

## Three Tools to Enable Local Governments to Recapture Costs and Enhance Revenues

by Peter Moy

Today local governments are faced with the challenges of coping with a sluggish economy, more restrictive tax and revenue limitations, and the public's demand for more accountability and results. With costs often rising faster than revenues, governments must either create opportunities to enhance revenues and cut costs or face the prospect of reducing services to their citizens. Even though a local government's general fund is often the most vulnerable source of revenue, it is still called upon to provide support for many basic services demanded by the public. Given this environment, what steps can local officials take to enhance revenue and contain costs? Three tools to identify such opportunities include:



- **Indirect Cost Allocation Plans**
- **Cost of Service and User Fee Analyses**
- **Program Effectiveness and Efficiency Reviews**

### Indirect Cost Allocation Plans

Local governments have overhead and administrative costs that are essential to operations. Examples include costs incurred for a City Council, a Board of Commissioners, a City Manager or County Administrator, Human Resources and Finance Departments, government facilities, records management, and clerk functions. These costs are usually funded by a jurisdiction's general fund, but a jurisdiction has many other types of funds that support a variety of services and that use administrative and overhead resources. If there is no indirect cost allocation plan, several steps are needed to identify the opportunities for recovering costs from these other funding sources. These steps include the following:

- ☑ Identify overhead and administrative costs,
- ☑ Identify the users of the overhead and administrative services,

- ☑ Determine if any costs are being recovered from other funds,
- ☑ Establish equitable allocation factors for distributing costs to other funding sources, and
- ☑ Calculate the non-general fund share of costs.

If an indirect cost allocation plan already exists, the plan should be reviewed and updated periodically to assure that all services are included and that the allocation factors are still appropriate. Indirect cost allocation plans are usually required for jurisdictions seeking reimbursement for administrative costs from federal programs and grants. Even if you do not use such a plan for this purpose, an indirect cost allocation plan can provide valuable information for use in setting fees and evaluating the full cost of services.

### Cost of Service and User Fee Analyses

Local governments charge a variety of fees for many of the services they provide, and the basis for the fees is often either unknown or out of date. According to the Government Finance Officers Association, measuring the cost of government services is useful for a variety of purposes such as measuring performance, benchmarking, setting user fees and charges, assessing privatization and competition initiatives, and performing activity-based costing and management. A cost of service and user fee analysis identifies the full costs associated with providing a service and will provide a basis to discuss the percentage of costs that should be recovered from users or subsidized by the general fund or other funding sources. The full cost of a service includes indirect cost allocation plan as well as the direct and support costs associated with providing the service.

Once the full cost of service is known, elected officials can discuss whether full costs should be recovered for all fees or whether there are certain costs or services where less than full cost recovery is warranted, such as youth services or senior programs. FCS Group characterizes this effort as the public versus private benefit analysis. Recognizing that costs not recovered from fees are paid for from other revenues, such as taxes, less than full cost recovery may be justified based on the benefit the service provides to the public at-large, local policy,

*Do other funding sources besides the general fund contribute their fair share of the jurisdiction's overhead and administrative costs?*

or the practical consideration of whether the market can bear the full cost fee. In addition, a cost of service and user fee analysis provides for defensible fees, communicates the amount and bear the full cost fee. In addition, a cost of service and user fee analysis provides for defensible fees, communicates the amount and type of costs necessary to provide the services, creates an equitable basis for determining fee levels, and provides management with a cost benchmark and management tool to address concerns about costs. The following are the types of departments where fees are often charged for services and where a cost of service analysis may be beneficial.

- Planning and Land Use
- Building
- Community Development
- Parks
- Library
- Public Health
- Police
- Fire
- Public Works
- Transportation
- Utilities
- Animal Control

(In short, pretty much any department receiving fee revenue!)

### Program Effectiveness and Efficiency Reviews

Once indirect costs have been equitably distributed and the cost of service has been established, program efficiency and effectiveness represent the next focus to assure that scarce resources are appropriately used and that services are commensurate with costs.

Program effectiveness or efficiency reviews can help determine whether costs can be reduced or whether fees must be raised. In some cases where fees cannot meet the targeted

*Are programs operated effectively and efficiently?*

cost recovery levels, a program effectiveness or efficiency review is the only available tool to identify ways to close the gap between revenues and costs without reducing service. In today's environment, there are increased community expectations and demands about the cost, quality, and level of municipal services. In an era where the public is demanding more accountability and results at a lower cost from all levels of government, effectiveness and efficiency reviews often result in opportunities to control costs, improve service, and realign activities to maximize the benefit and service to the public. In essence the levels of service and the costs to deliver the service are evaluated to assess the public benefits and the relative costs. Program effectiveness and efficiency reviews seek answers to the following questions:

- Do programs and services have defined goals and are they effective in meeting those goals?
- Are there performance measures and benchmarks that measure the cost effectiveness of the services?
- Are processes and procedures for delivering services efficient?
- Are there alternative service delivery methods (e.g. outsourcing) that can be more effective or efficient?
- Have there been any significant changes in costs or policies that have affected service delivery.

In these types of reviews, several different types of analyses are conducted, such as workload analysis, business process re-engineering, performance measurement, overhead cost analysis, and "input-process-output" reviews. All of these efforts focus on "Why do we do this, and what added value does it provide to the customer/citizen?"

### What's Next?

These three tools provide an opportunity for jurisdictions to re-examine the services they provide by identifying the cost of service, determining how much the user or the public should pay to support services, and evaluating the public benefits and results of providing the services. These tools will help jurisdictions take steps to assure equity, cost effectiveness, and public benefit. As elected officials and governmental managers review their jurisdiction's budget, key questions and concerns will likely be raised about a variety of programs and services. Using the tools described in this article will help answer the following questions that are often asked by decision makers and elected officials.

- Do we know how much a service or program really costs?
- Should we be charging a fee for the service or how much of our costs are recovered through existing fees?
- Is the program or service provided in a cost effective manner and does it meet its goals and objectives?

If answers to the questions in this article are not available, make a plan to address your concerns and use the appropriate tool that meets your needs.

For more information on this subject, e-mail to [peterm@fcsgroup.com](mailto:peterm@fcsgroup.com).

Copyright © 2002, FCS GROUP