HARVARD Kennedy School
ASH CENTER
for Democratic Governance
and Innovation

Fiscal Strategies to Help Cities Recover—And Prosper

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ABOUT THE AUTHORS

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Before joining Faegre Drinker, Stitt worked for over 20 years in senior-level positions in strategic consulting, with a Fortune 500 firm, and in government. He spent five years with the city of Indianapolis, including serving as senior deputy mayor and chief operating officer under then-Mayor Stephen Goldsmith. He holds a law degree from the University of Illinois.

ABOUT THE ASH CENTER

The Roy and Lila Ash Center for Democratic Governance and Innovation advances excellence and innovation in governance and public policy through research, education, and public discussion. By training the very best leaders, developing powerful new ideas, and disseminating innovative solutions and institutional reforms, the Center's goal is to meet the profound challenges facing the world's citizens. The Ford Foundation is a founding donor of the Center. Additional information about the Ash Center is available at ash.harvard.edu.

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EXECUTIVE SUMMARY

Despite robust economies, many local officials entered 2020 already worried about budget balances that looked fragile in the short term and problematic in the long term due to enormous pension and health-care issues. Today, in the wake of COVID-19, clearly federal support is necessary, but it is also apparent that it cannot alleviate all the pressures on communities as responsibilities related to the pandemic skyrocket while revenues plummet.

While many public managers will rightly deploy a host of tactical cost-cutting measures, the most creative among them will explore deeper and more strategic changes, such as those presented herein, which will help address the current crisis while preparing their cities for the future. This paper suggests a transition to a culture deeply focused on data, incentives for city workers to produce internal reforms, public-private partnerships that monetize operational excellence, and rapid adoption of both new technologies and good ideas borrowed from other jurisdictions. These more deliberate and strategic approaches may be harder to implement but those offered here need not harm incumbent public employees nor negatively impact cities' efforts to ensure access and equity. Rather, the strategies we outline should strengthen the efficiency and mandates of existing government offices while helping make cities more resilient and better prepared for tomorrow's challenges.

Notwithstanding an economic expansion that lasted for more than a decade,[1] many local governments were beginning to see financial storm clouds forming on the horizon earlier this year, prior to the widespread outbreak of the COVID-19 coronavirus in the United States.[2] One of this paper's authors regularly convenes city leaders at Harvard Kennedy School's Ash Center, working with them on innovative approaches to governance. The other consults to cities on operational excellence. And both have

1 David John Marotta, "Longest Economic Expansion In United States History," Forbes, January 21, 2020, https://www.forbes.com/sites/davidmarotta/2020/01/21/longest-economic-expansion-in-united-states-history/#21d0c77d62a2.

2 Heather Gillers, "For Growing Numbers of Struggling U.S. Cities, the Downturn Has Arrived," *Wall Street Journal*, March 3, 2020, https://www.wsj.com/articles/for-growing-numbers-of-struggling-u-s-cities-the-downturn-has-arrived-11583248603.

heard in these conversations looming pessimism as city managers and financial officers began to see preliminary revenue and expense projections for cities with fiscal years beginning July 1.

The coronavirus pandemic has now greatly amplified those earlier concerns as local governments face both staggering financial challenges and also tremendous increases in demand for services. While securing money from the federal and state governments will be an appropriate focus in the coming weeks (and perhaps months), it will not solve the financial challenges facing local governments. There is simply not enough money out there to address all the financial challenges local government will experience or to address the demand for services residents will ask them to deliver. Worse still, relatively few local governments have meaningful reserves upon which to draw—and many of their state governments are in even more dire shape in that regard due to un(der)funded pension, health-care, and infrastructure liabilities.

Managers who joined the public sector over the last decade or so have had the benefit of working in a (national) economy that was consistently growing and therefore have not yet faced this type of macro-level fiscal challenge. Those days are over—at least for the near term—and public managers must now transition to a new normal where massive revenue shortfalls will be coupled with significant demands for additional services. While higher taxes, fees, and other revenues will be part of the solution in many jurisdictions, it seems likely that cost reductions will be on everyone's agenda for the foreseeable future.

As local governments pivot to this new normal, we advocate for a cost-management strategy that includes an "all of the above" approach. Many city halls may be forced into serious budget cuts, including curtailing services or institutions that were previously considered off limits. However, we argue here against indiscriminate cost cutting, employee reductions in force, or rote across-the-board cuts and, instead, propose strategic responses designed to help cope with the present and better prepare for the future.

In the response to the 2007–09 financial crisis, some cities used federal Recovery Act money to prop up budgets and did too little to make the broader and more difficult changes in how cities work. The current funding crisis driven by COVID-19, coupled with the remarkable technology tools now available, provide local and state governments with a once-in-a-century mandate to change many of their outdated operating procedures. These daunting changes will, in the long run, prove fairer to employees and residents alike. While they are harder to deploy and take longer to implement than tinkering with the existing systems, these steps forward have the potential to have a more significant impact over time and to better prepare cities for future challenges.

We recommend that cities explore the following strategic changes:

1. **Reexamine Public Value**: Look at each agency's definition of public value and consider whether it should be modernized. And then examine its performance scorecard—does each activity actually increase public value. Too many activities are initiated with the agency's interest as the focus rather than that of the client.

2. **Create a Dedicated Office for Cost Savings and Innovation**: Create and staff (with some of your best people) a small internal office, outside of the existing departments, which focuses on cost management. An independent, empowered third party with the ability to focus solely on cost management issues can help policymakers understand the true tradeoffs associated with their spending decisions. Department directors, consumed by the day-to-day, often become captive to internal information flows and lose their objectivity when considering organizational change.

3. **Transition to a Culture Relentlessly Focused on Numbers and Data**: For anyone who has worked in an organization where the current leader is the former chief financial officer, you understand this mindset. The phrase you live by in such organizations is "know your numbers." Many governments have focused in recent years on data transparency—which is a good thing. But, in a resource-constrained environment, *everybody* must know and manage by the numbers (and data). "Gut feelings" and "instincts" won't cut it in the new normal.

4. **Use Lateral Benchmarking to Drive Innovation and Performance**: Public-sector competitive benchmarking reports typically have a paragraph that starts with

the phrase "Compared to similarly sized cities in this region . . ." Such comparisons help officials improve but sometimes broader benefit derives by looking to industries and sectors seemingly unrelated to their own. We remember years ago that when Southwest Airlines wanted to shorten the time it took to "turn" an airplane at the gate, it learned relatively little from studying other airlines (as Southwest was already a leader among airlines in this category). Instead, Southwest turned to the fastest fuelers and tire changers in the world—the pit stop crews at NASCAR and Formula One.[3]

Likewise, municipal solid waste departments will likely benefit only modestly from studying each other—or even their most efficient private-sector peers. Rather, they should be visiting the major hubs of FedEx and UPS in Indianapolis and Louisville, respectively. City building permit departments should not be visiting their better-staffed, technology-rich suburban counterparts. Instead, they should be visiting Amazon's warehouses, Dell's computer assembly operations, or Toyota's car assembly plants for inspiration.

5. **Reward Productive Employees—Use Gainsharing**: Gainsharing is a system of management that incentivizes a higher level of performance through the structured involvement and participation of employees. As performance improves, employees share in the financial gain created by cost savings. Enhanced performance yields greater compensation, in turn promoting continuous improvement through a reinforcing cycle. Gainsharing dates to the 1930s when a labor leader, Joseph Scanlon, developed a framework that would ultimately be called the Scanlon Plan. The premise of the Scanlon Plan was for labor and management to collaborate on how to reduce costs, boost productivity, and eliminate waste. The resultant savings were shared by the company and the workforce.

   For the plan to work, management had to share responsibility and information with workers. Employees had to become more productive, more

3 Aston Martin Red Bull Racing's pit crew set a new world speed record of 1.82 seconds at the 2019 Brazilian Grand Prix. See: Mihir Maddireddy, "The Fastest Pit Crew You May Ever See Set a New World Record of 1.82 Seconds," Car and Driver, November 18, 2019, https://www.caranddriver.com/news/a28567721/fastest-pit-stop-german-grand-prix/.

resourceful, and more flexible. Perhaps most important, workers and managers had to talk to each other openly. And because labor and management were working together toward a common goal, they inevitably began to see each other not as opponents, but as colleagues. Scanlon described his message this way: "What we are actually trying to say is simply this: That the average worker knows his own job better than anyone else, and that there are a great many things that he could do if he has a complete understanding of the necessary. Given this opportunity of expressing his intelligence and ingenuity, he becomes a more useful and more valuable citizen in any given community or in any industrial operation."[4]

6. **Rapidly Adopt Other's Innovations; Stop Reinventing the Wheel**: Local governments frequently start projects from scratch based on the premise that their local situation is somehow unique. While each community will have unique features, it is unlikely that each community's service function needs a bespoke design. Local governments have spent billions of dollars over the years modifying off-the-shelf software to accommodate the preferences of staff members in one agency or another. In many cases, the better solution might have been to conform the local practice to the industry standard—as it was reflected in the purchased software. Similarly, in many cases, local governments could find and borrow a proven idea, practice, or strategy from an existing public, nonprofit, or private partner. Rapidly contextualizing and adopting known best practices across all local government could potentially generate billions of dollars of cost savings and myriad service improvements.
7. **Leverage Competencies of Private Partners**: Full disclosure, the authors are fans of and have worked with public-private partnerships (P3s) for decades. When properly designed and implemented, P3s can lower costs, increase local control and oversight, and improve service. Similarly, these projects can increase access to capital, talent, economies of scale, and global best

4 Joseph N. Scanlon, personal correspondence, Papers from United Steelworkers of America Research Department: 1941–1945, Penn State University.

practices while simultaneously reducing risk and shortening project timelines—critical benefits at a time when local governments will need all the help they can get. Importantly, local governments can implement P3s while treating their incumbent staff fairly. Contractual obligations for no layoffs and the provision of comparable pay and benefits are now standard, as are the requirements for ongoing union recognition and good faith labor negotiations.

8. **Monetize Operational Excellence**: Many local governments have one or more underperforming (typically infrastructure) asset that may have significant untapped value. Representative examples include water and sewer utilities, parking garages and parking lots, golf courses and other recreational assets, office buildings, and potentially airports. Using an asset sale, concession lease, or management contract to unlock that value, while still controlling important issues of access, equity, and pricing, will be increasingly important as demand for services and costs rise exponentially in other areas of local government.

9. **Eliminate the Red Tape**: Local governments generate a lot of bureaucracy. Born out of the Progressive movement with the appropriate goal of eliminating waste, fraud, and abuse, local governments have created a vast regulatory apparatus. Endless rules designed to eliminate favoritism and cronyism have effectively ended discretionary decision-making in many areas. While originally well intentioned, much of this local regulatory state would not pass a standard cost-benefit analysis. And, some of the regulation (e.g., professional licensing) is downright harmful at a time when we want to get people in the country back to work. Our experience is that cities can accomplish these objectives without negatively impacting health and safety standards. Clear rules that protect the public do not require expensive and time-consuming handoffs from agency to agency coupled with often unnecessary documentation. These reforms present that double-sided value of saving city and petitioner expense.

10. **Adopt Self-Managed Teams**: With proper training and oversight, line workers should be increasingly capable of operating as self-managed teams. In addition to lowering costs and facilitating gain sharing (see above), the practice helps empower local governments' best employees to take on more ownership of their work as well as more leadership duties. Our personal experience is that many frontline employees are eager to take on more responsibility and be held accountable for their results.

11. **Rapidly Adopt Technology Tools:** Many local governments are notoriously behind the times in terms of technology adoption. Lengthy procurement cycles that often elevate hyper-technical interpretations of perceived legal requirements over actual value, prior bad experiences, an aversion to risk, and a lack of up-front capital all conspire to keep many local governments behind the curve on new technology. Local governments simply must overcome these barriers.

    Potential solutions include strong, center-led (but not necessarily centralized) technology leadership and teams, success-based and pay-for-performance contracting processes, and integrated solutions where technology tools are a part of a broader contracted service offering for which the provider partner is fully accountable. Finally, there are some areas where local government should strongly consider changing its current operating processes (even as it commits to protecting incumbent staff). In an Internet-of-Things (IoT) world, where remote monitoring and connected devices are ubiquitous, it may no longer make economic sense, for example, to staff municipal fuel sites or parking garages, monitor bus routes in person, or operate city-managed print and copy devices.

In the near term, we also expect to see cities implement tactical cost-management strategies. Cities should pursue these options in a thoughtful, nuanced fashion.

1. **Personnel**: Put in place *flexible* hiring freezes—which differ from standard-operating-procedure hiring freezes. Government tends to simply hire when someone retires or leaves without using the departure as an opportunity to reexamine productivity. Neither reflexively filling the position nor an absolute freeze makes

sense. Compelling a process to justify that hiring will produce innovation, new (higher) levels of professionalism in reconfigured jobs, and thoughtfully reduced headcount. Attrition management programs coupled with employee transfer and retraining programs ensure essential jobs are filled without new hiring. Government often constrains itself with unnecessary job classifications and other requirements that make internal labor markets difficult to manage.

2. **Third-Party[5] Reviews of All Claims, Contracts, and Expenditures**: Too many contracts simply renew, too few have performance requirements or innovation mandates, and too seldom are they held to the same standards and principles of employee headcounts during periods of contraction.

3. **Reexamine Capital Projects**: Fresh and clear-eyed reviews of planned capital projects, again by a third party. Both in New York and Indianapolis, we found that tasking an impartial third party to value engineer capital projects reduced costs by about twenty percent. As added benefits, the value-engineered solutions were often "greener" and had lower long-term operation and maintenance costs.[6] Deferring capital investment less carefully can often drive up operating costs in obsolete systems. In the end, retain only the essential or that which is legally required. For the rest, eliminate, trim, re-prioritize, and/or cut costs through value engineering.

4. **Trim All Non-Essentials**: Focus on your core. This is not the time for pet projects from either side of the aisle. Even if meritorious, they can become a distraction.

5. **Budget Management**: Capture the remaining, unspent capacity in Q4 budgets. Once and for all, let's end the public sector's "use it or lose it" practice at the end of the fiscal year.[7] Too often, public agencies will rush to spend

5 "Third-party" in this context means reviews by someone outside of the requesting agency, i.e., someone who is a non-advocate.

6 Typical examples included converting from gray to green infrastructure in the utility and stormwater space and aggressively using meadowing strategies on parcels that traditionally required intensive maintenance.

7 See: Kyle Rempfer, "Use-it or Lose-it: DoD Dropped $4.6 Million on Crab and Lobster, and $9,000 on a Chair

their remaining budgeted funds prior to the fiscal year end—lest appropriators later use the unspent funds as a rationale to cut future budgets. While no family would manage its budget this way, the behavior is viewed as entirely rational in the public appropriations process.

6. **Fines and Fees**: Make thoughtful policy decisions on enforcement and collections practices. Neither broadly expanding nor eliminating enforcement and collection of most fines and fees will be good public policy. Considerations of equity should be addressed to help those struggling and can be done so in a targeted way.

7. **Engage Nonprofit Partners**: Consider new methods to support and leverage your local nonprofit partners, many of which will be quite strained to meet the demand for services. Government can provide shared services, physical space, technology, equipment, and other vital supports that can increase their reach. Consider not just funding or use of assets but also how to relieve burdensome and non-value-added reporting requirements in those that contract with government. Tap the innovative reach of these charities already focused on the issues of the day (such as housing or health).

The weeks and months ahead will clearly be challenging. For public officials who have been managing in the context of a growing national economy for the last decade, the pivot to a new normal will be jarring and feel overwhelming. Faced with massive revenue shortfalls and huge increased demand for services, smart public managers will look past ideological moorings and embrace an "all of the above" mindset when it comes to managing costs. Virtually every local government will be forced into painful, short-term tactical cost controls. The very best managers will seek to deploy more lasting and impactful strategic tools that will help them weather this storm, manage the new normal, and prepare for the future.

in Last-minute Spending Spree," Military Times, March 12, 2019, https://www.militarytimes.com/news/your-military/2019/03/12/use-it-or-lose-it-dod-dropped-46-million-on-crab-and-lobster-and-9000-on-a-chair-in-last-minute-spending-spree/; OpenTheBooks, "The $100 Billion Use-It-Or-Lose-It Federal Spending Spree," RealClearPolicy, March 13, 2019, https://www.realclearpolicy.com/articles/2019/03/13/the_100_billion_use-it-or-lose-it_federal_spending_spree_111114.html.

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