MEMO 2019

PROTECTING THE COMMON GOOD IN PUBLIC SERVICES

As local and state policymakers look for ways to balance their government budgets, some consider privatization of important public services as a way to save money. But, as shown repeatedly in many localities, privatization is not a cure for financial woes. Privatization can actually increase costs for a city, compromise the quality of critical services relied on by residents, and harm the local community and economy. Policymakers may also lose the ability to ensure accountability and exercise critical oversight over public services . Privatization can also outsource responsibilities traditionally performed by government that can have long-lasting negative consequences for residents and undermine the very idea of the common good.

There are many different public services, and while the specifics around provision of each service vary, there are common issues that frequently arise in these types of government contracts, which this brief will discuss below. While this is not an exhaustive list, localities and state may be faced with privatization proposals for public services such as:

- City services, such as landscaping of public land, snow removal, fleet management, custodial services for public buildings, waste and recycling collection, emergency services, and building inspection services. These services may appear routine, yet they are critical to the functioning of a city, and handing over control of these services to private contractors can impact daily life for residents and even endanger public health. For example, across the country, waste contractors have overcharged residents[1], mismanaged recycling programs[2], and failed to pick up trash on time.[3]

- Information technology functions and/or programs. For example, in May 2019, Kansas terminated a $110 million, no bid contract for IT services. The company failed to meet key deadlines in the development of a new tax collection system, forcing the state to use the old system to process tax returns. The state decided to bring IT operations back in-house to be performed by state employees.[4]

- Health and human service programs, including the actual provision of the service itself, or in some cases, the management of the service, service eligibility determination, or functions that related to client and case management. For example, some states have experimented with privatization of their state Medicaid program, allowing large insurance companies to administer the program to detrimental results, including recipients not getting critical medical care in a timely manner.[5] Some localities and states have also privatized parts of their child welfare system, which can have life or death consequences for vulnerable children.[6]

- Functions related to the criminal justice system, including operations at jail or prison facilities, or privatization of services within such facilities, such as health care, food service, communications, commissary, and more. Privatization of prison and jail operations have resulted in increased violence within facilities, documented human rights abuses, and the perpetuation of mass incarceration.[7] Furthermore, companies that provide services within facilities often cut corners in an effort to reduce operating costs, resulting in lower quality food, inadequate medical care, and other compromised services. More information about this dynamic is available in In the Public Interest's report, *Cutting Corners in America's Criminal Justice System: How Corrections Companies Harm Prisoners and the Public in Pursuit of Profit* available at https://www.inthepublicinterest.org/wp-content/uploads/ITPI_CuttingCorners_Corrections_April2016.pdf

- School support services, including transportation, custodial, and food service. Cost savings often fail to materialize in school support service privatization efforts, and many contractors degrade the associated jobs, paying employees less than what the public school district previously paid these positions.[8]

RISKS OF PRIVATIZING PUBLIC SERVICES

Little or no cost savings. Unlike public agencies, private companies must ensure that they receive a premium over the amount it actually costs to do the job in order to guarantee profit.[9] Often, this means that privatization is more expensive than cities originally plan. Cost savings may fail to materialize or reach levels promised by the contracted private entity. A private company may overestimate cost savings in an attempt to win a contract. Cost overruns and change orders may occur, driving up the cost to the locality. According to a 2012 survey by the International City/County Management Association, 53% of governments that brought services back in-house reported that the primary reason was insufficient cost savings.[10]

Research shows that even in cases where nominal savings are found, these savings are usually offset by the "substantial agency costs associated with the contracting process, including the expense of preparing plans and specifications to a greater level of detail, the cost of advertising and processing bids, and the cost of monitoring, inspecting, and conflict resolution."[11] Numerous studies, including academic research and research from the Government Finance Officers Association, show that the cost of contract administration is typically around 20% of the price of the contract.[12]

Reduced service quality. Because a private entity's primary concern is maximizing profits, there are inherent pressures to cut corners, such as paying employees less, employing fewer workers, union busting or avoiding unionization in the first place, using inferior materials, or making programmatic decisions that run counter to the public interest, resulting in diminished quality.

A broad range of research shows that public services do not improve after being contracted out.[13] Many local public services are complex and the quality of the service is difficult to measure in a contract. For example, street maintenance staff must be ready on short notice when severe weather hits to be able to anticipate where emergencies are likely to occur and which roads may need to be cleared to ensure the safety of drivers. Public workers are able to respond quickly to emergencies, but these activities are difficult to define, measure, and evaluate within the limits of a contract. Additionally, companies must provide services for multiple municipalities, further limiting the company's flexibility for any single city. In the 2012 survey by the International City/County Management Association mentioned above, the second most cited reason for bringing services back in-house was unsatisfactory service quality with 51% of governments that insourced services reporting that reason.[14]

For example, the Chicago School Board signed three-year contracts with Aramark and SodexoMagic to clean the city's schools. By privatizing janitorial services, the district hoped to save up to $40 million over the contract period.[15] The companies reduced costs by cutting corners on staffing. Shortly after the start of the following school year, Aramark laid off 290 janitors.[16] The schools became plagued with problems stemming from the lay-offs, including filthy classrooms, spilled milk left uncleaned, and overflowing garbage cans sometimes not emptied for weeks. Cockroaches, mice, and bugs, which were attracted to the trash, overran the buildings, and a number of schools called exterminators.[17]

Loss of middle-class jobs. One way for private companies to increase their profit margin on service contracts is to reduce their operating costs. A common way to do this is to change formerly-public sector jobs that sustained families and included healthcare and retirement benefits to low-wage jobs without benefits, most of which are no longer unionized, when transferred to the private sector.[18] African Americans are particularly impacted by this dynamic, as approximately one in five black workers hold jobs in government.[19] Moreover, median wages earned by African American employees are significantly higher in the public sector than in other industries.[20] Due to their prevalence in public sector jobs, African American workers are more likely to be affected when jobs are outsourced to companies that pay reduced wages and benefits, potentially losing stable footing in the American middle class, which can have long-lasting impacts for future generations.

Loss of accountability and transparency. Localities can lose access to routine information about the service under a privatization scheme. The privatized service may not be subject to open records laws, taking away the public's access to key information they would otherwise have if the service were still being performed by the public sector. Governmental entities may not even have the information they need to adequately hold the contractor accountable for performance.

Lack of adequate monitoring and oversight. Research shows that contract monitoring is difficult and costly.[21] Many local and state governments do not have any formal procedures for monitoring contracts.[22] Additionally, a contracting agency should have a sufficient number of skilled staff to properly oversee private contractors. Yet contract oversight funds are often one of the first items cut from the budget during a shortfall.[23] As a result, agencies often don't have the experienced staff that is necessary to properly oversee contracts. The public ultimately loses as inadequate oversight paves the way for cost overruns, missed deadlines, and serious mistakes in service provision. For more information about contract oversight and management, see In the Public Interest's publication, *Standing Guard: How Unaccountable Contracting Fails Governments and Taxpayers at https://www.inthepublicinterest.org/wp-content/uploads/Standing-Guard_web.f.pdf*

Money leaves the community. When a city privatizes a vital government service and replaces public servants with a private company, large amounts of money leave the local economy. Public employees typically live and spend money in the communities in which they work. When a city privatizes the service, much of this money flows out of the community, as private companies that may not be located in that city, state, or even country take profits away from the municipality. Additionally, the dynamic of reducing worker wages and benefits through privatization discussed above has real consequences for local economies. Research by Daphne Greenwood, an economist at the University of Colorado, shows how declines in workers' wages mean less money to spend in their communities and directly affect local businesses.[24] Lower wages mean that workers spend less in local retail, restaurants, and other establishments. Lower wages also mean that local and state governments collect less in sales, income, property, and other types of taxes.[25] In short, less money flows into the local economy and more money is routed to for-profit corporations, their CEOs, and their shareholders.

Furthermore, workers may be forced to move out of the community to less expensive areas as a result of lower wages. Greenwood's research shows that in a medium-sized American city, dollars spent in the local economy fall from 49% of total payroll to 9.5%, or less when workers live elsewhere. Lower spending in the local economy can have a range of significant negative impacts on tax revenues, the housing market, and local businesses. And when contractors move operation of a public service (such as a call center) to another city, state, or country, the community then loses all the dollars workers used to spend locally.[26]

QUESTIONS TO ASK

When confronted with a proposal to privatize a public service, asking the right questions can help frame the conversation and bring out the potential risks and harmful impacts of these types of contracts. While not an exhaustive list, the below set of questions can be used as a starting point in this type of inquiry.

UNDERSTANDING THE SERVICE

Examining Options

- Has the government performed a thorough analysis of the current system(s) to understand problems and/or inefficiencies and determined alternative options that could address these issues? A thorough analysis of the current system will also allow for a more accurate cost comparison between various proposals later in the contracting process.

Impact on Current Workforce

- What will be the potential impacts on the existing workforce?

- Are the existing workers currently unionized and does the Collective Bargaining Agreement or government policy contain clauses that require workforce retention, retraining, or labor peace?

- How will the wages and benefits and the number of jobs change once control is shifted to the private sector?

- Will existing employees be moved to other jobs within the government and/or can they continue to perform the same work for the contractor?

COSTS TO THE GOVERNMENT AND THE PUBLIC

- Has the government performed a cost-benefit analysis?

- If so, does the cost analysis include the full costs of contracting, such as costs associated with holding hearings, drafting bid documents, analyzing proposals, monitoring the contract, training private contractor staff, moving equipment, the contractor using public resources, and possibly engaging in litigation arising from contractor failures or procurement problems?

- Is there documentation by the government that privatizing the service will produce a cost savings?

- Are there public fees associated with the service? If so, how will transferring the program to a contractor affect fees? For example, a public park that was once free to the public, may require public entrance fees once a private contractor takes over management functions.

IMPACT ON CONSTITUENCIES

- If the service in question is designed to serve a specific constituency, is there an advisory group or other forum with appropriate stakeholders that can provide the agency input regarding the potential effect that contracting may have on that constituency?

- Does the contract protect these constituencies or recipients? Does it address issues related to civil rights, ADA, limited English proficiency, etc.?

- Is there a process through which a member of the constituency or recipient can complain about the services provided by the contractor or appeal a decision made by a contractor?

- Will the private contractor be privy to sensitive or confidential information about the public or constituents? If so, are there mechanisms in place to prevent the mismanagement of sensitive information?

ENSURING A FAIR AND ACCOUNTABLE PROCESS

Transparency

- What rights does the public have to see documents related to the contract, especially through online disclosure?

- What type of information is available to the public during the contracting process and after the contract is signed?

- Are there adequate and meaningful forums for public input, such as public hearings or public comment periods?

- Do legislative or other oversight bodies have access to the information they need to effectively evaluate the contract?

Potential Conflicts of Interest

- Is the agency using a consultant or other advisory firm to advise them on any decisions related to the contracting process? If so, how are these contracts with consultants and other advisory firms structured? Do they collect fees for services rendered, or are they incentivized based on certain outcomes in the contracting process?

- Do any consultants related to the contract have conflicts of interest? What is their track record and background with these types of contracts?

- Are any public officials or evaluators involved in the contracting process former employees of potential contractors?

Government Capacity of Expertise

- Does the locality or state have the necessary experienced staff to negotiate a good deal?

- How many employees will the government allocate for contract oversight and monitoring responsibilities? Is this adequate staff for the agency to design the contract, monitor performance, and provide technical assistance to the contractor for the life of the contract?

- Will contracting out the service lead to a significant loss of institutional knowledge and/or experience related to the specific service within the agency? How will that impact the long-term mission and/or public purpose of the agency?

- Will the agency retain sufficient internal capacity to provide the service in the case of contract failure?

TERMS OF THE CONTRACT

Contract Requirements and Structure

- Is the length of the contract reasonable? The contract term should be short to allow for timely reevaluation of the contract.

- What are the criteria for activating contract renewal clauses? Beware of evergreen clauses, which allow a contract to be automatically renewed without agency review or oversight.

- How is the contract structured? Does it contain financial incentives for the contractor that may undermine the public interest?

- Does the contract clearly and effectively delineate between public and private contractor roles related to the service? Some aspects of a service may be required to be carried out by public employees, per state or federal law.

- What are the requirements for subcontracting? Does the RFP and contract clarify that subcontractors will have to meet the same requirements as the main contractor?

Accountability Provisions

- How does the contract measure success? Is there clear consensus among stakeholders and the agency regarding desired results? Does the contract contain clear performance measures and accountability mechanisms to ensure that the contractor is producing the desired results?

- Does the contract require regular independent oversight, such as audits performed by a local or state audit authority, per a specified timeline?

Planning for Problems

- Does the RFP and contract require a start-up/transition plan from the contractor that includes a contingency plan for problems at start-up or later in the contract?

- Does the agency have a contingency plan for dealing with problems and/or non-performance by the contractor?

- Can the contract be cancelled if problems arise in service provision or if the public needs change? If so, what are the criteria for cancellation and what are the agency's liabilities (e.g., costs) for canceling?

NOTES

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