



Privatization Watch

Analyzing privatization developments since 1976

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Privatization Watch

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Cleaning House with Comprehensive Reform

Ideally, “spring cleaning” should be confined to just one season. But the longer clutter and chaos are allowed to grow, the longer it takes to clean it all up. When governments muster the courage to clean house, it usually comes only after a prolonged period of procrastination. And so, the cleaning process takes a very long time.

A year ago *Privatization Watch* reported on how many state governments found themselves buried in one fiscal mess after another (see rppi.org/pw323.pdf). One of the few bright spots then was the e-Texas program, which examines state government operations each year and recommends cost savings. The program has saved billions of dollars and continues to do so.



Today, more states have decided to take action. And just as homeowners wouldn't clean out one drawer of one desk and say their house is in order, state leaders increasingly recognize that reform plans work best when they're comprehensive. Some states, like Florida, have stepped up longer running efforts (see “Efficiency at the Gate,” page 5). Others, like California, moved toward comprehensive reform only recently, and only after staring fiscal calamity in the face (see “The Bodybuilder's Guide to Government Reform,” page 4).

Still others are ramping up their efforts. In South Carolina, Gov. Mark Sanford (right) promoted five privatization projects during the last budget cycle, and Virginia passed the Competitive Government Act, which requires every state agency to analyze its workforce and identify competition opportunities.



Federal reform has faced tough resistance, but continues nonetheless (see “Battered but Breathing,” page 7). And, as “What's in the Government's Attic,” (page 8) notes, there is still much more to be done.

Ted Balaker
Editor

Privatization Briefs



Hooray

A year after Amarillo, Texas began offering it to private buyers, local officials have discovered that the sale of helium has generated enough revenue to justify a tax cut. The long-derided government stockpile of helium, begun in 1925, was authorized to be sold off by the Helium Privatization Act of 1996, authored by Rep. Chris Cox (R-CA). 2003 was the first year the Amarillo helium plant sold helium to private buyers.

Under the law, the Bureau of Land Management must sell off the entire stockpile between 2005 and 2015. The total proceeds are expected to be \$1.8 billion, ranking this among the largest federal privatizations (along with spectrum auctions, Conrail, the U.S. Enrichment Corp., and the Elk Hills Petroleum Reserve).

The government began the helium reserve when the War Department envisioned creating a fleet of fighter blimps. Naturally, the program survived long after the government abandoned plans for the fleet.

UN: Don't Worry About Outsourcing

The United Nations recently weighed in on offshore outsourcing, and, like many other research reports on the matter, it is decidedly less alarmist than the magazine cover stories that ask, "Is your job next?" The report noted that "the global shift in services offers large potential benefits for countries at both ends of the process."

The authors reinforce other themes noted in earlier reports: the magnitude of outsourcing is small, outsourcing is not just about saving money, most outsourcing remains a domestic matter and efforts to curtail offshore outsourcing "would likely destroy rather than save jobs in developed countries."

"World Investment Report 2004: The Shift Towards Services" is available online: unctad.org

Americans Gain, but not Germans

Recently, the McKinsey Global Institute explored offshore outsourcing's impact on national economies. Turns out that for every \$1 offshored from the United States, the U.S. economy gains \$1.12-\$1.14. This thanks to our flexible and relatively free labor markets.

McKinsey's analysis shows the gains are comprised of:

- a lot of savings for customers and investors;
- a fair amount of new production from re-deploying labor to other efforts; and
- a bit of gain from imports and increased transfers (insourcing) from the nations to which we offshore.

On the other hand, in Germany for example, restrictive labor markets lead to a very different outcome. McKinsey's analysis shows that for every euro offshored from Germany, the German economy gains only 0.80 euros.

Why? According to McKinsey it is due to "the limited ability of German workers to find new jobs." If the rate of re-employment matched that in the United States, offshoring would create 1.05 euros of value for the German economy for every euro of corporate spending offshored.

NYC Aiming for \$1 Billion in Sales

New York's Metropolitan Transportation Authority hopes to raise \$1 billion by selling or leasing many of its 14,000 properties. *The New York Times* reports the properties include train stations, commuter parking lots, and maintenance yards. At several Metro-North railroad stations the authority plans to retrofit large portions of the buildings for commercial use, noting that the distinct antique stations offer businesses an "excellent opportunity to quickly create an acknowledged presence in each community."

The authority will also turn to the private sector to market the properties, a practice outlined recently in the *PW* interview "Selling Smarter," available online: rppi.org/pw325.pdf.

For daily *Privatization Briefs*, visit: rppi.org/outofcontrol ■



The Bodybuilder's Guide to Government Reform

By George Passantino



Arnold Schwarzenegger's best-selling *New Encyclopedia of Modern Body Building* has inspired up-and-coming body builders the world over, providing practical advice on everything from nutrition and workout regimens to psyching out your opponents and effective posing. Who would have thought that it would also inspire me as I served as a Director of Governor Schwarzenegger's historic California Performance Review, which aimed to cut the flab of state government?

In the *Encyclopedia*, Schwarzenegger describes how, if you apply a 15-horsepower load to a 10-horsepower motor, the motor will eventually burn out. In contrast, over time the human body will change from a 10-horsepower motor to a 15-horsepower motor, getting stronger to achieve greater results.

This is the same way that we should think of government and why the California Performance Review is so important.

In recent years state expenditures have routinely outpaced state revenues and we are told that our only choices to confront this are to raise taxes or to cut vital services and watch our quality of life erode. This mindset treats government like a motor that is static and can only produce X amount of services for Y amount of taxes.

The bodybuilding philosophy of government, by contrast, sees government instead like the human body—dynamic, resilient, and able to become more efficient, doing more with less.

Using this framework, the California Performance Review is a tour de force directly confronting business as usual, and offering up a healthy lifestyle change to the Sacramento status quo. The report identified \$32 billion in savings that can be achieved over five years.

As with bodybuilding, the pain of government reform is at its worst getting rid of the initial flab, and there is plenty of flab in California. And the difficult process of change is the reason that many special interests in Sacramento are concerned about CPR. Getting on the treadmill is uncomfortable—particularly when you are so comfy on the couch. But by applying the key lessons of bodybuilding, we can build a leaner, healthier, and more efficient state government.



Reason's George Passantino with Governor Schwarzenegger

Accountability

One of the most important steps in bodybuilding is accepting responsibility for your lifestyle and diet, closely monitoring what you do, and then changing it. There is an old saying “what gets measured gets done.” That is why so many bodybuilders write down everything they eat in the course of a day and track their workouts with equal detail.

This is true for government as well.

For taxpayers to ensure that they get the greatest bang for their buck, government decisions and actions must be transparent and have consequences and rewards for actual performance. A number of CPR proposals illustrate this vision and seek to increase accountability in government.

Currently, the executive branch of California's state government consists of 11 agencies, 79 departments, and more than 300 independent boards and commissions. Under this structure, accountability is scattered and lines of authority are confused. As an example, when you consider the state entities responsible for critical infrastructure (roads, water, power), there are more than 30 with a direct hand in this function yet there is no single person that the governor can hold accountable for ensuring long-term planning and management of

See GOVERNMENT REFORM on Page 14

Efficiency at the Gate: How Florida is making government leaner and smarter

By Geoffrey F. Segal



Tackling statewide government reform is a huge task, one that would be nearly impossible without relying on a clear process. That's why Florida's Center for Efficient Government developed a centralized "Gate Process" to make it easier to bring competition and accountability to state government. Florida modeled its Gate Process after one developed in the United Kingdom. The process evaluates the best source to deliver services, and consists of a robust set of standards, templates and guidelines, as well as a transparent method of managing each stage of any outsourcing initiative.

The first and most important step of the Gate Process is a business case analysis, which simply provides a broad analysis of the project—how it will be developed, procured, implemented, and managed. The business case explains the current situation, the need for change and what the agency hopes competition will achieve. It also outlines potential costs and risks, and offers detailed recommendations.

The business case acts as a plan that is used throughout the Gate Process. It is a working document that is updated and reviewed throughout the process as new data or information becomes available, or as key assumptions or methodologies change. Once a contract is executed, a final business case is created to reflect the issues agreed upon in the contract, including specific performance metrics.

The document provides the basis for communication with the legislature, other agencies, advocacy groups, and taxpayers. It also increases transparency and accountability throughout the entire process, and is especially important during performance evaluations.

Specific goals of a business case:

- Communicate a clear business need.
- Obtain management commitment and approval for the project.
- Clearly present the rationale and documentation for investment.
- Justify the project in terms of benefits to be realized.
- Provide an audit trail for decisions made during the process.
- Estimate costs, benefits and risks associated with the pro-



Reason's Geoffrey Segal with Governor Jeb Bush

The Center for Efficient Government— What is it?

Mission: Conduct a statewide evaluation of Florida's outsourcing efforts, identify opportunities for additional outsourcing initiatives, and oversee execution of future outsourcing projects.

Activities: Evaluate the 138 competition initiatives implemented since 1999. Identify potential impacts of offshore outsourcing, assist agencies with developing business cases for potential outsourcing initiatives, and develop the "Gate Process."

Online at: dms.myflorida.com/dms/administration/center_for_efficient_government

posed project.

- Ensure that everyone involved understands the implications and scope of the project.
- Provide transparent rationale for gaining support from the governor, legislature and stakeholders.
- Demonstrate that the implementing agency is capable of managing the project.
- Provide a framework for decision-making.
- Provide a structure for further stages.
- Serve as a management tool to achieve maximum value.
- Document the policy, budget, and functional objectives.
- Identify key stakeholders, and gain their support.

The business case serves as the broad policy document guiding the initiative. Thus, it should be developed with the input of key stakeholders, both internal and external, and drafted by a team comprised of subject matter experts, budget staff,

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Government by Network: The new public governance

By Stephen Goldsmith and William D. Eggers



As President Bush prepares for his second term, government reform advocates stand poised, albeit precariously, on the verge of victory in the long struggle to replace monopolistic government with a more competitive, market-oriented model.

President Bush's policy agenda—from social security and Medicare reform to the faith-based initiative—strongly emphasizes leveraging private sector assets to accomplish policy goals. His management agenda firmly endorses competing out additional government work to the private sector. Indeed, the federal government already spends about \$100 billion more annually for contracts than it does for employee salaries, and numerous federal departments—NASA and Energy to name two—have become de-facto contract management agencies, expending upwards of 80 percent of their budgets on contractors.

At the state and local level, private contractors, long active in areas such as waste collection and road repair, now also dominate the provision of complex social services, including the welfare-to-work programs in states such as Texas, Florida, and Wisconsin and the child welfare systems in many places including the entire state of Kansas. In short, private provision of public services—increasing relative to government delivery for decades—shows no sign of abating.

Yet, as long-time advocates and practitioners of privatization, we fear these very milestones could lead not to success but failure unless they are accompanied by both a better public understanding of this new model and fundamental changes in how government is managed.

First, there's the issue of message. Reformers shouldn't allow themselves to be pulled into an argument for or against greater private provision from the standpoint of the old left/right privatization axis. The question is no longer whether a service should be delivered by a private or a public player, but rather how should the sectors, including nonprofits, be arrayed and managed to produce the best services. Whether it's Medicare, Social Security or education reform, the issue isn't whether government will abdicate its responsibilities to citizens, but how to conceptualize, configure, and manage a network of public, private and nonprofit providers in a way that produces more

value for citizens for each dollar spent.

Using private, market forces like private savings accounts, contracts, and school vouchers builds on a steadily emerging post-World War II trend: government funds and sets the rules for safety nets while injecting market-based creativity and freedom into the delivery of those services. Instead of inputs and processes, government focuses on accountability, rule-setting and outcomes, for example, a quality education. It's a different, but not diminished, role for government.

Second, reformers need to acknowledge that greater private provision of government services by itself is no panacea. Recent headlines reveal the serious difficulties government often has getting this right. In Iraq, private sector involvement has been critical—one contractor for every ten soldiers—but also at times controversial. Atlanta's effort to outsource wastewater treatment failed miserably. And in Kansas, two large, venerable nonprofits went bankrupt as a result of too much risk-shifting in the state's child welfare privatization.

The problem is that many public officials don't yet know how to manage well a government that does most of its work through third parties. Few have figured out how out to actually manage a government comprised more and more of public-private networks instead of people and programs.

One thing is clear: governing in this environment demands an entirely different set of competencies. "Networked management" requires becoming proficient in a host of new tasks, such as negotiation, mediation and contract management. Today, such skills aren't exactly plentiful in most government agencies.

Ultimately, a networked government will employ fewer people overall—particularly at the lower and middle levels—but it will need more highly skilled individuals at the top who have private sector experience and skills. Highly restrictive hiring and employment practices will need to be changed to attract a new kind of public employee. What the federal government calls the acquisition workforce must move to center stage, understanding how to set rules which protect the public and holding private partners accountable without stifling their creativity.

Balancing the need for accountability against the benefits of flexibility is one of the biggest challenges of this model, whether it concerns a defense contractor, a charter school, or a private investment account. The most valuable relationships are dynamic, learning relationships. In successful partnerships the goals and outcomes of the contract will stay sharply in focus, but the inputs and processes will change as required. Manag-

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Battered but Breathing: An update on the effort to bring competition to Washington

By Geoffrey F. Segal



Privatization at the federal level is alive and well...barely. In each of the last two appropriations cycles, members of Congress have attempted to insert language into bills that would limit, restrict, or in some cases outright kill competitive sourcing at federal agencies. Fortunately, these opponents have seen more failures than successes, but just one or two wins seriously sets back the president's plan to bring competition to half the federal workforce through competitive sourcing.

Despite this, a number of successes are worth mentioning. Studies of more than 650 commercial activities completed in FY 2003 and several competitions completed in the first quarter of FY 2004 comprised of more than 17,500 full-time equivalent (FTE) positions, are expected to yield \$1.1 billion in savings for taxpayers over the next three to five years, approximately a 15 percent cost reduction (or avoidance). This cost savings is generated regardless of whether the federal workers or a competing vendor wins, a savings of \$12,000 per position studied.

Success is tied to sound preliminary planning, consolidating activities, reorganizing inefficient in-house operations, and aligning competitive sourcing and human capital efforts.

Success is tied to sound preliminary planning, grouping related activities to generate private sector interest, reorganizing inefficient in-house operations, and aligning competitive sourcing and human capital efforts to close competency and skills gaps. The driving force behind the cost savings is competition. The cost savings will likely decrease from 15 percent if Congress elects to create a disincentive for vendors to compete by balkanizing the competitive sourcing process through piecemeal legislation.

Agencies report that their incremental ("out-of-pocket") costs total about \$90 million. Thus, for every dollar spent on competitive sourcing, the taxpayers saw approximately \$12 in cost savings or cost avoidance.

For more on this topic, see the 2003 *PW* cover story "Don't Make Us Compete!": rppi.org/sep03pw.pdf. ■



Competitive Sourcing at a Glance: Investments & Results

Competitive assessments completed in FY 2003

- Number of assessments completed: 662*
- Type conducted** : streamlined = 570; standard = 92
- Number of FTEs studied: 17,595*
- Percentage of studies where federal agency determined best value is provided by the in-house organization (based on FTEs studied): 89%

Competitive assessments announced but not completed in FY 2003

- Number of assessments announced: 73
- Type conducted** : streamlined = 17; standard = 56
- Number of FTEs announced for competitive assessment: 7,385

Out-of-pocket cost of competitive assessments***

- Incremental cost directly attributable to conducting completed competitive assessments: \$88 million
- Incremental cost directly attributable to conducting announced competitive assessments: \$15 million
- Average incremental cost per FTE studied: \$5,000

Results: estimated savings from completed competitive assessments****

- Gross: \$1.19 billion (over three to five years)
- Net: \$1.1 billion (over three to five years)
- Annualized gross: \$237 million
- Annualized net per FTE: \$12,000

* excludes direct conversions; includes 4 standard competitions completed in the first quarter of FY 2004.

** includes streamlined and standard competitions conducted under the revised Circular and streamlined and standard cost comparisons conducted under the old Circular A-76.

*** these are one-time expenses.

**** aggregate cost and savings figures were derived from agency calculations made in accordance with the general methodologies described in OMB Memorandum M-04-07.

See Office of Federal Procurement Policy for definitions and explanations: <http://www.whitehouse.gov/omb/procurement/index.html>

What's in the Government's Attic

By John M. Palatiello



In a nation built on the concept of private property, it is astonishing how much property our federal government owns. The Government Accountability Office (formerly known as the General Accounting Office) released a new report, GAO-03-122, which found that over 30 federal agencies control hundreds of thousands of real property assets worldwide, including facilities and land, worth hundreds of billions of dollars. However, the portfolio is not well-managed. Many assets are no longer consistent with agency missions or needs and are therefore no longer needed, and many are in an alarming state of disrepair. The GAO also found that there are no reliable government-wide data on these assets.

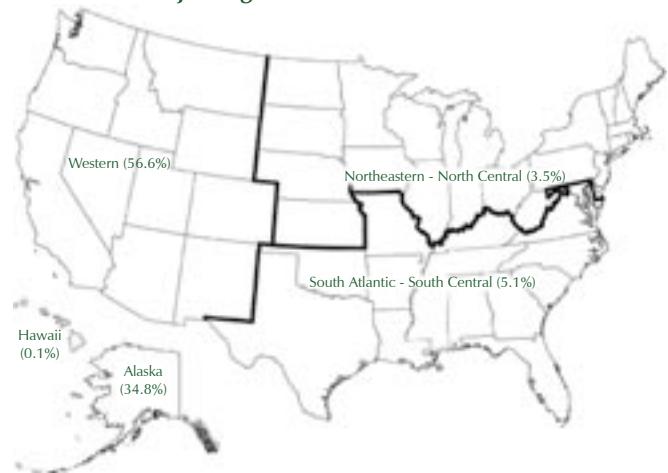
Many laws require the federal government to inventory land, but none of the inventories is current or accurate. Moreover, there are duplicative and redundant inventories that waste tax dollars. Most are created and maintained for a single purpose. Few are compatible with one another. So, although the government estimates that it owns more than 600 million acres of land, what remains unknown is where the land is, what it is being used for, and whether the land is being put to its best use.

Many local governments have used land information systems or geographic information systems (GIS) to more accurately and efficiently inventory real estate within the jurisdiction. It is time the U.S. government invested in a similar methodology and technology to identify and inventory its land holdings. Such a land system can help enhance the management of federal lands, identify lands that could be put to better use, as well as those that are no longer needed by the government and can be made surplus and sold, thus bringing revenue and savings to the federal government.

State and local governments have already demonstrated the benefits of maintaining accurate asset inventories:

- In California, Gov. Arnold Schwarzenegger issued an executive order instructing state agencies to catalog all property and assets, and he plans to start selling off the surplus. He expects to raise \$50 million next year and even more in the future.
- In 1995, Philadelphia used GIS to optimize its garbage truck routes. The next year the city saved over \$1 million in overtime.

Percentage of Federal Land Holdings in Major Regions of the United States



Source: GSA (GAO presentation of GSA data.)

- A study to determine the possible cost savings that could be achieved by implementing a multi-participant GIS system discovered that if data were exchanged electronically, Santa Clara County, California could reduce staff time by 75 percent and save \$720,000 per year.

As a starting point, Congress should request that the Congressional Research Service of the Library of Congress compile a list of all land inventories being maintained by federal agencies. Such an “inventory of inventories” will help take the important first step toward creating a multi-purpose land information system of federal and non-federal land holdings.

John M. Palatiello is president of John M. Palatiello & Associates, Inc., a public affairs consulting firm (jmpa.us). The preceding was excerpted from the Reason Policy Brief, What's in the Government's Attic, which is available online: rppi.org/pb33.pdf ■

Has PW helped you ...
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right and how we can improve.

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EFFICIENCIES

legal staff, personnel and purchasing officers, experienced project managers, senior managers, private sector providers, and seasoned technology project managers where applicable, at a minimum. It is important that all of these stakeholders have the opportunity to provide input or feedback on the front end of a project as each will have a different perspective and will, at some point, be responsible for managing certain components of an initiative.

To create a successful business case:

Provide the Benchmark: Describe Current Service, Program or Function: This section describes the current service, program or function, as it is currently conducted by the state. By capturing this information and establishing a benchmark, the agency will be able to compare future competitive sourcing activities with the benchmark data and determine successes and shortcomings.

Rationalize the Basis for Introducing Competition into Service: This part explains why the status quo is not desirable and notes the drivers of change, describes available alternatives and documents specific issues that need to be addressed in order to improve the quality of service or achieve new efficiencies.

Describe Assumptions and Methodology: This section details what assumptions associated with policy, legislation, agency direction, market conditions, and timing of events were made and the methodology used to determine them. It describes how these can change over time and identifies how changes in key assumptions would impact the project and outcome.

Formulate and Detail a Recommended Solution: This section should clearly communicate what the proposed project encompasses and the overall scope in terms of what responsibilities will remain within the agency or agencies and what is being shifted to the vendor. It states how the project will contribute to the agency or state's core mission.

Identify State and Agency Impact: This impact statement should begin by stating what division or unit of the agency is impacted, what functions, personnel and capital or technology resources will be impacted and how any changes in the business process will affect these resources. This statement should explain and evaluate any changes affecting the method of service delivery to the customer. A Risk Assessment and SWOT (Strengths, Weaknesses, Opportunities, Threats) Analysis should be included.

Explain Transition Management Strategy: This section

should determine employee transition management strategies and outline and describe communications and management transitions.

Identify and Document Critical Success Factors: This part defines what a successful project would be.

Outline the Proposed Procurement Process: Finally, this section identifies and creates the procurement strategy and procurement team for the competition.

With the right process in place states can realize impressive results. By introducing competition Florida has dropped the cost of highway maintenance by 15 percent and saved \$84 million. Simply outsourcing human resources will save roughly \$173 million. Perhaps most impressive of all is that during the last five years Florida has avoided deficits and returned over \$8 billion in tax relief. And that's just the beginning.

Geoffrey F. Segal, Reason's Director of Privatization and Government Reform, served as an advisor to Florida Gov. Jeb Bush's Center for Efficient Government. ■

How He Sees It:

A reformer on the process of reform

Reason staffers have been in the middle of the biggest state-level reform efforts: George Passantino as a Director of the California Performance Review and Geoffrey Segal as an advisor to Jeb Bush's Center for Efficient Government.

So what's it like to tackle such a huge task? Here's how our Geoffrey Segal sees it:



“Despite the success the governor and his administration had, there was still tremendous push back. I think much of it was political posturing because of the election year.

“With 138 initiatives since 1999, there were still so many opportunities and so much work to do. I was surprised that each initiative had largely been done on its own accord. There was little sharing of experiences and lessons learned, but I guess that's why the center was created.

“It was refreshing to have a governor be such a true believer. He had gone on the record saying that for the most part, only his office, legislative functions, and police officers were off the table. I recall the first time I met the governor. He simply said, ‘tell us what more we can do.’”

Chicago Skyway Sold for \$1.8 Billion

By Robert W. Poole, Jr.



The Chicago City Council voted unanimously on October 27th to accept the winning bid of \$1.82 billion for a 99-year lease of the Chicago Skyway.

The elevated toll road (a section of I-90) linking downtown's Loop with the Indiana border, will be owned and operated by the joint venture of Cintra and Macquarie. The former is a Spanish toll road company and the latter is an Australian financial institution which operates a global toll road mutual fund. Together, the two firms operate and maintain over 1,000 miles of toll roads in Australia, Canada, Chile, Ireland, Portugal, and Spain.

The historic transaction is the first U.S. privatization of an existing public sector toll facility. Comparable privatizations have taken place over the past five years in Canada (Toronto's Highway 407 ETR), Italy (a public stock offering of Autostrade, the country's largest toll motorway operator), Portugal (a public offering of BRISA, its largest toll operator), and Spain (public offerings of several public toll operators). Macquarie also owns the Detroit-Windsor Tunnel, which has always been private.

Mayor Richard Daley said the sale is "a great result for the taxpayers of the City of Chicago," and expects it to set a precedent for other transportation agencies. "[R]unning a toll road is not a core function of City government," Daley told reporters. "And the City faces financial challenges this year and for the next several years." It will use the proceeds to pay off the Skyway's \$450 million in bonds and use another \$130-150 million to retire other city debt. Daley said the balance will be used to create a long-term reserve fund and strengthen the city's financial position.

The franchise agreement provides for limits on toll rate increases, but unlike traditional toll roads, future tolls will be adjusted to keep pace with inflation. Specific caps on rates will apply through 2017, rising in steps from today's \$2.00 (for cars) to \$5.00 by 2017. But thereafter, annual increases of 2 percent or the rate of inflation (whichever is greater) are allowed. This assurance of a rising revenue stream was what made it viable for the Cintra-Macquarie Consortium to submit the high bid, besting four other international teams. Another innovative feature of the agreement permits truck tolls to be 40 percent higher than "regular" truck rates during daytime hours if the consortium reduces those tolls by an equal amount between 8 PM and 4 AM. The Consortium plans to install electronic toll collection soon after taking over the Skyway. ■

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GOVERNING

ing in a dynamic way while protecting the taxpayers—and keeping out of the crosshairs of the inspector general, GAO, and Congress—may be the ultimate challenge of networked government.

Reformers in the next four years have an historic opportunity to accelerate the shift away from government monopolies, bringing private provision to whole new areas of government. However, if private sector partners disappoint, if the public equates private participation with abdication, it will be impossible to develop the necessary support to change Medicare, education, and social security. If we want to win long term, we can't overlook the management "steak" while selling the policy "sizzle" of better, market-oriented programs.

Stephen Goldsmith is a professor at Harvard University and Chair of the Center for Civic Innovation at the Manhattan Institute. William D. Eggers is a Senior Fellow at the Manhattan Institute and Director at Deloitte Research. Goldsmith and Eggers are authors of Governing by Network: The New Shape of the Public Sector published by Brookings Press. ■



The New Model of Government.

Top-down government is fading in prominence, with a new model rising in its place. *Governing by Network* examines for the first time government's transformation from centralized control over public programs to facilitating services through networks of nongovernmental entities.

"In Governing by Network, Goldsmith and Eggers answer one of the most important public policy questions of our time: how public officials can achieve results and ensure accountability to citizens in an age in which government relies more and more on partners to do the public's business."

— Pennsylvania Governor Ed Rendell

For more information, go to
GoverningByNetwork.com

Managed Lanes Advance Across the Country

By Robert W. Poole, Jr.



High-Occupancy Toll (HOT) lanes and other forms of managed lanes have picked up new support in California, Florida, Georgia, New Jersey, Texas, Utah, Washington, and Virginia in recent months.

In September, California Gov. Arnold Schwarzenegger signed legislation (AB 2032) that permits Alameda, Santa Clara, and San Diego counties to develop toll-supported managed lanes on existing freeways. San Diego is already expanding its successful managed lanes on I-15 from eight miles to 20 miles, and from two lanes to four. Its recently adopted 2030 long-range transportation plan calls for adding managed lanes to portions of I-5, I-805, and SR 52. Alameda County plans to add a 14-mile HOT lane to the congested I-680 between Sunol and Milpitas, a major commuter route for Silicon Valley. In late October, that project was awarded a \$714,000 planning grant from the Federal Highway Administration's Value Pricing Pilot Program. Santa Clara County, meanwhile, is studying possible HOT lanes on several freeways.

The Value Pricing Pilot Program awarded two grants for managed lanes research and outreach in Florida. One project seeks to add express toll lanes to the heavily congested I-4 in Orlando; the grant funds will support public outreach about this project being planned by Florida DOT. A second grant will expand ongoing outreach work and traffic and revenue forecasting for the proposed conversion of the HOV lanes on I-95 in Miami to HOT/managed lanes.

In Atlanta, the State Road & Tollway Authority is studying the potential for both HOT lanes and truck-only toll lanes. It has just received a VPPP grant to supplement its ongoing studies with research on a possible HOT/BRT (bus rapid transit) project on the heavily congested I-75. And Georgia Tech is continuing a large research project on possible pricing of the entire Interstate highway system in greater Atlanta.

In the Northeast, the Port Authority of New York and New Jersey is researching the feasibility of adding a second exclusive bus lane on NJ 495 approaching the Lincoln Tunnel to Manhattan. But the new lane might sell its excess capacity to automobile drivers, making it (or both lanes) into HOT/BRT lanes.

The Dallas areas, already planning to add HOT lanes as part of the reconstruction of the LBJ Freeway (I-635), received an unsolicited private sector proposal in 2004 to add managed

lanes to the median of the east-west Airport Freeway between Ft. Worth and Irving. And in November the North Central Texas Council of Governments received a VPPP grant to evaluate the construction of HOT lanes rather than HOV lanes as part of the reconstruction of I-30, the main east-west freeway between Dallas and Ft. Worth. Houston, meanwhile, was awarded a VPPP grant to evaluate the possibility of converting existing HOV lanes to HOT lanes, linking them together into the country's first HOT Network.

In Virginia, the latest HOT lanes proposal—adding such lanes to a long stretch of I-95 south of the District of Columbia and on I-395 from the Beltway to the District—is picking up important local support. In late October, the boards of supervisors of Stafford and Prince William counties got together for a joint strategy session in support of the HOT lanes. The idea is to develop a coordinated position, first with each other, and later on with Arlington and Fairfax counties, as well. The latter are already on record supporting the planned HOT lanes on the Beltway (I-495).

Washington State received a VPPP grant of \$1.1 million for detailed analysis of the planned conversion of HOV lanes on SR 167 to the region's first HOT lanes. The necessary enabling legislation still needs to be enacted, but HOT lane proponents were encouraged by the defeat in November of the concept's principal opponent in the legislature.

Utah is the newest state to consider managed lanes and toll roads. In October, the Transportation Planning Task Force voted unanimously to recommend to the legislature a short list of managed lanes options. The task force and the Utah DOT have spent the last year looking at highway finance and how to get the most bang for the state's limited bucks. DOT executive director John Njord summarized the five options being recommended for consideration, as follows:

- Toll roads, where new highways or freeways are needed; most likely projects would need some degree of gas tax support in addition to toll revenues, he said;
- Reversible lanes, not necessarily with pricing;
- HOV lanes, which Utah launched on I-15 prior to the Olympics;
- HOT lanes, as used in California and Texas; and
- Cordon pricing, as used in London and Singapore.

Referring to this list, task force co-chair Sen. Carlene Walker told the *Deseret News*, "Some of these, in particular, have great potential, and we need to educate the Legislature on them." ■

Privatization Speeds Port Modernization

By Robert W. Poole, Jr.



Though it has received far less attention than the privatization of airports or highways, the privatization of ports is leading to dramatic gains in port efficiency around the world. Begun by Margaret Thatcher's sale of Associated British Ports in the 1980s, port privatization is now well-established in Asia, Latin America, and even parts of Africa.

One of the world's largest and fastest-growing port operators is Hutchinson Port Holdings, a division of Hong Kong-based Hutchinson Whampoa. One out of every seven containers worldwide passes through an HPH terminal each year. The company owns 30 ports in 15 countries in Asia, Africa, Europe, the Middle East, and Latin America. It is in the process of standardizing information technology and operating procedures at all 30, aiming for large savings in operating costs, shorter loading/unloading times, and quicker truck turn-around times. With the new systems, truck drivers will be able to make appointments up to three days in advance, check in using a fully automated process, and load and unload via an automated system.

HPH is one of two major overseas players now dominating Mexico's ports. Initially privatized in the mid-1990s to joint ventures of Mexican and overseas companies, most of the country's major ports are now run solely by HPN or its U.S.-based competitor, Carrix (formerly Stevedoring Services of America, SSA). Most Mexican ports were privatized via 20-year concession agreements, and when the Mexican partner companies concluded that they were too heavily in debt, SSA and HPN bought them out. It is universally concluded that privatization of the ports has led to huge improvements in performance, making possible expanded trade and double-digit growth rates since 2000.

Competition from a privatized port is shaking up stodgy Transnet, the government monopoly owner of South Africa's ports, railroad, and national airline. The British-owned port in Mozambique's Maputo is now giving Transnet's port at Durban a run for its money, and some think this pressure will spur port privatization in South Africa.

Even China seems to be edging toward privatization. In 2003, its largest port, Shanghai, was corporatized as Shanghai International Port. Already the world's third-busiest container port, it is the first port in China charged with operating commercially, which means growing and making a profit. Given the recent public share offerings of several of China's formerly state-owned airlines, it would not be surprising to see the Shanghai port offer shares within the next few years. ■

Catching the Aquaculture Wave

By Michael De Alessi



The fish dinner of the future may well come from a farm. While worldwide fish catches are flat, aquaculture is one of the fastest-growing new industries.

Most capture fisheries around the world suffer from what is known as "the tragedy of the commons," a phrase coined by Garrett Hardin in 1968 to describe that when valuable resources are free for the taking, they are depleted. Or to put it another way, when fish left in the sea are simply there for someone else to catch, there is no incentive to leave fish to maintain their numbers for another day.

The most promising improvement in fisheries management in recent years is the development of fishing rights, often called ITQs (Individual Trading Quotas) or IFQs (Individual Fishing Quotas), which allocate a certain percentage of the total harvest to specific fishermen. This ends the often-destructive (both to people and to the marine environment) race between fishermen, and even more importantly, creates an incentive to invest in the future health of the fishery, because the owners of those rights benefit financially from a healthier fishery. ITQs have been used successfully in New Zealand, Iceland, and Australia, and a small number exist in the United States as well.



Worldwide aquaculture production has increased during the last decade, and the reason is simple: by "farming" the sea, aquaculturists do not have to worry about the tragedy of the commons. An aquaculture facility allows entrepreneurs to literally "fence" parts of the sea (or even transport it onto land), ensuring that fish not harvested today will be there tomorrow. Aquaculture offers other advantages, such as dependable market supply. Controlling the feed allows fish growers to, for example, increase fat content for sushi chefs or lower it for producers of smoked fish.

The island chain of Hawaii is on the leading edge of the development of the legal and technical frameworks necessary

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The Rise of Education Management Organizations

By **Guilbert C. Hentschke, Scot Oschman, and Lisa Snell**

Education management organizations (EMOs) are largely for-profit firms that provide “whole-school operation” services to public school agencies. Since arriving on the public school scene a little more than a decade ago, they have grown despite a wide range of objections within the education profession.

Although nominally performing functions not unlike those of a school district, EMOs are usually structured as for-profit corporate entities, a fact that differentiates their structure and their internal operating performance from school districts. The forces fostering the current growth of EMOs lie less in the distinguishing features of EMOs, per se, than in how EMOs complement the school districts and charter schools with whom they typically interact. The future growth of EMOs will be determined in part by the degree to which EMO services will continue to be valued by a greater and greater proportion of the nation’s approximately 15,000 school districts with 80,000-plus schools and the growing number of charter schools.

EMOs contract with school districts’ charter-granting bodies to use tax money and venture capital to operate public schools. EMOs range in size from the largest, Edison Schools, which operates more than 130 schools, to firms that operate single (largely charter) schools.

The growth of EMOs has paralleled the growth of charter schools. Charter schools can be viewed as the largest example of education outsourcing with close to 2,700 individual contracts between charter schools and their government authorizers. Charter schools receive state funds but operate with varying degrees of autonomy from local school districts.

According to *Profiles of For-Profit Education Management Companies, Fifth Annual Report, 2002-2003*, more than 74 percent of all privately managed public schools profiled were charter schools. States such as Arizona and Michigan with the strongest charter school laws also have the most for-profit companies, with those two states alone accounting for 48 percent of all profiled EMO-managed schools. EMOs operate between 10 and 14 percent of all charter schools. In 2002-2003, 47 companies operated 417 schools in 24 states and the District of Columbia. Reliable data on the exact numbers are unavailable, and anecdotal reports of numerous one-school firms operating in some states, such as Michigan, would probably increase these estimates.

EMOs have become a part of a longer-standing political contest between professional reformers (largely educationists) and radical reformers (largely business leaders and community activists) over

what is wrong with public schooling and how to improve it. As a relatively new service option available to local education agencies, EMOs have been adopted so far in few settings, rejected in a few others, and not yet considered in many others.

Barriers to EMO Growth

EMOs will only grow as a function of demand in the market for the services they provide. Demand is influenced in part by arguments for and against contracting with EMOs. The most widely voiced argument against contracting is associated with assumptions about the inherent motivation of profit-seeking businesses. The general sentiment among many education writers is that if for-profit firms are allowed to operate public schools, they will attempt to do so at the lowest possible cost in order to maximize profits, and therefore will not maximize the educational experience of students.

Although it is true that a desire to make a profit gives for-profit firms an incentive to spend less on services, that same desire also gives them an incentive to attract and retain customers by providing services better than (or different from) those of their competitors. In the long run, efficiencies through innovation trump cost-cutting. And if for-profit firms fail, they face the consequence of losing business. Public school administrators do not share the same incentives. Because the people living in their districts are required to pay for the public schools, the cost savings that opponents of for-profit education firms believe should not go to corporations—or to the innovations produced by competition—are also likely to be unavailable to public officials not in partnership with for-profit firms.

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GOVERNMENT REFORM

infrastructure. With so many people responsible, nobody is accountable.

CPR even identified situations where the overlap and duplication has resulted in two state entities spending thousands of legal hours in a lawsuit against one another. The idea of two state agencies suing each other is appalling. No matter who wins their lawsuit, the loser is certain—the taxpayer.

The CPR proposal confronts these challenges head on, collapsing the existing structure into 11 departments that are aligned along quality-of-life priorities with clear missions and areas of responsibility. Under the CPR model, infrastructure would be consolidated into a single entity, led by a secretary who is directly accountable to the governor for this priority. The same holds for public safety. Those disparate functions would be joined together in one entity. As the CPR report notes, “If a program is failing Californians, good government demands that blame be easy to affix and hard to deflect.”

CPR also proposes fundamentally changing the budget process, which currently could be characterized as “baseline” budgeting, whereby previous years’ spending levels are used as the baseline and hence, assumed to be good investments. Instead, CPR proposes shifting to “performance-based budgeting” whereby programs are measured each year for what they achieve and that performance information, in turn, informs the level of spending. Programs that fail to achieve their goals and, hence, contribute little to the state’s quality of life, much like fatty foods and empty calories, can be targeted more easily for elimination or reductions.

Similarly, CPR proposes bringing more accountability to the way that the state manages and motivates its public employees. Shockingly, under current practice, more than 99 percent of state employees that are eligible for a “merit raise” receive it. Whenever this merit raise is denied (which does not happen very often), employees have the right to appeal the decision, which in most cases, is overturned. State managers complain that it takes as much documentation to deny a merit raise as it does to demote an employee.

Competition

In the *Encyclopedia*, Schwarzenegger relishes competition as a powerful force to bring the very best out of him. Similarly, competition can lead to increased performance and lower costs in the delivery of public services.

The CPR report proposes a number of approaches to lever-

age competition to improve the quality and reduce the cost of services provided and goods purchased by the state. Among them, CPR proposed the creation of a Competitive Government Panel to identify opportunities and barriers to competition and then implement and oversee competitive efforts.

The report also recommends ending the monopoly that has been granted to the Prison Industry Authority over state purchases. As it stands, all state agencies are mandated to purchase from the PIA all products that they provide. Waivers to this monopoly are only granted by the PIA themselves and the desire to attain a lower price is not a valid reason for such a waiver. As a result, state agencies overpay for products that they could purchase for much less on the competitive market. In a 1993 report, the Little Hoover Commission, the state watchdog agency, declared that the Prison Industry Authority was “holding state departments hostage to high prices and delayed deliveries.”

Much like the bodybuilder that gets a better pump and performs better because of competition, state government can pump up by breaking down artificial barriers to competition.

Innovation

Bodybuilders also routinely try new and innovative workout strategies to build the strongest bodies and target muscle groups in different ways. California needs a similar workout routine that uses new approaches to delivering services to the public. Bodybuilding technology and science have changed dramatically since the days of legendary bodybuilder Bill Pearl. Competitors that relied on the same approaches used in the 1950s could not compete in the modern world. The same holds true for government. The world around us has changed and yet government has changed very little in decades.

In addition to the structural deficit as a reason to change, 34 percent of the state workforce is eligible to retire within the next five years. To help cope with this new reality, CPR proposes a number of recommendations to leverage technology and improve customer service, even as the pool of state workers may decline in coming years.

For instance, while Californians can renew their vehicle registration online, they are unable to renew driver’s licenses online. As a result, approximately 1 million drivers will stand in line at a DMV field office to renew their driver’s licenses this year. Not only does this add to the expense of the renewal process, it also is a backward model when it comes to serving the customers of the state.

California Performance Review 2004-2005			
POTENTIAL SAVINGS FROM CPR RECOMMENDATIONS			
Section	General Fund FY 04-05	Other Funds FY 04-05	Five-Year Total— All Funds
General Government	\$270,250,000	\$49,918,000	\$12,437,970,000
Health and Human Services	\$815,000	\$1,139,000	\$4,918,120,000
Education, Training and Volunteerism	\$133,876,000	\$54,554,000	\$4,123,748,000
Infrastructure	\$56,087,000	\$24,388,000	\$3,363,243,000
Resource Conservation and Environmental Protection	\$2,204,250	\$5,938,750	\$349,631,000
Public Safety	\$0	\$1,200,000	\$7,600,000
Statewide Operations	\$218,132,000	\$222,626,000	\$6,405,768,000
GRAND TOTAL	\$681,364,250	\$359,763,750	\$31,606,080,000

CPR proposes a unified connection with the public for state information. Rather than wading through hundreds of toll-free numbers, CPR envisions a single number, a single Web portal.

The Time is Now

For many years, California has lurched from crisis to crisis—electricity, budget, workers' compensation. Sadly, rather than focusing on fundamentally reforming state government, the past several years have seen little more than attempts to put off the problems into the future. We have watched the health of state government decline in the process.

Seeing this trend, Schwarzenegger embarked on a comprehensive review of state government when he launched the California Performance Review and the report that resulted from that effort now sits on his desk.

In many ways, CPR is like a membership to a gym, complete with a comprehensive nutritional discipline and workout plan. But like all bodybuilding strategies, the plan only works if you develop the discipline to stick with it.

Now we wait to see if Sacramento has that discipline to reform itself. Even "Girlie Men" couldn't ask for a better trainer.

George Passantino is Reason's Director of Government Affairs. He also served as a Director of the California Performance Review. A version of this piece originally appeared in the California Political Review (cppf.us). Visit Reason's California Performance Review Resource Center: rppi.org/calperformance/index.shtml ■

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FISHFARMING

for open-ocean cage fishfarming. One offshore farm is up and running, and another has all the permits and licenses and is just waiting for the final rounds of financing. This could be the beginning of a tremendous boon to both Hawaii's economy and its general entrepreneurial climate.

Yet many obstacles remain. Despite studies that show no measurable impact to the environment, misplaced fears coupled with a stifling, extended bureaucratic process that allows individuals to contest the permit process with reasonable cause hampers Hawaii's chance to develop offshore fishfarming and expand its shrunken economy.

With a streamlining of its bureaucracy, Hawaii could soon lead the nation in offshore oceanic fish cultivation, spelling success for its citizens as well as taking pressure off of wild stocks of depleted fish populations. It would also demonstrate how human ingenuity, properly channeled through free enterprise, could feed people and maintain, or even enhance, a healthy environment.

Michael De Alessi is Reason's Director of Natural Resource Policy and a senior fellow at the Grassroot Institute of Hawaii. The preceding was excerpted from the Reason study, Catching the Aquaculture Wave, which is available online: rppi.org/ps327.pdf ■



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Who, What, Where

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