

Board and Executive Briefings: Major Capital Projects

VMA | **Van Mell Associates**

QUESTION-BASED BUSINESS PLANNING
BOARD-LEVEL PROJECT PLANNING

BRIEFINGS ON CAPITAL PROJECT PLANNING

WHY ARE BRIEFINGS ON CAPITAL PROJECTS NEEDED?

Decisions about major capital projects are among the most serious directors make. Having the right building in the right place is vital to so many things:

- Market share and position
- Productivity and efficiency
- Staff recruitment and retention
- Capital investment and liquidity
- Risk management

Decisions might be for new construction, renovation, campus improvements, acquisition, sale, lease renewal or financing—or several at once. These decisions relate directly to a director's duties of vision, oversight and community relations.

The pace, size and complexity of these decisions are increasing, and the Chair and chief executive need to keep directors up to date. The six briefings which follow will help the board anticipate and make decisions of which they can be proud:

1. **Framework:** How can we think critically about our buildings?
2. **Vision:** What are the leadership opportunities?
3. **Oversight:** How do we measure performance?
4. **Flexibility:** How do we increase flexibility and reduce risk?
5. **Community relations:** How can we build wide consensus?
6. **Governance:** How should we participate in project planning?

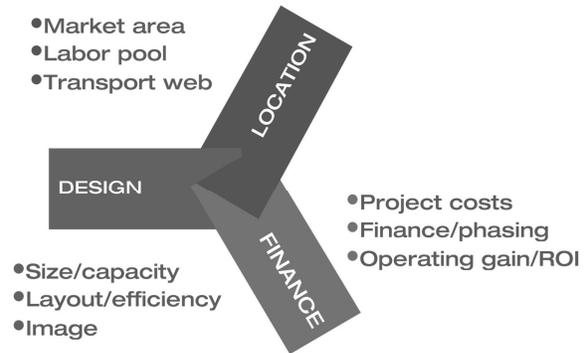
We shape our buildings; thereafter, they shape us. - Churchill

BRIEFINGS ON CAPITAL PROJECT PLANNING

1. Framework: How can we think critically about facilities?

Good project decisions depend on having clear objectives and good information. Planning should result in a summary comparison of the costs and benefits of reasonable alternatives.

Directors should not be asked to approve a major project without a plan or “feasibility study”, the core question of which is, *What buildings do we need to support our business goals?*



Issues

- The basic framework for these decisions is a triangle of integrated issues: design, location and finance.
- Project planning is an evolving and complex science and directors and executives should share its basic terms. Decision-makers need to give careful thought to the level and mix of information they want to review. (See the article on the next page)
- Directors should review a complete statement of objectives before approving a major project. There might be two dozen objectives for size, phasing, expansion, layout, image, location, quality, timing, financing, return, flexibility, etc.
- Real estate transactions must not be allowed to drive decisions.

Discussion

1. What relevant information do we already have? What do we need?
2. Do our advisors have a wide set of experiences? Are they objective?
3. Does our business plan need to be updated to make these decisions?
4. Do the directors agree generally on what issues are most important?

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Terminology and basic concepts

The terminology for capital projects is confusing. How is a “feasibility study” different from “due diligence” or a “master plan”? How do these differ from a “strategic master plan” or a “strategic facility plan”? Is a campus plan part of a master plan?

There is no standard and the professionals use these interchangeably. This article helps leaders get at the core question: *What buildings do we need to support our business plan?*

The core concepts

A good project plan integrates *all* the issues of design, location and finance (diagram) and follows this universal planning process:

1. A clear and complete statement of objectives
2. Summary analyses of the situation and needs
3. A reasonable set of alternatives
4. A cost/benefit summary
5. A process of evaluation

A plan can be for a single project or for a long-term series of projects. Plans can have different levels of detail, but should include some or all of these:

- Market maps: demographics, competition, etc.
- A map of the relevant labor pools
- A map of the relevant transportation web
- Site selection criteria: traffic, visibility, etc.
- Description of space standards / benchmarks
- Summary pie charts of space use optimization
- High-level workflow and processes diagram
- Block, fit and stacking plans
- Concept site plan or campus plan
- Architectural image concepts
- Project capital expense budgets
- Financing scheme summary (e.g., lease/own)
- ROA and/or ROI summary

While this might seem overwhelming, senior executives and directors should be helped to see the management implications of this information. It's important to decide early who's included in the planning.

Specialty studies

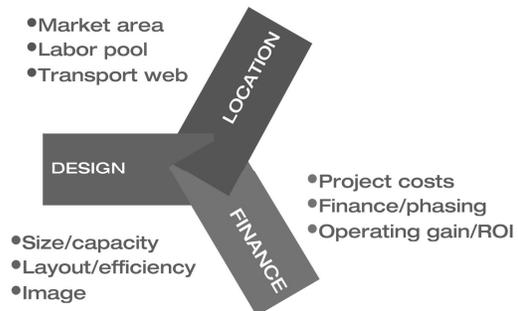
Organizations often need to study specific issues like those listed below, some or all of which would be included in a comprehensive long-term plan.

- Lease vs. own analysis
- Consolidation study
- Decentralization study
- Merger/acquisition facility study
- Analysis of highest and best use
- Space optimization
- Stay/go analysis (also buy/build/renovate)

The big picture

These decisions affect everyone on the organization and often raise critical management questions. The project plan has to clearly support your organization's long-term goals in each management discipline:

- Management structures and collaborations
- Marketing and sales (business development)
- Operations and logistics
- IT and other technologies
- Human resources
- Corporate finance



The scorecard

Planners should provide senior decision-makers a one-page summary of how each alternative fits the prioritized statement of project objectives. It should summarize their best and most objective thinking about how alternatives compare to the current situation. It should summarize key financial, performance and risk metrics.

The scorecard is a way to record the chief executive's recommendation as well as to be a point of control for assessing project performance.

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2. Vision: What are the leadership opportunities?

Many leaders believe getting a building designed and built is inherently chaotic and success means only avoiding serious problems. But history shows leaders using buildings to project their vision for the future, preserve and develop a positive culture and equip everyone for personal and collective success.

Issues

- The basic tests of a good building are a) that it brings the right people to its door, b) it equips everyone to do satisfying work and c) it inspires people to work a little harder every day.
- Buildings matter because they strongly—if indirectly—affect every department: marketing, operations, human resources, IT and finance.
- Buildings reveal a lot about an organization. All audiences will be interested in the personal spaces of the executives and Board.
- While it takes boldness and courage to approve a large project, those characteristics demonstrate leadership, too.

Discussion

1. How well do our buildings reflect our vision and culture today?
2. Where are the bottlenecks for growth?
3. What are competitors planning for their facilities?
4. What impressions do visitors get when taken on a tour?
5. What is design and construction quality and how do we measure up?

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3. Oversight: How do we measure performance?

Measuring a large project's success is difficult, but its location, design and financing affect the major line items on the P&L: revenue, direct and indirect payroll, and material costs as well as interest and facility expense. Predicting how a project will change the financial statements takes the careful judgment expected of directors.

Issues

- Few industries have financial benchmarks for project performance. Directors should ask staff to track the relevant internal ratios: ROA, debt to equity, expense to revenue, and profit per employee.
- Project performance is sometimes easier to learn about by looking at other industries. Directors can study the implications of the locations and designs of a retailer, distribution center or factory.
- The statement of facility objectives (Briefing #1) can be transformed into a scorecard of weighted criteria for evaluating projects
- Real estate market value is secondary: the critical measure is a building's operational value, its worth to the organization.
- Some projects are needed for non-financial reasons: defending market position, repairing infrastructure, or providing charity.

Discussion

1. Which metrics are most relevant to our buildings now?
2. How are our buildings performing today?
3. How certain are our cash flow projections after three or five years?
4. What qualitative issues do we feel most strongly about?

Facilities should enable and empower people to do their best. They should encourage a rising level of knowledge about corporate life: the competition, relationships, and ownership. – Max DuPree, CEO of Herman Miller

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4. Flexibility: How do we increase flexibility and reduce risk?

These projects are risky, and the biggest risks are those hidden in an uncertain future. In addition to typical risk management techniques—careful planning, insurance, hedging, etc.—it is possible to avoid risk by investing carefully in flexibility of design, location and financing.

Issues

- Design flexibility includes standardization of space types, investing in initially oversized infrastructure, careful site planning, column-free spaces, vertical expansion, etc.
- Geographic flexibility includes creative lease options, land banking, strategic real estate investments, flexible zoning, etc.
- Financial flexibility includes appropriate covenants, layered financing, balancing leasing and owning, options to purchase and to sell, etc.
- Project risks stem from design and construction problems, delays, accidents, and contract disputes. Good planning and competent professionals help reduce risk.
- Directors should see a detailed menu of flexibility options. Directors and executives, who see the risks in every department, are often more willing to pay for flexibility than middle managers.
- While some flexibility investments are costly, the long-term paybacks can be significant for protecting market share, productivity, morale, liquidity and goodwill.

Discussion

1. Have our attorneys and risk advisors thoroughly reviewed the risks?
2. How clear is our picture of the future? What are we willing to fight for?
3. Are our professionals and vendors of the highest caliber?
4. Do all the directors share the same appetite for risk?
5. What risks are we willing simply to accept?

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5. Community relations: How can we build wide consensus?

Many directors are directly responsible for helping their organizations maintain community goodwill. Project decisions have many audiences other than customers or patients: donors, volunteers, families, affiliates, investors, lenders, regulators, politicians, suppliers and the press.

This goodwill is sometimes essential for getting project approvals—political capital can take years to build, yet be spent in a day.

Issues

- Every dollar a business spends in its neighborhood can have an economic multiplier of four or five.
- Sustainable and urban infill projects are now getting more interest and public support.
- A building's architecture is essential to community relations. Architecture is too often rushed or treated as a commodity.
- Community relationships can be difficult to see, making relocation more disruptive than initially thought.
- Aerial photos are powerful tools for understanding a facility's socio-economic connections.
- Some organizations operate in several communities. Directors may need to establish facility objectives specifically about community relations.

Discussion

1. What does our community think of us today?
2. Does our community understand and appreciate our contributions?
3. Where do we fit in the municipal land use plan?
4. How can our buildings be used for positive community interactions?
5. Are our architects good listeners and talented designers?

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6. Governance: How should we participate in project planning?

Even if a board considers major projects infrequently, they still must organize themselves carefully. The Chair and chief executive need to recommend what the directors need and *do not need* to consider and how to marshal the board's capabilities. Super-majorities on approvals should be sought given that facility decisions are so important, lasting and risky.

Issues

- Directors should tour all their key facilities, thinking critically about the effectiveness of their location, design and financing.
- Directors should *not* review detailed architectural plans nor be involved in selecting the architect, broker, contactor or other professionals and vendors.
- The directors' facility-related duties will vary among a project's phases: planning, approvals, implementation and occupancy.
- Key points of control are: the statement of facility objectives, the cost/benefit recommendation, project budgets and financing.
- Project planning should be linked to the business and capital planning cycle. A project plan can take four to eight months to prepare.

Discussion

1. What are the pros and cons of having a building committee?
2. How should standing committees interact on project matters?
3. What could be the elements of a facility policy for us?
4. How might our culture of governance affect our approach to projects?
5. What are the next actions we will be asked to take?

WE ARE OBJECTIVE, INDEPENDENT ADVISORS WHO HELP OUR CLIENTS HAVE THE RIGHT BUILDING IN THE RIGHT PLACE AT THE RIGHT TIME. OUR BOARD-LEVEL PROJECT PLANNING IS COMPLEMENTED BY OUR QUESTION-BASED BUSINESS PLANNING SERVICE.

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BOARD-LEVEL PROJECT PLANNING*

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