



AMQ International's **STRATEGIC**
ASSET MANAGEMENT

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“AM is a Strange Business”

Out title story this week, **AM is a strange business**, p. 2. is, like those famous ‘IgNobel Prize’ entries which ‘first makes you laugh and then makes you think!’ It comes from Ype Wijnia and Joost Warners. The authors point out that what used to work in times of stability is unlikely to serve us well in times of change. This cannot be repeated enough for we are all creatures of habit and prefer the known to the unknown.

This leads on to a short introduction to the notion that Strategic Asset Management is not about ‘what to do’, but rather about ‘what to change’. See ‘What change do I need to make’ p. 3 and two more short pieces “Do we really want a common understanding of asset management?” p. 5 and “Who do we serve?” p. 6

By now many of you will have heard of the sad story of Mangawhai, how a small council got out of its depth in organising a PPP for a waste water treatment plant, how multiple safeguards failed, and how a tiny farming community of under 2,000 got landed with a debt of over \$63 million. In “Lessons from Mangawhai” p. 7 I look at some of the lessons that I took from this story. Maybe you will have seen others? Please share them and I will print them in the next issue. Better that we learn from the mistakes of others, than in making our own.

Finally I look at the role that Picasso played in Asset Management in Victoria, in **Picasso**, p.10

As always, please enjoy! Asset Management may not be easy - but it should be fun!
Penny

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Asset management is a strange business

YPE WIJNIA & JOOST WARNERS, Essent Netwerk

A typical Asset manager works with an asset base that is very old. For example, at Essent Netwerk, a large Dutch distribution company for electricity and gas, the oldest assets in operation are about 100 years old, and the average age of the assets is about 30 years. Each year about 3% of the asset base is either built or replaced. Typical maintenance cycles have a period of about 10 years. So, about 13% of the asset base is touched on a yearly basis.

This means our basic job is more like staying clear of the assets and let them perform their function than it is like actively doing something with them, as the term Asset Management suggests. Therefore it might be wiser to call ourselves asset non-managers.

The strangeness of Asset Management increases further if you look at the portfolio of asset and network policies. From long experience with managing assets, most policies have reached a high level of sophistication and they address not only the general situation but all kinds of possible exceptions which have been encountered over the period since the policy was put in place. Those exceptions have exceptions of their own, requiring further detailing of the policy.

In the life cycle of a policy attention therefore drifts from the original problem to managing exceptions. This means that as the sophistication of the policy grows, the knowledge about why the policy was developed in the first place diminishes.

Exaggerating a little bit you could say that Asset Managers do not manage most of the assets, and in case they do, they haven't got a clue why they are doing what they are doing. You would expect a system that is managed this way to collapse very soon, but somehow it does not, as the electricity grid in Europe has a reliability of about 99.99%.

However, this way of managing assets can only work in a stable environment with stable or at least predictable requirements for the assets. Unfortunately, the world we live in is nothing like stable.

For example, the liberalization of the electricity markets has resulted in an income cut of 50% for the grid companies in the UK in the period 1995-2001. Internally, issues like the retirement problem (due to age profile of staff about 50% will retire in the coming 10 years) or the asset replacement problem (due to age profile of assets) will require policies that solve other problems to sustain the operation of the network at its current performance. On the outside, issues like globalization, terrorism, global warming and oil depletion, most likely will set new requirements for the grids, again requiring policies to solve other problems. This change of needs may happen very fast.

The current policy adaptation cycle is by no means fast enough to follow those changing needs. How can asset managers overcome this problem? You can read the author's then solution to this problem in "Portfolio Management" pts 1-3 in SAM Issues 181, 182 and 183 available in the Archives. They have almost certainly moved on since then, but it indicates the way they think.

For Strategic Asset Managers the question is: **What do I need to Change?**

The challenge

It is the rare manager who is required, or has the opportunity, to be in strategic asset management mode all the time.

Instead, most have active operational or maintenance tasks and these occupy the greatest part of the day. Here the question is “*What do I DO?*” The tasks facing you are generally more than you can handle and the first task is prioritisation. In this situation you probably win no brownie points for taking time out to evaluate whether any particular task should be done at all, or what direction asset management should be taking.

‘Strategic’ asset management has generally to be fitted in around the edges, whenever there is time for it. Recently I had a conversation with a New Zealand asset manager who said that he never has as much time as he would like to spend on strategic asset management and he likes to read ‘*Strategic Asset Management*’ to make sure that he can get the maximum value out of the time he does have.

With that asset manager in mind, and the many others like him, let me suggest to you that the question you ask when you have the opportunity to be in ‘strategic mode’ is qualitatively different. The question is “*What do I need to CHANGE?*”

How can you figure this out?

Well, one way is to listen to the complaints that you hear around you, not only from your fellow asset specialists, but also from finance, from client services, from the customers themselves.

I have been asking asset managers that I meet

‘ If you had free reign to do anything at all, what is the first thing that you would do to improve asset management in your organisation?’

So far, no-one has had any difficulty in coming up with an immediate, thoughtful, and heart felt answer to that question. Try it for yourself! Here are a couple of the answers.

John Hardwick, Chairman, Asset Management Council, said that there are three major components to any business: people, processes and assets. He believed that we now had a good handle on the technical issues related to assets, and I agree with him. The challenge now was with people and processes.

(On this point, you might like to read “Living Asset Management” by JR Lafraia and J Hardwick, in which the authors take up the challenge of leadership and culture - the people and process side of the Asset Management equation)

David Daines, BHP, and Nicholas Philips, Yarra Trams, both said that their first call would be co-ordinated responses to the works management problems they faced, as they noted the tendency for different parts of the supply chain to march to their own tune (or, more accurately, to aim at their own local optima as set out by the KPIs by which they were being measured) rather than the organisational global optima.

What is your ‘first call’?

Now the question is ‘WHY? Why is change needed?’

For it to be successful, for example, might other things need to be done first? Does what you want to achieve require an attitude change? How might that be achieved? Don’t ignore this Why question. It will save you much wasted effort and misery down the track.

At first sight, it might seem as if the answer to all three responses to the “What would be the first thing I would do, if I could” type question above, is the same, namely

A Common Understanding of Asset Management

However, is this really the answer (or just the first idea that comes to mind)?

This is where we need to make a distinction between identifying the needed change and deciding what solution to adopt. This is because, every action you take has ramifications - on the asset management team or on other sections of the organisation, the customers or the community. If you fail to take these into account when deciding on your preferred course of action, you usually live to regret it.

Take the idea of a ‘common understanding of asset management’. Wherever asset managers gather this idea will surface. Probe a little, however, and you will discover, it is not just ANY common understanding, but rather THEIR understanding.

Everybody wants others to hold to their view of asset management! (Yes, I am just as guilty as anyone else here.)

Consider: Just last week, I spoke to a couple of chartered accountants who, over 25 years ago, were some of the first professionals to be offering services in asset management. What did they mean by AM? Then, they saw AM as the recording of

the value and location of assets for the balance sheet - and they still do! Others I have spoken to, see asset management as project management, some as asset construction, still others as maintenance and sometimes operations.

I have just had interesting email exchange with a fellow who was greatly irritated by what he called the 'hi-jacking' of the term 'asset management' by PAS 55 and now ISO 55000 to focus on service. He argued that although asset management was important to business it needed to be 'kept in its place' and that place, he saw, as being the development of asset management plans to attend to asset renewal.

Do you wish any of these interpretations to be the 'one' common understanding? Perhaps not.

A Common Goal

Maybe a 'common understanding of asset management' is not as important to success as having a 'common goal'?

Even if some think first of asset recording, others of operations and maintenance, still others of design, construction or project management, if all have a common idea of the goal to be achieved, we have a strong chance of getting there.

Indeed, a far stronger chance because of the multiplicity of different options that these viewpoints permit.

For all you Australian 'roadies' out there!

There's only so many jobs in building roads

MUNGO MACCALLUM, THE DRUM 17 February 2014

"He had always said that he wanted to be known as the Infrastructure Prime Minister, but now he told us just what he actually meant by [infrastructure in the 21st century: roads](#). Not a global information network or national broadband, not the airwaves, not even ports, harbours, railways and air terminals, but roads. Roads, those things cars run on, the cars that won't be made in Australia anymore. Roads, that were last at the cutting edge of innovation about 2,000 years ago when the ancient Roman Emperors were planning their future economies."



Who do we serve?

At first sight this may seem a strange question. But it is, in fact, critical to our success as asset managers. If 'assets exist to serve a purpose', then surely *asset management must also exist to serve a purpose. What purpose (or purposes)?* The only way to answer this question is to consider all the different roles that asset management supports.

Here I have suggested some of the services we provide, if we do our job well. I don't imagine I have captured them all, but next time you feel you need to defend your role as an asset management (to others, or even to yourself) think of this list!

Our organisations -

The board, the councillors and decision maker - *(provides information to support organisational objectives, advises on the consequences of different options, and generally provides reassurance that the organisation is on the right track.)*

The shareholders - *(keeps costs down, performance up, protects the reputation of the organisation by avoiding major breakdowns and disruptions, and thus protects the share price)*

The CEO and CFO - *(provides information on directions, capital, operations and maintenance costs, consequences, sustainability and flow on requirements from new assets to other services and training required in the organisation)*

Colleagues in maintenance and operations - *(Asset management decision making aids in maintenance timings, reduces down time for operations)*

Colleagues in finance and accounting - *(provides assessment on the level to which the asset is written down, advise on the appropriate values to assign, bearing in mind current replacement costs, modern engineering equivalent of assets, etc.)*

Colleagues in client or customer services - *(help them to maximise the capacity of existing assets and to choose the most appropriate, and affordable, modifications or new capacity)*

Also to the regulators, auditors and others who have a role to see that the organisation is performing well

Asset managers have a key role in demonstrating need, helping the regulators to understand what is involved in complying with regulatory requests and the costs involved, help them to find other ways to meet the regulatory standards which are not so cost onerous, and to act for the organisation when necessary in information exchanges with auditors,

as well as customers and clients and the media and the wider community.

Did you realise that you did so much - or could do so much? How much more value could you add to your organisation be doing more of the above?





How an idyllic spot got itself into a spot of bother

LESSONS FROM MANGAWHAI

The story in brief

Mangawhai is a small harbour on the east coast of Kaipara district, south of Whangarei. It has a small community of permanent residents. However, because it is a popular holiday destination, its population grows significantly during the summer. Because of concerns that leaking septic tanks were polluting the bay and recognition that the newer smaller blocks planned by developers would not support septic waste treatment in any case, the Waipara District Council decided to install a waste water treatment plant and to do this by way of a PPP. It was poorly managed, record keeping was abysmal and the small Mangawhai community of less than 2000 ended up with a debt for the treatment plant of \$63 million (The original cost estimate put to the community was \$10.8 M). The council has since been replaced by commissioners. A full report (470 pages) as well as a summary report (47 pages) are available from the NZ Auditor General's website.

What went wrong?

Many things, including poor auditing by the Auditor General's in-house audit team. The point of this story, however, is not to lay blame - that would be pointless - it is to see what we can learn.

Did they get the problem correct?

High levels of enterococci in the bay were thought to be the result of leakages from septic tanks. Some commentators pointed to other possible sources and the impact on water quality in the bay will not be known for some time. Nevertheless, after considering all the evidence the Auditor-General's report concluded that they made the right decision to build a wastewater treatment plant.

Better communication of the research, and the decision making process, may have helped to alleviate some of the subsequent criticisms. "In our experience, accusations of wrongdoing flourish when there is a lack of information about what actually happened." AG's report.

Growth and Development

Like many coastal councils, what started off as largely unregulated holiday shacks with temporary tenants not demanding the amenities of town, started to change as more people took up permanent residence. Sewage treatment was initially by septic tank which the large 1200 to 1600 hectare block size comfortably accommodated. However, the council believed that there was the opportunity for large scale growth and development with denser, 400 hectare blocks that would not suit septic tanks, and so they decided they needed a sewage treatment plant to cater not only for the existing population but for a tripling of the size. They borrowed to fund this and in the event, the expected (hoped for?) growth did not take place. Mangawhai is an attractive coastal town and could attract development, but so is just about every town in New Zealand.

So the question which needs answering - not just for Mangawhai but for all councils - is 'Are your growth expectations realistic - and where is the evidence to support them?'

The PPP Decision

The council decided that it could not fund a treatment plant and decided to use a PPP. This was dangerous because such financing vehicles are very complex and the council was too small to have the specialist staff able to manage it. An even more critical factor is that, along the way, it seems that the idea to take the plant 'off budget' took on a life of its own. Now the purpose of a council is to 'provide community service', it is not to 'take expenditures off budget'. Any PPP, or any financing vehicle, even one as simple as borrowing, should only be taken up if - and only if - it can be demonstrated to be the best way to provide community service.

Ultimately, as has been well proven in this case, the idea that somehow the private sector will 'fund' (i.e. pay for) public infrastructure is as crazy as an adult believing in Father Christmas. There is only one ultimate source of funding or payment and that is the community - no matter how complicated or 'clever' the intermediate financing methods. It is surprising to find how many still believe the contrary!

Project Management

The Mangawhai project is, of course, far from being the only case of poor project management - indeed it seems very difficult to find models of good project management, however, the decision to sign off on the PPP contract before they had identified a disposal site for the effluent. The costs for disposal were estimated in the contract signed in 2005 as being \$361,000, but ended up costing an estimated \$14 million involving the purchase of a farm some 11 kilometres away. Moreover, whilst the treatment station itself is capable of considerable extension, the disposal site does not, so the potential capacity of the treatment station cannot be taken advantage of without considerably more cost.

Staff in small councils can be reluctant to admit that they do not have the same range of expertise as those in larger councils and this becomes a source of weakness that others can exploit. The NZ Auditor General's office has now put out a set of guidance instructions for councils and others seeking to make use of PPPs, but it would be helpful if more training courses included practical instruction in matters of funding and such training courses were applied more widely.

Although it seems the private company engaged to build the treatment station was not held to account for allowing the sign off before the disposal site had been identified, perhaps they should have been? It might be time that more conditions were put on PPPs for public infrastructure to be 'in the public interest'.

Failure of Auditors

When auditors fail to identify problems, things can go very wrong (HIH, Enron). In the case of the Mangawhai Wastewater Plant, it seems that the auditors relied too much on the assurances of the executive and did not confirm by independent examination.

This is not good enough, but before you lay all the blame on the auditors, consider....

How many of you regard an identification of error by the Auditor as a blessed relief, something to keep you from greater trouble? I suspect few! How many of you are like the Waipara District Council staff and deliberately blindside your auditors? Do you believe that a problem is only a problem when you are caught out by the auditor? Do you play games with your auditor seeing 'how much you can get away with?'

Good organisations take audit seriously, carry out their own internal audits, and continuously check their practices with audit opinion.

Poor costing and pricing

This started with a reasonable desire to keep rates affordable and to stay within debt limits. But this should have been addressed by keeping the costs down, not by trying to shift costs 'off book'. Statements by the council as to how they were intending to fund the costs incurred were woefully inadequate, and it is clear that by the end, the council had not only lost control of construction and project management but any understanding of the real costs of the project.

This is a problem that occurs in councils and in government organisations a great deal. Not so much in business because they recognise the need for, and can afford to have, qualified economists. Small councils often share the services of a skilled engineer, perhaps consideration can be given to sharing the services of a skilled economist as well? It is not only a matter of actually knowing what the costs are - and they didn't - but also considering how to distribute those costs amongst various beneficiaries (not only the users of the waste water plant).

These are not all of the issues that this story raises. I would be interested to hear from others who have studied the report and/or know the situation at close hand. In any case, we can all think about how the issues above are being treated in our own organisations.

OK, Enough with the serious stuff! Here is a story from our history.

How Picasso aided Asset Management in Victoria.



On the weekend of 2/3 August 1986, one of the National Gallery of Victoria's prized works, Picasso's Weeping Woman, was stolen from the St Kilda Road gallery.

A group calling themselves the Australian Cultural Terrorists claimed responsibility, and issued a list of demands in exchange for its safe return. These included an increase in arts funding and the establishment of an annual art prize for artists under 30.

The painting was discovered two weeks later – after an anonymous phone call to The Age – wrapped in brown paper in a locker at Spencer Street Station.

NGV director at the time, Patrick McCaughey, said: "It is going to be bolted to the wall and placed behind glass. If you want to take the painting next time, you will have to take the entire airconditioning duct."

It was the theft of this valuable painting that suddenly made the National Gallery of Victoria painfully aware that it had no good records of what assets they had and what they were worth. For the first time, they realised the importance of having, as a basic aspect of good management - an asset register!