

Stewardship Series #2



Competitive Bidding and Privatization



Evergreen Freedom Foundation

P.O. Box 552, Olympia, Washington 98507 | (360) 956-3482
fax:(360) 352-1874 | effwa@effwa.org www.effwa.org

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The Authors

Bob Williams

President & Senior Research Analyst

Lynn Harsh

Executive Director & Senior Research Analyst

Amanda Jarrett

Research Analyst

The Evergreen Freedom Foundation

The Evergreen Freedom Foundation (EFF) is a non-profit, educational research organization. The Foundation's mission is to advance individual liberty, free enterprise and responsible government. EFF staff conduct research and publish analysis and policy alternatives in the areas of state budgets; governance and citizenship; and health, education and welfare reform.

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Competitive Bidding and Privatization

Mandating results not means

Faced with rapidly increasing costs and frustrated taxpayers, government at all levels is seeking ways to better manage resources. Two mutually-beneficial mechanisms used by a growing number of states and cities are “competitive bidding” and privatization.

As governments review their core missions, leaders will decide certain services are not a mission of government and can best be left entirely to the private sector. Even determination that a particular function is related to government’s core mission does not mean the government can best deliver the services.

For example, lawmakers or agency directors might question why state employees must be hired to wash windows or provide grounds maintenance for state office buildings. They might decide this has nothing to do with delivering core services and can be done less expensively by a private firm, especially since the private firm will pay taxes on equipment and supplies that the public sector is exempt from paying. If agency directors or lawmakers turn window washing and grounds maintenance over to outside contractors, they have privatized the service.

Competitive bidding is different in that public employees are able to compete with the private sector to provide a service. For example, if agency directors or lawmakers determine the washing of state office building windows is part of their core mission, they could put the contract out for bid in the private sector as well as with state employees currently employed in that arena. Each would bid for the contract according to prearranged specifications and guidelines.

Competitive bidding and privatization are logical outgrowths of the government subcontracting that has been used for years. But there are differences. Foremost among them is the primary question: Should government be delivering this service in the first place?

Additionally, subcontracting has been restricted to a narrow range of services and has not allowed public employees in the competitive loop.

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Far more than management tools, competitive bidding and privatization are a demonstration of government’s willingness to respect the people it is supposed to serve – the

people who pay the bills. **A strong message is communicated by government leaders when they agree to deliver quality services to taxpayers at the lowest possible cost regardless of powerful, contrary traditions.**

The following is taken from “Competition and Choice in New York City Social Services,” written in 1999 by Professor E.S. Savas at the School of Public Affairs, Baruch College, City University of New York.

CONTRACTING FOR SERVICES

“Governments hire for-profit and nonprofit organizations and pay them to provide services specified by the government. In the United States, governments at the local, state, and federal level have been contracting for services, usually under competitive conditions, for a wide range of activities. Contracting has been very successful, increasing efficiency and cutting costs without reducing the level or the quality of services. The summary in Table 2 shows the results of the major studies of contracting for government services. These studies were conducted in several countries and at different levels of government by a variety of independent agents.

Table 2. Summary of Before-and-After Studies of Contracting

Contracting Agency [Source of Study]	Number of Contracts	Cost before contracting (millions)	Savings (percent)
Los Angeles County, 1979-87 [Los Angeles County Auditor-Controller]	651	\$268	32
Los Angeles County, 1979-89 [Los Angeles County, Auditor-Controller]	812	701	28
U.S. Department of Defense, 1980-82 [same]	235	1,128	31
U.S. Department of Defense, 1983-84 [same]	131	132	33
U.S. Department of Defense, 1978-86 [U.S. General Accounting Office]	1,661	2,270	27
U.S. Department of Defense, 1978-94 [Center for Naval Analyses]	2,138	4,768	31
Wandsworth Borough, London, 1978-87 [Centre for Police Studies]	23	174	27
GSA Public buildings Service, FY92 [U.S. General Accounting Office]	576	N.A.	25
State of Western Australia, 1993-94 [University of Sydney]	891	324	20
E.S. Savas, <i>Privatization and Public-Private Partnerships</i> (Chatham House Publishers, New York, 2000), pg. 150.			

“The Los Angeles County Auditor-Controller examined all 651 contracts entered into by the County over an eight-year period for data conversion, grounds maintenance, and custodial, food, laundry, and guard services. The contracts totaled \$182 million and saved the County \$86 million from its original in-house cost of \$268 million; that is, the in-house cost was 47 percent greater than the contract price. ...A total of 2,700 positions were eliminated, or 3.6 percent of the county’s total. Los Angeles then expanded its privatization program even more aggressively, and a subsequent study two years later summarized the County’s ten years of experience: A total of 812 contracts costing \$508 million resulted in savings of \$193 million, or 28 percent; 4,700 positions were eliminated, or six percent of the total, yet this was accomplished with only a handful of layoffs. (No information is presented on the relative quality of the work or on the cost of contract administration and monitoring.) This study is particularly compelling as the county official who conducted these studies is independently elected and not part of the county administration that contracted for the services.

“At the request of the U.S. Congress, the Department of Defense reported before-and-after comparisons of its contract for commercial services. The study covered all 285 contracts awarded during a two-year period for support activities such as data processing, food service, and audio-visual services, and revealed that the cost of this work when done in-house prior to the competitions had been 45% higher than the cost of the contract work. (Therefore, the savings were 31%.) A similar study of all 131 contracts awarded the next year showed that the contracts cost \$87.5 million, but saved \$43.9 million; that is, the in-house cost had been 50% greater and the savings were 33%.¹

“No data on comparative quality are offered nor are the costs of contract administration and monitoring discussed. The studies cover only the cases where contracts were *awarded*; presumably there were many cases where no savings could have been realized and, therefore, no contracting took place. Thus, one cannot conclude from these Los Angeles and federal studies that *all* in-house services cost 28% to 50% more than comparable contract work.

“The U.S. General Accounting Office (GAO) examined 1,661 cost-comparison studies covering 25 major types of commercial functions performed by the Department of Defense. (This study encompassed the 416 studies (285 plus 131) discussed in the preceding paragraph.) The original cost of the in-house work was compared to the contractor bids and to lower-cost bids made by in-house units facing the threat of privatization. The GAO found that the original cost had been saved by this competitive process. This study was subsequently extended to cover eight more years, a total of 2,138 contracts; the updated data show that savings due to such competition increased to an average of 31 percent over the entire sixteen-year period. As in the case of Los Angeles County, this study was carried out by an independent agency.

...About one-third of the competitions were won by the in-house work force and two-thirds by private contractors, leading to overall savings of 27 percent.

“The other three studies shown in Table 2 reveal similar findings. The Borough of Wandsworth, in London, introduced competition for its municipal services. About one-third of the competitions were won by the in-house work force and two-thirds by private contractors, leading to overall savings of 27 percent. A GAO study of the Public Buildings Service of the U.S. General Services Administration

focused on custodial and maintenance contracts for buildings and found that savings averaged 25 percent for the services that were contracted out. The Competitive Tendering and Contracting Research Team at the University of Sydney studied contracting in the State of Western Australia and found that savings averaged 20 percent of the pre-contract cost.

“What is most striking about Table 2 is how similar the results are in the United States, England, and Australia; the savings range from 20 to 33 percent. Although these before-and-after studies did not examine the quality of the contractor’s work, other studies did and found no significant difference between the work performed by a government agency directly using its own employees and that of contractors selected by competitive bidding. Privatization by contracting for services clearly works. It works because it introduces competition among service providers and gives government agencies a choice among them. To survive in a competitive environment, service providers have to become efficient, innovative, and flexible, and adapt rapidly to changing circumstances.”²

PRIVATIZATION

Conversations about privatization have been held all around the country for the past twenty years. Competitive bidding has been championed for most of this decade. Both strategies have been tried numerous times at various levels of government and the balance sheet tips strongly in their favor. Yet the momentum to implement these strategies has been slow in building.

President Clinton and Vice President Gore discussed privatization as a major component of their government reform efforts. In December 1994, Gore told *USA Today* his goals for government reform included three elements, the third being, “...we will be bold in eliminating things that don’t work, that have outlived their usefulness, that can be done better by the private sector or by the state and local governments, and in the process will save money.”³

In January 1995, when Gore announced REGO II (Reinventing Government), he said, “...we will examine the basic missions of government, looking at every single government program and agency to find and eliminate things that don’t need to be done by the federal government.”⁴

But turning the talk into reality has been slow for several reasons. For one thing, genuine ideological differences exist between what the electorate and their representatives view as the role of government. Some believe, for example, that it is a proper function of government to regulate and distribute hard liquor. Others say government has no business in that business. The same differences surround welfare, education, health services, and the list goes on.

...we are so used to government’s involvement in almost every aspect of our lives, it is difficult to remember when it wasn’t so. While we clamor for change, it frightens us.

The reality is, we are so used to government’s involvement in almost every aspect of our lives, it is difficult to remember when it wasn’t so. While we clamor for change, it frightens us.

But the biggest reason implementation of privatization and competitive bidding strategies have been slow to start can be simply stated – *public employee unions!*

Little Shop of Horrors

Why *are* private contractors forbidden to wash windows in state office buildings? Why *are* state employees the only ones who can mow lawns at public sites? Shouldn't private firms be able to run the government mail rooms, maintain the computers, and procure and deliver supplies?

In reality, public employee unions dominate most state capitals. The word "privatization" is their call to arms. And "competitive bidding," while palatable to some union leaders, is not well understood by most union members.

Union objections are understandable when considered from *their* point of view. As an entity – separate from individual members – unions only survive when their membership is stable or growing. When portions of work, previously reserved only for unionized public employees, are successfully contracted to private firms, union membership eventually declines. A decline in membership equates to a decline in influence; not something to be taken lightly if you are a union leader.

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Enormous pressure is then exerted on lawmakers by the union to reject any proposal that might reduce their work force. Numerous objections are raised. Unions say privatization portends serious problems such as high unemployment rates and a lack of protection for public workers. Since union leaders equate the entity's (union's) survival with that of their members, protection for the organization will be demanded in tandem with protection for their employee members.

As Audrey discovered in the play *Little Shop of Horrors*, the line "Feed me, Seymour, feed me," is not a joke when it comes to public employee unions.

States that have attempted privatization or competitive bidding strategies have run into the union buzzsaw. Most legislators who support the concept find their spines turning to jello when faced with union anger and demands. So far, union pressure against privatization has generally guaranteed that any bill dealing with privatization ends up more worthless than the paper it is written on.

As a result of the union's ability to lock up most state capitals, America's big cities have been the ones leading the way in implementing privatization and competitive bidding.

But are the union's fears for their members justified? Will their members face high unemployment and will they lack the protection the union tries to provide?

Myth of State Employee Job Loss

Several nationwide surveys have found little evidence of unemployment among government workers after privatization and competitive bidding programs have been implemented. A survey completed by the Michigan Privatization Council discovered that ten of the twenty most commonly delivered services were contracted out in more than half of the 25 cities surveyed in their state. Even so, excluding one town

which was in receivership, very little unemployment of government workers was found. The breakdown was as follows:⁵

- 86 percent of public employees were hired by the private companies that took over the service
- 10 percent were placed in other government positions
- 3 percent retired
- 1 percent were laid off

When Lee County, Florida put its wastewater treatment plant out to bid, the winning bidder, ST Environmental Services, came in about \$7 million lower than the county staff and the next private bidder. Though these savings were great enough to finance a new water plant expansion and to add an injection well for effluent flow without any rate increases, no employees had to be laid off. The contractor agreed to take on all displaced employees and reduce the number of workers simply through attrition.⁶

AFSCME Position

It is suitable for a union to desire and work for the best wages, benefits and protections possible for its members. That is its job. But it is the job of legislators to procure the best possible services for taxpayers at the lowest possible price. Public employees can rarely deliver that combination, generally through no fault of their own.

From our immense federal government to local assemblies in hamlets scattered throughout the Cascades, most governments are structured to ensure costly mediocrity. Individual employees are rarely ever able to alter the structure either for cost effectiveness or excellence, but they take the brunt of voter anger. Reflect on this story printed in a pamphlet from the largest public employee union, American Federation of State, County and Municipal Employees (AFSCME) on how this works.

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“Consider the typical front-line worker who staffs the drivers license window at the motor vehicles bureau. She’s the only one there – the other three windows are closed. Fifty people are waiting in line. They’re looking at their watches; frustration is building. Finally, when they get to the counter, they’re not mad at the governor, the mayor or the politically-appointed manager. They are mad at her.

“It doesn’t matter that she had nothing to do with the public policy or the management structure that created the problem. It doesn’t matter that her supervisor won’t let her do anything outside of normal procedures – even if it would speed up the process. To the frustrated people waiting in line, she is responsible for the poor service.”⁷

Readers of this AFSCME pamphlet, however, will not find recommendations to turn over any of their current responsibilities to the private sector to enhance efficiency. Nor will the differences between wants and needs be discussed. AFSCME frequently uses the word “need” in reference to services that

they feel *must* be delivered to the public. They evidently believe it is imperative for government to continue performing all its current functions, but that it should do so more efficiently.

We disagree with the assumption that government should continue doing everything it is doing today, only in a more efficient manner. But as important as this fundamental disagreement is, AFSCME clearly pinpoints areas in need of immediate reform that can be addressed even by those who disagree ideologically on core government functions.

For example, AFSCME says “...as the need [we would say desire] for public services has multiplied, governments at every level have clung to old and out-moded management structures that stifle service delivery and inhibit the ability of front-line employees to meet the public’s changing needs.”⁸

AFSCME argues the benefits of giving front-line workers more training and responsibility, and greater flexibility and authority. They say “...cut inefficient hierarchies and wasteful layers of management” separating front-line workers from decision makers.⁹ We agree.

While lawmakers and the public debate the role of government, no ideological problems should stand in the way of streamlining the delivery of government services.

AFSCME developed a series of five principles they believe will change the way government does business for the better.¹⁰ The nucleus of its proposals is to change the command-and-control management model and to put trained, empowered employees closer to the public they are serving.

Principle #1: Government must always strive to provide the highest quality services to the public...

“...people pay taxes and expect quality services in return.” AFSCME calls this a social contract and to maintain it, they say “government must constantly strive to improve quality, eliminate waste and address the changing needs of the public.”

Principle #2: Treat front-line public employees and their unions as resources and partners in service delivery.

Allow workers to participate in decision making and in designing and developing public services.

Principle #3: Create a responsive and more flattened bureaucracy with fewer layers between decision makers and front-line workers.

“Sanitation workers and tree trimmers ask why their daily routes are devised by managers who have never been on a truck. Hospital workers can’t understand why procedural rules force them to find a supervisor before cleaning an overflowing toilet.”

“...the more layers of management, the more rules there are to follow, and the fewer resources available for the workers who actually perform the job.”

Principle #4: Invest in worker training to improve the delivery of services and the quality of these services.

In a workplace devoid of numerous layers of management, workers will be asked to assume more responsibility and make broader decisions.

Principle #5: Redesigning government requires a long-term commitment and protections for workers.

Now What?

If agreement exists that ideological differences about the role of government should not stand in the way of delivering services more efficiently, we can proceed toward making it happen. How do we start in our own state?

In the 1970s, a suit was brought against Spokane Community College by the public employees union when the college tried to contract with a private firm for janitorial duties performed in a new facility. In 1977, the Thurston County Superior Court ruled in favor of the college. But the union eventually won their suit when the 1978 Washington Supreme Court ruled, “...where a new need for services which have been customarily and historically provided by civil servants arises, and where there is no showing that civil servants could not provide those service, a [private] contract for such services is unauthorized.”¹¹

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The next year the legislature went even further and amended state law so that no contract “...may be executed or renewed if it would have the effect of terminating classified employees or classified employee positions existing at the time of the execution or renewal of the contract.” This is now RCW 41.06.380 and 41.06.382.

Since then, legislators have rarely even considered the benefits of privatization or competitive bidding. **In fact, legislators have found it easier to raise taxes on an angry public rather than risk antagonizing unions by discussing whether or not higher-quality services could be provided to citizens at lower costs.**

This being the case, we recognize the virtual inability of our governor or legislators to communicate with public employee unions on the subject of privatization at this time. EFF suggests that the governor and legislators drop most privatization ideas for now and implement competitive bidding instead.

WARNING: If competitive bidding is not implemented correctly, it would be better not to implement it at all.

COMPETITIVE BIDDING

A basic economic axiom is that competition in the marketplace improves performance or product and keeps costs down. On the other hand, government monopolies, with no competition-induced incentives, are characterized by higher prices and limited production. “Competitive bidding” acknowledges these principles while recognizing that most public employees are able to compete head-to-head with the private sector if given the opportunity. The challenge is finding a way to release worker creativity and reward initiative in government while making sure taxpayers receive the best value for their money.

A competitive-bidding system would empower state employees to make decisions, to take risks, to do the best job they can. It would enable state employees to compete fairly with the private sector.

Competition Lowers Costs

Competitive contracting would not necessarily result in the private operation of public services. It merely requires that quality public services be provided at the lowest possible cost.

Overwhelming evidence exists showing that competition in public services can spur lower delivery costs. The Reason Foundation found the effect of competition on service delivery can generate cost savings in the range of 20 percent to 40 percent.¹²

For more than a decade, the Phoenix Public Works Department has required city units and private firms to compete to deliver a variety of public services. In 1978, garbage collection became the first service opened to competitive bidding. Initially private trash haulers were able to win all the contracts. It took the Public Works Department several years before it became competitive with private firms. By the early 1980’s municipal workers were regularly winning contracts – 39% of contracts put out to bid are won by public employees.¹³

The most comprehensive competition program of any large city in America exists in Indianapolis. The administration of Mayor Stephen Goldsmith has identified hundreds of competition opportunities, and over 60 city services have already been shifted into the marketplace.¹⁴ Services opened up to competition include trash collection, printing, equipment maintenance, upkeep of municipal golf courses, street repair, and wastewater treatment operation¹⁵. City employees, when given time to prepare to bid competitively have won about 40% of the bids, while 60% are won by private companies. Over the last 8 years, the City of Indianapolis has saved \$450 million because of competitive bidding, and this number continues to increase.¹⁶

In Philadelphia, Mayor Rendell is aggressively pursuing a competitive process for delivering city services. Since October 1992, 46 city services have been contracted out. Competitive bidding has saved the city \$38 million per year.¹⁷

Two cautions are in order. First, competitive bidding does not take the place of determining core functions. As we have already stated, governments at all levels will likely decide that some of the services they are delivering are outside the scope of their core functions and are best left entirely to the

private sector. Putting this category of services out for competitive bid rather than eliminating these functions makes no sense.

Our second caution: Though our research indicates competitive bidding has generally delivered that which was expected and more, several notable failures have also resulted. Successful competitive bidding requires *strong support from elected leaders, explicit expectations and timelines, regular review, clear and cooperative lines of authority, and appropriate timing*. In other words, competitive bidding will fail if it is manipulated or poorly planned.

In 1996, California governor, Pete Wilson, proposed to privatize everything from road maintenance to the state worker's compensation fund. Two years later, "his successes in privatization could be counted on one hand, with a few fingers to spare."¹⁸ The bills that the governor introduced mostly quietly died away, and state employees sued the state a number of times to stop the administration's outsourcing contracts. Governor Wilson's only significant success took place in August 1998 with a large \$929 million contract to operate the state government's telecommunication network. The Reason Public Policy Institute states that Governor Wilson's story is in many ways similar to that of Massachusetts governors William Weld and Paul Cellucci – "all three underestimated the opposition they would meet and were not willing to fight the tough battles required to convince people that privatization was the right policy choice."¹⁹

Successful competitive bidding requires strong support from elected leaders, explicit expectations and timelines, regular review, clear and cooperative lines of authority, and appropriate timing.

Competitive bidding is a powerful weapon in the fight to reduce the cost of public services. One of our nation's largest CPA firms, Touche Ross, surveyed the locales and states using competitive bidding and reported cost savings in 98 percent of the competitively contracted services. In some instances savings were more than 40 percent.²⁰

Lower costs for other government services are realized when competitive bidding begins. Duties retained by governmental divisions, but subject to competitive bid, show improved efficiencies.

Competitive bidding may increase the tax base and thus boost state revenues. In contrast to government agencies which are tax exempt, private contractors must pay taxes on supplies they purchase, assets they own, or profits they earn. As a result of this increased revenue to government, net costs of providing contracted public services when the contract is awarded to the private sector may exceed 10 percent of the gross revenues.

Competitive bidding, which allows public employees to bid for jobs along side private firms, has an excellent track record of allowing public employees to keep their jobs. In other words, when given the opportunity, public employees were able to streamline service delivery to the point that they were competitive with the private sector.

Competitive bidding benefits can be powerful depending on how comprehensive and robust the program is. The degree to which contractors, be they public or private, are held to high performance standards will also determine its effectiveness.

In its report on privatization opportunities for the states, Reason Foundation listed seven advantages of privatization that we have found to be very sound. When applied to competitive bidding we feel they are as advantageous.

Reason says privatization can:²¹

- save taxpayers' money,
- increase flexibility,
- improve service quality,
- increase efficiency and innovation,
- allow policymakers to steer, rather than row,
- streamline and downsize government, and
- improve maintenance.

These should be powerful incentives for state lawmakers to review competitive bidding as an option to deliver many state government services.

Therefore, EFF recommends that the legislature develop and follow a competitive-bidding-program with the following components:

1. Designate a Competitive Bidding Director to carry out the goals as they will be outlined by the governor or lawmakers. This person needs to be highly visible and have direct access to the governor and lawmakers. Perhaps this is a job for the Lt. Governor.
2. Identify government services which would benefit from competitive bidding. These can range from support services to entire programs. The list of opportunities is long, but here is a start. In general: accounting, landscape and building design, auditing, construction, inspections, maintenance, central purchasing, computer systems design and maintenance, janitorial services, data processing, employee daycare, energy weatherization, engineering services, facility management, mail room, printing, security, archives, technical consulting, telecommunications, trash removal, etc.

Specific to Corrections: administration, maintenance, data processing, education, food service, health care, housekeeping, maintenance, rehabilitation, security, and transportation.

Specific to K-12 Education: school bus transportation, management of schools and school districts, custodial services, accounting, and “at-risk” education instruction.

Specific to Higher Education: administration, book store operations, custodians, data processing, management of dormitories, food services, health care, maintenance, security, recreational facilities, and transportation.

Specific to Transportation: development and upgrades of airports, roads and high-speed rail; rest-area maintenance (in return for letting businesses locate in rest areas, they would maintain the entire rest-area and pay a user fee to the state), public transit, motor vehicle registry, and fleet operations and maintenance.

Other:

- Liquor sales and distribution.
- Workers' compensation system.
- Health services including administration, clinics, community health, hospital operations, and mental health.
- Social services including child support enforcement, welfare administration, job training, retraining, day care, and rehabilitation services.

Important Considerations: Each opportunity will present a different set of circumstances that must be individually considered. Use the experience of other states as a guide to what has been successfully completed, what has failed, and why.

Key questions to ask when considering projects for contracting are:

- Is this a task or program suitable for a long term contract or does it need to be on a short lease?
- Can objective performance measures be determined including timelines?
- If the contract needs to be monitored, will contracting out allow this to occur. If so, how?
- Can more than one firm provide the service to ensure competition and to guarantee an option should the first firm have trouble completing the contract?
- What is the impact on current employees?
- Is the proposed competitive bidding contract legal? Do other obstacles exist that need to be removed?

3. Develop a **complete** financial analysis of the proposal. Two issues must be resolved.

First, indirect costs such as pensions, employee benefits, maintenance and depreciation, construction, interest, etc. must be added with direct expenses when calculating the total cost of running a particular program or operation. As Hamilton County, Tennessee, discovered when trying to compare costs of operating their prison using public employees versus contracting with a private firm, it is very difficult to determine actual operating costs. In government work, many expenses for one operation can be found on the books of other agencies.

Additionally, since private firms are not exempt from paying taxes, new or increased revenue will be generated from contracting out a service (i.e. sales taxes, property taxes, B&O taxes, user and license fees).

4. Educate the public and build coalitions for support.

5. Build bridges with public employee unions by developing an incentive program. Resistance from the public employees and the pressure they exert on lawmakers is one of the main reasons many privatization or competitive bidding attempts have been unsuccessful. Contracts can stipulate that private firms, if selected in the bidding process, must give government employees first consideration when hiring. Since private firms need experienced workers in order to succeed, they are generally willing to do this. Consider employee buyouts, one-time bonuses, and other incentive options. Keep in mind, overall public employee job loss will be minimized through attrition.

An example of how this works is Indianapolis, where the workforce has been substantially reduced, primarily through attrition. Mayor Goldsmith says, "...there is the notion that competitive bidding is all anti-union and the unions will oppose it. There is great union anxiety because there is a change in the status quo. But if the union believes the future economic health of the city is important to its long-term success, and if the public manager understands that the middle manager is more of a problem than the unions themselves; and if they understand you can create value by layering, and downsizing the control mechanism of government, I really believe you can create an environment where the unions can be players in this process. We are down 30 percent in two and one-half years yet few union workers have lost their jobs. So this does not have to be an anti-union activity."²²

6. Implement the program retaining full policy control. Be careful to follow successful models in researching potential, determining costs, writing contracts, and monitoring contracts.

Crucial to success is obtaining support from leadership strong enough to withstand the initial union opposition. Having said that, treat the union as a partner in the competitive bidding process.

SUCCESS STORIES

Before launching into a new endeavor, it's always easier if someone else has blazed something resembling a trail. A wise person learns from *watching* the mistakes and successes of others.

Several states and many large cities have employed privatization and competitive bidding as tools to help them reduce costs while increasing effectiveness. Even the federal government has gotten into the act. We have included one of their stories.

Bangor Naval Submarine Base

Some of the Evergreen Freedom Foundation staff took a personal tour of the Johnson Controls operation at Bangor Naval Submarine Base in 1995. We came away from the meeting feeling that our tax dollars were being spent very efficiently and economically at Bangor.

Two of Bangor's largest and most controllable costs (as with most sizable organizations) are maintenance and facility operations. To help reduce overhead, the Navy at Bangor implemented what they call "outsourcing" (competitive bidding) and hired a well-known company called Johnson Controls to provide maintenance and operations.

Outsourcing evolves from the practice of subcontracting. It is the ability to integrate all aspects of facility management, including staff and management, usually at a lower cost and with higher quality than otherwise would be achieved.

Outsourcing allows an organization to focus its energy on its *primary duties* with disregard for more routine matters. The reduced costs and higher standards generally accompanying outsourcing saves money for taxpayers as well.

Outsourcing allows an organization to focus its energy on its primary duties with disregard for more routine matters.

The primary duty of the Naval Submarine Base at Bangor is to maintain U.S. submarines. The primary duty of Johnson Controls is to relieve the Navy of cumbersome duties that do not directly benefit the defense of our nation. These duties include the management of engineering services, railroad locomotives, transportation services, and custodial services. It also contracted for the maintenance of vehicles, heavy equipment, motor-generators, alarm systems, and pavement and grounds. In addition, it provides machinery and fabrications; ships, food and mail services; pest control; refuse collection; family housing maintenance; fire protection; and other services as needed.

The goal at Johnson Controls is to satisfy the Navy with higher quality at lower costs, and ultimately to renew its contract each year. Contracted services go out for bid for each year. The Navy awards contracts to firms providing the “best value,” not necessarily the lowest bid. Once a contract has been awarded, an annual option exists to extend services another year.

An indispensable element of the Bangor success story is the *performance-based* nature of their contracting. Johnson Controls essentially bids at cost and only makes a profit if its duties merit a performance bonus. No longer is Johnson Controls entitled to a profit regardless of the quality of its performance.

The Government is still realizing the benefits of the competitive nature of this contract. In a recent 10-year contract awarded for FY98-FY07, Johnson Controls’ bid price included reductions of nearly \$2 million a year over past contracts, saving the government over \$19 million in ten years. In addition, Johnson Controls’ price included reductions in each of the option periods to account for anticipated efficiencies which had not yet been identified. These reductions were priced at 5-man-years per year, or more than \$10 million over the ten-year contract. Thus, even though the contract was already held by Johnson Controls, the competitive pressures asserted by having to compete in a market have resulted in savings to the government of nearly \$30 million on this ten-year contract alone.²³

Since more of the Navy’s work today requires tighter specifications and higher risks, outsourcing has become even more beneficial. Johnson Controls attributes its success, in part, to its ability to utilize industry experts. These experts are employed at a central location and look after similar Johnson Controls operations. An innovation at one location is recognized and considered at other locations.

An additional benefit has been improvements made on-site and paid for by Johnson Controls. For example, the boiler hatches at the steam plant at Bangor were modified at the expense of Johnson Controls to significantly reduce its maintenance costs. Johnson Controls ultimately benefits by having lower costs and the Navy benefitted from an upgrade they didn't pay for. This achievement would likely have been lost had marketplace incentives been absent.

The bottom line for the Navy is a better run Naval Base. For the taxpayer, less money is spent for increased, higher quality services.

State of Virginia

Virginia is the first state to contract with a private laboratory to analyze DNA collected from blood samples. The \$9 million, three-year contract was awarded to Bode Technology Group, based in Northern Virginia.

Bode Technology uses a new testing process which allows profiling on much smaller pieces of DNA. Using this new technique, Virginia's pre-privatization backlog of 200,000 samples waiting to be analyzed is estimated to be eliminated within three years.

Though the cost of this privatization was substantial, the ultimate savings cannot be calculated. As many crimes had been solved during just the first 10 months of the privatization as had been solved during the state program's first five years. "The head of the Division of Forensic Science is quoted as saying that 'if you prevent future crimes, that saves countless dollars to law enforcement.'"²⁴

State of Pennsylvania

Pennsylvania recently contracted with a Pittsburgh firm called FreeMarkets to help it save money in purchasing goods for the commonwealth. The state regularly places bids out for the purchase of paint for roads and highways, aluminum for license plates, and numerous other goods. Using FreeMarkets' software and services, the state may place up to \$20 million worth of bids out for contract. FreeMarkets actively seeks out and makes cold calls to suppliers they think might be interested in bidding.

The state will pay the firm \$225,000 for this service, and hopes this new system will generate competition that results in 15-18% savings. In the first day alone, a new aluminum supplier was found, which saved the state 10% or \$220,000.

FreeMarket's chief executive, Glen Meakem, believes that similar possibilities exist throughout Pennsylvania's counties and local governments.²⁵

San Diego County, California

County Administrators in San Diego County have decided to use a managed competition process for services put out for bid, allowing the in-house units to bid for contracts against the private sector.

Two service competitions were held in 1998. The fleet maintenance contract, a nearly four-year contract, was won by the in-house unit, which bid \$1.4 million lower than the lowest private bidder. This cut costs by 14 percent of \$1 million per year. A private bidder won the county's competition to provide alternate public defender and dependency services, cutting costs by \$235,000 per year.

County Administrators are evaluating other possible competitions such as the county's information technology service, county workers' compensation agency, correctional health services, road maintenance, and revenue and recovery services. Currently, San Diego County is saving nearly \$17 million per year and experiencing more competitive and improved county services.²⁶

City of Indianapolis, Indiana

Like state governments, most municipalities in America, are faced with rising costs, frayed infrastructures, ongoing and costly negotiations with major employee unions, unfunded federal mandates, and increasing unwillingness on the part of taxpayers to keep footing the bill.

A brief glimpse at how this big city helped solve its problems through competitive bidding of services may be very instructive.

“We have to find ways to produce more value for our citizens with new methods. The old structures won't work...a 21st century city has to be a city with new governance. A key component of new governance has to be competition or privatization if you want to be successful.”²⁷

So stated Stephen Goldsmith, Mayor of Indianapolis, a forerunner in implementing widespread competitive bidding to deliver public services.

Believing that the marketplace is a better place to deliver goods and services, Goldsmith initiated a far-reaching effort to allow private sector companies to compete against government workers to provide services and manage city assets.

Mayor Goldsmith carefully distinguishes his competitive bidding efforts from privatization endeavors. While Goldsmith believes the private sector should provide services outside the scope of government's core functions, he supports the ability of government workers to compete with the private sector in delivering the core municipal functions.

“[A] monopoly is inefficient by definition,” says Goldsmith. “The market is a better referee for value and money than I am.”²⁸

More than 60 services have been put up for competitive bid saving residents \$450 million. ...At the same time, Indianapolis added more private-sector jobs than ever before – nearly 47,000.

“When we increase taxes dramatically, accumulate wealth, and with that wealth have only public ownership of assets and say only public employees can produce these services, then we are essentially saying that in that in these areas, socialism – or at least government ownership of assets – is better than capitalism. We believe otherwise.”²⁹

Indianapolis' competitive bidding process has resulted in reduced costs and better service for the residents. More than 60 services have been put up for competitive bid saving residents \$450 million.³⁰ The budget is balanced and reduced by \$10 million, the non-public safety work force has been reduced by one third, and 100 more officers are on the streets; all the while undertaking the largest infrastructure improvement in the city's history. *All of this was accomplished without raising taxes.*

At the same time, Indianapolis added more private-sector jobs than ever before – nearly 47,000.³¹

Goldsmith notes that private companies are generally more efficient, innovative and customer-oriented than government. He points out that while the private sector scrambles to nurture a satisfied customer base by providing quality products at competitive prices, government becomes less responsive and more expensive. Because the private sector faces stiff competition, firms will go out of business if customers don't like the goods and services they offer.

Government, on the other hand, has tied up the delivery of a wide range of services and the management of assets. This creates a situation worse than a monopoly since government cannot go out of business – at least not without the unthinkable happening.

And this begins Goldsmith's description of the fundamental concepts behind the need for competitive bidding. We quote his comments as follows:³²

Government Cannot Go Out of Business.

“Every citizen of the U.S., like it or not, is a customer for government services – and a new customer is born every eight seconds. Poorer Americans, especially, are customers for government services and cannot afford to go elsewhere.”

Government Controls Revenue.

“If more money is needed to provide a given service, government can and will raise taxes to pay for it. While the private sector has to persuade people to make purchases, government simply takes dollars. General Motors would never close a plant if it could seize the assets of people who do not buy its cars.”

Government Is Allowed To Spend More Than It Takes In.

“While some states and cities are required by law to enact balanced budgets, most government entities are not – including the federal government. And even governments that by law must balance their budgets nevertheless avoid doing so by borrowing, deferring capital spending, and employing bookkeeping devices. Private companies, and families, can only deficit spend in the short-term before going bankrupt or out of business; government thinks it can go into debt indefinitely.”

Government Delivers ‘Essential Services.’

“Whenever reform-minded managers or elected officials exert pressure to reduce costs, status-quo managers can mount an effective defense by pointing to the essential nature of their task. A call for budget cuts in a municipal Department of Public Safety, for example, might be met with a cry that streets will be less safe. Attempting to slow the growth of education spending might be met with such a challenge as, ‘Aren't our kids worth a few extra dollars a month?’ This is a strategy that resonates

powerfully with the people, who do not have the time nor the inclination to scour budgets to see if savings are possible without cuts in service quality.”

The unions, who once wanted to meet Goldsmith at high noon, have expressed approval of his reforms. This is due to the fact that, while he cut hundreds of mid-management positions, not one union worker lost a job due to lay offs. Recently, the union agreed to give back a 10 percent raise over four years in exchange for a 20 profit share on all reductions in the budget.

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Goldsmith’s constant references to the strength of competition in enabling cities to efficiently deliver essential services while trimming their budgets resonates by example in his city. He underscores the fact that competition does not necessarily mean privatization.

To determine whether competition is sensible in given service areas, Goldsmith’s team executes what it calls the “core service” analysis. Core services (like police protection) are separated from those that are secondary (like microfilming). Indianapolis’ policy is that competition is sensible when the service is not part of government’s core mission.

If competition is deemed desirable, the administration performs the “Yellow Pages test.” Goldsmith says, “If the city Yellow Pages show several firms now provide services that the City is also providing, then competition is possible. The presence of private service providers also indicates that the market has established performance standards that can be written into contracts.”³³

“The Department of Public Works (DPW) exemplifies the inventive spirit that pervades City departments because of these initiatives. In older days customer requests at DPW would sit around for a long time before action was taken on them. DPW now has a rapid response team associated with its customer service center. The team puts three workers on a job rather than the usual four. Their jobs no longer use two trucks, one to put up the barricades and one to do the work. Instead the crew has reconfigured the work truck so that it can take the barricades with them. The crew can now do jobs in one or two days that used to be in the service files for years. They speak the language of competitiveness and are rightfully excited about what they have accomplished.”³⁴

Numerous government reorganization success stories can be found in Indianapolis. More information can be found in the book *The Indianapolis Experience: A Small Government Prescription for Big City Problems*.³⁵

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