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Commentaries

Of Planning, Privatization, and Accountability

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These days, it seems as if all public services and infrastructure—schools, prisons, liquor sales, roads, and parking garages—are being privatized. At the same time, it seems to be impossible to find a credible rationale that explains why services and infrastructure are provided by the private or public sector. While the average person can stay confused without causing much harm, planners need a credible rationale and analysis for making decisions concerning private or public provision of services and infrastructure. This article outlines an objective process focused on accountability and a comprehensive cost–benefit analysis in order to promote the public interest.

ACCOUNTABILITY

Why are some services and infrastructure private and some public?[1] The best answer seems to be based on accountability. A society needs all people and organizations to be good citizens. Those who cannot behave are disciplined in various ways, such as social disapproval, loss of reputation, and sanctions including fines and imprisonment. In the case of private-sector businesses, accountability is imposed through market competition. Companies that perform better and provide improved products and services will attract more customers, while those that perform badly will be disciplined by losing business to competitors.

Experience has shown that when there are no competitors—when there is a monopoly—the market provides no discipline. Monopoly businesses can behave badly toward their customers with no consequences because there is no other source for the good or service. These problems led to the enactment of antitrust laws.

In some cases, however, there are natural monopolies. Moshe Adler's research showed that, in the 19th century, New York City made every effort to provide street cleaning by private contractors, and used every device they could think of to prevent shirking by contractors, including methods advocated today, such as managed competition; however, problems such as poor quality and corruption left the city with filthy streets decade after decade.[2] More recently, privatization in Indianapolis revealed widespread problems of shirking and poor service.[3]

Obviously, natural monopolies, including regulated monopolies and government agencies, are not free from problems, as Adler's research also shows. Since competition cannot impose market accountability over natural monopolies, such as regulated monopolies and government agencies, public accountability mechanisms must be imposed. Examples of public accountability in general use today include regulations, freedom of information acts, open meetings and sunshine acts, various forms of citizen oversight, and federal and state administrative procedures acts.

Privatization of a public service, however, creates a situation in which a government service or infrastructure is not covered by public-sector accountability, and the privatized entity, which is a monopoly, is not disciplined by market competition. The result is no market discipline, no oversight, and no accountability—public or private.

COST–BENEFIT ANALYSES

There is a tacit assumption that when a decision is made to privatize a public service or infrastructure, a cost–benefit comparison between public versus private performance shows which competitor will provide the best service at the lowest cost. The accuracy of this decision-making process depends on including all costs. If all costs are not identified and included in the cost–benefit analysis, then a service might be privatized even though the public sector could provide better service at a lower cost. Unfortunately, comparisons are largely confined to dollars for worker pay and benefits, and large and important costs are ignored.

A 2008 study of the privatization of the Internal Revenue Service mailrooms found many failures, both in that specific event and in general. In that case, they failed to conduct any cost–benefit analysis. In addition, there has been a general failure to identify and include all costs. Examples of

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costs not taken into consideration included inefficiency created by the loss of institutional memory when an existing workforce is replaced by a new workforce, effects of job loss to the former employees, the cost to the public of paying unemployment benefits to displaced employees, and the large staff and complex infrastructure created by and within the Office of Management and Budget to control, guide, and monitor the privatization process.[4] In addition, the study found that Office of Management and Budget regulations forbade including large costs generated by the privatization process. A 2008 Government Office of Accountability study of the privatization of Department of Labor functions confirmed many of those findings, including that costs such as time spent on the privatization process and lowered productivity caused by the stress of employees who feared they were losing their jobs were real but not easily quantified.[5]

APPLYING ACCOUNTABILITY AND COST–BENEFIT ANALYSIS IN DECIDING WHETHER TO PRIVATIZE

Discussion of privatization issues often devolve into unhelpful pro–con arguments that provide no useful guidance to decision making. Therefore, providing an example of applying an accountability and cost–benefit analysis to a current issue can be helpful. Although not an issue that planners are likely to be professionally involved with, state privatization of alcohol sales, a process under way in several states, illustrates the problem. States vary in how alcohol is sold. Some states allow all or most forms of alcohol to be sold by private businesses, while others limit at least some sales to state-operated stores. In states that allow alcohol to be sold by private businesses, market forces of competition provide incentives to make the purchase of alcohol easy, including by adding sales outlets and extending hours. State taxes on those increased sales can then bring in more tax revenue that can be used for public purposes.

However, the consumption of alcohol is associated with disease, accidents, injury, death, and antisocial behavior. According to the Centers for Disease Control, drinking causes many harms whose effects can be multigenerational and whose costs are visited upon the wider society.[6] These costs are diffused, making them hard to calculate because their negative effects fall on society and nondrinkers and are paid for by the community and even by succeeding generations. In addition, people may differ in how to weigh those costs and on the appropriate level of accountability.

Though difficult to measure, we cannot exclude these very real costs. Doing so could lead to privatizing a service or infrastructure when there is no benefit, or possibly even substantial harm, to the public in doing so. However, after studying this issue, the Community Preventive Services Task Force, an independent, nonfederal, unpaid body, appointed by the Director of the Centers for Disease Control and Prevention,[7] recommended "against the further privatization of alcohol sales in settings with current government control of retail sales. This finding is based on strong evidence that privatization results in increased per capita alcohol consumption, a well-established proxy for excessive consumption and related harms."[8]

INFRASTRUCTURE PRIVATIZATION[9]

The same accountability and cost principles also apply to decisions to privatize highways, parking meters, parking garages, and other physical infrastructure. In addition to the issues of accountability and cost–benefit analysis already discussed, these deals generally involve multidecade leases and complex financial and contractual structures, the consequences of which may be difficult to understand and predict.

In approaching infrastructure privatization, planners should be aware that the standard terms and structure of these deals have been developed to promote the interests of investment firms, not the public's interest. For example, advisors to the government are often paid a "success fee" if they consummate a deal. That payment structure creates a financial incentive to consummate a deal, even when it is not in the public's interest. That bias toward privatization of infrastructure is exacerbated by advisors' strong ties to the infrastructure privatization industry. However, it is virtually impossible to find expert advice outside the industry itself. These ties create strong incentives not to advise governments to eliminate contract provisions that can generate infrastructure contractor revenues but that are not in the public's interest, because the advisors have and will play other roles in which they will want to include those provisions.

Commonly found provisions are "adverse action" terms and noncompete agreements in American infrastructure privatization contracts. They require payments to contractors when government actions lower contractors' anticipated revenues. Examples include requiring that a highway contractor receive adverse action compensation for lower levels of traffic because a government promotes carpooling; for revenue lost from parking meters as a result of closing streets for festivals or repairs; and for actions such as inspecting the contractor's compliance with specifications or emergency crews entering a highway when there has been an accident. "Noncompete" provisions can take many forms and can even require government agencies to create conditions that cause "competing" roads to be congested or otherwise slow traffic. They may also prohibit development of needed infrastructure for the life of the contract.

These terms raise troubling issues. For example, the Chicago parking meter contract required payment of compensation for street closings covering revenue the vendor would have received had the streets not been closed to parking; however, before the meters were privatized, the city would not have received compensation during street fairs or repairs. In other words, the contract put the private contractor in a

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better financial position than the city for providing the same service. Owing additional compensation raises the cost of government decisions taken to promote the general public interest. The extra cost may even mean forgoing actions necessary to the public's welfare.

In recent years, contractors have barred public access to the terms of infrastructure contracts. Requests by the author for copies of contracts have been turned down on the ground that the contracts contain "proprietary" material. Ohio State University (OSU) recently claimed that the details of privatizing its parking facilities were a trade secret;[10] however, it is difficult to understand what qualities would qualify the contracts as trade secrets. Indeed, an examination of a sample of infrastructure privatization contracts found most of their terms to be identical.

Denying public access to information concerning a valuable public asset allows a privatization contract to trump state law and could be used to shield wrongdoing. That may be the case here. An article in the *Columbus Dispatch* states that "Julie Roin, a professor who specializes in state and local finance at the University of Chicago Law School, describes the deals as 'debt masquerading as privatization.'"[11] Claims such as OSU's remove public accountability mechanisms, such as freedom of information or open meetings acts and, since the contractor would have a monopoly on parking facilities, there would be no accountability imposed by free market competition.

Being locked into multidecade infrastructure privatization contracts creates problems for all parties—contractors, as well as the public. Yet they are the norm because the federal tax code allows private contractors to take a highly accelerated amortization—in the area of 12 to 15 years—when an infrastructure contract's length exceeds the useful life of the infrastructure. For highways, that useful life is deemed to be in the area of 50 years. That does not explain the contracts that far exceed 50 years; however, it may be that the investors are able to engage in serial amortization through multiple sales of the infrastructure.

The loss of tax revenue from these tax breaks contributes to the financial problems that have prompted cities and states to use infrastructure privatization to provide for needs that the public could no longer afford. Meanwhile, the contracts place the public "partners" in contractual straitjackets. For example, a city that wanted to reduce smog or traffic congestion by building or expanding mass transit would find that the cost of solving that problem included paying adverse action compensation to the private lessee of the city's parking garages or highways because it would lower the number of cars paying tolls or fees.

There are alternatives. For example, before—or rather than—entering into a multigenerational lease, less risky alternatives, such as hiring a contractor to manage the infrastructure on a short-term renewable lease, would give the contractor a strong incentive to do a good job and would provide information as to the need for privatization.

In 2011, U.S. Sen. Dick Durbin of Illinois responded to studies showing problems with infrastructure privatization by proposing cutting off Surface Transportation Act funding to privatized transportation infrastructure. The goals of the bill were to protect taxpayer investments in major transportation infrastructure projects and require increased accountability and public involvement before major transportation projects could be leased or sold. The bill would attach a federal lien on all major transportation projects, defined as those that have received more than $25 million in federal funding or that have a value over $500 million. The lien would not be released until all federal funds have been repaid and action has been taken to increase accountability and public input in privatization.[12]

THERE ARE OTHER OPTIONS

Public infrastructure and building agency expertise represent a large public investment through our taxes in their construction and maintenance. Privatization can introduce interests adverse to those of the public. Therefore, before entering into any privatization contract, due diligence requires identifying costs, identifying who will bear the costs, considering how traditional methods to provide services or infrastructure can be made most useful, asking whether traditional methods continue to be viable, and finding ways to achieve goals while imposing the least risk possible to the public.

ENDNOTES

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3. SHEILA S. KENNEDY & INGRID RITCHIE, EDS., TO MARKET, TO MARKET: REINVENTING INDIANAPOLIS, University Press of America (2001).

4. Ellen Dannin, *Counting What Matters: Privatization, People with Disabilities, and the Cost of Low-Waged Work (Symposium on The Low Wage Worker: Legal Rights–Legal Realities)*, 92 MINN. L. REV. 1348 (2008).

5. Government Accountability Office, Department of Labor: Better Cost Assessments and Departmentwide Performance Tracking Are Needed to Effectively Manage Competitive Sourcing Program, GAO-09-14 (Nov. 21, 2008), *available at* http://www.gao.gov/new.items/d0914.pdf; *see also* Carol D. Leonnig, *GAO Report Says Labor Department Misled Congress on Cost of Outsourcing Jobs*, WASHINGTON POST (Nov. 25, 2008), *available at* http://www.washingtonpost.com/wp-dyn/content/article/2008/11/24/AR2008112402796.html.

6. *See* http://www.cdc.gov/alcohol/faqs.htm.

7. *See* http://www.thecommunityguide.org/about/aboutTF.html.

8. The Community Preventive Services Task Force, Preventing Excessive Alcohol Consumption: Privatization of Retail Alcohol Sales: Task Force Finding & Rationale Statement, *available at* http://www.thecommunityguide.org/alcohol/RRprivatization.html.

9. *See* Julie Roin, *Privatization and the Sale of Tax Revenues*, 85 MINN. L. REV. 1965 (2011); Ellen Dannin, *Crumbling Infrastructure, Crumbling Democracy: Infrastructure Privatization Contracts and Their Effects on State and Local Governance*, 6 NW J. L. & SOC. POL'Y 47 (2011).

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11. *Id.*

12. Protecting Taxpayers in Transportation Asset Transfers Act in their bill to reauthorize the Surface Transportation Act, *available at* http://durbin.senate.gov/public/index.cfm/pressreleases?ID=05475591-b743-4f98-93ea-b73f17725a58.