

The Route Out of Minnesota's Fiscal Crisis

# "We *Can* Change 'the Way We Do Things'"

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What do we do? Well, let's start by looking at the field of action.

	Revenue side actions	Expenditure side actions
Short-term actions	<b>TAX</b>	<b>CUT</b>
Long-term actions	<b>GROW</b>	<b>REDESIGN</b>

The 'realists' tell us the only options are to cut and to tax. They remind us: They have to balance the budget in the biennium. So for those projecting expenditure requirements in state government the present way of doing things is a given. And the spending interests' message is the same: With more we can do more; with less we have to do less. We don't do 'different'.

Near-term, the realist assessment is unarguable. Within the biennium neither of the long-term strategies can balance the budget. Not GROW and not REDESIGN. So near-term Minnesota will cut and tax in some combination. Some persons will argue for all budget problems to be solved with revenue; some, with cuts. Bet on some of each happening.

But longer-term we can change 'the way we do things'. Neither growth nor redesign can be accomplished quickly. Nor will the changes made pay off quickly. But it can be done.

Which sets the central question for the 'expenditure' side.

- Will we only cut-and-tax every time the economy turns down, each time at successively higher levels of expenditure?
- Or will we also organize a continuing program of innovation for our institutional infrastructure, working -- in good times and in bad -- to reduce costs and improve effectiveness in our major systems?

Think about the sober forecasts for state revenues presented this morning; near-term and long-term. They cry out for a major effort to find ways to meet public needs more imaginatively and more productively.

A response limited to cutting-and-taxing would destroy Minnesota. To offset the disadvantages of our cold, remote location we sell a quality state at a high but reasonable price. This is a fragile balance. We could easily lose what attracts people to come here and to stay. And the fight would poison our politics; tear the state apart.

We do a pretty good job upgrading our physical infrastructure. And we do think about productivity in the private economy. But we lack a program for productivity in the public sector.

Surely we understand now that we have to be careful about spending.

Until recently the discussions about Social Security, education, health care, transportation and infrastructure always concluded about like this: "Yes, the fix will be expensive. But we need to do it. This is a rich country. We can afford it." Almost nobody added it all together.

Today we do add it together. And it looks -- as former Gov. Carlson put it after last week's 'Leadership Summit' -- like an "economic tsunami" coming at us.

The only hope is to 'do different'. But today we have no general strategy for the redesign of our major systems, and no serious effort under way to develop one -- even though maintaining the quality of our public and quasi-public institutions is key to growing the economy.

Focused as it is on the budget-balancing ahead, most all the talk today is about cutting-and-taxing. Not much in last week's 'Leadership Summit' was about fundamentally changing the way things are done.

I assume your organization is concerned about the basic policy direction on expenditure. Probably you worry mainly about tax rates and tax incidence. But surely you worry about aggregate expenditure since that inevitably plays out as taxes.

I hope today to persuade you that sound policy must include a major effort to get at what fundamentally drives spending. That it is possible to come up with dramatically different approaches to meeting public needs. And that you should help to organize the effort to do that.

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## **It is possible to change 'the way things are done'**

How would we "change the way things are done"?

'Leadership' from the political sector, as I will explain shortly, is not the answer. No more than the rest of us do leaders know today what to do. Calls for 'leadership' tend to result in people simply restating problems and reaffirming goals. In the education discussion calls to "close the achievement gap" are an example of mistaking goals for strategies.

Strategies are methods: They tell us how. Today the question is: How?

For a sense of the 'How?' we might consider the nation's response to the energy crises in the 1970s. Energy use came down relative to GDP by about a quarter. This was not the result of an expensive program to

increase supply. It was a major effort at conservation, driven by price-incentives that reduced demand.

But let's focus on the two areas that dominate our discussion about spending.

O Our hospital system. This is an interesting case of redesign.

In the '60s Victor Cohn at the Tribune began writing about prepaid medical plans; Kaiser-Permanente. In time people came to see the system problem; the perverse incentives.

*"In no other realm of economic life", the Somers wrote in 1967 just as Medicare was arriving, "is repayment guaranteed for costs that are neither controlled by competition nor regulated by public authority and in which no incentive for economy can be discerned".*

In Minnesota Paul Ellwood, thinking about what to do, designed the 'health maintenance organization'. By the '70s the Twin Cities area led the country in managed care. Length of stay in hospitals fell dramatically. Harry Sutton remembers that when he transferred to Prudential's home office our area was running perhaps 1200 patient days per thousand. When he returned 10 years later that was about 400.

Multiply it out: the population of the area, the length-of-stay, the cost-per-day. The productivity gain is bound to have been huge.

At the same time, however, hospital construction was booming, with Hill-Burton coming into the metropolitan area and with capital being

raised less from fund drives, more from borrowing and third-party-reimbursement. To fill beds we were creating new 'needs': insuring, for example, 28 days of inpatient care for chemical dependency.

Inevitably it became an issue that a hospital system carrying such excess capacity continued simply to send the bill to the community for payment. To their credit the hospital trustees took this on. First the hospitals merged into groups; then within the groups closed wings and buildings, bringing our hospital system down to appropriate size.

O K-12 education -- at least laying the basis for greater effectiveness.

After World War II the schools were hugely popular. But by the 1970s discontents were visible. Why *couldn't* Johnny read?

Out of a long process of thinking we saw, again, a system problem. The state had created for districts an essentially public-utility arrangement that ensured these organizations and the people in them their customers, their revenues, their jobs, their compensation -- almost everything about their material success. And this guarantee from the state was good whether or not the students learned.

Public education was at that time, as Dan Loritz says, essentially in "the opportunity business". The state provided schools; required you to attend. Whether you learned was up to you.

For a country serious about learning this was an absurd arrangement.

And in the '80s state and national policy switched; made learning the objective. Legislation withdrew the exclusive franchise that worked to suppress change: Chartering, Minnesota's institutional innovation in 1991, spread to most states. Today we have real dynamics for improvement. The redesign is moving. But the work is far from finished.

## The key was to challenge the traditional 'givens'

System-change of this scale took time; took hard and critical thinking. It required courage in the face of controversy. It took a willingness to see the larger public interest and the long-term economic benefits. Above all it required challenging the way things were traditionally done. We learned some key lessons.

### O The symptoms are not the problem

People naturally think problems are what they see, and want to 'do something' directly about what they see.

In discussions about education I found myself listening over and over to people talk about the bad things being done that ought not to be done, and about the good things not being done that ought to be done.

I began to say: "In all this discussion nobody has disagreed with anything. And everybody has heard it all before. Yet nothing changes. Surely that tells us there is something *causing* the bad things and blocking the good things. Why don't we find what that is, and fix that?"

As a wise European liked to say: Problems are the product of circumstances. They are not solved by attacking their symptoms. You have to change the circumstances that produce them.

Bill Andres made the same point when leaving Dayton-Hudson to chair a state project on productivity for Gov. Perpich. "Is productivity something you do?", he asked, "or something that happens if you do the fundamentals right?"

If you paused to think he would say: "I was in retailing. In retailing turnover is very important. When a store manager tries to do turnover the store isn't profitable any more. So we decided a long time ago in Dayton-Hudson to concentrate on doing the fundamentals right".

This is the central principle we need to apply in our public sector. We cannot 'do improvement' endlessly from the outside. The strategy has to be to get the fundamentals -- the incentives -- right, so the operating organizations will do improvement themselves: on their own initiative, in their own interest and from their own resources.

O 'Doing something' does not have to mean 'delivering service'

In our public sector the dominant notion of 'doing something' is 'delivering service'. We 'solve problems' by hiring professionals to do things for people for pay. (Too often the media judge a political commitment by the size of its money-number.)

The pressure is tremendous to see solutions always as professional service or some high-cost technology. That's understandable. This is where the money is made: in jobs and contracts.

Non-service and low-capital approaches, by contrast, spread their benefits broadly. Productivity is low in political appeal.

Still, productivity is necessary. And possible.

Think about 'domestic service'. In the household sector families realized long ago they could not maintain cooks and gardeners, chauffeurs and maids. These disappeared, replaced by systems of supported-self-help. Businesses emerged to sell you the equipment, the plans, the materials, the know-how. You put in your own labor. Henry Ford, Betty Crocker, Toro lawn care and Singer sewing machines.

In our public sector now the idea is not to 'deliver service' more efficiently. The idea is to reduce the use of the 'service-delivery' model.

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**Are there ways to make these major changes today?**

Sure there are. Again, let's stay with the two big systems.

O 'Health care'

Almost incredibly, 'health care' is defined today as medical-hospital services. Health, even prevention, is assumed to result from services. Reform is defined as making more professional services more affordable to more people.

But the -- socially necessary -- effort to expand access to medical-hospital services must come at a cost the country can afford. If all the doctors and hospitals really are to be paid to provide all the services all patients want, won't it then be imperative to work down the demand for medical-hospital services?

I heard Mary Brainerd, CEO of Health Partners, say last week that 80 per cent of medical-hospital costs are generated by chronic diseases.

Jan Malcolm, the former commissioner of health, is compelling about this: The problems are overwhelmingly heart disease, stroke, cancer, lung disease and diabetes. These are chronic conditions; neither preventable nor curable by medical-hospital services. They result largely from smoking, drinking, bad diet, and lack of exercise. They are heavily problems of personal behavior.

But prevention in this public-health sense is barely visible in the current political discussion.

We do need to reform the medical-hospital system. That should mean, as Walter McClure says, identifying the high-quality/low-cost doctor groups and hospitals and arranging the benefit programs to send them

patients. Which in turn means providing consumers with the information to know and the incentives to select those cost-effective providers.

Reform also means getting at causes -- which means changing personal behavior. This is hard. We tend to think behavior can't be changed. But just think how many attitudes and behaviors common 20 or 30 years ago are by now radically changed.

### O K-12 education

In education, too, we have problems in system and school design that present opportunities to improve on both effectiveness and cost.

Learning is still defined as teaching: the 'governess' instructing the children; personal service transplanted into the school as courses and classes.

We think and talk in terms of -- now 56,000 -- teacher-workers 'delivering education' to 900,000 -- often unmotivated -- students. Even with teachers not paid like professionals it is an expensive, labor-intensive, system; a third of the state general fund. Possibly not sustainable.

What might we do? Well, there are ways to do 'learning' different.

Using digital electronics we might redesign 'school' to customize learning, making the students increasingly the workers. In other words: might move learning to the model of supported-self-help. That could

simultaneously motivate students and motivate teachers (giving them at last a truly professional role and freeing them from the curse of 'classroom management'). We would then have 956,000 workers working harder -- and student labor, note, we do not compensate: The effort we get from students comes for free.

We can do more to start learning earlier, using existing public financing to create Age3/Grade3 schools that improve literacy.

We might also think about ending high school at age 16; moving young people, who are increasingly adults, into adult roles. Minnesota now has about 75,000 juniors; an equal number of seniors. We spend perhaps \$10,000 a year on each. Multiply \$10,000 by 150,000 and you get a rather large number. And that is for a single year.

It would take time to phase that in. But the gain would be significant; not least, from moving young people ahead earlier in life.

The way learning is changing we might also put the brakes on the construction of these \$100,000,000 high schools -- sometimes closed before they're paid-for.

One more.

O Governance

We might redesign governance to generate efforts to improve productivity at the local level.

During the '60s the Legislature did great work adapting the system -- the structure and financing -- of government in the Twin Cities area to the reality created by regional growth; switching from 'municipal' to 'metropolitan' as the definition of the city.

Today there needs to be a comparable adjustment in Greater Minnesota. I count 54 counties with populations smaller than Richfield. It is time to think beyond 'better management' of cities, counties and school districts separately; time to think what they can do together.

There is a way.

In the '70s the counties amended the Joint Powers law to permit any governmental unit (broadly defined) to join any other governmental unit to do what either is authorized to do separately. We have not yet begun to explore what this might accomplish; outside the Twin Cities area or, for that matter, within it.

The opportunities for these approaches are almost endless.

Be clear: None of these ideas is ready for bill-drafting. I mention them only to give you a sense of the need to think deeply and, if you will, "irreverently" about things we have long taken as given. And to show you the kind of ideas we should now seriously explore.

So: What needs to be done to get that design work moving?

## Will 'politics' block action?

Talk about change and immediately we hit the objection that our politics has deteriorated so badly as to make it impossible to do things like this any more. There is a wistful hope that 'leadership' might override politics. But much skepticism.

Like many popular notions this one might be mistaken. Consider:

First: What really has changed? When has politics not been short-term, partisan, personal, emotional, ideological, filled with special interest and resistant to increasing taxes?

What's changed is that we no longer generate the policy initiatives that countervail against the pressures from politics. In my *Cold Sunbelt* talk in 2001, recounting the rise and decline of public life in Minnesota, I listed the institutions for policy design and discussion that have since deteriorated and disappeared.

Today's criticism of 'politics' is the visible result of this carelessness. So don't blame politicians. The fault is ours -- for not being there today with good proposals, giving elected officials compelling reasons to override partisanship in the public interest.

Second: Political leaders do not, anyway, generate the policy initiatives that break radically with the way things are conventionally done. These initiatives have to come from outside, from private-sector, groups.

When a senator, Jack Davies wrote tellingly about "The Limitations of the Lawmaker". Essentially, he said, a legislature functions to say 'Yes' or 'No' to ideas brought to it by others.

Conventionally we look to governors to put proposals before the Legislature. Yet governors, too, do not often propose radical change.

Elmer Andersen, when I asked once who he felt might be governor some day, said: "I don't think that's very important right now. When the public is clear about what it wants, elected officials are important. They get it done. But in a time like this, when the answers are not clear, politicians hesitate." Today, he said, the leaders are those who deal in ideas.

Once it's clear what needs to be done, and how it can be done, the politician's skill is indispensable. "Politics is not the art of the possible", somebody nicely says. "Politics is the art of making possible what is necessary". But, again: Action starts with proposals from the outside.

Political leadership then becomes the willingness to listen -- especially, to ideas beyond the 'safe' consensus created by consultants. Then it is the courage to carry and sell the need to do what's necessary -- as Rudy Perpich did with public-school choice. We need to regain this tradition

of politics as the education of the public -- along with the capacity to generate proposals.

Let me finish on that question of how to organize to generate the ideas for what is 'necessary'; for changing "the way things are done".

## How does it get done?

Minnesota used to have a competitive advantage in system-change. The 1970s get a bad rap today -- sideburns and double-knits and all. But, out of the '60s, there was a significant coming-together of the radical left and libertarian conservatives. Minnesotans were deeply involved in the new thinking about alternatives to the bigness and impersonality of bureaucracies, public and private.

David Osborne drew a lot of *Reinventing Government* from what he heard in Minnesota. Minnesotans worked with the Rand Corporation, with SRI, with the Urban Institute. A lot was learned. Much of that knowledge is still around.

Again, that taught us some lessons. Quickly:

Redesign is not a job for one organization or one project. The work has to be spread broadly across government, nonprofits, business.

State government clearly ought to revive its planning function. Tom Stinson and Tom Gillaspay are indispensable. But more is needed. It is

ridiculous to be flying through these storms without better radar to see what lies ahead. And the Legislature -- consistent with Jack Davies' view -- should seek out proposals and arrange time to discuss them.

The focus has to be on systems. Redesign is not mainly about management efficiencies, since 'management' often accepts the service model. We have to develop people who can think in system terms: always asking, "Why?"; finding the underlying causes of poor system performance, designing remedies that will produce and reward good system performance.

The 'design shops' must be protected; free to propose things bound to unsettle the status quo. For sure: Do not count on the so-called 'stakeholder groups' that never propose radical change.

Get the reforms first. No more "money for promises". Too often in the past both the Legislature and private donors have thought they had a deal: money for reform. But this is not like buying a house, where you hand the sellers a check and they hand you the deed. The big systems can't re-form right away. So they hand you an IOU; a promise of 'change' later. Too often the money disappears into the system, with the reform never delivered.

The constraints on those currently in office suggest asking those not now in office to use their political skills to implement the proposals. Happily many of these are now coming forward: former governors and

experienced legislators. They understand how systems work, and they are now free to say what they believe.

It will take continuing financing. This policy work is not terribly expensive. Still, the system redesign and its implementation will cost money. It can be the best money we spend. Much of that should be general financing; not the 'contract philanthropy' that starts with some conventional idea and looks for organizations to 'build it'.

For the financing it will be best not to rely on business. Our biggest firms now have horizons far wider than Minnesota, and corporate public affairs is oriented less now to the institutional needs of this community and this state. Too many firms have vanished in mergers or have moved their headquarters away.

Increasingly, and visibly, the leadership entities with the permanent stake in Minnesota are today the large non-profits -- the universities, medical centers and arts and cultural institutions; the governments, state and local -- and the foundations.

But of these only the foundations have money to put into this work.

Historically, our foundations have not much done this kind of giving: They have preferred to keep commitments limited and to make grants to organizations that serve people directly.

But the work of redesign depends on them; especially on the two community foundations, whose assets have risen dramatically in the last 20 years. These were among the group of five major foundations that made a start on redesign earlier this year with their *Bottom Line* contract to Public Strategies. The group emphatically saw that project as the beginning, not the end, of the work.

To pursue that work the Saint Paul Foundation and the Minneapolis Foundation should set up a fund for redesign, built with contributions and commitments from their donor-advisers.

## One final urging

This innovation, this redesigning of the infrastructure of our major public systems, cannot be episodic; stop/start.

Arne Carlson found a deficit when he came in as governor in 1991. Some cutting and taxing followed. But he also put John Brandl and Vin Weber to work on system redesign.

Unfortunately, by the time their report appeared the crisis was past. It was the mid-'90s; the sun was shining; Hey, we're rich; Let's live a little. Few took its recommendations seriously. So when the troubles returned, as they have today, little progress had been made, no base of understanding about options had been laid, and no inventory of useful proposals existed, for action.

If we throw away the umbrella every time the sun comes out again we will create the worst of all situations. We will be caught endlessly in short-term fixes, forever cutting and taxing when the crises recur -- as we are caught today. We will, as I said earlier, destroy Minnesota's advantage.

We have got to get to work on the redesign of our public systems and processes; finding radically different, effective and economical ways to do things. There simply is no way to finance our public needs without this major effort to improve productivity in our major systems.

The more efficient we make our big systems, even in the private sector, the easier it will be to finance the costs of state and local government.

Unprecedented conditions call for unprecedented responses.

The requirement on the state to balance its budget represents a major driver for reform -- that does exist for the national government.

The longer-term the payoff, the sooner the work needs to begin.