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1911

## Business management of municipalities

Harvey S. Chase

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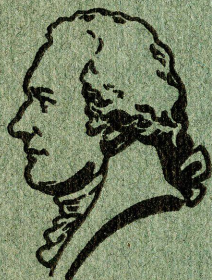
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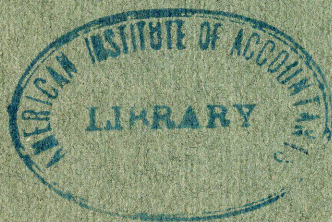
# BUSINESS MANAGEMENT OF MUNICIPALITIES

by  
Harvey S. Chase



**ALEXANDER  
HAMILTON  
INSTITUTE**

H-65



# **BUSINESS MANAGEMENT OF MUNICIPALITIES**



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# BUSINESS MANAGEMENT OF MUNICIPALITIES

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By HARVEY S. CHASE, C. P. A.

Public Accountant, Expert on Municipal  
Affairs and Member of President's  
Commission on Economy and Efficiency

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One of a Series of Lectures Especially Prepared  
for the Alexander Hamilton Institute

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HARVEY S. CHASE

## HARVEY STUART CHASE.

Harvey S. Chase was born in Portsmouth, New Hampshire, June 18, 1861. His boyhood was passed at Haverhill, Massachusetts, where he graduated from the high school in 1879. The next four years were spent at the Massachusetts Institute of Technology, Boston, from which he was graduated in 1883 with the degree of Bachelor of Science in the course of mechanical engineering; he was secretary of his class, and has continued so since graduation. Upon graduation he entered the cotton mills at Manchester, New Hampshire, and spent two years learning the business of cotton manufacture. In 1886 he was appointed superintendent of outside work at the Great Falls (New Hampshire) Cotton Manufacturing Company, having charge of the gas works and water works, and two years later was made treasurer and manager of the company. In 1891 he became treasurer and manager of the International Ore Separating Company, and other enterprises connected with mining and manufacturing in New York City, with mines in Tennessee. At this time he was elected member of the American Society of Mechanical Engineers, of the American Institute of Electrical Engineers, of the American Institute of Mining Engineers, and of the Engineers' Club of New York. After the panic of 1893, which interrupted mining enterprises, Mr. Chase became treasurer and auditor of various corporations, and in 1897 removed to Boston and established offices as a public accountant, from which the firm of Harvey S. Chase & Company resulted. This firm has offices at 84 State

Street, Boston, and Mr. Chase's work during the last fifteen years has been almost wholly along the lines of investigations, audits, and installation of systems of accounting in New England and various parts of the country.

Mr. Chase was appointed a member of the National Municipal League's Committee on Uniform Accounts and Reports of Municipalities in 1899, and has been foremost in introducing standard methods of accounting and reporting in a large number of individual cities in various parts of the country, as well as having acted as consulting expert accountant for state boards, including the states of Ohio, New York, and Massachusetts. Mr. Chase was retained by the Mayor of Boston to make a long series of investigations of the different departments in 1902-3, and has been engaged continuously in the reorganization and standardization of accounting methods and reports in other New England municipalities. In 1911 he was appointed by the Governor of Massachusetts as an expert investigator to examine and report on various departments of the Commonwealth of Massachusetts, and in May, 1911, Mr. Chase was called to Washington to take part in the work of the President's Commission on Economy and Efficiency, and was appointed by President Taft as one of the five Commissioners.

Mr. Chase is recognized the country over as an authority on organization and accounting and is considered an expert in state and municipal affairs. He has frequently been called upon to address such bodies as the National Municipal League and the Economic Club of Boston.

## Business Management of Municipalities

The rapid advances during the last quarter century in the development of scientific principles underlying the management of commercial enterprises, have led more than one citizen to the question—"Why does not our city or town manage its business along the same efficient business lines?" Officials and others have attempted to answer this question by pointing out that a government is not conducted for profit; it has nothing to sell; it does not encounter keen competition; there is no capital invested upon which a return is expected. "Therefore," it is argued, "business principles do not apply." While these premises are, on the whole, truthfully stated, the conclusion drawn is fallacious, for, as a matter of fact, cities and business concerns are alike in very many respects.

While it is true that it is the aim of a commercial enterprise to furnish its proprietors with the greatest amount of profit at the least possible cost, it is also true that the municipality has as its object the furnishing of the greatest amount of public good to its proprietors (the citizens) with the least possible outlay. The owners of a commercial undertaking dictate the policy and hold responsible the employees charged with carrying on the work. The voters in a community similarly dictate the policy (or are presumed to) and should hold the officials responsible.



Consider, for example, a water-works or gas works owned by private interests. The public service corporation would hardly be satisfied with anything less than maximum efficiency on the part of its employees and its plant. It knows just how much it costs to maintain the various departments, and immediately becomes aware of any unusual increase in that cost—which increase is followed by prompt investigation. It also knows when the cost is lowered, and recognition is generally given to the individual or individuals responsible. It would scarcely be possible for a new improvement or invention to exist very long without attracting the attention of the management, and, if its acquisition would result in reducing the cost of production, or increasing the life of mains, machinery or other assets, it would only be a question of time when the company would cause it to be installed.

That is to say, the stockholders, through their board of directors, expect that each gallon of water sent through the mains shall be delivered at the lowest possible cost, and that the pumping station and other equipment shall be kept at the point of greatest efficiency. By comparing the company's financial and statistical reports with those of other similar enterprises, the directors and stockholders are able to determine whether or not this condition exists.

There is no sufficient reason why a water-works, owned by a city, should not enjoy the same kind of efficient management.

A business concern is obliged to dispose of its product and this involves careful attention to its

selling organization. With this activity we are not here concerned. The municipality has a constant market for its product; in fact, the demand exists before the supply is created. Putting aside, therefore, consideration of selling methods, perhaps the most important elements upon which a business is founded are (1) organization; (2) financial policy; (3) system of records. And it will not require much thought to perceive that the same elements enter into the efficient management of a municipality.

### **Organization**

The business executive has continually before his mind's eye a compact, orderly, smooth-working engine. He selects and arranges the controls, the various functional parts, and sees to it that each smallest wheel or screw exactly fits. When one part becomes obsolete and unable to perform its duties, it is replaced. The engine, as a whole, must produce, and each individual part must do its share. There is no final reason why the organization of a governmental body should not be planned and executed with equal care. This subject of organization has, however, been discussed on the platform and on the stump, in magazine articles and in books, and I should hardly attempt to deal with it in this paper. The purpose of this Lecture is rather to discuss the manner of handling a city's capital by those already in charge.

### **As to the Financial Policy**

The method of providing income for current expenses and purchases of additional property, as it

exists in most cities to-day, is briefly this: Some-time before the beginning of the fiscal year a committee or other authoritative body (sometimes called a Board of Estimate and Apportionment or a Tax Board) estimates the amount of money which will be required to run the various departments during the ensuing year. This is called "making a budget." Each department of the municipality is required to submit to the board a statement of expected expenses, and is finally allotted an appropriation which may or may not equal the amount asked for. To the appropriations thus allotted are added requirements for interest to be paid on outstanding bonds and notes; sinking fund contributions; outlays to be made for permanent improvements (not paid for by bond issues) and the like. Finally a total sum is reached which must be provided for from the year's income. After the assessors have appraised all taxable property in the community, the total of the budget is provided by establishing a tax rate which when levied on the total property will provide the total amount of the budget (less other sources of municipal income). Each property owner is obliged to pay into the city treasury an amount found by multiplying the assessed value of his property by the tax rate. If, during the year, all the taxes were paid, and all the appropriations were expended, the slate, at the end, would be clean—no cash on hand, no debts owing by or to the city, while during the period of collecting taxes expenses would be paid out of temporary short time loans which would be liquidated out of tax receipts. But my experience in all the cities—

both large and small—with which I have had to do, is that this desirable condition is never reached—not even approximately. Why?

In the first place, all the taxes are not collected during the year—a small percentage never; secondly, the appropriations are rarely sufficient to cover actual expenses. This latter factor is largely due to another reason, namely, insufficient information in the hands of the authorities; to this I shall refer later in this Lecture. Consequently, before the year is over it is found that more money is required. The only thing which can then be done is to borrow or use money from other funds, usually derived from long term bond issues, so that the greater part of the interest and practically all of the principal must be paid, not by the taxpayers who reap the benefit of the money borrowed, but by citizens who pay taxes during subsequent years. Manifestly, this is inequitable.

In addition to this evidence of inefficient management, there is another serious fault to be found in connection with issuing long term tax loans. I refer to the obvious waste of public money. Estimates are usually based upon figures of past years and frequently fall short, indicating that at least some of the additional money required is due to lack of control over expenditures.

Any clear-headed business man would not permit such a condition in his own business. He would insist that current expenses be paid out of current income. Only money for permanent improvement, such as public buildings, parks and the like, should be raised by bonds, the interest and principal of which are spread over a term of

years and consequently borne by those to whom some, at least, of the benefits accrue. Lastly, he would see to it that a proper system of accounts is installed, enabling him to ascertain monthly the exact state of affairs and furnishing reliable records, properly classified, of income and expenditure upon which to base judgment for future operations.

The city of Lynn, Mass., supplies us with an interesting example of the results which may be obtained through the use of a scientific accounting and reporting system. The city caused such a system to be installed in 1909, and the City Auditor's balance sheet of October 31, 1910, exhibits a noteworthy reduction in the deficiency of annual revenue. At the close of 1908 the deficiency of revenue was \$78,386.21; at the close of 1909 this figure had been hammered down to \$8,702.18—a reduction of almost 90%. This reduction came about solely because in the monthly reports the prospective deficiency stared the Mayor and Council in the face and could not be escaped.

### **History of the Uniform Municipal Accounting Movement**

During the past eleven years a movement has been taking place that means more for the ultimate regeneration of our Municipal Government than any other one factor. This movement is the one for standard and uniform municipal reports, mandatory by statute law upon all cities in a state. By the operation of the United States Census a standard classification of municipal accounts is now applicable, and in the Census bulletins has been already applied to every city of reasonable size

throughout the whole country. The story of this movement is interesting. It began in Newton, Mass., in the year 1900, when the city for one year by vote of its mayor and aldermen made the first practical experiment in standard and uniform reporting by adding an appendix to the City Auditor's report drawn up on the schedules adopted by the National Municipal League. This printed report was sent all over the country. The same form was immediately adopted by Baltimore, and later Chicago, Cambridge, New Bedford, Brookline, Minneapolis, Rochester, Duluth, Pawtucket, R. I., St. Louis, and Houston, Tex., followed the new plan.

On May 10, 1902, the State of Ohio passed a uniform public accounting law, giving the state auditor complete control of the accounts and reports of all Ohio cities, towns and counties. This statute directs that the auditor shall formulate and install a uniform system of accounting, and that he "shall require from every taxing body and public institution financial reports covering the full period of each fiscal year"—such reports are to be published by the state in an annual volume of comparative statistics. The forms for the annual reports group receipts and expenditures in a similar manner to the grouping adopted by the National Municipal League.

It was about this time that the Census Bureau began to survey the municipalities of the country in order to carry out a federal law for the collection of statistics of cities. It found the National Municipal League schedules in use in so many cities that these classifications were adopted at once as its own basis. A conference on this subject was held

at Washington, (November 19 and 20, 1903,) attended by officials representing various sections of the country, by several prominent public accountants, and by representatives of mercantile associations and of state boards. This conference and the subsequent suggestions arising from the experiences of city auditors and treasurers the country over led to a second similar conference, February 13 and 14, 1906. At this time the uniform schedules were modified and improved and schedules for reporting the operations of municipal industries and public service corporations were discussed so that now we have arrived closely to a standard classification for city reports whereby comparisons of financial results can be correctly made.

The State of New York, during the period between 1902 and 1906, passed various laws leading toward standardization of municipal reports and the State Comptroller is directed to procure reports from the municipalities of the state. The form of these reports is prescribed by the Comptroller who has followed the schedules adopted by the Census Bureau.

Iowa was the next state to fall in line. On April 5, 1906, the general assembly approved an act providing for an annual report of the financial condition and transactions of each city and town. The auditor is required to prescribe the system of accounts to be adopted, embodying "so far as practicable the latest and most approved methods in municipal accounting, especially the classifications and definitions of municipal finance in use in the National Census Office."

During the same year the first Massachusetts act relating to uniformity of municipal reports was passed after an educational campaign of three years. It required that each city and town in the Commonwealth should report to the Chief of the Bureau of Statistics on blanks provided by him. These blanks, also, were modeled after the census schedules, modified to suit local conditions. At this writing (June, 1911) the Commonwealth is causing investigations to be made with a view toward still further improvement.

The State of Indiana has enacted an exceedingly detailed and mandatory law relating to control of county and municipal accounting methods.

While various states have thus been busy remodeling the reports of their municipalities, a large number of cities have, of their own initiative, adopted improved methods. In addition to those already mentioned, are Atlanta, Ga., Birmingham, Ala., Camden, N. J., Charleston, S. C., Denver, Colo., Grand Rapids, Mich., Haverhill, Mass., Holyoke, Mass., Kalamazoo, Mich., Milwaukee, Wis., New Rochelle, N. Y., New York, Philadelphia, Portland, Me., and many others.

### Prominent Features of the Uniform System

It might be well to here emphasize the *likeness* in certain fundamental aims, of both municipal and commercial systems of accounting. Almost every one is familiar with the primary distinctions of commercial accounts "Capital" and "Revenue"; that is to say, between those classes of accounts which have to do with "assets and liabilities" and those which have to do with "income and outgo."



The one represents properties, securities and other assets belonging to the organization, together with the debts owed by the organization as well as its capital stock liabilities. The other relates to earnings which have come in during a certain period or have accrued during that period, together with expenses which have been incurred during the same period. It has been said frequently by persons actually engaged in governmental accounting that the likeness I am endeavoring to demonstrate does not exist. In fact, to quote the words in a recent address by a public accountant familiar with ordinary methods of governmental accounting, such a relationship ought not to be considered at all. This gentleman said: "The consideration of 'Capital' and 'Revenue' which characterize the accounts of all private undertakings are conspicuously absent in the accounts of cities and, in fact, in all public accounts, and accordingly neither the 'Balance Sheet' as commercially understood, nor its inseparable companion the 'Profit and Loss' account, finds any place in the reports of public finances."

I wish to make immediate and emphatic objection to this statement. My experience among cities, both large and small, in various parts of the United States during the last fifteen years, has led me to certain conclusions from which I find myself unable to escape, and one of these conclusions bears very closely upon this matter of "Capital" and "Revenue" in municipal accounts. In fact, it appears to me that we do have and must necessarily have in city affairs, the same distinction in classes of accounts which are represented by

these titles "Capital" and "Revenue" in commercial affairs. It will be found impractical to install sound accounting methods in municipalities, in my opinion, unless these distinctions are recognized, whatever be the titles given to these different classes of accounts. The word "Capital" is not a satisfactory term to apply to municipal accounts. For this reason I have coined and used the word "Non-revenue." The term "Revenue," however, and "Revenue Account," used in very much the same sense as a "Profit and Loss" account is used in commercial affairs, is one of the most essential features of a proper installation of sound methods of accounting in cities. Of this I am fully convinced, and for this reason: While, as the authority I have quoted says, "The question of *gain* or *profit* finds no proper place in municipal accounts," the question of *surplus* or *deficiency* of revenue is an exceedingly important item in such accounts. This question: Whether or not the revenue pertaining to a fiscal period is in excess of the expenditure which that revenue is supposed to meet—is one of the fundamental problems which a proper system of accounts in a municipality should answer clearly and definitely. The corollary of this statement is evident. If the current revenue has not provided for the current running expenses of the city, then borrowed money must be used to supply this deficiency, and such borrowed money can be liquidated only out of future revenue. Thereby such deficiencies of the present become unwarrantable burdens upon the taxpayers of the future.

I have examined city after city in which, owing to the crude methods of accounting in vogue, the municipal officers year after year permitted the expenditures to exceed the revenues available, and thereby municipal debts have piled up. These debts, being complicated by and mixed with other debts which have been issued for public improvements and similar purposes, have been almost inextricably confused in the accounts, and it has been beyond the capacity of the officers to determine whether, or by how much, the city was running behind annually. In fact, as may be readily imagined, a considerable number of municipal office holders do not sincerely desire that the public shall know how much to the bad their expenditure is carrying the city. They prefer that the finances of the city should run along as best they may until their own terms of office have expired. "After us, the deluge," is too frequently the motto of political office holders. Even if these officials are honest, and do desire to exhibit the actual conditions to the public, they find themselves handicapped by unsound methods of accounting, based on mere cash accounts, which, under provisions of law, are the prevailing methods of accounting in many municipalities to-day.

### Aim of the Uniform System

Briefly stated the Uniform classification, as laid down by the United States Census Bureau, aims to place in the hands of city authorities, and through publication, in the hands of the citizens, monthly reports showing income accrued or received, its sources and how applied; showing expenses in-

curred and to what appropriations they have been charged; showing balances remaining in the various appropriation accounts, and showing comparisons with similar income and expenditure of the previous month and of the same month during the previous year. The monthly reports should also include a balance sheet, similar to the balance sheet furnished to business executives, exhibiting the exact relation of assets to liabilities, and showing the surplus or deficiency at the end of each period. On pages 20 and 21 is reproduced a balance sheet rendered by the city auditor of Lynn, Mass. (previously referred to), which will serve as an illustration.

### The Critic Answered

This movement, like all others, is not without its critics. "What we need," they say, "is the right kind of men to take care of our affairs. The book-keeping system will then take care of itself." Very true, as to the first point, but how shall we get the men? Have not cities been trying throughout the whole municipal development in this country to get the right men, and when they get an efficient man to keep him; and have they not found themselves unable to do so? They tell us that in the good old times of small municipalities we did get the men and did get efficient and economical government without scientific systems of bookkeeping. This is very likely true, but so also we did business in those times in single entry ledgers and often with the whole bookkeeping of a considerable establishment carried by the manager

“under his hat.” Would such methods do for the commercial enterprises in the year of grace 1911? They certainly would not, and no more can the old methods in cities and towns provide for the present with its immense development of municipal functions. What did the cities do in the recent past and what do they do for their citizens to-day? Compare any city fifty years ago with the same city to-day. Look at the increase of city departments, the enormous development of civic functions, and remember that the amount now spent annually upon streets alone would have been sufficient to cover the whole cost of the municipal government not many decades ago.

Suppose the stimulation for competition for credit and honor from the community be added to the present inducements for capable public officials. Suppose by promptly issued comparative reports it should become evident to all that the head of one department has done better than others in his own city or better than those in similar departments in other cities, and suppose that thereby this official's hold upon his office and his hope of future promotion become strong, how will all this help in the Augean task of raising the level of capacity and efficiency in our public service?

To be commended for good work by his fellow citizens is almost unknown to public officials in these days. We are too apt to condemn all public servants together, the good and bad alike, whenever some unsavory story of municipal politics appears. This injustice should be stopped. There should be discrimination, the capable must be dis-

tinguished from the incapable, the prudent from the extravagant, and the incorruptible public servant from the corrupt one.

How can this be done except by uniform and comparative public accounting and reporting? How else can these distinctions be made? How otherwise can the capable man be rewarded and the incapable one dismissed? Let the official who does well be shown forth in the results of the administration of his trust; let him receive the honor and the security of office which are due him, and we will never lack for public servants to play the same important parts that honorable and successful men play in private affairs. This is what uniform and comparative public accounting and reporting stands for, as I understand it.

### **The Voter Benefited**

Furthermore, such reports would form the basis, the starting point for intelligent discussion of city affairs by public officials, and by the citizens generally.

All this is bound to come, and the sooner it comes the better, for then public comparisons can be made of different experiments in municipal administration, such as commission government in Galveston, mayor and council as in Nashville, town selectmen as in Brookline, representative council as in Newport, and all others, so far, at least as financial results are concerned. The intelligent citizen will, under such conditions, have no excuse for misunderstanding his city's affairs, or for failing to take part promptly in remedying bad government.

CITY OF  
**City Auditor's**  
 November 15, 1910 as  
**GENERAL REVENUE**

Asset Accounts

CASH

In Banks and Offices..... \$864,415.95

ACCOUNTS RECEIVABLE

Uncollected Taxes, 1908 and prior (books)...	\$83,424.73	
Estimated uncollectible.....	\$76,831.38	
Less overlay reserved for abatements 4,717.45	<u>81,548.83</u>	\$1,875.90
Uncollected Taxes, 1909, (books).....	\$128,737.60	
Less overlay reserved for abatements.....	<u>50,782.82</u>	77,954.78
Supplementary Taxes, 1909.....		150.00
Uncollected Taxes, 1910, (books).....		467,030.88
Unredeemed Tax Deeds.....	\$40,473.79	
Less estimated shrinkage.....	<u>13,000.00</u>	27,473.79
Property taken for Taxes, (final takings) ....	\$31,081.01	
Less estimated losses, (interest, etc.).....	<u>19,092.95</u>	11,988.06
Estimated Receipts.....	\$185,650.00	
Less collections to date.....	<u>117,663.17</u>	67,986.83
Total Revenue Fund Assets Available...		<u>\$1,518,876.19</u>

DEFICIENCIES

Deficiency of Revenue, 1907 and prior.....		66,921.51
Deficiency of Revenue, 1908.....		78,386.21
Deficiency of Revenue, 1909.....		8,702.18
Deficiency of Revenue, 1910 (if appropriations are fully expended) .....		<u>9,845.27</u>
		<u>\$1,682,731.36</u>

LYNN

# Balance Sheet

of October 31, 1910

## FUND ACCOUNTS

### Liability Accounts

#### CURRENT DEBTS: GENERAL REVENUE FUND ACCOUNTS

Audited Vouchers Payable (October Audit) ..	\$17,428.76
Temporary tax loans, 1910.....	1,100,000.00
Temporary tax loans, 1909.....	50,000.00
State Tax.....	145,107.46
County Tax.....	102,818.34

#### APPROPRIATION BALANCES (Details Page 2)

General Appropriations.....	\$129,030.81	
Interest.....	28,806.41	
Sinking Fund Appropriations.....	58,210.00	
Serial Bond Appropriations.....	3,000.00	
		<u>219,047.22</u>

#### ASSESSMENTS IN PROCESS OF COLLECTION

Sidewalks.....	529.84
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#### SUPPLEMENTARY TAX:

Collections in advance of Warrant.....	194.00
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OVERLAYS, 1910..... \$44,078.83

Less Abatements of Taxes, 1910.....	<u>7,973.09</u>	36,105.74
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SALE OF BONDS for Revenue Purposes (1909)..... 1,500.00

SALE OF BONDS for Revenue Purposes (1910)..... 10,000.00

\$1,682,731.36