Privatization Watch

Not So Easy, After All—
Governments Enter the Telecom Business

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Privatization Watch

What is Government Sprawl?

by Ted Balaker

People who worry that government might be doing too much often point to the rapid growth in the size of government. And by that measure, government is indeed growing.

Reason's Editor-in-Chief Nick Gillespie and the American Enterprise Institute's Veronique de Rugy recently noted that George W. Bush has boosted non-defense discretionary funding more than even Lyndon Johnson.

But size isn't the only way to measure government growth. In this issue of *Privatization Watch* we focus on something else—scope. Government is engaged in a wider variety of activities than ever before. My colleague, Geoffrey Segal, calls this "government sprawl" because government spills into new ventures all the time. Long forgotten are James Madison's words that the federal government's duties are "few and defined." Today federal workers do all sorts of things from servicing cars to mowing lawns that, in modern jargon, just aren't "inherently governmental" functions (See "Keeping Private Private," p 7).
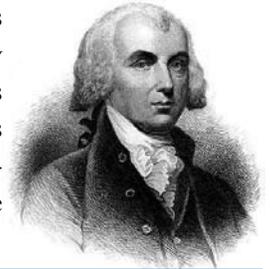
Long forgotten are James Madison's words that the federal government's duties are "few and defined."

And it's not just the federal government. State and local governments aren't content with schools, roads, police and the few other core duties that used to define what governments should do. Often governments compete directly with the private sector. Governments are building convention centers, financing hotels, golf courses, ski resorts, and cable TV (See "The $125 Million Question," p 6). They're even getting into the mapping business (See "Off the Map," p 8). And perhaps nothing is trendier these days than getting into the broadband Internet business (See "Governments Enter the Telecom Business" p 4). The mayor of San Francisco even calls high-speed Internet access a "fundamental right."

Everyone loves high-speed Internet, but what about the basics? Are schools as good as they could be? Are neighborhoods as safe as they could be? When government does many things, it's easy to lose focus. It's harder to do the important things right. ■

Privatization Briefs

L.A.'s Convention Center Hotel Flounders

Like so many others, Los Angeles' convention center is floundering. Each year it loses $1 million in operating costs alone, plus $30 million in annual debt financing for the initial construction.

What to do when government-sponsored revitalization doesn't turn out as planned? Cut your losses? Not in L.A.

In October the City Council agreed to provide $270 million in public subsidies for a hotel that would sit next to the down-town convention center. Yet that didn't stop Apollo Real Estate Advisors from getting cold feet. In November Apollo pulled itself—and the $60 million it was supposed to invest—out of the hotel project. *The Los Angeles Daily News* notes that the hotel project would survive only if AEG, the developer of the adjoining l.a. live entertainment-sports-condominium complex, finds another investor to fill the gap left by Apollo.

Unwiring Austin with Volunteers

Austin ranks third on Intel's list of America's Most Unwired Cities (behind San Francisco and Seattle). Yet this happened without a municipal program.

Much of the success stems from the efforts of the Austin Wireless City Project, a non-profit organization dedicated to spreading the availability of free wireless throughout the Austin area. They do it the way grassroots groups used to, through door-to-door visits and face-to-face persuasion.

Volunteers, called "walk-ers," visit coffee shops, res-taurants and other businesses where there is a solid level of traffic. Their pitch is that local businesses benefit from offering free Wi-Fi. Richard MacKin-non, president of the Austin Wireless City Project, told the *Austin Business Journal* that Wi-Fi users pumped an additional $500,000 into businesses participating in the Austin Wireless project last year. Austin business patrons are demanding free Wi-Fi, he says.

Austin City Wireless will assist any business or organiza-tion seeking to create a hotspot. It will designate a "network caretaker" to install and maintain a hotspot, and even provide necessary hardware from a pool of donated computers and equipment.

Participants are not limited to the stereotypical upscale bookstore or coffee house; its Web site lists 93 hot spots, which include several branches of the Austin Public Library, two movie theaters, a carwash and a collision repair shop.

While Philadelphia, Anaheim and other cities are turning to the private sector for wire-less, they still plan to institute larger municipal agencies to promote services. These agencies rarely match the enthusiasm and commitment of a community non-profit. In Austin, a few committed individuals who chose to leverage market mechanisms have accomplished far more already. Wireless initiatives elsewhere are targeting $20 a month for basic service and won't be online until next year. But how is that better than what has happened in Austin, where people already enjoy free service across a broad swath of locations?

Privatizing Welfare Application

After welfare-to-work processing was successfully priva-tized in the 1990s, the next step has been to privatize the pro-cessing of food stamp, Medicaid and welfare applications.

Texas is pushing ahead with such a plan. Privatization is expected to save the state $150 million a year and improve the quality of application review. The *Dallas Morning News* reports that call centers would replace many state eligibility offices. Those applying for aid would be encouraged to dial 211 and speak with operators who will help them assess their benefits qualifications. Aid applicants will also have the option of applying online or by mail or by asking for face-to-face interviews with an eligibility specialist. ■

Not So Easy After All:
Governments Enter the Telecom Business

By Adrian Moore

An increasing number of local governments are proposing either to build and operate broadband networks for residential and business use, or to develop broadband infrastructure for wholesale lease to commercial service providers, or otherwise take action to accelerate the availability of broadband Internet access throughout downtown areas.

But it's unclear what problem they are trying solve. Over a third of all American households already have broadband Internet service, which is over half of the households that use the Internet. Considering that mass use of the Internet is only about a decade old, the technology has amazing market penetration. And prices have been falling steadily.

Yet a 2004 survey found that 621 public power systems supply broadband services. About 23 municipalities offer fiber-optic service to the public. News reports claim that "hundreds of cities" are considering some type of municipal Wi-Fi. And San Francisco Mayor Gavin Newsom even declared free or low-cost wireless Internet access a "fundamental right." High-profile proposals in Philadelphia, San Francisco, Houston and other cities like Minneapolis have drawn a lot of attention (See "Cities Step Back," p 5).

Many argue that government deployment of broadband will spur economic development, attracting high-tech jobs and business investment. But government-subsidized broadband services actually discourage private investment, leaving less opportunity and incentive for private firms to enter the market. Just as bad, a great many government broadband systems lose money and drain local budgets while falling behind new technologies, so their service quality declines.

Townships, cities, counties and even states getting into the telecom business to compete directly against the private sector undermines technological progress and violates fundamental principles of American free enterprise. Most existing government broadband systems compete with private firms, or enjoy local monopolies, to the detriment of broadband consumers.

Many of the proposed city-wide wireless systems are less problematic. Cities like Anaheim, California, Houston, and even San Francisco now, are looking at proposals where a winning bidder will get access to city light poles and properties to install wireless antennas and other equipment in exchange for broad availability or low-cost services. Other companies can install competing systems if they so desire.

But there are organized activist groups diligently working to make sure that broadband services are provided by government agencies or regulated monopolies with taxpayer subsidies. They abhor market competition in broadband services and are aghast at proposals from Google and others to provide free wireless broadband services and make their revenue off of ads.

A large group of policy analysts have signed the Municipal Broadband Compact to establish principles for efforts to create citywide broadband access. The principles seek to maximize competitive private provision of broadband services and avoid monopolies and subsidies. Reason has published a list of over *50 Questions Public Officials Should Ask About Government Broadband Services* that will help officials evaluate the technical, economic, political, and legal aspects of municipal broadband proposals.

You can read the *Municipal Broadband Compact, the Questions Public Officials Should Ask About Government Broadband Services*, and a great deal of research and commentary on these issues at reason.org/wifibroadband/index.shtml.

Access to broadband can often be expanded by eliminating unnecessary regulations that delay, raise the cost, or even effectively ban the construction of new network facilities. The Compact recommends that in order to optimize broadband deployment:

1. Municipalities and other local units of government should be prohibited from investing in, managing or operating broadband infrastructure and services.

2. Congress should restrict the authority of states to regulate and tax broadband infrastructure and services in the interest of preserving interstate commerce.

3. Telecom taxes and cable franchise fees should be eliminated to encourage investment in broadband services. ■

Cites Step Back:
More Are Deciding Against Funding Wireless Networks

By Steven Titch

Minneapolis has become the latest major U.S. city to back off from funding a municipal wireless network, joining cities like Philadelphia and Anaheim that have turned to the private sector to build, operate and own their large-scale citywide wireless networks.

In November Minneapolis designated EarthLink and U.S. Internet, a ten-year-old nationwide ISP based in nearby Minnetonka, Minnesota, as finalists for a citywide Wi-Fi system that it aims to have in place by early next year. The two companies will now build pilot systems that the city will evaluate as part of its final determination. As the plan now stands, the winner will receive a contract to provide wireless telecommunications services to the city, and as part of the deal, gain access to city-owned right-of-way and be able to sell wireless Internet access to residences and businesses, as is the case in Philadelphia and Anaheim.

Each company is using different technology approaches. Whoever wins, however, will be given ownership of the network and will have the right to set terms for how wholesale and retail service is marketed or sold. The winner will ultimately compete with wireless service providers such as Sprint Nextel, Verizon Wireless and Cingular, as well as other independent Wi-Fi hot spot providers and aggregators.

Like Philadelphia and Anaheim before it, Minneapolis took a long hard look at the realities of network ownership. Significantly, its decision to back away from outright municipal ownership came after it examined the highly-touted municipal system in Chaska, Minnesota, an outlying Twin Cities suburb. While the city reports that 2,300 of 8,000 households have signed up for Chaska.net, David Pokorney, Chaska City Manager, told the *St. Paul Pioneer Press* that about one-third of the users complained about poor performance in the early months of operation. In the end, he said, optimization of the radio network contributed to a 50 percent increase in costs, from $600,000 estimated to $900,000. It looks like fears of those types of cost overruns, which would be proportionally higher in Minneapolis, led city leaders question the wisdom of funding the cost of the network.

Though far from ideal, Minneapolis's approach is still better than pouring city resources into a bureaucratic effort at competition that would likely muck up an otherwise fast-developing and competitive market in the Twin Cities. And unlike most city franchise agreements, such as cable TV, competitors will still be able to build their own networks and provide competitive services.

Why have cities changed course? The change started with Philadelphia, which ditched its original plan to create a city-owned wholesale broadband backbone and instead turned over the whole kit-and-caboodle to EarthLink. It is no coincidence that municipalities opted to shift risk, cost and operational responsibility to the private sector, after the release of several reports that took a closer look at municipal wireless.

One watershed moment in the municipal wireless trend was this summer's report from JupiterResearch examining the costs of municipal wireless systems. Its estimate that the average cost of building and maintaining a municipal wireless network is $150,000 per square mile over five years was twice as much as what municipal wireless consultants had been saying. JupiterResearch (jupitermedia.com/corporate/releases/05.07.06-newjupresearch.html) further predicted that half the current municipal wireless systems would fail to break even. It advised communities to seek private industry partners, structure a deal from which the city itself could derive value from the network as a large user, and pointedly warned against the idea of building wireless systems for the sole reason of providing consumer broadband Internet access.

Despite all the municipal wireless hype, it is gratifying that voices of knowledge and experience are being heard when talk of cost comes up. Take Andrew Seybold of Andrew Seybold Group. Seybold is a respected, long-time technology and marketing consultant with a specialty in converging mobile technology with data communications.

Like JupiterResearch, Seybold has concerns as to whether any type of reliable wide area service can be set up on unlicensed frequencies that Wi-Fi uses. His recent comments in *Wireless Week* are good food for thought:

> This is my issue. If you plan to spend millions of dollars on muni Wi-Fi, you will have to spend millions more to keep it running and to fix it when it breaks due to new interference. You cannot simply sweep an area, find places where there is no interference and install access points. There is no guarantee that tomorrow there won't be new access points that will affect your system.…

> Interference will be an ongoing issue, and coverage and data speeds will denigrate over time. Who will handle

The $125 Million Question:
How Will New Competition Affect Municipal Telecom Networks?

By Steven Titch

Soon you'll never have to worry about missing an episode of your favorite TV show again. In separate agreements, CBS and NBC will allow Comcast and DirecTV, respectively, to make shows from their nightly primetime schedule available for on-demand viewing.

That means if you still can't figure out how to use your digital video recorder (DVR) or you are hit by a power outage, you can order a missed episode of "CSI" or "Survivor" off an on-demand menu. Ditto for NBC programs and DirecTV.

"I think the floodgates have opened," Comcast CEO Brian Roberts told *The Wall Street Journal*. On-demand episodes will be available after they air in their regular time slot, the *Journal* reports. NBC and DirecTV are shooting for a price of 99 cents per episode.

The decision by the networks to go off the long-sacred primetime programming grid demonstrates their recognition of how content delivery is changing. Notably, the deals came just three weeks after ABC began making episodes of "Lost" and "Desperate Housewives" available for Internet download on Apple's iTunes podcasting service.

So what will they make of this in Lafayette, Louisiana, which this spring voted to leverage itself to the tune of $125 million to create a fiber-optic-based competitive cable TV, phone and Internet service? What does this mean for municipalities such as Ashland, Oregon; Bristol, Virginia; and Lebanon, Ohio; which continue to struggle financially against a growing number of competitors with growing menus of differentiated services?

In a phrase, more competitive pressure. The Comcast and DirecTV deals are just the beginning. No doubt similar content pacts between the networks and cable companies will follow in the weeks ahead. And they won't be cheap from a programming acquisition perspective. Networks have to consider the value of advertising they may lose. Yet at the same time, they need to retain viewership and the cable companies need to retain customers. For both sides, the value proposition was too good to pass up, especially as telephone companies such as Verizon and SBC roll out video service of their own.

Municipal systems, some of which do not yet offer HDTV or DVRs, will find themselves caught in the crossfire. It's doubtful they have the financial resources to answer competitively. Still, they might say that video-on-demand, even for missed TV episodes, is a premium service and their mission is to serve low-end customers with economical alternatives.

All well and good, except wireless service providers, such as Sprint Nextel and Verizon Wireless, have reached the point where their networks also can support large Internet downloads, including video. Now a cell phone may not be the best platform to watch "Smallville," let alone "Lord of the Rings," but that's not the point. Wireless is becoming a viable commercial alternative for Internet access because it can now better accommodate content delivery. It's not lightning-fast 30 Mb/s cable, but it's not dial-up either. Cities that once thought they would have to build and own their municipal networks have been happily besieged by the likes of EarthLink, HP and Google eager to do the job themselves. It's been true from the beginning—applications and content drive broadband access.

The people of Lafayette voted to fund a $125 million municipal broadband project in the mistaken belief that, some 24 months down the line, the competitive situation in their community would be the same—that Lafayette Utilities System would enter the market as a third company that could compete with Cox and BellSouth solely on the basis of price. By the time LUS gets its system up (if it doesn't reconsider the idea outright), Cox and BellSouth could be the least of its problems.

In the months since the nationally watched vote in Lafayette, we've seen moves by the likes of Yahoo and Google into the low-end market for Internet access. Meanwhile, eBay has purchased VoIP provider Skype. At the high-end, we see strategic agreements like today's Comcast and DirecTV deals that will keep current customers on board.

Moreover, Lafayette straddles the regions hit hardest by

Keeping Private Private

By Geoffrey F. Segal

Over the years the federal government has expanded into hundreds of activities that are commercial in nature. Many of these are support functions that service the bureaucracy. These functions are not inherent or unique to government, but rather they can be found in the Yellow Pages in virtually every town in America. The feds have gone beyond support functions and opened up new services that directly compete with the private sector.

Upon entering office, President Bush attempted to expand the widely successful practice of "competitive sourcing" that has been used by previous administrations to deliver savings to the American taxpayer. Bush's plan was simple: require federal agencies to subject commercial activities of the government to market-based competition.

Several years earlier, Congress passed the Federal Activities Inventory Reform (or "FAIR") Act, requiring agencies to classify jobs as either "commercial" or "inherently governmental," and identifying more than 800,000 federal employee positions that could be provided by the private sector. These commercial activities—operated by a federal executive agency and providing a product or service that could be obtained from a commercial source—include such positions as computer programmers, landscapers, veterinarians, photographers, construction workers, laundry workers, printers, auto repairmen and drivers. Competitive sourcing requires agencies to compete these functions against the private sector, with the provider offering the best value to the taxpayer—regardless of whether that provider is the government or a private firm—winning the right to do the work. Since the government's in-house incumbent has to modernize and economize in order to beat the private sector, the taxpayer wins regardless of whether the work stays in-house or gets contracted.

While this is good, it unfortunately has been stalled by Congress. What's worse, perhaps, is that this policy represents a fundamental shift in thinking about what government should and should not do. This past January represented the 50th anniversary of President Eisenhower's budget bulletin that proclaimed:

In the process of governing, the Government should not compete with its citizens. The competitive enterprise system, characterized by individual freedom and initiative, is the primary source of national economic strength. In recognition of this principle, it has been and continues to be the general policy of the Government to rely on commercial sources to supply the products and services the Government needs … The Federal Government shall rely on commercially available sources to provide commercial products and services … the Government shall not start or carry on any activity to provide a commercial product or service if the product or service can be procured more economically from a commercial source.

The key here is that Government should not be in competition with its citizens.

It's also time to reevaluate competitive sourcing. Currently the in-house team is winning 91 percent of the competitions. Just four years ago, before a tweak to the governing rules, the split was typically 50-50. This tremendous shift suggests that something is terribly awry.

The key here is that Government should not be in competition with its citizens.

For competitive sourcing to work and deliver benefits, the executive branch needs to use it. The next administration may not see as much value and could scrap the plan altogether. That's why it's important to start asking the fundamental questions now, before it's too late.

A renewed effort should be established—one that stops government from competing against the private sector. It could be modeled after the White House Office of Privatization or the Office of Private Sector Initiatives in the U.S. Department of Transportation's Urban Mass Transit Administration (UMTA) established by President Reagan in the 1980s.

This office would not focus simply on competitive sourcing, but a wide range of strategies for creating opportunities for the private sector, small business and individual entrepreneurs by empowering free enterprise, rather than competing with or

Off the Map:
Government Competes With Private Mapping Firms

By Leonard Gilroy

Government-sponsored competition in the provision of aerial photography and mapping services is causing a great deal of concern among private sector geospatial service providers. Universities and state government agencies are competing with private mapping firms in a variety of ways, ranging from increasing capabilities for in-house mapping services to direct competition with private professional firms in the commercial market.

Government-Sponsored University Competition

Schools of higher learning are increasingly venturing away from their core missions of education and conducting basic research. Facing significant financial pressures—ranging from reduced government funding to pressures to limit tuition increases—universities are generating revenues from commercial activities to supplement their budgets. Exemplifying this trend, taxpayer-supported universities are entering the mapping, remote sensing and geospatial business by selling services in the commercial marketplace, creating a new form of unfair government-sponsored competition.

Since the 1930s, mapping has been routinely identified in various government investigations as a community subjected to unfair competition from government-sponsored entities. University competition in the commercial market is not unusual; in fact, it is becoming the norm. At a recent Management Association for Private Photogrammetric Surveyors (MAPPS) conference, more than 80 percent of attendees indicated they have encountered competition in the marketplace from universities. In a recent MAPPS poll, over 85 percent of respondents indicated that university competition was an issue they felt deserving of public policy attention. A 1980 report by the Small Business Administration also singled out universities as a major source of taxpayer-supported, unfair competition with private companies, particularly small firms.

Universities enjoy significant advantages over for-profit companies. Specifically, they:
- are eligible for billions of dollars in grants from federal and state governments;
- often have the ability to secure non-competitive, sole-source contracts with government agencies;
- pay no taxes;
- benefit from "free" overhead—buildings, electricity, and equipment;
- have access to a student labor force that is either unpaid or compensated well below prevailing market wages;
- carry no professional liability insurance, do not have to pay unemployment compensation, and are often exempt from social security contributions;
- usually insist on "best effort" clauses when they enter into contracts to perform services that absolve them of ever completely finishing a project; and
- receive millions of dollars in free or discounted hardware and software, donated from vendor firms.

University Competition in Geospatial Service Provision

In 1997, The Ohio State University's Center for Mapping embarked upon an effort to develop a high-resolution digital camera to take aerial photographs for use in mapping. Diverging from its core academic mission, the university was preparing to go into the digital aerial photography business and sell its services in the commercial marketplace. It even commissioned a marketing study to identify potential clients, determine the size of its market, and recognize potential competitors.

Another blatant example of university competition with the private mapping community is North Carolina State University. NCSU is engaged in the commercial production of electronic image-based maps (known as digital orthophotos) for the National Park Service (NPS). Procurement announcements for aerial photography issued by the NPS include specific instructions that the photos are to be delivered to its contractor, NCSU, for the professional value-added process of creating digital orthophotos. There is neither research nor education value to the NCSU operation. The services performed are widely available from dozens of private firms and involve processes and techniques resident in numerous commercial enterprises.

Finally, the University of Florida has purchased fully equipped aircraft and LIDAR (light detection and ranging) sensors. LIDAR was a NASA program that was commercialized over a decade ago. Government agencies at the federal, state and local level, as well as private clients, retain private firms to provide commercial LIDAR services on a regular basis. Yet the University of Florida, in partnership with the University of California at Berkeley has been awarded National Science Foundation (NSF) funding for the establishment of a National Center for Airborne Laser Mapping (NCALM).

The private sector believes NCALM is inappropriate for NSF

Florida DOT Competes With Private Sector Mapping Services

By Leonard Gilroy

As government-supported universities compete with private sector mapping services (see "Government-Sponsored University Competition in Mapping Services" p. 8), they aren't alone. Government agencies themselves are getting in on the act, with Florida leading the way. (See "Building Highways or Bureaucracies", *Privatization Watch*, Vol. 28, No. 5, 2005, page 14.)

The Florida Department of Transportation (FDOT) consolidated its survey, mapping, and aerial photography divisions under its new Surveying & Mapping Office. The stated justification for this consolidation was the purchase of a whole suite of Z/I Imaging products, culminating in the purchase of a new, state-of-the-art digital mapping camera (DMC) in late 2003.

FDOT claimed that the DMC purchase would allow it to alleviate the demands on its schedule for aerial photography missions, as well as provide mapping services for other state agencies. But this provision of aerial mapping services is in direct competition with private firms operating in Florida that provide the same services.

Under the administration of Gov. Jeb Bush, the Florida state government has taken significant steps toward less state government and more privatization of state services through its Commission for Efficient Government. It appears that activities of FDOT are not in keeping with the governor's strategic mission and spirit of thinking regarding outsourcing and government efficiency.

In fact, there are several capable and qualified private firms that can get the job done in Florida. There are 11 firms on the Department of Revenue (DOR) pre-qualified list of licensed, professional firms. Six of these firms have digital cameras. There are eight firms pre-qualified under service code 8.3 (photogrammetry) with FDOT and four of these firms are not on the FDOT list.

It would be difficult for a state-owned and operated aerial acquisition operation to be competitive compared to private companies. Since the demand for public services is growing and government resources are limited, it is in the best interest of state agencies to use the services of private vendors. This creates a win-win for both government and companies that are located in, and provide employment and tax dollars to, the state. State govern-ments benefit from market competition among firms and schedule flexibility, while private firms generate tax revenue.
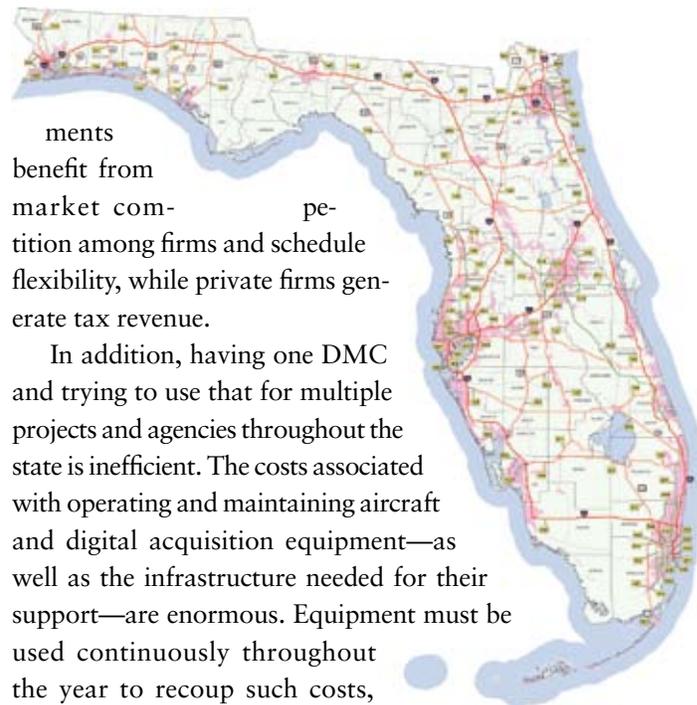
In addition, having one DMC and trying to use that for multiple projects and agencies throughout the state is inefficient. The costs associated with operating and maintaining aircraft and digital acquisition equipment—as well as the infrastructure needed for their support—are enormous. Equipment must be used continuously throughout the year to recoup such costs, leading private contractors to fly aerial missions nationwide to consistently accommodate region-specific "windows of opportunity." (Aerial photography for mapping can only be captured in good weather and when leaves are off trees, sun angle is high in the sky, cloud cover is minimal, and other factors to minimize shadows are prevalent.) This gives private vendors the competitive edge over state agencies that operate in a constrained geographic area. In Florida, the window of opportunity for aerial photography is limited by these factors, yet hundreds of aerial missions must take place. Given the size of their workload and the restricted time horizon, state agencies need the flexibility to acquire imagery through their contracting mechanisms in order to fulfill their own project schedules and demands, rather than carrying the overhead cost of attempting to maintaining its own aircraft, camera, crews and other infrastructure to meet its own project requirements.

With respect to quantifiable time savings in overall production—which translate directly into taxpayer savings—the financial implications to FDOT and/or other state agencies in maintaining aircraft and providing mapping services is unclear. There is a real potential for these costs to far exceed the projected savings.

It has even been reported that FDOT has not maximized the use of its DMC due to mechanical problems with the aircraft in which the DMC is installed. To remedy this problem, it is alleged that FDOT is now planning to purchase a new aircraft.

Massachusetts Tries to Ban Water Privatization

Testimony by Geoffrey Segal

What follows are portions of recent testimony given by Geoffrey Segal, Reason's Director of Government Reform, before the Massachusetts Joint Committee on Environment, Natural Resources and Agriculture. At issue was a bill that would ban water privatization in Massachusetts. The entire testimony is available online: reason.org/commentaries/segal_20051024.shtml

More than 40 percent of drinking water systems in the United States are private, regulated utilities—more than 25,000. Of the remaining systems, more than 1,100 local governments have entered into a public-private partnership and contracted out the operations and maintenance (O&M) to a private company. In addition, another 1,300 communities have contracted out wastewater operations.

Several factors have been driving the shift toward private operation of water and wastewater systems. For example, officials struggle to meet more stringent environmental requirements and to replace decaying infrastructure. Population growth poses additional challenges. Extending systems either to cover more area or to handle increased demand is costly and complicated.

Local government surveys have found that public officials turn to privatization in response to fiscal crisis and/or when privatization has been shown to work in other jurisdictions. According to the U.S. Conference of Mayors, four out of ten cities are actively considering privatization in order to reduce costs and attract private capital investment.

So how does private sector participation in water and wastewater systems affect quality? If anything, privatization improves quality. Indeed, it was President Clinton's Environmental Protection Agency that endorsed private participation as a means by which local governments can meet environmental standards. The EPA wrote, "[Privatization case studies] provide concrete examples to local officials of how successful partnerships and other models can be used by communities to provide needed environmental services more efficiently. They also show how public-private partnerships can be used as a way to provide substantial benefits to both the public and private sectors, creating the classic 'win-win' situation."

Furthermore, a recent study released by the Brookings Institution and the American Enterprise Institute found that public systems are somewhat more likely to violate maximum levels of health-based containments allowed under the Safe Drinking Water Act (SDWA).

Private participation can also save municipalities money. Indeed, the AEI-Brookings study found that as the share of private ownership went up, the average household expenditures on water went down. In addition, a 1999 study examined public-private partnerships in water and wastewater systems in 29 cities serving over three million customers throughout the United States. It found that all of the privatizations resulted in lower rate increases than were planned prior to privatization, and at 17 percent (five) of the facilities, public-private partnering brought cost savings of between 10 percent and 40 percent, allowing local governments to avoid large increases in water rates.

> More than 40 percent of drinking water systems in the United States are private, regulated utilities.

Case studies of savings abound. The EPA has collected a set of case studies where cities were able to meet water quality standards more efficiently thanks to privatization. Contract renewal rates are also indicative, since privatization is primarily motivated by communities seeking cost savings. That 17 out of 20 privatization contracts are renewed at the end of their term indicates that communities are satisfied with the savings being achieved.

One argument often used against water and wastewater privatization is that water is so vital we can't trust it to the market. This is a conceptual rather than a research question, but grounded in basic facts about our lives in the United States. Yes, water is vital, and along with most other vital things, the market has proven exceptional at providing it. The closest analog is food, which the market provides, as it does medicines and healthcare. Our government hires contractors to maintain the airplanes that transport the president, to run the space shuttle, to guard our nuclear power plants, and to build, maintain, and often operate submarines, fighter jets and other high-tech weapons systems.

The sheer track record of water and wastewater privatization, with thousands of satisfied communities, reveals concerns over privatization to be mainly rhetorical, rather than factual. Government remains responsible for establishing and enforcing quality and reliability standards and contractors have every incentive to ensure the same. Just as with government-run facilities, employees and managers, and their families, live in the community and are customers of the services they provide. ∎

FAA Outsources Flight Service Stations

By Robert W. Poole, Jr.

On October 4, 2005, Lockheed Martin took over the operation of the Federal Aviation Administration's network of Flight Service Stations, in one of the largest non-Defense outsourcings to date under the provisions of OMB's A-76 process. It involves 58 facilities around the country, which provide flight-plan and weather-briefing services to private pilots. The technology used at these facilities was obsolete, very labor-intensive (most such services can easily be provided on-line, rather than by voice over the phone), and there is no particular reason why there were 58 such stations scattered about the country. Moreover, the cost of the program was in excess of $500 million per year.

In early 2005 the FAA announced Lockheed Martin the winner of the hard-fought competition. One of the other bidders consisted of the current employees and Harris Corporation—the so-called "Most Efficient Organization" approach (internal restructuring of a government agency in the face of real competition). The others were all aerospace contractors. By consolidating the program into 20 facilities instead of 58 and equipping them with state-of-the-art equipment to maximize on-line services, Lockheed Martin was able to bid $1.9 billion over 10 years (an average of $190 million per year, versus more than $500 million yearly today). Net savings, after transition costs, should be about $2.2 billion. There will be no more "walk-in" briefings for pilots, but only 2 percent of pilots got their briefings that way in any case. The principal private pilot group, Aircraft Owners & Pilots Association, supported the competition from day one, and cheered the results in its publications and on its Web site.

Net savings, after transition costs, should be about $2.2 billion.

As for the 2,500 existing staff, Lockheed Martin expects to downsize with minimal layoffs. Nearly 1,900 of the current employees accepted offers from the company. The process will take advantage of the fact that about half the staff will become eligible to retire over the next several years, as the consolidation takes place (by March 2007). In addition, the FAA encouraged those who were qualified to apply to become air traffic controllers (where thousands need to be hired over the next decade to replace upcoming retirees). And the FAA also encouraged transfers to other vacancies within its Air Traffic Organization.

Getting the contract implemented involved overcoming several hurdles. First, the Most Efficient Organization team filed a formal protest, which was resolved in the FAA's favor. Next, the House accepted an amendment to the transportation appropriations bill to prohibit the FAA from spending any money on implementing the contract. (This reflected intense labor union lobbying, as well as some "jobs-in-my-district" protectionism by some House members.) No such amendment was offered in the Senate, so the matter had to be resolved in the conference committee, which took place late in November, more than six weeks after Lockheed Martin took over. The final bill eliminated the House language, though it did impose some additional procedural steps for future outsourcings.

Overall, then, this is an impressive victory for competition—and better service to private pilots. ■

PART of the Solution:
Performance Budgeting at the Federal Level

By Adam B. Summers

The Bush administration has been taking heat from Republicans and Democrats alike recently for the federal government's lack of fiscal restraint and responsibility. According to a recent Heritage Foundation article, "Federal spending has surged 33 percent since 2001 to a peacetime record of $22,000 per household." Given this, and numerous examples such as the pork-laden 2005 highway and transportation bill, it might surprise some to hear that there is an ongoing effort in the executive branch to identify wasteful or poorly performing government programs, and to adjust their funding accordingly. Yet Congress is not doing all it can to implement these common-sense solutions.

Background

While there has been some interest in using performance information in the budgeting process at the federal level for decades, one of the more significant recent attempts to incorporate this tool was embodied in the Government Performance and Results Act of 1993 (GPRA). GPRA requires agencies to develop performance measures and collect information to evaluate federal program effectiveness and efficiency. It furthermore requires agencies to publish activity-based strategic and annual plans so that results can better be linked to appropriations decisions.

The Office of Management and Budget (OMB) took things a step further when it developed its Program Assessment Rating Tool (PART) to evaluate programs based on their purpose, strategic design, management, and results. PART was created in 2002 and is a central component of the president's management agenda. OMB takes these assessments into account while reviewing agency budget requests, and the results are reported in the president's budget submission to Congress.

The PART analysis is a methodological, standardized, and evidence-based evaluation offering hard data on whether federal programs are doing what taxpayers are paying for them to do and assessing whether they are being managed properly. In each of the last three years, PART reviews have examined one-fifth of the federal government—60 percent of the federal government has been analyzed to date—and the administration expects to complete reviews of the remainder of programs by 2007 when the president submits his fiscal year 2008 budget proposal to Congress.

PART investigates the most important aspects of performance. It enables managers to paint an in-depth picture of just what exactly they are achieving, or if they are achieving anything at all. Agencies are scored as either "Effective," "Moderately Effective," "Adequate," "Ineffective," or "Results Not Demonstrated." Ratings are made based upon agencies' responses to a series of roughly 25 questions (different types of programs may have some additional questions). The assessment includes questions such as:

- Is the program purpose clear?
- Is the program designed so that it is not redundant or duplicative of any other federal, state, local, or private effort?
- Does the agency regularly collect timely and credible performance information, including information from key program partners, and use it to manage the program and improve performance?
- Does the program use strong financial management practices?
- Has the program demonstrated adequate progress in achieving its long-term performance goals?

Recent Results

For 2005, barely 40 percent of the 607 programs analyzed received "effective" or "moderately effective" scores. The ratings were broken down as follows: 15 percent "effective," 26 percent "moderately effective," 25 percent "adequate," 4 percent "ineffective," and 30 percent "results not demonstrated."

The Management Scorecard uses similar ratings but, at the federal level, PART represents a clearer link between an agency's rating and its budget. According to the Government Accountability Office (GAO), "OMB, through its development and use of PART, has more explicitly infused performance information into the budget formation process and increased the attention paid to evaluation and performance information."

In the president's fiscal year 2006 budget proposal, "effective" programs enjoyed an average budget increase of 3.1 percent, "moderately effective" programs achieved an average increase of 2.5 percent, and "adequate" programs saw an average increase of 1.64 percent, while "ineffective" programs were cut by a dramatic average of 19.7 percent. The cuts to "ineffective" programs could have been twice as great, but some of the savings was diverted to other programs. Funding for programs designated "results not demonstrated" was cut an average of 1.5 percent.

Oftentimes, PART recommendations address program performance and management issues, rather than funding

issues. In fact, 82 percent of PART recommendations for fiscal year 2004 concerned program assessment, design, and management; only 18 percent were directly related to funding concerns. As a January 2004 GAO report notes, PART recommendations illustrated program deficiencies—and offered solutions—for programs such as the Department of Health and Human Services (HHS) and the Department of Labor:

OMB and HHS officials agree that the foster care program as it is currently designed does not provide appropriate incentives for the permanent placement of children; the program financially rewards states for keeping children in foster care instead of the original intent of providing temporary, safe, and appropriate homes for abused or neglected children until children can be returned to their families or other permanent arrangements can be made. The PART assessment provided support for OMB's recommendation that legislation be introduced that would create an option for states to participate in an alternate financing program that would "better meet the needs of each state's foster care population."

Performance information included in the PART for the Department of Labor's (DOL) Community Service Employment for Older Americans program helped to shape OMB's recommendation to increase competition for the grants. OMB concluded that although the Older Americans Act of 2000 amendments authorize competition for grants in cases in which grantees repeatedly fail to perform, the programs' 10 national grantees have historically been the sole recipients of grant funds regardless of performance. OMB recommended that DOL award national grants competitively to strengthen service delivery and open the door to new grantees.

Other programs marked for improvement by virtue of their "ineffective" PART scores for FY 2006 include the following:

Department of Education
- Even Start
- Federal Perkins Loans
- Safe and Drug Free Schools State Grants
- TRIO Upward Bound
- Vocational Education State Grants

Department of Health and Human Services
- Health Professions
- Substance Abuse Prevention and Treatment Block Grant

Department of Housing and Urban Development
- Community Development Block Grant (Formula)
- Project-Based Rental Assistance
- Rural Housing and Economic Development

Department of Labor
- Migrant and Seasonal Farmworkers
- Trade Adjustment Assistance
- Youth Activities

Department of the Treasury
- Earned Income Tax Credit (EITC) Compliance

Environmental Protection Agency
- Alaska Native Villages
- Pesticide Enforcement Grant Program

Congressional Roadblocks

In order for PART to be truly effective, of course, Congress must act on the OMB's recommendations. For a number of reasons, it has been reluctant to do so. An October 2005 GAO report concluded that PART was effective at getting government agencies to focus more on program performance, but that more must be done to engage Congress in the evaluation and budgeting processes. In a subcommittee hearing held in June, Comptroller General David Walker testified that while PART scores have provided a wealth of information about federal government program performance, spending patterns and congressional program oversight have remained largely unchanged.

Congress has a regrettable history of ignoring solutions to reduce government waste. The 1984 Grace Commission report on government waste and the recommendations of then-Vice President Al Gore's National Performance Review of 1993-1995 were summarily discarded by legislators despite their many merits. In its FY 2005 appropriations bills, Congress provided funding for all but one of 13 programs the administration had recommended eliminating due to their "ineffective" or "results not demonstrated" PART scores.

The problem is that legislators simply do not have incentives to reduce government waste. Voters often reward their local legislators for "bringing home the bacon," blissfully ignorant of the fact that the "benefits" won for them are inconsequential compared to the costs they must bear for the pork doled out to the other 49 states or 434 legislative districts. Thus, even purportedly fiscal conservative legislators frequently engage in vote trading, or "logrolling" ("I'll vote for your pork-barrel project if you vote for mine"), to obtain their pet projects

duplicating it. The office would look at ways in which direct conversion, contracting out, vouchers, asset sales and leases, public-private partnerships, privatization, divestiture, and other instruments could transfer activities from the government to the private sector.

Furthermore, it could help identify and implement methods of developing, supporting and promoting private sector leadership and responsibility for performing government activities that are commercial in nature, where private sector performance makes better sense, and where such performance enhances services to meet public needs. It could make recommendations for appropriate action by the president to foster greater public-private partnerships and to decrease dependence on government for programs, activities and services that can be better performed in the private sector. It could serve as a focal point for private sector action addressing government's needs. Moreover, the office could develop methods of increasing public awareness of the importance of public/private partnerships, removing barriers to development of effective use of the private sector, and eliminating government activities that duplicate or compete with the private sector.

Ending government competition will create new jobs, save tax dollars, re-focus government and tax revenues.

Among the areas the office would explore are those agencies or programs that have completed their intended purpose and can now be left to the private sector to perform in the free market, those that are now more inefficiently performed in government and which can provided a better level of service if performed by the private sector, or those where the program or activity provides a personal benefit or the benefit of a special interest group that can be otherwise transacted in the private sector, free market economy rather than through the government. The Performance Assessment Rating Tool (See "PART of the Solution," page 13) provides a foundation for making this analysis.

Congress and this administration should recommit themselves to ending government competition. Doing so will help small firms grow and create new jobs, save tax dollars, and, at the same time, re-focus government and tax dollars on important inherently governmental functions—those which only government can perform—to address higher priority national needs. ∎

and programs. Special interests, upon which incumbent and aspiring candidates typically rely for a significant portion of their campaign funding, also play a significant role in the ever-growing nature of the government bureaucracy.

Despite the challenges of overcoming these strong incentives, there are proposals intended to get legislators to refocus on program results and priorities. Sunset commissions could continually evaluate programs to determine if they are ineffective, have outlived their purpose, are duplicative of other programs, or are otherwise wasteful. Greater use of sunset provisions in authorization legislation would force agencies and programs to justify their existence more frequently. In addition, the military Base Realignment and Closing (BRAC) process, which has been successful in minimizing logrolling behavior by forcing legislators to vote up or down on an entire set of recommendations, rather than voting on each individually, might be similarly utilized for program reduction/elimination recommendations.

Conclusions

The PART process has been a valuable tool in generating the information necessary to determine whether or not a government program is being managed well and achieving its goals (information that, astonishingly enough, did not previously exist in many cases). It has had limited success in tying program performance to funding levels, although congressional foot-dragging has hampered these efforts.

Some have complained that the PART process allows the administration to substitute its program priorities for those of Congress, and that the executive branch is trying to encroach upon the powers of Congress to assess, authorize, and appropriate funds for government programs. Yet, given that Congress has thus far reneged on its responsibility to oversee the programs it regularly funds, the administration's efforts to inject some fiscal responsibility into the federal budget are welcome indeed.

Further improvements, such as the creation and utilization of sunset commissions and the adoption of a BRAC-like process for the elimination or reduction of ineffective or wasteful programs, would lead to greater fiscal responsibility in an era where government spending is greatly outpacing government revenues.

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MAP

funding, is behind the development curve and is a wasteful and duplicate expenditure of scarce federal taxpayer funds. Moreover, the Center is engaged in unfair university competition, subsidized by the federal government, to the disadvantage of the private sector. Since 1955, it has been government policy that the "federal government will not start or carry on any commercial activity to provide a service or product for its own use if such product or service can be procured from private enterprise through ordinary business channels." The Center's expenditure of federal funds violates this policy.

Of particular objection is the participation of the University of Florida in the Center. The university has a long history of being engaged in unfair competition with the private sector, conducting numerous, production-oriented LIDAR projects. There is no pretense of education or research to what the University of Florida does with its LIDAR capability. It openly provides commercial, production services on projects, in direct competition with the private sector.

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FLORIDA

It is not clear whether this acquisition was anticipated when the DMC was purchased and whether the cost of the new aircraft was factored into the justification for purchasing the DMC, rather than contracting with the private sector for digital aerial photography.

FDOT's decision to compete with private sector aerial mapping firms contrasts sharply with recent actions taken in other states. Over the last several years, the Texas Department of Transportation (under then-Governor George W. Bush), the Tennessee Department of Transportation, and the Tennessee Valley Authority have each decided to contract with private sector firms for aerial photo and mapping services.

To date, few other states have followed FDOT's lead, but Florida's precedent could lead to similar activities in other states, intensifying unfair government competition with private enterprise.

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NETWORKS

Hurricanes Katrina and Rita. As a result, telecommunications infrastructure improvement may get a well-needed boost from an industry dying to try out new technologies and protocols. In fact, the eastern Gulf Coast could become the biggest U.S. test bed for low-priced wireless Internet access—funded not by local municipalities, by the private sector and, ironically for die-hard advocates of municipal ownership, the federal government.

Amid all this upheaval, where does a highly leveraged, highly localized municipal operation fit? How will Lafayette taxpayers, or their counterparts in Ashland, Bristol and Lebanon, feel about going in hock at up to $1,000 per household for an uncompetitive, money-losing cable TV service while neighboring towns end up with what everyone wanted all along—a cheap alternative for basic broadband Internet access—without floating a single taxpayer dime? Call it a $125 million question.

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CITIES

customer support calls? Who will be available to answer questions about getting configured and on line? Who will spend the time and money to educate people about the potential hazards of a non-secure, non-encrypted connection to the Internet?...

There are plenty of questions I have not seen answered anywhere except by bidders assuring city fathers that it will be built and it will work as advertised....

The questions I am raising should be addressed by city leaders before moving forward. If they think they will have a clear shot at this spectrum, they are sadly mistaken. If they think they will not need customer service, they are sadly mistaken. If they think the networks, once built, will continue to function and provide years of trouble-free service, they are equally mistaken.

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Who, What, Where

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