

Tools: Charges, Incentives & Targeting

"The policy making lesson of the contemporary economics of organization is this: construct policy so that individual and group interests coincide." ----John Brandl, 1998

A tried and true approach to redesign is aligning economic incentives to make policies more effective. We know that if a person has an incentive to do something, he or she is more likely to do it. Similarly, if a person has a reason *not* to do something, he or she is less likely to do it. For example, a higher sewer hook-up fee can result in less development because of the additional financial burden. Economic incentives may be related to paying for government or a government service, or they may be related to internal incentives to make the organization more productive. They may also be related to targeting fees or services to citizens most in need.

Paying for government services

Local governments primarily use general property taxes and state aids to fund their services. More and more frequently, local officials are faced with the question of which services should be funded by these general revenues, and which should be funded through a specific charge or tax? The provision of water by cities is an example of where general resources are *not* being used typically to support a service. Rather, cities charge citizens for water directly by the amount of usage (e.g., a fraction of a cent per gallon). In a sense, a person can choose how much to pay for water by regulating his or her household consumption. During a hot summer, a city could ban water use for sprinkling grass or it could simply charge more for the water.

Parks and libraries, on the other hand, are paid for by general resources. But in addition to this, cities and counties have historically used more than general resources, in part to accomplish a given goal. For instance, libraries assess users with fines for late returns. This is a case where the fine is an incentive to return the materials in a timely manner so that others have access to the materials. Similarly, some park programs are free while some require a fee.

Innovation and service redesign asks the question of whether the current mix of general resources and special charges is appropriate. Should water fees be increased to help support general city services? Should transportation to school be paid for on a subscription basis, rather than being paid out of general

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resources? If it were, would the people living farthest from the school pay more?

We charge some fees because certain people benefit directly from the service provided. Permit fees for developers, school fees for extracurricular activities, ambulance costs and restaurant inspections are all examples of this.

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Minnesota has traditionally used general resources more than direct charges for services. Should this continue? Common good versus special interest is the decider, but the bias toward common good could be shifted if there were a shortage of general revenues. For example, some cities and counties charge for response to home alarms on repeated calls. Parking is no longer free in some parks. A new approach might have prisoners pay for the expense of their jail time if they could afford it. Should there be a greater use or increase in share of assessments?

A local government may also choose to target the fees to those more capable of paying, i.e., means testing. The free lunch program in schools is one example of this. Another example is reduced park program fees for low-income or senior citizens. A government may also attempt to use "value capture" methods like tax-increment financing or assessments. Listed in the examples is the City of Minnetonka's innovative value capture for a new interchange.

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It's imperative that local governments review fee discounts or special services regularly. Often, a discount or a special service is enacted and then never—or infrequently—reviewed. Local governments should periodically reexamine these decisions. For instance, should a senior discount be retained with the number of seniors increasing? Are seniors those over 55, or 60, or 65, or the age of eligibility for social security, which is now 66 years old?

Incentives within local government

There are many incentives that can be used in local government. One is to make sure a given activity is charging for all of its costs, so that citizens don't overuse the service. Some local governments don't allocate overhead costs like accounting, human resources, elected officials, communications, payroll processing, etc. to departments when they consider the fees that are needed to offset the full costs of the function. Are overheads allocated to the water department so that the water charges pay for the total cost of water production? Are overheads allocated to special assessments?



Each year, many local government departments close the books with positive budget balances. Traditionally, there is no reward for the departments producing the positive balances. Should a department producing unspent balances be able to roll over a portion of the dollars to the following year? This would be an incentive that would help to avoid hasty end-of-year spending to simply use up unspent dollars.

Osborne and Gaebler (1992) used an approach to innovation and redesign to create adequate balances at year's end: "As originally conceived and implemented, [expenditure control] budgeting strategy gave each department the same basic mission and the same budget as in the previous year (with an inflation adjustment) but abolished the line-item specification of expenditures, permitting the department to keep any savings and reinvest them in other mission related activities." This could be a powerful technique to get departments thinking more creatively.

Another form of incentives is the tools schools use to motivate students to learn. The following photo depicts a school that has moved fully to an individualized testing-progress approach. Does this look different from a traditional classroom?



Employee incentives

Rewarding employees directly for performance is another way to motivate them. Osborne and Hutchinson (2004) cited the following examples of employee incentives that improve performance:



- Direct customer feedback
- Performance awards
- Performance cash bonuses
- Gain-sharing
- "Psychic" pay (telling employees they're doing a great job)
- Performance-based contracts
- Performance scorecards

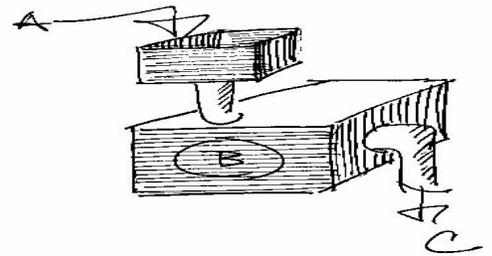


A controversial idea is to compensate employees partially or wholly on performance. This would require a well-functioning performance appraisal system in local government that sets specific and measurable goals for employees. Today, local government employees receive salary increases mostly for "time in grade" or for added education. A jurisdiction that wanted improved performance could consider blending performance evaluations with longevity in determining salary increases.

To illustrate the *problem to redesign* methodology for this chapter, an example of implementing a garbage-recycling program follows:

Step 1. Clearly define the problem

Need to recycle home garbage to save the cost of landfills and help improve the environment.



Step 2. State the desired measurable outcome

Separated garbage at all households will be recycled once every two weeks.

Step 3. Investigate why traditional approaches aren't working

Pass an ordinance requiring compliance. Send garbage inspectors out to give citations to those citizens violating the policy. Citizens become angry about inspections and government control.

Step 4. Identify alternative theories or assumptions that address the problem

Incentives are effective motivators for citizens when they believe they can save money.

Step 5. Innovate and Innovation/redesign

Give a discount on garbage collection fees for recycling. If the garbage collectors note the absence of recycling, they let the sanitation management know to eliminate the discount for the homeowner.

There are limitations to using economic incentives to accomplish a chosen policy more effectively:

- Not all people are motivated by economic incentives.
- Incentives can outgrow their usefulness.
- Targeting those in need can reduce a supportable majority for the program, because there are too few people receiving the benefit.
- Charges can become onerous and are not tax-deductible.



Real examples of charges, incentives and targeting include:

- [City of Chanhassen Tiered Water Pricing](#): This city instituted a fifth tier in its water pricing to have the largest users of water pay the highest rate. It also promotes water conservation.
- [Foster Children Placement Incentives](#): In 1998, Minnesota began to contract for adoption services. The State pays providers only when they complete certain activities designed to expedite adoptions. Through these contracts, private adoption agencies focus on the hardest to place children. Private providers work across the state, but select certain service areas toward which to target their efforts.
- [Roseville False Alarm Charges](#): The City of Roseville gives homeowners three false alarms from security systems. After that, the city charges \$100, \$135, \$170 and \$205 for repeated false alarms. (Roseville typically receives 1,200 alarms calls a year.)
- [PaySchool Program](#): MSBA, with MASA and the Service Coops as co-sponsors, have developed a no-cost program that allows parents to pay school fees by credit card and for the schools to allocate these funds appropriately to the correct lunch and activity accounts.
- [Q Comp](#): Nearly a third of Minnesota's K-12 teachers will have some form of incentive compensation under the Q-Compensation program begun in 2006. The 50 school districts and 54 charter schools participating in the Q-Comp program receive \$260 more per student from the state.
- [P-Card System](#): MASA, with MSBA and MASBO as co-sponsors, has developed an on-line credit card based invoice payment system. This system, while more secure and efficient for school districts, also provides a rebate to participating districts. This past year \$355,000 was rebated to school districts.
- [Minnetonka Interchange Financing](#): In order for Minnetonka based UnitedHealth Group to proceed with an expansion that would bring 1,600 more employees to its Minnetonka campus, a new interchange at Highway 169 and Bren Road needed to be built. United Health Group agreed to contribute \$5 million toward completion of the project.



- [Hennepin County Juvenile Detention Alternative Initiative](#): The Hennepin County Dept. of Community Corrections and Rehabilitations participated in the Juvenile Detention Alternatives Initiative, a collaboration of juvenile justice stakeholders who assign the least-restrictive, community-based alternatives for low-risk offenders.
- [Minneapolis “smart” parking meters](#): The latest way Minnesota’s largest city is attempting to maximize its parking revenue. One of the key features is the inability of a new parker to use the previous parker’s unused time.
- [Opportunity New York City](#): NYC offers cash incentives to its poorest citizens for socially acceptable behavior.
- [Incentives for personal responsibility for long-term care](#): Proposed by the Citizens League, similar to programs in other states, this program encourages families to care for elderly family members themselves, shifting the burden of long-term care back to the family rather than the state.
- It’s easy to “[Give a Compliment](#).” The City of Saint Paul has created an online tool for citizens to provide employees or offices with “psychic pay” in its “Give a Compliment” section of the city website.
- [Residential parking permits](#): The City of Saint Paul charges residents to alleviate parking problems in high-demand areas without installing meters or strict time rules.
- Mahnommen County Social Services: Mahnommen County has partnered with a local car dealership to purchase used cars for qualifying MFIP (public assistance) recipients who do not have reliable transportation, in order to make it possible for them to maintain work and thus move off public assistance. This has resulted in 75 percent of participating families leaving public assistance because they maintained employment.



Further readings and examples of Charges, Incentives and Targeting are available at The Humphrey School of Public Affairs [Local Government Innovations Website](#).

