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Institutional and Organizational Restructuring

Innovation: Competition and Costing, Indianapolis, USA

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What was the problem?

In Indianapolis, the twelfth-largest city in the United States, Mayor Stephen Goldsmith's administration contended with two administrative challenges: improved service and lower, or at least stable, taxes. To meet these goals efficiently and with minimal disruption of service delivery, municipal innovators chose between privatization and the bidding of public employees against private firms to provide publicly funded services.

What was the innovation?

Rather than simply encouraging privatization, the city government focused its goals on marketization. The first step to increasing the competitiveness of the public sector was to find out how much a given service would cost to perform in-house. Any reasonable evaluation of competitive bids depended on the ability of the government's own workers to estimate the costs involved in their projects. In the spring of 1992, the municipality instituted a process called activity-based costing. For every identifiable activity of government, civil servants determined all the associated costs of its implementation. The process used private-sector definitions of depreciation and included all costs of idle equipment, building space, and other fixed costs.

There were benefits to the costing process wholly independent of competition: because every dime of government spending was allocated to an outcome, managers scrambled to reduce waste and overhead. It was competition that caused managers to take the activity-based costing process seriously and use the new information at their disposal to make prudent choices about service delivery. By this means, innovators were able to empower the workforce and inject competition that enhanced the quality and quantity of public goods.

If marketization is structured properly, it can also provide business opportunities for citizens, especially residents of poorer urban neighborhoods. Under the previous system, the government taxed residents in poor neighborhoods, accumulated their limited wealth, and then used that wealth to hire workers from outside these neighborhoods to provide services. By generating competition in the delivery of services, municipal governments can provide opportunities for business development, as neighborhood groups can bid to perform their own services and use the revenue stream to leverage other possible business opportunities.

What obstacles did innovators encounter?

Innovators in Indianapolis met with entrenched resistance from members of the government with a vested interest in the status quo. It had taken decades for governments to integrate itself vertically into performing services that might best be performed by networks of private and nonprofit organizations.

What were the planned versus actual results of the innovation?

By May 1994, the city, through its Office of Enterprise Development acting at the behest of the Service Efficiency and Lower Taxes for Indianapolis Commission, had scrutinized some 70 individual activities of city government, deciding whether to reorganize, compete, or privatize each activity. The Office of Enterprise Development estimated budget savings for the 1994 fiscal year at U.S. $27 million, with cumulative savings over the years approaching of half a billion dollars. Between 1992 and 1994, the city reduced its payroll from 5,400 employees to 3,900 employees, primarily by not filling positions that became vacant. No union members were laid off. Indianapolis also enjoyed significant increases in public employee and citizen satisfaction, and increased quality in service provision. To the extent that marketization reduced the size and cost of government, it left more money for families to spend themselves. It moved services into the marketplace, which can be the most equitable way to approach city service delivery.

Materials adapted from:

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