

Operating Government Like a Business

In a February 18, 2009 [Government Executive](#) article, [John Mercer](#) opined that in order for the new administration to succeed, they “must bring about dramatic transformation in transparency and accountability throughout federal government. The best way is through a system of cascading performance budgets that show how spending is linked to planned results in every program at every level of an agency.”

Over the years government has made numerous attempts to operate more like the private sector. The ["Whiz Kids" of the '60s](#); [Total Quality Leadership \(TQL\)](#); importing corporate talent into the organization; and [Lean Six Sigma \(LSS\)](#). Few such ideas have succeeded and of those which did, even fewer have endured. Government has simply been unable to break old habits and has not been inclined to reward innovative or transformational change. In [Neal Thornberry's](#) book, [Lead Like an Entrepreneur](#), he states entrepreneurial creativity is not just relegated to “...coming up with brand new products or services: it can involve creative distribution and delivery, an innovative business model, or merely improving on the better mousetrap.” If we want to operate more like a retail corporation, improve transparency, and drive accountability, we must transform and adopt an “innovative business model.”

The Profit Paradigm: Corporations exist to make a profit and their missions, visions, strategic objectives, actions, systems, processes, and performance metrics are aligned to do so. This does not denigrate other values/virtues worth aspiring to...it just means they must generate a profit if they expect to stay in business and continue to deliver shareholder/stakeholder value. Organizational alignment requires that strategic objectives support the mission and vision and performance metrics, skill sets, systems, and processes be developed to drive these objectives forward. Since corporations have a strategic objective to maximize profit, their financial metrics are designed to focus on profit and profit drivers. Additionally, their leaders are rewarded for maximizing profit and are held accountable for failing to meet profit targets. This is not to say that maximizing profit takes precedence over other strategic objectives, but it should have equal importance if significant gains in efficiency are going to be achieved and shareholder value returned.

Government can, and should, operate the same way. When provided revenue (execution dollars), government activities should be expected to deliver a profit while maintaining/improving service levels. Additionally, the leaders of these activities should be held accountable and rewarded for doing so. Despite existing paradigms (comptroller centric, budget oriented, spend mentality), government can operate like a “for profit” organization and run more efficiently and effectively. As in private industry, government leaders can be held accountable and indeed measured on their ability to maximize stakeholder value through profit generation.

Defining “expenses” for government organizations is easy since government has traditionally been run with an “expense centric” view. Expenses are the cost of doing business or in the government’s case, the cost of operating. Defining “revenue” on the other hand requires a willingness to break old habits and perceptions. Revenues are simply the execution budget an activity or command receives. The typical objection to a “government for profit” model is that “government organizations cannot make a profit, because they don't have any revenues.” Simply treating the funding received to execute a budget (regardless if it is equal to, more than, or less than what was requested) as revenue allows us to determine profit. A simple profit equation becomes: ***Profit = Execution Dollars (Revenue) - Expenses***

This only works if government leaders break the, “Here is your budget for the year, now go out and spend it” mentality. Instead, if they operate from a profit perspective, they can establish a “Here's your revenue for the year, now go out and return a 5% profit” mentality. Think about this for a minute...would your behavior change if instead of being rewarded to spend your budget, you were rewarded to return a 5% profit?

The Balanced Scorecard Framework: Using a balanced scorecard framework for driving efficiency and effectiveness aligns goals, systems and rewards to maximize profit AND service levels. In 1996, [Robert S. Kaplan](#) and [David P. Norton](#) wrote [The Balanced Scorecard](#). This framework measures efficiency and effectiveness across four quadrants: Financial, Customer, Internal Process, and Innovation/Growth (see Appendix A for an example). The balanced scorecard should be designed so each quadrant's measures align with the command's strategic objectives, vision and mission. Profit should be the key financial measure as it is the measure which changes the way we think and drives change. However, profit is just one measure in the balanced scorecard and it must be measured in concert with the other objectives to drive desirable behavior. By aligning balanced scorecard objectives with strategic goals and measuring them, leaders will be expected to achieve profit objectives while also working to improve customer satisfaction, enhancing internal processes, and driving innovation and growth through their employees. In this light, the balanced scorecard is like a rheostat. Tweak it too far toward profit and customer satisfaction and morale may suffer. Tweak it too far toward customer satisfaction and innovation/growth or profit may suffer. Leadership, through empowerment of the workforce, seeks to set the rheostat just right. If done from a balanced scorecard perspective, an organization will be focused on achieving profit, and improving employee and customer satisfaction.

With this framework, it is also possible to create a single metric for measuring the success of a government agency, activity, installation or an individual. By using a weighted average, each balanced scorecard quadrant can be scored and a single metric generated. It is also possible for additional metrics to be adopted, such as return on assets (where assets equal the dollar value of buildings/capital equipment on an installation). In this case, government leaders would have an incentive to improve return on assets by increasing profit and/or reducing infrastructure.

Combining Profit and the Balanced Scorecard: The balanced scorecard allows an organization to align metrics throughout the organization (cascading in John Mercer's view). For the financial quadrant, a top level scorecard would show overall profit as the financial metric. Drilling deeper would show profit at program, region, installation, and even individual (tied to their [National Security Personnel System \(NSPS\)](#) objectives) levels. This capability would allow leaders to identify opportunities for improvement and take action. Profit issues could be analyzed by drilling down into other financial metrics to determine what is driving poor performance. This same approach would be undertaken for all balanced scorecard quadrants. After setting strategic objectives and balanced scorecard metrics, regular monitoring of progress would ensure organizations and individuals are held accountable for results. Most importantly, the subjective view of an individual's or organization's performance would be replaced with an objective view that helps align the organization both vertically (drill-down) and horizontally (all organizations measured and compared in the same way). In sum, by using a profit and balanced scorecard framework, government organizations can operate like a retail corporation and provide more value to their stakeholders.

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APPENDIX A – Balanced Scorecard Single Metric Example

The following example depicts how to develop a single performance metric using the balanced scorecard approach for two different organizations. Assume the organizations use a 5-point scale for measuring each quadrant and that Profit is weighted at 50%; Customer Service at 25%; Process at 15%; and Innovation/Growth at 10%. The four factors could be measured as follows to determine a single performance metric:

Profit: Execution Dollars (Revenue) – Expenses, or in other words, a positive balance after budget execution.

Goal is 5% profit. A 5-point scale might look like this:

1 < 4% profit 2 = 4% - 5% profit 3 = 5% - 6% profit 4 = 6% - 7% profit 5 > 7% profit

Customer Satisfaction: customer surveys which grade on a 5-point scale. Goal is 4.5.

1 < 4 2 = 4.0 - 4.5 3 = 4.5 - 4.6 4 = 4.6 - 4.75 5 > 4.75

Process: use a readiness or LSS improvement as an indicator of process capability

In this example, we will assume each achieved their readiness goal and received a score of 3.0.

Innovation/Growth: could use # of Best Practices; # of completed LSS projects; Training \$ per employee.

We'll use # of completed LSS projects for this example.

1 = 1 2 = 2 3 = 3 4 = 4 5 or more = 5

ORGANIZATION A

<u>PROFIT</u>	<u>CUSTOMER SATISFACTION</u>
Profit Achieved = 3%	Customer Survey Score = 4.70
Score on 5-pt scale = 1.00	Score on 5-pt scale = 4.00
<u>Weighting</u> = 0.50	<u>Weighting</u> = 0.25
Weighted Score: = 0.50	Weighted Score: = 1.00
<u>PROCESS (15%)</u>	<u>INNOVATION/GROWTH (10%)</u>
Readiness Score = Achieved goal	Completed LSS Projects = 3
Score on 5-pt scale = 3.00	Score on 5-pt scale = 3.00
<u>Weighting</u> = 0.15	<u>Weighting</u> = 0.10
Weighted Score: = 0.45	Weighted Score: = 0.30
Organization A Performance Score = 2.25 0.50 (P) + 1.00 (CS) + 0.45 (Proc) + 0.30 (I/G)	

ORGANIZATION B

<u>PROFIT</u>	<u>CUSTOMER SATISFACTION</u>
Profit Achieved = 6.5%	Customer Survey Score = 4.55
Score on 5-pt scale = 4.00	Score on 5-pt scale = 3.00
<u>Weighting</u> = 0.50	<u>Weighting</u> = 0.25
Weighted Score: = 2.00	Weighted Score: = 0.75
<u>PROCESS (15%)</u>	<u>INNOVATION/GROWTH (10%)</u>
Readiness Score = Achieved goal	Completed LSS Projects = 2
Score on 5-pt scale = 3.00	Score on 5-pt scale = 2.00
<u>Weighting</u> = 0.15	<u>Weighting</u> = 0.10
Weighted Score: = 0.45	Weighted Score: = 0.20
Organization A Performance Score = 3.30 2.00 (P) + 0.75 (CS) + 0.45 (Proc) + 0.20 (I/G)	

Organization A achieved an overall performance score of 2.25 versus Organization B's score of 3.3. Organization B returned more shareholder/stakeholder value than Organization A and the leaders of Organization B should be evaluated/rewarded at a higher level than Organization A. Viewing the balanced scorecard results also allows drill down capability into underperforming areas.