

An illustration of a city skyline with several skyscrapers of varying heights and patterns (solid grey, horizontal stripes, vertical stripes, and a grid pattern). The skyline is positioned on top of a dark blue boat with a red upper hull section featuring five black circular portholes. The boat is shown from a side profile, floating on a blue, wavy surface representing water. The background is a light blue sky with a yellow sun partially visible on the right and a yellow cloud on the left. A yellow and blue checkered pattern is visible in the top left corner.

Balancing the Budget in Bad Times

Reducing Costs and
Enhancing Revenues in
the Next 12–18 Months

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The June 2020 issue of *Government Finance Review* featured resources for local governments navigating the economic crisis resulting from the COVID-19 pandemic. These included an overview of retrenchment techniques and opportunities to access more cash (“Cash is King”)—early steps in GFOA’s 12 steps to recover from financial distress.

This article takes a close look at Near-Term Treatments, which build on the concepts introduced in the first four steps of the recovery process. **Near-Term Treatments are the next level of treatment for the ensuing 12 to 18 months.** They might be enough to resolve minor cases of financial distress. For severe cases, the Near-Term Treatments buy time for extensive changes, such as those suggested in Step 8, Long-Term Treatments.¹

Diagnosis Before Treatment

Step 4² of the recovery process is the “initial diagnosis.” You might wish to refer to this step along with reading this article to help focus your use of the Near-Term Treatments.

This article covers four topics:

A decision-making environment for Near-Term Treatments. These are things leaders can do to shape the environment to help reach the best decisions about how, when, and why to use Near-Term Treatments.

A two-part management system for using Near-Term Treatments. These practices will help you get the most from your uses of the treatments.

The “primary” Near-Term Treatments. These are the lowest-risk things you can do to balance your budget.

Riskier Treatments and how to assess whether it is advisable to implement them. The lowest risk Near-Term Treatments are the proverbial “low-hanging fruit” that government leaders often seek to close budget gaps in good times and bad. But the reality is that many governments will have to go beyond the primary techniques to address their economic and fiscal challenges. Governments facing a drop in revenues, increases in expenditures, spikes in demand for services, and loss of capacity are unlikely to overcome these problems by doing the basics well. Leaders will likely have to consider some of the riskier techniques and evaluate them carefully.



A Decision-Making Environment for Near-Term Treatments

The leaders of the financial recovery process can create a decision-making environment that encourages clear thinking and wise choices about Near-Term Treatments.

First, set up a “culture of frugality.” Everyone needs to understand that every dollar counts during severe financial distress, including expenditures and revenues. When they understand that, they will understand why Near-Term Treatments are necessary. When they understand why, they are likely to support it or even volunteer ideas for balancing the budget.

Start by announcing that being frugal is more important now than ever. Leaders need to *show* this, so that everyone *sees* that the culture change is serious. During the 2008 Great Recession, the mayor of one city went so far as to start mowing the grass in front of city hall himself to cut back on contracted maintenance costs! Of course, not every local government leader can or should start doing the yard work, but the mayor’s actions showed that he took the city’s spending seriously. There are other, less dramatic ways local government leaders could send the same message. As the mayor’s actions imply, the message will be best received if people can see that leadership is taking the same bitter medicine that they are asking others to take.

Below are examples of actions leadership could take. Many of these will not generate huge savings, but they can be symbols that show that leadership is taking the situation seriously and expects everyone else to do the same.

- Agree to look at all programs and areas for cost savings and be clear that there are no “sacred cows.”
- Delay or cancel noncritical projects, purchases, or contracts. If these are projects or purchases that leadership was enthusiastic about, it sends an even more powerful message.
- Delay or cancel programs or events that are low priority or are no longer right for times of fiscal distress (e.g., office holiday parties or golf outings).
- Cut back on office equipment, especially the kind that might be seen as “perks,” like desktop printers when electronic documents are available or when and where shared printers are practical. Don’t exempt leadership positions from these frugalities.
- Delay or end the replacement of vehicles where this won’t lead to increases in maintenance costs beyond the available savings. Don’t exempt vehicles used by management staff or elected officials.
- Publicly acknowledge and celebrate people in the organization who find ways to cut costs in responsible and constructive ways.

However, culture change can’t stop there. Emphasizing simplistic frugality could lead to penny-wise and pound-foolish decision-making. Hence, a complement to frugality is valuing results over inputs and outputs. For example, improving public safety (a result) should be valued over the number of police officers (an input) or the number of patrols (an output). If inputs and outputs are the definition of “success,” then success will become difficult, if not impossible, in an environment of reduced resources. If results are the definition of success, then people can still succeed by finding creative and cost-effective ways to reach the result.

An emphasis on results can also support a second part of the decision-making environment: a willingness to spend money to save money. Sometimes it is necessary to spend money to spur cost-saving innovation. Examples

of worthy expenditures could include labor-saving technology, bringing in outside technical expertise where staff members are missing a valuable skill, and using a consultant to validate financial position and condition to increase credibility and build the case to act. Leaders should put in place ways to make sure value is received for the money spent. This could include milestone or performance-based payments or gain-sharing arrangements with the vendor. It is equally important to have tools that apply to internal staff who often must create value in conjunction with the outside vendor. For example, buying new technology does not ensure greater efficiency. Staff must learn how to use new technology and include it in work processes.

Leadership can frame others’ perceptions. How the situation is defined is crucial.

After creating a culture of frugality and a willingness to spend money to save money, the next piece of the decision-making environment is how the financial crisis is framed. There are two basic ways a crisis could be framed: one is productive, and one is destructive. A “siege” or “bunker” mentality is destructive because it promotes conformity as people “hunker down” and try to preserve the status quo. This stifles innovation that will be needed to navigate the recovery process. The other frame is to see a crisis as an opportunity. A crisis produces “game-changing” events that can be used to break free of constraining past practices and habits. Traditional examples associated with a financial crisis include revenue losses or a bond rating downgrade. The COVID-19 pandemic creates new game-changing events, including the need to develop new emergency management processes, the need to work remotely, and the need to develop new and efficient electronic processes to replace paper-based ones, and the opportunity for local governments to provide leadership to their communities.

Leadership can frame others’ perceptions. How the situation is defined is crucial. Sharing information

helps avoid rigid reactions and may keep leaders and the organization open to solutions. How information is shared is crucial to how it impacts the decision-making environment. Often, information shared during a financial crisis is not pleasant. GFOA's research suggests a three-part rule for how to share bad news while maintaining the trust of the audience and optimizing their ability to act:

- **Be prompt.** This maximizes the time that decision-makers have to act on the information. This also preempts misinformation. It is harder to correct misinformation once it is out than to inoculate your audience against it by getting to them first. Promptness is supported by the transparency of financial information.
- **Be straight.** Don't sugarcoat or go gloom and doom. If the audience believes they are being manipulated, leadership will lose credibility. People will take their cues from the ability of the organization's leadership to portray reality.
- **Provide solutions.** Be honest about what is achievable. Give a *limited number of credible and achievable* options for how to address the problem. Research shows that too many options paralyze decision-making. And providing only one option gives no room for people to contribute to the discussion (other than rejecting the option).

Finally, the decision-making environment must ensure that the steps taken to reach a balanced budget in the short term are consistent with building a strong financial foundation for the community over the long term. Many short-term budget-balancing techniques have long-term consequences. If the local government over-relies on these types of solutions, it could find that it must endure lower grade but persistent financial stress after the crisis has passed. This is not conducive to making the community the best place it can be for its citizens or for making the local government resilient against future problems. A good example is delaying maintenance on capital assets. This increases future maintenance costs, may shorten the asset's life, and may reduce benefit the public receives from the asset today. Incorporate long-term planning and forecasting³ into your recovery effort to make sure your Near-Term Treatments attempts don't cripple your organization in the long run.



A Two-Part Management System for Using Near-Term Treatments

Putting management controls and practices in place will help you get the most out of using Near-Term Treatments. Good management does this by creating accountability for getting results and by managing the financial situation so that the organization has time and flexibility to apply Near-Term Treatments on its own terms.

The first part of the two-part management system is to secure financial position. Certain cost-cutting tactics like a short-term hiring freeze, reducing travel, or delaying payments to vendors can help stabilize financial position in the *short term*.⁴ However, certain management techniques can help make sure the local government is *consistently* stable. The second part is to be data-driven and results-oriented. This complements the advice we gave earlier to emphasize results in the decision-making environment. The management system brings this ideal into reality. Exhibit 1 summarizes the subcomponents of these two parts. We will assess them in detail.

EXHIBIT 1

Summary of the Two-Part Management System

Securing Financial Position

- Cash flow forecasting and monitoring
- Control system
- Identify sources of liquidity

Be Data-Driven and Results-Oriented

- Make managers manage
- Give timely, accurate, and understandable information about spending
- Help departments manage unexpected and unavoidable spending
- A budget should be formulated in a way that is data-driven and results-oriented
- Inventory your programs and determine their costs
- Compile key indicators of financial condition and benchmarking data

Securing Financial Position

A basic technique for securing financial position is **cash flow forecasting and monitoring**. Cash flow modeling⁵ shows the flow of cash in and out, cash balances, and events that impact cash position, such as expenditures or revenues that occur during predictable points of the year. Cash flow forecasting and monitoring helps a local government understand its financial position for the next 12 to 24 months (or longer). This kind of analysis can pinpoint when Near-Term Treatments will need to be used or when bridge financing will be needed.

The **control system** helps you stay on track with your financial plans and forecasts. Review your control system for weakness in the following areas:

- **A good place to start is budgetary variance.** Monthly reporting of changes in real spending from planned spending reveals problem areas that need attention.
- **Review position controls** to make sure headcount is kept within limits and that vacant positions are not filled unless it is affordable.

- **Check purchasing controls.** Everyone needs to understand the importance of following regular procurement practices and using purchase requisitions and purchase orders. Purchase requisitions not only make sure that proper approvals have been met before the purchase, but they also pre-encumber or place a hold on funds in the budget. This allows financial managers to develop an accurate picture of their current financial position.
- **Consider capital project controls.** Are schedules adhered to and are estimates correct? For planned projects, are the operating/maintenance impacts of projects known and accounted for in financial plans? If not, the local government has created new, ongoing expenditures that it is not able to fund.
- **Don't overlook performance.** Cost reductions will have some negative impact on services at some point. Be sure to monitor performance against goals to see where performance is slipping. You can then decide where slippage might be acceptable in exchange for lower costs or where attention is needed to bring performance up to where it needs to be.

The last part of securing financial position is **identifying sources of liquidity**. Bridge financing is often needed for recovery. Therefore, you must find sources of cash that can serve as life support until Fiscal Near-Term Treatments have their effect. A government's reserve or "rainy day fund" is the obvious candidate. Here, decision-makers may need a better sense of how they can responsibly use it⁶ to address the current financial crisis. A reserve policy that is supported by a risk analysis informs decision-makers about other risks (e.g., natural disasters) that the reserve needs to cover. This will suggest how much of the reserve is available to use for the current downturn, without creating unacceptable risks with respect to future potential exposures (e.g., floods, hurricanes, etc.). You can also check for unnecessary balances in internal services funds and determine if they can be moved to the general fund to help deal with the crisis. A related strategy is to check internal charges or contingencies to see if they have gotten too high, thereby setting apart needed cash. Another source of liquidity is internal borrowing,⁷ where one fund borrows from another that has available resources. Policies should be created to make sure internal borrowing doesn't create long-term problems. Finally, federal or state/provincial programs or local

banks could be sources of external liquidity, if favorable terms can be arranged.

Before leaving the subject of bridge financing, note that the recovery leadership must have a sense of where the bridge is leading to. The leadership must acknowledge that bridge financing can only be used for a limited time and be clear about the need for cost-reduction and revenue-raising measures.

Be Data-Driven and Results-Oriented

The second part of the two-part management system is to be data-driven and results-oriented. A good starting point is to **make managers manage**. In some organizations, layers of control may have built up that add overhead costs and give limited value. Instead, put the onus on managers to do their jobs. To illustrate, in one Midwestern city, departments regularly exceeded their budget. The first response of the finance director was to assign budget analysts to each department (another layer of control) and the analysts would try to cajole the departments into following their budgets. Unsurprisingly, this did not work, so the finance director removed the analysts and told departments that they would manage their own budgets. If they went over, they would need to go before the city's ways and means committee in a public meeting and explain why they were over budget and what they were doing to fix it. They would then have to report back to the committee on how they were doing with staying within their budget. Unsurprisingly, this worked. Departments started to comply with their budgets almost immediately.

Next, look for places where an excessive and costly control system may have developed to compensate for lack of management accountability. The budget analyst case above is one example. Another might be spending controls enforced at the level of detailed line items. Instead of requiring managers to seek permission from budget authorities to move money between the line items for office supplies and equipment, allow them to move money between all line items in the "commodity" and "contractual services" categories and hold them responsible for staying within the total budget.⁸

The finance office must help managers manage. Lack of good information for decision-making is a prime contributor to financial distress. Therefore, the finance

office must **give timely, accurate, and understandable information about spending**. Many local government finance offices have had success with financial "dashboards" that give at-a-glance information on a department's financial condition. Dashboards can vary but three needed features are:

- **Timely information.** The information must be available soon enough so that managers can use it to change course quickly. ERP systems are capable of providing real-time budget reports that can communicate to managers the current status of available budget, expenditures, and encumbrances, along with spending data by contract, vendor, project, or grant.
- **Intuitive.** Visual indicators, like shapes or color coding, can convey the meaning of the numbers. For example, red might mean the budget is off track, yellow signifies dangerously close to off track, and green is on track.
- **Recognizes seasonal variation in spending.** A dashboard, as described here, requires breaking an annual budget into several guideposts. However, dividing the annual budget into 12 equal months may not work well for spending that has seasonal variation. An obvious example would be the snow removal budget in a cold-weather city or budget associated with tourist or vacation seasons. However, there are often seasonal patterns not obvious in local government spending. Use prior year actuals to discover seasonal patterns and use them to break the annual budget into meaningful monthly guideposts.

These ideas bring us to what research has shown to be the most effective accountability system.⁹ People will be less likely to avoid accountability when: A) their actions are transparent (e.g., a dashboard that shows real spending compared to the plan); and B) their reputations are on the line (e.g., they will publicly be called to account for failing to stick to the plan).

That said, there will be times when some managers are unlucky, and circumstances make it impossible to stick to their spending plan. For example, first responders, public health staff, and others working to coordinate emergency operations during the COVID-19 crisis are dealing with an unprecedented situation that most governments did not budget for. In these cases, **the finance office must help departments manage**



A good place to start with developing a new way of budgeting is to inventory your programs and determine their costs.

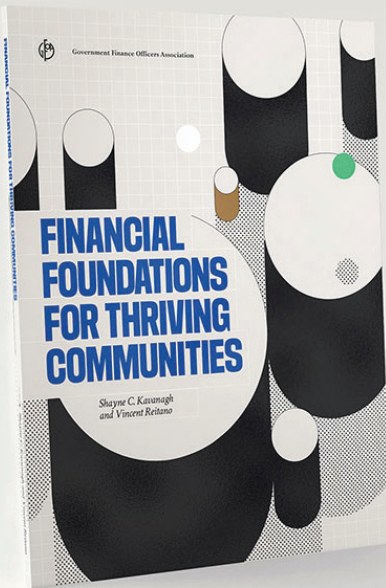
unexpected and unavoidable spending. If managers are “punished” for bad luck, the logical response for them is to build more padding into the budgets. More padding across all departments adds up and makes it difficult to balance the government’s budget. Finance departments can help by setting up a central contingency and giving departments access to manage the unexpected and unavoidable. The finance department can also help departments explain unlucky variances from the plan to elected officials and the chief executive officer.

Accommodating bad luck is important during the COVID-19 pandemic. Departments may have workers fall ill (requiring overtime or substitutes to cover gaps) or have surges in demand (e.g., a greater number of emergency response calls). Finance staff must understand the financial implications of these unexpected changes and be ready to help departments manage them. This builds trust, and more trust will be valuable as the government makes its way through the recovery process.

So far, we have discussed being more data-driven and results-oriented in the management of day-to-day spending. The ultimate expression of a local government’s financial management system is budget formulation.

The budget should be formulated in a way that is data-driven and results-oriented. However, the traditional line-item budget is neither of those things. It is input- and output-oriented and driven mainly by historical precedent. The line-item budget has its advantages in a stable environment, but it does not have a good answer for how to cut back spending. Therefore, it is common to see across-the-board cuts where every department is asked to cut an equal amount. However, this fails to recognize that some spending is more important than other spending. It also misses the opportunity to shape and size local government for its new environment.

A good place to start with developing a new way of budgeting is to **inventory your programs and determine their costs**. A program inventory shows what services government is in the business of providing and at



Looking Ahead to a Strong Financial Foundation for Your Community

The GFOA 12-step recovery process is not intended just to help you deal with immediate financial distress; it is intended to put your government on the road to a strong financial foundation for the long term. GFOA's recent book *Financial Foundations for Thriving Communities* describes the five pillars of a solid financial foundation. The advice we have given so far is designed to help you enact these five pillars. Below are some examples.

- **Establish a long-term vision.** Use cash flow forecasting and modeling to give people a sense of what to expect in the months ahead. Use long-term forecasting to make sure short-term recovery techniques don't cripple you in the long term.
- **Build trust and open communication.** Provide tangible symbols of leadership's commitment to "walking the talk" of a culture of frugality. Communicate bad news in a way that builds trust.
- **Use collective decision-making.** Work toward a data driven and results-oriented budget process.
- **Create clear rules.** Review your control system and clarify what the rules are.
- **Treat everyone fairly.** Help departments manage unexpected and unavoidable spending. Don't punish them for bad luck.

what cost. Creating the inventory may highlight unproductive or unnecessary programs that can be dropped with little controversy. Even if no such programs are found, an inventory and sense of program cost is a crucial prerequisite to wise budgeting in a cutback environment. Programs provide the ideal unit of analysis for deciding where cuts can be most strategically located. Two examples of successful cutback budgeting methods that benefit from a thorough program inventory are priority-based budgeting and zero-based budgeting.

Finally, **compile key indicators of financial condition and benchmarking data**, like employees per capita, overtime spending ratios, benefit costs, claims costs, etc. This can reveal areas of over-spending and generate ideas on how to reduce expenditures or increase revenues. Workload indicators might show where resources can be repurposed. For example, if the anticipated number of building inspections is expected to decline, perhaps inspector staffing levels need to decline as well.

Benchmarking data also gives tangible proof of the need to change. For example, in one city, benchmarking highlighted excessive benefit costs and revealed that terminated employees weren't being removed from the health care plan in a timely fashion (with sometimes up to a three-month lag), costing thousands of dollars. As this example shows, benchmarking won't tell you where cost savings can be found, but it can highlight where you should be taking a closer look at your operations.

That said, be mindful of the limitations of benchmarking. You must ensure consistency in measurement across all organizations. For example, reported costs for programs can vary, depending on whether overhead expenditures, capital costs, or other indirect costs are included—or not included. There can also be contextual factors that frustrate "apples-to-apples" comparisons. This doesn't mean that benchmarking is not helpful. It means that it is thought of as a *clue* where saving *might* be available, not a certainty on where saving is available.

EXHIBIT 2

Overview of Primary Near-Term Treatments

Control Personnel Costs

- Vacancy control
- Monitor and limit overtime use
- Address health care costs
- Review the use of consultants and temporary staff

Enhance Purchasing Practices

- Many small opportunities add up

Review Ongoing Expenditures

- Audit routine expenditures
- Investigate risk management practices and workers' compensation claim patterns

Pooling Resources and Partnering

- Cooperate with other governments to achieve economies of scale
- Pool department resources
- Look for ways to partner with private organizations and citizens

Better Manage Capital Spending, Equipment Costs, and Debt

- Better align capital financing with project schedules
- Use long-term capital improvement planning to make better near-term decisions
- Develop an equipment replacement schedule
- Improve fleet management
- Review opportunities to refinance debt at lower interest rates

Enhancing Revenues

- Obtain federal and state/provincial aid
- Examine fees for services
- New taxes with a strong connection to a desired service
- Improve billing and collection methods
- Audit tax revenue sources



The Primary Near-Term Treatments

Near-Term Treatments help you balance the budget; however, not all techniques are equal. They differ along many dimensions, such as long-term consequences, short-term cost benefits, impact on morale, and more. These differences add up to differences in risk. Some Near-Term Treatments are less risky while others have major potential drawbacks. In this article, we will focus on the techniques with the lowest risk, which we call “primary” techniques.

The “primary” techniques mostly take sound, proven financial management practices and explain how they can be helpful during financial distress. Governments shouldn’t wait for a crisis to use many of the primary techniques. They are things governments should be doing in good and bad times to maximize the value of taxpayer money. We have grouped primary techniques into the following categories: control personnel costs; enhance purchasing practices; review ongoing expenditures; better manage capital spending, equipment costs, and debt; and enhancing revenues.

Exhibit 2 overviews the techniques under each group. If your financial situation calls for more extensive help than the primary techniques can give, you can consult GFOA’s Financial First Aid resources, available at www.gfoa.org/ffa.

Primary Techniques versus *Cash Is King*

If you have read GFOA's article and whitepaper, *Cash Is King*, you might notice some areas of overlap with the primary techniques. This is intentional. Some techniques in *Cash Is King* may not have been viable for your organization when you were early on in the recovery process. As you proceed deeper into the process, perhaps people are willing to reconsider ideas that they weren't ready for before.

Control Personnel Costs

Vacancy control. Personnel is not only the largest area of cost for most local governments; once full-time employees are hired, reducing costs can only be made with strategies like layoffs, furloughs, or compensation reductions. Therefore, it is best to avoid hiring new employees for vacant positions unless the hiring is affordable and necessary. The government should require that any decision to fill a budgeted vacancy be subjected to review to find out if it is possible to put off hiring. The GFOA 12-Step recovery process advocates forming a recovery leadership team. This team could conduct the review. The review should consider the total cost of the position, the accuracy of the job description, and if the tasks of the proposed position could be addressed in a less costly way. The team should also discuss how not filling the position would impact the goals of the government. If department managers are not part of the recovery team, they should be brought into this discussion. The goal is to develop a rough understanding of the cost and benefit of each position and to prioritize positions across the local government, using the input of all departments.

The finance department can *support good decision-making* on vacancies by providing integrated finance and human resources information such as the cost of vacant positions, including salary, benefit, and equipment/training/onboarding costs associated with new hires.

Finally, it is worth noting that this technique differs from a hiring freeze. A hiring freeze is a blunt instrument where no positions are filled. Vacancy control uses data to make wise decisions about when to hire and when not to hire.

Monitor and limit overtime use. During the COVID-19 pandemic, overtime may be unavoidable given the needed public safety response and covering for ill

employees. That said, taking steps to control overtime can limit the financial impact. First, analyze overtime costs. Are overtime costs excessive compared to regular wages? You can *benchmark* departments to similar departments in comparable local governments or other departments in your government. If there appears to be an opportunity to cut overtime, there are many possible avenues to find the savings:

- Can different schedules create less need for overtime or can part-time employees fill staffing gaps? Or is the overtime high enough that hiring junior full-time staff would be cheaper than paying more senior staff overtime? Look at the practices of governments with less overtime to see how they do it.
- Are there specific employees who consistently work overtime? Sometimes a few employees create a large part of the problem. It might be best to deal directly with these individuals.
- Are there special projects or services that consistently create overtime? Can the services be approached differently?
- Is there a clear personnel policy about when overtime is allowed and how it is approved? If not, there could be some reduction in overtime available by clarifying the policy.
- Could the financial recovery present a chance to adjust long-standing overtime policies or practices that are unsustainable now?

Overtime is an opportunity to *make managers manage*. For example, one county government created a single pool of funding from which overtime costs had to be drawn. All departments shared the funding pool rather than each having its own overtime account. Managers had to justify when they wanted to draw funds from the central account. This made every manager's action transparent. Their reputation was on the line because fellow department heads would be critical of proposals to use a disproportionate share of the pool.

The finance officer should *give timely, accurate, and understandable information* about overtime spending to help managers manage. The CFO of one city did a regular report comparing overtime by department year-over-year and budget versus actual. The report included the top 25 overtime earners citywide. As you might guess, departments did not want to find their employees on that list.

Address health care costs. Healthcare costs are a large and rapidly growing cost for many governments, making healthcare cost control vital to financial stability. However, during the COVID-19 pandemic, governments must

exercise care in how they manage employee healthcare. First, employees may be sensitive to changes in health benefits. Second, some types of health plan reform can have the unintended result of employees seeking less medical care. This might be an especially bad time to run this risk. Here are some cost reduction techniques that have proven cost savings without reducing employee benefits. They require less effort than many other healthcare cost containment strategies.

- **Rebid existing insurances.** Especially if you have been with your current provider for a long time, there might be a chance for competitive purchasing to reduce costs. You can benchmark your rates against comparable local governments to get an idea if you can find a lower-cost insurance option.
- **Conduct an eligibility audit.**¹⁰ It is common for dependents or former employees to be carried on a government health plan even though they are not eligible or no longer qualify. Consider requiring spouses with coverage from another employer to use that plan as the primary plan for themselves, not the government's plan.
- **Put a section 125 or “cafeteria plan” in place.** Section 125 of the Internal Revenue Code allows employers to offer their employees a plan to receive certain health, dependent care, and other qualifying benefits on a pretax basis. This type of plan can produce tax savings for employees and employers.
- **Control the cost of prescription drugs.** Prescription drugs are a large and growing part of many governments' health plans. Tiered prescription drug benefits encourage plan participants to choose generic drug options by charging different co-pay amounts depending on the tier the drug is in. Research has shown that educational efforts to make plan participants aware of the price differences between brand-name and generic drugs can improve the chances that participants will choose generic. Finally, mitigate the use of drug company coupons, which allow the employee to avoid a higher out-of-pocket charge for brand-name drugs and shift the cost to the employer.
- **Hire an employee healthcare concierge service.** Such a service helps employees “shop” for healthcare, review bills, and recommend healthcare providers. Employees often value the help the service provides, and it can save the local government money by helping employees find cost-effective services.
- **Consider joining a healthcare cooperative purchasing pool.** Pooling with other employers provides economies

of scale, purchasing power, and access to best practices that might not otherwise be available. For example, a purchasing pool may have already applied self-insurance and wellness practices that would take an individual government longer to set up.

Review the use of consultants and temporary staff.

Often, consultants become quasi-permanent staff out of habit or because they become integrated into the organization. Consider if the consultant is the best value for your needs. Sometimes outsourcing is not the best method for providing service, nor the cheapest. Sometimes former employees who are now retirees consult for the local government, drawing two checks. Review the number of hours consultants provide, the results you are getting, determine if you have become over-reliant on consultants, and see if there is a better approach.

It could be that there is a way to make greater use of consultants. A consultant or contract arrangement can be useful for part-time service. If the demand for service and/or your budget does not support the cost of full-time employees, perhaps a contractor could help fill the gap. For example, perhaps you hold a vacant full-time position open but use a part-time contractor to do the most important duties the full-time position would have done.

Enhance Purchasing Practices

Maintain and enhance competition. Reevaluate vendors regularly. Too long with any provider may create complacency. This can be important for professional services as well as commodities. During an economic recession, some firms may be more interested in government contracts than before. Take steps to let them know about ways to get involved in your procurements. Consider relaxing requirements that are obstacles to new competitors. For example, if bid specifications are too limiting and allow only a handful of competitors to take part in the procurement, the government may be missing an opportunity.

Better management of contracts. Check your current contracts to see if you are taking advantage of prompt payment discounts. Governments in distress sometimes delay paying bills to conserve cash. As a result, prompt payment discounts may be sacrificed. Find out where such discounts are available and take advantage. This may require contacting suppliers, apologizing for past payment delays and promising to do better. Institute practices to avoid late payment penalties.

Consider opening and renegotiating your largest supplier contracts. In an environment of fiscal distress, vendors may be willing to lower prices to keep the business.

Develop multiyear contracts with vendors if they will offer and/or guarantee lower prices. This is true with construction-related activities, landscape, printing, and heavy equipment. Energy may be important from a long-term perspective. With this strategy and the prior one, recognize that private firms are not as stable during a recession. Be ready to find another option if the vendor goes out of business during the term of the contract.

Improving purchasing practices. There are ways governments can save money by improving their purchasing practices:

- **Better management of bulk purchases.** Identify the items that make up the bulk of your purchasing and see if new quotes or suppliers can lower costs. Check purchases across the organization, not just by department. Encourage or require joint purchasing of similar items, especially office, janitorial, and communications supplies.
- **Standardize.** Develop standard specifications for commodity items. This will allow for better terms to be negotiated with vendors and could reduce operating costs down the line. For example, standardizing certain kinds of computers results in lower upfront costs and lower maintenance costs for the IT department.
- **Just-in-time purchasing.** Put in place just-in-time purchasing for products like office supplies, auto parts, and janitorial supplies to reduce or eliminate warehouse and inventory costs. Many vendors will

provide ordering software that controls the approval process and allocates the bill per the organization's parameters—at no cost. However, be aware of the need for some redundancy in emergency response supplies. A just-in-time approach can make a process fragile if the supply chain is interrupted.

- **P-cards.** P-cards have purchasing controls that give individuals the ability to make purchases. P-cards can help reduce the overhead that is often involved in government purchasing and help set up a just-in-time purchasing environment. P-cards may also give rebates on purchases. These can add up to a material benefit for the local government across all P-card users.
- **Inspect incoming purchases.** Significant parts of orders received may be unneeded or unusable, increasing costs and cash out the door. Hold suppliers accountable for providing goods in the right quantity and in good quality.

Review Ongoing Expenditures

Audit routine expenditures. Many routine expenditures are on “autopilot.” Over time, the costs can get off course. Savings can be had by auditing these charges and getting them back on course. Even if these audits do not result in huge savings, they help create a culture of frugality. Examples of expenditures to assess include:

- **Retiree pensions and benefits.** Make sure that only those entitled to benefits are receiving them. It is not unheard of, for example, that a new spouse of a deceased employee's spouse is receiving health insurance and the pension payment at the government's expense. Verify that health coverage is coordinated with Medicare and other available coverage. Use positive re-enrollment procedures.

Many small opportunities to enhance purchasing practices can add up to sizable cost reduction. Consider implementing as many of the purchasing strategies as is practical.

- **Cell phones.** Consider replacing cell phones with IRS-compliant allowances budgeted at a lower level than annual cell cost, then requalify every user with stricter criteria. Negotiate pooled minute plans and compare rates with other agencies.
- **Vehicle allowances.** Some staff might be getting vehicle allowances and have access to government vehicles. There is not a strong case for having both.
- **Paper.** Large paper costs might indicate an opportunity to go paperless and save money. For example, many local governments have saved money by buying every board member a tablet PC and distributing materials for board meetings electronically, rather than printing. There are other ways to save money by eliminating paper.
- **Purchasing habits for office and janitorial supplies.** Determine average use per month in each department (perhaps on a “dollar-per-employee basis”) and compare across the organization. Of course, some departments will use more than others, but this exercise can help set up a check for reasonable use.
- **Energy consumption.** Audit energy consumption to find where use is high and efficiency-enhancing technology or techniques might be useful. Solutions don’t need to be exotic or high tech to be effective. For example, better route planning can save fuel costs, and timers or motion sensors for lights can save electricity (especially for buildings that may be closed to the public or on reduced hours).
- **Publications, travel, and memberships by employee.** Review these to find out which are the most valuable to your organization and commit to them. Be selective about future purchases and look for the best value, including online options. Professional development is where staff can get the ideas and new capacities to help your organizations through the recovery, but some professional development provides more bang for the buck than others.
- **Audit for held funds.** Audit encumbrances and purchase orders for “held” funds. Investigate planned projects for which funds are carried over more than a year. Even six months without spending requires some explanation. If the project is not realistic, perhaps it should be canceled.

Investigate risk management practices and workers’ compensation claim patterns. Insurance premiums and claims settlement can be a large expense. This can result from poor risk management practices, mismanagement, or even fraud. Start by *benchmarking* your experience

for workers’ compensation and liability claims against comparable local governments. If yours seem high, consider using a third party to help investigate, especially if staff do not have the expertise.

Also, look at insurance deductibles. These are often left alone for long periods when a review of claims history may show that a higher level of deductible can reduce premiums. This should be done with a consideration of the funding sources for claims that are greater than deductibles. For example, are there enough funds in an insurance or risk management reserve?

A culture of frugality and getting results can have tangible benefits when it comes to risk management. For example, a safety program can reduce injuries and accidents. This produces short- and long-term benefits, such as reduced claims and overtime (for shift coverage). Aggressive management of claims through challenge, negotiation, and mitigation can reduce future claims as well as payments for current claims.

Finally, improving risk management could be a way to get employees positively involved in combating fiscal stress by creating a safer work environment.

Pooling Resources and Partnering

Cooperate with other governments to achieve economies of scale. In normal times, jurisdictions might be hesitant to give up the freedom that comes with going it alone. During a financial crisis, local officials may be more willing. Wherever possible, look to join existing cooperative arrangements, not start a new one. It will take far less effort to get on board with an existing arrangement. Good opportunities for cooperation include:

- **Joint purchasing.** Purchasing office supplies, vehicles, computers, and operating supplies is common. State contracts, council of government, or special government pricing schedules provided by major vendors give ready-made access to these savings. Look at already-established cooperatives or work with others to develop a multi-jurisdiction cooperative.
- **Joint health benefit purchasing.** Health insurance can be purchased with other agencies or through pooled insurance arrangements.
- **Risk pooling.** A larger, more diversified risk pool can provide savings on property, casualty, liability, and workers’ compensation insurance.
- **Surplus inventory.** Share surplus inventory with other agencies or departments through an intranet or virtual warehouse system.

- **Other support services.** Besides these mentioned, there could be economies of scale in other support services like training, facilities management, etc.

Pool department resources. An opportunity that often pays big dividends is a shared budget contingency. This is an opportunity for risk pooling. To illustrate the potential, imagine that a government has 10 departments, each with a 10% chance of incurring an extra \$1 million in added costs. In the absence of risk pooling, each department builds \$1 million of “padding” into their budget to account for the risk, for a total of \$10 million in padding across the government. On average, however, the government will only incur \$1 million in unexpected costs each year (10 departments x 10% chance x \$1 million loss), resulting in \$9 million in unnecessary padding. The finance department can *help departments manage unexpected and unavoidable spending* by creating a shared budget contingency that can be used for unexpected and unavoidable spending. For this Near-Term Treatment to work, departments must trust that the finance department has their back and will help them access the contingency if needed.

Savings can often be had by sharing resources across departments. Often, personnel resources can also be shared. Besides making an effective use of the government’s limited resources, employees may value the chance to learn new skills. For example, perhaps a decrease in new construction reduces the demand for building inspectors. Perhaps these inspectors could offer support to the fire department in fire prevention programs or could take on a greater role in code enforcement.

Look for ways to partner with private organizations and citizens. There might be ways to work with private organizations in your community to help resources go further. For example, not-for-profit organizations might be able to help run or fund services like libraries, senior centers, recreation programs, cultural institutions, and more. This technique might be useful for noncore services that the government would otherwise be forced to cut. It helps reduce the sting of the service cut for clients. Governments might be able to support the nonprofit sector by providing in-kind donations of unused space or equipment to community service organizations.

Private citizens might also be willing to volunteer time to provide services, especially if their normal source of employment has slowed down. Be mindful that volunteers can present their own set of management issues. Workers’ compensation and liability insurance must cover volunteers. During the COVID-19 pandemic,

local governments might be limited in their ability to provide personal supervision of volunteers’ efforts. Nevertheless, volunteers could have potential. During the 2008 Great Recession, one midsized city cut costs in the police department by using volunteers for support duties like courier service, chaplains, information desk, and more.

Better Manage Capital Spending, Equipment Costs, and Debt

Better align capital financing with project schedules. In local governments with a capital program, capital projects have a huge impact on financial position. Improving capital project management and monitoring can provide near-term benefits. For example, it is common for the start of a project with approved budget authority to be delayed. Monitoring of delayed or canceled projects can free up funds for other uses. Project schedules may also be overly optimistic about how quickly a project will proceed, thereby overestimating the rate at which project funding would be drawn upon. This could result in bonds being issued before funding is required, in larger amounts than needed, and the potential for interest-earning rebates due to failure to meet bond arbitrage spend-down timing requirements. It could also result in premature allocations for pay-as-you-go financing projects, thereby tying up scarce funding.

Use long-term capital improvement planning to make better near-term decisions. Foremost, get a firm understanding of all capital projects on the horizon. Though a capital improvement plan is a long-term commitment, it can provide near-term benefits too.

- It will help the local government prioritize projects and focus on those that reduce costs. For example, a new asset may require fewer staff members to operate or have lesser maintenance requirements. A powerful tool to help think this through is lifecycle costing.¹¹
- It can help you understand the operating and maintenance costs of new assets. Even if the cost of acquiring an asset doesn’t impact the operating budget, its operating and maintenance costs will. The government should consider future operating and maintenance costs when deciding which capital projects to delay or cancel.
- It can help the government rethink its use of pay-as-you-go (i.e., cash) funding versus debt funding. Many local governments prefer to fund a large portion of their capital projects using current resources. There is a strong case for using more debt during a financial downturn. First, it will free up current resources for current operations. Second, interest rates are often favorable during a downturn, so using debt is a savvy decision. Third, there is a good argument that using more debt is fairer to citizens. Using

accumulated cash takes resources contributed by past and current citizens to buy an asset that will be enjoyed mostly by future citizens. A debt repayment schedule results in each generation of citizens covering some of the cost of the asset. A local debt management policy, including local measures of debt affordability, can help make sure the increased use of debt is done wisely.

- It will support cash flow forecasting and analysis. Cash flow analysis can estimate the timing of inflows and outflows based on historical characteristics of similar projects and align financing accordingly.
- Should the federal or state/provincial government make available funds to support infrastructure construction in local communities, your government will be ready to take part.

In addition to considering new assets, local governments should assess the condition of existing assets and facilities. This provides near-term benefits:

- It highlights the need to maintain the community's existing portfolio of assets. It might help convince decision-makers to direct limited resources away from buying new assets and toward maintenance and replacement, which will often be the savvier financial decision.
- It allows for better decisions about where maintenance and replacement could be delayed and where it can't.

Develop an equipment replacement schedule.

A replacement schedule for noncapital equipment such as computers and other small equipment will give forewarning of future cost increases in the cash flow analysis. A schedule will give the leadership team the ability to start thinking about where delaying replacement could be a viable option and where replacement is essential.

Improve fleet management. Examine the vehicles in the fleet to decide which ones are necessary. For example, during the 2008 Great Recession, one small city convened a cross-departmental team to check its fleet practices. The team discovered that many vehicles seized by the police department had become part of the city's motor pool. These "free" vehicles added huge costs because they required maintenance, and departments expected to replace them at the end of their life. The team determined which vehicles were necessary for city business and stopped adding seized vehicles to the fleet (and started auctioning them off). Also, look for ways to better share vehicles across departments. Reducing the idle time of the vehicles in your fleet will mean you will need fewer total vehicles. Finally,

optimize the replacement schedule for vehicles so that they are replaced before they start to cause the government excessive maintenance and repair costs.

Review opportunities to refinance debt at lower interest rates. Economic downturns are often associated with lower interest rates. Take advantage of these times to lower the cost of debt service with the help of qualified municipal advisors. Also, assess the risk associated with existing call or put options or variable interest debt. Warren Buffet famously referred to derivative products as "financial weapons of mass destruction," so know your exposure to potential damage.

Enhancing Revenues

Obtain federal and state/provincial aid. During the COVID-19 pandemic, local governments may be eligible for federal disaster relief funding and federal and/or state/provincial "stimulus" support. Understand the rules on how to access these funds and get the staff and/or consultant resources in place to secure the funding.

Beyond aid specific to the COVID-19 downturn, states sometimes have legal provisions for distressed local governments that can provide relief from costly regulations, give temporary grants and loans, and perhaps increase tax authority. Universities or quasi-governmental regional consortia may be able to provide low-cost technical support.

Examine fees for services. Fees are useful in helping local governments recover at least part of the cost of providing a service. Fees also help increase revenue diversity, which is why local governments should set up fees for services where applicable and regularly adjust these fees to keep pace with inflationary growth. That said, fees will need to be weighed against impact. For example, local governments may need to explore fee waivers as a way of supporting small businesses. Some fees are counterproductive. For example, there is a strong case to suspend criminal justice fees and fine collection where collection rates are low. The fees and fines impede people's ability to get through the criminal justice process.

To examine the potential for fees, make sure there are clear cost-recovery policy goals. Consider the definition of "cost." Are only direct costs or fully allocated costs considered? Verify that fees are meeting cost recovery goals. Compare your fees with comparable and area agencies to find out if they are reasonable. Check to see if your fee structure is having unintended consequences. For example, a fee might dissuade people from using a service that has communitywide benefits.

Fees that have a strong case for charging full cost include building, parking, recreation fees, and utilities.¹² A common

and often controversial area where fees are undercharged is fees to automobile and homeowner insurance companies for fire calls (especially false alarms), cleanup of hazardous materials, and nonemergency calls, despite the inclusion of such fees in most insurance policies. Other fees include those for services rendered to nonresidents or businesses, such as title searches, permit records, voter information, research, and “extras” on road construction or tree planting. Make sure that operating departments are incented to keep their fees updated and include a policy for regular reviews. Central user fee policies are an important first step, but tactics like connecting operating budgets closely to program revenues can also help. Otherwise, departments may not give fees attention or may be disinclined to raise fees (e.g., for fear of upsetting supporting constituents).

New taxes with a strong connection to a desired service.

New taxes are generally not something the public wants to pay during an economic downturn. However, sometimes there is a public service that is desired by the community, and citizens might be willing to pay to get it. Taxpayers will often be supportive of taxes that have a perceived close link to the benefit received.¹³ Furthermore, a service that benefits a narrow segment of the community is often paid for by members of that community. For example, many cities have set up a special tax area that assesses a tax for the upkeep of streetlights and sidewalks, which is paid for by local merchants. In another example, a large county set up snowplowing taxes for mountainous areas of the county that required this service, while desert regions did not pay the tax. In both examples, the taxpayers favored the tax because they value the service. That said, any successful new tax depends on the community believing the government is a credible steward of their money.

Improve billing and collection procedures. Improving billing and collection procedures is about receiving revenues that are rightly due to government. However, billing and collection must be sensitive to the hardships that citizens and local businesses face. A good place to start is to create a standardized process for how to collect revenues—including for cases of hardship. A consistent approach is the foundation of a fair approach. Next, make sure billing procedures are standardized for all receivables, including insurance claims, damage claims, rebates, and fees for service. Make sure nothing falls through the cracks due to lack of communication between departments and staff. Map out processes and find out where handoffs between departments occur and make sure these are working smoothly. Make sure this process identifies where cases of hardship are identified and

how they can be routed to the right staff members to make arrangements with the affected ratepayer.

Other considerations to improve billing and collections include:

- Certain types of fees, billing, and collections may be more appropriate to relax than others during the COVID-19 crisis. Look at the fees your government charges and decide where relaxed procedures make the most sense.
- Consolidate billing and collections with a purpose unit to achieve standardization and consistency.
- Investing in technology or people to improve collections and billings could pay off. An example is parking meters, where better technology and/or more staffing can often increase revenues. This is an example of spending money to make money.
- Look for ways to improve information sharing between agencies. For example, property tax records can be confirmed against utility bills, other agencies’ property tax records, and court records.
- Outsourcing aspects of collection to the private sector can provide financial benefit. But beware that the collection methods used in the private sector may not treat constituents in a way that reflects well on government, especially during an economic downturn when many people are vulnerable. For example, a tax lien sale sells tax liens to private investors and converts a nonliquid asset to a liquid one; however, it could also result in a citizen losing his/her primary residence.
- Consider an amnesty program for past due fees. Done well, an amnesty program brings in revenues and gives ratepayers a chance to remove a financial burden for a lower cost. To be effective, amnesty programs should be rarely offered and vigorously enforced.

Audit tax revenue sources. Many revenues are remitted to the government based on the self-reporting of tax liability. Often, liability is underreported or reported as due to the wrong jurisdiction (e.g., sales tax for a large retailer on the border of the community). Auditing can find new revenues. Personal property assessments beyond the minimum requirements of state law, sales taxes, and utility taxes are examples of revenues where audits can pay off. This is a fair way to raise revenues because it is meant to make sure that those liable are paying their rightful share. That said, the revenue available can vary depending on factors like the number of payers and the complexity of tax. For example, utility taxes are usually paid to the government by a small number of utility companies (not by each constituent), thereby limiting the number of payers to audit. Also, an audit can be time-consuming.

EXHIBIT 2

Overview of Primary Near-Term Treatments

Control Personnel Costs

- Vacancy control
- Monitor and limit overtime use
- Address health care costs
- Review the use of consultants and temporary staff

Enhance Purchasing Practices

- Many small opportunities add up

Review Ongoing Expenditures

- Audit routine expenditures
- Investigate risk management practices and workers' compensation claim patterns

Pooling Resources and Partnering

- Cooperate with other governments to achieve economies of scale
- Pool department resources
- Look for ways to partner with private organizations and citizens

Better Manage Capital Spending, Equipment Costs, and Debt

- Better align capital financing with project schedules
- Use long-term capital improvement planning to make better near-term decisions
- Develop an equipment replacement schedule
- Improve fleet management
- Review opportunities to refinance debt at lower interest rates

Enhancing Revenues

- Obtain federal and state/provincial aid
- Examine fees for services
- New taxes with a strong connection to a desired service
- Improve billing and collection methods
- Audit tax revenue sources



Evaluating the Use of Riskier Near-Term Treatments

The most obvious factor to consider when evaluating the need to employ riskier techniques is the size and nature of the projected deficits. How large are they? How quickly will they arrive? Will they grow over time or remain constant? Are there underlying structural issues that have been worsened by a crisis? Or will the government's problems end once the crisis does? Cash flow forecasting¹⁴ and scenario planning¹⁵ (see Step 4 of the 12-step process, Initial Diagnosis¹⁶) can help shed light on these questions. With any financial crisis, especially the COVID-19 pandemic, it is impossible to answer these questions with certainty. Even so, an analysis—presented with transparency around the assumptions and commitment to update as information becomes available—is better than flying blind.

Once you determine the likely size of the deficit—or better yet, outline different scenarios that suggest a range—then you can make decisions on how to address it, including techniques you will go to first and those you might save for later if the situation continues to deteriorate. As the name implies, Near-Term Treatments are not exhaustive of every treatment a government might need to regain financial health. However, they do provide a place to start. You can evaluate the potential of Near-Term Treatments according to the following criteria. A scoring sheet is available at the Fiscal First Aid website (gfoa.org/ffa) that summarizes these evaluation criteria.

Do we have the authority to do it? At first glance, these criteria may seem basic and not worth mentioning. However, research has shown that local governments consistently overestimate constraints placed on them by enabling legislation, other levels of government, and labor contracts.¹⁷ Local governments often underestimate their ability to change the constraints that exist. So, before ruling out a technique because you believe you don't have the authority, consider doing the following: Start by reading the letter of the law or the labor contract. You may find you have the authority after all. See if other governments—particularly those in the same state—are using the same technique you are considering. Check to see if there is clear, settled case law that mitigates the risk of future legal challenges. If the technique you are considering is truly not authorized, find out if state or federal agencies have the administrative authority to grant you leeway. You could also work with other local governments to lobby for change, but that might need to happen later—after you've bought yourself some time with other Near-Term Treatments.

What is the potential financial benefit? Estimate the potential cost reductions or revenue increases from Near-Term Treatments. Treatments that generate small or uncertain benefits can be set aside in favor of those that generate larger and/or more certain benefits. The estimate should consider the following:

- What is the projected benefit in the first year, factoring in time for implementation?
- What are the projected benefits over a multiyear period? How does the financial impact change over time? For example, a one-year base salary freeze creates savings in subsequent years when future salary increases are applied to a lower base. In contrast, revenue gained from increased parking fines may drop over time as compliance with the ordinance increases.
- What are the financial costs for implementation?

What is the service impact? Some Near-Term Treatments may reduce service levels. This could be an important consideration for services that are involved in responding to the COVID-19 public health threat. If your government has a capacity to measure and monitor the performance of public services, then evaluating service impact will be easier. If not, even basic data

about the demand for services that could be negatively impacted by Near-Term Treatments can be helpful, such as the number of emergency response calls, the number of patrons at libraries or recreational facilities, etc.

You can also consult with the managers of services that could be negatively impacted by proposed Near-Term Treatments. Seek to learn whether the impact will be felt in a small way across a large number of people or more pronounced in a smaller population. This is important for making sure that service cuts don't fall unfairly on certain groups of citizens and that vulnerable populations are not harmed.

Where possible, leaders should get input from the constituents most likely to be affected. Even in instances where financial needs outweigh service concerns, it is better to communicate the move ahead of time and give the impacted citizens a chance to be heard.

Finally, when Near-Term Treatments will reduce service, consider if there are ways to mitigate the impact. For example, can a service be provided at a reduced level rather than be eliminated? Can service be restored later? Are there less costly ways to provide service?

How feasible is implementation? Leaders should consider whether they have the time, staff capacity, technology, information, and other resources to implement a given Near-Term Treatment. For example, some fees may be hard to implement without adding staff to issue bills, collect cash payments, and pursue delinquent accounts. Other fees will be easier to implement where there is staff and a billing/collection process in place. Selling or leasing an asset may produce a financial benefit, but the process may also require an investment of time and professional expertise that is hard to muster during a crisis. Also, during the COVID-19 pandemic or a resurgence of the virus, it may not be practical for employees to work together—or for citizens to come into government facilities or engage in activities that would otherwise have been attractive options.

For each initiative, local leaders need to understand whether implementation will be limited or complicated by collective bargaining agreements. *A crisis can be an opportunity* to renegotiate terms under collective bargaining agreements. Always negotiate in good faith to maintain trust with employees.

Not Mandated After All— A Real-Life Example

Many years ago, a large city was faced with severe funding shortfalls. The city ran several homes for the aged. These were thought to be mandated, so they were initially exempted from the search for cost savings. However, a careful reading of the law revealed the city was only required to operate a single home. This did not lead to widespread elimination of the homes, but it did bring them to search for cost savings.



Will elected officials support it? Many Near-Term Treatments will have to be approved by a body of elected or appointed officials, either as standalone measures or as part of a larger budget. While a financial crisis is no place for sacred cows, elected and appointed decision-makers do not have an unlimited supply of political capital either.

Investing time and effort in developing strategies for which it will be almost impossible to win approval diverts resources from initiatives that may be politically palatable. This does not mean that certain strategies should be dismissed by uttering, “that will never pass.” But political consideration has to be part of how strategies are prioritized and how they are presented.

Politically challenging Near-Term Treatments could be considered if local leaders are able to make the case in a way that reflects the current conditions. That’s why assessing the nature and size of the budget hole is important, as are the recommended steps designed to gather data on the financial and operational impacts of proposed strategies. As important, by considering politically difficult alternatives, it may help the case for less draconian but still challenging steps.

With an evaluation framework in place, you are ready to consider the riskier Near-Term Treatments. We’ll start with the “cautionary” treatments, which present the least risk of those in this article.



The Cautionary Near-Term Treatments

The Near-Term Treatments in the cautionary category are riskier than the Primary Treatments we just reviewed. However, governments may have no choice but use them when in financial distress. Governments do need to be mindful of the risks these techniques entail and be ready to mitigate them. They have been put into the following categories: control personnel costs; reduce near-term capital spending, equipment costs, and annual debt costs; organizational strategies; sourcing strategies; and enhancing revenues. Exhibit 3 overviews the techniques in these categories.

Control Personnel Costs

Wage freeze. A wage freeze limits personnel costs without making employees worse off—meaning their nominal compensation is not reduced. This technique will be difficult where employees are covered by a collective bargaining agreement. Even if a wage freeze is possible, care should be exercised, as it might encourage capable employees to leave. It might also make it harder to recruit high-quality employees. That said, during high unemployment, these risks may be reduced.

One way to lessen the impact of a wage freeze on morale is for top management and/or elected officials to take a temporary pay cut for the duration of the wage freeze. This promotes a culture of frugality and a sense of shared sacrifice.

The Risks

- It may be hard to enact in a collective bargaining environment.
- Wage freezes may encourage staff, especially your best staff, to consider other employment options.

EXHIBIT 3

Overview of the Cautionary Techniques

Control Personnel Costs

- Wage freeze
- Hiring freeze
- Increase part-time labor
- Reduce hours worked and pay
- Close facilities
- Layoffs or reduction in force
- Increase employee contributions to pensions or OPEBs

Reduce Near-Term Capital Spending, Equipment Costs, and Annual Debt Costs

- Defer and/or cancel capital projects, maintenance, and/or replacement
- Defer noncapital special projects
- Use short-term debt to pay for vehicles
- Restructure debt

Organizational Strategies

- Small and/or temporary across-the-board budget cuts
- Reorganization
- Centralize financial management and human resources activities

Sourcing Strategies

- Outsource
- Insource
- Divest

Enhancing Revenues

- Revisit interfund transfer policies
- Obtain better returns on idle cash

- The broad nature of a wage freeze makes it harder to take a results-oriented and data-driven approach to recovery planning.

Hiring freeze. A hiring freeze is different from the vacancy control technique described under the Primary section. A hiring freeze is a blanket stop on all or almost all hiring. It will help control costs and can be used with an attrition strategy to cut the size of the workforce. However, a hiring freeze is a blunt instrument. Vacancy control, in contrast, is more akin to a scalpel and asks the recovery leadership team to consider holding positions vacant on a case-by-case basis. A hiring freeze makes it harder to take a focused approach on what to cut and what to keep. It is important to set up policies governing the hiring freeze, especially exceptions, and adhere to the policies, if possible, to avoid a lack of trust and morale issues.

The Risks

- The nature of a hiring freeze makes it harder to take a results-oriented and data-driven approach to recovery planning.
- Some exceptions to the freeze may be necessary. If these are seen as unfair or capricious exemptions, support for the recovery could decrease.

Increase part-time labor. This could transform labor into a variable cost and reduce benefits costs. Part-timers can also cut overtime costs by adding staff at times of peak demand. Part-timers can be a cost-effective way to help with temporary demands related to the pandemic,

even if overtime for full-time staff is not an issue. However, increasing part-time labor could increase exposure to risk. For example, part-time police officers may not have the same training standards as full-time officers or have the same familiarity with the community.

The Risks

- Be cautious when substituting part-time employees for full-time employees. Part-time employees may have less training, knowledge of the job, etc. This could increase the government's exposure to risk.
- Morale can be affected, depending on how the changes are viewed. For example, employees who are involuntarily changed to part-time status will still be part of the organization and may negatively impact work atmosphere.
- Collective bargaining agreements might limit the government's ability to use this technique.

Reduce hours worked and pay. A furlough or a change in work schedule [e.g., going from a 40-hour week to 35] can reduce personnel costs while providing employees with more personal time. This gives employees a reasonable trade-off: more personal time in exchange for reduced pay. The salary savings depend on how many furlough days are required of employees. Some cities have realized up to 10% in salary savings. This technique will reduce the cost of fringe benefits that are based on salary but will not impact other benefits, like healthcare, that are provided equally, irrespective of salary.

Similar to what we suggested under the wage freeze, to lessen the impact on morale, top management and/or elected officials could take a temporary pay cut that is about equal to the impact of the furlough on employees. Again, this promotes a culture of frugality and a sense of shared sacrifice.

The Risks

- Not all employees will value personal time and wages equally. Those who value wages more may become dissatisfied, lose productivity, create morale problems, or leave the organization.
- Consider the impact of reduced work hours on services. Is the government willing to accept lower levels of quality or timeliness for certain activities? Will some activities be discontinued?

Never Let a Crisis Go to Waste

A financial crisis may present an opportunity to take on sacred cows or other long-standing arrangements that some officials have realized is not a good use of public money but haven't had the motivation and/or opportunity to address up to this point. The financial recovery could provide the impetus.

Close facilities (or reduce hours of operation). This reduces costs by reducing the need for personnel to staff the facility and by reducing utility costs. Closures or reduced operations should be part of a strategic, prioritized approach to service reduction. Consider supplementing closings with availability of online options to mitigate service impacts. Online options could be important when in-person interaction becomes difficult under social distancing guidelines. Identify and evaluate service impacts with an emphasis on what alternatives are available when the office is closed. Thorough communication is needed before changes in hours to ensure a smooth transition.

The Risks

- Make sure that closings do not fall unfairly on vulnerable populations.
- Reducing hours of operation reduces costs only when employees are not paid for the time. Getting the most from this technique raises personnel issues (see the earlier technique of reducing hours worked).

Layoffs or reduction in force (RIF). A layoff or reduction in force (RIF) is different from reducing hours worked and pay because a RIF separates staff members from their jobs. Because personnel costs are a large part of most governments' cost structures, it may be necessary to cut the number of employees to cope with fiscal stress. A RIF can lead to significant and, perhaps, ongoing cost savings.

The Risks

- A RIF will be one of the greatest challenges to maintaining good morale of any of the Near-Term Treatments we have examined so far.
- A RIF could reduce service effectiveness more than most other Near-Term Treatments.

Increase employee contributions to pensions or OPEBs.

A short-term solution to growing liabilities for pension or other post-employment benefits (like healthcare) is increased employee contributions or retiree co-payments, deductibles, or premiums. Some jurisdictions may need to suspend retirement earnings credits during periods of distress (no pension benefits are accrued and thus no liabilities are created, thus no payments are required).

This technique runs the risk of compounding the burden on employees. That said, this may be more politically feasible if required employer contributions are increasing as a result of market losses.

The Risks

- The technique will be less politically feasible if employees are already enduring wage cuts, furloughs, etc.

- For most governments with organized labor, the contracts often run several years, and benefits changes are hard to negotiate.

Reduce Near-Term Capital Spending, Equipment Costs, and Annual Debt Costs

Defer and/or cancel capital projects, maintenance, and/or replacement. This is a relatively common strategy and can be useful. However, the government must be careful not to delay projects that are crucial to the viability of the community. In the primary techniques, we advocated for long-term capital planning and maintenance/replacement schedules for existing assets. This will help manage the risks associated with delaying or canceling projects.

When considering deferral/cancellation of capital projects, consider potential cost and revenue impacts. For example, perhaps a road project is needed to improve access to commercial areas, which would increase business activity and sales taxes. Identify the point at which delaying a capital project becomes fiscally unsound. For example, might the delay of a major road repair project require large-scale replacement reconstruction later? Lifecycle costing¹⁸ is a proven and powerful technique for identifying the most cost-effective point at which to maintain or replace an asset. Risk analysis¹⁹ can help determine the consequences of deferral.

The Risks

- This strategy is popular because it allows expenditures to be taken off the budget without impacting day-to-day services or staffing in the near term. Make sure that a delay of a capital project is not just a delay of the financial reckoning day; make sure that it won't negatively impact the operating budget.
- Risks associated with delay can include higher maintenance costs later, increased downtime, decreased productivity, extra costs to restart a project, violating the terms that grants used to fund the project, and perhaps decreased safety.

Defer noncapital special projects. Some projects can be costly and important but not necessarily urgent. For example, perhaps an update to a comprehensive land-use plan and master plan could be put off for a year or two without irreparable harm. Make sure to understand the potential consequences of deferring these projects. For example, will an out-of-date community master plan make it harder to make capital spending decisions or get grants?

The Risks

- Make sure that delaying the project won't create difficulties in other areas. For example, would deferring planning

projects make it harder to make wise decisions with community resources?

Use short-term debt to pay for vehicles. This spreads out the cost of these assets over many years. While this strategy offers breathing room, it must be paired with a policy that limits the life of debt to the life of the asset. Otherwise, the strategy comes dangerously close to issuing debt for operational expenses. Also, this strategy is limited to situations where the capacity for issuing debt exists. Otherwise, financial flexibility may be reduced.

The Risks

- The usefulness of this strategy will vary with the type of vehicles purchased and how many are purchased. For example, debt would be more helpful for a long-lived asset, like a fire engine, than for a short-lived one, like a pooled car that will be driven many miles each year.
- If the term of debt exceeds the life of the vehicle, then the government will have more serious financial problems.
- Bank loans and direct placements have similar disclosure requirements compared to traditional bonds. The government should discuss financing instruments with its municipal advisor.

Restructure debt. Payment schedules might be able to be changed to reduce financial pressure. Options for restructuring debt could include stretching out the term of the loan, backloading the principal repayment schedule, and making interest-only payments. In some cases, loan forgiveness may be possible. However, be mindful that even though extending the maturities of debt can provide a near-term cash flow fix, it can also increase total debt service costs over the life of the issue.

The Risks

- Beware of causing intergenerational inequity issues by stretching debt out past the life of the asset it is funding.
- Consider the operating impacts of debt restructuring on future budgets, especially when evaluating structures such as interest-only flexible payments and other shifts in payments over time. Backloading a debt issue with higher principal payments can be harmful to future years' budget conditions.
- Tight credit markets may limit the ability to use this technique.
- State/provincial law might limit the use of this technique. For example, the law might limit the allowable term of debt for local governments.
- Credit rating agencies will likely view the restructuring of debt for anything other than interest cost savings negatively.

Organizational Strategies

Small and/or temporary across-the-board budget cuts. Small across-the-board budget cuts can be as useful as a Near-Term Treatment because they enlist managers in the solution by giving them a target to meet. It is an uncomplicated and reversible tactic and is perceived as equitable. Also, it starts the conversation about how budgets can be reduced. For example, department heads could be asked to provide options for how their budgets could be reduced by different increments (e.g., a 5% cut versus a 10% cut).

However, across-the-board budget cuts have drawbacks—chief among them being that the reductions are disconnected from priorities. Rather than aligning spending with services, all services are provided at a lesser level. Therefore, if a small across-the-board cut is used to buy time, it should be followed by a planning and budgeting approach that better matches priorities and spending.

The Risks

- Be wary of overreliance on this tactic, as it eventually harms core services. See The Extreme Caution Near-Term Treatments for more discussion of this point.

Reorganization. Your organization structure could lead to higher expenditures if there is too much overhead, too many layers of management, too many managers per frontline staff person, etc. You can evaluate your organization structure for savings opportunities. However, be aware that research has shown that the savings available from reorganizations are often overestimated.²⁰ For instance, if a reorganization moves around the boxes on an organizational chart but doesn't impact the underlying processes or result in better use of staff time, then the benefit will be limited or nonexistent. Also, the managers of consolidated departments often demand higher pay, eating into the potential savings. Further, reorganization can elicit a great deal of internal resistance. That said, if there are opportunities available from using a reorganization to apply efficient processes and make use of human resources, it would be realistic to expect 2% to 3% in near-term savings and perhaps more over the long term.²¹

Start by diagramming processes and lines of communication. What is the reporting structure? Who approves what? Who is responsible for key steps in the workflow? Are there handoffs between employees or departments where work is lost or delayed, thereby increasing costs? Can certain tasks be done in parallel that are now done sequentially? Also, evaluate the ratios of supervisors to frontline employees. Are there too many managers per frontline staff person? Use benchmarking to compare with other organizations. See how many layers of

management there are between the chief executive and frontline staff. Explore ways to flatten the organization and/or combine departments where there are opportunities to reduce overhead. Positions and the size and complexity of the organization—not promotional opportunities for long-time employees—should drive the administrative structure of any department.

Restructuring might be useful for correcting systems that contributed to financial distress and may be required as a prerequisite for far-reaching reform. For example, perhaps certain kinds of decision-making authority need to be more centralized to make faster changes. Or perhaps lower levels of management need to be empowered to make other kinds of decisions.

The Risks

- The potential savings of reorganizations are often overestimated.
- Reorganization can elicit a lot of resistance from people who lose power and authority in the new structure.

Centralize financial management and human resources activities. In a crisis, it is important to have an understanding of and control over inflows and outflows of cash. This could mean personal review of proposed expenditures by the CFO (in a small government) or by centralized finance staff until the emergency has passed. Not only will centralization slow the rate of expenditure, but it will also give the CFO a better understanding of spending patterns and may highlight problems that make financial challenges even more difficult. Centralization can also improve working capital by rounding up cash from decentralized divisions and dormant bank accounts. After the emergency has passed, responsibilities can be redistributed to emphasize accountability and teamwork.

Concerning human resources, only the largest and most service-diverse organizations call for human resources staff in each department to address grievances and administer needed process variances. Centralized HR will help create consistency in personnel policies and practices throughout the organization, which is important, as fiscal distress may require personnel actions.

Centralization strategies may reduce headcount by eliminating duplicate positions and tasks in departments. The trade-off is that centralized resources will have less knowledge of departmental operations, so they might be less effective at serving departments in certain respects.

However, centralization is not necessarily a good long-term strategy. Even in the short term, it could reduce the organization's ability to respond quickly to on-the-ground emergencies. It risks limiting the ability of the

organization's best managers to do their jobs. Many of the same benefits can be achieved with the right information technology. For example, a good control system ensures spending does not exceed defined parameters—without requiring centralized staff to manually review the transactions. Modern IT systems also can give the finance office up-to-the-minute spending information without having to implement more centralized controls (which might increase nonvalue-added overhead).

The Risks

- Centralization may make the organization less nimble, which is important to consider in a public health crisis.
- Centralization fails to make the best use of the organization's talent outside of the centralized functions. For example, the best managers outside of the centralized functions will not be able to realize their full potential. This works against making managers manage.
- Many of the same benefits can be had from using modern information technology to create real-time controls on spending without the need for human intervention.

Sourcing Strategies

Outsource. Many public officials consider outsourcing as a way to cut costs. However, cost savings are far from guaranteed. For financially stressed governments, a first step is to look at services where the private sector market for a service is stable. *Benchmark* to see what services other governments outsource. This will help reduce risk.

Studies have shown that outsourcing does not always save money. You can evaluate outsourcing opportunities against several key criteria for realizing cost savings from outsourcing. Be specific in defining the service requirements and expectations so that service quality and quantity are as expected.

One way to ensure a cost-beneficial outcome from outsourcing is to use partial provision of the service by public employees as a “check and balance.” For example, years ago, one large city outsourced half of its waste collection by moving existing union staff to one side of the city and outsourcing the other half. This allowed the government to compare the costs and productivity of outsourced versus insourced collection. The private sector had to prove that they continued to be a low-cost alternative. This provided protection against the risk of vendor “lock-in,” where an incumbent provider gains a huge advantage over other providers.

The Risks

- Make sure outsourcing is cost beneficial over the full term of the contract and possibly longer. For example,

some vendors pursue a “loss leader” strategy, where they offer a service at an artificially low initial cost with the intention of making it back (and maybe more) later in the deal or subsequent deals, if it will be too expensive for the government to switch providers.

- Getting savings from outsourcing often requires giving up control of how the service is provided. For many public services, it might matter how the service is provided. For example, the fair treatment of all constituents is an important characteristic of how a service is provided.
- Outsourcing can be hard to undertake in a unionized environment.
- Outsourcing usually entails start-up costs (political and economic) so the cost-benefit decision should consider these.

Insource. In some cases, private contractors may be more expensive than public employees. Examine services that are outsourced now and compare them to the criteria for outsourcing cost savings. If the criteria are not met, then there is a chance that insourcing could be cost beneficial. Even if insourcing is not cost beneficial, the government can avoid the pain associated with reducing the cost of public employees by reducing the money spent on contractors and then having public employees take over the work. For example, a lot of design contracts are entered into because the government staff lack capacity to do the work. If staff now have more time, those contracts could be canceled and the work done by staff.

The Risks

- If contracting was the most efficient arrangement before, having public employees do the work may be a step backward on the road to a strong financial foundation for the local government.
- Depending on how much flexibility the local government has in its labor structures, it might be challenging to outsource the service again in the future.

Divest (or at least temporarily halt) subsidized enterprises.

Governments sometimes get into business-like activities that don't cover their own costs and have to be subsidized by the general government. This siphons tax dollars away from general services. Examples include airports, golf courses, or parking garages. Divesting these activities or putting a temporary stop or a slowdown on their operations can stop the losses and may generate revenue through the sale of assets and/or putting the property back on the tax rolls. Divesting or halting subsidized activities is often done through a data-driven and results-oriented budget process. Such a process allows decision-makers to consider what is important as core services of government—and to weigh the

value of the enterprise against other services that compete for funding.

The Risks

- Certain types of loss-generating enterprises might be politically sensitive because the clientele of the enterprise will resist losing their subsidy.
- If a government tries to sell an enterprise to a third party during financial stress, it may not be negotiating from a position of strength.

Enhancing Revenues

Revisit Interfund Transfer Policies. A distressed government could reexamine its policy for transfers to the general fund from other funds (particularly self-supporting enterprise operations, such as utilities) to see if there is a basis for increasing the amounts transferred. Perhaps the general fund has been unintentionally subsidizing the activities of other funds. For instance, perhaps the other funds have not been paying the full cost of technology services, insurance, or other support services. Such a strategy must be pursued carefully, though, in case it degenerates into unjustified subsidization of general services at the expense of the clientele of these other funds.

It could be that the general fund is subsidizing other funds, thereby causing a drain on general tax dollars. It may be worth revising these policies to see if the policy should continue.

The Risks

- This can be a risky technique because cross-subsidization is a quick and easy fix to financial woes within a fund. There may be good reasons for revisiting subsidization policies, but the policies must follow sound financial reasoning.

Obtain better returns on idle cash. Better investment strategies could provide new revenue, but chasing yields could increase risk. The opportunities are probably going to be limited in an economic downturn. Consider benchmarking investment return performance against a conservative standard. Make sure there is a comprehensive investment policy in place to guide decisions. Look at investment pools that exhibit strong, stable histories and are affiliated in some way with many governments.

The Risks

- Chasing yields could increase the risk to principal. At best, a higher yield strategy will probably require investing in less liquid assets. Liquidity could be especially important during a downturn.
- In an economic downturn, the benefit of this technique will probably be limited and undependable.



EXHIBIT 4

Overview of the Extreme Caution Techniques

Reducing Expenditures

- Large or sustained across-the-board budget cuts
- Across-the-board wage cuts
- Defer compensation
- Offer an early retirement program

Enhancing Revenues

- Levy a broad tax increase
- Create an independent special district with its own taxing authority
- Long-term borrowing without a supporting re-source for repayment
- Tax anticipation notes

The Extreme Caution Near-Term Treatments

The techniques described here are riskier than those listed in the cautionary category. Though they could be viable options for distressed governments, they should be among the last options considered. These techniques have been categorized into expenditure reductions and revenue enhancements. Exhibit 4 overviews these techniques.

Reducing Expenditures

Large or sustained across-the-board budget cuts.

We listed small or one-time across-the-board cuts as a “cautionary” technique. Expanding the use of these cuts evaluates it to “extreme caution.” Across-the-board cuts have a cursory sense of fairness because they “spread the pain” equally. However, this assumes that all services are of equal importance to the citizens and that programs have equal ability to absorb cuts.

Across-the-board cuts usually reduce the value created by public services. This problem is amplified when the cuts are large or when they are repeated. Reduced value lowers citizen opinion of the government, making it harder to gain support for constructive reform. Also, vulnerable populations are more likely to be hurt when programs are cut indiscriminately.

The Risks

- Local government misses the opportunity to plan cuts and size and shape programs to fit the current environment.
- The important services are cut as much as the less important services.
- Sometimes the notion behind across-the-board cuts is that departments can “cut the fat.” However, this rests on two dubious propositions: First, that the “fat”

is equally distributed; it probably isn't. Second, that managers know how to find it. The less skilled managers probably have more fat in their programs and are less able to find and eliminate it.

Across-the-board wage cuts. Across-the-board wage cuts are seen as riskier than the other Near-Term Treatments to reduce personnel costs that we have reviewed so far. First, though some of the other techniques we have seen earlier also reduce pay (e.g., furloughs, reduced schedules), they also compensate employees with personal time. Across-the-board wage cuts don't provide this, at least partially, offsetting gain. Hence, the cuts will provoke more resistance than these other techniques, especially in a unionized environment. Second, across-the-board cuts are untargeted. Reducing everyone's wages by the same amount could drive off the local government's best employees.

The Risks

- Across-the-board wage cuts are harmful to morale and could drive off the best employees.
- Similarly, this technique would create more resistance than other techniques to reduce personnel costs.

Defer compensation. If a local government doesn't have the funds to compensate employees in the current period, then some of that compensation can be deferred to future periods. Examples include post-retirement health benefits or increased pension benefits. However, this only defers the financial reckoning day and can create large liabilities that hit the budget sooner than people may have expected. This is a slippery slope and can be difficult to reverse. If this technique is going to be considered, a government must use data like other post-employment benefits (OPEB) liability and pension funding ratios to disclose and analyze the cost and impact of deferred compensation.

The Risks

- Deferring compensation creates future liabilities, making it harder to achieve a long-term, solid financial foundation for your government.
- This doesn't just "defer" costs; it increases total costs when considered over a multiyear period.

Offer an early retirement program. An early retirement program (or early retirement incentive) is simple in concept but realizing savings can be complicated. The government must figure out how to redesign its work to reduce the number of positions. Otherwise, if all

the positions are filled with new employees, then the government will again be in a position of unaffordable personnel costs. Further, this practice often shifts the costs to the pension fund, which will be repaid by the employer—along with interest rates that are often much higher on average compared to other kinds of debt governments have access to. Finally, veteran employees often have valuable knowledge. If they take the earlier retirement system, the government loses this knowledge and incurs the cost of replacing it or operating without it.

The Risks

- Many early retirement plans are more costly than a budget alone reveals. These programs can increase long-term costs associated with pension contributions and retiree healthcare coverage. These may not be paid directly from the operating budget or are masked in the total contribution rate. This makes their negative impact on a government's financial condition harder to see.
- Work processes must be redesigned to reduce the need for personnel. Replacing retired employees with lower-cost junior employees may result in short-term savings. Structural imbalances will be perpetuated.
- The employer can have difficulty predicting who will take the incentive, making the financial and operational impact harder to predict.

Enhancing Revenues

Levy a broad tax increase. While a broad tax increase is fair—everyone pays—it may not be in the best long-term interest of the government. It could reduce citizen support for the government, hurt economic competitiveness, and remove pressure for needed reform. It is essential to evaluate all legal and economic implications of a proposed tax increase. If a tax increase is a necessary part of the recovery, consider a targeted tax increase that is aligned with services that citizens want, as described in the earlier Near-Term Treatment about new taxes with a connection to the desired service.

The Risks

- A broad tax increase may not be affordable for the community, especially in an economic downturn.
- Broad tax increases generate much less public support than tax increases that are aligned with services that the public finds valuable.
- A broad tax increase should not be used as a way to escape other needed reforms.

Create an independent special district with its own taxing authority.

Special districts are units of government separate from general purpose local governments, with their own governing board, elections, etc. In some cases, special districts have been used to get around tax limitations on general purpose government by creating a new unit of government, with its own taxing authority, and shifting service responsibility to the new unit. This is different from the Near-Term Treatment we described earlier about aligning taxes with valued services through a taxing district. This is because the taxing district is under the control of the governing board of the general purpose local government. This helps maintain accountability to the public for public spending. Creating an independent special district could be acceptable if the public has a demand for the service that the district would provide, but if it is an alternative way to raise taxes, then it might work against the long-term health and livability of the community.

The Risks

- Creating special districts increases government fragmentation, thereby increasing the total cost of government to the public.
- Fragmentation makes it hard for the public to understand their government, perhaps eroding their support.

Long-term borrowing without a supporting resource for repayment.

Debt can be useful during a financial recovery for freeing up cash in the near term. For example, if a government was going to use accumulated cash to pay for an asset, then the debt could be used to spread the payments out over time, creating more financial flexibility. This strategy becomes riskier if there is no underlying support for repayment of the debt, in the form of accumulated cash or a dedicated revenue stream for repayment (e.g., like is often associated with general obligation bonds). Without support for repayment, debt may harm your ability to balance future budgets.

The Risks

- Debt without a supporting resource for repayment will make balancing the budget in the future difficult.
- Becoming overindebted will harm a government's credit rating, leading to higher interest rates and financial problems.

Tax anticipation notes (TANs). TANs are a form of short-term debt that local governments can use to receive an injection of liquidity, with repayment based on tax revenue that is anticipated later in the year. Normally, TANs are used only by governments that have mismatches between the timings of their inflows of cash and their outflows. For example, a government that is dependent on property taxes might receive the majority of its revenues during just a few months of the year, when taxes are due. However, it likely spends its budget in even monthly amounts during the year. During an economic downturn, more governments might find themselves with a mismatch between inflows and outflows and take an interest in TANs to provide relief, especially if internal sources of working capital are exhausted.

The Risks

- TANs are a form of borrowing for operations, which means the local government is accruing interest costs to pay for operations.
- It is not impossible that during the uncertainty associated with the COVID-19 downturn that fewer tax revenues could be received than was expected. This would complicate repaying the debt.
- Given the uncertainty associated with the COVID-19 downturn, it is not inconceivable that the market for short-term debt could behave abnormally. This might make TANs a less reliable technique than under normal economic conditions.

EXHIBIT 5

Overview of Inadvisable Treatments

- Underfund accrued liabilities like pensions
- Pension obligation bonds
- Default on debt
- Shift operational costs into capital budgets
- Dilute/dismantle internal controls
- Use accounting manipulations
- Have an asset “fire sale”



Inadvisable Near-Term Treatments

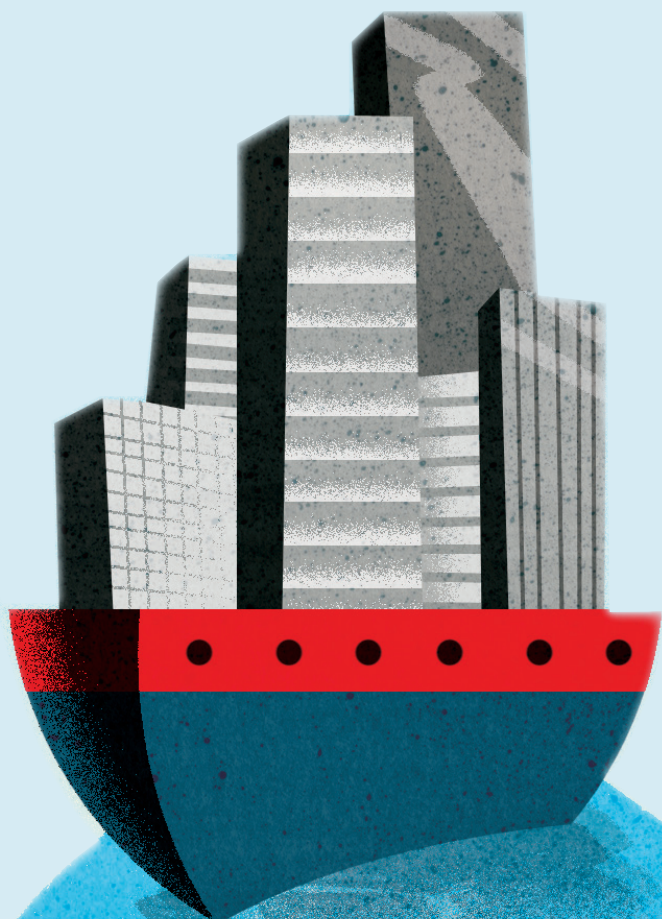
These are the riskiest techniques. They have great potential drawbacks. Exhibit 5 overviews the inadvisable treatments.

Underfund accrued liabilities like pensions. The government can use its available resources to fund current obligations rather than future obligations. For example, pension contribution “holidays” can preserve cash but will likely have long-term costs. This is because of the foregone investment income the government could have had by making its contribution during depressed market levels and “buying low.”

The Risks

- This is a way of sticking tomorrow’s generations with today’s tab.
- This can create negative repercussions on bond ratings, public perception, and employee relations as well as large liabilities that impact future budgets—and probably sooner than people expect.
- It is a lost opportunity to “buy low” and pay off liabilities during opportune market conditions.

Pension obligation bonds. In a regular economic climate, governments should avoid issuing pension obligation bonds (POBs). POBs are issued to fund the underfunded portion of pension liabilities. This involves investment risk and requires timing of the market. Public finance officers (and few other people) can successfully time the market. While economic downturns present market opportunities, governments should look elsewhere for cost savings.



The Risks

- POBs are complex financing instruments that must be scrutinized.
- Proceeds might fail to earn more than the interest rate owed over the term of the bonds, leading to increased liabilities.
- POB issuance may not be viewed as credit positive by rating agencies and market investors, given their inherent risk.
- Beware of causing intergenerational inequity issues, as POBs are often structured in a way that defers the principal payments or extends repayment over a period longer than the actuarial amortization period.
- GFOA has an official advisory recommending that state and local governments do not issue pension obligation bonds.²²

Default on debt. A government could refuse to pay back creditors in whole or in part. That would save the cost of the debt payments but would likely eliminate or curtail the government's ability to access the market in the future.

The Risks

- The government may not be able to access the debt market in the future, limiting its ability to build capital assets.
- At the very least, creditors would demand higher interest rates, increasing the cost of borrowing.

Shift operational costs into capital budgets.

Governments can inflate the budgets of capital projects to carry operating and maintenance costs for a time.

The Risks

- This distorts the true cost of capital investments and makes governments vulnerable to unsustainable operating and maintenance costs when the capital financing runs out.
- This is not permitted under some state/provincial laws, which require operating expenses to be paid from operating revenue. Even if it isn't illegal, using this technique endangers the organization's credibility and its ability to return to good practices in the future.
- If the capital program is supported by debt, there are restrictions on what the proceeds can be used for outlined in the debt offering documents.

Dilute/dismantle internal controls. Some temporary advantage might be gained from ignoring (or dismantling) important internal controls. For example, perhaps there would be saving in staff costs by not separating duties between as many staff people so you could operate with a lower headcount. However, this establishes a bad precedent and opens up the door to fraud. The risk of fraudulent activity generally rises during times of crisis. Unscrupulous people may suspect that controls and monitoring may be reduced and/or people may be placed in decision-making roles that they do not normally occupy.

The Risks

- Internal controls exist to prevent fraud, waste, and abuse. Without proper controls, the government risks incurring fraud, waste, or abuse exceeding the cost to operate the controls.
- Even beyond a simple cost/benefit analysis, any instance of fraud, waste, or abuse will decrease the credibility of management, making it harder for them to lead the recovery process.

Use accounting manipulations. Accounting practices can be manipulated to disguise the nature and magnitude of the problem. Examples include delaying deliveries, payrolls, and payments to the next fiscal year, manipulating or distorting estimates or forecasts, or recognizing anticipated (or even worse, speculative) savings or revenues.

The Risks

- This only makes the problem worse by creating a culture of unaccountability and delaying the recognition of the problem.
- "Accuracy above balance" is the fundamental rule of budgeting. If the budget is balanced but not accurate, it is not balanced!
- Future trust and credibility and the ability to manage is damaged by false or misleading information or by the perception of intentionally being misinformed.
- Condoning the use of accounting manipulations is a step toward deeper corruption and malfeasance.

Have an asset "fire sale." Normally, selling or leasing assets to a third party can work if assets are underutilized or if the government has made a decision to leave the associated line of business. Selling or leasing land (or other types of facilities) could generate

ongoing revenue by putting the property back on the tax rolls or adding an ongoing lease payment to the revenue budget. However, at the point of applying Near-Term Treatments, a local government may be desperate for financial relief and find little demand for the assets. This can lead the government to accept prices below the actual value of the asset. Worse, the government could be in a position to have to repurchase the assets later. For instance, it may not be advisable to sell or lease away parcels of vacant land that might be needed for the expansion of government facilities in the future.

The Risks

- A government may be in a poor negotiating position and/or not have the time to plan a sale or long-term lease during a financial crisis. “Fire sales” can lead to a perception of mismanagement.
- It may be hard to determine the fair price of a public asset with no clear market analog, especially under the stressful and time-constrained conditions associated with applying Near-Term Treatments.
- An asset sale is a one-time revenue. Normally, leasing would be a better option to generate a continuous revenue stream and to maintain ownership over the underlying asset. If one-time revenue is all that can be obtained, be sure the revenues are used to create a permanent solution, not just plug holes in the budget that will open up again next year.

Conclusions

The primary Near-Term Treatments are your lowest risk options to reduce costs and enhance revenues in the near term. By creating the right decision-making environment and putting in place the right management disciplines, you can get the most out of these techniques. However, the primary techniques alone might not be enough to address your local government’s financial challenges. The Riskier Treatments in this paper can help reduce expenditures or enhance revenue but present risks in doing so. By evaluating these techniques and being aware of the risk, you can get the most out of the techniques while limiting your risks. ■

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- ¹ <https://www.gfoa.org/detail/step-8-long-term-treatments>
- ² <https://www.gfoa.org/detail/step-4-initial-diagnosis>
- ³ <https://www.gfoa.org/detail/step-9-long-term-financial-planning>
- ⁴ Find ideas for these kinds of short-term cost-cutting techniques in the June 2020 *Government Finance Review* article “Cash is King.”
- ⁵ <https://www.gfoa.org/materials/webinar-managing-cash-flow-crisis-4-24-20>
- ⁶ <https://www.gfoa.org/materials/webinar-reserves-how-much-4-30-20>
- ⁷ Ibid
- ⁸ However, a government would not want to allow departments to move money from non-personnel to personnel expenditures because personnel expenditures are much harder to reduce in subsequent budgets.
- ⁹ For more information on this research, please consult: Shayne Kavanagh and Vincent Reitano. *Financial Foundations for Thriving Communities*. (Government Finance Officers Association: Chicago, IL). 2019.
- ¹⁰ <https://www.gfoa.org/materials/controlling-health-care-costs-with-dependent-eligibility>
- ¹¹ <https://www.gfoa.org/materials/getting-the-most-for-your-asset-management-money>
- ¹² With the exception of making arrangements to accommodate utility customers who are facing financial hardship.
- ¹³ <https://www.gfoa.org/materials/new-taxes-that-work>
- ¹⁴ <https://www.gfoa.org/materials/webinar-managing-cash-flow-crisis-4-24-20>
- ¹⁵ <https://www.gfoa.org/materials/webinar-financial-scenario-planning-4-8-20>
- ¹⁶ <https://www.gfoa.org/detail/step-4-initial-diagnosis>
- ¹⁷ Frederick M. Hess. *Cage-Busting Leadership*. Harvard Education Press (February 1, 2013).
- ¹⁸ <https://www.gfoa.org/materials/getting-the-most-for-your-asset-management-money>
- ¹⁹ <https://www.gfoa.org/materials/risk-aware-infrastructure-maintenance>
- ²⁰ Note that we are not referring to eliminating lower priority programs or closing underutilized facilities as part of a “reorganization.” Reorganization refers to streamlining reporting structures, reducing overhead, etc.
- ²¹ Reorganization research was popular during the 1980s when this was a common response to financial distress. A survey of the research from this period is available in: James Conant, “Reorganization and the Bottom Line.” *Public Administration Review*, Vol. 46, No. 1 (Jan. – Feb., 1986), pp. 48 – 56.
- ²² <https://www.gfoa.org/materials/pension-obligation-bonds>