be of interest "Turning principles into action: A guide for local authorities on decision-making and consultation" <http://www.oag.govt.nz/2007/decision-making/>

### **Re-View**

Sorry, Folks, I know a number of you are enjoying these articles but we will need to defer them for a few issues. However they *will* be back! And, in the meantime, please take advantage of some shorter "Re-View" type articles that I have now placed on the website - see 'Oldies but Goodies' at [www.amqi.com](http://www.amqi.com)

### **Next Issue: New Zealand Experience**

This coming week I will be in New Zealand. How do local government asset managers there see the new requirements? Where do they find them helpful, where do they find them burdensome? Overall, have they found them useful in winning the hearts and minds - and commitment to long run sustainability - of senior management and elected members?

We will also be reporting on other current New Zealand issues.