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UNIVERSITY

FAIRMOUNT COLLEGE OF
LIBERAL ARTS AND SCIENCES

*Hugo Wall School of Urban
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A vertical stack of various coins, including pennies, nickels, and dimes, is positioned on the left side of the slide. The coins are slightly out of focus, creating a textured background element.

Cutback Management: Techniques for a Down Time

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John D. Wong, Interim Director & Professor
Michael Woodrum, Graduate Assistant

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Introduction

- Forty-seven states are facing fiscal stress, with combined budget gaps for the remainder of this fiscal year and state fiscal 2010 and 2011 estimated to total more than \$350 billion.
 - New midyear fiscal 2009 shortfalls of \$60 billion have opened up in the budgets of at least 42 states and the District of Columbia.
 - Budget deficits are already projected in 46 states for the coming fiscal year. Initial estimates of those shortfalls total \$133 billion.
 - As the full extent of 2010 deficits become known, shortfalls are likely to total \$145 billion. Combined budget gaps for the remainder of this fiscal year and state fiscal 2010 and 2011 are estimated to total \$350 billion to \$370 billion before accounting for various remedial measures (Shafroth, 2009: 563).
- According to Ray Scheppach, the executive director of the National Governors Association: “It looks to me that the [revenue] gap is about \$ 75 billion per year over the next three years, which is about 11 percent of general revenues.
 - Adjusting for this, the best estimate of state budget shortfalls for the three-year period is between \$200 billion and \$250 billion.
 - This is a huge number, given the fact that total general fund revenues for all states are estimated to be about \$644 billion in 2010 (Shafroth, 2009: 563).”



Nature of the Beast

- Crying wolf?
- Revenue options: Are revenue enhancements an option?
- Expenditures priorities
- Across the board cuts?
- Defer spending?
- Impact of federal stimulus money?
- Short term crisis?
- Long term trend?



How Local Governments React

- Selling property
- American Recovery and Reinvestment Act (ARRA) funding
- Cutting expenditures
- Increasing taxes and fees
- Service sharing
- Public-private partnerships (PPP)



What Local Governments Have Done in Past Crises (Miller & Svara, 2009: 12-15)

“Lessons learned” call for strategic, targeted actions

- Cities and counties usually combine revenue increases, cuts in spending, and cutbacks on capital projects to neutralize a fiscal crisis. In the past, delaying action has been the typical response in hopes that the cutbacks are only a temporary slowdown.
- “Cutback management,” the well-known body of work to come out of the financially stressful 1970s, is a method for coping with fiscal turbulence, as summarized by Barbara Lewkowitz.
 - Charles Levine, the person most closely associated with the concept, observed cities being challenged by escalating periods of resource scarcity and foresaw the necessity for public sector contraction.
 - Levine emphasized that management needed to maintain credibility, civility, and consensus.
 - He dismissed any alarmist mentality; he felt that cool, rational actions would preserve necessary municipal services and help the community understand the scope of the problem.
 - To him, “orderly retrenchment,” or a managed organizational response, creates the necessary flexibility to handle fiscal stress and loosen the rigidity of municipal budgets.
 - Levine advised elected officials and managers to:
 - Recognize or predict impending decline.
 - Educate the public about necessary reductions and engage in thoughtful cutback management.
 - Refrain from moving money around for short-run expediencies or deferring maintenance. Leaders should prioritize programs and target budget cuts.



On the Bright Side

- You are not in this alone, will affect all communities
- With difficulty comes a great opportunity for change
- Saying “no” just got easier
- Early retirement options



Challenges

- Strong unions
- Council/employee skepticism—prior failed change initiatives
- Distrust of management
- Old style supervisory and management culture – limited skill depth
- Declining size of workforce (ahead of efforts to adapt)
- Media scrutiny



Framework

- Identify the problem and calculate your projected shortfalls
- Start early to identify solutions
- Develop a long range plan
- Educate and inform stakeholders
- Provide monthly or quarterly assessment projections and impact on 3-5 year financial projections



Create the Vision

- Establish the rationale and ground rules for changes—***DEFINE THE MANDATE***
- Identify key areas of opportunity—*Biggest bang for the buck*
- Engage the employee teams to consider changes—*People support what they create!*



The Impossible Dream...

- *Doing more with less* seems increasingly impossible
 - Already cut to the bone
 - Focus on doing more of what you presently do, the way you presently do it, with fewer people to get it done
- Cannot do more with less by doing it the same



Processes Not Functions

- Focus on outcomes, not activities
 - Filling potholes is an activity
 - Assuring paved surface integrity is a process with a defined outcome
- Focus on the integrated sequence of tasks
- Focus on creating *value*
 - In a service, value results from the allocation of time
 - Time is far more scarce than money
- Time is the resource over which you have the most control
- A significant amount of time is spent on non-value-added activities
- Pursue the opportunities with the greatest potential for adding value and cost savings



Basic Tasks Facing the Public Manager in a Cutback Environment (Behn, 1996: 68)

- Deciding what to cut
- Maintaining morale
- Attracting and keeping quality people
- Rallying the support of key stakeholders
- Creating opportunities for innovation



Key Strategic Questions (Thomas, Pierce, & Tomes, 2002: 2)

- What services are you (entity) providing (mission, purpose and mandates)?
- What is your vision for the future (what are you striving to become as an organization; what outcomes are you seeking for our stakeholders)?
- What are your guiding principles or values?
- Who are your stakeholders?
- What do they expect from you?
- How well are you performing?
- What difference(s) do your programs and services make (outcomes)?
- What would happen if the organization did not exist or did not provide a particular service?
- What opportunities does this fiscal environment present that you could exploit?
- What are the threats you must avoid if the organization is to succeed?



Basic Change Management Principles

- Involve people in the changes that affect them
- Don't expect people to eliminate their own jobs
- Be specific about the outcomes you expect
- Invest in planning and design—The payoff is in implementation
- Encourage boundary spanning

Revenue Sources



Fees

- Charging for all activities?
- New programs to utilize existing capacity?

Grants

- Under-utilized and non-utilized community-owned assets
 - Sell assets
 - Sub-lease space
 - Consolidate operations
- Special assessments
- Permit, inspection and other fees
 - Do fees equal cost?
 - Does cost include not just direct costs but all costs?
- Financial performance analysis of all programs
- Traffic/ordinance enforcement—Benchmarking volume
- Court fines and fees
- Collection
 - Traffic and other outstanding warrants/judgments
 - Personal property tax audits
 - Miscellaneous receivables
- Re-examine cost allocation to enterprise and non-general fund activities



Service Delivery Reviews

- Definition: “An evaluation process in which a specific municipal service is systematically reviewed to determine the most appropriate way to provide it.”
- An overall approach to keeping costs down and services up
- Focus should not be on “how much should be spend,” but on:
 - Getting a clear picture about what outcomes are desired for the specific service
 - Determining the most efficient and effective way to realize those outcomes.
- Program budgeting
- Performance budgeting



Relevant Questions

- Does the local government really need to continue providing this service?
- What do citizens expect of the service and what outcomes does council want for the service?
- How does current performance compare to expected performance?
- Do the activities logically lead to the expected outcomes?
- How is demand for the service being managed?
- What are the full costs and benefits of the service?
- How can benefits and outputs of the service be increased?
- How can the number and cost of inputs be decreased?
- What are the alternative ways of delivering the service?
- How can a service change be best managed, implemented and communicated?



Services

Review all services

- Examine utilization of all programs—Benchmark past, current and future demand
- Should we be providing this service?
- Is the private sector already providing the service?
- Is demand insufficient?
- Can we not recover our costs with a reasonable fee?

Review all business processes

- Assuming we are delivering the right mix of service offerings, are we delivering them as efficiently as possible?
- Are we optimizing the use of technology?
- Look at both internal and external service offerings

• Shared services/selling services

- Other governments
- Private sector

• Attrition plan

• Other staffing alternatives

- Part-time / temporary personnel
- High school co-op students
- Volunteer help
- “On loan” program with private sector



Other Issues

- Employee participation
 - Co-pays—health, pension
 - Cafeteria plan
 - Defined contribution plans
- Energy audit
- Refinance outstanding debt



Characteristics of Organizations That Cope Well with Fiscal Stress (Miller & Svara, 2009: 15-17)

- Leadership, resiliency, and a long view are needed.
- Fiscal health reflects the adaptation of a local government's revenues and expenditures to the resources and constraints provided by its environment. Jonathan Justice found that adaptation takes place over the long term of several business cycles and in the short term within a cycle. Adaptation positions a local government to sustain a politically and economically appropriate level and mix of services throughout the business cycle. In turn, the locality can accumulate sufficient reserves as revenues cycle up to take the organization through normal downturns without disruptive cutbacks or revenue increases.
- Long-term adaptation tactics, according to Jonathan Justice and Jeff Chapman, include:
 - Avoiding excessive commitments to fixed expenses such as debt service and unfunded post-employment liabilities, being flexible and efficient in spending choices.
 - Trying to diversify revenue sources so that they are fairly stable and may be controlled locally across economic cycles.
 - Engaging in long-term financial planning.
 - Maintaining reserves adequate to deal with abrupt, temporary shock.
 - Using charges for services and a land value tax as a benefit tax for local government capital improvements.
 - Working to educate stakeholders about their jurisdiction's financial situation and the need for fiscal planning and prudence.



Research on Cutback Techniques

- Research reveals that fiscal cutback techniques have important differences, especially as they may be used in state and local governments compared to the federal government.
- Increasing a tax has a greater impact in speeding economic recovery than cutting expenditures.
- Financial controls applied across the organization from the top have more unintentional than intentional consequences. Across-the-board cuts do not distinguish essential from less-important activities or the impact of proportional cuts on programs of different scales.
- This type of cut confuses the purposes of local government activities among stakeholders. Without a rational, understandable basis for cutting spending, across-the-board cuts encourage politicking for budget restoration by inspiring competition among programs, their allies, and local government stakeholders. Hiring freezes weaken organization performance more than targeted layoffs. Pay freezes can be implemented most easily and are perceived as fair by employees. Reducing work hours with subsequent reduction in pay has less impact on employee morale than pay reductions.



Predictors of Successful Downsizing (Cameron, 1994)

- Systematic planning and analysis prior to downsizing
- Gradual, incremental implementation of downsizing
- Increased communication
- Increased employee participation and involvement in downsizing



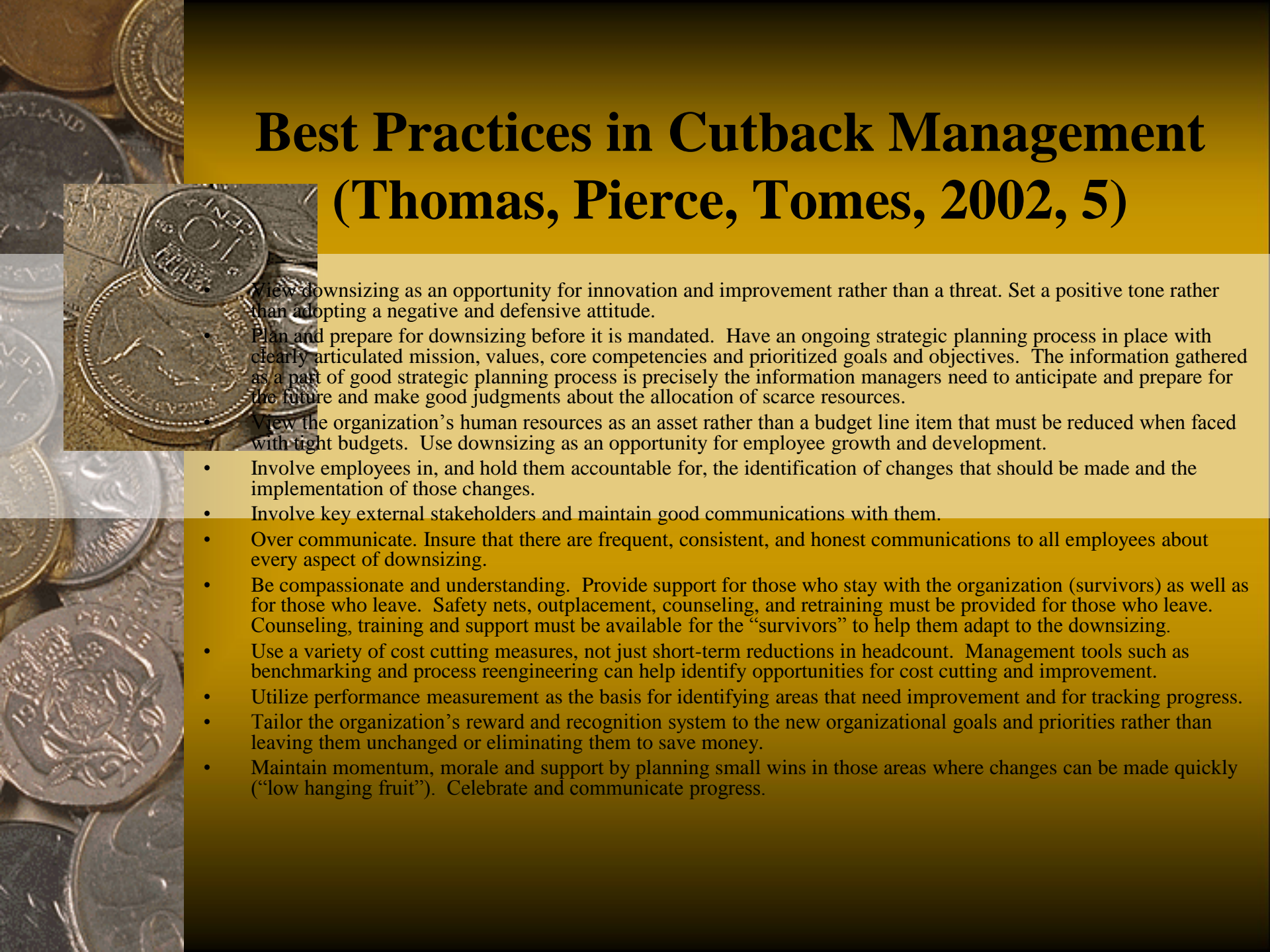
Best Practices in Downsizing (*Serving the American Public, 1997*)

- Senior leadership plays a vital role in downsizing.
- Over-communication is impossible during downsizing.
 - Morale is lowered when there is no clarity regarding the reasons for the downsizing.
 - When budget is the only driver behind downsizing, denial can take hold.
 - A common mistake is to assume that each part of the organization has an equal share of excess staff; hence, the organization may make erroneous across-the-board cuts in personnel.
 - Productivity and quality often suffer when there is no change in the way work is done—i.e., the same workload is redistributed among the survivors, rather than rethought and reconfigured.
 - When a key portion of the workforce is lost, so too are valuable contacts, knowledge, and experience. Organizations that eliminate people they later need can face costly increases in overtime, temporary, and contract work—expenses that can exceed the savings created by job cuts.
- Planning for downsizing begins with getting the right people together.
- Information not normally required in an organization's day-to-day operations becomes critical during downsizing.
- Successful planning for downsizing includes the development of business plans from various departments within the organization.
- Identification of work processes that will not be needed in the future organization is vital to the success of the downsizing action.
- Incentives such as early retirement and buyouts work well and are popular with employees.



Best Practices Continued

- The use of multiple strategies and techniques to accomplish goals for downsizing helps to leverage the outcome.
 - A hiring freeze in conjunction with a review process to evaluate vacated positions for elimination;
 - A retirement incentive program;
 - Guidelines for reducing management layers;
 - An assessment of services across the organization;
 - Establishment of teams made up of employees from across the organization to reengineer processes.
 - Establishment of training as a strategic resource, exemplified by:
 - Creating a training office separate from the human resource department,
 - Retraining employees transferred into new positions, and
 - Offering all employees training in stress and change management, customer service, and working in teams;
 - Investments in technology to achieve greater productivity; and
 - Establishment of a customer service center to improve service to the public.
- Organizations that have successfully downsized provided career transition assistance to both separated and surviving employees.
- Monitoring progress is a chief component of successful downsizing.



Best Practices in Cutback Management (Thomas, Pierce, Tomes, 2002, 5)

- View downsizing as an opportunity for innovation and improvement rather than a threat. Set a positive tone rather than adopting a negative and defensive attitude.
- Plan and prepare for downsizing before it is mandated. Have an ongoing strategic planning process in place with clearly articulated mission, values, core competencies and prioritized goals and objectives. The information gathered as a part of good strategic planning process is precisely the information managers need to anticipate and prepare for the future and make good judgments about the allocation of scarce resources.
- View the organization's human resources as an asset rather than a budget line item that must be reduced when faced with tight budgets. Use downsizing as an opportunity for employee growth and development.
- Involve employees in, and hold them accountable for, the identification of changes that should be made and the implementation of those changes.
- Involve key external stakeholders and maintain good communications with them.
- Over communicate. Insure that there are frequent, consistent, and honest communications to all employees about every aspect of downsizing.
- Be compassionate and understanding. Provide support for those who stay with the organization (survivors) as well as for those who leave. Safety nets, outplacement, counseling, and retraining must be provided for those who leave. Counseling, training and support must be available for the "survivors" to help them adapt to the downsizing.
- Use a variety of cost cutting measures, not just short-term reductions in headcount. Management tools such as benchmarking and process reengineering can help identify opportunities for cost cutting and improvement.
- Utilize performance measurement as the basis for identifying areas that need improvement and for tracking progress.
- Tailor the organization's reward and recognition system to the new organizational goals and priorities rather than leaving them unchanged or eliminating them to save money.
- Maintain momentum, morale and support by planning small wins in those areas where changes can be made quickly ("low hanging fruit"). Celebrate and communicate progress.



More Characteristics

- Short-term coping tactics include moving promptly to rein in controllable expenses and adjusting the revenue mix and tax rates to the extent permitted by law and by other constraints. Local governments should look for opportunities to improve productivity and financial management practices, consider shedding activities that can be appropriately divested or eliminated, explore introducing or increasing charges for services that can appropriately and feasibly be priced, enacting temporary tax increases, and secure special assessments for certain capital improvements. Adaptation may require major reductions in services, often made after zero-based reviews of service mixes and levels or by other methods of ranking priorities among services.
- Resilient local government organizations pursue “bricolage.” In construction, it means using whatever materials are at hand, and in budgeting, it means doing what’s necessary with what’s at hand. By distinguishing the essential from the “just good to do,” local managers decide what’s necessary to do. By choosing balanced revenues, setting realistic tax rates, and assessing the cost-effectiveness of tax gifts as recruitment tools for firms for economic development, local leaders determine what’s at hand. Bricolage permits fiscal sustainability. Fiscal sustainability strategies build the capability of a government to consistently meet its financial responsibilities. In the short term, this can be done by adjusting spending to revenues and revenues to spending, and in the long term by protecting future generations’ fiscal abilities.



Positive Actions in Hard Times

(Miller & Svara, 2009: 17-18)

- Opportunity can rise out of crisis
- Managers also recognize that well-managed organizations can find ways to make constructive changes with positive long-term impacts even in the midst of a fiscal crisis. Jim Svara argues that organizations will use hard times as the occasion for introducing change, and these actions can approximate the process of innovation. The destructive aspects of retrenchment with the loss of good people and programs make it hard to look at a cutback period as a time of innovation.
- Other actions that have been taken or systems established in advance include:
 - Understanding community values and establishing priorities to guide choice of programs and services.
 - Establishing an early-warning system to discern which trends and factors will affect strategy and timing.
 - Implementing a strategy for increasing fiscal sustainability.
 - Defining key service delivery areas and using performance indicators to measure results. Rigorous analysis determines whether programs are working. If cuts are needed, the government can identify relative program and service effectiveness.



Actions by Local Government Leaders for Economic Recovery (Miller & Svara, 2009: 18-21)

- Intelligent public investment can reap rewards
- Actions to promote constructive change.
 - Cut quickly, avoid delay.
 - Take a long-term view.
 - Focus on core mission, purpose, and highest priorities.
 - Invest in innovation and continuous improvement.
 - Manage revenues as carefully as expenditures.
 - Examine and improve organizational design and process.
 - Foster stewardship and cost containment.
 - Create a sense of inevitability, devise a workable schedule, and stick with it.
 - Commit to communicating with all stakeholders.



Lessons Learned

- Focus on long-term benefits/be willing to make some short-term concessions
- Don't erode management prerogatives
- Collective bargaining agreements were written for different circumstances.
- Start with the efficiencies, not tasks
- Be prepared for “*me too's*”
- Start with a specific function and evaluate additional opportunities

Conclusion

Insofar as possible, maintain spending rather than cutting revenues and eliminating even more programs and services. In particular, do not trim capital projects with limited impact on the operational budget.

- In making budget reductions, avoid across the board cuts that take funds away from higher priority programs and services along with those with lower priority.
- If reducing positions, avoid eliminating only vacant positions that either randomly distribute vacancies or leave high turnover agencies severely understaffed.
- Lead inclusively and encourage creativity and engagement at all levels of the organization rather than tightening controls and making top-down decisions.
- Draw on the organization and the community's ideas and support, and use the crisis to identify how the organization can be strengthened.
- Local governments should make cuts in strategic, programmed ways and look for ways to improve the organization while making changes forced by reduced resources.
- Local governments better serve their residents and do more to counter the downturn by offering sound programs and services than by reducing revenues and cutting services indiscriminately.

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