

BACKGROUND BRIEF • JUNE 21, 2011

## Privatization and Contracting Out of Municipal Services

**A**s local officials look for ways to balance their city's budgets, some are considering privatization of core municipal services as a way to save money. But, as the repeated experiences of many cities and local municipalities show, privatization is not a cure for financial woes. Privatization can increase costs for a city, give up democratic control, and compromise the quality of critical services that residents regularly rely on.

### AT A GLANCE

Privatization can increase costs for a city, give up democratic control, and compromise the quality of critical services that residents regularly rely on.

Even in this dismal economic climate, some cities are saying no to privatization. The city of Yuma, Arizona recently turned down bids from private contractors to take over vital government services, such as garbage collection, golf course operations, and fleet management. Public officials determined that the private companies' cost estimates were significantly more expensive than public provision of the services. Residents would have paid twice the amount in fees to a private company over what they currently pay to the city for the same service.<sup>1</sup>

This backgrounder brief will explore these and other common themes related to the privatization of municipal services, and provide examples of experiences from

<sup>1</sup> <http://www.yumasun.com/news/city-67409-wilkinson-private.html>

cities around the country that have considered or have privatized critical services. Specifically, this brief will examine privatization in the following areas: park maintenance, street maintenance, garbage collection, building inspection, information technology, printing services, and “contract cities.”

## What Research Shows

### **Local governments report insufficient cost savings from privatization.**

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.<sup>2</sup> Often, this means that privatization is often more expensive than cities originally planned. According to a 2007 survey by the International City/County Management Association, 52% of governments that brought services back in-house reported that the primary reason was insufficient cost savings.<sup>3</sup> 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.”<sup>4</sup> The Government Finance Officers Association estimates that these indirect costs, such as contract monitoring and administration, transition costs, and the contractor’s use of public equipment and facilities can add up to 25% to the price of a contract.<sup>5</sup>

### **Quality and responsiveness of municipal services decline following privatization efforts.**

A broad range of research shows that public services do not improve after being contracted out.<sup>6</sup> 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 a survey of more than 600 U.S. cities that had contracted out important municipal services, researchers found that over 88% brought at least one service back in-house. One of the main reasons that cities cited for cancelling or not renewing contracts was poor service quality.<sup>7</sup>

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<sup>2</sup> CUPE, “Costs and Consequences of Solid Waste Collection Alternatives in Peterborough,” April 2010.

<sup>3</sup> [http://icma.org/en/results/surveying/survey\\_research/whats\\_new](http://icma.org/en/results/surveying/survey_research/whats_new)

<sup>4</sup> Michael Ballard and Mildred Warner, “Taking the High Road: Local Government Restructuring and the Quest for Quality,” April 2000.

<sup>5</sup> AFSCME, “Government for Sale: An Examination of the Contracting Out of State and Local Government Services,” <http://www.afscme.org/publications/10040.cfm>

<sup>6</sup> Michael Ballard and Mildred Warner, “Taking the High Road: Local Government Restructuring and the Quest for Quality,” April 2000.

<sup>7</sup> CUPE, “Costs and Consequences of Solid Waste Collection Alternatives in Peterborough,” April 2010.

## **Monitoring and oversight of municipal contracting is typically inadequate.**

Research shows that contract monitoring is difficult and costly.<sup>8</sup> In an analysis of survey data from the International City/County Management Association, researchers found that over half of the governments that contracted out did not have any formal procedures for monitoring contracts.<sup>9</sup> When agencies are unable to adequately monitor contractors, costs increase and service quality greatly suffers.<sup>10</sup> In many privatization contracts, public monitoring staff is laid off. Rather than increasing capacity to monitor expanded contracts, local governments reduce contract management staffing. As a result, agencies 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.

## **Money leaves the community when a city privatizes.**

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 live and spend money in the communities in which they work. When a city privatizes, 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. When Davis, California considered privatizing its wastewater treatment plant, the city council recognized the damage that privatization would cause to the local economy. Often this issue is not taken into account when cities perform cost-benefit analyses of privatization, but it poses a serious risk to the community.<sup>11</sup> Additionally, many jobs that are privatized are degraded – our neighbor's wages are reduced and benefits are cut.<sup>12</sup> The local economic base further erodes when these good jobs are replaced with low-quality, low-paying jobs.<sup>13</sup>

## **What Local Communities' Experiences Show**

### **Park Maintenance**

City officials in Sacramento, California recently turned down proposals to privatize city park maintenance. They worried that privatization would significantly reduce service levels, and that residents would no longer receive timely responses to inquiries. Specifically, city staff reported that "privatization of basic park maintenance would continue to require city staff to provide contract management and inspection, and more specialized services including irrigation system oversight and emergency repair and oversight of park facilities such as playgrounds, tot lots, all-weather fields, sports courts, picnic and seating areas," therefore not actually reducing the city's

<sup>8</sup> Michael Ballard and Mildred Warner, "Taking the High Road: Local Government Restructuring and the Quest for Quality," April 2000.

<sup>9</sup> Michael Ballard and Mildred Warner, "Taking the High Road: Local Government Restructuring and the Quest for Quality," April 2000.

<sup>10</sup> Ibid.

<sup>11</sup> <http://cityofdavis.org/meetings/councilpackets/20110301/07%20Wastewater%20Treatment%20Plant%20Upgrade%20Update.pdf>

<sup>12</sup> Michael Ballard and Mildred Warner, "Taking the High Road: Local Government Restructuring and the Quest for Quality," April 2000.

<sup>13</sup> AFSCME, "Government for Sale: An Examination of the Contracting Out of State and Local Government Services," <http://www.afscme.org/publications/10040.cfm>

workload.<sup>14</sup> They ultimately decided against privatization after Sacramento officials concluded that privatization would result in much lower quality work than residents were used to.<sup>15</sup>

## Street Maintenance

When streets aren't properly maintained, the safety of residents is severely compromised. Fresno, California experienced significant problems with the privatized portions of the city's street maintenance work. When the city compared the public employees' work with the private contractor's work, they found the public staff to be superior in almost every way – they provided better quality, in a more time-efficient and cost-effective manner. The city noticed that the private contractors failed to properly maintain wheelchair ramps, curbs, and gutters. Median islands that were maintained by the private company were left overgrown, and actually became safety hazards for drivers. City workers had to work for more than three months to repair the city's irrigation system after contractors failed to adequately care for it.<sup>16</sup>

The city of Tulsa recently decided against privatizing their in-house street maintenance crews, concluding that the department's work is central to the safety of the city. A snowstorm in February 2011 made city officials question the recommendations of a KPMG study, which urged the city to privatize the maintenance department. The city street maintenance crews were so vital in quickly and efficiently clearing the snow and later repairing the battered roads, that city leaders could no longer imagine dismantling the department through privatization.<sup>17</sup> City officials noted that public in-house street crews could be deployed in emergency situations much faster than contractors.

## Garbage Collection

Numerous studies show that the costs between public and privately-operated garbage collection are either comparable or higher for private service provision. The City of Houston discovered just how high private provision could be. A city audit revealed that its contractor, Republic, billed the city for the collection and disposal of tons of garbage collected in other cities.<sup>18</sup> In February 2006, the company settled a legal dispute with the city for \$2 million, approximately the amount that the city had been overcharged. The audit also revealed that another trash contractor, BFI, failed to calibrate its scales as often as required by the contract.<sup>19</sup> Contract oversight is critical, but too often cities are unable to provide the necessary in-depth oversight, and are taken advantage of by contractors.

The South Bayside Waste Management Authority, which encompasses cities in northern California, contracted with Allied Waste for solid waste service. A 2006 annual performance review exposed that the company received 10,000 complaints from residents that year for missed trash pick-up. Seven hundred complaints failed to be cleared within the required 24 hour period.

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<sup>14</sup> [http://www.sacramentoexpress.com/headline/8337/Residents\\_continue\\_campaign\\_against\\_budget\\_cuts\\_to\\_parks](http://www.sacramentoexpress.com/headline/8337/Residents_continue_campaign_against_budget_cuts_to_parks)

<sup>15</sup> <http://www.redding.com/news/2010/oct/12/outsourcing-city-parks-wont-save-funds-report/>

<sup>16</sup> [http://inthepublicinterest.org/sites/default/files/UOE%20Local%2039\\_Privatization%20letter%20to%20the%20Council.pdf](http://inthepublicinterest.org/sites/default/files/UOE%20Local%2039_Privatization%20letter%20to%20the%20Council.pdf)

<sup>17</sup> [http://www.tulsaworld.com/news/article.aspx?subjectid=298&articleid=20110219\\_296\\_0\\_Thismo677346&allcom=1](http://www.tulsaworld.com/news/article.aspx?subjectid=298&articleid=20110219_296_0_Thismo677346&allcom=1)

<sup>18</sup> Office of the City Controller, City of Houston, "Controller's audit confirms overcharges by city trash hauler." April 11, 2006. Available at: <http://www.houstontx.gov/controller/pressrelease/press041106.html>.

<sup>19</sup> Ibid.

The contractor was fined due to poor performance, as the contract stipulated that Allied Waste could only have 180 missed pick-ups per year before being penalized.<sup>20</sup>

## Building Inspection

Public building inspection departments are essential in promoting the health and well-being of communities. Importantly, they ensure that buildings and other structures adhere to consistent safety standards. In summer 2010, Jacksonville, Florida decided not to privatize the city's building inspections department after it received bids from five private companies. All bids were more expensive than what it cost the city to do the work in-house. They determined that none of the companies could provide the same high quality service at a cheaper price. City-area businesses report that the public inspection department provides good quality service at reasonable prices, and they do not want to change that.<sup>21</sup>

Several years earlier, Jacksonville learned firsthand the risks of using private building inspectors when a parking garage that was inspected by a private company collapsed, killing a young man.<sup>22</sup> Inspection services must ensure that buildings and structures meet safety standards. Without proper inspection, the public has little protection against construction companies that take shortcuts to increase profit margins. These risks increase when a private company, instead of a public agency accountable to the public, is charged to inspect and regulate itself and other companies in its industry.

## Information Technology

Local-level information technology projects have been plagued with cost overruns. A recent contracting of information technology services in New Orleans has come under fire after the inspector general's office reported that the city wasted \$1 million privatizing the service.<sup>23</sup> The salaries of the private contractor employees alone would cost the city \$960,000 more each year than having city employees perform the same tasks.<sup>24</sup>

New York City experienced massive cost overruns when the city contracted out the design of its timekeeping project, called CityTime. The project was originally supposed to cost \$63 million, but after 12 years and many missed deadlines, the project remains unfinished and has cost the city more than \$700 million – a 1,000% increase from the original contract amount.<sup>25</sup> This troubled system, which was supposed to save the city money by consolidating and automating records of the time clocked by city all workers, is only currently used by 35% of the workforce.<sup>26</sup>

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<sup>20</sup> AFSCME, "Government for Sale: An Examination of the Contracting Out of State and Local Government Services," <http://www.afscme.org/publications/10040.cfm>

<sup>21</sup> <http://inthepublicinterest.org/article/idea-privatize-building-inspectors-cools>

<sup>22</sup> <http://jacksonville.com/opinion/letters-readers/2010-06-23/story/privatization-building-inspectors-good-deal> and

<sup>23</sup> City of New Orleans Office of the Inspector General, "Review of City of New Orleans Contract With Telecommunications Development Corporation: OIG-I&E-09003(C)," August 30, 2010, Available at: [http://media.nola.com/politics/other/TDC%20FINAL%20Report\\_8-30-10.pdf](http://media.nola.com/politics/other/TDC%20FINAL%20Report_8-30-10.pdf).

<sup>24</sup> <http://fcw.com/articles/2010/09/01/new-orleans-mayor-wasted-money-with-outsourcing.aspx>

<sup>25</sup> [http://www.dc37.net/news/pep/2\\_2010/Citytime\\_contract.html](http://www.dc37.net/news/pep/2_2010/Citytime_contract.html)

<sup>26</sup> [http://www.nypost.com/p/news/local/manhattan/six\\_charged\\_in\\_citytime\\_rip\\_off\\_CpKbE5tdMoiTQ0PKvmb8VJ](http://www.nypost.com/p/news/local/manhattan/six_charged_in_citytime_rip_off_CpKbE5tdMoiTQ0PKvmb8VJ)

## Printing Services

Municipalities must also think carefully before contracting out reprographic and other printed-related services. There can be serious consequences when a contractor completes a job incorrectly. In 2009, Dallas County contracted with a printing company to send out notifications from the elections office in time for the November 3 election to let residents know about the consolidation of voting precincts. The printer was late mailing the notice. As a result, many voters failed to receive the important notification informing them of their new precinct until the day of or after the election. The printing company gave numerous excuses for the delay, including that they had run out of paper and lost a disk containing the county's information.<sup>27</sup> Nevertheless, these contractor errors may have compromised the fairness of the election.

## Contract Cities

Several cities have experimented with large-scale privatizing of their local government. Typically in these arrangements, a city will provide a large lump sum to a company, like CH2M Hill, a large construction and operations firm, to run almost every day-to-day municipal government function, such as garbage collection, park maintenance, and human resources. However, these privatization experiments have been short-lived as cities realize that they could actually save money by bringing these functions in-house. After three years of privatization, Milton, Georgia brought many municipal services back in-house. The city manager explained that rebuilding its public workforce would translate into a savings of at least \$1 million per year.<sup>28</sup> Johns Creek and Chattahoochee Hills, Georgia also decided to significantly roll-back their contracts with CH2m Hill.<sup>29</sup> These cities note that with declining tax revenues, they could no longer afford the privatized services.<sup>30</sup>

## Conclusion

When cities contract out public functions, they are handing over control of vital services that residents rely on to corporations primarily concerned with their bottom line. As the experience of cities around the country shows, privatization is often a bad deal for the public – cost savings fail to materialize, service quality declines, and contractors evade accountability. Money leaves the community as the local economy erodes and neighbors lose their jobs. However, some cities are taking a stand against privatization, and keeping public functions in the public realm. Others are taking services that were formerly privatized back in-house, in a trend called “reverse privatization.”<sup>31</sup> They have found that these services can be provided more efficiently and cost-effectively by the public sector.

Before deciding to privatize, cities must ask themselves the right questions before they make a decision that will impact their community for years. In *The Public Interest* recently released a list

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<sup>27</sup> <http://cityhallblog.dallasnews.com/archives/2009/11/dallas-commissioner-john-wiley-3.html>

<sup>28</sup> <http://www.ajc.com/news/north-fulton/milton-ends-privatization-experiment-270080.html>

<sup>29</sup> <http://www.ajc.com/news/north-fulton/johns-creek-plans-move-593349.html> and <http://www.ajc.com/services/content/printedition/2009/05/07/contract0507.html>

<sup>30</sup> *Ibid.*

<sup>31</sup> Warner, M.E. with Mike Ballard and Amir Hefetz, 2003. “Contracting Back In - When Privatization fails,” chapter 4, pp. 30-36 in *The Municipal Year Book 2003*. Washington, DC: International City County Management Association.

of questions that helps decision makers and voters decide whether privatization makes sense. You can find these questions at: <http://inthepublicinterest.org/article/ask-right-questions-privatizing>.

For additional resources on municipal services privatization, visit In The Public Interest's webpage on municipal services at: <http://inthepublicinterest.org/sector/municipal-services>