

Profit from Projects

Method for
Improving the Financial Success of
Portfolios, Programs and Projects

a guide for
project owners, project executives,
project counselors, project auditors,
finance experts and everyone else who
is financial responsible for projects

drs. Jan G. Bloem RA CMC

inspired by organizing five editions of
the Dutch Project Portfolio Management Annual Congress

Profit from Projects

Method for Improving the Financial Success of Portfolios, Programs and Projects

ISBN 978-94-90003-01-2

© 2009 PSO Publishing

No reproduction without permission of PSO Publishing.
All rights reserved.

Bilthoven, The Netherlands
www.psopublishing.nl

Cover: Patrick Bals, Voorzien design & web

Production: Ton van Vliet, Van Setten², Houten

Preface

Profit, financial success, is not always easy to measure! And not measuring is not knowing. In 2008 we are in the center the economic disasters in the world of financial institutes: the banking industry and the stock markets. Billions of euros seem to be lost in space. Complete banks have disappeared.

Whatever the exact reasons for these disasters might have been, insane financial control should have been one of the causes. We might assume that all banks release a lot of successful projects but in the end the banks and their shareholders were not successful and faced discontinuity. High direct project revenues (sold mortgages) combined with high risk (on the final payment of loans) in the end made projects and banks performing very badly.

In this book we present ways to improve your organization in defining and realizing financial successful projects. It has become a book about projects, programs and portfolios, about processes and roles, and IT-systems to produce the adequate and reliable information. It's not necessary to read this book from start to finish. You can start in any chapter.

Proper finance is a precondition for project success, just like the availability of critical resources, clear project ownership and well-defined project goals. Proper financial information during a project's start-up, preparation and execution is not a guarantee for project success. Adequate and reliable financial information is necessary for making the right (commercial) decisions at starting and during projects, to lead you to the success which adds real value to your organization.

Acknowledgements

I would like to thank all those who stood by and helped me with the writing of this book. Special thanks to Loek Meijers (ConQuaestor) and Arian Kaandorp (ATOS Consulting) who first encouraged and ultimately pushed me into writing the book. I'm indebted to those colleagues who have given me feedback concerning the concept, especially Harvey Levine (The Project Knowledge Group), Pieter van Bijnen (The PMO Company) for use of their articles and Gerard Geurtjens (Transavia.com), Helen Meijer (Getronics) and Marc van Gent (KPN) for their input. Further I would like to thank Fred van Willigen (The PMO Company), Bart Derksen (VKZ, Ground Exploitation Expert), Rob Stevers (controller at RIVM), Freerk André de la Porte (Adelpo), Henk Bellinga (Advitec) and Wim Lindner (film producer). And my neighbor, a chartered accountant specialized in "work in progress" and member of the Dutch Counsel for Accounting Standards & Annual Reporting, for connecting me to the rules of IFRS and GAAP. Thanks to Nikki Segal for advising me in spelling American English correctly and to Willem Lang for building the website!

Special thanks to those who inspired me with their presentations in our annual congresses on the topics of Project Portfolio Management and Project Driven Organizations. Thanks to all my clients over the last 25 years who gave me their confidence and shared their problems and challenges with me. Thanks to all software-suppliers who joined our portals P solutions.nl and PSA plaza.nl and provided us with examples of IT-systems they developed for the market. Thanks to *Projectplace.nl* for using their virtual project workspace to share my writings with the other experts in the team during the first stages of this book.

And special thanks to my family, friends and colleagues for giving me their time energy and patience.

I hope this book inspires many of you to improve your business and projects.

Jan Bloem

Bilthoven, November 2008

Money is an enticing, strong and magical power. If you can't handle it, money can destroy you. Change the money-paradigm, look at it as being energy in stead of matter and many problems become clear!"

George Parker, stand-up magician

TABLE OF CONTENTS

1	Introduction to Project Finance	11
1.1	No Money - No Projects	11
	The challenge of optimizing business performance and project finance	11
	Unsuccessful projects	12
	Different situations: small and large projects	13
1.2	Various Types of Projects for Different Industries	15
	Some examples of industries with projects	15
	Project-delivery structures in the professional services industry	16
1.3	The Bermuda Project Triangle	17
	More examples ...	18
	Different systems and the reporting dilemma	19
	The black hole: hidden costs & operational cost tsunamis	19
1.4	Managing Project and Program Expectations	20
	From idea to realization and exploitation	20
	Hydraulic project-law: how time influences cost	21
	Costs of a delay in benefits-delivery	22
	Transparency in communicating goals and strategy	23
1.5	Budgets, Progress and Valuation	24
	Percentage of completion and completed contract method	25
	Baselines	28
1.6	Don't Drown in Sunk Costs (by Harvey A. Levine)	28
	Sunk Costs in Projects	28
	Sunk Costs in Project Portfolio Management	29
	Innovation at FrabCo (example)	29
1.7	CAPEX and OPEX, Tariffs and Work In Progress	30
	Operational Expenditure (OPEX)	30
	Capital Expenditure (CAPEX)	31
	Work-in-progress	32
1.8	Project Finance for Internal and for External Clients	34
	Optimize finance monitoring to stay in market position	35
	Monitor financial aspects for internal invoicing (or budgeting) of project costs	35
	Benchmarking to improve financial performance of projects and portfolios	35
1.9	Accounting Department and Project Management Office	36
	Accounting and controlling rules in small and large companies	36
	Financial reporting in the project (portfolio) management office	37

2	Project Finance Governance	39
2.1	Why is Project Governance Important?	39
	Effects of poor governance	39
	Good governance	40
	Essence of project governance	41
2.2	Business Development and Portfolio Alignment	41
	The business plan	41
	Portfolio categorization	42
	Portfolio governance	43
	Monitoring performance	43
2.3	Successful Monitoring of Finance of Programs	43
	Timing of benefits	45
	The program manager	46
2.4	Key Roles for Project Finance Control	47
	Transparency in finance control for each role	48
	Separate roles for reliable estimating	49
	Approval techniques at stage-gate toll ports	50
2.5	Financing programs and projects	51
	Financing techniques	51
	Tax regulation	51
2.6	Benefits Management (by Pieter van Bijnen)	52
	Benefits Mapping	53
	The Value Management Office	55
2.7	Earned Value Management (EVM)	56
	Basic EVM elements	57
	Never ending projects ...	60
2.8	Why Should You Use Earned Value Analysis? (by Harvey A. Levine)	61
	Versatile EVA	61
	Cost Tracking not Required	63
	Baselines	63
3	Six Key Project Finance Processes	65
3.1	Overview of Key Program & Project Finance Processes	65
	Visualize and measure	65
	Some basics of process optimization	66
	Quality of estimating and managing earnings and costs	66
3.2	Selecting and De-selecting Projects and Programs	67
	Procedure	67
	Financial risks	70

Financial reports and communication	71
3.3 Managing Business Cases	71
Procedure	71
Financial risks	73
Financial reports and communication	75
3.4 Funding and Contracting	76
Procedure	76
Financial risks	78
Financial reports and communication	79
3.5 Planning and Budgeting	80
Procedure	80
Financial risk	82
Financial reports and communication	83
3.6 Presenting Results	84
Procedure	84
Financial risks	89
Financial reports and communication	89
3.7 Closing Projects and Programs	90
Procedure	90
Financial risks	91
Financial reports and communication	91
3.8 Collecting Financial Data	91
Using a Project Management System (PMS)	91
Reconciliation of PMS and corporate finance system(s)	92
3.9 Portfolio- and Multi-Project Financial Reporting	92
Selection decisions	94
Delivering projects to the external market	95
4 Six Trails For Improvement	97
4.1 No Pain, No Gain	97
Improving step by step: make a project!	98
Assessment	100
Don't forget: Quick Wins	101
4.2 Maturity of Project Finance Control in the Organization	102
Stage 1: The beginning	102
Stage 2: Project-based working	102
Stage 3: Benefits realization	102
Stage 4: Portfolio optimization	102
Points of growth	103
4.3 Creating Awareness and Energy for Improvement	104

Positives and negatives toward change	104
Stages of change: from unconsciously inefficient to unconsciously efficient	105
4.4 Categorizing Projects by Finance Profiles	106
From small to large projects, a generic classification	106
Characteristics of the project-classes	106
Control-elements and performance-indicators for a project-class	106
4.5 Standardizing Processes for Project Finance Control	107
Starting with the project types	108
Process mapping	108
Defining process information	110
4.6 Tuning Financial Performance Measurement and Reporting	110
Presentation formats for decision makers	112
Presenting trends to decision makers	114
Personal dashboards	115
4.7 Architecture of Project Finance Information Systems	115
Improving integration of systems	117
Importance of systems for finance information	119
4.8 Developing Competencies and Roles	120
Desired project finance discipline and competences	120
Transformation of culture and skills	121

Looking back - and forward! 123

APPENDICES 125

I Financial Ratios for Investment Decisions	127
1. PBP - payback period	127
2. DCF - discounted cash flow, or NPV - net present value	127
3. IIR - internal rate of return	128
4. ROI - return on investment	128
5. EBIT(DA) - earnings before interest, tax (depreciation and amortization)	128
II Checklist Project Finance Information Domains	129
1. Strategy and Business Planning	129
2. Portfolio Alignment	129
2.1 <i>Classification of Projects</i>	129
2.2 <i>Portfolio Scenarios</i>	129
2.3 <i>Portfolio Ranking</i>	130
3. Demand Management	130
4. Program Management	130
5. Delivery Management	131
5.1 <i>Result Directed Delivery ('Project')</i>	131
5.2 <i>Time Directed Delivery ('Dossier')</i>	131
5.3 <i>Milestone Directed Delivery ('Event')</i>	131

5.4 <i>Client-Object Directed Delivery ('Object')</i>	131
5.5 <i>Resource Directed Delivery ('Posting')</i>	132
5.6 <i>Product Directed Delivery ('Trade')</i>	132
6. Project Planning	132
6.1 <i>Scheduling</i>	132
6.2 <i>Performance Appraisal</i>	133
7. Resources Occupation	133
7.1 <i>Availability</i>	133
7.2 <i>Allocation</i>	134
7.3 <i>Sub-contracting</i>	134
8. Project Finance	134
8.1 <i>Business Case</i>	134
8.2 <i>Contracting</i>	135
8.3 <i>Calculation</i>	135
8.4 <i>Project Budgeting</i>	136
8.5 <i>Project Expenditure</i>	136
8.6 <i>Project Invoicing</i>	137
9. Project Risk	137
10. Result Management	138
10.1 <i>Specification of requirements</i>	138
10.2 <i>Issue management</i>	138
10.3 <i>Logging Scope Changes</i>	138
10.4 <i>Acceptance</i>	138
10.5 <i>Project Closing</i>	138
11. Corporate Finance and Accounting	139
11.1 <i>Corporate Budgeting</i>	139
11.2 <i>General Ledger and Cost Control</i>	139
Literature	141
Index of Key Words	143
Table of Figures	147
About the authors	149
Author Jan G. Bloem	149
Guest author Pieter van Bijnen	150
Guest author Harvey A. Levine	150