

Planning for Reduced Operating Expenses

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Key Points

- Consider long-term impacts of spending cuts such as [reducing capital spending](#) and hiring freezes.
- Avoid across the board cuts that take funds away from higher priority programs and services.
- Prioritize cuts that have a short time-to-benefit, are not complex, and are easily reversible.

Local governments may be looking at ways to cut costs in some areas as they face current or anticipated revenue decreases and cost increases related to the COVID-19 pandemic.

Before making cost-cutting decisions, local governments should ensure that they clearly understand their financial situation and clearly articulate their goal. That goal could be something very specific like “Find \$50,000 that can be re-allocated for emergency response operations.” It could also be something broader such as “Reduce total spending in the short-term by 10% to increase reserves if emergency response is necessary” or “Plan for 10% reduction in spending to adjust for decreased revenues in coming months.” Strategies to enhance liquidity are outlined in further detail in [a companion paper here](#).

Governments should also examine their rainy-day fund. A healthy rainy-day fund could cover increased costs or fill gaps in revenue in the short term. Under normal circumstances, the Government Finance Officers Association recommends maintaining an unreserved general fund balance that is equal to about 15 to 20% of general fund revenues, and many local governments maintain fund balances well in excess of this threshold. This approach must also be paired with a medium or long-term plan to reduce spending so that reserves aren’t completely drawn down before local budgets regain stability after the pandemic. For those with a healthy fund balance, using cash reserves can be considered as a first step to mitigate painful budget cuts. Those with less healthy reserves should immediately focus on reducing costs where possible to preserve cash.

In general, governments should consider reducing spending in areas where any short- or long-term impact is minimal, and where the decision is easily reversible if conditions are not as bad as expected.

Possible Process to Guide Decision-Making

Whatever cuts are considered, it is important to make decisions with as much information as possible. The more detailed information local governments have about programs and services provided, the better they can make decisions related to these programs. The following steps may help determine how to ensure essential services continue, and identify where some cost savings may be found:

- Identify all programs through a program inventory
- Identify essential vs. non-essential programs
- Evaluate savings (or potential costs) of performing or not performing each program or service
- Assess which employees support essential vs non-essential programs (and which programs need back-up support if an employee gets sick)
- Determine the mandate, reliance, and partnership opportunities for each program

Proven Strategies

While the current pandemic is unlike anything previously experienced in many ways, prior experience with local government fiscal crises does offer some guidelines on strategies that have proven effective in mitigating crisis situations. For example, Ammons and Fleck (2010) examined the cost cutting strategies local governments used during the 2008 great recession that can provide useful insights for today ([the article can be found here](#)). Governments should consider these principles to guide decisions as they navigate this crisis:

- Cut quickly; avoid delay – an early, deep cut, produces better results and is less harmful to morale than a steady stream of smaller cuts. This also allows cuts to be restored if the crisis is not as bad as feared. Good surprises are better than bad ones.
- Take a long-term view - Does the proposed reduction create increased costs in the future?
- Focus on core mission purpose, and highest priorities
- Emphasize innovation - empower departments and staff to come up with creative solutions to cut costs while maintaining services.
- Manage revenues as carefully as expenditures
- Examine and improve organizational design and processes
- Foster stewardship – be creative about encouraging all departments to engage in cost savings. Think about what might be done to incent departments to reduce spending.
- Look for areas of consistent surplus in prior budgets – reallocating these funds doesn't reduce costs, but frees up funds for high-priority use.
- Create a sense of mission, responsibility, and sacrifice, devise a workable schedule, stick with it
- Commit to communicating with all stakeholders (Miller and Svara 2009)

If cuts are going to be made, useful questions to consider include:

- Is the proposed reduction a one-time reduction, or an ongoing reduction?
- Is this a true reduction in spending or a deferment?
 - If it's a deferment, what is the plan to pay for it in the future?
- When is the greatest benefit related to this cut realized? Short term or long-term?
- What is our plan for this post-pandemic? Restore funding? Restructure?

Specific Considerations Related to Common Cuts (Kavanagh and Casey 2020)

Potential Action	Potential Pitfalls and Other Considerations
Short-term hiring freeze	<ul style="list-style-type: none"> • Should be targeted, rather than general. Evaluate whether not filling a position is going to create a staffing gap for an essential service. • Savings should be returned to a centralized pool so they can be directed where they are needed most.
Share personnel	<ul style="list-style-type: none"> • Consider if personnel can be shared across departments to meet increased needs in some areas. • Make sure personnel are qualified to adequately assist in the area they are being shifted to. • Be mindful to maintain integrity of internal controls.
Voluntary part-time status or voluntary furlough for employees	<ul style="list-style-type: none"> • Consider repercussions such as eligibility for benefits, pension calculations, etc. • Limit who can participate (make sure essential services are adequately staffed). • If these are precursors to potential mandatory time off or layoffs, be very clear about that.
Unpaid furloughs	<ul style="list-style-type: none"> • Clear rules needed for how to ensure essential functions are still performed.
Reduce energy usage	<ul style="list-style-type: none"> • Changing turn-off schedules or tightening temperature controls for buildings can save money. Some of these savings may be automatic if buildings are closed while employees work from home.

Sources and Additional Information

- Ammons, David., and Fleck, Trevor. "Budget-Balancing Tactics in Local Government." February 2010. <https://www.sog.unc.edu/sites/www.sog.unc.edu/files/reports/BudgetBalancing.pdf>
- Kavanagh, Shayne C., and Joseph P. Casey. "Cash Is King." GFOA. Last modified, 2020. <https://gfoa.org/cash-is-king>.
- Miller, Gerald J., and James H. Svara. "Navigating the Fiscal Crisis: Tested Strategies for Local Leaders." Alliance for Innovation. Last modified January, 2009. https://icma.org/sites/default/files/302108_alliance_icma_crisis.pdf.

This memo is part of a series of memos in the Local Government COVID-19 Fiscal Strategy and Resource Guide, available at closup.umich.edu/COVID-19. CLOSUP has partnered with public finance experts from universities, consulting firms, and research institutions from around the state to provide local governments up-to-date information as well as a set of ideas and tools that will help them strategically navigate the new fiscal landscape.

Have additional questions or issues you think we should address?

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