Reinventing Government
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Reviewed work(s):
Published by: M.E. Sharpe, Inc.
Accessed: 05/03/2012 00:20

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Reinventing Government

David Osborne

What have you changed that has changed everything else?

When people hear “reinventing government,” their first thought is that I am referring to the federal government. But the solutions to our country’s problems are not coming from Washington, D.C. They are coming from state and local governments all around the country. They are coming from the kind of people who have won Exemplary State and Local awards.

Fiscal pain has been intense, and the sad thing is that the pain is not going to go away, even when we come out of this recession. The fiscal problems are due in part to the recession and in part to spending that is out of control. Two of the largest expenditures items in state government are Medicaid and corrections. Medicaid costs have gone up 20 percent a year. Corrections costs have nearly quadrupled in the 1980s. The demand for these services will continue to grow as our population and prisons age.

We are in for a decade of excruciating pain at state and local levels. The federal government is facing huge deficits, yet it continues to mandate services at state and local levels without the money necessary to deliver these services.

The federal deficit this year is $350 billion; next year it is projected at $400 billion. I think we have lost sight of what that means. Indexed for inflation, this $400 billion deficit would be the size of the entire federal budget in 1964. The interest payments on the debt are over $200 billion a year. That means the average American family is paying more than $3,000 a year in income taxes on the interest alone. By the year 2000 it will be $5,000 per family before we get a penny’s worth of government from Washington.

The public is frustrated, angry, disgusted, and ready for change. A CBS News poll in late May showed that 51 percent of respondents believe that the federal government needs “fundamental changes”; another 34 percent believe it needs “a complete rebuilding.” In other words, 85 percent of those polled believe fundamental change is needed in Washington. As a result, every politician in America is desperate to find new ways to operate. Providing more services with fewer dollars is what productivity is all about.
Government today consists of a lot of very dedicated people trapped in bad systems—budget systems that provide incentives to waste money, personnel systems and civil service systems that are cumbersome and provide little incentive. These systems and others must be changed if government is to improve its performance.

But what has been done instead? Governments cut services that are politically vulnerable. That is similar to someone cutting off a few fingers and toes instead of going on a diet to lose weight. Unfortunately, at the local level we are beyond fingers and toes: we are up to our hands and feet, and it is getting very painful.

The task is to make government more productive, do more with less, without cutting off our hands and feet. The first step is to identify the underlying problem. Why did government become so bloated and ineffective? The answer is fairly simple. It has, of course, many parts, but one reality underlies most of them, and it is a commonsense reality: we are doing business in an outmoded way.

Remember that the systems we are frustrated with, public housing or public education, for example, actually worked when they were first created. Some worked very well. But that was fifty or a hundred years ago, and the world has changed. Unfortunately, too often the public sector does not change.

Think about the way public institutions were created during the industrial era. Typically, there was a big problem to solve; a public program was set up to solve it; bureaucracy grew; civil servants were hired to deliver services. All this was done in a very top-down, hierarchical fashion, with a great many rules and regulations. The approach was very impersonal. Delivering standardized services to a mass market—the same kind of education for every child, the same kind of welfare check for every poor person—was considered the right way to do things, the fair way to do things.

Professionals and bureaucrats had all the control, and the people they served were dependent on them. Monopolies were created that had no competitors and therefore began to take clients for granted. Clients became captives; over time their needs changed, but the monopolies did not.

This is a rough outline of the way government did business in 1940. At the time it was the modern way; it was how the private sector delivered services, the General Motors organizational model. Today the bureaucratic monopolies function inefficiently. Envision these top-down, centralized, bureaucratic monopolies in a period of rapid change. Think of the pace of change, the technologies we have all become accustomed to, from personal computers and electronic mail to fax machines, automatic tellers, and cellular phones. These technological changes have an enormous impact on government.

When the postal service was created, the only way to communicate with
distant persons was to send a letter. Then the telegraph was invented, then the telephone, then satellites, fiber optic cables, computers, and modems. One public monopoly managing that communications marketplace today is unthinkable. Under the competitive pressure of all these technological advances, public monopolies are coming apart at the seams.

Society is being transformed not only by technological changes but by social changes as well. Consider how rapidly two-income families and single-parent families became the pattern. Only 27 percent of households in the United States today still fit the traditional definition of a family. A generation ago we were a mass society. People watched three television networks and read three news magazines. They looked at and read and talked about the same things. Today we have become used to hundreds and hundreds of choices. In the public sector, however, one size still fits all. Choice is something that must be addressed in the public sector.

In this environment of rapid change, the old top-down bureaucratic monopolies delivering standardized services are not effective. To be effective today, an organization must be lean, fast on its feet, responsive to its customers, capable of adjusting to constant change, able to improve productivity continually. In other words, it needs to be entrepreneurial rather than bureaucratic.

*Entrepreneurial* does not mean “for profit.” The word is far broader than that. An entrepreneur shifts resources out of an area of low productivity and minimal yield into an area of higher productivity and greater yield. Is that something public managers can do? Absolutely. It applies to public sector, it applies to nonprofit sector, and it applies to private sector. It is exactly the challenge the private sector has been struggling with for ten years.

Ten years ago, during the last recession, the book *In Search of Excellence* was published. It talked about restructuring a corporation to make it effective again in a radically new environment. It launched a decade of effort. The excellence movement and the total quality management movement were introduced as efforts to restructure corporations, to make them more entrepreneurial, more flexible, more decentralized. That movement was designed to empower employees, introduce quality circles, measure performance, and focus on quality.

In the current recession, ten years later, we are beginning finally to wake up to the necessity of doing the equivalent in the public sector. The tough question is, how do you do it? How do you take a bureaucratic system and transform it into an entrepreneurial system? To answer this question Ted Gaebler and I spent five years traveling around the country, examining the most entrepreneurial public organizations we could find. We looked at state agencies, school districts, and public housing authorities. We looked at parts of the Pentagon. We asked a very simple question: “What have you changed that has changed everything else?”

We found ten principles that underscore how public entrepreneurial
organizations structure themselves and move from centralization to decentralization, from monopolies to competition, from bureaucratic mechanisms to market mechanisms, from funding inputs to funding outcomes or results. All ten principles need not be present in one agency; in fact, usually they are not. In most entrepreneurial organizations, however, we typically found at least six simple, commonsense principles in practice.

Catalytic Government

The first principle, probably the most basic, we labeled "catalytic government." It embraces the idea that government should steer rather than row. In the old bureaucratic model, to solve a problem, a bureaucracy was created and staffed by civil servants, and they delivered the public service. That is a fairly expensive way to do business.

To do its job, the government need not always raise taxes, hire more people, or deliver more public services. There are alternatives. We identified thirty-six alternatives to traditional public service delivery already in use in this country. To manage a flexible organization, it is necessary to incorporate some of these alternatives.

It is very difficult to change a big organization if inefficient employees must be retained because of their civil service status. In that situation, a business would become captive to a sole source supplier for its most important resource. No business does that, and governments should not either. Government needs to separate steering from rowing so that those who are steering have some flexibility.

Competitive Government

A related principle is that of competitive government, of injecting competition into service delivery. The old model uses monopolies. The new model, increasingly, uses competition. Competition is a fundamental force that leaves the organization no choice but to heighten its productivity.

One of my favorite examples comes from Phoenix, Arizona, where in 1978, during a tax revolt, the city council decided to contract out garbage collection. The manager of the department of public works, Ron Jensen, decided he wanted his department to bid on the contract along with the private carters. Competition from outside vendors was the incentive the department needed to increase its productivity and efficiency.

Managers began by evaluating their equipment and found that it was outmoded. They experimented with one-driver trucks equipped with automatic side arms that picked up the garbage. Then management, realizing that drivers knew where the slack was and where productivity could be improved, asked the drivers to redesign the routes. The department created quality circles, labor-management committees to improve
communications, and bonus and awards programs to provide incentives. By 1988 the department of public works won back the contract and was able to provide sanitation services for the entire city at half the 1978 cost.

**Mission-Driven Government**

The third principle is that of mission-driven government. Public organizations are driven by two things—rules and budgets. We found that entrepreneurial organizations tend to minimize the rules and focus on their mission. They ask very basic questions: "What is our mission? What is our goal? What are we trying to accomplish?" Once goals and missions are clear, managers are allowed to manage. Entrepreneurial organizations let the managers determine the best way to accomplish their agency’s mission.

The traditional line-item budget system incorporates rules that encourage managers to waste money. In the traditional line-item system, money is cut up into many parts, and it is often difficult to move it from one line item to another. If every penny in every line item is not spent every fiscal year, it is lost and less money is allocated the following year. The built-in incentive is to waste money.

There is a very simple solution, which, to the best of my knowledge, was invented in Fairfield, California. With the passage of Proposition 13, Fairfield lost a quarter of its revenue overnight. Out of desperation, the city decided to change its budget system: Line items were eliminated and each agency was assigned a budget number. Agencies were allowed to roll over unexpended money from one fiscal year to the next. This change saved Fairfield millions of dollars.

Another very positive outcome was the change in the behavior of managers and employees. Empowering the manager and employees to design their own budgets enhanced motivation and creativity. Budgets soon reflected the mission and needs of the agencies; they were no longer dictated by line items or by individuals far removed from agency operations.

**Results-Oriented Government**

With the elimination of line items comes the question, How do we hold managers accountable? The answer is that, to make this work, we must also embrace the next principle: Accountability must shift from inputs, such as line items, to outcomes and results. We need a government that measures the results of what an agency does, and ties incentives to achieving those results.

Most public agencies do not have the slightest idea what the real outcomes of their efforts are. They cannot tell what they are buying with their money—how much students are learning, how clean their streets are, what impact "environmental protection" is having in the world.
Entrepreneurial governments have learned to measure the outcomes of what they spend—how clean their streets are, how many job trainees get jobs, and what their career tracks look like. They have learned to measure how satisfied their customers are with the transit system, the parks, and the schools.

Sunnyvale, California, in the Silicon Valley and full of computer experts, is an example of a city that has put all these principles together. They started about twenty years ago to measure everything, and they know the efficiency and cost-effectiveness of everything they do. As a result, the city council no longer has to vote on line items; they vote on service levels. They decide what service level to buy.

Take, for example, streets. Suppose one-third of the streets are in bad condition and a third of streets are in fair condition. Councilmembers want to get half of the streets in good condition in the next biennium. They ask the staff, "How much would that outcome cost?" The staff tells them, and they decide whether to buy it and how much of it to buy.

Or let us say that they have a customer survey in which 70 percent of people give positive approval ratings to city parks and recreation programs. They decide they want to raise that rating to 80 percent. They ask the staff, "How much would that cost?" The staff comes up with the number and the city decides whether to buy. Now an incentive has also been created.

If you are a manager whose unit has a certain performance target, and you exceed it, you are eligible for up to a 10 percent bonus on your salary that year. That is one incentive to do better. But once you have exceeded it, the level you hit becomes your expected base for the next year. Sunnyvale thus constantly rations the performance upward. With this system Sunnyvale increases its productivity 4 percent a year, year after year. In ten years they can cut the cost of delivering the same services in half. This kind of budgeting is spreading. Many other cities are doing it all over the country. The Pentagon is now budgeting the way Sunnyvale budgets, and exactly the same trend can be seen in other countries as well.

**Customer-Driven Government**

The best way to tie spending to results is to give the resource to the customer and let that customer choose the service provider. Providers are forced to be responsive to their customers, because they will be out of business otherwise. Providers that must compete are constantly trying to lower costs and raise quality. Customers value a choice of services because all have different needs.

*Customers* is a fairly new word for government and customer choice sounds like a radical notion. But this is not a new idea. Arguably the single most successful social program in U.S. history was the GI Bill. After World War II, a generation of young men returned home. The government pro-
vided them with an education, and they became productive citizens. The government did not build veterans' universities. Instead, it gave the veterans vouchers and permitted them to select the colleges they wanted to attend.

In health care the government chose the traditional route. It built veterans' hospitals and assigned veterans to hospitals. The hospitals had captive customers. Consider the difference in quality between the veterans' hospital system and education under the GI Bill. You will begin to appreciate the power of putting the resource in the customers' hands and letting the customers choose.

The voucher system is not always the best way. In public education, for example, I do not think it is the best way, for equity reasons. But similar results can be achieved in public education by changing the finance system to equalize spending per child. Let the parents pick the school and have the money follow the child. In essence, that is what School District 4 in East Harlem did ten years ago.

Community School District 4 was New York City's worst district in the 1970s. Only 15 percent of the students could read at grade level. Out of frustration and desperation, the district created an alternative school system that proved very successful. In 1982, it expanded to a full choice system at the junior high level. Parents could choose what school they wanted their children to attend. Suddenly, the school district had a score card. It could tell which schools were performing, because they were in demand. Schools that were not performing were not in demand.

Schools were forced to compete with other schools within the district to maintain and increase enrollment. The success of the alternative school system can be attributed to the fact that the system is customer driven. Parents, as customers, had a choice. The measure of the district's success is that, by 1989, 64 percent of its students were reading at grade level and 319 students had entered selective high schools—double the city average. That is the power of choice, of letting the customer drive the system.

Enterprising Government

The last principle is that of enterprising government—the idea of earning rather than spending. About 99.99 percent of energy in most governments is focused on decisions about spending money; .01 percent is focused on decisions about earning money. What would happen if the incentives changed? What would happen if employees were given about 15 percent of the revenue for any new earning resulting from their ideas, or if departments kept half of anything new they earned? I will give you one example.

Orlando, Florida, has many small lakes; it also has more hotels than New York City. Each of those hotels has a huge parking lot. When it rains, the water runs off the parking lots, collects gasoline and other chemicals,
and runs into lakes. The lakes thus accumulate a terrible amount of pollution, requiring tremendous investment in public infrastructure. The city of Orlando created an enterprise fund, "Public Storm Water Utility," and funded it with the fees collected from parking lots—the larger the impermeable surface, the higher the fee. If hotel owners put in their own drainage and treatment systems, the fee is reduced. Through the enterprise fund, the city of Orlando created an incentive for the private sector to solve an environmental problem. In addition, Orlando developed a way to raise money for the public infrastructure that was needed to solve related problems.

Conclusion

Those are six of the principles that we found in our investigations. Entrepreneurial governments are catalytic, competitive, mission driven, results oriented, customer driven, and enterprising. The other four principles are equally commonsensical. Decentralization means empowering employees, pushing decisions down from one level of government to another. Community-owned government pushes control out of bureaucracy and into the community. Anticipatory government stresses prevention rather than cure. Finally, market-driven government explores the idea of changing markets rather than always using public programs to solve problems.

These ten principles can be used to address many of the problems government and society face. Incorporating these principles will help managers develop new ways to address existing problems. The challenge for leaders in the 1990s is how to restructure dysfunctional public systems and make them effective again. There is much that we can do. My hope is that we will think seriously about the problems we face and the principles I have discussed and find one new thing that each of us can do to become part of the solution.

David Osborne is coauthor of the highly acclaimed book Reinventing Government.