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Solving New York City's Fiscal Crisis

*It is a miracle
that New York
works at all.*

*The whole thing
is implausible.*

—E.B. WHITE
Here Is New York

The City's View

Sitting back, feet propped up on a cluttered wooden desk, clad casually in well worn loafers, dark corduroy slacks, and a plaid shirt open at the neck, Steve Clifford reflects on his last two years at the helm of perhaps the biggest municipal accounting project ever undertaken. And he makes it seem so easy.

"We simply had the mandate," he says. "There was no alternative. It *had* to work, that's all."

As a special deputy in the New York City comptroller's office, Clifford's task these past two years has been to act as a director of that city's integrated financial management system (IFMS). Devising the system, which went on line July 1 at the beginning of the 1977-78 fiscal year, was under the direction of Clifford and co-director David Woodbridge of the mayor's office, the pair working closely with five independent consulting firms.

Frank Zolfo, New York partner and the Touche Ross project director from 7-1-76 to 7-31-77, characterizes the development of IFMS as "motivated by the city's need to improve its procedures for obtaining timely, reliable financial information and for controlling its revenues and expenditures."

Essentially, the objectives of the new system were four-fold: (1) to facilitate improved financial management of the city's resources by each agency; (2) to exercise sound budgetary and accounting control over city revenues and expenses; (3) to report financial information accurately to city managers, federal and state officials, the investment community, and the general public; and (4) to develop an auditable system, one which will ultimately enable an independent auditor to render a clean opinion.

And it was anything but easy. Putting such a system together involved close cooperation between the mayor's office and the comptroller's office, the diligence of close to 1,000 municipal personnel involved in the project, more than 500,000 man-hours of support work among the five consultants, and a cost to the city of more than \$16 million.

"At the outset," says Clifford, "the city's financial systems were a shambles. That was recognized by any number of people at the state and federal levels. As the city's fiscal crisis heated up in 1975, these people began asking for certain types of information, and the city just couldn't produce that information. It became painfully evident that the city really didn't have a hold on its own budgetary systems, accounting systems, or control systems. It was pure chaos."

The first step to alleviate that chaos came with the issuance of a white paper from the comptroller's office in June, 1975, calling for a new accounting system. But what really got IFMS under way was the state's passage of legislation that same year establishing the Municipal Assistance Corporation (MAC). This legislation required the city to reform its accounting and budgeting systems to conform to standards acceptable to the state comptroller.

"However, the MAC law spoke only to accounting," Clifford recalls, "whereas the big problem in the city was the lack of control and the lack of information. Accounting is an after-the-fact kind of thing, and, after the fact, if we had enough accountants we could probably put together proper statements on an annual basis without changing the system. But nobody knew this at the time, certainly not the appropriating bodies."

Woodbridge and Clifford, therefore, ordered a system to be designed that would simultaneously meet the city's needs for financial control, planning analysis, and accountability—with an emphasis on control. The scope of the project would encompass most citywide financial management functions, such as budgeting, payroll, purchasing (encumbrance control), accounting (including accounts receivable, accounts payable, and warrant reconciliation), and financial reporting of all kinds. The plan called for IFMS to operate as a unified system. Citywide budgeting, accounting, purchasing, and payroll functions would be brought together in a single computer facility at the new financial information services agency (FISA).

Each major subsystem (such as payroll) would be able to access data from a single data base that would also hold information from the other subsystems (such as budgeting). Thus the need for payroll to maintain its own separate version of the budget would be eliminated. Moreover, account coding in the budgeting and accounting subsystems would be identical, greatly simplifying agency coding on vouchers and comparisons of budgeted to actual performance.

There seemed little question in anyone's mind that the project could succeed. What bothered most people was the time frame imposed by that MAC legislation, which called for an auditable system as of July 1, 1977. That gave co-directors Woodbridge and Clifford scarcely more than a year and a half to put their program in working order. Woodbridge, however, feels the compressed time frame may have been a blessing in disguise.

"What happens in the public sector as well as in the private sector," says the conservatively dressed, baldish, 40-year-old systems expert on loan from Chase Manhattan, "is that the amount of work needed for completion of a given project will always expand to fill the amount of time allotted for it. In this case, there was a tight deadline and everyone knew it. We either got the job done or we didn't. So we broke all the rules of the book and got away with it because there was no other way. We'd give city management a chance to be involved in every decision, for example, but if the people didn't respond quickly enough we went ahead and implemented the decision on our own."

Woodbridge's sentiments are echoed by Kenneth S. Axelson, then deputy mayor for finance and the man who handpicked Woodbridge for the job. Says Axelson: "All the objectives and obstacles, all the political differences one might expect at every stage of such a vast municipal undertaking were effectively swept aside through legislative mandate. For example, we were asking the city council to appropriate \$16 million. Normally, this would have resulted in prolonged debate. In this case, there was not time for debate. There was no alternative to the program we were proposing."

That sense of direction is one major reason why, according to Axelson, the project was able to succeed where others might have failed. "Failure to succeed," he said, "would have been a mark against all of those involved. It was an important measure of the managerial skills of the city and of the will and determination of the political community, as well as the supportive business community, to cope with the city's fiscal problem."

Steve Clifford puts it more succinctly: "It is important to remember that this was an election year. If my boss Jay Goldin, the comptroller, had wanted to make an issue out of this mess, he certainly could have. It wouldn't have been a very big issue, but it would have involved the same old charges of continued mismanagement, a waste of \$16 million, et cetera, et cetera. In this connection, it is important to realize the degree of interest the press had already shown in the project. It is very unusual for a system to have that sort of visibility, that sort of pressure. What that meant was that we really got whatever we wanted."

What exactly was it that the architects of IFMS wanted? "From the outset," Clifford answers, "we wanted to devise a system that was able to control the city budget.

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This was the most critical function. There was no way under the existing system to assure that the budget would remain in balance, but we wanted to make it possible without handcuffing the managers of city agencies. You can always impose such rigid budget controls that managers can't get their jobs done; but we sought to increase their discretion, their flexibility of operation. Obviously a fundamental goal was to establish proper accounting procedures for the city agencies. This, however, was not enough. We also wanted to improve the information available, to help them make managerial decisions that depended on accounting procedures and control systems."

Given the ambitious nature of these goals, then, and the collapsing time frame in which the IFMS co-directors had to work, it became clear that working procedures must be radically different.

"To give us a running start," says Woodbridge, "outside consultants were brought in. They had the expertise we needed to solve organizational problems as they arose—or before they arose." Altogether, five outside firms played separate but interrelated roles in shaping the organization of IFMS. American Management Systems had already done work with the city in other areas of computer systems development. Bradford National had both the hardware and the experience to set up the potentially unwieldy city payroll system.

"Two accounting firms worked closely with us," says Woodbridge. "Touche Ross and Ernst & Ernst. The former proved especially useful in anticipating and coping with operational problems arising in the office of management and budget (OMB) and the comptroller's office. Also, the Urban Academy did a whale of a job in undertaking training in all levels at the outset of the program.

"There was no sense of competition among the consulting firms," adds Woodbridge. "There wasn't time for that. Each group recognized what its own contributions should be and what it might expect of the others."

Representatives of the consulting firms, for their part, cite yet another reason for the program's success—namely, Woodbridge and Clifford themselves. "I think Steve and Dave just did a superb job in managing the project, making hard decisions in overseeing all the work all the time," says Harvey Susswein, project director for American Management Systems. "They also ran interference for all us outside consultants, which, in turn, permitted us to do a more effective job. What they did, essentially, was establish a new city agency on three months' notice."

"They were an excellent team," agrees Frank Zolfo. "Clifford took the role of looking at things from an

overall macro level, and Woodbridge looked at things at a micro and detailed level. They coordinated with one another very well. They kept each other informed, and I don't think the project could have been done by either of them alone."

Axelsson notes a singularly interesting aspect of this relationship. "Dave Woodbridge and Steve Clifford are two very different types of personalities," he points out, "with different backgrounds and different working styles. Yet they worked so well together that their leadership gave the whole project the sense of unity it needed for success."

Still, there were serious doubts that the project would be successful.

"I suppose the reasons for such skepticism," says Axelsson, "were twofold. First of all, nothing of this magnitude had ever been accomplished—especially not in this time

"From the outset, we wanted to devise a system that was able to control the city budget."

frame. Then, too, it was common knowledge that New York City's bureaucracy supposedly was hopelessly inefficient and incompetent. Hence, if private industry had never been able to bring off something of this sort, it was inconceivable that it could be done in the public sector."

Two operational factors seem to have been responsible for the remarkable success of IFMS. The first is implicit in Woodbridge's attitude toward "breaking all the rules of the book." TR's Gerald R. Riso, New York partner and project director from 8-1-77 to the present, describes Woodbridge himself "as a man with skill at organizing data systems techniques. To the extent that Woodbridge felt it necessary to break out of this mold, he demonstrated not only the technical proficiency, but the sense of urgency for getting the job done." Of Clifford, Riso notes some modification of style as well: "He never lost sight of the overriding objectives—namely, to make things work. He was capable of making on-the-spot decisions, yet backing down from those decisions anytime it could be demonstrated to him that the negative consequences outweighed the positive. In short, he was a businessman in an environment that wasn't used to it."

While decisions were being made all along the way,

there remained the need to train a vast crew of 7,500 city personnel at all working levels. The decision was made early to formulate an entirely new system of operation.

"Looking back," says Sandi Manilla, chief of the division of financial planning in the comptroller's office, "it would have been otherwise impossible to motivate three or four thousand people to do new jobs in new ways." This meant the clerical staffs at each city agency had to be trained, not only to perform new functions but to think in new directions.

How successful was this motivational effort?

"There were some older people," says Manilla, "who took their retirements rather than adapt. But, by and large, the staffs adjusted well. Not without the usual grumblings, naturally. Nobody particularly likes change; but, when you can show them how much easier their jobs will be as a result of the change, they are a lot more willing to make the effort."

With proper training and motivation, the newly constructed system emerged unscathed, and the curtain went up on July 1. "Despite all predictions of doom, there were no May-day strikes, no fouled-up purchase orders," says Susswein. "In fact, we managed under IFMS to achieve, initially, an 80 percent acceptance rate on documents processed through the system, compared with an expected 50 percent error rate. And, by the second pass, we generally had that rate over the 95 percent mark."

Now in place, the "integrated" system means that city planners will have good numbers on which to base their estimates and control functions. "Certainly," says Riso, "if city officials want to, they can still play with numbers; they can still create problems by being unrealistic about revenue estimates, the probability of securing grants and such. However, the presumption from the start was that people wanted to do their job on the basis of accurate information, and these people are now going to be able to do a better job. So the will to use controls is up to the agency managers and, indeed, to the top levels of city government."

It was a hectic two years for city personnel. So much so that the implementation has been almost anticlimactic.

"During the week before July 1," says Pat Hardiman, assistant to the city's chief accountant, "we were all pretty much geared up for misses and near-misses and a lot of overtime, trying to iron out whatever bugs developed once the system was in place. Then came the big day . . . well . . . no big bugs, no overtime. In fact, we simply went home at five o'clock, which was something we hadn't done in weeks.

"So what else is there to say? It worked."—K.P.

The Consultant's View

Little has been written about the reorganization of New York City's financial management systems from the consultant's point of view. This has in part been deliberate. One of the major objectives of the reorganization has been to establish the city's own credibility—for its people, its structure, its systems.

"The city's success was to be our success," says John McCreight, the first of three partners to be responsible for the Touche Ross role in the reorganization. "And our first objective in late 1975 was to enable the city to tell the financial community to be patient until 1977, that fiscal changes were on the way."

What occurred behind the consultants' doors during this \$16 million effort by New York City? Clearly, a major challenge to the professionals of all five consulting firms was the deadline—July 1, 1977—for putting the city's records into auditable shape. This left but 18 months to accomplish what *The New York Times* has termed "perhaps one of the most important reforms in city government in this century."

Frank Zolfo, second Touche Ross partner to head his firm's efforts in this crucial period, compares the experience with running a 26-mile marathon. "Most of us were physically tired at the end and mentally tired, and I think the city people were as well." Adds Touche Ross manager Neil Thall, "We're talking about something like 150,000 man-hours for Touche Ross alone—probably the largest systems operation ever conducted in so short a time."

The time pressure was compounded by the complex environment the consultants had to work in. Manager Richard Stanton, quiet and friendly behind a built-in frown, describes "working with a client who often did not know how its own systems worked. That is, a few city people knew the general flow of the manual systems, but they were not familiar with the details—while clerks would simply process a form without knowing where it came from or where it went next. And the information available was often wrong. It was extremely difficult to build the master files on which to base our work."

Moreover, four of the five consultants were not only seeking the same information, they were also reviewing each other's work. Partner Gerald Riso currently leads the Touche Ross implementation work for the city with a low

key approach that contrasts to the intensity supplied by Zolfo during the critical months. "At first, I wondered if there were not more problems than it was worth—asking consultants from five firms to work together in an equal partnership. Would they admit a problem to a competitor, such as a failure to meet a deadline? But equality worked. And city officials told me that it gave them a sense of participation, a knowledge of what was going on that was important to them. Happily, they were dealing with people who adhered to high professional standards, people driven to get the job done."

Coordinating upwards of 200 consultants from five firms and three major city offices was another concern. According to Frank Zolfo, his consultants attended 30 to 40 meetings daily just to keep their activities integrated to a constantly changing situation. On a more formal basis, representatives from each consulting firm and the city met once a week to review developments. In addition, Touche Ross assigned one staff person to interface with an equal at each consulting firm. Indeed, the firms were always alert to upcoming changes in the strategy and plans of the other organizations. When it came to Touche Ross' own 35 to 40 consultants keeping in touch with each other, says Zolfo, "we lived with tape recorders in our pockets. Being tied up at evening sessions, we were constantly taping the day's activities to let the left hand know what the right hand was doing."

Over all this activity hung the possibility that the state legislature's July 1, 1977 deadline would not be met—that the new system would break down in a cloud of smoke and the dismantled old system would not be available to replace it. The consequence of firemen, policemen, and others not getting paid, for example, was a development the city dreaded to face. Thus, Touche Ross put together a team that worked for four months on a contingency plan—a fact that was little known because the plan was never used.

Meanwhile, New York City employees—long used to seeing consultants ask questions, project new ideas, and then disappear without causing a ripple of change—discovered that this time the consultants were not going away. Unlike in private industry, where management decides whether or not to exceed the budget, in the

public sector the budget is law. The consultants were engaged to assure that the law was followed.

The city's fiscal problems in the mid-70s had been compounded by budget improprieties. For example, vocational education expenses might be included in the capital budget, rather than the expense budget where they belonged. The theory was that benefits would be enjoyed by students for years to come. "Under a capital budget, if \$40 million were raised by 20-year bonds," explains senior consultant Ira Feinberg, "only \$2 or \$3 million would need to be paid that year rather than the entire \$40 million." Tall, with curly hair, Feinberg has the relaxed, casual manner typical of the new breed of consultants. "Also, controls were minimal. Expenses would be broken down by their purpose—such as snow removal, which might cut across several agencies—instead of being under one department responsible for the activity."

To make the city's records auditable, the entire new system had to work within the framework of generally accepted accounting principles. Neil Thall, a slight, neatly tailored Touche Ross manager, worked in the comptroller's office. "Our job was to determine how applying accounting principles would impact our control of the city's finances. Which revenues could be accrued and which could be accounted for on a cash basis? How would the accounting be handled for such items as bonds and sales tax revenues in the financial statements of the Municipal Assistance Corporation (MAC) Fund? How would we account for the fact that pension fund administrators were two years behind in calculating pension liabilities? The questions went on and on."

The biggest challenge, Thall states, was to establish consistent principles that were understandable. "Formerly the financial statements ran up to 500 pages and were completely incomprehensible. You had to be an insider to understand what a line of information meant. The comptroller's office eliminated three-quarters of that material and set up an understandable and consistent statement to which we then applied the figures for fiscal 76 and fiscal 77. This was to give the official 78 audit under the new system a base to compare its figures to."

The consultants' world of accounting, budgeting, and systems was held together in New York City by an idea

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called IFMS. Pronounced "iffmiss," it is the acronym for integrated financial management system—in simple terms a computerized system in which a change in the amounts for one agency or department hooked into the system will impact all other departments affected by that change.

Ira Feinberg explains the key encumbrance concept that grew out of the IFMS. "That was an innovation. When a purchase order is placed, the money is reserved, or encumbered, in the budget center—there are 1,000 such centers—responsible for the purchase. Thus, a purchase order can be stopped from going out whenever it causes that budget category to be exceeded."

Altogether, the IFMS project has required the development of 20 general procedure manuals, 60 operation manuals for the user agencies, and 10 manuals for the operation of the computerized information system. To some of the consultants, the time spent preparing such manuals did not offer a major intellectual challenge. Frank Zolfo agrees that "it was not the type of analytical work they enjoy, perhaps, but there was certainly an intellectual challenge in writing a set of manuals that city people could understand, that provided the controls needed, and that would provide a system that worked." Clearly, keeping the professional staff stimulated and not bogged down in detail was a constant challenge to project managers.

There were 7,500 people on the city's staff who had to be trained in the new system. What was the caliber, the commitment of these city personnel? There is no clear answer. Feinberg describes a group of budget examiners, "young college grad types," who were highly cooperative, while other members of the city's staff did not care to learn a new way of doing things. Thall cites a dozen people in the comptroller's office "who were motivated, who really wanted to help, who spent a lot of overtime hours on the project—and they are the ones who are going to be running the comptroller's office from now on. Sandi Manilla, for example, got right in there and called a spade a spade; she wasn't afraid of going after people who weren't doing things correctly. Pat Hardiman was another excellent person."

The challenge, says Feinberg, was to establish credibility with city people. "For example, you could not get in front of 30 budget examiners and give a typical consulting presentation with transparencies. You had to learn to sit back and let people blow off steam, which wasn't directed at you but at their own frustrations. You had to understand where they were coming from. And you never said, here is the solution that will save the city; you described six ways to do a job and then got them to agree that one was the easiest or most effective. It was important to preplan the meeting, to know who was coming, what their points of

view would be, and who were the one or two people whose opinion really mattered."

"At first," notes Gerald Riso, "some consultants were prejudiced against municipal employees. Some of us doubted they were sufficiently motivated or smart enough to make the new system work. But the answer to this is that today the new system is working. The data is accurate, reports are coming out when they are supposed to, and the right information is getting to the right people."

Thus, the city did not go up in smoke and recrimination on July 1, 1977. Riso sums up the basic achievements: "First, a single system, not a separate set of books, now exists for the mayor and the comptroller. Second, the city's accounting policies are in accord with generally accepted accounting principles. And, third, sound financial planning is possible—because there are budget and purchasing controls, and because you cannot take credit any more for revenue that does not exist."

"What is not sure," adds Frank Zolfo, "is whether the people who run the city are going to use the system properly. Are Koch and his team going to have the courage and wisdom to make the right choices?" If they do not, he suggests, "people who are outside looking in are going to have a much clearer sense of what is happening in their city—and that may not be a bad thing, either."

Assuming the system is used, how much will it impact the city's financial crisis? Gerald Riso believes the problems of New York City go beyond the scope of its IFMS project. "The city must also ask itself if it should be in the health care and education businesses. Should it provide services or contract for them? Is it taxing the right people? Are its labor negotiations sound? What IFMS can do is help the city to respond to those issues, and, if so, it will have paid off even more."

When John McCreight assumed responsibility for Touche Ross' initial involvement in the city's fiscal crisis, he was asked: will the patient die? His answer: the patient is not the physical presence of New York City, nor is it the city administration. "It is the people who live and work in the city. And the patient is alive and well. The administration may go through hell, and perhaps people in the administration will die. But the patient itself will not die."

"I'm not a native New Yorker," says Neil Thall, "but it's my home now, and I feel an affinity for this city. I often look at the consulting jobs I do and the clients I work with, and I ask myself if what I am doing is having a positive impact on society. Well, on this New York City project, I really believe I helped the city. I honestly feel I impacted it and caused positive change. I was helping my community and it felt good. I met a lot of people who will be important some day in this city, and they feel the same way."—R.P. 