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INSTITUTE FOR PUBLIC POLICY

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*Campaign Briefing Series 2003*

**Making Privatization Work  
for State Government**

By: Adrian Moore  
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Reason Foundation

September 2003

## Thomas Jefferson Institute for Public Policy

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## **Foreword**

Adrian Moore is one of the leading experts in our country on making governments more efficient and less burdensome on our taxpayers. He is recognized as a person who is a reasoned and sensible advocate of government doing what government does best and for the private sector to help government accomplish its mission by helping where possible. Sometimes this means privatization and sometimes this can mean public private partnerships.

A year ago, the American Legislative Exchange Council (ALEC), a non-partisan group of over 4,000 state legislators in the United States, published a short and concise article by Adrian Moore that outlined ways state governments can make privatization work best for the taxpayers. He also outlined why privatization sometimes fails. This article is reprinted by the Thomas Jefferson Institute as part of its Campaign 2003 Briefing Series.

The ideas brought forward by Adrian Moore are particularly important to our opinion leaders here in Virginia, both elected and non-elected, as our state begins the bi-annual effort to craft a state budget. And tax reform efforts will begin as well very shortly.

Working to make government more efficient, accomplishing public policy goals by bringing the private sector into the mix as a full partner, should keep government budgets contained by reducing the cost of government services and programs. And this should be the goal of all our elected officials and our opinion leaders in the private and non-profit sectors of our society.

The ideas brought forward in this paper do not necessarily reflect the opinions of the Thomas Jefferson Institute for Public Policy or its Board of Directors. Nothing in this paper is meant to influence pending legislation in the General Assembly.

Michael W. Thompson, Chairman and President  
Thomas Jefferson Institute for Public Policy  
September 2003



## **Executive Summary**

Privatization is a bi-partisan effort to cut costs and improve government services.

Usually privatizing government services is done to save money and avoid raising taxes.

Today, efforts at privatization are aimed at cost savings as well as providing:

- Quality services to government
- Flexibility in the use of resources for the government
- Speed of completing projects needed by the government
- Access to expertise not available inside the government
- Innovation in the private sector available to government

President George W. Bush hopes to have federal agencies and private companies compete to perform work currently being done by over 400,000 government workers.

Privatization efforts don't always succeed.

Failure tends to occur when government provides no incentive to pursue privatization.

Effective leadership by government managers is key to avoiding failure.

Virginia's Commonwealth Competition Council is the nation's leading model of a government agency with the mission to make government work better through privatization and competition.

A well-designed, well-run privatization agency can be a valuable asset to state government. To be successful these agencies need to:

- Build a constituency within the elected leadership
- Build the right Mission and objectives to stay focused.
- Staff needs the skills to research and manage, identify privatization opportunities and potential contractors, compare costs and outcome, etc.

Although cost savings is the budget driver for privatization in many cases, it is the avenue to also improve the quality of government services.



# **Making Privatization Work for State Government**

By Adrian T. Moore  
Vice President of Research, Reason Foundation.

Privatization—the transfer of responsibility for services or assets from the government to private firms—in the United States is changing. Long thought of as strictly a conservative idea, privatization has gone bipartisan as key state and local democratic leaders have embraced it as a means of cutting costs and improving services.

Privatization as we know it began in the late 1960s and was mainly practiced by local governments. In the 1980s, Ronald Reagan brought the idea of privatization to the federal government at the same time Margaret Thatcher was revolutionizing Britain via privatization. Here in the United States we have traditionally privatized services for the money; tight fiscal times often convince governments to cut costs to avoid raising taxes, and privatization is one way to accomplish this.

And times have been tight for over a year now—almost half of the states and more than half of cities are facing revenue shortfalls. A good example of privatization driven by fiscal concerns can be seen in Florida, where for the past two years Gov. Jeb Bush has been pushing for state agencies to use privatization to reduce their budgets by at least 5 percent.

It's not just Florida. Reason Foundation just released its 16<sup>th</sup> annual report on trends and practices in privatization in the United States.<sup>1</sup> From new highways to welfare-to-work programs, state agencies have ramped up their use of privatization over the past year as a means of balancing tighter budgets and increasing service demands.

## **Shifting Motivations for Privatization**

Cost savings is still very important, but recent years have also seen the start of dramatic shifts in why and how governments are privatizing. More and more often, privatization is driven by a desire for cost savings linked to other factors such as:

- **Quality.** Cities contract water and sewer utilities with private firms that can achieve compliance with environmental standards;
- **Flexibility.** States privatize the design and construction of new roads to avoid having idle architects and engineers sitting around on the public payroll for years between projects;
- **Speed.** Privatized construction of buildings and other facilities takes half as long as government-run construction projects, and private firms can set up new databases or information technology systems and deliver services much faster than government agencies;

- Access to expertise. The people with the most experience and highest technical skills can make a lot more money in the private sector than in government, so when governments need those kinds of skills, often the only way is by private contracting.
- Innovation. Competitive private firms have greater freedom to innovate and more incentive to do so than government agencies. Privatization takes advantage of innovations in everything from helping foster children find permanent homes more quickly to designing more efficient prisons.

All of these motives can be rolled together simply as “performance.” Privatizing to achieve a combination of cost savings, quality, innovation, speed, expertise and innovation is privatizing to achieve higher performance.

This is most obvious in cases like the controversial privatization by Pennsylvania this spring of Philadelphia’s worst-performing schools. After years, if not decades, of trying to turn the schools around themselves, the city is privatizing to improve performance, including all the kinds of changes discussed above.

Less widely known, is Pres. George W. Bush’s ambitious goal to have both federal agencies and private firms compete over the next few years to perform work currently being done by more than 400,000 federal workers. This goal is part of the President’s Management Agenda and is rooted in the recognition that improved performance is more a result of competition itself than it is of who—private firms or government—ultimately does the work.<sup>ii</sup> In the Bush plan, competition will induce various units within government agencies to find ways to improve their performance, and will lead to contracts for the private firms only if they can deliver better performance than the government can.

**Where the Action Is:  
Some Oft-privatized State Services**

- ✓ Highway Design
- ✓ Highway Maintenance
- ✓ Engineering Services
- ✓ Information Technology
- ✓ Custodial Services
- ✓ Mental Health Services
- ✓ Welfare-to-work Programs
- ✓ Child Care
- ✓ Adoption Programs
- ✓ Juvenile Rehabilitation
- ✓ Correctional Medical Services
- ✓ Prison Operations
- ✓ Building Repair and Maintenance
- ✓ Environmental Lab Analysis
- ✓ Marina Management
- ✓ Golf Courses

*Source: Council of State Governments and Reason Foundation.*

**Strategies for Success**

A common failing of privatization efforts is that state agencies have little incentive to pursue privatization and they have little experience and real knowledge of it. Hence agency privatization efforts are often piecemeal and haphazard, and fail to learn from other state agencies’ relevant good and bad experiences. Even the most ardent fans of privatization will



admit that sometimes it goes bad or fails to deliver on its promises. It's no silver bullet, but when done right, privatization is overwhelmingly successful and is rarely reversed.

The first key to avoiding those pitfalls is for the legislature and/or administration to take a decisive leadership role and form a coherent and consistent approach to privatization.<sup>iii</sup> One strategy in particular that can be effective is creating a competition or privatization commission. Ideally a privatization commission brings together a group of stakeholders or others to examine privatization opportunities, create strategies for implementation, and advise the legislature and executive agencies on privatization best practices. Virginia's Commonwealth Competition Council has been the nation's leading model for some years. It produces top-notch research and assistance to state agencies, and analysis to the legislature, and its legacy is cost savings in the hundreds of millions of dollars.<sup>iv</sup>

The success of commissions also depends on proper implementation. Poorly designed commissions can be hogtied by unrealistic mandates or lack of authority, and poorly led commissions can bog down in interest group squabbling. A more common failing is lack of follow-through by legislative or administrative leaders. In 1997 Colorado created a privatization commission that did an excellent job of research, identifying opportunities for privatization statewide. More importantly, it developed a set of processes that agencies could adopt, compiled a useful guide to best practices, and drafted model legislation to address a few key issues and barriers it uncovered.<sup>v</sup> Unfortunately the legislature never picked up the ball. There was no serious consideration of the legislation the commission recommended, nor any incentive for agencies to follow through.

Though free-market conservatives and libertarians are generally no fans of creating new government bodies or bureaucracies, some evidence suggests that a well-designed, well-run privatization commission can be a valuable asset to state government and taxpayers, and is one of the more politically viable foundations for broader privatization efforts. Successful privatization efforts require political capital, knowledge, analysis, incentives, and follow-through—disparate elements that a privatization commission can help bring together.

The real secret to privatization commissions is building constituencies for reform, setting obtainable objectives, and hiring commission staff with a specialized understanding of the activities the state would like to privatize or competitively outsource.

1. **Build a constituency.** Effective commissions have wide authority to gather and disseminate information and don't get overly bogged down in battles to keep their appropriations. More important, the commission's recommendations have to be translated into legislative or executive actions as appropriate, which will not happen without committed support from elected officials willing to spend some political capital on the commission. That means not only developing a formal or informal group of elected officials to work the commission, but also making the effort to get other groups—chamber of commerce, labor unions, taxpayer groups, academics, etc.—involved in participating with, if not always agreeing with, the commission.

2. **Build the Right Mission and Objectives.** A commission charged with simply identifying privatization opportunities, or with studying the potential for privatization in state agencies, is not likely to accomplish much. Nor is any legislature likely to give a commission power to compel agencies to privatize. The right mission and objective for a privatization commission is to help find better and less costly ways to provide government services. That means at a minimum: identifying privatization opportunities, evaluating structural and other barriers to change and ways to overcome them, advising elected officials on management and reform strategies, building tools and processes that agencies can use to implement privatization, keeping on top of best practices in privatization from around the nation, helping agencies with research and implementation issues, and being proactive in anticipating emerging issues that should be addressed.
  
3. **Include the Right Skills.** A successful commission needs the right skills to manage a complex mission and objectives. Staff must have good research and management skills, understand how to identify privatization opportunities and potential contractors, know how privatization is conducted (requests for proposals, cost comparisons, contract administration, etc.), be well-versed in employee transition issues, understand asset management and accounting, know state procurement and acquisition law, and so on. The bottom line is that skills have to match the mission and objectives.

## **The Bottom Line**

Even if budget pressure and cost savings are what puts privatization on the legislative table, state leaders with foresight will look for privatization and competition to also improve the quality of services. That requires leadership, and understanding of strategies with a track record of success, and a willingness to create the institutions that will provide the right incentives, accountability, and transparency for privatization efforts.

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<sup>i</sup> Geoff Segal, editor, *Privatization 2002* (Los Angeles: Reason Foundation, 2002), [www.rppi.org/apr2002.pdf](http://www.rppi.org/apr2002.pdf).

<sup>ii</sup> Executive Office of the President, *The President's Management Agenda* (Washington, D.C.: Office of Management and Budget, 2001) [www.whitehouse.gov/omb/budget/fy2002/mgmt.pdf](http://www.whitehouse.gov/omb/budget/fy2002/mgmt.pdf)

<sup>iii</sup> William D. Eggers, *Designing a Comprehensive State-level Privatization Program*, Reason Foundation How-to Guide No.1, (Los Angeles: Reason Foundation, 1993).

<sup>iv</sup> Visit the Commonwealth Competition Council at [www.vipnet.org/cc/home.htm](http://www.vipnet.org/cc/home.htm)

<sup>v</sup> You can see their report at [www.state.co.us/gov\\_dir/gss/edo/priv/privtext.htm](http://www.state.co.us/gov_dir/gss/edo/priv/privtext.htm)

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(\*Mrs. Bowen is on a leave of absence during her tenure with Governor Warner.)



*“... a wise and frugal government, which shall restrain men from injuring one another, shall leave them otherwise free to regulate their own pursuits of industry and improvement, and shall not take from the mouth of labor the bread it has earned. This is the sum of good government, and this is necessary to close the circle of our felicities.”*

*Thomas Jefferson*

*1801*

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