

PRIVATIZATION IN THE U.S.:
CITIES AND COUNTIES

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EXECUTIVE SUMMARY

A privatization revolution is taking place among cities and counties throughout the country. Privatization--the practice of transferring assets and activities out of the public sector and into the private sector--is an option local governments are increasingly turning to in order to cut costs and avoid tax increases.

- About 35 percent of local governments now contract with private companies for residential garbage collection.
- About 44 percent of local governments contract for commercial garbage collection.
- About 80 percent contract out vehicle towing and storage.

Private, for-profit firms also are under contract with city governments to repair streets, to control traffic, to provide ambulance service, to fight fires, to provide crime control, to manage public works, to manage cemeteries, museums, parks, tennis courts, swimming pools and arts and cultural centers and even to manage entire city governments.

Over the last decade there has been a virtual explosion in the extent of privatization by local governments.

- Between 1973 and 1982, the use of private firms to manage parks has increased by 2,700 percent.
- For managing recreational facilities there has been a 1,600 percent increase; for data processing a 3,600 percent increase.

The reason for privatization is almost always the same: to save money. When cities rather than private firms provide city services, street cleaning costs about 43 percent more, garbage collection costs about 42 percent more, janitorial services cost about 73 percent more, and asphalt-overlay costs about 100 percent more.

Most city governments are not well-managed, and in most cases local governments pay far more than they have to for basic city services. A California study showed that:

- Some cities spend seven times as much as other cities for janitorial services.
- For traffic signal maintenance, asphalt overlay, grass maintenance, payroll preparation, garbage collection, street sweeping, and street tree maintenance, the variation in cost among cities ranges from 350 to 650 percent.

Such variations in cost are literally unheard of in the private, for-profit sector of the economy. On the average, city governments can cut in half the cost of city services by contracting with private firms.

PRIVATIZATION: A WORLD-WIDE REVOLUTION¹

The explosive growth of government is a world-wide phenomenon. So are the problems that accompany it. Nations around the globe are experiencing more and more demands on their treasuries and a limited supply of tax revenues to pay these services. Increasingly, countries are turning to privatization as a way of dealing with budget problems.

Privatization means the transfer of government activities and assets to the private sector. It can be accomplished by selling an activity, by leasing it to the private sector, or even by giving it away. Britain began a major program of privatizing numerous state-owned industries in 1979, under the new leadership of Margaret Thatcher. Other countries, including the European nations of Belgium, West Germany and France, are experimenting with the idea. Japan, Malaysia and Singapore have major privatization projects under way. There have even been privatization experiments in the People's Republic of China.

PRIVATIZATION IN THE U.S.

The most extensive use of privatization techniques in the U.S. is occurring among U.S. cities. Increasingly, municipal governments are beginning to contract with private companies to provide city services--everything from landscaping and vehicle maintenance to dog-catching and garbage collection. Why

¹Among the earliest works pointing out the potential benefits of privatization to city governments are Robert W. Poole, Cutting Back City Hall (New York: Universe Books, 1980); James T. Bennett and Manuel Johnson, Better Government at Half the Price (Ottawa, Illinois: Caroline House Publishers, 1981) and E.S. Savas, Privatizing the Public Sector (Chatham, New Jersey: Chatham Publishing House, 1982). A data bank on local privatization in the U.S. is maintained by the Local Government Center, Reason Foundation, Santa Barbara, California. The first book to explore the political theory behind privatization and examine successful techniques for achieving privatization through the political process is Madsen Pirie, Dismantling the State: The Theory and Practice of Privatization (Dallas, Texas: National Center for Policy Analysis, 1985). The proceedings of a conference designed to explore ways of implementing these techniques in the U.S. is contained in John Goodman, editor, Privatization (Dallas, Texas: National Center for Policy Analysis, 1985), forthcoming.

are cities turning to privatization? Privatization is often politically practical because it doesn't eliminate services; it transfers them to the private sector. And, it has proven to be an effective tool for reducing government expenditures.

City administrators for years have been using private contractors on an ad hoc basis. Now government contracting with private companies is becoming a regular approach. In cities across the U.S., officials who once thought of privatization as a possible alternative are now considering it a necessity. Consider the extent to which cities now contract with private, profit-making firms:²

- 35 percent of local governments contract out residential garbage collection; 44 percent contract out commercial garbage collection.
- 42 percent contract out the operation and maintenance of their bus systems.
- 80 percent contract out vehicle towing and storage.
- 35 percent contract out the operation of day-care facilities.
- 30 percent contract out the operation and management of hospitals.

Private, profit-making firms are now under contract with cities to manage cemeteries, museums, parks, tennis courts, swimming pools, and arts and cultural centers. Profit-making firms also are under contract to repair streets, control traffic, provide ambulance service, fight fires, provide crime patrol, manage public works, and even to manage entire city governments.

Table I provides a partial list of services now being provided to cities and counties by profit-making firms. What is most striking about the table is the length and diversity of services. Indeed, there is hardly a single city service that is not being contracted out to a private firm somewhere in the U.S.

²Carl F. Valente and Lydia D. Manchester of Management Information Service, Rethinking Local Services: Examining Alternative Delivery Approaches (Washington, D.C.: International City Management Association, 1984) p. XV.

The major reason why cities are privatizing their services is an economic one: to reduce the strain on tight budgets at a time when voters are resisting higher taxes. City governments that are awash with cash rarely privatize anything. Two developments have spurred the trend: (1) growing demands on city budgets from interest groups which are becoming increasingly better organized and more skillful at exerting political pressure in pursuit of their interests, and (2) a cutback in subsidies by the federal government. As Washington scales back on aid provided to local governments, there is more pressure on city managers to find efficient ways of delivering city services.

The use of private firms to deliver goods and services previously provided by government has grown steadily in recent years. More cities are contracting out for the first time, and cities which already have tried privatization are increasing the number of privately delivered programs.

Table II shows the amazing growth in privatization between 1973 and 1982. In virtually every category of city service privatization is on the upswing. In many cases, the growth rate in privatization has been explosive.

- Over the last decade, the use of private firms to manage parks has increased 2,700 percent.
- For managing recreational facilities there has been a 1,600 percent increase; for data processing a 3,600 percent increase.

It is worth noting that the numbers in Table II probably understate the growth of privatization, because fewer cities and counties were sampled in the 1982 survey than in the 1973 survey.

How far can privatization go?

- La Mirada, California (population 40,000), contracts out more than 60 city services, and has only 55 employees.
- The Trophy Club, a recently incorporated suburb of Dallas, has only one paid city employee--a secretary.

Yet by and large, most U.S. cities have not taken full advantage of the opportunities which privatization offers. As Table III shows, among major U.S. cities typically less than half of city services are delivered privately, and less than half of those are delivered by for-profit firms. Even when cities rely on private delivery, about half of the time privatization is only partial, with the city continuing to provide some of the service with city employees.

GROWTH OF PRIVATIZATION
Cities And Counties Contracting With
Profit-Making Firms
(1973 and 1982)

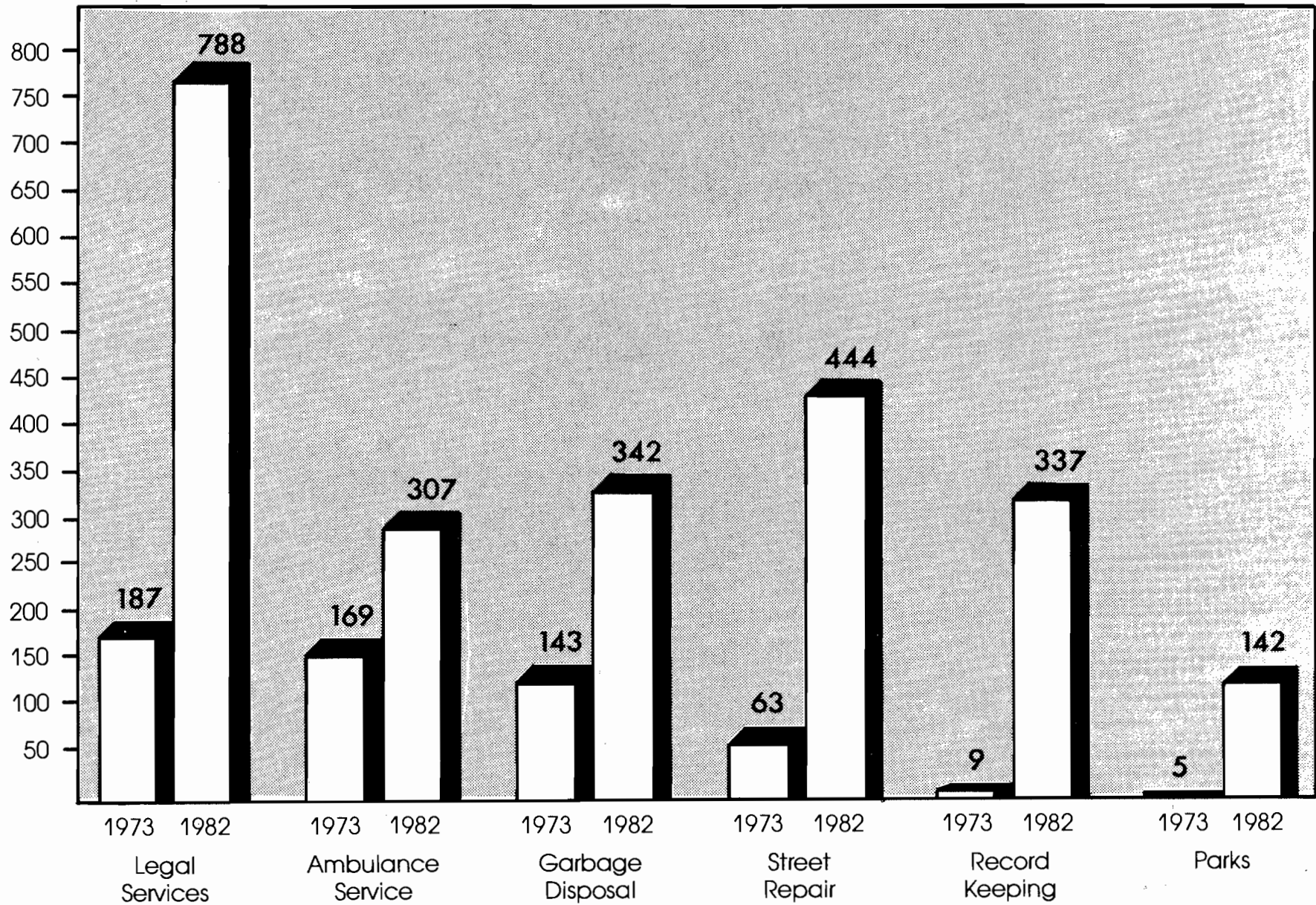


TABLE 1
EXTENT OF PRIVATIZATION
Number of Cities and Counties Contracting
With Profit-Making Firms, 1982

<u>SERVICE</u>	<u>NUMBER</u>
Public Works and Transportation	
Residential solid waste collection	482
Commercial solid waste collection	487
Solid waste disposal	342
Street repair	444
Street/parking-lot cleaning	133
Snow-blowing/sanding	180
Traffic signal installation/maintenance	408
Meter maintenance/collection	45
Tree trimming/planting	450
Cemetery administration/maintenance	77
Building inspection/code enforcement	111
Parking lot/garage operation	94
Bus system operation/maintenance	122
Paratransit system operation/maintenance	129
Airport operation	127
Utility meter-reading	120
Utility billing	162
Street light/operation	501
Public Safety	
Crime prevention/patrol	50

Police and fire communications	17
Fire fighting/prevention	15
Emergency medical service	187
Ambulance service	304
Traffic control/parking enforcement	15
Vehicle towing/storage	1,028

Health and Human Services

Sanitary inspection	9
Insect/rodent control	145
Animal control	89
Animal shelter operation	159
Day-care facility operation	153
Child welfare programs	28
Programs for the elderly	48
Operation/management of public housing for elderly	78
Operation/management of hospitals	108
Public health programs	58
Drug-alcohol treatment/programs	38
Mental Health/retardation programs/facilities	36

Parks and Recreation

Recreation services	58
Operation/maintenance of recreation facilities	123
Parks landscaping/maintenance	162
Operation of convention center/auditorium	22
Operation of cultural arts programs	49

Operation of libraries	12
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Operation of museums	20
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Support Functions

Buildings/ground maintenance	334
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Building security	120
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Fleet management/vehicle maintenance	526
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Heavy equipment/emergency vehicles	483
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All other vehicles	473
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Data processing	337
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Legal services	788
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Payroll	172
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Tax billing processing	137
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Tax assessing	73
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Delinquent tax collection	121
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Secretarial services	66
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Personnel services	83
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Labor relations	348
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Public relations/information	108
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SOURCE: Carl Valente and Lydia Manchester, Rethinking Local Services: Examining Alternative Delivery Services (Washington, D.C.: International City Management Association, 1984), Table B, p. XV.

TABLE II
GROWTH OF PRIVATIZATION:
CITIES AND COUNTIES CONTRACTING WITH PROFIT-MAKING FIRMS
1973 AND 1982

<u>SERVICE</u>	<u>1973^a</u>	<u>1982^b</u>
Ambulance Service	169	303
Solid Waste Disposal	143	342
Refuse Collection	339	486
Hospitals	57	108
Street Repair	63	444
Utility Billing	104	161
Cemeteries	47	77
Data Processing (records maintenance)	9	337
Payroll	65	172
Legal Services	187	788
Public Relations	30	108
Recreational Facilities	7	123
Parks	5	142
Fire	2	15
Crime Patrol	2	50
Traffic Control	5	15
Museums	12	20
Number of Cities and Counties Sampled	2,375	1,780

NOTE: Columns are not exactly comparable because of differences in the sample base and, in some cases, differences in the definition of the service.

(a) Derived from Advisory Commission on Intergovernmental Relations, The Challenge of Local Government Reorganization, Vol. 3, (Washington, D. C.: U.S. Government Printing Office, 1974) Appendix Table 3.A. Reprinted in E.S. Savas, Privatizing the Public Sector (Chatham House, 1982), Table 4.2, pp. 63-64.

(b) Derived from Carl Valente and Lydia Manchester, Rethinking Local Services: Examining Alternative Delivery Services (Washington, D.C.: International City Management Association, 1984), Table B, p. XV.

TABLE III

PRIVATIZATION IN SELECTED CITIES

<u>City</u>	<u>Number of Services Provided by For- Profit Firms</u>	<u>Number of Services Provided by Private Delivery: All Types*</u>
Atlanta	10	24
Dallas	7	17
Detroit	6	14
Philadelphia	16	27
Phoenix	24	32
Pittsburgh	10	19

* In about 50 percent of these cases the service is partly provided by the local government and partly provided by an alternative means.

SOURCE: Local Government Center, Reason Foundation; Santa Barbara, California.

SEVEN METHODS OF PRIVATIZATION

There are seven major methods that cities and towns have used to privatize the delivery of services:

I. CONTRACTING

This is the most widely used approach. It most frequently is used for public works and transportation, health and human services, city support functions and some public safety services.

An important feature of contracting is that of all the seven privatization methods, it holds the most potential to reduce costs. The competition between firms bidding for a service contract drives the cost down. Another potential benefit of contracting is that it allows a local government to temporarily increase services, for example on a seasonal basis, without having to hire permanent employees. It also allows a government to use workers with highly specialized skills that may be unobtainable through its own civil service.

It is worth noting that a contract can have a negative price, i.e. a private producer can pay the government for the privilege of performing the service. In New York City abandoned cars are picked up by private firms who pay the city for the right to perform the service.³ The collection of waste-paper or other recyclable materials are other examples.

Many cities and counties contract with nonprofit organizations for certain services. According to a recent survey, at least 20 percent of local governments contract with nonprofit organizations for services such as operating day-care facilities, child welfare programs, programs for the elderly, hospital management, museums and other cultural programs.⁴

2. FRANCHISES

Under a franchise arrangement a government grants a private provider the authority to deliver a service within a geographic area. Users of the service pay the provider, not the government. However, the government can regulate the level of service, its quality, and sometimes its price.

³E.S. Savas, Privatizing the Public Sector (Chatham, New Jersey: Chatham House Publishers, Inc., 1982), p. 65-66.

⁴Rethinking Local Services, p. XV.

Franchises are most frequently used for garbage collection and disposal, bus and airport operation, utility billing and meter reading, street light operation, vehicle towing and storage, ambulance service and emergency medical service. The primary benefit of franchising is that it allows a government to completely turn a service over to a private firm, while still allowing it to set service standards and rate structures. Because users of the service pay the provider directly, franchise arrangements work best when there is competition among providers and when consumers can freely change providers.

3. SUBSIDIES

Many cities find that subsidizing a service provided by a private entity is a lot cheaper than when the service is provided by the city itself.⁵

- Garden Grove, California, saved about \$72,000-a-year by turning its cultural arts center over to a nonprofit group, to which some subsidy is given.
- The city also cut the cost of its youth counseling program in half by turning it over to a nonprofit organization.

4. VOUCHERS

Under a voucher system, consumers are issued a coupon with a monetary value that can be used to purchase a particular good or service. The food stamp program is a voucher system. Although used infrequently, vouchers have the potential for a widespread application.

A principal advantage is that consumers can shop with their voucher in the marketplace and take advantage of the benefits of competition.

- In Hennepin County, Minnesota, low-income residents can use city-funded vouchers at any licensed day-care center.⁶
- In Kinston, North Carolina, elderly and handicapped people can use vouchers to pay for cab fares.⁷

⁵Rethinking Local Services, pp. 224-226 and pp. 227-230.

⁶Rethinking Local Services, pp. 231-235.

⁷Rethinking Local Services, pp. 236-239.

- Vermont has had an educational voucher system for decades.⁸

5. VOLUNTEERS

As local governments face increasing pressures on their budgets, many city managers may be surprised to learn that there is a large pool of intelligent, able-bodied workers willing to work for free. Volunteerism is not a relic of the past. Nor is it confined to small cities. Many large cities are finding the volunteer efforts of teenagers, housewives and senior citizens can be used to save a lot of money.

- In Baltimore, deputized volunteers are used to enforce sanitation and building codes.⁹
- In New Orleans 3,000 volunteers are used city-wide in 85 different agencies.¹⁰

Virginia Beach, Virginia, (pop. 263,000) seems to have taken the lead in showing how far volunteerism can go:¹¹

- The Virginia Beach libraries use more than 100 volunteers, saving the city about \$42,000 annually.
- Virginia Beach recreational programs are run with the help of about 3,000 volunteers.
- The Virginia Beach police department uses more than 60 volunteers in its non-uniformed divisions, and can draw on up to 90 additional volunteers trained to serve as uniformed officers.

⁸John McClaughry, "Who Says Vouchers Wouldn't Work?," Reason, January, 1984, pp. 24-32.

⁹Rethinking Local Services, pp. 249-251.

¹⁰Rethinking Local Services, pp. 252-255.

¹¹Rethinking Local Services, pp. 256-259, 260-262, and 266-270.

6. SELF-HELP

Self-help is a variation of volunteerism whereby workers are the beneficiaries of their own efforts. Neighborhood watch groups are an example. Other programs often having at least an element of self-help include programs for the elderly, recreation services and cultural programs.

REGULATORY AND TAX INCENTIVES

These techniques are used by local governments to encourage the private sector to provide public services, thereby reducing demand on public revenues. This strategy involves reducing regulatory barriers to business, and reducing taxes or establishing new tax incentives for the private sector to deliver a public service. Although a frequent tool of the federal government, it is used infrequently at the local level. Applications include residential garbage collection, bus system operation, ambulance service and insect and rodent control.

PRIVATIZATION THROUGH THE MARKET¹²

There is an eighth way of encouraging private sector provision of goods and services. It often is an unintended consequence of government policy rather than the result of deliberate design. If government refuses to provide public schools, private schools will soon flourish. If government refuses to carry the mail, private mail carriers will do so. If government refuses to provide police protection, private protection companies will develop. We tend to forget that throughout the 19th century, government was usually a latecomer in providing most public services--entering the market only after private entrepreneurs had demonstrated that a demand for the service was there.

Today, market provision of public services is most common in areas where government provision becomes notoriously inadequate. Take police protection, for example. Since 1960, the number of serious crimes in the U.S. quadrupled, rising from 3.3 million crimes in 1960 to 13 million in 1982. The public response to a rapidly rising crime rate has been predictable. People have sought to purchase privately the protection and security that is not being provided publicly.

- In 1960, the number of publicly employed policemen outnumbered private security guards. Today there are twice as many private security guards as there are policemen.
- Households and businesses now are spending about \$15 billion per year on private police protection--about the same amount that we spend on public police protection.

¹²The statistics in this section are taken from Morgan Reynolds, Crime by Choice (Dallas, Texas: Fisher Institute, 1985) and conversations with the author.

HOW INEFFICIENT ARE CITY GOVERNMENTS ?

Before examining the potential benefits of privatization, we can profit by taking a look at what city governments are doing right now.

Economist Barbara Stevens recently made an exhaustive study of eight major city services in 121 cities, in the Los Angeles Standard Consolidated Statistical Area.¹³ One of the most interesting findings was that there exists huge variations in the cost of providing services among the cities--variations on an order that are virtually inconceivable in the private, profit-making sector of the economy.

For example, Stevens found:

- The cost of janitorial services in some cities is more than 700 percent greater than in other cities.
- The cost of street tree maintenance in some cities is almost 650 percent greater than in other cities.
- For traffic signal maintenance, asphalt overlay, turf maintenance, payroll preparation, refuse collection and street sweeping, the variations in cost range from 350 percent to almost 600 percent.

A natural question to ask is whether these differences in the cost of city services reflect differences in the quality of the services. As it turns out, Stevens found large differences ranging from "extremely high" quality to "extremely low." Yet these differences in quality were uncorrelated with amounts spent. In her own words, "Without exception, differences in service quality were not found to explain differences in service cost."¹⁴

What, then, does explain the wide variation in cost of services among the cities. Stevens found that most of the cost differences can be explained by the use of technology and management practices. She concludes that without any change in the level of service and without any reduction in the quality of

¹³Barbara J. Stevens, "Comparing Public and Private Sector Productive Efficiency: An Analysis of Eight Activities," National Productivity Review, Autumn, 1984, pp. 395-406.

¹⁴Ibid., pp. 399, 401.

TABLE IV

**VARIATION IN COST OF CITY SERVICES
FOR 121 CITIES IN LOS ANGELES COUNTY**

<u>SERVICE</u>	<u>LOW-COST CITY</u>	<u>HIGH-COST CITY</u>	<u>DIFFERENCE IN HIGH AND LOW COST</u>
Street Sweeping cost per curb mile swept:	\$ 6.24	\$ 36.92	592%
Janitorial Service cost per 1,000 sq.ft.:	1.52	10.92	718%
Refuse Collection cost per ton collected:	12.48	43.62	350%
Payroll Preparation cost per check issued:	2.35	10.27	437%
Traffic Signal Maintenance cost per intersection:	843.00	2,801.00	332%
Asphalt Overlay cost per ton laid:	30.65	136.77	446%
Turf Maintenance cost per acre mowed:	39.02	193.46	496%
Street Tree Maintenance cost per trimming visit:	20.25	130.99	647%

SOURCE: Barbara J. Stevens, "Comparing Public and Private Sector Productive Efficiency: An Analysis of Eight Activities," National Productivity Review, Autumn, 1984, p. 398

service, the average city in her study could cut its budget for these services in half. If the cities in and around Los Angeles County are at all representative of cities elsewhere, the implications of these findings for the nation as a whole are staggering.

Is there a way for city governments to set up procedures so that there is a systematic tendency to keep costs at a minimum? The answer is: Yes, by turning to privatization.

THE BENEFITS OF PRIVATIZATION

There is a wealth of evidence that privatization can save governments a lot of money. The fundamental reason centers around competition and business incentives to accomplish a task in the most efficient and effective way, thereby retaining the contract and profiting from it. These profit and loss incentives stand out in stark contrast to the incentives of a government bureau--a monopoly removed from the benefits of competition. Municipal officials have no profit-and-loss ledgers to guide their decision-making. Typically, they are rewarded according to the size of their agencies: the number of employees and the dollar amount of its budget. Their motives are centered around expanding their territory, rather than encouraging efficiency and reducing costs.

A second reason privatization can cut costs has to do with economies of scale. For small-to-medium sized cities, the area and population often is not large enough to take advantage of economies of scale that large government-run services make possible. In these cases it makes sense to purchase the service from a supplier large enough to serve more than one city. On the other hand, for other types of services that same city may be too large to achieve maximum efficiency by using only one supplier. In these cases costs can be lowered if multiple suppliers do the job. Ironically, the one arrangement least likely to be most efficient is the one used by most cities: Services are provided by one supplier (city government) on the scale set by the size of the city.

The presence of multiple suppliers is central to both of the reasons why privatization saves money. Multiple suppliers mean competition. A monopoly that a government-provided service creates is largely insulated from consumer feedback (i.e. people's decisions on where to spend their money) and from producer cost-consciousness. Studies comparing the costs of public service show that the most important factor is not whether the service is delivered publicly or privately, but whether it is delivered by a monopoly or under competition with other providers.

Competition injects a whole new set of disciplines into a service that was previously provided solely by government. Simply having a contract go out to bid for the first time brings almost immediate changes. Local officials often find that the private supplier is far more responsive and careful about service

quality than municipal workers who took it for granted that their department would be providing the service forever.

Garbage collection is one city service that has been studied on a systematic basis. A nationwide study by two Columbia University professors found that government-run solid waste collection was 68 percent more costly than private contracting in cities with populations above 50,000.¹⁵ This study, together with other studies covering the U.S., Canada and Switzerland offer "overwhelming and clear" evidence that private, contracted-out collection is more efficient than municipal collection.¹⁶

For example,¹⁷

- A study of 131 Canadian municipalities found municipal collection was more than 50 percent more expensive per household than collection by private contractors.
- Private collection crews were found to be 95 percent more productive.

What is true for garbage collection also appears to hold for many other city services. Again, the most complete and comprehensive study to date is the study of cities in the Los Angeles area. After adjusting for differences in quality of services, level of service, scale of service, etc. Stevens found that:

- When cities do their own street cleaning, the cost is 43 percent higher than the cost for private contractors.
- The cost of city-provided janitorial services is 73 percent higher than when the service is provided by private contractors; for asphalt overlay, the cost is almost two times higher.
- Only in the area of payroll preparation do city governments keep their costs as low as private contractors.

¹⁵E.S. Savas and Barbara J. Stevens, Evaluating the Organization of Service Delivery: Solid Waste Collection and Disposal, (New York: Columbia University Graduate School of Business, 1977.)

¹⁶E.S. Savas, Privatizing the Public Sector, p. 93.

¹⁷Terry Peters, "Privatization: Public Services and the Private Sector," (Austin, Texas: Texas Research League Analysis, Vol. 5 No. 8, August, 1984) p. 5.

TABLE V

HOW MUCH CAN PRIVATE CONTRACTING SAVE ?
(based on 121 cities in the Los Angeles County area)

<u>SERVICE</u>	<u>EXTRA COSTS AS A RESULT OF CITY PROVISION *</u>
Street Cleaning	43%
Janitorial Services	73%
Refuse Collection	42%
Payroll Preparation	-0-
Traffic Signal Maintenance	56%
Asphalt Overlay Construction	96%
Grass Maintenance	40%
Street Maintenance	37%

* These cost differences are adjusted for differences in the scale of service, quality of service and physical conditions under which the service is provided.

SOURCE: Barbara J. Stephens, "Comparing Public and Private Sector Productive Efficiency: An Analysis of Eight Activities," National Productivity Review, Autumn, 1984, p. 401.

Although there was a significant reduction in the cost of the service, Stevens found no difference in the quality of the service when provided by a private contractor.

How did private contractors manage to keep costs down relative to the city governments? By using more capital, more intensive production methods, and more frequent incentive systems. Also by reducing absenteeism, giving supervisors more authority to hire and fire workers, and holding managers responsible for the maintenance of equipment, etc. In short, by doing many of the things that most business managers would do if they wanted to cut costs.

ALLAYING FEARS ABOUT PRIVATIZATION¹⁸

Some critics of privatization claim privatization will bring numerous damaging consequences, including higher costs, lost jobs and more corruption. Although it is always possible for a privatization program to be managed poorly, experience indicates that managed correctly, privatization produces good results. The following are a few principles that have been tried and tested in various cities with great success.

1. Use of private firms should reduce costs. Frequent and open competitive bidding on contracts will prevent private firms from gradually "padding in" additional costs over time. There are numerous examples of a contracted-out service being switched from one firm to another after a genuinely competitive bidding process. These include paramedic services, data processing, vehicle maintenance, and garbage collection.

2. Privatization can help eliminate corruption. The introduction of publicly advertised bidding on contracts (along with objective selection standards) helps eliminate corruption. Decisions that were once concealed from public view (particularly those made by city officials regarding public employee unions) are now out in the open and a matter of public record.

3. Privatization can create jobs. When jobs are eliminated in the public sector, resources are freed to create new jobs in the private sector. Frequently, the transfer increases overall productivity. For example, when cities use five full-time employees for a garbage collection crew when three could do the job, they are undermining the productive efforts of two people who could be producing something of value in the private sector. The transition to private suppliers may pose temporary employment problems. However, there are ways to alleviate these problems. One is to require the incoming private firm to give

¹⁸This section is based on Robert W. Poole, "Objections to Privatization" in Policy Review (Washington, D.C.: The Heritage Foundation, Spring, 1983).

the displaced government workers first preference for the job openings created by the contract. The federal government's official policy on contracting out already requires this. When a data processing company won a seven-year contract in Orange County, California, it offered all employees a job. More than 98 accepted, although after two years staffing was down to 72 percent. How did the company do it? Not by firing, but by attrition and by transferring workers upward or laterally to other jobs in the company. The opening of new career paths was a key factor in keeping the workers' morale high.

4. Privatization is politically practical. Under threat from public employee unions, political leaders may shy away from privatization proposals. However, once the majority of voters see that a particular service is being delivered more efficiently at a lower cost (which smart politicians document and publicize) public support soon materializes. The current tax-revolt attitude of the public coupled with widespread suspicion of public employee unions already is working toward privatization's favor.

5. Consumers are better served. Efficiency, responsiveness and service innovation result from privatization. When public services are organized for profit, the benefits of competition (i.e. the threat of a loss of the contract) will accrue. If a new way of performing an old task will save the company money, the company will innovate. One good example is the case of Rural/Metro, the private firefighting company contracted by Scottsdale, Arizona. Rural/Metro pioneered a "portable pipeline" feeding two or three conventional lines from a portable hydrant. The change resulted in significant savings to the city because it could double the spacing between fire hydrants. Rural/Metro also invented a remote control robot for firefighting in dangerous situations.

CASE STUDIES IN PRIVATIZATION SUCCESS

Firefighting. The case of Scottsdale's experiment with private firefighting is one of the oldest and most widely-noted privatization success stories. Scottsdale has had private firefighting (provided by Rural/Metro, Inc.) since 1952. In the mid-1970s a detailed study compared Scottsdale with three other Arizona cities of comparable size. In terms of cost effectiveness, Scottsdale came out way ahead. Over the five-year period from 1971 to 1975, the average annual cost in Scottsdale was \$6.48, or only 56 percent of the \$11.58 per capita average cost of the other cities.¹⁹

In addition to Rural/Metro's equipment innovations, the company has made shrewd and brilliant changes in the way it uses manpower. The company uses a mix of full-time and reserve firemen. The reservists are less intensively trained, are on call one week a month, and are called only for building

¹⁹Poole, "Objections to Privatization."

fires. (Full-time firefighters handle the frequent grass and trash fires.) The reserve firemen are paid only for the time they spend training or responding. Thus, the company's manpower costs are much lower than the city-run fire departments of other cities, even though its wage levels are comparable.

Prisons. Pressed by the escalating costs of housing criminals, many states are turning to the private sector to construct and operate prisons. Nationwide there is a growing list of private firms getting into the correctional industry.

One of the first to enter the field was the Nashville-based Corrections Corporation of America. CCA runs two corrections centers--a community facility for juveniles in Memphis and a processing center for illegal aliens in Houston.

Buckingham Securities, Ltd. of Lewisburg, Pa., has received approval to proceed with the design, construction and operation of a 720-bed penitentiary outside of Pittsburgh. According to officials of the firm, Connecticut, Indiana, Kentucky, Maryland, New Jersey and West Virginia have expressed interest in contracting with the facility once it is finished.

Chief Justice Warren Burger recently called on prison officials to do what they can to transform the nations prisons into "factories with fences."²⁰ Here again, the private sector already is moving ahead on that front. "Free Venture" is the name of a number of projects launched in the late 1970s in which private firms contract with prison officials for goods or services produced by inmates.

Another unusual privatization experiment in the prison industry is happening in Minnesota. A private, nonprofit data processing company leases space in one of the state's correctional facilities. Inmates do computer programming for firms such as Data Control, 3M, and Honeywell, and can earn as much as \$6 per hour.

Entrepreneurs of the private prison business say they can run prisons and jails more efficiently than public agencies. Many experts are cautiously backing the experiments. Said Anthony Trivisono of the American Correctional Association, "Many public officials hate running jails and find it attractive to get the problem off their backs while saving tax money."²¹

Education. Sharply falling student scores over the last decade attest to the fact that public education is not doing the job. But while education

²⁰U.S. News and World Report, July 2, 1984, p. 46.

²¹Ibid. p. 45.

quality has gone down, the budgets of schools continue to climb. An indicator of climbing budgets is the proliferation of nonteaching employees in schools. Some 40 percent of all public school employees have nothing to do with teaching--and in some districts that number is as high as 60 percent. Many private schools operate with less than 10 percent nonteaching personnel.²²

In comparisons of public and private schools, the private institutions usually win out. For example, the city comptroller in New York compared the city's two approaches to educating handicapped children--in public schools and in private schools by contract. The per pupil costs were greater in public schools than in private schools--\$6,196 and \$4,730 respectively.²³

- According to a 1980 study, the cost of educating a student in a private school is consistently less expensive than educating a student in public schools.
- By contrast, the average cost of public schooling is \$1,740 per pupil, according to the National Center for Educational Statistics.²⁴

Private schools are succeeding where public schools fail for a number of reasons, all of which center around the quality of teachers and the students' incentive to learn. In public schools teachers are rewarded according to how many degrees they can accumulate, not how effectively they teach. As for student incentives to learn, declining academic standards have meant thousands of graduates each year cannot read, write, or compute adequately.

For years economists have contended that to improve schools and get equal educational opportunity, the government should issue vouchers that would allow individuals to attend the schools of their choice. Schools would end up competing to attract new students, and presumably would be judged on the quality of their education. Although it is not widely known, Vermont has had a type of voucher system for education for years. Today, 95 of Vermont's 246 towns have no public high school, nor do they belong to any of the state's 27 high school districts.²⁵

²²Poole, Cutting Back City Hall (New York: Universe Books, 1980) p. 179.

²³E.S. Savas, Privatizing the Public Sector, p. 102.

²⁴Poole, Cutting Back City Hall, p. 184.

²⁵McClaghry, "Who Says Vouchers Wouldn't Work?", p. 24.

City Management. If just about every municipal service can be contracted out, what about contracting out the management and administration of the city itself? The contracting out of city management is the newest and most innovative way to shrink government.

In what he describes as "private enterprise competition to bureaucracy," a Florida entrepreneur has won contracts with two Florida municipalities to provide management, administration and even clerical services. Another entrepreneur in Florida also is winning city hall contracts to provide management and administrative services.²⁶

A third entrant into the field is the California-based Management Services Institute, headed by Douglas Ayres, a former city manager who pioneered the adaptation of private sector cost accounting to government accounting. The company already has completed extensive cost-accounting analysis for many California cities. Its staff is well-qualified. Employees include former city managers, financial directors, city clerks and municipal planners. The benefits of contracting out the management and administration of city governments are similar to the benefits of contracting out almost any other municipal function. They include reduced costs, more accountability, and better service quality. Private firms are able to spread the costs for the same management services among several municipalities. In addition, professional management firms can give more independent recommendations to municipal policymakers than a city manager whose job involves helping to meet the political needs of elected officials.

According to Ayres, injecting an entrepreneurial outlook among city hall bureaucrats usually requires a complete reorientation in thinking because "costs are an alien concept in local government." Nevertheless, the contracting out of city hall operations may become one of the most sought-after methods of cost-cutting through privatization. Reforms such as California's Proposition 4 require the strict accounting of municipal costs, which will necessitate the entry of management firms into this area. In the new climate of cost-consciousness among city bureaucrats, contracting-out may start to look more and more appealing.

THE REAGAN ADMINISTRATION'S PRIVATIZATION STRATEGY

The Reagan Administration's commitment to privatization is best known through its well-publicized attempt to sell Conrail, the federal freight railway. Less well-known, however, are the Administration's efforts to encourage privatization at the local level. For example, the federal government

²⁶Philip E. Fixler, Jr. "Contracting Out Management/Administration" in Fiscal Watchdog bulletin (Santa Barbara, Ca.: Local Government Center, March 1984).

now spends about \$870 million per year subsidizing mass transit. However, the Administration has been pressuring the recipients of this aid to look to private sector provision of services as a means of reducing costs.

In December, 1984, a regulation went into effect requiring local governments that get mass transit funds to allow private operators to bid for contracts to operate bus lines and other transit facilities. In addition, the Administration is considering proposing legislation that would require recipients of transit subsidies to turn over at least 20 percent of their operations to private enterprise.

So far, the Administration has made measurable progress on the transit front:²⁷

- Private industry has taken over operation of as much as five percent of public mass transit--up from one percent in 1981.
- Nationwide, about 100 private companies now operate mass transit buses on fixed routes.
- Private concerns also operate about 400 van services.
- The cost of private operation averages from 35 to 50 percent less than the cost of public operation.

PRIVATIZATION IN GREAT BRITAIN

Britain is far and away the leader in the world-wide trend toward privatization. Since taking office in 1979, Margaret Thatcher has presided over a vast transfer of government property and activities from the government to the private sector. In the process, both the politics and the economy of Britain have been transformed.

While other countries have just begun to experiment with privatization, the British have honed it to a science. The Thatcher government has employed more than two dozen different techniques to achieve public-to-private transfers: nearly every aspect of British economic life has been changed as a result.

²⁷ Martin Tolchin, "Private Concerns Gaining Foothold in Public Transit," New York Times, April 29, 1985. pp. 1,9.

Among the dozens of state-run enterprises that have been wholly or partially transferred to the private sector are the following:²⁸

- British Telecom, a huge government-owned telephone and telegraph company, was sold to the public last November. It was the largest public offering of stock in history. Two million Britons bought shares; about half were first-time investors.
- Nearly 190 million shares of British Leyland (manufacturer of the Jaguar) were sold to the public in 1983. There were traffic jams and fights in the street as potential buyers rushed to apply for the stock.
- The government has sold all of its stock in British Sugar, and 51 percent of its stock in Britoil (North Sea oil exploration) and British Aerospace.
- It has sold almost 40 percent of its stock in British Petroleum, and has sold off subsidiary operations of British Steel, British Rail and British Airways.
- Every city and town in Britain has contracted at least one service out to private firms, and most are contracting out several services.

One of the most successful transfers has been the sale of government-owned housing. When Thatcher took office, one-third of all British housing was owned by the government. Thatcher began selling the houses to the tenants at greatly reduced prices--up to a full 50 percent below the market value. The response since then has been overwhelmingly positive. According to Madsen Pirie, president of the London-based Adam Smith Institute, a behind-the-scenes architect of many privatization programs, the housing sale was the "largest transfer of property since the dissolution of the monasteries by Henry VIII."

The British have even applied the privatization scalpel to entitlement programs. Although Thatcher can't claim all of the credit for it (the previous Labour government enacted the law), about half of all British workers have been contracted out of the second tier of Britain's social security system. Under the arrangement, workers are allowed to substitute private pensions for participation in social security.

²⁸Madsen Pirie, Dismantling the State: The Theory and Practice of Privatization (Dallas: National Center for Policy Analysis, April, 1984).

A recent Background Briefing released by the British Treasury says that privatization "ranks among the most radical reforms of the UK's economic and industrial structure since 1945."²⁹ The government's record thus far supports this claim:

- Nationalized industries once accounted for 10 percent of Gross Domestic Product and one-seventh of total investment in the economy. The government has sold more than \$5.5 billion of stock in nationalized companies and intends to continue selling at the rate of about \$2 billion a year.
- When Thatcher took office, nationalized industries employed 1.5 million people and dominated the transport, energy, communications, steel and ship-building sectors of the economy. To date, more than 400,000 jobs--almost one-third of the total nationalized work force have been transferred to the private sector.

CONCLUSION

The growth of government can be halted and reversed by privatization. Dozens of U.S. cities already are experimenting with privatization (some on a large scale) as a means of improving city services and controlling their costs. Privatization is a solution for other reasons as well. It can create jobs. Consumers are better served. And it is politically practical.

The U.S. can look toward Britain as a privatization role model. In the last five years Prime Minister Margaret Thatcher has been "dismantling the state" on a massive scale, proving that even in countries which have strong socialist backgrounds privatization can work, and with support from the voters.

NOTE: Nothing in this report should be construed as necessarily reflecting the views of the National Center for Policy Analysis or as an attempt to aid or hinder the passage of any bill before Congress or any state legislature.

²⁹British Treasury, "Privatization in the United Kingdom", January, 1985.

APPENDIX

PRIVATIZATION IN TEXAS

A 1982 survey revealed that contracting-out is becoming an established practice among Texas cities. Of 50 major city services, 45 are being provided by private firms in at least one Texas city.

- Ninety-five percent of Texas cities contract with the private sector to perform at least one service.³⁰
- Nearly every municipal service is being contracted out to some extent by Texas cities.³¹

The survey found that a relatively small number of municipal services account for most of the private sector contracting. (Of the 1,042 contracts issued by Texas cities, 23 types of services accounted for 90 percent of all contracts). The most frequently contracted out services are listed in Table IV.

Although contracting with private firms is a common practice among Texas cities, in many areas Texas is well behind the rest of the country in its privatization efforts:³²

- Garbage is collected by private contractors nationally three times more frequently than in Texas.
- Ambulance services are contracted out nationally at twice the rate of Texas.
- In transportation, half of U.S. cities have private contracts for some form of public transportation, yet only four Texas cities have contracts of this kind.

Table VII indicates that not only does Texas lag behind the rest of the country in privatization, it also lags behind neighboring southern and western states.

³⁰David W. Tees and Stanley E. Wilkes, Jr., The Private Connection: A Texas City Official's Guide for Contracting With the Private Sector (The University of Texas at Arlington: Institute for Urban Studies, December, 1982), p. 11.

³¹Ibid. p. 15.

³²The Private Connection, p. 15.

TABLE VI

**SERVICES FREQUENTLY CONTRACTED
OUT BY TEXAS CITIES**

<u>Service</u>	<u>Percent Contracting</u>
Engineering	65%
Legal	48%
Architectural	36%
Street Lighting	35%
Garbage Collection	33%
Street Construction and Maintenance	27%
Ambulance Service	23%
Mapping	22%
Tax Collection	21%
Utility Billing	15%
Planning	15%
Police Training	15%
Water Supply	11%
Building and Mechanical Inspection	11%

SOURCE: David W. Tees and Stanley E. Wilkes, Jr., The Private Connection: A Texas City Official's Guide for Contracting With the Private Sector (Arlington, Texas: Institute for Urban Studies, University of Texas at Arlington, 1982), p. 12.

TABLE VII

PRIVATIZATION: TEXAS VS. THE REST OF THE NATION
(late 1970's)

<u>REGION</u>	<u>AVERAGE NUMBER OF CONTRACTS PER CITY</u>
North Central	9.0
North East	7.0
West	6.0
South	5.8
Texas	5.0

SOURCE: Patricia S. Florestano and Stephen B. Gordon, "Public vs. Private: Small Government Contracting with the Private Sector," Public Administration Review, January/February, 1980, p. 30. Cited in David W. Tees and Stanley E. Wilkes, Jr., The Private Connection: A Texas City Official's Guide for Contracting with the Private Sector (Arlington, Texas: Institute for Urban Studies, University of Texas at Arlington, 1982), p. 16.

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