

structure, mission and objectives, these entities do actually share many of the same traits that led them – and continue to lead them – down a path of economic failure.

Common Ground Between FPs and LGAs

Inability to Accept Reality in Time. Theodore Roosevelt once said: “The best thing you can do is the right thing; the next best thing you can do is the wrong thing; the worst thing you can do is nothing.”

Unfortunately, nearly all restructuring organizations opt for the latter – until it’s almost too late. Facing a decline elicits many of the same emotions as the five stages of grief: denial, anger, bargaining, depression and acceptance. Many executives need to arrive at “acceptance” before they admit external independent support is needed.



While this is certainly true for all executives, it’s more common in LGAs. The thought process is simply that the agency is “too big to fail” or that the state or federal government will bail them out.

In addition, due to bylaws and bureaucracy, LGA executives are not empowered to address the challenges a distressed entity is facing in a timely manner.

So while a corporate executive views company distress as a mark against their own personal reputation and fortunes, a governmental executive simply views it as part of “the system.”

Corporate executives also typically have an entrepreneurial mentality, sometimes to their own detriment. They are eternally optimistic and believe they can change the situation without independent support. Oftentimes, these executives are too close to the action to find and deal with the sources of distress – let alone implement the required solutions.

Aversion to Change. Restructuring requires change, plain and simple. What is interesting, though, is that change management is actually the biggest obstacle when it comes to restructuring both LGAs and FPs. People in general do not like making changes – including employees, supervisors and senior executives.

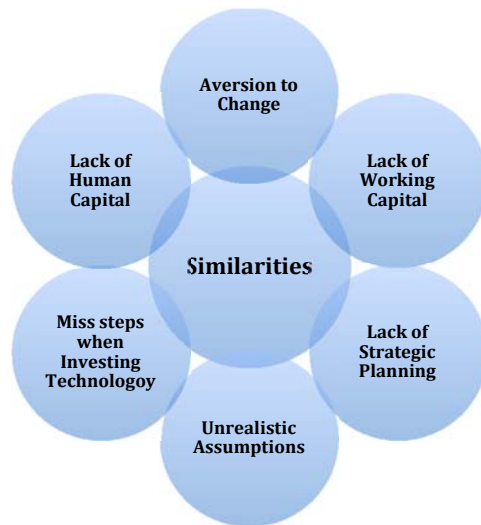
Lack of Working Capital. Whether an FP or LGA, the very fact that the organization is distressed indicates a challenge with working capital. That means obligations are due within weeks / months and yet, the revenue source either is not sufficient to absorb the expenditures or not available in the immediate future. Working capital requirements must therefore be generated from non-traditional sources.

Lack of Formal and Realistic Strategic Planning. The decisions required to properly develop a meaningful strategic plan can be daunting. However, a strategic plan is vital in order to identify assets, opportunities, timing, costs and cash requirements.

The strategic plan needs to include not only financial projections and realistic budgets, but a detailed roadmap on how and when goals will be realistically achieved, quantifiable milestones and ramifications of missing them, and internal and external required resources.

However, for many distressed FPs and LGAs, this process is seriously flawed. These organizations place too much emphasis on numbers “after the fact” with little focus on foresight.

For example, many organizations are required to have their year-end results reviewed / audited by independent experts. However, no independent professional input is sought in developing the budgetary process before the start of the next year – which would be far more insightful than a post year “snap shot.” A pro-active approach to planning vs. firefighting historical problems is a key difference between successful and distressed entities.



Unrealistic Assumptions. For those FP and LGA organizations that do go through a formal budgeting process, unrealistic assumptions can produce a shaky foundation. The most common include:

- Too much reliance on historic budgets.
- A budget tied to the economy or industry as a whole – e.g. “The economy increased 4.2%, therefore my revenue or opportunity increased 4.2%.”
- Perverted logic – i.e. “My expenses are going up X% because my revenue base is going up X%.” This is akin to stating: “All cats have four legs and my dog has four legs. Therefore my dog must be a cat.”
- Budgets are prepared year over year in the same methodology by the same teams.
- Budgets have become a financial exercise, not a business / operations one.

If an FP or LGA is serious about reducing their risk exposure due to unrealistic assumptions, they need to consider an approach such as “zero-based budgeting.”

Missteps When Investing in Technology. Technology (IT) is a great strategic asset for virtually any organization, whether an FP or LGA. When utilized properly, IT optimizes core processes in an effective manner.

However, it's also a very expensive tool when considering the necessary investments in the form of infrastructure, best-of-breed processes, support and training, along with the limited life cycle and security ramifications. Technology for technology's sake – without this complete investment – yields few tangible results. And yet, a trend in many FPs and LGAs is to shortcut one or more of these areas.

For example, one common mistake FPs and LGAs make is lack of proper, continuous training. This is astounding considering the amount spent on the solution – with nothing budgeted for training. On average, a successful implementation of a software solution should include a 30% investment of the total expenditures on end-user training.

Lack of Human Capital. Troubled FPs and LGAs generally do not have the resources or skill set on staff to address the problems occurring in a distressed organization – which is why they need a turnaround professional.

In medical terms, the turnaround specialist is analogous to the ER doctor. A surgeon or general practitioner may be ideal in their milieu, but in an emergency, one prefers to have the skill of the triage specialist that can work quickly, analyze the problem, take the right lifesaving steps, and then turn the patient over to the surgeon or general practitioner once stabilized.

Where FPs and LGAs Differ

While distressed LGAs and FPs clearly share many of the same traits, there are also a variety of dissimilarities as well.

Ability to Restructure Non-Effective Services / Entities. Generally speaking, LGAs cannot fail. They cannot just cut the most costly service to balance their budget. For example, a city is not going to stop taking 911 calls, or sell its fire department because of a budgetary issue. This fact alone puts them in a different category than FPs. An effective FP can simply jettison its non-core, or non value-added entities.



Leadership. Another major difference involves the way in which change is implemented. A CEO or CFO of a company can implement a set of changes via being a “benevolent dictator”; a governmental agency environment, on the other hand, requires multiple sets of players to review, buy-in and re-review the situation and solutions. Furthermore, the metrics by which the turnaround implementation is measured are far more defined in an FP.

Sales / Marketing. FPs must be able to communicate their products / services and convince the market to buy them. An LGA, on the other hand, does not have to “market” their services (although effective ones do). By mandate, constituents pay for services via taxes or fees. As a result, the LGA has a monopoly on services provided, which can breed major inefficiencies.



In addition, the sales department in an FP provides a turnaround specialist with an important opportunity to generate revenue that generally does not exist within an LGA.

Human Resources. By far, this is the biggest dissimilarity when dealing with FPs vs. LGAs. One is not better than the other; they are just completely different. Some of these differences include:

- Employee turnover in an LGA is less than half that of FPs.
- FPs, on average, invest far more in employee training and development, as well as succession planning / organization continuity planning.
- There is no “tenure” in FPs.
- FPs generally create long-term strategic plans that outline the next five – 10 years, while LGAs develop them based on election cycles.
- Unions are stronger in the LGA sector and declining among FPs.
- Entrepreneurs thrive on taking risks; in LGAs, risk is averted.
- Empowerment is extremely limited in LGAs.
- Compensation structure differs greatly.
- Cross training is not available in an LGA. For instance, a fire chief does not rotate to police chief.

All that said, it’s ironic that the larger an FP becomes, the more it operates like an LGA.

Competition. Herbert Hoover once said: “Competition is not only the basis of protection to the consumer, but is the incentive to progress.” Accepted statistics and reports demonstrate that our education is in decline and our infrastructures are also deteriorating. A degree of change is therefore required, but when it comes to many failing LGAs, they treasure their monolithic economic positions more than the services to be provided.

The competition FPs face can be brutal, unfair and biased. But the alternative of inefficiency and ineffectiveness is far worse.



Financials. When it comes to financing, there are a number of areas in which FPs and LGAs differ, including:

- **Cost structure.** In most situations, the costs for LGAs are inherited and obligated labor expenses and pensions. The true “discretionary costs” are minimal and decreasing every year.
- **Number of options to raise capital.** The FP has equity + debt, whereas the LGA has revenue / tax base + debt. Therefore, securing financing for an FP is generally easier than for an LGA.
- **Ability to raise taxes.** From an economic perspective, raising taxes cannot be justified unless the LGA can demonstrate additional service(s) are a greater value than the marginal increase in taxes. This is a monumental hurdle. The government’s track record in the past is so poor that taxpayers no longer give much credence to this position.
- **Measurements of the organization.** This is the “Achilles’ heel” of an LGA. For any chance of Continuous Improvement (CI), one must be able to quantitatively measure progress. One must know the exact starting point and where they seek to be during the CI process. There is no doubt that the accounting, financial reporting and urgency for short-term progression is much more in line with an FP organization and its processes.
- **Quarterly reporting.** Unlike LGAs, public FPs are required to generate and publish quarterly financial reports. Doing so forces financial discipline and accountability within a regular meaningful time period. It also enables organizations to remain proactive before year’s end and keeps stakeholders informed.
- **Financial training.** LGAs, as a general rule, do not implement training programs that ensure a natural progression of the team. For example, in an FP, a clerk may perform accounts payable-related tasks until he or she learns the vendors and the processes and is then promoted to supply chain or assistant controller.

- **Progression.** The top role within an FP organization is typically held by someone with decades of financial experience and a clear career progression within the organization or a similar organization. Unfortunately this is not the case for most of the smaller LGAs. An LGA's top financial executive does not generally possess a graduate degree or a CPA designation despite the overall dollars involved.
- **Compensation.** The average senior financial executive with similar credentials in an LGA and FP earned in 2013 \$71,000 and \$137,000, respectively.
- **Control of federal / state governments.** Reporting requirements LGAs must comply with are onerous and often outdated. As a result, LGAs are discouraged from "thinking outside the box" to find alternative solutions for the specific needs of their community.
- **Reporting / GAS complexity.** Reporting from an LGA is not as transparent as from an FP. More importantly, the Governmental Accounting / Auditing Standards do not avail themselves to the myriad challenges currently facing LGAs. A simplified means of measuring the true economic condition of the LGA is required. However, deferring results may be politically advantageous though not economically advantageous.
- **Mergers / acquisitions.** Even though redundancies are apparent between counties, cities, villages and towns – mergers have become the "third rail" in the LGA sector. In addition to the complexity of a merger and the basic fact that most mergers never reach the planned synergies or other economic benefits, even a preliminary analysis is avoided.

Communications / PR. An FP environment is based upon maintaining candid communications with stakeholders – boards of directors, shareholders, banks, employees, customers, vendors and the public. An Investor Relations or Public Relations team typically adds tangible value in presenting a clear picture of the FP entity on a quarterly basis. And by legislation, it is required to be accurate and complete.

With an LGA, however, the organization's financial picture is not generally communicated on a quarterly basis – if at all. In addition, much of the information conveyed is spun in the most positive light, so not necessarily accurate. What's most interesting about this differentiator is that it is the one that can be corrected the fastest.

Keys for Success

Every turnaround engagement and organization has its own unique set of circumstances that produced the challenging situation, thereby requiring distinctive solutions. However, when it comes to FPs and LGAs, there is certainly some common ground shared, as well as some clear differences between the two.



In the end, though, the recipe for success consists of:

- Ability to accept change
- Leadership
 - Accountability
 - Responsibility
- Communications and Public Relations
- Planning and processes
- Investing in people, including training, development and empowerment
- Understanding and delivering the services / products required by the client, customer or constituency
- Implementing proven processes, if applicable via leveraging proven technology
- Striving for Continuous Improvement and openly measuring progress
- Achieving all of the above in a cost / benefit economic manner

Michael R. Koepfel is the managing director of Lakelet Advisory Group LLC. Mr. Koepfel holds several prestigious credentials, including Certified Public Accountant (CPA), Certified in Financial Forensics (CFF), Accredited Business Valuator (ABV), Certified Information Technology Professional and Chartered Global Management Accountant (GCMA).