ACHIEVING CONTRACTOR BUY-IN TO ASSET MANAGEMENT

Mike Levery, MCL Consultancy Ltd

INTRODUCTION

This paper will examine the reasons for contractor's fear of being involved in asset management, and how clarity of roles, responsibilities and financial accountability can help to remove some of the barriers. Attention can then focus on achieving contractor buy-in to the future asset management strategy..

ASSET MANAGEMENT – THE CHALLENGE FOR THE CONTRACTOR

To get an understanding of why contractors treat asset management with suspicion, the progress of the privatised utilities, particularly in their contracting out services since privatisation, must be examined.

Most privatised utilities have focussed heavily on shareholder value and demonstrating efficiency to the regulator through reducing their direct labour force and cutting operating costs. The "beneficiaries" of these policies have been the contracting companies, who have taken on more business and the client's own labour force providing a service back to the client company. This has generally been carried out in a highly "competitive" environment with the utility companies demanding greater efficiencies in the service provided and hence reduced operating costs.

The margins generated by many supplier companies have been very low, compared with the benefits gained by the client organisation. The move to more outsourced services has, however, been established as the long term way forward for utility companies and supplier companies have "hung in" in the hope of more stabilised relationships in the future and therefore an opportunity to improve their margins. Railtrack as one of the last of the privatised utilities has demanded a reduction of 30% in operating costs from its infrastructure maintenance contractors, with a 2% bonus on profits as a reward for achieving this target.

Is it any wonder, then, that contractors treat with suspicion the latest client initiative – ASSET MANAGEMENT – when they are invited to sign up to its aims and objectives. Consider the contractor's view when bidding for this recent multi-million pound contract for maintenance services with a major utility company and reads these two statements in the covering letter:

> "… we will move in the direction of asset management where the contractor will take more ownership to increase availability and productivity and to reduce overall maintenance costs"

and

> "… securing further reward by sharing in the benefits realised through increased productivity, asset availability and the general reduction of problems with troublesome plant".

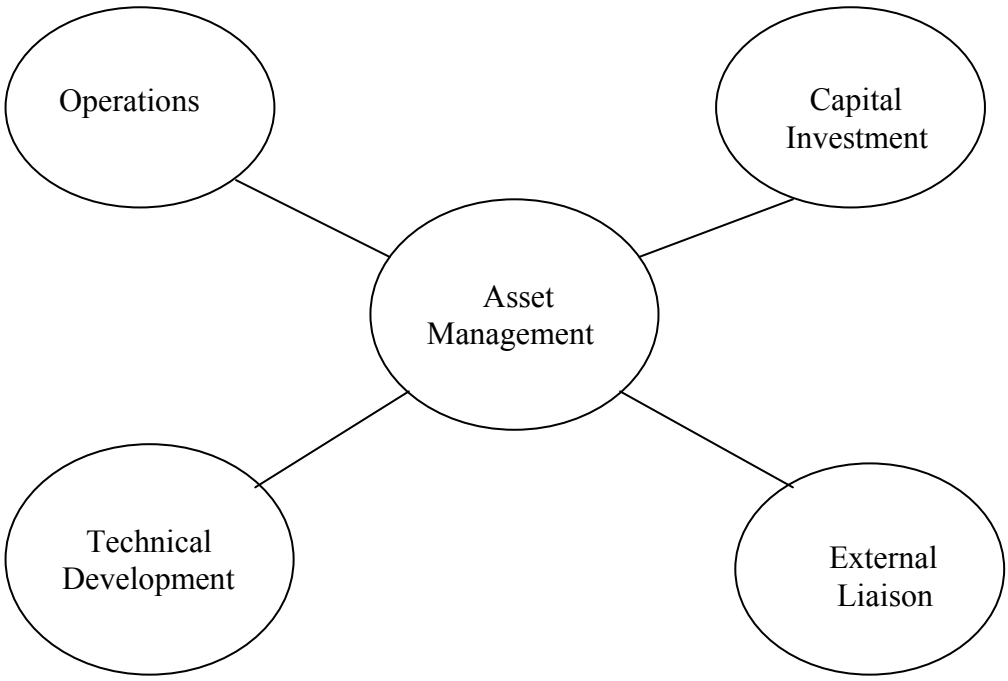
Bearing in mind that this is a maintenance contract, and the contractor does not control either the operation of the plant or any capital investment decisions, how would he interpret these two statements? I would suggest he would see asset management as a mechanism for reducing client operating costs whilst the contractor takes responsibility for asset performance. His reward for improving asset performance is to give some of his hard-earned savings back to the client. I am sure any tenderer would be cautious on their level of commitment to such a working arrangement.

This example is indicative of a new trend in outsourced services from a contractor not merely being a service provider, but now responsible more and more for asset performance. This involves transfer of RISK from the client to the contractor, and as such is a significant cost on the contractor's services. The value of such risk is significantly enhanced if the contractor only has partial control of the activities that influence the performance of the asset, but may be expected to provide performance "guarantees" in terms of availability and effectiveness of operation. It is not unusual for client companies to fail to recognise the risk that the contractor is taking on, and misread this as an unwillingness to be involved in their asset management strategy.

CLARITY OF PURPOSE

A full understanding of the client's asset management strategy which gives clear definition of the contractor's roles and responsibilities is a critical starting point for any asset management plan.

In assisting the development of an asset management strategy for the sewerage network of one of the water companies, clarity of purpose has been achieved through asset management being the core strategy for all aspects of the sewerage business.



Such a philosophy is all embracing in its approach, with the asset management strategy focussed on the NEEDS OF THE ASSETS. Separate contractual arrangements will be established for operation of the sewerage network and long term technical development with management of capital investment and all aspects of external liaison (client, regulator, highways, etc) being the client's responsibility.

With clear establishment of roles and responsibilities, then realistic objectives can be set for each of the four key areas of asset management.

Note that "operations" is one of the limbs of asset management. Too often, organisations treat "operations" as a separate and standalone activity, mainly due to its size and complexity, finding that overlaps occur with the asset management organisation leading to duplication and confusion. Asset management is not a standalone activity, it is a philosophy for running an organisation, and "operations" is an integral part of that philosophy.

Contractor buy-in will further be achieved if the three key rules for asset management are observed:

1. All decisions made in an asset management strategy are made in the best interests of the ASSET, and not one of the associated parties.

2. The asset manager must truly be the asset champion and not merely a vehicle for reducing costs.

3. Revenue expenditure maintains an asset at its optimum performance within its predicted lifespan. Capital investment either enhances asset performance, extends lifespan, or does both.

ACHIEVING CONTRACTORY BUY-IN – THE APPROACH

The client organisation should first determine the sort of relationship that exists with the contractor. Is it predominantly a COMPLACENT relationship, where the client believes the contractor is under-performing and is looking for better value for money, or a COERCIVE relationship, where the contractor is continuously exposed to competition and a more long term relationship needs to be established. The initial approach in bringing the contractor on board with the asset management strategy must recognise the position the contractor is currently in.

Can the client's assessment of the contractor's current performance be backed up with meaningful data? Are there performance measures in place, which address QUALITY, QUANTITY, COST and EFFECTIVENESS, of the work that the contractor does now? How well does the contractor perform in delivering this type of work? Can we benchmark these performance measures with other suppliers across the industry? If the contractor believes that the client doesn't understand the value he brings to the business, then this isn't a good starting point for the contractor taking on more responsibility.

The client must be prepared to work towards achieving the contractors personal objectives if he wants him to take on the client's asset management strategy. Taking on risk works both ways – if the client wants ownership of his strategic objectives, then he must own the contractor's strategic objectives. This will provide a huge boost to the relationship, and joint objectives can then be developed which rewards both parties.

The area that causes most stress in a working relationship is that of MONEY. I have yet to see a successful working relationship where TRANSPARENCY OF COSTS has not been an integral part of the financial arrangements. If one or other party feels it inappropriate to expose their financial relationship through an "open book" approach, mistrust will continue to hamper any opportunities for improvement. Asset management is about achieving best value for the assets, and visibility is key to successful decision making.

Having determined the mutual objectives between client and contractor, attention must now focus on performance measures. There needs to be a shift of emphasis from measures that specifically look at the one party (eg the contractor) to asset based performance measures, which truly monitor value for money decisions made in managing the assets. Asset based measures must be coupled with measures based on the mutual objectives of the parties involved. Any mutual objectives set must be measurable or how will you know that they have been achieved? Should finance be considered as an area for performance measures, then an asset measure would be based on cost per unit production. Financial objectives would include achievement of client budget and contractor's profit and appropriate measures would monitor these objectives.

Integration of the contractor into any new management structures and procedures must be based round the already developed mutual objectives. This is most successfully achieved through a two-tier approach to management. A management team involving the key players working full-time on the project will be tasked with delivery of the mutual objectives and managing day to day decision making. They are supported by a leadership team from a senior level in each organisation who support and advise the management team when requested, define the mutual objectives and establish and monitor performance targets focussed on the endpoint of the working arrangement.

This two-tier leadership/management team will have effective communications as a stated mutual objective, and will develop a communication strategy to ensure all those involved are fully updated with progress, objectives and targets.

SUMMARY

The reality of wishing contractors to buy-in to client's asset management strategies is that the client wants the contractor to take on more risk. The mere fact that the client recognises this, can quantify it and discuss the impact on the contractor, will give the contractor confidence that the client understands his issues and the impact that new client policies have on him.

Successful implementation of an asset management strategy can only be achieved by an open and honest relationship with the contractor, with objectives focussed on not only the needs of the parties, but also the needs of the assets.

Building trust in a relationship takes time and effort on all sides, yet one inconsiderate act can break that trust in an instant.