

by Scott Collins, Brendan Hanlon, and Ed Scholz

Faltering Economy: Time to Thoughtfully Challenge the Status Quo

Traditional local budgeting strategies, although relatively easy to implement, are failing to adequately address the fiscal needs of local jurisdictions. The current national economic condition and its long-term ramifications require a dynamic budgeting model that focuses on outcomes instead of inputs.

It seems likely that revenues for local governments will continue to deteriorate in the near term, and a thoughtful review of the services each community delivers will be required to realign resources with community goals. Program prioritization and continuous improvement efforts are difficult tools to implement, but they produce the results local governments need as they respond to these challenging fiscal times.

Local governments, which typically rely heavily on property taxes, or sales taxes, or both, for their operations, are dealing with the reality of an economy that continues to significantly erode these revenue streams. A National League of Cities survey has reported that 84 percent of city finance officers said they are facing fiscal difficulties.¹

Denver, for example, experienced declines in monthly sales tax revenue from October through December 2008; declines were 5 percent, 5 percent, and 8 percent, respectively, compared to the same months in 2007. Although the declines were not unexpected in light of the disruption of the national economy, it is especially challenging for Denver government officials given that the sales tax represents 50 percent of its general fund revenues.

Even apart from the major difficulties caused by the current recession, the trend during the past 30 years in Denver is alarming. The compounded average annual growth rate in sales tax revenues for the past 30 years is 7.5 percent although the rate drops to 5 percent for the past 20 and to 3 percent for the past 10.

Similar trends have been recorded across America. In Santa Cruz, a small beach and university town in California, sales tax receipts have actually flattened during the past seven-year period. In prior years, however, growth neared 5 percent annually.

Declining revenues on account of cyclical recessions is one thing, and they can temporarily be addressed with such cost-saving measures as hiring and wage freezes, temporary reduction of services, deferment of capital equipment purchases, and so forth. These measures are usually only stop-gap measures, however, and they are effective for a year or two at best.

But as the annual cost of services continues to grow at a much faster clip than available revenues, local governments continue to throw around ideas on how to generate additional resources for the short term, with little thought given to long-term strategies. Moving toward a pay-to-play scenario—charging citizens for the use of parks, for example—has gained popularity during the past decade in some communities.

In most cases, however, these efforts frighten or infuriate citizens, who perceive those ideas as the government taking more of their money while they get only the same level of service they always received. They can't see anything new coming out of it, and they don't understand why their local government needs more money. It also can feel as though the government is suddenly trying to tax and regulate everything it possibly can.

A more comprehensive and strategic approach is required in order to address the widening structural deficit. Forecasting ahead three to four years, managers should consider three strategies: prioritization of services,

continuous improvement, and revenue enhancement options.

Martin Bernal, assistant city manager of Santa Cruz, California, believes that no options should be taken off the table—survival will require a mixture of all such measures.

Local public officials can use the following list as a how-to guide to help them form a more comprehensive, strategic approach to budgeting.

PRIORITIZATION AS A TOOL IN THE TOOLBOX

The overall objective of prioritization² is to help any government achieve fiscal stability in the short term, realign resources with the priorities of citizens in the near term, and determine a responsible level of

27562	124,52	126,07
27563	4.689,12	97,70
16919	268,89	89,64
21606	63,27	63,42
21606	253,08	63,42
21606	3.796,20	63,39

taxation in the process. As a tool in the local government administrator's toolbox, prioritization is important in that the process systematically guides decisionmakers, policymakers, and citizens to the actions necessary to achieve this objective.

Take, for example, revenue enhancement as a tool to help a local government achieve fiscal health in this difficult economy. How does the government administrator or elected official know if it's the right tool—the right treatment for the symptoms they've observed? And which revenues are the revenues to enhance?

Chris Fabian, business process analyst for Jefferson County, Colorado, who helped implement prioritization in this second-largest county in Colorado, comments on how prioritization

as a system leads decisionmakers to revenue enhancement opportunities when they're appropriate:

"In the process of scoring programs based on their influence on results, we recognized that it wasn't enough to value a program based on results alone. As we developed the process, we conceived of a hypothetical program that might not meet any of our results but that was completely supported by direct user fees.

"If that program fell to the bottom of our prioritized list of programs, should that program potentially receive fewer resources in the future? Thinking this through, we incorporated the scoring criteria of 'program sustained by direct user fees' into the scoring process, meaning that whether or not a program gets a high score relative to its influence on results, if that program can demonstrate that the customers completely support it, then we recognize that this takes pressure off of decisionmakers to have to choose to allocate resources to the program, and therefore the program should be elevated in priority.

"The hypothetical thought experiment proved to work, as we did encounter several of these programs that did not score well relative to any of Jefferson County's results, but recognized that their survival depended on appealing to the users of their services to generate higher user fees. It worked!

"One example of this comes from our county fairgrounds operation. At one time in our county's history, we were more rural, and so the fairgrounds were probably a highly valued institution. But now we're a highly urban county in the Denver metro area with a population of close to 540,000, and so the fairgrounds programs do not relate to our current results.

"Most every program offered at the fairgrounds fell to the bottom of the program priority list as a result of the prioritization process. The director of the fairgrounds operation recognized the likelihood that general government revenues will come less and less

to these low-priority programs, and so here's what has happened:

"One, the operation has been successful in increasing user fees for such things as facility rentals (they offer a site for banquets and meetings), space rental (they offer an RV parking lot), and special events.

"Two, they conceived of new ways to generate revenue, including selling space for advertising (signage on a major highway next to where the fairgrounds is located), and they are in the process of trying to lease out space on the fairgrounds for an animal shelter that is looking for property.

"The future of the fairgrounds is still uncertain because the programs are of low priority, but the operation has moved from being totally dependent on general government revenues to being considerably more self-sufficient.

"Other examples of this behavior, driven by the incentive to score higher in the program prioritization process, are all across the organization, including our airport operations (increased fees for hangar rental), our social services programs (increased impetus to access grants), our transportation department (revenue from cities for loaned work and cost sharing), etc."

Prioritization as a tool in the toolbox will also lead to:

Establishing and defining results. Engaging elected officials, decisionmakers, administration, and citizens by using the strategy mapping technique, in a collaborative process designed to clearly identify and define results while diverting others from arguing, blocking, or otherwise deterring the process.

Establishing a definable value for programs. Establishing a clear value for every program; accounting for the objectives of the community, of the elected officials' specific platforms and policy objectives, and of citizen interest groups; conforming with mandates; and responding to demands for service among other criteria that would influence value.

Linking results and strategic planning to resource allocation decisions.

Prioritization as a process helps us better articulate why the programs we offer exist, what value they offer to citizens, how they benefit the community, what price we pay for them, what objectives they are they achieving, and which citizen demands they are answering.

And prioritization puts into focus how strategic we are about understanding what we do, why we do it, and, in times of strife as well as abundance, how we should invest our resources to achieve the results our communities need.

essary costs, leading to unprecedented profits for Gillette.

The goal of ZOG is simple and can be related easily to the public sector. The goal is mainly to reduce ongoing overhead costs in order to fund ongoing programs. This is achieved by ridding the organization of unnecessary costs.

In a local government that adopts ZOG, all government agencies are responsible for this effort. According to Kilts, for the philosophy to take hold and be effective, it has to be more than a "one-shot deal, but rather, an everyday full-court press."³ The ZOG philosophy may seem a bit extreme, but when citi-

The upshot from the horrendous economic condition is that it provides an excellent opportunity to be courageous through prioritizing services, streamlining processes, and instilling a culture of continuous improvement.

CONTINUOUS IMPROVEMENT EFFORTS

Your organization must demonstrate efficiency to your residents. Do an assessment of your organization's overhead costs.

How do your organization's operations compare with industry standards for information technology, fleet, facility management, and management, in terms of both cost and performance? Do you have a standard target percentage for administrative costs as a percentage of total organizational expenditures?

The current crisis demands that cities and counties answer these questions and drive down their overhead costs. While it may be easy to cut cost, it is important to maintain quality services.

You may consider adopting a zero overhead growth (ZOG) philosophy, as developed by James M. Kilts, chief executive officer of the Gillette Company from 2002 to 2006. During his tenure as CEO, ZOG efforts eliminated more than \$800 million of un-

zens' demands for services grow yearly, we must take responsibility to limit administrative and programmatic overhead. That way, a greater percentage of resources can be allocated to direct service delivery.

ZOG is a philosophy; it isn't a panacea. Managers need to consider using a mixture of internal service funds, process audits and improvement, automation, reallocation of resources, and benchmark data to ensure the continued success of the government organization.

The tactics listed below are effective in driving down overhead costs:

Create internal service funds for IT, fleet, facility management, and other internal support functions. This is an "enterprise management" approach, whereby agencies become customers that pay for the services they receive from these overhead functions. Budgeting those costs in departments will drive businesslike decisions. If costs become too high, agencies can look to contract out the work.

Service agreements should be used to document service commitments and the cost for any given service. Agency service choices should have clear costs associated with them. Support agencies can become the target of public scrutiny, but their costs can be driven by unknowing agencies that expect Porsche services at Cadillac prices. The greatest utility of internal service funds is that they create transparency in decisions.

Process improvement efforts systematically document, analyze, and reduce redundancies and inefficiencies in processes. The best systems focus employees on customer needs to drive improvements. These efforts are not easy to implement. They require time and management commitment across the organization.

An organization needs to invest in employee training and set an expectation for participation in the effort. A centralized process improvement team will be effective, but long-term success will be based on the organizational culture embracing the system.

Develop a target percentage for overhead costs because a target allows you to gauge progress in your overall efforts at lowering costs; a target also affirms the organization's commitment to doing what matters.

These tactics serve a larger purpose than simply lowering costs. If carried out effectively, they can free up resources to deploy in areas of greater need. Such efforts should be marketed to residents, showing that the government is concerned about its costs of doing business and that it is working to find ways to cut spending without impacting overall effectiveness.

REVENUE ENHANCEMENT OPTIONS

Only after going through prioritization and continual improvement efforts, where you can show you are being strategic and efficient, should you go to residents to ask for revenue enhancement options.

Too often we try to couch requests for increased revenue as something new and justifiable in itself. Most people can see through it. If the government didn't start out charging for trash collection and now it's going to, most likely it's because general, ongoing revenues have been steadily decreasing, not because the government suddenly realized that it costs money to collect trash.

Efforts to raise new revenues for things such as trash pickup are usually effective only when the locality has proven to taxpayers that it's doing a great job with the funds it already has. Performance measure reports that extol crime-fighting efforts, improved street conditions, cost effectiveness, and great customer services go a long way toward justifying revenue increases when times are tough.

Similarly, you will have greater success in developing fees for services that fall to the bottom of a prioritization effort, as explained in the Jefferson County example above.

Tax increases are generally supported only for specific services or capital improvement projects. Demonstrate to residents the effectiveness of government programs, reduced administrative costs, and a generally agreed alignment of resources to top priorities. Such efforts are critical to the successful passage of a tax increase.

For programs that are currently funded through fees—recreation centers, business inspections, and the like—develop a cost-recovery methodology you can support politically. For some communities, full cost recovery may be appropriate.

To sustain these programs, tie fee increases to a clearly understood index, such as inflation, population growth, or both. Don't wait 10 years to increase fees; generally those increases are significant and too difficult to support politically.

FREE TO CUT AND STREAMLINE

The fallout from the current economic downturn has been nothing short of breathtaking. Managers and

finance officers across the country are under the gun, facing seemingly insurmountable budget deficits. Fear and loathing, however, should not rule the day.

The upshot from the horrendous economic condition is that it provides an excellent opportunity to be courageous through prioritizing services, streamlining processes, and instilling a culture of continuous improvement. Here's a chance to consider tabling services that don't achieve outcomes or that serve purposes that are no longer relevant.

Feel free to streamline processes and cut unnecessary overhead. Keep these efforts going and publicize them at every opportunity to residents, business groups, and local media. Use these efforts to justify such revenue enhancement options as funding lower-priority services through fees and increasing taxes for capital improvement projects.

This work is never done. These efforts should be conducted continuously into the future. When times are good—and here's wishing the good times come soon—don't grow back to old levels just because you can. Inevitably you will find yourself in the same situation you are in today. **PM**

¹Chris Hoene and Gregory Minchak, "NLC Survey: City Fiscal Conditions Continue to Worsen," February 2009, www.nlc.org/articles/articleItems/NCW2909/fiscalconditionsupdate.aspx.

²Chris Fabian, Scott Collins, and Jon Johnson, "Getting Your Priorities Straight," *PM Magazine*, June 2008.

³James M. Kilts, with John F. Manfredi and Robert L. Lorber, *Doing What Matters: How to Get Results That Make a Difference—The Revolutionary Old-School Approach* (New York: Crown Business, 2007), 63.

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