



# *South Dakota Legislative Research Council*

## *Issue Memorandum 94-5*

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### **TOTAL QUALITY MANAGEMENT AND PERFORMANCE BUDGETING**

Along with countless other organizations around the country, large or small and both governmental and private sector, South Dakota state government has sought self-improvement over the years. Previous Legislatures, for example, have enacted attempts here at governmental reform such as Sunset Laws and Zero Based Budgeting. Both of these ideas were spawned by movements which aimed at improving the way government operates, is structured, or is funded. The outcomes of the Legislature's experiences with Sunset Laws and Zero Based Budgeting can be found on shelves in the Library of the Legislative Research Council.

Other movements of note have been embraced by the Administration or Executive Branch itself, usually without legislative approval. For example, toward the end of Governor Bill Janklow's administration, upper-level management employees attended sessions in the Capitol taught by the Wharton School of the University of Pennsylvania. This paper's purpose is to discuss two improvement theories (or tools) that have recently been implemented in South Dakota, Total Quality Management (TQM) and Performance Budgeting.

On October 20, 1993, Governor Walter D. Miller announced his Initiative for Quality Government. As the central part of that, he named the bipartisan Commission on Quality Government. Governor Miller assigned Lt. Governor Steve Kirby to head this Commission.

Nationally, government has come under fire from--or received the attention of--followers, students, and readers of Reinventing Government, the book by David Osborne and Ted Gaebler (1992). According to Governor Miller in his public announcements concerning both his Initiative and the Lt. Governor's Commission on Quality Government, the quest for improvement here is different. His administration is "taking a somewhat different tack. We are looking for ways to make state government more responsive to its customers--the taxpayers who pay for what we do. We are NOT [emphasis his] reinventing South Dakota's government. It does not need to be reinvented."

Instead, the most visible approach so far in South Dakota has been to invest in TQM. This is the concept professed by executive, theorist, and entrepreneur Philip B. Crosby in his books Quality is Free (1979) and Quality Without Tears (1984), to name just a couple. Jonathan Walters, writing in the Council of State Governments' *GOVERNING* (May, 1992) defines TQM as "the system of ideas that W. Edwards Deming taught Japanese corporations in the 1950s and has been preaching in the United States ever since".

Basically, TQM has come to be used as a generic term for the entire quality movement based upon the principles of Crosby, Deming, and a school of others, that has its roots in the efforts to rebuild Japan following World War II. At least one writer (Greech, p. 4) says "In fact,

the term TQM has become so widely used that it has become the number one buzzphrase to describe a new type of quality-oriented management."

While the TQM principles espoused by Crosby in his books have been applied almost exclusively to the private sector, particularly manufacturing, there have been efforts to apply TQM to government. The implementation of TQM in government has both supporters and opponents. For example, it has been specifically rejected by many legislative agencies because they have seen it as inappropriate for their operations (Weberg, 1993). "The bad news is that [TQM] is very hard to do well: Despite the success stories, it is no magic formula for instant government rejuvenation. For one thing, it is expensive and time-consuming to implement" (Walters 1992). Crosby himself said that it "takes four or five years to get people to understand the need for, and learn to have confidence in, an improvement program" (1979, p. 10). He recognizes that such a significant education process as convincing every employee of an organization to do a job right the first time takes a while. "You have to lead people gently toward what they already know is right" (1979, p. 129).

Strict, honest adherence to a decision to implement TQM means that a formal system of training is essential. Crosby teaches that the solutions to problems get lost in informal systems. As part of its decision to focus attention on quality and the improvement of government process, the Executive Branch is well underway in a program which they have named Quality Government Improvement Process (QGIP). This program is totally reliant on the purchase of consultant services from Proudfoot Crosby Associates, which is Philip B. Crosby's company. The company does have a

considerable reputation, as Crosby is considered "one of the Big Four" (Greech, p. 210) of management theorists along with Deming, Joseph M. Juran, and Armand V. Feigenbaum.

Crosby's company, which hails from Winter Park, Florida, has worked with a large number of corporations and divisions of government in other parts of the country--as well as agencies of the federal government--but has heretofore not worked on a statewide basis with the entire executive branch of a state's government. The company was selected by Governor Miller following a three-hour "chief executive officer conference" at the Governor's Residence on a Saturday during the early days of the 1994 Session.

To implement QGIP, the administration's Bureau of Personnel has entered into several contracts with Proudfoot Crosby, totalling just over \$394,000. As of mid-May 1994, slightly more than \$225,000 has been paid to the company in a number of checks, the earliest dated January 19. Initial estimates by the Governor's Office and the Bureau of Personnel put the total of projected contract costs over the life of QGIP in the \$100-per-FTE range. Using a figure of 13,000 state FTEs, this would amount to nearly \$1.3 million for the project. To date, these funds are being paid from existing state government budgets; i.e., the Legislature has made no specific appropriations for this activity.

Proudfoot Crosby's services are being delivered here over the course of a number of training sessions and phases aimed at the different strata of government managers among the departments. Here is a list of the five consultant contracts signed so far with Proudfoot Crosby Associates:

<b>CONTRACT NUMBER</b>	<b>CONTRACT AMOUNT</b>	<b>DESCRIPTION</b>	<b>DATE SIGNED</b>
0101-409-001	\$11,770	To "provide consulting and training on quality management".	January 28, 1994
0181-409-003	\$41,685	Same as above.	April 4, 1994
0181-409-004	\$80,380	To "provide training on quality for step team members and develop systems to support quality implementation."	April 4, 1994 and April 20, 1994 (extension)
0181-409-005	\$172,000	To "provide two QIPM and two QEST training sessions."	April 4, 1994
no number, as of 5/27/94	\$88,700	To "provide one QIPM. . .one QES instructor training. . . and one QWG training"	May 23, 1994

While QGIP is described in the Administration's materials as "never ending," the timeline of events scheduled thus far runs until November 4, 1994, (Attachment #1). None of the contracts listed above covers a period ending later than June 30, 1994, with the exception of the last one which is for sessions on June 27-30, July 11-14, and July 15.

To its followers, the ideas behind TQM are simple. "Deming teaches organizations to treat the people they serve as precious customers and to place customer satisfaction as the organization's primary goal; to base decisions on carefully gathered statistical data about all facets of the operation; and to bring labor and management together and keep them working closely together to find the best ways to get the job done" (Walters). The Governor has stated

his Initiative's emphasis on considering taxpayers as customers.

Opponents, however, cite the obvious: Government is not business. "Producing a product in a government agency is different than a private firm producing a car or selling insurance" (Battle and Nayak, 1994). Proponents counter that "TQM's emphasis on defining the customer and focusing on inputs and processes" is just as critical to government as it is to business (Battle and Nayak). This raises another very interesting point: Are taxpayers government's customers or are they the owners? Intuitively, what pleases the owner of a company is not necessarily what pleases the customer.

Further, TQM has a history of having been

implemented in jurisdictions by politicians who have been defeated shortly thereafter. For example, Joseph Sensenbrenner, mayor of Madison, Wisconsin, and governors Rudy Perpich of Minnesota and James J. Blanchard of Michigan were all unseated after implementing TQM. "In most places, when top elected or appointed officials dedicated to TQM make their departure, TQM very often goes right along with them" (Walters). In those cases, TQM is discontinued before any real benefits could have been gained that would have merited the trouble and expense.

It is fair to say that this effort to improve the quality of South Dakota state government is responsible for the creation of a new form of bureaucracy, to which considerable time by many employees has been --and will be--dedicated. This is because of the formal nature of a TQM program. At first glance, the Quality Government Initiative's organizational chart looks rather simple. (See Attachment #2.) It is important to note, however, that the Governor's eight-member Commission on Quality Government, according to the Administration's materials, only provides advisory input to QGIP; it is not a part of QGIP. The Commission is responsible for holding public hearings and soliciting ideas.

Thus, the real bulk of the QGIP organizational chart appears in Attachment #3. It is the activities and structure shown there that will consist of several hours of meetings each week for a number of weeks for many--and eventually almost all--Executive Branch employees. Attachment #2 only shows that part of the process up through Phase I, which occurs in late May. Looking at Attachment #1 again, one can see what is yet to occur between now and November 4.

Briefly, the flow of events has been such: following the initial sales presentation to the Governor at his residence, there was an Executive College conducted on three

consecutive days immediately following Session. This seminar was attended by the Steering Committee, the Executive Branch's twenty-three top-level managers and cabinet heads, at a contracted cost to the state of \$1,950 per attendee.

Following this, a Quality Council was assembled and charged with the responsibility for planning and implementing the overall QGIP. The Quality Council is made up of the chairpersons of seven teams of twenty-four senior managers representing each state agency. This group "developed the formal systems that will be used to implement and maintain [QGIP] within agencies." The Quality Council reports to and is directed by the Steering Committee.

The next layer of the QGIP bureaucracy's activities is a number of "Management Colleges," one for every agency, and scheduled in phases. These are four-day programs attended by all the directors of all the divisions of the various departments of the Executive Branch. Following these Management Colleges, all the attendees are to communicate the teachings of Quality according to Crosby back to all the employees of their departments via formally structured--even scripted to a point--weekly quality awareness meetings. (See Attachment #4.) The contract price for the Management Colleges was \$2,150 per attendee.

Following all these training sessions, QGIP will involve hours of in-house training for all the individual Executive Branch agencies' personnel wherein the division directors dispense to program administrators who dispense to their employees and on down the line the knowledge gained. Particularly stressed during TQM programs by Crosby's company is the formal statement of policy, which is shown in Attachment #5. In adherence to the teachings of Crosby, QGIP has adopted as its policy one which mentions "Do it right the first time, on time, every time," and which will be posted conspicuously for all executive branch

employees to view.

Crosby's emphasis on prevention as the way to quality as being something an organization learns from the top down is obvious, and he recognizes that organizations are made up of people. Thus, it's the people at all levels who have to be reached, which is why one of their programs, if it is actually completed and followed, takes so long. "Just because the general manager and the department heads have gotten religion doesn't mean that anyone else has" (Crosby, 1979, p. 55).

Perhaps what could be a significant obstacle to QGIP, that being finding the right incentives to improve process and performance, will come from tradition. This would especially be the case if the Administration used TQM-found savings to just make budget cuts. "Traditional governments actually penalize departments for saving money, first by returning the savings to the general fund, rather than the department's own budget, and then by making a cut in the next year's departmental appropriation" (Walters). Should the agency and/or its employees benefit from savings that might be realized? If so, how? Another problem, therefore, might be the crucial reliance which will be placed on whatever methods are chosen for assessing results and evaluating performance.

Perhaps these points are what make House Bills 1368 and 1369 enacted by the 1994 Legislature so crucial. The former, HB 1368, was entitled "An Act to enhance state government productivity and to continuously appropriate a portion of the certified savings." This Act says the Commissioner of the Bureau of Finance is to certify any agency savings of funds appropriated in the General Appropriation Act due to management practices. Of these savings, 50 percent is to be "continuously appropriated and limited to expenditures that enhance productivity or provide employee cash payments for innovation that contributes to

enhancing productivity". The Commissioner is to promulgate rules for this, but the Act gave few specifics. The latter Act was entitled "An Act to create a performance budgeting system for the state of South Dakota". Again, the Commissioner of the Bureau of Finance is directed to implement the law.

Performance Budgeting is defined as "the allocation of resources to achieve specific objectives based on program goals and measured results" (Carter). South Dakota uses what is known now as the Traditional Budgeting Method, wherein the Legislature appropriates money to specific programs by two expenditure categories, personal services and operating expenses. The former category consists of employee salaries and benefits. The latter consists of travel, contractual services, and capital assets, etc. Traditional Budgeting places great emphasis for accountability by the recipients or spenders of dollars appropriated by a legislature, in South Dakota it is the agency, as it attempts to precisely direct what money is to be spent and where by which agency or program.

The two expenditure categories mentioned above are further broken down to represent their components of three types of funding, those being general, federal, and other. General funding is from the state general fund. Federal funding is money appropriated to the state by Congress--usually on a matchrate basis--and other funding is usually fees received from clients, although it can also be money paid by one state agency to another state agency, as is the case with purchases of computer support or other "central services."

There is some, but not a great deal of, statutory basis for these practices. SDCL 4-8A-5 says merely that "amounts authorized as a result of the general appropriation act shall be classified and coded for budgetary accounting purposes in accordance with the provisions of chapter 4-7." Sections of that chapter,

especially §§4-7-1 and 4-7-10, dictate South Dakota's budget structure, methods, and timelines. This method of budgeting is also called Line Item Budgeting because the state's budget document consists of many, many specific "line items" of expenditure.

Like TQM, Sunset Laws, and Zero-Based Budgeting, Performance Budgeting is another movement that has received considerable attention among state governments in recent years, with some states having gone so far as to codify it. Some of those states have even codified the requisite performance goals, or "Benchmarks," as they are often called. Oregon and Minnesota have in-depth legislative/executive processes wherein quantifiable goals are defined, then their legislatures write those goals into law. The goals are sometimes long-term, sometimes intermediate, sometimes short-term. Whichever, the crucial point is that they are measurable.

South Dakota has for many years used performance indicators in measuring agencies' activity and workloads. Performance indicators themselves, which generally could be exemplified by the number of license applications processed or the number of school children or welfare recipients, should definitely not be confused with Performance Budgeting. A true system of Performance Budgeting would involve setting a societal goal, then appropriating the money to accomplish the missions associated with the goal. For example, the Legislature might set a target of a certain percentage reduction by a certain date in the number of people in South Dakota who live below the federal poverty level.

Here is where a very significant change would be necessary in the way the Legislature operates. Rather than appropriating money in the General Appropriations Act department by department and program by program, the money would probably be appropriated to less strictly defined

units of government, but with the purposes of accomplishing certain missions. This would take a lot of work because the line item way of thinking is very ingrained in South Dakota's Legislature, just as it is in South Dakota's local governments, and as it is in most places. "Most public organizations are driven not by their missions, but by their rules and budgets. . . . Entrepreneurial governments dispense with...[their] rule books and dissolve the line items" (Osborne and Gaebler, p. 110).

That is by no means to say, however, that the Governor and the Executive Branch should display complete disregard--or disrespect-- for the Legislature's line items. Definitely, the branches of government would have to agree on the merits for a successful break with line item dictates. In South Dakota, the Governor has a very powerful tool called Transfer Policy. SDCL 4-8A-8 says money "may be transferred between program accounts within or between departments and bureaus" and that the Bureau of Finance and Management has the power to approve these transfers. While Transfer Policy has been successfully and wisely used to allow for shortages in certain programs, such as Medicaid, to be funded with excesses from others, it could also be said to have been abused. For example, in Fiscal Year 1984 funds appropriated for personal services in the Department of Education and Cultural Affairs were used to buy systems furniture to furnish the Kneip Building. In that same year, funds appropriated for Aid to Dependent Children were spent as part of the expense of converting Hilger's Gulch near the Capitol into a park. For several years, there were attempts by legislators to pull back the reins on Transfer Policy, but none of them was successful.

In Reinventing Government, Osborne and Gaebler speak highly of mission-oriented approaches to government, which is what Performance Budgeting is. They would be critical, however, of any government's total reliance on just one tool or method, even if it is

not a new or trendy one. They, as well as others, would never say that a tool such as TQM--or performance budgeting, for that matter--is the one answer to all questions or problems of government. According to Steven Cohen and Ronald Brand (p. xvii), "TQM is not a cure-all, and it can be difficult to implement." They particularly criticize TQM when it places too much reliance on numerical targets because of "the games that organizations play in setting these targets. (p. 50)" They illustrate that too much attention on numerical targets can create problems rather than solve them.

Like Crosby, Cohen and Brand emphasize that TQM requires serious, long-term commitment by all levels of an organization for it to be worth the trouble and the expense. "For the people or organizations who decide to learn all they can about this way of working, who work at understanding the theory and . . . principles, who struggle to make TQM pervade every aspect of their work, and who persist over months and years, significant improvements and breakthroughs can be and have been achieved. (p. 56)" If it is dropped within a few months of its implementation, South Dakota's QGIP, with its expensive, crash-course implementation, may not meet the standards of a successful TQM project.

Osborne and Gaebler have some less flattering things to say about TQM and Performance Budgeting when either is too heavily reliant on numbers and quotas. They say that TQM does not go far enough (p. 22). They are especially critical of overemphasis on service delivery (central to the Quality Government Initiative is attention to improving customer service) and say TQM alone will not merit its trouble. "[G]overnments preoccupied with service delivery often abdicate [the] steering function", and government, to be effective, has to steer, not row, they say. They quote Mario Cuomo's statement, "It is not government's obligation to provide services, but to see that they're provided" (p. 32).

When Osborne and Gaebler do support TQM, their support of TQM could be said to be rather weak, or at least qualified. "[M]ost public sector TQM projects focus on very minor systems, the ones that are easiest to change: the schedule for garbage truck drivers; the way the city's fleet is purchased. Changing these is important, but the real challenge is whether TQM can address the big systems: budget, personnel, and accounting, or education, job training, and unemployment insurance" (p. 309). Clearly, they are addressing the need for radical changes in infrastructures, processes, and philosophies, as opposed to simple, penny-pinching improvements in paper shuffling.

Government has to become "entrepreneurial", according to Osborne and Gaebler, and they cite success stories in places like Visalia, California, and East Harlem, New York, and certain divisions of the United States Department of Defense. "Our fundamental problem is that we have the *wrong kind of government*. We do not need more government or less government, we need *better* government. To be more precise, we need *better governance*" (emphasis theirs, p.23). They do not say TQM or Performance Budgeting are bad or that they are the wrong things to do. Rather, they say that these can be wisely chosen tools, but only if used correctly as part of an honest-intentioned, drastic, systemic change in the way a government operates.

Would or could what is cited by some as proof of the success of Entrepreneurial Government ever be allowed to happen in South Dakota? The story told by Osborne and Gaebler of Visalia, California, demonstrates how, on very short notice, that city's Parks and Recreation Department was able to purchase a swimming pool that was put up for sale following the Los Angeles Olympics. Within a few hours of learning of the pool's availability, an employee was on the way with a five-figure check for the downpayment, and plans were made for moving the pool. In South Dakota a

department must plan some 18 months in advance to buy a vehicle, and then must justify it to the Governor and the Legislature.

To a certain extent, they place TQM in the same category of government reform movements as Sunset Laws, Zero Based Budgeting, and privatization. Despite attempts by so many states, none of those movements or methods ever lived up to their promises. They are particularly critical of Zero Based Budgeting when they say that process was "too cumbersome, too time-consuming, too fraught with paperwork, and too easy for managers to manipulate"(p. 116). TQM requires considerable time and effort by an organization, a point on which its proponents would agree, and Performance Budgeting, obviously, requires considerable time and paperwork and process as well. As for privatization, those "who advocate it on ideological grounds--because they believe business is always superior to government--are selling the American people snake oil. . . .Business does some things better than government, but government does some things better than business" (p. 45).

Can Entrepreneurial Government and TQM, therefore, coexist? Central to TQM is the motto "Do It Right the First Time," yet entrepreneurs "are people who fail many times. Tom Peters and Robert Waterman told managers to make sure their organizations generated a reasonable number of mistakes--because if they weren't failing occasionally, they weren't trying hard enough to succeed" (Osborne and Gaebler, p. 135). Crosby, et al stress how all levels of an organization have to completely believe in and practice TQM. So, while it may work well for processing vouchers or determining eligibility for assistance programs or maintaining vehicle fleets, is it appropriate for highest-level managers of a department or government? How would TQM come into play, for example, in the decision making process of a Department of Corrections as to whether or not to build a new prison, and, if it is decided to build, to what degree of security?

As for Performance Budgeting, Osborne and Gaebler say it is "a truism in government that the amount of money in a line item is inversely related to the amount of time the legislature spends debating it" (p. 124). It has been shown here how much more time can be spent discussing whether there should be one or two area weed and pest control supervisors, or "Weed Cops" as they are commonly known, than in evaluating critical assumptions and policies that drive the \$300-plus million Medicaid and welfare programs. Would the Legislature ever appropriate significant amounts of money for particular missions, as opposed to appropriating it to line items in departments?

So, going back to Governor Miller's press releases and comments when he announced his Quality Government Initiative, perhaps it is understandable why he makes a distinction between the purpose and efforts of his Initiative and QGIP. He said that there is no reinvention of government necessary here, but instead that they are going to improve it. Since the Performance Budgeting law previously described does not take effect until July 1, no one can predict what kind of effect its implementation will have here, or whether it will be enacted in any kind of form that is true to what has been accomplished elsewhere.

Similarly, the infancy of TQM here prevents any kind of analysis as to its success. It was mentioned earlier that TQM requires years before it is really known and understood by all levels of an organization. If it is discontinued at any time in the near future, it will be before the knowledge gained at the price of almost four hundred thousand dollars and countless hours of upper-level management's time is distributed to all the workers of all departments of the Executive Branch. All that can be known now is that that would just be an expensive waste, one which could have been prevented.



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**This issue memorandum was written by Mark Zickrick, Fiscal Analyst for the Legislative Research Council. It is designed to supply background information on the subject and is not a policy statement made by the Legislative Research Council.**

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