



Privatization Watch

Analyzing privatization developments since 1976

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Privatization Watch

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When Government Jobs Go Overseas

By Adrian T. Moore



In the midst of current debate, small in scale but important to many people, is the outsourcing of government services, some of which have gone offshore. Programmers in India are helping revamp South Carolina's unemployment tax system. In 40 states and the District of Columbia people collecting food stamps use foreign help desks.

Various House and Senate proposals would halt or hinder offshore outsourcing by the feds, and dozens of states are considering banning their agencies from using foreign offshore labor, and some states have already reversed course on offshore outsourcing. Last year, Indiana cancelled a \$15 million contract with an Indian consulting firm that would have handled calls in India. In March, North Carolina legislators voted to spend \$1.2 million to bring 34 child support call center jobs back from India. Perhaps the most famous case comes from New Jersey, where roughly 10 unemployment assistance call center jobs went overseas, only to return again after much negative publicity.

The New Jersey example is instructive. It cost the state about \$100,000 per year per job brought back to American soil. For each outsourced job, the state could have spent \$50,000 for training, education and employment support and still enjoyed large savings in subsequent years.

Purchasing lower cost services could have allowed New Jersey to spend less or to devote more funds to higher priorities. Such decisions keep taxes lower which stimulates business activity and generates more tax revenue for the state. New Jersey would experience a boost in productivity and living standards, and everyone in the state would be marginally better off.

This is another version of the long running debate over privatization, of which outsourcing is but a type. All levels of U.S. government currently outsource close to \$500 billion in contracts. The New Jersey story tells us why—outsourcing can dramatically reduce costs. Kansas could not resist the cost savings. Lawmakers were initially so outraged by a plan that would send food stamp call center jobs overseas that they wrote a ban into this year's contract. Once legislators learned the move would make the contract nearly 40 percent more expensive, they discarded the ban.

Even with high satisfaction rates (over 90 percent of outsourced services stay outsourced) and well-established savings,

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Privatization Briefs

Space Travel Breaks Government Barrier



When Mike Melville left the Earth's atmosphere on June 21st, he became the world's first private astronaut. Scaled Composite's craft SpaceShipOne reached an altitude of 328,491 feet (62 miles) and then landed safely in California's Mojave desert, completing the private sector's maiden space voyage. The trip was also a triumph for project sponsor Paul G. Allen and Scaled Composite CEO Burt Rutan, who declared, "Our success proves without question that manned space flight does not require mammoth government expenditures. It can be done by a small company operating with limited resources and a few dozen dedicated employees."

Virginia Warms to Private Prisons

In April Virginia Gov. Mark Warner signed HB 1042, which requires the state Department of Corrections to conduct a cost-benefit analysis between public and private facilities before any new facility can be built in the state. Delegate Christopher Saxman (R-Staunton) carried the bill, which followed Warner's announcement that the state would likely have to build two new prisons in coming years. Saxman, chair of the Cost Cutting Caucus in the House of Delegates saw prison privatization as an important opportunity to save money given the state's fiscal realities.

It's Not Just Virginia

The Corrections Corporation of America (CCA) announced the reopening of its Northeast Ohio Correctional Center. The 2,016-bed medium security facility began receiving inmates from the U.S. Marshals Service, and is expected to house an

estimated 300 federal prisoners from Northeastern United States federal courts. Several other federal agencies and numerous states have expressed interest in housing inmates at the Ohio facility. CCA has hired and trained approximately 135 correctional employees at the facility, and expects to have nearly 400 employees once the facility reaches capacity.

Taking Over Amtrak

The Bush administration in April formally requested information from states or groups of states about taking over routes now operated by Amtrak. In a regulatory filing, the Department of Transportation asked states to tell it how they might contract out various Amtrak routes to private companies, and which routes they think would be most viable. The Administration has proposed turning over long-distance service to the states, which could contract with either private firms or Amtrak to keep such trains in operation.

Mississippi Votes for Tolls

Both houses of the legislature passed and sent to the governor a bill that would permit the Mississippi Transportation Commission, cities, and counties to authorize toll roads and bridges, operated either by themselves or by the private sector. Assuming the governor signs the bill, this action will bring the total of states with such measures to 22.

Our Pain, Their Gain?

If America outsources manufacturing jobs to developing nations, those nations must be gaining manufacturing jobs, right? Maybe not. Writing in *Foreign Affairs*, Daniel Drezner points out something interesting:

An Alliance Capital Management study of global manufacturing trends from 1995 to 2002, however, shows that this was not the case: the United States saw an 11 percent decrease in manufacturing employment over the course of those seven years; meanwhile, China saw a 15 percent decrease and Brazil a 20 percent decrease. Globally, the figure for manufacturing jobs lost was identical to the U.S. figure—11 percent. The fact that global manufacturing output increased by 30 percent in that same period confirms that technology, not trade, is the primary cause for the decrease in factory jobs. ■



More Good Than Harm

Can America Learn to Love Outsourcing?

By Adrian T. Moore



Just about everyone is in a tizzy over “offshore outsourcing” the latest efficiency-seeking practice that sends service jobs to India, China and other developing nations. Over two dozen states have considered banning or restricting the practice, CNN’s Lou Dobbs rails against the “Outsourcing of America,” and John Kerry hopes blaming “Benedict Arnold” CEOs will land him in the White House.

The purveyors of panic are right about one thing—outsourcing is not a passing fancy. It is the latest stage in the ongoing evolution of the economy. And just like every other stage in that evolution, from interstate commerce to international trade, the change will offer more benefit than pain. But, just like every other stage in the evolution, a lot of people do not want change.

The politics of offshore outsourcing

The offshore outsourcing debate simply places the politics of globalization and international trade in a white-collar setting. The new free-trade opponents are white-collar employees and executives who long believed that their education protected them from foreign competition.

Workers grow anxious when faced with layoffs and job changes, and we should help them cope with the destructive side of market creation. But the objections to the evolution of

the economy are like a broken record. Once we thought all you had to do was to work hard on a plot of fertile land, and you could make a good living farming forever. Then we thought if you got a job working at one of the nation’s industrial giants, you effectively had a job for life. More recently, people believed that if you stuck it out through college and got your degree, you’d always have a job. None of those approaches proved to be a failsafe route to job security, and Americans are learning that they have to provide skills that the market demands, and yet, even with the churn of the market, today’s workers enjoy ever-improving standards of living. More than ever, job security is about personal improvement and flexibility to work within the changing market.

British Prime Minister Tony Blair recently told his nation’s industry, “What I can’t do is shield you from the world. The economy out there will be decided by knowledge, skills, and education, by value-added goods and services.”

When White House Chief Economist Gregory Mankiew took a beating over his comment that offshore outsourcing is just international trade, most people overlooked that at least four top economic advisors from the Clinton administration publicly agreed with Mankiew.

But in politics, protectionism sells because it comforts people. Voters hope politicians can shield them from change, and often protectionism only delays the pain, making it more acute in the long run.

The economics of offshore outsourcing

The media buzzes with stories about American jobs going offshore. High-end estimates predict that between now and 2015 3.3 million U.S. information technology jobs will move offshore. But that prediction ignores that the information technology industry continues to grow and now job creation outpaces job loss.

It was widely reported that the nation lost 2.3 million jobs during the last economic downturn. What gets overlooked is that about two-thirds of those jobs were “tech bubble” jobs, not permanent jobs in the economy. The remaining 800,000 jobs are what we would expect to shed with normal cyclical fluctuations in the economy.

But even as the market churn cuts some jobs, it adds many more. At the end of World War II, there were about 138 million Americans. Today about 138 million Americans have jobs. From 1980 to 2002 the U.S. population grew by 23.9 percent; meanwhile the number of people with jobs grew 37.4 percent. In other words, an efficient market is the best jobs program.

Creating jobs at home

When companies save money by sending rote work overseas, they invest more to create new jobs at home. An analysis by the Institute for International Economics (IIE) shows that while more than 70,000 computer programmers have lost their jobs since 1999, more than 115,000 higher paid consumer software engineers have been hired. Even with a slower economy and with the offshore movement in full swing, the U.S. IT industry created 148,000 new jobs in the last quarter of 2002.

The story is the same for the service sector as a whole. While recently 10 million jobs per year have been lost, 12 million per year have been added. The IIE finds that most of the jobs that will be lost offshore pay less than the U.S. average wage and are likely to be eliminated through technology whether outsourced offshore or not.

What gets outsourced overseas are jobs that have become routine and commodified, and where the U.S. worker productivity no longer beats foreign workers. Meanwhile, two-thirds of the economic benefit from offshore outsourcing accrues in the United States in the form of lower prices, expanded overseas markets for U.S. products, and improved profits that are reinvested to create new jobs. A recent McKinsey Global Institute study notes that offshore outsourcing creates value in four ways:

- **Cost savings:** For every dollar of spending on business services that moves offshore, U.S. companies save 58 cents. Reduced costs are by far the greatest source of value creation for the U.S. economy.
- **New revenues:** Indian companies that provide offshore services need goods and services themselves, ranging from computers and telecommunications equipment to legal, financial and marketing expertise. Often they buy these from U.S. companies.
- **Repatriated earnings:** Many Indian offshore service providers are in fact U.S. companies that repatriate earnings. Such companies generate 30 percent of the revenues of the Indian offshore industry.
- **Redeployed labor:** Beyond the direct benefits to the United



States in the form of savings, new exports and repatriated profits, offshoring can indirectly benefit the economy. as capital savings can be invested to create new jobs.

Politicians who pump up public fears hope that voters will regard offshore outsourcing as a newly invented threat to jobs. Of course, outsourcing is not a new creation; it's merely the latest evolution of a process that has been around for a long time—trade. Trade has given people ever-rising standards of living, as well as more and better jobs. Like trade in general, outsourcing will continue to create more than it destroys.

An efficient economy can offer hope even to its victims, for victimhood itself is a temporary state. According to Bureau of Labor Statistics, most of the unemployed find new jobs within three months, and the efficiency-seeking forces that fire workers are the same forces that will ultimately rehire them. Sending 1,000 call center jobs to India saved Delta Airlines \$25 million, allowing for the hire of 1,200 reservation and sales positions in the United States. Choosing inefficiency over outsourcing means slowing the most robust job-creating machine the world has ever known. It means less money will be reinvested, fewer firms will seek to expand, and ultimately fewer jobs.

As the market evolves, the worker's mindset must also evolve. Job security no longer means fighting to keep the same job for 30 years, it means keeping oneself marketable. Just as the market searches for ways to do things better, so will tomorrow's workers—by gaining new knowledge and skills—seek to better themselves. ■

Truths About Trade

By Brink Lindsey

Jobs churn constantly

The steady increase in total employment masks the frenetic dynamism of the U.S. labor market. Gross changes—total new positions added, total existing positions eliminated—are much greater in magnitude. Large numbers of jobs are being shed constantly, even in good times. Total employment continues to increase only because even larger numbers of jobs are being created.

According to economist Brad DeLong, a weekly figure of 360,000 new unemployment insurance claims is actually consistent with a stable unemployment rate. In other words, when the unemployment rate holds steady—that is, total employment grows fast enough to absorb the ongoing increase in the labor force—some 18.7 million people will lose their jobs and file unemployment insurance claims during the course of a single year. Meanwhile, even more people will get new jobs. It is as inevitable that some companies and industries will shrink, as it is that others will expand. Localized challenges and problems should not be confused with national crises.

“Deindustrialization” is a myth

Between 1980 and 2003, American manufacturing output climbed a dizzying 93 percent. Yes, production fell during the recent recession, but it is now recovering: the industrial production index for manufacturing rose 2.2 percent in 2003.

It is true that manufacturing’s share of gross domestic product has been declining gradually over time from 27 percent in 1960 to 13.9 percent in 2002. The percentage of workers employed in manufacturing likewise has been falling, from 28.4 percent to 11.7 percent during the same period. But the primary cause of these trends is the superior productivity of American manufacturers. Output per hour in the overall nonfarm business sector rose 50 percent between 1980 and 2002; by contrast, manufacturing output per hour shot up 103 percent. In other words, goods are getting cheaper and cheaper relative to services. Since this faster productivity growth has not been matched by a corresponding increase in demand for manufactured goods, the result is that Americans are spending relatively less on manufactured goods. Accordingly, manufacturing’s shrinking share of the overall economy is actually a sign of American manufacturing prowess.

“Offshoring” is not a threat to high-tech employment

Despite the trend toward offshoring, IT-related employment is expected to see healthy increases in the years to come. According to Department of Labor projections, the total number of jobs in computer and mathematical occupations will jump from 3.02 million in 2002 to 4.07 million in 2012—a 35 percent increase. Of the 30 specific occupations projected to grow fastest during those 10 years, seven are computer-related. Thus, the recent downturn in IT is likely only a temporary break in a larger trend of robust job growth.

The wild claims that offshoring will gut employment in the IT sector are totally at odds with reality. IT job losses projected by Forrester Research amount to fewer than 32,000 per year—relatively modest attrition in the context of 6 million IT jobs. These losses, meanwhile, will be offset by newly created jobs as computer and mathematical occupations continue to boom. The doomsayers are confusing a cyclical downturn with a permanent trend.

Fears that the U.S. economy is running out of jobs are nothing new

In the late 1950s and early ’60s the ongoing progress of factory automation, combined with the growing visibility of electronic computers, led many Americans to believe, once again, that the economy was running out of jobs. During the 1960 presidential campaign, John F. Kennedy, who ran on a pledge to “get the country moving again,” warned that automation “carries the dark menace of industrial dislocation, increasing unemployment, and deepening poverty.” And yet more jobs were created. For the record, U.S. employment in 1962 stood at roughly half the current total.

In the early 1980s, the coincidence of a severe recession and a string of competitive successes by Japanese producers at the expense of high-profile American industries sparked predictions of the imminent “deindustrialization” of the American economy. As financier Felix Rohatyn complained, in a fashion typical of the time, “We cannot become a nation of short-order cooks and saleswomen, Xerox-machine operators and messenger boys....These jobs are a weak basis for the economy.” It should be noted that U.S. manufacturing output has roughly doubled since 1982.

In the early 1990s, another recession resulted in yet another job shortage scare. Ross Perot won 19 percent of the presidential vote in 1992 with a campaign that, among other

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Ever Heard of Insourcing?

Outsourcing's lesser-known relative creates jobs at home

Interview by Ted Balaker

Listen to a few campaign stump speeches and you would start to get the impression that outsourcing is a one-way street, where jobs travel to distant lands never to return. But like international trade in general, outsourcing goes both ways: U.S. companies send jobs to foreign nations and foreign companies send jobs to the United States. Insourcing represents another often-overlooked aspect of outsourcing that creates jobs at home. According to the Organization for International Investment, U.S. subsidiaries of foreign companies employ 6.4 million Americans, and insourced jobs have grown by 117 percent over the past 15 years.

Samsung's Austin-based semiconductor plant (SAS) is just one example of insourcing. The South Korean company recently announced plans to add 300 high-paying tech jobs to the Austin facility that already employs nearly a thousand people.



William Cryer

SAS executive William Cryer realizes why the United States can be attractive for foreign investment, but he also understands that today's advantages may not last forever. For example, a faltering education system could erode our nation's skilled labor pool. Cryer says its "absolutely critical" to improve education in order to lure more foreign investment.

Recently, PW editor Ted Balaker interviewed William Cryer.

I'm sure many nations would have loved to have Samsung open this facility on their soil. Why did your company choose the United States?

The United States is still the largest consumer of microchips and is central to our market. A U.S.-based company also solves many trade issues with the U.S.

On a similar note, you could have set up shop anywhere in America. Why Austin?

Several reasons: Austin is a semiconductor center and has the required infrastructure for a large manufacturing plant, e.g. chemical suppliers, clean room equipment, and so on. The location is close to two of our largest buyers of memory chips: Dell Computer is about five miles from SAS and HP is in Houston, 150 miles away. There are also trade issues, and the availability of a trained workforce.

In terms of business climate and workforce, what positive

features does America offer Samsung that would be different from other nations?

Obviously, the U.S. has an established infrastructure that supports manufacturing: water, good power grid, trained, well-educated workforce, and it is the largest economy in the world.

What could elected officials do to entice Samsung to create even more American jobs?

They need to face up to the challenges of international competition in education, work environment, etc. While the U.S. still has advantages in, say, workforce education, this is not a given and seems to be eroding rather quickly as other countries catch up (and surpass the United States). The U.S. cannot afford to write off large segments of its population. This will be a continuing challenge. ■



Inside Austin's semiconductor plant

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Jobs

things, railed against the "giant sucking sound" of jobs lost to Mexico and other foreign countries. That hand-wringing was followed in short order by one of the most remarkable expansions in American economic history.

Again and again, over many decades, cyclical downturns in the economy have prompted predictions of permanent job shortages. And each time, those predictions were belied by the ensuing economic expansion. The root of the error is always the same: confusing a temporary, cyclical downturn with a permanent reduction in the economy's job-creating capacity.

Brink Lindsey is a senior fellow at the Cato Institute and director of its Center for Trade Policy Studies. He is the author of Against the Dead Hand: The Uncertain Struggle for Global Capitalism (John Wiley & Sons). This preceding was excerpted from a longer article, which is available here: reason.com/0407/fe.bl.truths.shtml ■

GAO Weighs in on Competitive Sourcing

By Geoffrey F. Segal



The General Accounting Office (GAO) recently reported to Congress on the progress agencies had made toward competitive sourcing goals, identifying major challenges, and strategies agencies are using to fully implement competitive sourcing. The review consisted of seven departments, including Defense, Education, Interior, and Veterans Affairs, which together account for fully 84 percent of commercial positions in the federal government.

The report noted that given the current environment in which the federal government operates—new security threats, rapidly evolving technologies, increased pressure for results, and growing fiscal concerns—that agencies needed to “engage in a fundamental review of how they accomplish their mission.” Competitive sourcing is a powerful tool to help agencies determine “how best to acquire and delivery such services, including whether to obtain services in-house or through private sources.”

The report noted that civilian agencies undertook more than 600 competitions in 2003. Of those 363 were streamlined competitions (affecting 65 or fewer positions) and 130 were direct conversions to a performance contractor. In addition, Defense completed another 126 assessments, including 54 direct conversions and 7 streamlined competitions. In all, over 17,000 positions were studied—and in-house teams retained almost 76 percent of the positions covered by competition studies.

Other progress includes the creation of at least two inter-agency forums for sharing competitive sourcing information—including the Federal Acquisition Council. The Office of Management and Budget (OMB) has actively encouraged this exchange of information. In fact, as the report notes, OMB plans to use these systems to monitor agency implementation and generate more consistent and accurate cost and savings data for reporting to Congress.

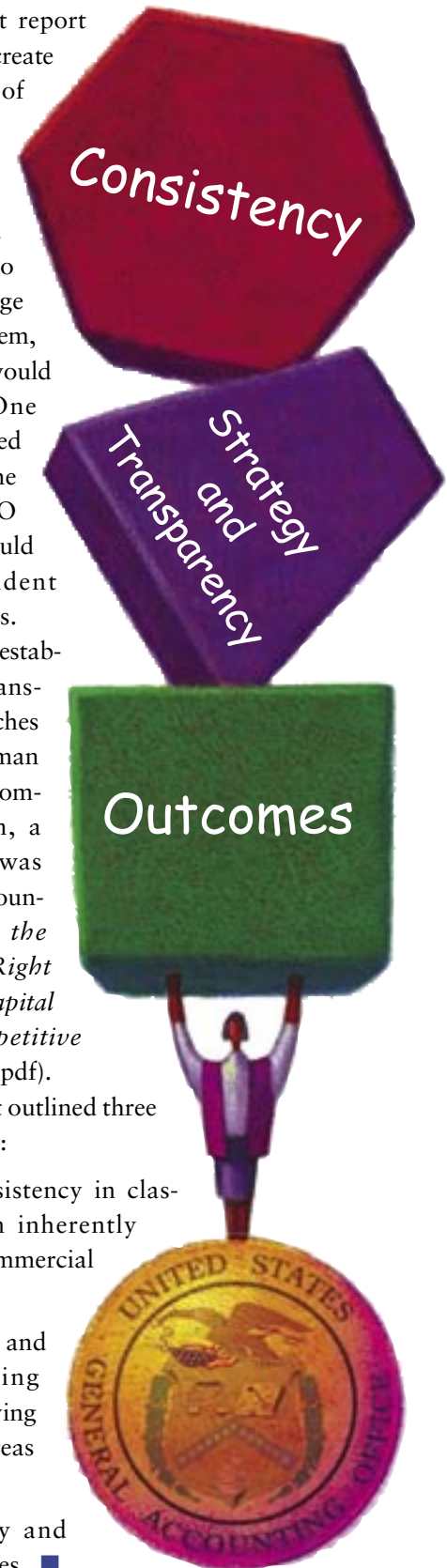
However, agencies are struggling to ensure that enough staff, with necessary procurement skills, are in place to properly manage their programs. Agencies have to build and maintain capacity to manage competitions, build the in-house MEO (most efficient organization), and manage the implementation and oversight of competition decisions. This recommendation is in line with Reason Foundation’s October 2002 report *Designing a Performance-based Competitive Sourcing Process*

for the Federal Government (rppi.org/ps299.pdf). In that report we suggested that OMB create a “Competition Corps” of highly trained competitive sourcing managers who would be assigned to each study conducted by the agencies. Similar to the public-defender/judge roles of the justice system, the Competition Corps would assume two roles. One manager would be assigned to assist employees in the development of an MEO and another manager would serve as the independent reviewer of the proposals.

Several agencies have established strategic and transparent sourcing approaches by integrating their human capital plan with their competitive sourcing plan, a recommendation that was outlined in the Reason Foundation study, *Getting the Right People for the Right Job: Solving Human Capital Challenges with Competitive Sourcing* (rppi.org/ps31.pdf).

Ultimately, the report outlined three broad recommendations:

1. Ensure greater consistency in classifying positions in inherently governmental or commercial positions;
2. Make more strategic and transparent sourcing decisions by identifying broader functional areas for competition; and
3. Focus on efficiency and performance outcomes. ■



Major Private Toll Road Proposals Refute GAO Report

By Robert W. Poole, Jr.



The early months of 2004 have witnessed a whole raft of private sector proposals and state government initiatives, all pointing to tens of billions of dollars in potential private sector investment in new, tolled-highway capacity. Ironically, in the midst of all this activity, the General Accounting Office released a report concluding that “private sponsorship [of transportation projects] seems best able to advance a small number of projects, but seems unlikely to stimulate significant increases in funding for highways and transit.” (The GAO report is available at www.gao.gov/cgi-bin/getrpt?GAO-04-419.)

Here are some of the newest private sector proposals.

1. Fluor has proposed to add HOT/BRT (High-Occupancy Toll/Bus Rapid Transit) lanes on the Shirley Highway (I-395) and I-95 south of Washington, D.C., extending over a total distance of 56 miles. The project is estimated at \$1 billion, all of which would be financed with toll revenue bonds. This project is competing with a shorter (37-mile) proposal from Clark, Shirley, and Koch for HOT lanes on I-95 only, from the Beltway to Fredericksburg, Virginia.

2. In Texas, Kiewit has proposed adding four express toll lanes in the median of the Airport Freeway between I-35W in Fort Worth and I-35E in Dallas, a distance of 27 miles. This, too, would likely be a billion-dollar project, though no cost estimate has yet been released. A planned expansion of the highly congested freeway is two decades behind schedule. The express lanes would use variable pricing, fully automated via electronic toll collection.

3. Three competing proposals have been submitted to the Georgia DOT to upgrade GA 316 between Athens and Atlanta, a distance of 39 miles, as a toll road. This project, too, would cost upwards of a billion dollars. The teams are led by Washington Group International, CINTRA, and Horizon Corridor.

These three new billion-dollar projects are in addition to others in various stages of planning around the country. Virginia is already far along with two other major private tollway projects. The STAR Solutions consortium has been selected by VDOT for a \$7 billion project to add two lanes in each direction to the entire 325 miles of I-81 across the state. The new tolled lanes would be for trucks only on this major truck route. And VDOT has also accepted Fluor’s unsolicited proposal to add two HOT lanes in

each direction to the southwestern quadrant of the Washington Beltway, I-495, at an estimated cost of \$700 million.

Much more ambitious, but still in the planning stage, is a proposed \$16 billion system of toll truckways linking the twin ports of Los Angeles and Long Beach to the inland logistics center of Barstow, California. The most likely route for these truckways would be north up I-710, eastward on SR 60, then north on I-15 to Barstow. The proposal was included in the new 2030 long-range transportation plan adopted by the Southern California Association of Governments (SCAG) in April. SCAG has prepared draft legislation that would create a truckways authority to franchise some or all of the project to private consortia.

And this may be just a foretaste of what lies ahead. Maryland’s State Highway Authority in April formally requested private sector ideas for financing, building, and operating new lanes on all its major highways, after earlier unveiling the concept of Express Toll Lanes as the preferred form of capacity expansion. ETLs would use variable tolls, electronically collected, both to manage traffic flow and to help pay for the new lanes. The projects of greatest interest include the Capital Beltway (I-495/95), I-270, the Baltimore Beltway (I-695), I-95 between the two Beltways, I-95 north of Baltimore, US 50 from Annapolis to the D.C. line, and the proposed new Inter County Connector. Combining these projects with the proposed HOT/BRT lanes on the Virginia side of the border could produce one of the first HOT Networks in America.

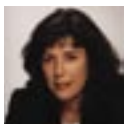
But perhaps not the first. Minnesota Gov. Tim Pawlenty in January proposed a network of investor-financed express toll lanes for the Twin Cities of Minneapolis and St. Paul. Minnesota DOT envisions the new lanes being added to I-35W, I-94, I-394, much of the beltway I-494 and I-694, I-35E, and several other highways. They are premised on passage by Congress of Rep. Mark Kennedy’s (R, MN) FAST Lanes bill, different versions of which are included in the House and Senate bills to reauthorize TEA-21 for another six years, but would also make use of provisions of Minnesota’s existing public-private partnership law.

In addition, both Dallas and Houston have studies under way on the potential of creating such express lane networks. And Texas now has the most sweeping transportation public-private partnership statute in the country.

Add it all up and there is easily \$40 to \$50 billion in new private investment that could be generated should all these projects come to fruition. Surely, the GAO will need to revisit this subject in a few years. ■

The Outsourcing-Education Connection: Would Better Schools Keep Better Jobs at Home?

By Lisa Snell



While today's fears about losing high-tech jobs to offshore outsourcing may be overblown, a faltering education system could eventually prompt employers to look overseas for skilled labor.

Recently several prominent sources have called for strengthening American education as the crucial strategy to prevent the excessive outsourcing of high-tech jobs. A report by the American Electronics Association (AEA) argues that American public education is the reason why so many companies are exporting jobs to other countries (see Sidebar on next page). The AEA suggests that because students do not get a strong enough education in math and science, high tech firms are forced to look for skilled workers in other nations. In other words, as other nations catch up to us in terms of education, companies will ship jobs overseas looking for smarter, not cheaper, workers.

Recently, Federal Reserve Chairman Alan Greenspan agreed that the United States must produce more highly skilled workers. Greenspan noted that even though incomes continue to rise there is reason to be concerned about the future:

[W]e have developed a shortage of highly skilled workers and a surplus of lesser-skilled workers. . . . More broadly, in considering the issue of expanding our

worried about OUTSOURCING?

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skilled workforce, some have a gnawing sense that our problems may be more than temporary and that the roots of the problem may extend back through our education system. Many of our students languish at too low a level of skill, and the result is an apparent excess of supply relative to a declining demand.

Similarly, in March 2004 testimony before the U.S. House of Representatives Committee on Education and the Workforce, Robert Grady, president of the National Venture Capital Association, highlighted the importance of improving education.

"The health of our schools is essential to the health of our country," said Grady. "In this regard, legislation that ensures that our schools are performing, our kids can read, and parents of children in failing schools have more rights to do something about it is critical. In particular, we would urge support of programs to increase the number of students pursuing mathematics, science, and engineering education in the United States."

Falling behind

Mounting evidence shows American students are falling behind in math and science:

- Eighty-two percent of our nation's twelfth graders performed below the proficient level on the 2000 National Assessment of Educational Progress (NAEP) science test.
- The longer students stay in the current system the worse they do. According to the 1995 Third International Mathematics and Science Study, U.S. fourth graders ranked second. By twelfth grade, they fell to 16th, behind nearly every industrialized rival and ahead of only Cyprus and South Africa.
- Recently the National Science Board has noted the decline in the number of American students training to be scientists. It states that the number of 18 to 24 year olds who receive science degrees has fallen to 17th in the world, whereas the United States ranked third three decades ago.
- More than 50 percent of all engineering, math, and science degrees awarded at U.S. universities go to foreign nationals.

Not only are many high school graduates not prepared for high-level college courses in math and science, they often graduate without basic skills in language and mathematics. For example, a 2003 report by California's Legislative Analyst's Office notes that in the California State University system close

to 50 percent of all enrolled college freshman must take remedial education courses in math and writing before moving on to college-level courses. What's worse is that these students are allegedly representing the top one-third of California's high school graduates. Yet, the state of California must spend a huge amount of tax dollars subsidizing remedial courses for students who have been accepted into California's higher education system.

Over the years several legislative fixes attempted to increase the math and science knowledge of American students. Most recently, the No Child Left Behind (NCLB) Act called for The National Science Foundation and the U.S. Department of Education to provide an estimated \$1 billion over five years for results-oriented partnerships between local districts and universities and colleges. The NCLB also requires that beginning in 2007 states measure students' progress in science at least once in each of three grade spans (3-5, 6-9, 10-12) each year.

Competition abroad, competition at home

In addition to attempts to legislate math and science curriculum, the outsourcing debate gives us one more reason to support a competitive education system that will offer parents more education choices including an enhanced math, science, and technology curriculum. Legislation that helps break up the monopoly that traditional public schools have over school curriculum and offers parents more school choices may be a more efficient mechanism to increase the supply of higher-skilled students. Many parents are already choosing innovative private, magnet, and charter schools that have an explicit focus on math, technology, and science. However, the

Techies Tout Outsourcing More Findings from the AEA Report

- The magnitude of offshore outsourcing is unknown.
- A weak international and domestic economy and productivity improvements are the primary cause of the lost jobs over the last three years—not outsourcing.
- Changes in the international marketplace are posing far more significant new competitive challenges for U.S. companies than is offshore outsourcing.
- The United States experienced a similar anxiety to offshore outsourcing in the late 1980s and early 1990s when there was a common view that Japan was going to take over the world. It didn't.
- We should not forget that the United States remains an immensely attractive location for foreign direct investment and insourcing by foreign companies, employing millions of Americans.
- Although some people will be hurt, offshore outsourcing is likely to be a long-term benefit for the United States.
- If protectionist legislation should emerge from the states or Congress, high tech, as the largest exporter, stands to lose the most.

Source: "Offshore Outsourcing in an Increasingly Competitive and Rapidly Changing World," available at: rppi.org/outsourcing-myths.pdf

demand far exceeds the supply of these schools.

A substantial number of the 3,000 charter schools nationwide are schools that specialize in math and science, including schools like the Anvil City Science Academy in Alaska, The Sonoran Science Academy in Tucson, and High Tech High in San Diego. These schools offer parents a chance to give their child a competitive math and science education. For example at the Sonoran Science Academy students have the opportunity to participate in math, science, robotics, rocketeering, and engineering competitions.

In addition charter schools have created a demand for research and development of science curriculum. For example, more than 200 schools use E.D. Hirsh's highly regarded Core Knowledge math and science curriculum and other schools use Bill Bennett's K12 interactive math and science curriculum. These innovative curriculums cannot be created without breaking up the financial monopoly that public schools hold over education. These alternative schools often have long waiting lists and illustrate the demand to build more capacity in schools that focus on these high-tech subjects. An efficient way to increase math and science knowledge would be to meet parental demand for schools that offer these high-performing options

through a more competitive education marketplace.

In other words, as low-skill computer work gets sent overseas, the U.S. market will increasingly need American workers with high technological skill levels and also managerial skills, as these are the jobs that are staying in this country. Allowing schools that provide education opportunities demanded by parents who understand the needs of the coming market is essential to meeting this goal. ■

A Privatization First in Chicago

By Robert W. Poole, Jr.



March saw the city of Chicago request that prospective bidders submit their qualifications to buy and operate the Chicago Skyway, one of the Midwest's premier toll facilities. The six-lane, 7.8-mile elevated tollway would be offered for a long-term franchise of not less than 50 years. Bidders had until April 21st to submit their qualification packages. Goldman Sachs is advising the city on this historic privatization.

Although no such sale of a major existing highway or bridge has taken place thus far in the United States, four major transactions of this sort have taken place in the last five years. Autostrade, the huge Italian state tollway authority, was sold via a public stock offering in 1999, for \$6.7 billion. What investors actually purchased was a long-term franchise (called a concession in Europe) to own and operate the toll road system for 38 years. The same year, Portugal sold its state toll agency, BRISA, for \$2 billion, with a similar 33-year concession arrangement. The Canadian province of Ontario sold a 99-year concession to own, operate, and expand the pioneering Highway 407 Electronic Toll Road for \$2.1 billion. And in 2003, the Spanish government sold a number of state-owned toll roads to investors for \$1.8 billion.

The privatization is an opportunity to cash out its investment in this one-of-a-kind enterprise

The Skyway had some difficult early years, losing money and having to be refinanced. But during the past decade, due in part to growing congestion on the non-tolled alternate routes and the advent of gambling casinos across the Indiana border, traffic and revenues have boomed. The city has nearly completed a major refurbishment, getting the Skyway ready for sale. The private acquirer will be expected to implement 21st-century electronic tolling, replacing the manual toll plaza still in use on the Skyway.

For the city, the privatization is an opportunity to cash out its investment in this one-of-a-kind enterprise, paying off its Skyway bonds and receiving an ongoing revenue stream from the tollway without having to operate and maintain it. If the transaction is completed as planned, it could set a precedent for other states to consider the pros and cons of getting out of the tollway business in a similar manner. ■

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OVERSEAS

some resist outsourcing on different grounds, like privacy. The government possesses personal information about many citizens, and when many kinds of services are outsourced, some of that information is handled by contractors, some of whom might be overseas.

Certainly only careful handling of such information can protect privacy. But why might offshore information handling pose a greater risk? Say a young woman in India answers a help call and in the process sees financial, medical or other private information about the customer. Does she have more reason and opportunity to abuse that information than a contractor in the United States? Actually, she may have less incentive and opportunity to violate customer privacy. Her company has every incentive to protect privacy. The company rides the most exciting wave to hit India in years, and the surest way to get knocked off the wave is to do something that drives customers away, like violating privacy agreements.

When customer complaints prompted Dell to bring its help center business back to the United States, Indian firms reacted quickly. They placed more emphasis on improving English language skills and guaranteeing customer satisfaction.

Privacy concerns are not new. Since the first time an outsourcing agreement included information sharing, contractors have sought to protect privacy. From outsourcing of general services to medical transcription to IT, outsourcing practitioners have developed means of ensuring privacy.

Of course, the evolution of outsourcing into a more international market may require some changes in order to integrate U.S. law with existing international laws that guard against privacy invasion.

But while they address small changes, legislators should take care to not quash the benefits of outsourcing. The technology industry is too dynamic and complex for legislators to answer legitimate concerns about the downside risks and consequences of using offshore resources. Trying to create bright distinctions in a rapidly changing market will only invite outcomes in which the taxpayer loses. ■



Who's taking American jobs?



Machines ...

By Ted Balaker

From the save-our-jobs perspective, the new protectionists have more to fear from machines than from foreign workers. After all, those soulless slaves to efficiency have stolen more American jobs than any foreigner. Hollywood visionaries use films like *The Terminator* and *The Matrix* to warn us of the coming war against the machines. Well, the war is here. Actually, it's been here for a long time.

The printing press swallowed human scribes and the photocopier and personal computer destroyed countless office jobs. Machines like the tractor have overrun agriculture so much that during the last century farmers' share of the American workforce has fallen from 40 to 3 percent. Recently, a Kentucky city mourned when a machine replaced its last human elevator operator, and even the recently resolved Southern California grocery strike may turn out to be another victory for machines. Here man and machine used to work together in peace—for example, human checkers appreciated how scanners would remember thousands of prices for them. But now some stores have begun phasing in automated checkout machines, which means human checkers work alongside machines that may eventually take their jobs. Moreover, an analysis of Bureau of Labor Statistics data notes that even without outsourcing technology would have eliminated most of the jobs now going overseas. Sometimes it seems like our society is so mechanized that there's almost nothing left for us humans to do.

Of course, cursing machines misses the point because it tells only half of the story. Pundits can point to a specific sector or a narrow time frame and tell a tale of woe. And the quest for efficiency does kill jobs, but, in the long run, it creates more than it destroys. Sometimes an industry disappears or shrinks to a nub of its former self, and yet new life continues to sprout. It would be tough to find many scribes today, but the printing press and the PC haven't wiped out office jobs. In fact, the United States has 19.5 million of them.

Still, can we connect the dots from efficiency gains to job growth? Some imagine that CEOs fire humans, hire machines, and then throw the extra cash on their money pile. This view may not be far off the mark in assuming ambition—perhaps even greed—motivates the CEO. However, the truly greedy won't simply stash the cash—they will reinvest it and dream of an even bigger payday. Since reinvestment spurs job growth, in order to accept the efficiency gains-job growth link you simply have to assume that corporate greed is alive and well. For most of us, this isn't a huge leap.

As the market evolves, we don't just exchange fewer jobs for more, we also trade up for better jobs. Since today's office mates squabble over a couple of clicks on the thermometer, it's a good thing few of them will have to find out how they'd survive in, say, a mineshaft. During the past 50 years we've lost over a quarter-million mining jobs, but we've gained 78 million service sector jobs. Today, 19 times more Americans work in finance than in mining, 22 times more work in hospitality and 54 times more work in health and education.

It's often difficult to track job growth by a particular occupation, because many of today's jobs were created recently. Today's jobseeker has more choices than ever, which means that we are more likely get paid to do something we enjoy. Americans hold millions of jobs that did not exist a century ago. For example, our nation is home to 758,000 software engineers, 299,000 fitness workers and 128,000 aircraft mechanics. And many of the old-style jobs—far from being outsourced into oblivion—are more plentiful than ever. Our nation has 6.5 million teachers, 718,000 hairdressers, 281,000 chefs and 112,000 biologists. The chance for work to aid rather than hinder our quest for fulfillment is a truly historic development. How many miners stuck deep within the earth would have rather been video editors, web designers, or car customizers?

Who else is taking American jobs?

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Focus on Offshore Outsourcing

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OTHER AMERICANS

Most outsourced jobs never leave American soil, the U.S. Labor Department noted in a June report. The report suggests fears over losing American jobs to cheap foreign competition may be overblown.

According to the Labor Department, 9 percent of non-seasonal U.S. layoffs in the first quarter were due to outsourcing, but less than a third of those jobs were sent overseas. "In more than 7 out of 10 cases, the work activities were reassigned to places elsewhere in the U.S.," the Bureau of Labor Statistics said in its report on mass layoffs for the January-to-March period.

In other words, Americans are taking American jobs. Interstate outsourcing may be more palatable than offshore outsourcing to some, but for an outsourced worker, whether the job goes across the nation or across the world, it is just as lost. Should workers scorn the CEO who decided to move to a different state or legislators who make the cost of doing business unnecessarily expensive?

States, like nations, compete for capital and jobs by offering business-friendly climates. The Electrolux refrigerator plant recently moved 1000 jobs from Michigan to South Carolina. New York's Scalandre, a luxury fabric manufacturer, also recently relocated to the Palmetto state and CEO Mark Bitter was clearly motivated by the same forces that move jobs overseas. Bitter notes that in South Carolina "you have lower overhead, lower taxes, lower occupancy costs, lower labor costs, lower everything."

It would seem that high tax states that lose jobs to low tax states would have two options: lower taxes to produce a better business climate or lobby the federal government to ban interstate outsourcing. Of course, then some might get upset with intercity outsourcing. ■

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Developer Creates "First Archaeological Subdivision"

By Pamela Villarreal

Western real-estate developer Archie Hanson has found a way to preserve the past while developing for the future in what he calls "America's first archaeological subdivision." Located on 1,200 acres in Cortez, Colorado, Indian Camp Ranch consists of several 35-acre lots and over 200 archaeological sites from the Anasazi tribe. A purchaser can build a home on his land, and enjoy the unusual amenity of a backyard archaeological dig. The subdivision is governed by a neighborhood covenant controlling excavations and requiring preservation of artifacts.

Privatized archaeology has advantages for both residents and researchers

Observers say that privatized archaeology has advantages for both residents and researchers:

- Residents will receive the help of a trained archaeologist in excavating their land, and are permitted to keep and display found artifacts in their home.
- When homeowners die or move, their artifacts will be donated to a planned museum.
- Since privately owned land is exempt from the 1990 Native American Graves Protection and Repatriation Act, which requires federally funded museums or digs on public land to return human remains or sacred objects to the original tribe or descendants, Hanson says he will provide artifacts to researchers for DNA study and use of new scientific technology.
- Instead of digging small areas and reburying them, as many archaeologists now do, artifacts will be put on display for the public.

The concept could provide an economical way for private landowners to preserve Native American ruins, which are often damaged by looters. For example, a rancher in Utah recently revealed thousands of acres of ruins on his land he had kept hidden for 50 years. Eventually unable to care for his land, he sold the ranch to the Land for Public Trust in 2001.

Pamela Villarreal is an intern with the National Center for Policy Analysis. ■

GAO Turns Away Federal Employee Protest

By Geoffrey F. Segal



The General Accounting Office issued its decision in the National Federation of Federal Employees and American Federation of Government Employees' recent protest of the Forest Service's A-76 decision to award work currently performed by government employees to a private sector firm (and concurrently resolved four additional A-76 challenges to other agencies' A-76 award decisions). GAO held that representatives of federal employees do not have standing to protest an agency's A-76 decision because they are not an "interested party" under the Competition in Contracting Act (CICA).

Federal employees and their unions do not have standing to challenge an agency's procurement decision.

CICA is the law that establishes GAO's bid protest authority. That law clearly limits standing to protest to "an actual or prospective bidder or offeror whose direct economic interest would be affected by the award of the contract or by failure to award the contract." GAO determined that an agency's "most efficient organization" (MEO) does not and cannot have a "contractual" relationship with the agency. Unlike contractors, an MEO commits to very little binding legal or financial liability when it wins an A-76 competition.

The ruling furthered GAO's long-standing precedent that federal employees and their unions do not have standing to challenge an agency's procurement decision. However, GAO Comptroller General David Walker, in a letter to Congress released with the decision, noted that this is a matter Congress should consider even though Congress declined to consider the issue in 2003. ■



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New Orleans Drops Privatization

By Geoffrey F. Segal

After five years of study and controversy, the city of New Orleans has dropped plans to privatize its water and sewer systems.

The privatization effort began in 1999 as a way to stave off future rate increases by holding down costs. Former Mayor Marc Morial initiated the privatization drive seeking a 20-year \$1 billion contract. That effort stalled when labor and environmental groups including Public Citizen, Association of Community Organizations for Reform Now (ACORN), and the local Service Employees International Union (SEIU) waged an all-out assault on the plan. Ultimately, getting a citizen initiative passed requiring contracts would be subject to a public vote.

In 2002, Mayor Ray Nagin was elected and chose to press on with the privatization plans. However, in October 2002 the water board voted 6-5 (*PW*, December 2002) to reject all of the bids. In February 2003 Nagin solicited new bids, but after failing to garner enough response, Nagin threw in towel.

The city will now have to spend as much as \$650 million to upgrade and fix leaking sewer pipes, yet there has not been any discussion of how the city will finance these repairs. Certainly residents can expect double-digit rate increases.

And Ft. Lauderdale Picks it Up

In an attempt to streamline and downsize, city commissioners in Ft. Lauderdale, have begun examining which municipal services are appropriate to privatize. Additionally, the commissioners, headed by Mayor Jim Naugle, have established a list of criteria for determining the feasibility of privatization.

Staff will report back to the commissioners in early May on what can be privatized and how to do it. Some of the initial services being considered include park rangers, parking meter collections, installation and repair, parking operations, marine facilities, development plans review and inspections, community vision planning, water and sewer operations, and operating major recreation facilities like the International Swimming Hall of Fame, War Memorial Auditorium and the city stadium.

The initiative received unanimous support from the commissioners, who aim to conduct a major overhaul of how the city operates. The effort stems from a budget crunch that surfaced last year. The initiative could affect up to 1,000 employees, but these employees will also be allowed to bid on contracts. ■



Who, What, Where

Reason Studies

Reason's Offshore Outsourcing Resource Center: rppi.org/outsourcing/index.shtml

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Conferences

Workforce Excellence Summit, September 14-16, Washington, D.C.: workforceexcellence.org

State Policy Network 12th Annual Meeting, October 21, Austin, TX: spn.org

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