



White Paper 2015-04

Why Contingency Reserves Need to Be Owned by Senior Management

Proper contingency management is essential during project execution and contingency should not be released too early. In a previous White Paper we have explained 'How to Manage Properly Your Project Contingency Throughout Project Execution' (refer to [White Paper 2014-09](#)). In this White Paper we elaborate further on the ownership of Project Contingency, and the fundamental reasons why it needs to be owned by an authority above the Project Manager.

Preamble – terminology issues

When we published our previous paper about contingency (refer to [White Paper 2014-09](#)) some discussions on social networks highlighted that the word 'contingency' can be used in different ways depending on the industry or the cost management standard that is followed. In this paper, contingency is a single amount of money that is designed to cover the entire project risk, at least the Known Unknowns. It is sometimes called 'Management Reserve'.

It is different from other cost elements that are managed by the Project Manager, including risk elements sometimes also called "contingency" that are sometimes allocated to the project cost on a line-by-line basis by some organizations (we believe that reserves to cover risk should be a single amount at the project level and should not be distributed amongst the different project cost elements to ensure effectiveness and reasonableness of the protection afforded).

Introduction – lessons from the military

Contingency can actually be considered as a reserve that is available to the organization to throw into action when required.

Let us look at what the military are teaching in the field of reserves. The military are expert at evolving in a very uncertain environment – often described in strategy circles as the 'fog of war', because the reality of the tactical environment is only known very partially by the commander due to incomplete information. In military circles it is well known that "*reserves are the tool of choice to manage uncertainty*" and that "*it is through the play of reserves that victory will be fixed*" – (General Colin). Furthermore, for Churchill, "*engagement of the reserves is the ultimate responsibility of the leader*"¹.

These thoughtful statements obviously bring a different perspective in the way contingency should be used in Project execution. In Projects, the usage of the contingency is also the greatest responsibility of the Project Manager. However, they often don't realize how important it is.

In Projects, the usage of the contingency is the greatest responsibility of the organization.

Why contingency needs to be used massively when used

The military have long known that the timely engagement of reserves is often the decisive factor in battle. The moment and the form of action need to be chosen carefully for the maximum impact. There is no need to engage the reserve only for minor disappointments; it should not be sprinkled across the front line. Engagement of the reserve needs to be a concentrated effort at a decisive turning point of the action, when and where the front forces are about to be overwhelmed at some point of the front line.

In reality, the same principles apply when it comes to Project execution:

- Contingency utilization is only effective when it is massive and concentrated,
- Contingency utilization must be timed for maximum effectiveness, i.e. when the normal project execution tactics have been significantly overwhelmed locally. This might happen quite late in the project, typically during the construction phase.

Contingency should hence not be sprinkled across the project; it needs to be used massively when it is really needed to turn around the project situation.

Why contingency engagement needs to be a significant decision

Utilizing contingency needs to be a significant decision for the organization. It means somewhat of a last resort decision to gain victory. Once the contingency depleted, there will be far less resources available to face

another unexpected situation.

We observe in too many project organizations that contingency engagement is a decision that is taken too lightly by management.

Making such a decision a key decision will also help avoiding using the contingency for resolving small issues, thus effectively significantly diminishing the potential effectiveness of the sudden injection of the Project reserves on a significant issue.

The fact that contingency cannot be used continuously to fix small issues, but that it needs to be kept in reserve for a massive intervention if needed, justifies the level of authority involved with the usage of contingency: it definitely needs to be above the Project Manager, at Senior Management level.

¹ Quoted from 'Décider dans l'incertitude' (Decide in Uncertainty), book by General Vincent Desportes (in French)

Keep manpower reserves

One area warrants significant attention, still it is not considered explicitly in most situations: the manpower reserves in the Project Management Team.

When setting up the budget for a Project we have observed that the Project Management Team and Engineering Costs, which are often mainly internal costs, are the first to get slashed during management reviews. This is due to the fact that they are often the easiest to revise, as the rest of the cost is often based on quotations from suppliers and subcontractors, and usage of key construction resources which cost is set. Still manpower generally represents limited amounts in large projects, hence savings that are significant at project level lead to very significant slashing of these budgets.

This issue is often clearly visible when the Project Manager, upon award of the Project, revises immediately upwards the forecast cost of Project Management and Engineering. However, without proper manpower planning, actual mobilization will lag, when the Project initiation stage is so important in ensuring the success of the Project.

It would make sense on the contrary to consider that such costs, and in particular the Project Management costs, and the Engineering costs related to the management of suppliers and subcontractors, are an investment into coordinating a successful Project. Therefore that additional expenditure on such budgets, within reasonable bounds, should rather lead to a measurable return on investment in the form of a lesser final Project cost and schedule.

Even more so, it is arguable that the Project Management team needs to have spare capacity to deal with Unknowns-Unknowns when they appear, without obviously falling into the complacency offered by a too comfortable Project setup. When unexpected events happen, it is often useful to create specific task forces to deal with them without disturbing the rest of the Project, and this requires sufficient reserves to be readily available.

This follows the same logic as the one described in our [White Paper 2012-23 'The Urgency of Project Startup: How to Ensure Success of your Project by Creating the Space to Lead'](#) where we emphasized that one key objective of a successful project startup is to create space

to lead and react to unexpected events during project execution. A suggestion is thus to provide the Project Manager with a tangible reserve and add a specific contingency element to Project Management as a discretionary resource for the Project Manager to draw on to reinforce his team when required.

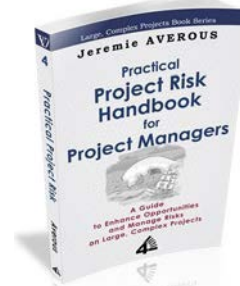
Conclusion

The engagement of contingency is a key decision that needs to reside above the Project Manager, because it is similar to engaging the reserves in the battle. Engagement of contingency when it happens must be massive, focused and coordinated to ensure the maximum effectiveness. We recommend setting up a task force at the Project Management Team level to manage this engagement, drawing on the reserves that will have been made available through a proper start-up process (which will have created space to lead) and sufficient available reserves in the Project Management Team itself.

Proper contingency usage can make or break your project. Use contingency properly!

Do no sprinkle contingency. When you need to engage it, do it in a massive and focused way, supported by a task force

Find all these principles of Project Opportunity and Risk exposed in a comprehensive manner in our new Handbook,
[Practical Project Risk Handbook for Project Managers](#)
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