MEMO TO: John Marchione, Mayor
           City Council

FROM: Michael E. Bailey, Finance & Information Services Director   556-2160
           Malisa Files, Financial Planning Manager   556-2166

DATE: April 20, 2010

SUBJECT: **STAFF REPORT:** Government Finance Officers Association Assessment of Redmond's Budgeting BY Priorities Process

At the beginning of the year, the Finance Department began working with the Government Finance Officers Association (GFOA) to evaluate Redmond's Budgeting by Priorities (BP) process and identify opportunities for enhancement in the 2011-2012 budget cycle.   The GFOA's task was to apply the knowledge and experience of budgeting-for-outcomes it has gained through research and consulting, solicit ideas from Redmond participants, and conducts a document review to provide recommendations on how to improve Redmond's process.   In addition, GFOA specifically addressed the degree to which BP is achieving the Mayor's initial goals for the process, including:

- Align the budget with citizen priorities
- Foster continuous learning in the City
- Measure progress toward priorities
- Get the best value for each tax dollar
- Foster regional cooperation

Attached to this memorandum is the final report of GFOA's assessment describing the findings and recommendations for the high-level process, supporting processes and roles and individual BP processes and steps.   GFOA does note in its report, although opportunities for improvement exist, participants at all levels of the organization said they much preferred BP to the former process and expressed enthusiasm for continuing to use BP as Redmond's budgeting framework.   A brief description of the findings and recommendations was shared with the Public Administration and Finance Committee on March 18, 2010.

Anne Kinney from the GFOA will be at the Council meeting on April 20 to present a summary of the report's findings and recommendations.   Staff will also be available that evening to answer any questions you may have.   However, if you have questions or comments before that time, please call me (x2160) or Malisa Files (x2166).

The Government Finance Officers Association Research and Consulting Center

Opportunities to Enhance the City of Redmond's FY 2011-12 Budgeting by Priorities Process

April 2010

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Opportunities to Enhance the City of Redmond's FY 2011-12 Budgeting by Priorities Process

An Assessment by the Government Finance Officers Association

Introduction and Overview

Like other local governments across the United States, the City of Redmond is continuously challenged to provide the services necessary to meet the diverse needs of its residents and businesses within its revenue-raising capacity. To help in addressing this challenge, the City initiated its innovative Budgeting by Priorities (BP) approach in its 2009-2010 biennial budget-development process.

Following initial implementation, the City surveyed participants and held meetings to identify opportunities to improve the process and address issues that arose during the implementation process. The City has already made several revisions to the 2011-12 budget development process.

However, the City also wanted an external perspective to assist in further optimizing the process and to learn from the experience of other governments that have implemented a Budgeting for Outcomes (BFO) process. The City asked GFOA to conduct such an assessment. GFOA's task was to apply the knowledge and experience it has gained in BFO through its research and consulting, and solicit ideas from elected officials, citizens involved in the Redmond BFO process, and high-level managers in the City to provide recommendations on how to enhance the process. The question was posed as "What would the process look like if it were perfect for Redmond?"

GFOA also conducted a document review that included the City's internal documents as well as public budget documents available on Redmond's Web site from the first BP process.

In addition, GFOA specifically addressed the degree to which BP is achieving the Mayor's initial goals for the process, which included:
- Aligning the budget with citizen priorities
- Fostering continuous learning in the City
- Measuring progress toward priorities
- Getting the best value for each tax dollar
- Fostering regional cooperation

GFOA was charged with developing findings and recommendations and providing the City with a summary report.

GFOA's approach

GFOA's approached this project as follows:

- GFOA reviewed documents and met with City staff that coordinated the BP process, gaining as full an understanding as possible of the 2009-10 budget development process.
- GFOA conducted individual and group interviews to get participants' views of the 2009-10 process and how BP might be enhanced.
- GFOA applied its experience in assisting other government in planning and implementing BFO, along with its research on BFO, to assess City's BP process.
- Using all of this information, GFOA identified opportunities for enhancing the process.

GFOA conducted a site visit in February 2010 and presented its preliminary findings and recommendations to City staff in a briefing in early March. This report presents GFOA's final findings and recommendations.

Terminology

The Budgeting for Outcomes (BFO) approach is described by Peter Hutchinson and David Osborne in their book, *The Price of Government.*[1] BFO provides both new concepts for public-sector budgeting and a methodology for putting the concepts into practice. Essentially, rather than focusing on "cutting" departmental budget requests to fit available revenue, BFO begins by establishing budgetary revenue and then developing an operational and spending plan based on a set of citizen-centric strategic priorities. Budgeting by Priorities (BP) is Redmond's version of BFO. In this report, we use the term BFO when discussing general concepts and BP when discussing Redmond's process.

Key findings and recommendations

Participants at all levels said they much preferred BP to the former process and expressed enthusiasm for continuing to use BP. In fact, all interviewees in GFOA's assessment said they expected to and wanted to continue the BP process. GFOA also found that the process follows the BFO model in all key respects and that the Mayor's initial goals were either achieved or are currently being addressed. In addition, interviewees consistently said they felt the Mayor's active support for and involvement in the process was the single most important element in the successful implementation of BP.

GFOA also found that the budget development process was completely consistent with BFO concepts and practices. We believe the City can gain additional benefits, however, by putting greater emphasis on BP in budget administration and budget monitoring. In addition, the City has a tremendous opportunity for enhancing performance by using BP as the basis for a performance management framework, to assure that the City's planning initiatives, process improvement efforts, intergovernmental initiatives, and other policy and management initiatives are aligned with the high-level priorities developed through BP.

Because BP implementation was successful and has been well accepted, City managers as well and the Mayor and City Council have expressed interest in incorporating

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[1] *The Price of Government: Getting the Results We Need in an Era of Permanent Fiscal Crisis,* Basic Books (New York), 2004.

additional elements. On the other hand, City staff members expressed the hope that the second BP process will entail less change, take less time, and enable them to apply what they learned in the 2009-10 process. To continue incorporating additional elements while assuring that staff is not overwhelmed with many changes at once, GFOA recommends that the City develop a long-term plan for BP, enabling the City to plan and implement additional elements in a systematic and predictable manner over time.

GFOA will present its findings and recommendations in subsequent sections of this report according to the following categories:
- High-level process
- Supporting processes and roles
- Individual BP process steps

Findings and Recommendations

High-Level Process - Findings

Participants much prefer BP to the former process.

In interviewing groups and individuals who participated in the first BP process, including elected officials, upper management, Results Team members, and citizen participants, GFOA found that all said the BP process was better than the old process and they by no means wanted to return the way things were before. Nearly all participants said the first BP process did take a lot more time than they expected, and they were looking forward to the second iteration taking much less time.

The BP process followed the BFO model originally selected by City leaders.

Based on GFOA's consulting and research, we have learned that governments implement BFO in slightly different ways (while adhering to the basic concepts), reflecting the diversity and creativity of individual governments. Through these adaptations, governments have helped to expand and enhance BFO as a tool that allows governments to better link spending to citizen priorities and to better manage organizational performance.

One of the less-explored areas of BFO is how department directors can contribute to a successful budget, beyond their responsibility to prepare offers. A significant adaptation made by Redmond was the creation of the Directors' Team, made up of the Mayor and his direct reports. This team made a significant contribution by reviewing all the Results Teams' recommended rankings and then recommending ways the allocations among priorities could be adjusted to get the best total budget package for the Mayor to propose to the City Council. The Directors' Team also regularly reviewed the BP process.

The Mayor's stated goals for the process are listed above, in the Introduction and Overview section. These high-level goals have implications in terms of both short-term

process and long-term results. GFOA's assessment found that the first two goals – aligning the budget with citizen priorities and fostering continuous learning – were very well addressed during the BP process. The remaining three goals – measuring progress toward priorities, getting the best value for each tax dollar, and fostering regional cooperation – were addressed in the process and are being worked on as follow-up projects to initial BP implementation. Several interviewees said that the City continues to learn about selecting and applying measures and that measures are improving. The Mayor's efficiency initiative, currently underway, is focused on the goal of getting the best value for each tax dollar. Efforts toward regional cooperation are also underway, and intergovernmental initiatives are expected to play a more significant part in the 2011-2012 BP process.

More opportunities exist to apply BP concepts in budget administration and monitoring.

Managers who were interviewed varied on how they were using BP in budget administration. Most managers said that while they were very aware of how they were doing in their programs, they were not explicitly using the BP format to administer their budgets and monitor progress. Council members who were interviewed also said they did not explicitly use BP information to monitor the budget. Two important forthcoming changes could support putting greater emphasis on BP in administering the budget. First, the City's current financial system does not have the capability to do financial monitoring in the BP format. However, Microsoft Dynamics, which is being developed by the City, does have that capability. Second, because measures are a work in progress, central monitoring of program performance has not been emphasized. Performance measures will become more important in subsequent budget development processes because departments and the Results Teams will need information on current performance to evaluate and rank offers for subsequent budgets. This situation will be addressed in the high-level recommendations section below.

High-Level Process - Recommendations

Use BP as the basis for a City performance management framework.

One of the issues staff discussed with GFOA is the positive effect BP has had on the City's organizational culture. More City staff members have been involved in the budget process, thereby creating a greater knowledge base and understanding of City services and processes. In addition, more City staff have a good understanding of the challenges related to prioritizing services. Expanding the knowledge base and involving more City staff is consistent with the Mayor's desire to make continuous learning and a citizen focus a permanent part of City government's DNA.

These factors, added to the success of the City's first BP process, prompt GFOA to recommend that the City use BP as the basis for its performance management framework, incorporating the City's planning, funding, management, and evaluation efforts to assure that they are aligned and consistent with the high-level priorities developed in the BP process. This would help assure that what otherwise could be disparate, unconnected initiatives are aligned to what matters most to Redmond's citizens.

GFOA further recommends that if the City decides to develop a BP-driven performance management framework, the Directors' Team identify and articulate – in writing – how the City's planning, management, and evaluation processes conform to the central concepts of BP, or how these processes need to change. This could be an important step in creating a BP-based performance management framework and assuring that a results focus is embedded in the organizational culture.

The Mayor's six current initiatives are very consistent with BP and have the potential to produce even greater benefits to the extent that they can be integrated into a BP-based performance framework. As an example, business process improvement as a stand-alone tool is useful for gaining efficiency and improving customer service. However, it can also support BP by helping departments prepare more competitive offers in the BP process. Using BP as the basis for a performance management framework will also facilitate using BP concepts in budget administration, evaluation, and performance reporting.

Incorporate improvement efforts into the BP framework.

This recommendation is linked to the above recommendation. The City can build on the organizational learning that occurred in the budget process to foster a continuous learning culture. Budget staff could act as facilitators of continuous learning and provide evidence-based research capabilities to strengthen BP.

Innovative, creative offers are a perpetual hope and challenge in the BP process. Recent research shows that individuals and groups can benefit significantly from training in innovation and creative thinking. Such training could be used to drive innovative offers and contribute to a learning culture.

The City is already using business process improvement methodology in its efficiency initiative. Systematic training and application of such methodologies is becoming an important management skill, and if encouraged by City leaders, this skill can strengthen BP and become a major element in sustaining BP over time and through changes in administration.

Prepare a long-range BP plan.

Our interviews, discussions, and document review all indicate that the City's leaders wish to move quickly to incorporate new elements such as private-sector offers and intergovernmental partnerships into BP. It is also very clear that many city employees feel they were over-extended in the first process and, while they very much want to continue to participate, they are looking forward to having a calmer and less time-consuming process the second time around. To meet the needs and expectations of City leaders while not overwhelming City staff with change, GFOA recommends that the City prepare a long-term BP plan (10 years is suggested, so five biennial budget processes can be incorporated). Such a plan could help the City incorporate additional elements on a timeline that would help assure that new features are implemented thoughtfully and deliberately. A long-term plan could aid in allocating appropriate time for planning, staff training, and funding to assure that staff are not overwhelmed with too much change simultaneously, which creates a risk of sub-optimal performance. Appendix A contains a sample timeline for such a plan.

Implementing a long-term BP plan also supports making the BP approach part of the organization's DNA and provides a written roadmap that all participants can use and reference to others. It is also consistent with BP as a tool for transformation, which by definition is long term and long lasting.

If competitive options (outsourcing, privatization, managed competition) are to be incorporated into BP, do so no earlier than the 2013-14 budget process.

BP provides an excellent process for incorporating offers from entities beyond a government's own internal departments. Competitive options[2] are consistent with BP's philosophy to hold down costs, improve results, and maintain a buyer-seller relationship in the process. Consequently, some officials are interested in moving ahead quickly to invite private-sector involvement.

Our recommendation to incorporate competitive options no earlier than 2013-14 is based on GFOA staff's experience in implementing public-private partnerships. Systematic approaches require considerable time for planning and raise several issues that governments typically must address before services are opened up to private competition. Some of these issues include:

- **True cost comparison**. Comparing a private contract price to in-house provision is not a simple dollar-to-dollar comparison. For example, insurance, indemnification, and monitoring costs must be factored into the comparison. Also, savings must be adjusted for internal costs that will not go away. Overhead that is avoidable (cost that can go away) must be identified and separated from unavoidable overhead (costs that cannot go away, at least right away).
- **Term of contract**. For many services provided by the private sector, start-up costs may mean that profit will occur in the out-years of a contract. Consequently, Redmond will need to decide how that situation will correspond with offers that extend only through a two-year (biennial budget) term.
- **Purchasing procedures**. A review of standard purchasing provisions (often known as boilerplate) is necessary to determine whether these requirements will apply to private offers and how the purchasing process and the BP process need to work together.
- **Transition of assets and personnel**. What will happen to current city staff if a private-sector offer is selected? Will the private-sector winner be required to hire them? Will the City's assets be used by the private-sector provider? If so, what provisions are necessary to assure that these assets are maintained and replaced as needed?
- **Monitoring and measureable performance standards**. The City is developing measures to use as part of BP, but many of those interviewed felt that more work is needed to assure that the measures are in fact good indicators. Measures must be incorporated into contracts with private-sector firms so the City can monitor performance and assure that it gets what it is paying for.
- **Intangibles**. In-house providers are usually flexible; when asked, they typically are able to provide additional services as needed. Private-sector firms perform services as specified in the contract. If additional services are requested, they

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[2] Because there are a number of approaches, the term "competitive options" will be used in this report to cover various public-private arrangements.

are typically considered out of the scope of the agreement, and additional payments must be made for those services.

All of these issues have been thought through and resolved by governments that have initiated public-private partnerships. They are not raised to discourage the City from considering such partnerships but rather to emphasize that planning, conducting, and implementing competitive processes is a significant undertaking. Additional information on this topic is provided in Appendix B.

Supporting Processes and Roles - Findings

Processes and roles in BP include such things as the City's communication process and the roles played by the Mayor, Council, Results Teams, and others.

The City's communication process for BP worked extremely well, and the Mayor's role was critical.

In the 2009-10 budget process, the Mayor took a strong leadership role and set up an excellent ongoing communication process. Many interviewees pointed to the key role the Mayor played in keeping employees, the public, and the Council informed in the process. Several individuals said the Mayor's active involvement, especially the regular meetings and memos, caused employees who otherwise would have turned against the process to continue to support it. One of the challenges is how to continue the excellent communication process, whether or not the Mayor is able to be as significantly involved. An additional challenge is to capture important lessons learned about what works and what does not work in the communication process from year to year. Related recommendations appear in the Supporting Processes and Roles – Recommendations section.

The City's financial system supported BP, but improvements are desirable.

One of the most challenging parts of implementing BP is getting the financial information right. Costs must be aggregated by program in addition to department and line item. Further, internal to the BP process, the total of the "above the line" offers ranked by the teams must balance with total revenue, and offers funded by restricted revenue funds must also balance to revenue estimates for such funds. Fortunately, the City's technology was sufficient to enable the budget office to accomplish all of this. Combining information on allocations for programs (offers) and program performance measures would be difficult using the current system. The City's implementation of Microsoft Dynamics is timely in this regard.

Participants wanted more training on the nuts and bolts of the process but found that working through these issues caused them to learn it well.

At the beginning of a BP implementation, participants are faced with the challenge of both understanding a new way of thinking about budgeting and learning how to do the process. Participants said training in the first BP process was more focused on BP concepts and less on the nuts and bolts of the BP process. But they also said the struggle to create maps, strategies, requests for offers (RFOs), and offers caused them to learn and internalize BP. The Project Team has already identified training needs and

has begun providing training sessions. GFOA believes there is a specific need to provide support for departments in developing and using performance measures.

The initial time commitment was greater than expected, and participants expect to spend less time this year.

As mentioned previously, team members, department representatives, and citizen participants all said the process took much more time than they expected, but they also typically added that because the first year contained a lot of unknowns, it was understandable that it was time-consuming. They said they are looking forward to spending less time on the process this year. This expectation suggests that for the 2011-12 development process, the City might be better off focusing on improving and enhancing the process rather than introducing major new initiatives. This would prevent participants from experiencing change fatigue, which could affect the quality of the process.

Roles in the process were well executed.

Key roles included Results Team participation, process management (the Project Team), budget/finance support, citizen involvement (the Results Teams and the Guidance Team), and the involvement of department directors, the Mayor, and the City Council. GFOA found that all of these roles were performed consistently with the BFO model. Specific observations on roles are described below.

Results Teams. The diversity of skills on the teams helped the process. Team members who were interviewed said members took their roles seriously and took ownership of the priority they were working on. They said they learned a lot that they hoped to apply if they are involved this year. Also, even after they submit their recommended rankings, they want to know what the Mayor's budget contains.

In terms of enhancing the process this time around, communication will remain critical. The role of team leader as a communicator will be especially important if the leaders are expected to be conduits of information to their teams about what is happening in the process outside the teams.

Project Team. The Project Team plays a crucial role in the BP process and has multiple responsibilities. It is charged with assuring that the process is working, making sure elected officials are getting the information and input they need, ensuring that the Results Teams receive sufficient support, assessing and meeting training needs, and many other activities. In 2008, the team consisted of four members and the number declined to three in 2010. A three-member Project Team is unusually small (but not unprecedented). Further, Results Team members who were interviewed said they wanted to continue receiving a high level of support they received from the Project Team in 2008. Expanding team membership could help the team to meet its multiple responsibilities and devote the necessary time to BP while also leaving time for them to fulfill their other, non-BP-related responsibilities.

Budget and finance staff. The budget and finance staff are critical behind-the-scenes participants in the process. They are often challenged to move beyond the role of reviewing budgets themselves to provide assistance and expertise to Results Teams. GFOA concluded that Redmond's budget and finance staff performed very well, both in

learning and assisting with the BP process, and in comparison to other governments that have implemented the BFO model.

Involved citizens. Involved citizens were committed to the process. They suggested that process managers make special efforts to keep citizens informed. Other participants stressed the importance of having citizens involved on teams. Even when everyone is told to wear the citizen hat, having citizens serving on teams assures that that the citizen perspective is front and center in all discussions. As mentioned previously, they also said the heavy time commitment could deter citizen involvement.

Guidance Team. This group, made up of citizens, representatives of business, and an official from another government in the area, provided a sounding board to the Mayor in creating the BP process. The feedback they provided proved valuable to the Mayor and others in deciding how to set up the process initially and how to go about making changes during the start-up period. Now that the process is up and running, this team's purpose has been fulfilled. In government it is often difficult to disband an effort, even when its purpose has been achieved. The Guidance Team is viewed as a part of the City's carefully constructed and managed effort, and GFOA sees the City's decision not to continue a group that has accomplished its mission as one of a series of astute decisions that have made BP a success.

Department directors. Department directors said that they appreciated being able to be actively involved in reviewing the Results Teams' recommendations before the Mayor's budget was completed. This is an important shift, from making offers to looking at all offers from a citywide perspective.

Mayor and City Council. After reviewing documents and interviewing these elected officials[3], GFOA concluded that both the Mayor and City Council exhibited strong leadership and that they trusted the process and used the BP model for making budget decisions. In other words, they fulfilled their roles very much as described in *The Price of Government* and in BFO methodology. The level of involvement of both the Council and Mayor was the highest GFOA has seen in its experience and research.

Further, although it is impossible to prove that this is the case, we strongly believe that the major factor in the success of BP was that the process was initiated and driven by these officials. In addition, we have not in our research and direct work with governments seen a BFO process with this degree of involvement from the CEO. The Mayor's personal involvement, coupled with the large amount of time he devoted to regularly communicating with and meeting with employees, was invaluable. Many employees we interviewed quoted directly from statements by the Mayor and said that the Mayor's strong support helped them stay with the process even when problems arose.

Council members were highly knowledgeable about the process, and most said they had "read the book" (*The Price of Government*) so they could fully understand and participate in the process*.* It is also our understanding that this the first time in memory where the budget was unanimously approved by Council members. Council members we interviewed said they were very satisfied with the process and want to continue to

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[3] All Council members were asked for interviews, and all but one were able to participate.

enhance it. They identified improvement of measures as one of the things they would like to pursue in this second iteration.

The challenge for the Mayor and council now is how to best sustain the process. Recommendations in the previous section focus on that question. In addition, some of the recommendations below provide more specific suggestions on sustaining BP.

Supporting Processes and Roles - Recommendations

Build on the successful communication process to assure consistency and involvement.

The Mayor remains actively involved in the process; however, as BP becomes a more routine process, and because the Mayor may take on more initiatives that will consume his time, it will be important to assure that communication continues to be frequent, clear, and consistent. Instituting routine communication mechanisms in addition to the Mayor's involvement will be is important. In addition to communication *to* employees and citizens, it is also important to have a good mechanism to encourage two-way communication *with* City staff and the public.

To capture lessons learned as a result of the highly effective communication effort from the first BP process, we recommend that the Project Team memorialize the communication elements that contributed to the 2008 BP success in a written communication plan for BP. Such a plan would include a description of current communication mechanisms and success stories as a basis for planning future communication efforts. Communication plans typically include identification of key stakeholders and audiences, messages, resources, a schedule, and a process for each element.

Internally the budget office staff would continue to work with both the departments and the Results Teams during the process to facilitate good communication.

An additional recommendation is that the City make special efforts to assure that citizen team members always get electronic messages and that teams agree to distribute information electronically so citizen members are never left out of the loop. The City has already made a change in the City's budget portal to assure that citizen team members regularly receive all team communication.

Take advantage of Microsoft Dynamics implementation to make the underlying BP financial process easier and to link funding to performance measures.

The City is currently implementing Microsoft Dynamics, which presents an opportunity to both simplify and assure accuracy in the BP process. The implementation might also provide a model for other governments for simplifying the financial mechanics of BP and linking program funding to program performance measures. GFOA recommends that the City explore the opportunities for Microsoft Dynamics to cross-walk budgetary information between programs and the City's financial chart of accounts, and combine financial and performance information. Doing so would help not only in budget development but in budget administration and performance monitoring.

Customize training to meet the stated needs of team members and departments by using more coaching and less formal training.

Because this is the second time the City has done BP, there is less need for large group training. Of course, new team members, new Council members, and new department directors will need to have training and other information to assure that they understand the process and their roles in it.

We recommend that individual coaching might prove more beneficial this time around. That would enable the City to pinpoint specific training needs and address them in a focused way on a continuous basis.

In addition, based on our assessment, we recommend that training and/or group coaching on performance measurement be provided to departmental staff and Results Team members before and during the offer development and ranking process.

Expand Project Team membership, and continue and enhance central support for Results Teams.

In interviews, team members said they understand that in the first process, they and others were learning on the go. This time around, they would like to be provided with very clear and consistent information on their tasks. To assure continued consistency for Results Teams, an approach the Project Team could take is to split up responsibility for being the "authority" on one or more aspects of the process (e.g., pricing, cost allocation, RFO preparation, ranking, and offer preparation) so questions regarding these aspects could be referred to that individual. Currently, there are three members of the Project Team: the City's Deputy Director of Administration, Director of Finance, and Financial Planning Manager, all of whom have multiple areas of responsibility. To provide central support for the Results Teams as well as manage the entire process, we recommend that the City consider adding two members. The new members need to have a citywide perspective and a good grasp of BP concepts and practices, and they should be strong supporters.

In other BFO governments, we have found that the subject matter expert (SME) role on each team tends to become less the expert and more a facilitator who identifies sources of evidence, whether that means other experts, research reports, or other resources. This role places a special burden on a single individual. The City has eliminated the SME role on teams for this reason. The responsibility for identifying resources and evidence related to the team's priority outcome will be divided among team members like other team responsibilities. We believe this is a positive way of addressing the need for subject matter expertise.

Leverage the BP expertise of budget and finance staff.

Budget and finance staff have become subject matter experts in the BP process and are able to train and coach teams and departments. They communicate regularly with team leaders and provide information as necessary. We recommend that they continue to support teams and departments in this manner – in other words, to provide continuous subject matter expertise on the BP process itself.

In addition, we recommend that the City consider assigning budget analysts to create a virtual library that contains effective strategies and programs. Budget analysts could also maintain records of the research that teams conduct so information does not have to be recreated every two years.

Budget analysts might also be given the role of in-house experts on performance measurement and performance management so they can coach departments and assure consistency citywide.

Enhance the role of the Directors' Team.

Department directors regularly meet as a team, year-round, with the Mayor. They also meet quarterly to review the BP process. Based on their strong involvement in the process, they could also serve an important role in institutionalizing BP in budget monitoring and administration, which was the subject of a GFOA recommendation in the High-Level Process - Findings section of this report. For example, this team could conduct quarterly reviews of program results and share what they've learned about methodologies (e.g., how to develop and use performance measures in managing).

The stature and knowledge of the Directors' Team's could also strengthen the Mayor's business process improvement initiative. The City has already made significant process in this area by identifying and conducting initial process improvement projects. A challenge now is to move from a one-time initiative to assuring that process improvement is embedded in the organization's culture, as part of a continuous learning focus, so it becomes a standard expectation. The Directors' Team could make a significant contribution by assisting the Mayor not only in selecting, prioritizing, and assessing project results, but by making expertise in process improvement a standard requirement for departmental managers. Further, visible support for process improvement department directors can send a strong message across the organization that process improvement is a part of the way the City will operate now and in the future.

Institutionalize the role of elected officials in BP.

The BP process was advocated and sustained by the Mayor and Council. The challenge for the future is how to continue this high level of support as individual elected officials change. In other words, how can the City institutionalize BP as the City's budget and management process while maintaining Council members' role of independently elected officials? It is important to be clear that supporting the process does not mean always agreeing with proposed rankings or that revenue estimates cannot be questioned. In fact, the BP process encourages debate and discussion – the expression of a variety of perspectives to gain full understanding of an issue before decisions are made. As new officials come into the City, therefore, it will be important to assure that they receive good training and information on BP concepts, why the City adopted the process, and how elected officials can effectively play a role in the process. Beyond providing information to incoming Council members, the City may wish to consider more formal ways of institutionalizing BP by incorporating BP concepts and practices in Council-approved budget policies and procedures. One example is the City's work this year to incorporate long-term financial projections into the process.

Supporting Processes and Roles - Recommendations and Findings

This section provides information and recommendations on the way the City conducts each step on the BP process. It is based primarily on GFOA's research and consulting experience in the BFO approach.   Conclusions and recommendations are provided together for each process step addressed.

Price of government

Redmond made greater use of the price of government concept than do most governments that implement the BFO model, to our knowledge. More typically, governments develop revenue estimates in the traditional manner without calculating or considering the price of government. The price of government concept can be very helpful when considering what the "right" level of fees or taxes should be for a specific community, and we strongly recommend that the City continue to use it. Our understanding is that the finance department is working with the Mayor and Council to develop long-range forecasts and apply price of government to that analysis.

Allocation process

In discussions with budget and finance staff, they indicated that they feel confident about the second allocation process because they now have a baseline from two years ago. GFOA agrees that using the previous allocation as a baseline is helpful; however, we recommend that the City be cautious about creating an expectation that the percentage of revenues allocated to each priority will remain the same in each budget. This expectation, although it was applied to departmental budgets, was one of the pitfalls BFO was created to overcome. To avoid this expectation, the City must continue to devote serious discussion in *each subsequent budget process* to the relative importance of each priority. Having performance measures that promote understanding of priority results should add depth and substance to that discussion.

It is common to have changes in allocations toward the end of the process. According to information provided by the City, there was a 6 percentage point change in allocations from the initial allocation to the allocation in the Mayor's budget that was sent to the City Council. Our recommendation in this regard is to clearly communicate such changes at the appropriate time in order to maintain transparency, especially to those who are very invested in the process, such as Results Team members.

In addition, some BFO governments set aside a certain amount at the beginning of the process for priorities that may arise over the course of the budget development phase. We recommend that if Redmond decides to do this, that this fact be communicated, along with the rationale for doing so.

Cause and effect analysis and RFOs.

As previously stated, teams said they struggled in the first BP process in creating maps, developing purchasing strategies, and writing RFOs. In addition, they expect the process to go more smoothly this time. The second process and subsequent processes

will be different than the first not only because of the organizational learning that took place but also because team membership has changed. Consequently, even though the teams will have existing maps, strategies, and the previous RFOs to refer to, it will be important to do an analysis that is focused on the City's needs over the next biennial and beyond – essentially, to review and, if necessary, rethink the cause-effect relationships to assure that factors are still the same. If factors have changed, it will be necessary to identify changes to create timely and relevant RFOs.

Based on the experience of other governments and the positive feedback about the process from departments and teams, we also suggest that the City is now in a position to challenge departments to emphasize intergovernmental partnerships and service delivery innovation, and to place even more emphasis on efficiency as they prepare for the 2011-12 budget.

Offers

In the first BP process, the quality of offers varied considerably. Team members said in interviews that they sometimes ranked offers lower simply because they were not well written or did not provide adequate explanations. This experience suggests some opportunities for the current process. First, it could save considerable time in the process if departments prepared well-written offers the first time around. Second, the budget staff can play an important role by reviewing departmental offers from an outsider perspective and providing straightforward critiques to departments.

Scalability has been a challenge for governments using the BFO approach, and this challenge and has been addressed in various ways. It is our understanding that for the 2011-12 budget process, departments may be required to submit an alternative service level for some offers at a price that is less than the price of the offer, along with implications. The challenge for departments will be to clearly communicate the implications of a lower-priced offer. The challenge for teams will be to clearly understand those implications rather than accepting the alternative service level simply because it allows them to put more offers above the line.

Another issue is how to encourage innovation through the BP process. We often hear from other governments that they expected more innovative offers in the second process, but that typically does not happen without a focused effort. Over the last few years, structured processes for producing innovation have been developed. We recommend that the City consider providing training to departments, perhaps along with Results Team members, on creative thinking as a way to encourage innovative offers.

Finally, and significantly, a very important purpose of the written offers is to communicate to the teams, elected officials, and the public how the offered program or service relates to achieving results for the community. A concise, well-written offer would be important for that reason, if for no other. We recommend that the City revise forms, train teams and departments, or take any other actions necessary to assure that this information is clearly communicated in the offers at all steps in the process, including inclusion in the final adopted budget.

Ranking process

In Redmond, and in other governments that practice priority-driven budgeting, departments that are funded through legally restricted funding streams often express frustration that they have to prepare offers and go through the ranking process. In our discussion, Redmond's Project Team articulated an excellent rationale for having such programs go through the same process as other programs. BP provides an excellent opportunity to gather the best thinking across the organization and also to collect and review evidence from research and experience elsewhere to assure that Redmond's programs are on point, regardless of funding source. This may be particularly important for departments that have designated funding sources because their services might not have been given as much scrutiny in past budgets, where much of the attention was necessarily focused on services funded with general funds. We believe that having the Project Team educate staff about this rationale through multiple channels would help them understand the benefits of having *all* programs incorporated into offers and ranked.

Budget adoption

According to interviews, the budget adoption phase went very smoothly. Giving the Council information on both the offers that are funded and those that are not funded provides the opportunity for a much richer discussion than is typically possible in a traditional line-item, input-driven budget process. Our only recommendation here is to continue to assure that these discussions are open and that their content is well communicated to the public. Our understanding from discussions with City staff is that the City's Web site will be improved over the next year. This offers an excellent forum that the City can use this year for providing information on offers, rankings, and the BP process.

Conclusion

The City of Redmond has reason to be proud of what it accomplished in adopting its first BP budget. The City has already made many process improvements in preparation for the second BP process, and we hope that our assessment provides additional support for strengthening and sustaining the process to benefit Redmond's citizens.

GFOA would like to thank all the individuals who graciously agreed to participate in interviews and were forthright in their responses to our questions. We would also like to thank the Project Team members, who provided us with background information and documents we used in our research, and offered helpful feedback during the study.

APPENDIX A: Example Long-Term Plan Timeline for Budgeting for Priorities

The following table provides an example of a 10-year BP plan. GFOA recommends a 10-year planning timeframe that would be updated periodically to place individual activities into a long-term context and cover multiple biennial budget processes. Action items shown here are illustrative examples of specific actions that might occur in the short- to mid-term. Possible actions for the out-years are necessarily more conceptual; detail would be added as Redmond gains more experience in BP.

Example 10-Year Budgeting by Priorities Plan Timeline

2019-20
- Review changes needed for next budget process
- Update Strategic Priorities
- Evaluate entire BP process based on emerging practices
- Evaluate individual performance management process

2017-18
- Review changes needed for next budget process
- Review/update performance management framework based on emerging practices
- Evaluate long-range financial planning methodologies

2015-16
- Review changes needed for next budget process
- Align individual performance evaluation process with BP

2013-14
- Review changes needed for next budget process
- Invite private-sector offers and transition services as warranted
- Complete performance management framework
- Implement evidence resources database (virtual library)

2011-12
- Implement MS Dynamics budget system linked to BP
- Train/coach employees on innovation
- Review pilot programs for potential contracting out
- Revise guidelines for including private firms in BP
- Design/implement BP-based performance management framework
- Update strategic priorities

2010
- Identify potential pilot programs for contracting out
- Incorporate long-range financial planning into BP
- Improve department offer training
- Develop/implement new CIP process/add 7th Results Team
- Improve performance measures
- Review changes needed to second BP process

2008
- Develop/implement City's first BP process

APPENDIX B: Information on Public-Private Competition Process

1. Competitive Options Resources

City of Charlotte, North Carolina, Managed Competition Program:
http://www.charmeck.org/Departments/Business+Support+Services/Procurement/PCAC+Main+Page.htm.

State of Virginia Competition Council: http://www.egovcompetition.com/.

An Elected Official's Guide to Competitive Options: From Managed Competition to Privatization, published by GFOA.

2. GFOA's Best Practice on Managed Competition (www.gfoa.org)

Government Finance Officers Association

Recommended Practice

Managed Competition as a Service Delivery Option (2006) (BUDGET)

Background. Governments are continually tasked with providing high-quality services within the constraints of limited financial resources. In order to meet this challenge, many governments have turned to the private sector or other governments as an alternative to in-house service delivery as potential ways to save money or improve services. One choice within potential service delivery options is managed competition, in which governments require in-house service units to compete with external providers.

Recommendation. The Government Finance Officers Association (GFOA) recommends that governments systematically identify and evaluate the major factors in considering a managed competition option. Service level, cost, efficiency, effectiveness, quality, customer service, and the ability to monitor the service provider's work should be essential components of any managed competition decision**.** In addition, governments should clearly define the service parameters in the expected service delivery.

When evaluating whether to undertake a managed competition initiative, governments should consider the following key points:

(1) Executive Direction. The heads of government must support a move toward a managed competition service delivery model. Support from the government's executive and legislative leadership is essential. The governmental leaders should establish clear expectations and standards for such an initiative. It is necessary to have a transparent process.

(2) Environmental Consideration. Consideration must be given to how managed competition is affected by demographics, the economy, geography, citizen sensitivity, and the local political environment. Organizations are encouraged to closely evaluate the strengths and weaknesses of the jurisdiction relative to the managed competition option. Consideration should also be given to an analysis of opportunities and threats on the environment external to the organization. A look at how other communities have fared with managed competition for that particular service may be necessary.

(3) Stakeholders' Support. Stakeholders need to be appropriately involved. Stakeholder groups may include unions, employees, media, advocacy groups, local businesses, and the public. By involving stakeholders in the managed competition process, governments will have a better opportunity to convince stakeholders of the value of a competitive service model.

(4) Legal Ramifications. Issues associated with employment law compliance and existing labor agreements must be considered. If a switch to managed competition affects union employees, options like workshops, meetings, and open forums should be considered to communicate to labor unions the possible benefits of managed competition. Human resource impacts should be a factor when making the determination whether to go ahead with managed competition. As part of the negotiations with potential contractors, thought should be given to hiring the current workforce or retraining current employees for reassignment. It should be noted that shifting a service to a contractor might transfer liability and other risks to the contractor (even though these risks are likely built into the contract price).

(5) Service Availability. The services considered for managed competition should be measured against the availability of the service in the market place. Some services, such as trash collection and building construction, may lend themselves to competition. Fairness of competition should also be analyzed. In addition, consideration should be given to the total investment that the government has made in the current service delivery. A substantial prior investment may preclude the government from entering into a competitive situation.

(6) Cost. The cost decision as to whether to perform a service "in house" or outsource it to an external provider involves four basic steps. Determining the different cost structures is necessary before proceeding with the request for proposal (RFP). However, cost should not be the only basis in comparing competitive bids. Governments should develop a decision-making process that seeks to account for all relevant factors.

> *A. Service definition.* The first step in a cost analysis is to clearly define the government service that is being considered for outsourcing. A thorough analysis of the service level and performance standards will

provide the best framework for evaluating the full cost of the service, whether it continues to be delivered in-house or it is outsourced to an external provider.

B. Calculate the in-house costs that could be avoided by outsourcing the service.
GFOA's Recommended Practice, *Measuring the Cost of Government Services*, defines the full cost of a service, as that which encompasses all direct and indirect costs related to that service. Governments should understand that not all indirect costs would be avoided if the service were outsourced.

C. Estimate the total costs of outsourcing. The costs of outsourcing include the contractor's bid price, the government's contract administration costs, and the government's transition costs, less any new revenue generated from outsourcing.

D. Compare the cost savings from outsourcing to the costs incurred. The final step in a make-versus-buy cost analysis is to calculate the difference between the costs saved by outsourcing a service and the costs incurred. If the costs saved are significantly greater than the costs incurred, then outsourcing may make financial sense.

(7) Transition Process. Governments must be fully prepared to allow for a smooth transition if a change in a service delivery provider takes place. It is essential that initial monitoring occur to make sure that no disruption in service arises.

(8) Performance Metrics. Governments must employ performance metrics as a means of comparing and evaluating efficiency and effectiveness standards for service activities. Elements like productivity, quality, timeliness, and desired outcomes are needed. Contract staff must be prepared to develop and manage a competitive services agreement. The success of competitive service delivery often rests on the ability of the organization to develop and manage a strong performance-based services agreement (including appropriate incentives and penalties). It is imperative that an organization develops the skills to design relevant performance metrics that ensure service quality. Establishing consistent benchmarks that measure service performance is essential.

References.
• GFOA Recommended Practice: *Performance Management: Using Performance Measurement for Decision Making (2002 and 2007).*
http://www.gfoa.org/downloads/budgetperfmanagement.pdf
• GFOA Recommended Practice: *Measuring the Cost of Government Services (2002).*
http://www.gfoa.org/downloads/MeasuringtheCostofGovernmentService.pdf
• GFOA Government Finance Review, "Make or Buy? Using Cost Analysis to Decide Whether to Outsource Public Services" (August 2004).
• GFOA Recommended Practice: *Establishment of Strategic Plans* (2005).
http://www.gfoa.org/downloads/budgetStrategicPlanning.pdf

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