

# STREAMLINING SAN DIEGO:



## Achieving Taxpayer Savings and Government Reforms Through Managed Competition

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## FOREWORD

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This year the City of San Diego will have gross budget revenues of more than \$2.7 billion. If it was a private company in the Fortune 1000, the city would rank #692, just behind Jack in the Box (#685) and ahead of Cooper Tires (#701). The City takes on such diverse tasks as running a municipal water system, operating the region's largest landfill, and maintaining more than 39,000 acres of parks and open space. According to the FY 2007-2008 budget, the City funds more than 10,500 positions with salaries and wages of almost \$700 million.

Managing an organization of that complexity and size requires leadership, experience, and attention to detail. This is why Proposition C, passed by San Diego voters in November 2006, was so important. The changes to the city charter provide management with greater flexibility when it comes to staffing and offers the promise of providing taxpayers with more efficient and effective services.

In this policy study, Geoffrey F. Segal, Adam B. Summers, Leonard C. Gilroy, and W. Erik Bruvold take a look at the lessons learned in other jurisdictions about managed competition and how they can inform San Diego leaders. Identifying eleven functions currently carried out by the City of San Diego, they show how jurisdictions throughout the country have used managed competition in these areas in ways that benefits both taxpayers and municipal employees. Rather than a tool used for "slashing and burning" budgets, managed competition can spur on innovation and allow cities to focus on their core competencies and functions.

Because of the need to address the City's pension, retiree healthcare, and deferred maintenance obligations, in FY 2009 San Diego is projected to face a structural deficit in its general fund of more than \$96 million and a cumulative 4-year general fund deficit of \$375.2 million. This situation makes the speedy implementation of managed competition imperative. To put this problem in perspective, the FY 09 deficit is nearly three times the size of the FY 08 budget for the library department or 51 percent

of the budget for San Diego's fire department. The size of this problem means that officials will have to do more than simply eliminate unfilled positions or make modest reductions in the growth of government but, instead, will need to fundamentally rethink the way the City does business.

The San Diego Institute for Policy Research hopes this study will challenge the status quo. The authors examined not only the functions often discussed as candidates for outsourcing, such as the print shop and fleet maintenance, but also functions San Diegans have rarely discussed putting through managed competition efforts, such as golf course operations, routine permitting, and the water department. To take just one example, we hope it comes as a surprise to readers to learn that Riverside County has used a private-sector company to manage its library system. According to the authors and data from the state library system, by using this approach, Riverside County has nearly the same number of branch libraries as San Diego and has been able to preserve hours and exceeded customer expectations even as finances have grown tighter. Whether our library department is a prime candidate for managed competition can be debated, but this study suggests that contemplating that step is neither extraordinary or beyond the pale of prudent municipal management.

As the authors remind us, the City will need to prioritize and undertake managed competition efforts in a way that builds internal systems and institutional memory. The City can not do everything at once. The 30+ case studies laid out in this report should, however, spur innovation and point the way toward where San Diego policy makers can learn from others. Ultimately, we hope this study provides a resource that encourages hard questions and "outside-of-the-box" approaches so San Diegans can be served by a government which operates in the most effective and efficient way possible.

**Steven C. Francis**  
*Chairman and Founder*  
*San Diego Institute for Policy Research*

“IT IS BETTER FOR THE PUBLIC TO PROCURE  
AT THE MARKET WHATEVER THE MARKET CAN  
SUPPLY; BECAUSE THERE IT IS BY COMPETITION  
KEPT UP IN ITS QUALITY, AND REDUCED TO ITS  
MINIMUM PRICE.”

– THOMAS JEFFERSON, 1808

“IT IS THE POLICY OF THE GOVERNMENT OF  
THE UNITED STATES TO RELY ON COMMERCIAL  
SOURCES TO SUPPLY THE PRODUCTS AND  
SERVICES THE GOVERNMENT NEEDS. 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.”

– DWIGHT D. EISENHOWER,  
BUREAU OF THE BUDGET BULLETIN 55-4, 1955

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# EXECUTIVE SUMMARY

**T**he City of San Diego's current financial straits have led residents and elected officials to search for serious solutions. One promising measure is the introduction of competition to provide government services.

Managed competition is different from simply "outsourcing," or "contracting out" in that it encourages public employees to submit bids and compete with private bidders. Thus, it is a way of bringing private-sector competitive pressures and incentives to the public sector. Under managed competition, it does not matter whether public employees or private providers earn the contract; the simple introduction of competition means that taxpayers win either way.

San Diegans welcomed the idea in November 2006 when 60 percent of voters approved Proposition C, allowing the city to utilize competition with the private sector to provide cheaper and better services to the community.

For this study, we reviewed the city's budget and activities and identified at least eleven functions currently performed by city workers that are prime candidates for managed competition. Our cost savings estimates, based on an extensive analysis of managed competition and privatization case studies, assumed an average tax-dollar savings range of 10 to 25 percent. If all eleven of the identified managed competition targets were contracted, the expected savings would be \$80 million to \$201 million per year (see the case studies in Part III and Table 10 below for a breakdown of potential cost savings by service). Even if the city achieves just a 15 percent savings rate (towards the low end of our potential savings range), this would result in savings of almost \$120 million each year.

While cost savings is often the biggest reason given for implementing the managed competition process, this is just the tip of the iceberg. There are numerous benefits of competition and contracting:

## **Cost Savings**

Competition encourages would-be service providers to keep costs to a minimum, lest they lose the contract to a more efficient competitor. Cost savings may be realized through economies of scale, reduced labor costs, better technologies, innovations, or simply a different way of completing the job.

## **Quality Improvements**

Similarly, a competitive process encourages bidders to offer the best possible service quality to win out over their rivals.

## **Timeliness**

Contracting may be used to speed the delivery of services by seeking additional workers or providing performance bonuses unavailable to in-house staff.

## **Flexibility to Accommodate Peak Demand**

Changes in season and economic conditions may cause staffing needs to fluctuate significantly. Contracting allows governments to obtain additional help when it is most needed so that services are uninterrupted for residents.

## **Access to Outside Expertise**

Contracting allows governments to obtain staff expertise that they do not have in-house on an as-needed basis.

## **Innovation**

The need for lower-cost, higher-quality services under competition encourages providers to create new, cutting-edge solutions to help win and retain government contracts.

## **Improved Risk Management**

Through contracting and competition, governments may better be able to control costs by building cost-containment provisions into contracts. In addition, contracting may be used to shift liability from the government to the contractor.

An analysis of the City of San Diego's budget revealed that there are a number of services that are not inherently governmental, providing opportunities for managed competition. These services include:

- Water/Wastewater Treatment
- Environmental Services (Including Trash Collection, Landfills, and Recycling)
- Fleet Maintenance
- Street Maintenance
- Parks and Recreation
- Golf Courses
- Libraries
- Permits
- Facilities Management
- Information Technology
- Printing/Copying

Deciding to implement a managed competition process is only the first step. As is the case in all contracting, there are good and bad ways to execute it. In order to avoid potential pitfalls and maximize the benefits of managed competition, there are a few keys to success that San Diego officials should utilize when putting the voter-approved managed competition program into practice:

## 1. TRAINED PROCUREMENT STAFF

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Staff must be properly trained in contracting best practices and, in particular, how to build service level standards into agreements and monitor provider performance, in order to avoid possible ambiguities, misunderstandings, and disputes.

## 2. CENTRALIZED MANAGED COMPETITION UNIT

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The city should maintain an expert team of procurement and competition officials to guide other departments in developing their managed competition initiatives. This central unit will help to break down the "silos" that departments sometimes operate within and identify city-wide or enterprise-wide competition opportunities that might not otherwise be considered.

## 3. ESTABLISHING PERFORMANCE MEASURES

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It is crucial that the city identify good performance measures to fairly compare competing bids and accurately evaluate provider performance after the contract is awarded.

## 4. RELIABLE COST COMPARISONS

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The city must establish formal guidelines for cost comparisons to make sure that all costs are included in the "unit cost" of providing a service so that an "apples-to-apples" comparison of competing bidders may be made. This is especially important when public employees are competing with private-sector bidders since the public- and private-sectors operate under different rules.

## 5. IMPLEMENTING PERFORMANCE-BASED CONTRACTS

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Performance-based contracts should be used as much as possible to place the emphasis on obtaining the results the city wants achieved, rather than focusing merely on inputs and trying to dictate precisely how the service should be performed. Performance standards should be included in contracts and tied to compensation through financial incentives.

## 6. VIGILANT MONITORING AND EVALUATION

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Regular monitoring and performance evaluations are essential to ensure accountability and transparency, and that the city's management and the service provider are on the same page. This can help to address any problems that might arise early, before they become major setbacks.

Finally, we must recognize that managed competition may encounter opposition from public employee unions who view it as a threat to their jobs and influence. Well-managed competition initiatives need not put undue burden on public employees, however. Comprehensive examinations of competition initiatives have found that competition has resulted in few, if any, layoffs and that public employees can actually benefit in the long term from private-sector management. Nevertheless, it is important that management communicate early and often with the public employee unions and encourage them to bid for

managed competition initiatives. Again, so long as there is an open and fair competition process, taxpayers will be better off, regardless of whether the winning bidder comes from the public or the private sector. In the event that significant city employee jobs are at risk, the city should develop a plan to manage public employee transitions.

For some time, the trend has been towards increased contracting and managed competition programs at all levels of government. Decades of experimentation and success stories have demonstrated that competition is an important tool for improving government efficiency, accountability, and transparency. By aggressively pursuing managed competition initiatives while following the best practices outlined in this study and heeding the lessons of other jurisdictions, the City of San Diego can achieve significant cost savings while maintaining or improving the quality of the services it provides. Considering the city's financial difficulties, taxpayers deserve no less.



# PART I

## INTRODUCTION: WHAT IS MANAGED COMPETITION?

San Diego is currently embroiled in a serious financial crunch. According to the city's Five-Year Financial Outlook, the fiscal year 2009 structural deficit, before taking into account the "corrective actions", is projected to be \$174 million.<sup>1</sup> The unfunded actuarial accrued liability (UAAL) of the city's pension plan in June 2005 was calculated at \$1.4 billion,<sup>2</sup> although strong pension investment fund returns and increased city contributions have reduced that amount to an estimated \$1 billion today.<sup>3</sup>

Many reforms have been proposed to address the city's fiscal problems. One measure that deserves special consideration is managed competition. Managed competition is similar to outsourcing, but the difference is that under managed competition government employees are encouraged to devise and submit their own bids to compete with private-sector providers for the contract. Oftentimes, the incumbent municipal employees win because the process itself provides strong incentives and powerful tools for an aggressive internal overhaul that cuts away bureaucratic constraints and redesigns how employees serve the public. For the taxpayer, the competition among both public- and private-sector bidders allows the city to minimize costs while maximizing the quality of services provided. The experiences of other state and local governments illustrate that managed competition provides public officials with the opportunity to better serve their citizens and serves as a model of good government practices.<sup>4</sup>

While sometimes criticized as a fad, managed competition is not a recent public policy idea. For at least 30 years, governments at every level have used managed competition to deliver high-quality public services more efficiently and effectively. It has a successful and proven track record of lowering the costs while simultaneously improving the quality of those services—vital services that taxpayers, citizens, and visitors rely on. The federal government has successfully used managed competition for decades to save billions of taxpayer dollars; however, competitive sourcing was greatly

expanded more recently in 1998 when Congress passed the Federal Activities Inventory Reform (FAIR) Act, which directed the head of each executive agency to submit to the Director of the Office of Management and Budget a list of activities performed by Federal Government sources that are not inherently governmental functions and consider these activities for competitive contracting. At the municipal level, the City of Charlotte has extensively used competition for a dozen years, undertaking some sixty-one initiatives. City employees have won all but ten of those, an 84 percent win rate. Yet, each time the city has significantly cut costs, adding up to millions of dollars over the years.

Managed competition has also been used extensively as a management tool in Florida, Virginia, and Indiana, as well as in cities such as Phoenix, Philadelphia, Indianapolis, Long Beach (CA), and countless other municipalities around the country. Its value in fostering more efficient and effective public services has been acknowledged by government reform experts David Osborne and Peter Hutchinson, who wrote in their recent book, *The Price of Government*, "the fastest way to save money and increase value is to force public institutions to compete."<sup>5</sup>

San Diego is poised to join this list and begin leveraging this tool for taxpayer benefit. In the November 2006 election, San Diego took a large step toward achieving greater efficiency and improved government services when residents overwhelmingly passed Proposition C by a 60 to 40 percent margin. Proposition C asked voters to amend the city charter "to allow the City to contract services traditionally performed by civil service employees if determined to be more economical and efficient while maintaining the quality of services and protecting the public interest."<sup>6</sup> The implementing ordinance became law on January 17, 2007 (see Appendix 2 for the full text of the implementing ordinance in the Municipal Code).

The charter change was critical. Prior to Proposition C's passage, Article VIII, section 117, of the city charter strictly limited the city's ability to contract with private-sector providers for city services.<sup>7</sup> According to the Fiscal Impact analysis of Proposition C included in the voter guide, "This restriction in most cases prevents the City from entering into contracts with private companies even if doing so is shown through the bidding process to save the City money or create improved services or greater efficiencies."<sup>8</sup>

In addition to allowing for more competition between public- and private-sector providers, Proposition C directed the mayor to establish a seven-member Managed Competition Independent Review Board to advise the mayor whether city employees or private-sector contractors will provide certain services more efficiently and effectively. The board's recommendations are subject to approval by the mayor and the City Council.

After the passage of Proposition C, the mayor's office indicated that a number of city services would be candidates for managed competition, including:

- Solid waste collection and disposal
- Fleet maintenance
- Street pavement maintenance
- Building plan check
- Recyclables collection and processing
- Print shop
- Custodial services
- Grounds maintenance<sup>9</sup>

This report provides civic leaders with additional guidance. First, we lay out some of the key benefits that government and citizens can realize through a robust and well-organized managed competition process. As the following pages will show, the benefits of managed competition efforts go far beyond simply cutting costs. It can lead to significant innovation and increased effectiveness within local government agencies.

Next, we examine eleven major city functions which have been the subject of successful managed competition in other jurisdictions. According to the City of San Diego's implementing ordinance, the mayor (or his designee) is responsible for identifying possible functions to examine. Our list highlights the broad array of prime candidates for review and encourages further interest in and consideration of these functions. By examining the costs of these functions, and then applying conservative cost savings estimates based on the experiences of other jurisdictions, we have calculated a baseline for tangible savings that San Diego taxpayers could realize.

Finally, we conclude by discussing some of the lessons learned in other managed competition efforts. While experiences around the country demonstrate that critics are badly mistaken in their blanket rejection of this management tool, local lawmakers must remember the importance of establishing transparent processes and the need to protect taxpayer interests by clearly identifying service and performance measures.

# PART II

## BENEFITS OF MANAGED COMPETITION

Defenders of the bureaucratic culture and the status quo in government often claim that managed competition will devolve into political favoritism and harm public employees and government services. Typical of this view is J. David Cox of the American Federation of Government Employees, AFL-CIO, who has characterized managed competition as a “race to the bottom for employee compensation.”<sup>10</sup>

Such rhetoric discounts marketplace efficiencies and overemphasizes the differences between all municipal services and services that are regularly provided in the private marketplace. In fact, under the right rules, competition creates a “race to the top.” Every day, competition in the private sector is leading to innovations and greater effectiveness in serving the shifting demands of customers. Oftentimes, this allows contractors to provide comparable or even superior wages and benefits while reducing service costs and improving service levels. Truly open competitive environments foster innovation and continuous improvement, maximizing benefits while preventing price-gouging. In contrast, without routine and robust competition, public agency processes all too often become stale and inefficient. Incentives to learn and change are largely absent and public agencies must hope that management directive and “esprit de corps” will be sufficient to drive progress. Competition provides stronger incentives to innovate and offer better services more efficiently and effectively, lest a company or public agency lose a contract to a more suited competitor.

The public debate over managed competition generally revolves around cost savings. Indeed, this is the case in San Diego where the thrust behind Proposition C was to counter the city’s spiraling cost of providing government services and other fiscal challenges. This is understandable—costs are easy to grasp, the figures are usually large, and contracts are transparent. To be sure, one of the purposes of this study is to estimate some of the savings that the city could realize by implementing a comprehensive managed competition process.

But it would be a mistake to myopically focus on costs and ignore many of the other benefits of managed competition that are more subtle and often overlooked.<sup>11</sup>

Indeed, initiatives that are considered best practices for government procurement and service contracting utilize “best value” techniques where, rather than purchase based on cost alone, governments choose the best mix of quality, cost, and other factors. In addition, many competitive contracting failures are linked to a low-cost selection where the allure of increased cost savings negatively impacted service quality.

Data from the Council of State Governments (CSG) indicate that flexibility, access to personnel or skills not available in-house, and tapping of private-sector innovation are all important drivers of outsourcing.<sup>2</sup> Indeed, best practices for government procurement and service contracting are steadily moving toward “best value” techniques. The Federal Acquisition Regulations were amended in 1996 (FAR 2.101) to allow best-value source selections in outsourcings. Federal Acquisition Regulations define “best value” as “the expected outcome of an acquisition . . . providing the greatest overall benefit in response to the requirement.”

The ascendance of best value selection criteria is rooted in the simple concept of value—recognizing that the cheapest is not always the most desirable. Requiring the government to always buy the cheapest assumes all other things are equal, which they rarely are. The more complex the procurement or competition is, the more important issues other than lowest absolute cost will be.

From extensively reviewing case studies and historical literature on managed competition, it becomes clear that there are a number of major benefits that government can realize from this process.

## 1. COST

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While cost savings should not be the only factor for consideration, it is an important one. A review of over 100 studies of managed competition showed that cost savings range between five and 50 percent depending upon the scope and type of service.<sup>13</sup>

## 2. QUALITY

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Enhanced quality is one of the largest motivations for seeking competitive contracting. Competition provides independent contractors and government agencies with strong incentives to produce high-quality work and ensure proper performance. In addition, the contract can build in new accountability mechanisms that allow greater oversight, monitoring, and performance guarantees that are generally not present with in-house service delivery. According to data from the Council of State Governments (CSG), more than 18 percent of state agencies indicate that the desire for high-quality service is one reason they have outsourced.<sup>14</sup>

## 3. TIMELINESS

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Speedy implementation and timeliness of delivery is also an important motivation for competitive contracting.<sup>15</sup> Municipalities can tie payment to deadlines and milestones, shifting the incentive onto the contractor to complete the work faster or in a timely manner. A study of consultant use on transportation projects agreed: “Consultants represent a larger reservoir of manpower resources... and consultants usually have greater freedom to marshal resources at short notice.”<sup>16</sup> Consider the rapid response and repair of Los Angeles freeways following the Northridge earthquake in 1994, thanks to the aggressive use of contracting with incentive clauses. According to then-Governor Pete Wilson, “We were rebuilding the roads and bridges within 24 hours of the earthquake. . . . Each contract included an incentive—if the work was late, we charged a fine and if it was completed early, we paid a bonus and the motorists in Los Angeles were happy each time we did.”<sup>17</sup> More recently, Bay Area commuters greatly benefited from a contract which built in performance incentives to repair the

severely-damaged Interstate 580 connector to the San Francisco-Oakland Bay Bridge.<sup>18</sup>

## 4. ACCOMMODATE PEAK DEMAND

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Private companies, with more flexible staffing policies, can accommodate fluctuating demand more easily than government departments, which are often hamstrung by civil service rules and lengthy hiring and termination processes. That flexibility is important in areas where demand for services exhibit natural ebbs and flows. For example, the demand for construction permit review at San Diego’s Development Services Department (DSD) closely tracks with overall real estate activity. When the market is active, as it was between 2000 and 2005, workloads are greatly increased. When real estate activity is slow, as it currently is, there is more staff than work to go around.

This problem of a gap between the workload demands and staffing levels can be successfully resolved through managed competition processes that help right-size the organization to meet base level demand while augmenting staff through judicious outsourcing. For example, a 1990 study by the Wisconsin Legislative Audit Bureau concluded that contracting was used primarily for two reasons: to provide expertise unavailable to in-house staff, and to meet short-term, or “peak,” demand levels for which the addition of permanent staff would be uneconomical.<sup>19</sup>

## 5. GAIN ACCESS TO EXPERTISE

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People with the most experience and highest technical skills can oftentimes make more money in the private sector than in government. When governments need those kinds of skills, often the only way to obtain them is by competitive contracting. More than 32 percent of state agencies reported lack of state personnel and expertise as important reasons for contracting.<sup>20</sup> The Wisconsin Legislative Audit Bureau study attributed much contracting to need for special skills,<sup>21</sup> and a study for the Texas DOT found that one of the key reasons given for contracting was lack of in-house expertise.<sup>22</sup>

## 6. INNOVATION

Competitive contracting can produce innovative solutions to public service delivery. The freedom to invent “allows for old processes to be discarded in favor of entirely new ones—processes that integrate relevant technological advances and streamline communication channels.”<sup>23</sup> According to CSG data, at least one in five state agencies says that increased innovation is one of the top reasons for contracting.<sup>24</sup>

Why is competition necessary for innovation? One answer is that the public system does not always reward government employees for innovative ideas. In his study on government innovation, Sanford Borins found that public sector workers often are confronted with ingrained procedures and bureaucratic barriers that inhibit change.<sup>25</sup> Moreover, employees may not have property rights in their jobs or missions and rarely have independent authority to make change. Ideas typically need to flow up through multiple levels of management and often be approved by superiors who have a direct and personal interest in the existing status quo. At the end of the day, even if the employee’s idea is accepted, he or she is not likely to reap any professional reward.

In contrast, individuals in private firms have far more opportunity and incentive to develop and pursue innovative ideas at all levels than their public-sector counterparts.<sup>26</sup>

## 7. MANAGE RISK MORE EFFECTIVELY

Competitive contracting often allows governments to shift risks to contractors, which helps achieve the most efficient risk allocations and allows risk to be used as a management tool, rather than just something to fear. This attribute of contracting can be seen in San Diego County’s decision to sell its solid-waste assets—including four landfills, a recycling facility, and ten rural bin stations—to Allied Waste Industries in 1997. Not only did the \$184 million

sale provide much-needed funds during a financial crisis, but it also transferred environmental liability to Allied Waste.

Contracting also allows governments to mitigate the risk of cost escalation, since prices are established in the contract, making them more predictable. In addition, contracting allows public officials to address performance risk by building quality assurances and/or quality controls into project delivery under the terms of the contract.

Different officials often see different reasons to undertake a managed competition effort. For example, when the Council of State Governments surveyed budget directors about their primary reasons for competitive sourcing, a majority pointed to cost savings, followed up by lack of personnel/expertise and enhanced flexibility (see Table 1). However, when agency heads were asked the same question, lack of personnel/expertise was the number one answer (see Table 2). Other factors mentioned included speedy implementation, high quality service, and innovation.<sup>27</sup>

**Table 1**  
**Primary Reasons for Privatization**  
**(Budget/Legislative Directors)**

Cost Savings	68.4%
Lack of Expertise/Personnel	53.9%
Flexibility	32.8%
Speedy Implementation	14.4%
High Quality Service	9.2%
Innovation	1.3%

**Table 2**

**Primary Reasons for Privatization (Executive Agencies)**

Lack of Expertise/Personnel	50.7%
Cost Savings	36.6%
Flexibility	27.1%
Speedy Implementation	20.6%
Political Leadership	13.5%
High Quality Service	12.5%

These results are not surprising. In this case, budget directors are more interested in savings,

whereas agency heads list access to personnel and expertise as more important. In addition, it is important to note that this survey was conducted during a period of deficits and financial hardships. Indeed, the first CSG survey that was completed before the “dot-com” bubble burst on the economy in 2000 found that cost saving was becoming less dominant a motivation for contracting out as governments became more adept at it, and that acquiring the best value for public dollars was increasingly the goal.<sup>28</sup> Without the pressure of deficits and financial hardships, government entities had more flexibility in setting their goals and objectives when competitively contracting.

## SAN DIEGO COUNTY’S MANAGED COMPETITION PROGRAM

San Diego County has engaged in a number of successful managed competition and outsourcing projects since the late 1990s, earning it praise and making it a national model for other governments to follow. By 1999, the county was using private-sector contractors to provide hundreds of millions of dollars worth of government services. In 2005, nearly 19 percent of the county’s \$4.1 billion budget was devoted to paying for services provided by private companies, nonprofit organizations, and other government agencies. Nevertheless, most of the managed competitions the county has conducted have been won by government employees. In the past ten years, county employees have won 13 of the 17 managed competitions.<sup>1</sup>

### The county has performed managed competition projects in areas such as:

- Fleet Maintenance Services
- Workers’ Compensation Claims Administration
- Correctional Facilities Medical Services
- Alternate Public Defender’s Juvenile Dependency Division

The resulting contracts have resulted in annual savings of \$1 million for fleet maintenance services, \$330,000 for workers’ compensation administration, and \$235,000 for the Alternate Public Defender.<sup>2</sup> In the case of fleet maintenance, the county’s Fleet Operations Division beat out four private bidders to win a 46-month contract to maintain and service the county’s 3,200 cars, trucks, buses, tractors, and other heavy equipment. It achieved its savings by reducing staff by almost 25 percent and consolidating nine satellite garages into six. The county offered a \$1 million employee protection program to assist employees displaced by the streamlining.<sup>3</sup>

1 Jeff McDonald, “City looks at county’s outsourcing as blueprint,” *San Diego Union-Tribune*, July 23, 2006, <http://www.signonsandiego.com/news/metro/20060723-9999-1n23private.html>.

2 Lawrence B. Prior III, Lana Willingham, and Dr. William Eimicke, County of San Diego, “Bringing Private Sector Principles into Government,” undated, p. 33, <http://www.co.san-diego.ca.us/cnty/cntydepts/CAR/Principals.pdf>.

3 “SD County Competition,” City News Service, October 8, 1998.



# PART III

## MANAGED COMPETITION OPPORTUNITIES FOR SAN DIEGO

One of the challenges that managed competition efforts often face is finding the right starting point. The scope of modern government has grown over the years to include thousands of different services and activities. Faced with a daunting array of possible areas to focus on, decision makers risk “paralysis by analysis.”

Former Indianapolis Mayor Stephen Goldsmith simplified the process of identifying managed competition targets by applying the “Yellow Pages test.” According to Goldsmith,

*“If the phone book lists three companies that provide a certain service, the [government] should not be in that business, at least not exclusively. The best candidates for marketization are those for which a bustling competitive market already exists. Using the yellow pages test, [you] can take advantage of markets that have been operating for years.”*<sup>29</sup>

In this study we take a slightly different approach: we examined a sampling of the major activities the City of San Diego undertakes which have been subject to successful managed competition and outsourcing efforts by other municipal, county, or state governments. By no means should our review be considered an exhaustive selection of all managed competition and privatization efforts, but it provides a solid first step.

We first examined various City of San Diego documents to determine what the core functional activities of the city were—and which activities were not in that category. We then compared that list to the literature on successful managed competition. Where we found multiple case studies we undertook further examination to ensure that we were comparing “apple to apples” and that the case studies illustrated potential courses of action to the city’s management.

That process led us to identify eleven different functions that are, at the very least, strong candidates for potential managed competition. While

undertaking a review of all of these functions right at once would unduly tax management resources, we believe that these functions should form the basis of a core list to be considered. Hopefully, these case studies and services identified as opportunities for competition will serve to encourage city management to move with all due speed so that taxpayers may realize the benefits of managed competition.

## 1. WATER / WASTEWATER TREATMENT

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Currently, investor-owned water companies serve approximately 15 percent of the U.S. population, and 22 percent of California’s. The remaining population, including San Diego residents, receives its water from government-operated systems.

There are two leading factors responsible for the increased interest in public-private partnerships for municipal water services:

- Unfunded federal mandates related to requirements of the Safe Drinking Water Act (SDWA) and the Clean Water Act (CWA); and
- The lack of public resources available to address aging water and wastewater infrastructure.<sup>30</sup>

San Diego faces these problems in spades. In 2007, the city passed a \$440 million rate increase, phased in over four years, which will help finance over \$1 billion in infrastructure upgrades<sup>31</sup> that proponents of the rate hike have argued are needed to bring the system into compliance with various court orders and federal mandates.<sup>32</sup> On top of this, another increase has been planned that would cost an additional \$8.8 million—almost an extra 3 percent a month for the average San Diego resident—starting in January 2008.<sup>33</sup> This is despite the fact that San Diegans already pay some of the highest water and sewer prices in the nation (compared to other large cities).<sup>34</sup> At the same time, salaries and compensation are exerting increased pressure on the department’s budget. In the FY 2008 budget,

for example, more than \$166.4 million is budgeted for wages and benefits for the water and wastewater departments and combined they employ about 1,769 workers.<sup>35</sup>

Use of private sector companies to operate water and waste water systems has been shown to be a cost-effective tool for many municipalities. Cost savings from outsourcing water-delivery services typically range from 10 to 25 percent. A 1996 Reason Foundation study found that investor-owned water companies in California provide water at the same price to consumers as municipal water operations, even though the former must pay local, state, and federal taxes; generally cannot make use of tax-exempt debt; and are expected to earn a profit for their shareholders.<sup>36</sup>

It is critical to note that the private sector has an excellent decades-long record of providing clean and safe drinking water and complying with applicable environmental regulations. In fact, as federal environmental regulations have become more stringent, some cities have looked to the private sector as a means of meeting or exceeding these standards.<sup>37</sup> According to the U.S. Environmental Protection Agency under the Clinton administration,

*[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.*<sup>38</sup>

In addition, a 1999 survey found that privatizing water and wastewater services can improve compliance with environmental standards. Prior to privatization, 41 percent (12) of the facilities surveyed were not in full compliance with the federal Safe Drinking Water Act. One year after entering into a public-private partnership, all were

in compliance with federal water standards.<sup>39</sup> In short, private operators want to maintain their business, so they have just as much incentive to provide good service (in this case, high-quality water and wastewater services) as they do to keep costs and prices down.

### **Case Study: Hawthorne, California Long-Term Lease**<sup>40</sup>

In March 1996, the first ever long-term lease of an existing municipal water system was completed by the City of Hawthorne to the California Water Service Company (Cal Water). Cal Water made an up-front payment of \$6.5 million and must pay annual lease payments of \$100,000 for 15 years. The lease made Cal Water responsible for all needed capital improvements. City residents benefited from the economies of scale made possible by sharing some fixed costs with Cal Water’s adjacent Hermosa-Redondo Beach operations. The agreement included a provision that existing Hawthorne employees would be transferred to Cal Water at the same pay and benefit levels. Customer rates in Hawthorne were pegged at the same level as those in the Hermosa-Redondo district. By partnering with California Water Service Company, ratepayers in Hawthorne were able to bring market forces to bear to reduce the cost of mandated infrastructure upgrades as well as benefit from a greater economy of scale. Such lease arrangements could be an important consideration for San Diego, especially in light of the looming cost of necessary upgrades to the Point Loma Treatment Facility.<sup>41</sup>

### **Case Study: Auburn, Alabama Build, Own, Operate**<sup>42</sup>

In 1984, the City of Auburn faced the urgent need for capital improvement of a new wastewater treatment system. Trying and failing to secure federal grant funding for construction, in 1985 the city competitively bid a contract to build and own two new treatment facilities serving 34,000 people, and to operate them for 25 years.

The contract was won by a subsidiary of Metcalf & Eddy. The city provided \$26 million of the construction costs with tax-exempt bonds, and Metcalf & Eddy provided \$10 million in equity funds. The use of equity funds helped keep rates lower than they would have been if the city had used the traditional approach of financing the entire project through bonds and operating the new facilities with government employees. While rates did rise to cover the costs of the expansion, they were far less than they would have been if the city had performed the capacity expansion itself.

Important oversight powers were preserved. The city retained annual review of rates and the contract spelled out the terms under which increases in cost could be reflected in rates. The city also has the right to repurchase the plants at current market value at any time. In 1992, Auburn reviewed that repurchase option and decided against it. The company, now known as Veolia Water, continues to operate wastewater treatment facilities for the city under a 36-year agreement.

***City of San Diego Estimated FY 2007 Expenditures on Water/Wastewater: \$350,165,278. See table 10 on page 61 for discussion of how expenditures for these departments were adjusted.***

***Potential Savings from Managed Competition: \$35,016,300 - \$87,540,800 (10 – 25 percent)***

## 2. ENVIRONMENTAL SERVICES

More than 50 percent of U.S. cities of varying sizes contract all or part of their solid waste collection services. The Wall Street Journal estimates that the fraction of local governments contracting for waste collection grew from 30 percent in 1987 to 38 percent in 1990, to 50 percent by 1995.<sup>43</sup> Likewise, a 1995 study of 120 local governments in 34 states found that, between 1987 and 1995, the percentage of cities contracting out for solid waste collection increased by 20 percent and that 100 percent of participants saw cost savings from this approach.<sup>44</sup> Indeed, the vast majority of residents

in nearby municipalities and in the unincorporated areas of the county are served by private waste haulers, and most San Diego apartments and commercial buildings are served by a private hauler and not the city's Environmental Services Department.

Research has confirmed that competitive delivery of solid waste services typically generates cost savings on the order of 20 to 40 percent. A 1984 study of 20 California cities demonstrated savings of 28 percent to 42 percent from privatization, and a 1994 Reason Foundation study showed City of Los Angeles costs to be 30 percent higher than costs in neighboring cities with competitive contracting of waste services. In San Diego, there could be important benefits to contracting out some or all of collection services.<sup>45</sup> These include taking advantage of economies of scale, particularly in communities bordering jurisdictions that are served by private companies.

The use of managed competition, partnerships with the private sector, and outright privatization are not limited to waste collections. There has also been a growing trend in private sector management of landfills. The percentage of these facilities owned by the public sector declined from 83 percent in 1984 to 73 percent in 1997 and to 64 percent in 1998. A 1998 R. W. Beck survey showed that 27 percent of municipalities with populations greater than 100,000 were considering some form of privatization as an option to fulfill their disposal needs.<sup>46</sup>

The many reasons for this trend include managing liabilities, improving efficiency, cutting costs or debt, improving access to capital, and improving accountability. Each reason, or combination of reasons, lends itself to a different option for managing landfills. Options range from cooperative agreements with private firms for support services to management contracts, asset sales, and even complete reliance on the landfill market for services.

Finally, the story of managed competition in environmental services is one of competition encouraging innovations and productivity gains by the public sector entity. Indeed, in the examples of Phoenix and Charlotte (see the case studies below) a key theme is that the process of managed competition broke down bureaucratic barriers to change and the city department innovated in ways that allowed them to keep the contract but save taxpayers millions of dollars.

### **Case Study: Phoenix, Arizona Managed Competition for Solid Waste Collection**

In the late 1970s, a looming fiscal crisis prompted the City of Phoenix to become the first city to implement managed competition across a broad range of government services, including the collection of residential solid waste and recyclable materials. Under Phoenix's system, the city's Public Works Department bids alongside private firms for the right to serve each of six geographic sectors, with collection services in each sector being put out to bid on a rotating schedule (every seven years).

There have been 11 bid processes for solid waste collection since managed competition bidding began in 1979, resulting in savings of \$24.7 million.<sup>47</sup> Combined with the cost savings from managed competitions for landfill operation (\$7.7 million) and solid waste transfer hauling (\$6.5 million), the total savings due to managed competition for waste-related services totals nearly \$39 million, accounting for 87 percent of the \$44.8 million saved through the all of the city's managed competition efforts to date.<sup>48</sup>

Competition clearly prompted the city to review its service delivery methods. After private firms won the first two bids, Phoenix Public Works Director Mark Leonard recalls that "there was a concerted effort to evaluate why we weren't competitive in those two and what we needed to do."<sup>49</sup> The city developed a program called ROAM (Reduce Operating and Maintenance Expenses), under

which public managers, city employees and union representatives were able to streamline and find efficiencies to deliver more cost-effective, competitive solid waste services.

Since 1979, the city has won five of the 11 contracts and now serves many of the city's service zones. Over the first 15 years of competition, the inflation-adjusted costs of solid waste collection declined by 38 percent citywide.<sup>50</sup> In a recent interview, Deputy Public Works Director Mike Lopker stated that managed competition, "motivates everyone to do their best every day" and requires the public agencies to closely examine their service delivery costs, operations, and competitiveness.<sup>51</sup> Lopker added that a recent customer satisfaction poll ranking municipal solid waste as third highest among city services, an indication that the Public Works Department is performing well under managed competition.

An important lesson to be learned from Phoenix is that the entire system does not have to be privatized. What they found was that in some parts of the city the government-operated service was cost-effective and efficient. However, in other areas, the private sector was better. Such an approach has merit in San Diego where there are geographic areas in close proximity to existing private sector haulers and where economies of scale could help keep costs down. In other areas, remote from the marshalling yards and infrastructure of existing private-sector companies, the city's department might be the more cost-effective option. The experience of Phoenix suggests that managed competition can help San Diego think strategically about waste collection and examine in an open-minded fashion these kinds of competitive innovations.

### **Case Study: Charlotte, North Carolina Managed Competition for Solid Waste Services**

In 1996, the City of Charlotte decided to competitively bid trash collection services in the south quadrant of the city, shifting service provision from

the city's Solid Waste Services department to a private sector firm. According to Solid Waste Services' Wayman Pearson, "that really was a wake-up call for this department . . . . It made it easier for me to really start changing the way we perform."<sup>52</sup>

By applying private sector practices and innovations to their operations, Solid Waste Services was able to compete for and win a public-private bidding process for the west quadrant in 1997. In this competition, the city's final bid of \$2.2 million came in \$1.1 million under that of the lowest-cost private sector bidder. The city now bids out one quadrant at a time, and of the city's four quadrants, three are currently run by the city and one is under private contract. According to Pearson, "we've competed... and only lost one managed competition."<sup>53</sup>

There were important cost savings. According to Ed Sizer, former director of Charlotte's managed competition program, competition for solid waste collection services produced \$14 million in cost savings over the first five years of the program.<sup>54</sup> As Pearson notes, "competition is a winning proposition for the taxpayer . . . it drives efficiency."<sup>55</sup> In addition to competition, the city realized efficiencies from switching from backyard pick-up to roll-out service and investing in automated collection vehicles; these operational changes allowed the city to reduce the size of collection crews from three employees to one.

Charlotte's success is most clearly evident when looking at trash services in other parts of the state. A 2004 statewide study of 15 North Carolina cities found that Charlotte consistently outperforms other cities in cost and efficiency for garbage, recyclables, and yard waste collection; Charlotte's collection costs per ton for garbage were 45 percent less than the statewide average, while it spent 41 percent less per household to collect garbage than the statewide average.<sup>56</sup>

## **Case Study: San Diego County, California Landfill Asset Sale to Resolve Fiscal Crisis<sup>57</sup>**

Like many other jurisdictions, San Diego County responded to concerns about landfill capacity by constructing a new recycling facility, the North County Resource Recovery Facility in San Marcos, completed in 1994. High construction costs and low scrap values combined to leave the facility over \$100 million in debt. San Diego County was in trouble financially, and debt obligations began to affect other essential county services, as budget cuts dipped into already limited funding. The new chief administrative officer, Larry Prior, began to focus on running the county more efficiently. He explored alternatives for the future of the county's solid-waste system.

Prior sent the board of supervisors four alternatives. In late 1997, San Diego County completed a sale of all solid-waste assets to Allied Waste Industries (AWI). Before the divestiture, the county had contracted landfill operations to Norcal/San Diego Inc. (one of the initial eight bidders). The experience with Norcal proved positive enough for county supervisors to take full advantage of private-sector abilities; hence, the sale.

The sale included four landfills, the recycling facility, and 10 rural bin stations. The divestiture is the largest of its kind. The county netted \$184 million from the sale, after paying off \$100 million in debt from the construction of the recycling facility. The county used these funds to create an environmental trust fund to finance the long-term maintenance of closed county-owned landfills, to fill up a number of reserve funds, and to enhance other county services. Most important, the sale increased the county's bond rating (from Moody's Baa1 to A2 and from Fitch's A- to A+), further stabilizing the county's financial position. The higher bond rating enabled the county to refinance various projects at tremendous cost savings. Bill Kelly, the assistant auditor-controller, estimated that the county would save between \$280,000 and \$700,000 per year because of lower interest rates that accompany higher bond ratings.<sup>58</sup>

In addition to financial benefits, the divestiture transferred environmental liability from the county to AWI. Along with the facilities, AWI received all future liability, and all current liabilities were transferred through a contractual arrangement and figured into the price. County officials note that public health will continue to be protected, safety and environmental standards will be maintained, and regional trash disposal will be accomplished.

San Diego County supervisor, Dianne Jacob, said of the sale: “Our responsibility was to find a long-term solution that would achieve all our objectives—and divestiture was the solution. The fact is that the [private] sector can function far more cost effectively in this industry—resulting in better services and lower trash collection rates for consumers.”<sup>59</sup> Jacob also pointed out that even though the county had sold all its assets, it would “still control one of its core competencies by serving as the local enforcement agency.”<sup>60</sup> In this role, the county will continue to monitor AWI to enforce compliance with health, safety, and environmental regulations.

### **Case Study: Fort Worth, Texas Landfill Contracting**

In 1982, the City of Fort Worth began contracting with Waste Management (WMI) to operate the Southeast Landfill in Fort Worth, Texas. According to Assistant City Manager Charles Boswell, city officials were happy with the performance of WMI, noting that landfill operations were “problem free” once WMI took over.

Fort Worth officials also noted that WMI brought expertise that local employees did not have. For example, similar to the situation that San Diego faces at the Miramar landfill, WMI and Fort Worth officials determined that something needed to be done to address future needs, as the Southeast Landfill had an estimated five years of remaining capacity. Absent expansion of the landfill, the municipality would incur additional costs. Through a public-private cooperative, WMI initiated four pilot programs—at no additional cost to the city—to

better manage the waste and preserve landfill space. These pilot programs included:

- Separate brush collection;
- Separate bulky-waste collection;
- A composting program; and
- Automated container collection that enables “pay as you throw” (PAYT) rate structure—customers who discard more waste pay more.

The brush and bulky-waste programs turned out to provide few benefits, but after conducting the seven-year, 8,000 customer PAYT pilot program, city officials decided to launch a larger program in July 2003 covering 163,000 households. And cost savings have been dramatic: solid waste disposal costs fell from almost \$32 million under the old system to approximately \$25 million under PAYT.<sup>61</sup>

Fort Worth is also managing its waste more efficiently, using a combination of PAYT and increased recycling. Since March 2003, the program has diverted over 30,000 tons of recyclables, 11,000 tons of yard trimmings, and 2,600 tons of brush away from landfills. Taxpayers can now expect longer life for their landfill, saving them the cost of expanding or constructing new facilities.

### **Case Study: Chandler, Arizona Competitive Contracting to Extend Landfill Life<sup>62</sup>**

The City of Chandler, located just outside of Phoenix, owns one landfill. City officials opted to contract out the operation of the landfill, hoping to extend its life expectancy. They anticipated that a private firm would have more expertise and greater access to innovative techniques than were available in-house.

Chandler originally opted to enter into a contract with Laidlaw in 1996. Purchased by Allied Waste Industries (AWI), the firm continued to win re-bids on the contract until the landfill was closed in October 2005. AWI extended the life of the landfill

by an estimated 40 percent through the initiation of a sophisticated compaction system. Simply put, by squeezing the trash together more effectively, it allowed the landfill to take in more waste and extended the life of the landfill. Specifically, Chandler’s landfill achieved a compaction rate of 2,000 pounds per cubic yard, versus the waste disposal average of 1,200 to 1,400 pounds per cubic yard.

To do this, the city put in place an incentive structure for Laidlaw. For compaction rates below 1,600 pounds per cubic yard the company paid a penalty. If the company achieved a compaction rates above 1,699 pounds per cubic yard the firm received a bonus (see Table 3). The rate was measured by the city.

**Table 3**  
**Chandler, Arizona: Compaction Rate\* Bonus and Penalty Structure**

1,200–1,299 =	\$2.00 per ton penalty
1,300–1,399 =	\$1.50 per ton penalty
1,400–1,499 =	\$1.00 per ton penalty
1,500–1,599 =	\$0.50 per ton penalty
1,600–1,699 =	No penalty, no bonus
1,700–1,799 =	\$0.50 per ton bonus
1,800–1,899 =	\$1.00 per ton bonus
1,900–1,999 =	\$1.50 per ton bonus
2,000–2,099 =	\$2.00 per ton bonus

*\*pounds of refuse per cubic yard*

Source: City of Chandler, Arizona, “Special Terms and Conditions: Municipal Solid Waste Landfill Operations,” Bid No. SW6-0495-1236, April 1996, p. GS-11.

The compaction rate produced cost savings for citizens in two ways: first, citizens were able to avoid landfill expansion costs; second, tip fees fell, in part because more waste “fits” in a smaller area. The city’s superintendent of solid waste and recycling, Gerry Backhaus, suggests that these sorts of incentives are not found in the public sector. Backhaus went on to praise AWI: “They [worked] with me,

not against me...like a mutual marriage.”<sup>63</sup> Beyond landfill operations, Chandler uses competitive contracting for other solid waste disposal services.

### **Case Study: Philadelphia, Pennsylvania Contract to Build and Operate New Biosolids Recycling Center**

Motorists crossing Philadelphia’s Platt Bridge frequently smell the foul odors emanating from the City of Philadelphia’s Biosolids Recycling Center (BRC). The BRC is operated by the city’s water department and treats sewage sludge and turns most of it into compost for gardening and horticulture, revegetation of strip mines, fertilizer for farmlands, and restoration of city parks and play fields. The rest (approximately 30 percent) is sent to landfills.<sup>64</sup> Bad smells aside, the Environmental Protection Agency warned the city that it is violating its own clean-air laws and is threatening significant fines.<sup>65</sup>

To address these problems, in early 2007 the administration of Mayor John Street proposed contracting the construction and operation of a smaller recycling center with Houston-based Synagro. The company would build a \$66 million plant on the existing 72-acre BRC site but take up only about half as much space, freeing up land for other city uses.<sup>66</sup> The new recycling center would be an enclosed, state-of-the-art facility which would dramatically reduce the smell of the plant and bring it into compliance with federal regulations.

In addition to the technological and environmental benefits of the contract, it would provide the city with significant cost savings. According to the city’s managing director, Pedro A. Ramos, the contract would save the city \$190 million over 25 years.<sup>67</sup> None of the approximately 130 current BRC employees would lose their jobs, as they would either be hired by Synagro or transferred to other city positions, and many would fill some of the 300 Water Department positions that are presently vacant. The mere prospect of contracting out the BRC brought stiff government-employee union opposition and union promises to reduce costs,



but on top of Synagro's estimated cost savings, the Street administration still favors the company for its improved technology and smaller environmental footprint.

As of this writing, the proposal is still under consideration. If approved by the city council, the plan would be the city's first major outsourcing in a decade.

### **Case Study: Buffalo, New York Curbside Recycling Program**

Facing poor performance and soaring overtime costs, the City of Buffalo decided to contract its curbside recycling program in 2002. Said Mayor Anthony M. Maisello at the time, "Overtime is rampant. We're not finishing our routes on time. We've had to resort to weekend pickups."<sup>68</sup>

Three companies bid on the contract, with the winning bid going to Browning-Ferris Industries, Inc. (BFI). BFI submitted the lowest bid of \$1.57 million per year for five years. Under the agreement, the company continued to use city recycling trucks, but picked up all fuel, maintenance, and insurance costs. According to Mayor Maisello, the contract was expected to save \$758,000 without eliminating any permanent full-time jobs. The agreement would transfer 43 city recycling employees to garbage collection positions and eliminate 55 seasonal positions.<sup>69</sup> Public Works Commissioner Joseph N. Giambra claimed the changes should practically eliminate overtime costs, except during snow emergencies.

BFI has since been acquired by Allied Waste Industries, Inc. The Phoenix-based company currently has about 26,000 employees, operates in 110 markets in 37 states plus Puerto Rico, serves approximately 10 million customers, and operates 168 active solid waste landfills and 57 recycling centers.<sup>70</sup>

***City of San Diego Estimated FY 2007 Expenditures on Trash Collection: \$39,323,442***

***Potential Savings from Managed Competition: \$3,932,344 - \$9,830,861 (10 – 25 percent)***

***City of San Diego Estimated FY 2007 Expenditures on Landfills: \$25,805,497***

***Potential Savings from Managed Competition: \$2,580,550 - \$6,451,374 (10 – 25 percent)***

***City of San Diego Estimated FY 2007 Expenditures on Recycling: \$19,600,811***

***Potential Savings from Managed Competition: \$1,960,081 - \$4,900,203 (10 – 25 percent)***

## **3. FLEET MAINTENANCE/MANAGEMENT**

A 1990 survey by the Mercer Group found fleet maintenance to be one of the key areas in which governments used privatization. Governments increasingly are turning to the private sector to maintain their vehicle fleets for many reasons, including:

- Technology changes superseding government mechanics' job skills;
- Inventory shrinkage;
- Uncontrolled expenditures through excessive subcontracting; and
- Lack of rigorous preventive maintenance, causing increased replacement costs.<sup>71</sup>

Between 1982 and 1992, the use of private contractors for fleet management and vehicle maintenance increased 27 percent.<sup>72</sup> Though there are no comprehensive recent surveys, industry executives are still seeing an upwards trend toward outsourcing fleet operations. According to one executive with Penske Truck Leasing, "fleet maintenance and management are ancillary to the job of running the business of government. More and

more, municipal fleets are turning to companies whose core competence is fleet maintenance, allowing them to focus more on the services that fleet provides.”<sup>73</sup>

Experiences from numerous jurisdictions demonstrate that contracting, when properly implemented, can result in substantial first-year cost savings and even greater savings in subsequent years. A 1988 study comparing in-house and contract services for motor vehicle maintenance found that contractor costs are 1 percent to 38 percent below municipal costs for equivalent or higher levels of service. In conversions to contracting, wage levels generally remain similar, but the number of operating and overhead employees is reduced because of greater productivity.

### **Case Study: Dallas, Texas Heavy Sanitation Vehicle Maintenance & Repair**

In 2003, the City of Dallas undertook a managed competition process for the provision of fleet maintenance services. The bid received from the Equipment Services division of the city’s Equipment & Building Services department (which maintains the city’s 4,600-unit fleet) was selected over the bids submitted by three private vendors. Consistent with best practices, city staff committed to monitor the cost of service and ensure that the department was meeting the goals it had stated in its bid.

In the first two years of its contract, Equipment Services’s costs exceeded the budgeted amount by approximately \$2.8 million, largely due to unexpected, unpredictable repairs necessitated by accidents, abuse, or misuse of equipment, as well as vandalism, acts of nature, and vehicle modifications.<sup>74</sup> In May 2005, the city issued a request for bids for privatized fleet maintenance and repair services for a five-year term, and Equipment Services did not submit a competing bid. The objectives of this process were to reduce overall fleet maintenance costs and increase overall fleet operating efficiencies while maintaining equipment

availability levels currently provided by Equipment Services.

Through this process, Dallas officials determined that taxpayers could receive the greatest benefit through contracting out only the maintenance and repair of heavy equipment class sanitation vehicles. While the 293 vehicles in this class represented just 6.4 percent of the total city fleet in 2005, they accounted for 23 percent of total fleet maintenance expenses.<sup>75</sup>

After evaluating bids, the city awarded a five-year, \$16 million contract for heavy sanitation vehicle maintenance and repair contract to Serco North America, Inc.<sup>76</sup> The city expects this contract to produce an annual savings of approximately \$910,000, though savings in the first year of the contract were lower due to implementation costs associated with service center consolidation and upgrades.<sup>77</sup>

### **Case Study: Indianapolis, Indiana Fleet Maintenance**

Under the administration of Mayor Stephen Goldsmith, the City of Indianapolis initiated a comprehensive managed competition program in 1992, and the case of Indianapolis Fleet Services (IFS) is widely regarded as one of the city’s most successful managed competitions.

In the spring of 1995, IFS was selected in a competition with three of the largest private-sector vehicle maintenance providers for the fleet services contract. Competition prompted IFS to streamline and make other operational and structural changes. It cut middle management positions and enabled employees to create self-managed work teams, giving mechanics more control over their work and allowing IFS to simultaneously shrink its workforce and improve quality.<sup>78</sup>

The union employees also agreed to forego some automatic cost-of-living increases and take a portion of their compensation in performance

bonuses, which could be offset by financial penalties if the department misses certain performance expectations outlined in the contract. To increase their productivity—and minimize down time of vehicles—employees also asked to be able to keep some workers on the job during scheduled government holidays. (Table 4 compares cost and performance data before and after IFS competition.)

**Table 4**  
**Indianapolis Fleet Maintenance:**  
**Before and After Competition**

	Before	After
Annual Costs	\$5.3 Million	\$2.8 Million
Productivity per mechanic	very low	up 22%
Employee Compensation	Automatic Cost of Living Increase	Performance Bonuses
Ratio of Workers to Managers	1.1 to 1	4 to 1
Number of Employees	119	82
Number of Complaints	24	5
Number of Vehicles Serviced	2,104	2,202

maintenance employees began to propose outsourcing to save money. For example, the in-house unit was not competitive with private shops for auto body work, so it began outsourcing that work and moving the displaced employees into more competitive areas.

Unfortunately, in 1998, the union local and the city administration added a Memorandum of Understanding (MOU) to the contract that discontinued the use of performance bonus and returned to flat pay rates for employees with annual 3 percent increases. IFS employees supported this change, seeing little potential for additional performance bonuses once

the city had realized the cost savings resulting from the original contract.<sup>80</sup> By reducing their incentives for innovation, they went back to the “old way” of thinking about providing services.

According to a 1997 U.S. General Accounting Office report, Indianapolis’s managed competition for fleet maintenance produced significant results:<sup>79</sup>

- Approximately \$4.2 million in total cost savings from 1995 to 1997;
- An estimated cost savings of 21 percent over government provision of service;
- Fewer labor grievances in first year of contract than in the preceding year; and
- A 66 percent reduction in workers compensation claims between 1994 and 1997.

In the first year of the contract, IFS surpassed its cost-containment goals. Even after deducting for penalties imposed for failing to fully comply with certain other performance goals, the employees earned over \$75,000 in incentive payments. Due to the financial incentives to save money, fleet

Nevertheless, the value of managed competition persists. Even though the city no longer competitively bids its fleet maintenance operations, IFS has continued to streamline its operations in recent years. Even as the number of vehicles maintained by IFS nearly doubled from 2,200 in 1995 to 4,200 in 2005, the number of employees dropped from 82 workers to 76 workers over the same period.<sup>81</sup> To control costs, IFS continues to outsource some work to private vendors. It has also pursued federal grants to acquire more fuel- and cost-efficient technologies.

***City of San Diego Estimated FY 2006-07 Expenditures on Fleet Maintenance: \$51,018,594***

***Potential Savings from Managed Competition: \$5,101,859 - \$12,754,649 (10 – 25 percent)***

## 4. STREET MAINTENANCE

A 1995 study of 120 local governments in 34 states found that between 1987 and 1995, the percentage of cities contracting out for road maintenance increased by 19 percent, bringing the total percentage of cities outsourcing for road maintenance services to 37 percent. Cost savings from outsourcing road maintenance services typically range from 25 to 50 percent. A 1984 study showed that contracting out for highway maintenance cost half as much as delivering these services in-house.<sup>82</sup>

### **Case Study: Indianapolis, Indiana Public-Private Competition**

As part of its comprehensive managed competition program in 1992 under the administration of Mayor Stephen Goldsmith, Indianapolis opened up pothole filling, asphalt laying, crack sealing, berm repair and other street maintenance functions to competition. The first of these was pothole filling.

Forced to compete, city workers streamlined operations, dropping from eight workers on a crew to four, and going from two trucks to just one. Even after these changes, costs were still not competitive with private firms. In investigating the reasons why, city employees discovered that the overhead costs of indirect management were enormous. There were 92 truck drivers and 32 management supervisors. “We can’t compete if you are going to attribute their salaries into our costs of doing business,” the union told the mayor.<sup>83</sup> In response, Mayor Goldsmith laid off most of the supervisors. The city unit subsequently won the contract.

Changes to the government accounting process played an important role in enhancing the competitiveness of city workers. To ensure a level playing field for public and private sector bidders, the city hired KPMG Peat Marwick to bring activity-based costing to the city’s government accounting process. This allowed the city’s maintenance division to calculate the total costs—including equipment, material, labor, and overhead costs—for all of the services

they perform and to discover sources of waste and opportunities for efficiency gains. As a result, the city was able to determine exactly how much it costs to seal every mile of cracks in the road or to repair every pothole. It is an important lesson. To make the most of managed competition efforts, it is critical that cities have the means available to measure activity costs so that the indirect costs are also measured. Not only does this ensure a level playing between the public and private sectors, it better enables the public-sector participants in managed competition to identify waste and inefficiencies.

As a result of managed competition, cost savings for street maintenance in Indianapolis were estimated at approximately \$700,000, or 30 percent, between 1992 and 1996.<sup>84</sup> During that same period, city employees reduced the projected cost of pouring a ton of asphalt by 25 percent from \$407 to \$301, and the chuckhole (pothole) crew experienced a 68 percent increase in productivity, increasing the number of lane-miles worked per day from 3.1 to 5.2.<sup>85</sup> In sum, the city also experienced a 200 percent annual average increase in lane miles repaired between 1993 and 1996.<sup>86</sup>

### **Case Study: District of Columbia Asset Management Contract**

In 1998, the District of Columbia Department of Public Works (DCDPW/DDOT) and the Federal Highway Administration (FHWA) sought to establish a performance-based contract for the National Highway System in the District, covering the maintenance of 75 miles of major streets and highways, as well as ancillary facilities like traffic signals, drainage ditches, and maintenance of street curbs and gutters.<sup>87</sup> The contract was awarded in 2000 to VMS. The DCDPW project manager monitors the contract using public surveys and monthly field inspections. Ratings of good, fair, and poor are given in relation to performance criteria including rideability, cracking, skid, public satisfaction, and other factors.<sup>88</sup> Payment includes incentives for performance and depends on compliance with the performance measures. The five-year \$60 million contract was

awarded on a best-value selection.<sup>89</sup> The project (The DC Street Initiative) is the largest transportation investment in DDOT's history and is also the first time that the FHWA has joined with a DOT on a program to preserve transportation assets.

Since the contract was signed, Washington, D.C. has seen major improvements in the quality of its roads. In the first year, performance was the low 80's (out of 100).<sup>90</sup> This improvement is in part attributable to the specialization through subcontracting to smaller companies or companies that VMS creates for an area of maintenance. VMS has positively affected the neighborhood with new job hiring, community service participation, and subcontracting.<sup>91</sup> The DC government team is specifically satisfied with the progress on tunnels, which were dilapidated prior to the contract, snow removal, and emergency responses.<sup>92</sup> Overall, DDOT, FHWA, the DC public, and VMS are satisfied with the project in that the assets are generally in better condition than they were two years ago.<sup>93</sup>

### **Case Study: Laguna Niguel, California Competitive Contracting**

The City of Laguna Niguel, California, began contracting for street maintenance with Charles Abbott Associates on July 1994. The contractor manages subcontractor work crews on an as-needed basis to repair streets, clean storm drains and channels, install signs, replace broken sidewalks, trim street trees, and perform other services.

In its first year of competitive contracting, the city saved approximately \$360,000, 31 percent cheaper than the same services previously performed for the city by Orange County. The cost savings totaled more than \$1 million between fiscal years 1992-93 and 1996-97.<sup>94</sup> The city used these savings to significantly expand its street maintenance services, while keeping the budget well below its previous level before competitive contracting.

"The real reason we are contracting is that now I have control over maintaining our streets, whereas

before, the county was the one that decided what got done and when. So the significant difference just in administering the street maintenance program is not only in cost savings, but the fact that I can direct it and make the decisions," said Public Works Director Ken Montgomery.<sup>95</sup>

The private contractor has also improved the level of service for city residents. The average number of complaints decreased 44 percent,<sup>96</sup> with over 40 percent of complaints resolved on the same day.<sup>97</sup> In addition, the response time in resolving customer complaints dropped from 30 days to under 5 days.<sup>98</sup>

The response time for emergencies also had to be considered when the city privatized. Officials wrote into the contract that "all of the subcontractors that our maintenance contractor hired had to be available to respond to call-outs (emergencies), and this has worked out extremely well," said Montgomery.<sup>99</sup>

The city has been very satisfied with the services provided by Charles Abbott Associates. In 2004, it voted unanimously to add five additional years to the firm's contract to provide weed abatement services, and in January 2007 it unanimously approved a five-year contract for building and safety services with the firm.

In addition to street maintenance, the City of Laguna Niguel also contracts with private vendors to provide street sweeping services and traffic signal maintenance.

***City of San Diego Estimated FY 2006-07  
Expenditures on Street Maintenance: \$50,681,086***

***Potential Savings from Managed Competition:  
\$5,068,109 - \$12,670,272 (10 – 25 percent)***

## **5. PARKS AND RECREATION**

In the City of San Diego, grass located on a city park is cut and maintained by city employees. Grass in an adjacent road median or on a city-owned slope may be maintained by a contractor hired by the city. If

there was a function which could be looked at to see if costs savings could be achieved through managed competition, it would seem to be this one.

Subjecting park maintenance to managed competition is not extraordinary. A 1995 study found that between 1987 and 1995, the percentage of cities contracting out for park maintenance services increased by 10 percent, bringing the total percentage of cities contracting the service to 33 percent.<sup>100</sup>

Cost savings from outsourcing recreation facilities operation and management typically range from 19 to 52 percent. Cost savings from outsourcing park landscaping and maintenance ranges from 10 to 28 percent.<sup>101</sup>

A 1984 study comparing in-house and contract park turf maintenance found that contract service had 28 percent lower costs and equivalent service quality.<sup>102</sup>

### **Case Study: Indianapolis, Indiana Competitive Contracting**

Indianapolis competitively contracts for lawn trimming at more than 45 neighborhood parks. Since contracting began, mowing complaints have fallen by 95 percent. This has freed up Parks Department employees to concentrate on the city's large regional parks.<sup>103</sup>

The city initially contracted to have grass cut every six weeks, but since temperatures and other weather conditions vary with the seasons—grass grows much faster during the spring than during the winter—this was a meaningless performance measure. In addition, monitoring contractors to ensure that they really were mowing when they said they were was costly and tedious.<sup>104</sup> During the next round of contracting, the city decided that it did not really want the grass cut every six weeks; it wanted the grass kept short. So now the city contracts with a company to keep the grass less than four inches high and pays by the acre. Monitoring is easier now, too, as a city employee can simply go out at random intervals and measure the grass with a ruler.<sup>105</sup>

### **Case Study: Rancho Palos Verdes, California Commercialization**<sup>106</sup>

In 1993, a municipal budget shortfall prompted the City of Rancho Palos Verdes, California, to reconsider its priorities. Pressed for cash, Rancho Palos Verdes eliminated its recreation programs. Before getting out of the recreation business, the city surveyed the surrounding area and discovered that private for-profit and non-profit organizations already were providing—at reasonable prices—most of the recreation services the city was running. After hearing the city would be dropping the recreation programs, many of the class instructors went to the city and said, “We will continue the programs if you will rent us your facilities.” The result: many of the city recreation classes still are being offered. The only difference is they are being run privately and without a subsidy from the city. In fact, the city is now making a small net profit from the facility rental.

### **Case Study: Central Park, New York City, New York Transfer to Non-Profit**<sup>107</sup>

Turning over partial ownership or management of city parks to non-profit groups and neighborhood associations often is the best way to ensure they remain a public asset. New York City's Neighborhood Open Space Coalition has assumed control from the city of hundreds of abandoned lots and parks in this way, turning many dangerous eyesores into gardens. Nearly one-fourth of the city's nearly 1,500 public parks are now cared for by community associations under the Operation Green Thumb program.

Even one of the most famous parks in the country is run by a non-profit and was only cleaned up when it was spun off from the city government. The non-profit Central Park Conservancy has raised more than \$100 million for New York City's Central Park since its founding in 1980, taking over the care of trees, lawns and plants, and providing more than half the Park's operating costs. By 1989, 72 percent of Central Park users said the park felt safer after the Conservancy got involved.

Crime dropped 59 percent and robberies plummeted 73 percent. The drop in crime is attributed to the large increase in park activities put on by the Conservancy. Good uses drove out a lot of the bad uses.

The Conservancy has since funded two-thirds of the renewed landscaping project “Wonder of New York.” When the project is completed, the Conservancy will have paid for just over half of the \$135 million in capital improvements in Central Park since 1980.

As manager of the park, the Conservancy has protected the park by maintaining and then increasing park staff. Since 1991, Central Park has lost 54 city-funded staff due to budget cuts. Today, the Conservancy’s payroll includes 172 of the park’s 244 workers, and the city now pays only \$5.4 million of the park’s \$15.9 million total operating budget. Additionally, the city has profited from the renewal of Central Park, taking in \$4.25 million in concessions from the skating rinks, vendors and many other sidewalk businesses.

Conservancy leaders recently have called for outsourcing the management of all of the city’s parks, for it would bring competition, accountability, and marketplace discipline.

**City of San Diego Estimated FY 2006-07 Expenditures on Parks and Recreation (excluding golf courses):**  
**\$95,495,273**

**Potential Savings from Managed Competition:**  
**\$9,549,527 - \$23,873,818 (10 – 25 percent)**

## 6. GOLF COURSES <sup>108</sup>

Managing golf courses is not a core municipal service. Between 1987 and 1995, the percentage of cities contracting out for golf course services increased by almost 10 percent, bringing the total percentage of cities contracting for golf course operations to 25 percent. Here in San Diego, the cities of Oceanside, Escondido, Encinitas, Carlsbad, and Chula Vista have all found it advantageous to outsource some or all of the operations of facilities which the city either owns or had a significant role in helping to develop. In contrast, while the City of San Diego has franchise agreements to operate the Torrey Pines and Balboa Park pro-shops, city staff is responsible for managing and maintaining the city’s three 18-hole regulation courses.

Most municipalities privatize golf operations to increase revenues and to provide needed capital improvements. Table 5 provides a comparison of the revenues received by some California cities following the privatization of golf courses.

**Table 5**  
**Municipal Golf Course Revenue Comparison**

Descriptive Information			Revenue		
Course Name	City	Last Year Public	Public Operation	Private Operation (First Year)	1995-96 Fiscal Year
El Dorado	Long Beach	FY 1983	(\$68,918)	\$201,087	\$609,714
La Mirada	Los Angeles	FY 1981	\$155,547	\$182,558	\$1,006,537
Los Verdes	Los Angeles	FY 1981	\$94,553	\$56,412	\$1,187,307
Mountain Meadow	Los Angeles	FY 1988	\$569,233	\$708,704	\$1,407,377
Rec Park 18	Long Beach	FY 1983	\$126,249	\$201,087	\$690,532
Rec Park 9	Long Beach	FY1983	\$24,403	\$67,029	\$187,155
<i>Source: Reason Foundation.</i>					

Of the six examples cited, five cities achieved revenue increases between 24 percent and 400 percent within the first year of private operation.

There are scores of examples of successful golf-course privatization. More than 500 municipalities throughout the United States have successfully completed the privatization process. To be sure, some contracts have been more successful than others. It is important to consider the range of outcomes when thinking about how the City of San Diego might use managed competition in relationship to its golf course operations.

### **Case Study: Los Angeles County, California Increased Revenue**

The County of Los Angeles currently contracts out 16 of its 19 municipal golf courses. Of these 16 courses, nine are leased to small firms or groups of individuals (mostly local golf pros) and the other seven to larger management firms.

The county started the contracting process as a way to increase revenue, and has been satisfied with the effort. An example of the county's success is the Mountain Meadow Course. Before the course was privatized in fiscal 1989, it was generating revenues of approximately \$570,000. After privatization, county revenues increased to \$708,000. As of fiscal 1996, Mountain Meadow generated revenues of \$1.4 million, more than doubling the profit of the pre-contract year. The important thing to note about Los Angeles is that the process can reward locally-based entrepreneurs who, knowing the facility, can help the city minimize costs and maximize the value of its assets.

### **Case Study: New York City, New York Rescue from Decrepitude**

Since contracting out 13 golf courses, New York City has gone from losing \$2 million a year to realizing a profit of over \$2 million a year. Seven of New York's courses are run by American Golf Corporation

(AGC). New York City officials are quick to emphasize the courses' disarray and disrepair when run by the government. "Abandoned cars littered the courses, golfers had been mugged by others, and employees spent more time playing cards than working." To date, American Golf has invested more than \$4.5 million into improving the courses, far in excess of the minimum-contract requirements. It did so not out of philanthropy but because it understood that these sorts of investments would improve services, and thus its business.

The company overhauled the clubhouses, repaired the irrigation systems, brought in new golf carts, and revamped the pro shops and snack bars. AGC has overhauled cash handling and security procedures and instituted full financial accountability and reporting standards. As a result, AGC now sets the standard for other city concessionaires. Rounds played at the seven courses have increased by 50 percent—from 300,000 before AGC took over to more than 450,000 in 1997. Before AGC assumed responsibility for the seven courses, the city was losing \$1 million a year on operating the seven courses. In 1997, AGC paid New York City more than \$1.7 million in rent for the seven courses.

Privatization did generate some initial resistance from club members at these courses who were afraid they were going to lose their privileges. These problems have worked themselves out. Most of the employees were transferred to other departments or hired by the private contractor. New York City officials attribute the success of the privatization to a strong monitoring program.<sup>109</sup>

### **Case Study: San Francisco, California Environmental Innovation**

In 1995, Arnold Palmer Golf was selected by the National Park Service to invest over \$4 million in capital to renovate and operate the Presidio Golf Course in San Francisco. That year, the former military course was opened for public play for the first time in its 100-year history. To date, Arnold Palmer Golf has invested over \$6 million in course improve-



ments without closing the course or interrupting play. The capital improvements include a three-phase project. First came the refurbishment of the grounds, including a \$1.1 million irrigation system; the second phase included a 45-stall practice range featuring three tiers of grass tees and five target greens; the final phase is the completion of a 7,000 square foot clubhouse with underground golf cart storage. In 1996-1997, the Presidio has doubled the income paid to the National Park Service and surpassed their original revenue projections by 13 percent. Rounds have increased 250 percent since 1995 and revenues have increased by 550 percent. The Presidio Course is currently supporting 68,000 rounds per year and bringing in annual revenues of approximately \$5 million.

In partnership with the Center for Resource Management, a nonprofit group that helps develop working relationships between industry and environmental groups, Arnold Palmer Golf is using the Presidio as a demonstration project for implementing environmentally friendly programs that can be utilized by golf courses throughout the nation. Specific environmental innovations include a multi-phased water conservation and management program based on a state-of-the-art irrigation system, a weather monitoring system providing the exact amount of water required, the use of reclaimed water when available, the incorporation of a least-impact turf maintenance program aimed at preserving the quality of the grounds, and implementation of a chemical-applications management plan to control chemical use and minimize pesticide use. Based on Arnold Palmer's innovative environmental practices, the Presidio Golf Course was selected as one of nine winners of the 1996 Environmental Achievement Awards by the San Francisco Green Ribbon panel, a nonprofit group of environmental professionals from the business community and the public sector.

Arnold Palmer's management plan has been designed to provide maximum public access to the game. Programs include a project with the San Francisco police to bring golf to at-risk

youths and partnerships with community-based groups—such as the Center of Independent Living and Whistlestop Wheels—to provide easier access for seniors and the disabled.

San Francisco's entire parks and recreation program also benefits from privatization. Palmer Golf's maintenance staff regularly shares state-of-the-art maintenance equipment with the city for use on softball fields and other open spaces and lends expertise in recreational services to the Gordon F. Moore Park.

***City of San Diego Estimated FY 2006-07  
Expenditures on Golf Courses: \$11,690,024***

***Potential Savings from Managed Competition:  
\$1,169,002 - \$2,922,506 (10 – 25 percent)***

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## 7. LIBRARIES

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Across the country, tight municipal budgets have prompted dramatic cuts in funding for public libraries in the 1990s, forcing so many libraries to close their doors in recent years that the American Library Association says it is no longer able to keep track of all the closures. For example, in 1990, officials in Worcester, Massachusetts, a city of 170,000, closed all six library branches. In Los Angeles, the county library system was threatened with the closure of about 50 of its 87 branches.<sup>110</sup> Chicago Mayor Richard Daley claimed that the city saved \$3.7 million by contracting out management of the Harold Washington Library.<sup>111</sup>

Lack of funding is hardly the only motivation for contracting library services, however. Other reasons local governments have sought to contract their library services include improving the quality of management, improving service levels, acquiring expertise that is lacking in-house, and meeting time constraints.<sup>112</sup>

To date, the City of San Diego has managed shrinking resources by cutting hours at branch libraries. As of the summer of 2007, most branch libraries are open less than 45 hours a week. Indeed, library supporters

considered it a great victory in 2007 when the city was able to avoid another round of reductions in the number of hours of system operations.<sup>113</sup>

There is another way. Municipalities have increasingly looked to privatization of library operations to not only reduce costs, but also to maintain or even expand the quality and quantity of their library services (see Table 6). They have also (as the Palm Springs case study below indicates) sought innovative public-nonprofit partnerships to keep branches open when municipal budgets would otherwise demand cutbacks. By thinking “outside the box” municipalities have been able to maintain services even in the face of constrained budgets.

### **Case Study: Riverside County, California Outsourcing**

Riverside County became the first county in the nation to privatize its library operations. Maryland-based Library Systems and Services Inc. (LSSI) won a \$5.3 million, 1-year renewable contract to run Riverside County’s 25-branch, 85-year-old library system in 1997.

Under the contract, LSSI was charged with increasing library hours by 25 percent and increasing the annual book purchasing budget from \$144,000 to \$180,000. In addition, the company was to retain current employees at their existing salaries. Other specific improvements included adding more Internet terminals at county libraries and a better phone-up library reference service.<sup>114</sup>

LSSI surpassed its contract benchmarks. Library hours increased 34 percent, book purchases nearly doubled, and the company increased staff while maintaining existing salaries.<sup>115</sup> At the Temecula branch, couriers picked up and dropped off books and other materials twice a day instead of three times a week as was done previously.<sup>116</sup> According to Deputy County Executive Officer Tom Desantis, “Cutbacks left the library system in a shambles; many of our libraries were barely open. Now [through contracting], we are able to be open more

hours and we can add staff. The result has been a win-win situation for everyone involved.”<sup>117</sup> This solid performance led the Board of Supervisors to unanimously approve a new \$5 million contract with LSSI that challenged it to increase book purchases an additional 30 percent.<sup>118</sup>

### **Case Study: Germantown, Tennessee Outsourcing**

Germantown, Tennessee (population 41,000), needed to come up with a solution quickly when the county government cut off operating funds for its public library. For years, Shelby County had paid for library services in Germantown and other suburban Memphis cities. During a budget crunch and debate over the FY 2004 budget, however, the county decided to phase out library funding over a five-year period, leaving the city governments to ultimately pick up the entire tab. The cities persuaded the Shelby County Commission to give them a one-year reprieve to prepare for the transition.

One alternative the city considered was to continue library operation under the Memphis Shelby County Public Library and Information Center (MSCPLIC) by contract. An initial cost estimate by the MSCPLIC put the bill at a little over \$1 million a year, but the estimate kept rising until the tab was ultimately pegged at over \$1.5 million. Moreover, not only were cost estimates raised, but the new estimate also resulted in reduced hours of operation and less spending on materials and automation.<sup>119</sup>

In the meantime, Germantown was exploring other options. A proposal by LSSI offered the city more services and expertise while saving \$500,000 off of the MSCPLIC proposal and putting the city—not the county—in control of its library. Elected officials quickly approved a three-year contract with LSSI. The LSSI proposal allowed the city to increase library hours from 60 to 65 per week (including staying open on Sunday for the first time), spend more on the materials of most interest to community residents, increase automation, and improve accountability.<sup>120</sup>

**Table 6**  
**Reasons for Public Library Contracting**

<b>Location</b>	<b>Justification</b>
<b>RIVERSIDE COUNTY, CA</b>	• Structure
	• Lack of control
	• Funding problems
	• Level of service provided
<b>CALABASAS, CA</b>	• Staffing problems (6 months to find someone to run and staff the county library system)
	• Lack of control over management of resources and services
	• Unhappy with service levels for money provided to county (patron complaints)
	• Poor quality of collection
<b>HEMET, CA</b>	• Inability to find a qualified library director
	• Need for special assistance in planning for a move to a much larger facility and in assessing current and future needs
<b>JERSEY CITY, NJ</b>	• Substantial automation needs with no in-house expertise
	• Concerns with overall management and conditions of the library
	• Resistance to change old methods
	• Community's needs were not being served
	• Lack of staff training
<b>LINDEN, NJ</b>	• Communication problems between library staff and Library Board of Trustees
	• Poor management by library director
	• Lack of automation
	• Resistance to change
	• Problems with staff work and attitudes (need training)
<b>FARGO, ND</b>	• Poor facility conditions
	• Lack of fundraising expertise
	• Poor management
	• Difficulty in recruiting library director
	• Alienation of library staff by previous directors
<b>LANCASTER, TX</b>	• Lack of senior leadership for 6 months
	• Diminished quality of service
	• Lack of technology and grant writing expertise
	• Loss of library director
<b>LANCASTER, TX</b>	• Lack of staff and management expertise for newly constructed library
	• Significant decrease in funding

Source: Florida House of Representatives, Committee on Tourism, Report on Privatization of Public Libraries – Pros and Cons, January 2002, [http://www.leg.state.fl.us/publications/2001/house/reports/tourism/lib\\_pdfs/exe\\_sum.pdf](http://www.leg.state.fl.us/publications/2001/house/reports/tourism/lib_pdfs/exe_sum.pdf).

As Mayor Sharon Goldsworthy explained, “Overnight, the city went from just owning a library building to being responsible for its operation. We hit the ground running with the LSSI management team leading the way.”<sup>121</sup>

### **Case Study: Palm Springs, California Volunteers/Transfer to Non-Profit**

In June 1992, the City of Palm Springs, California, closed the Welwood Murray Memorial Library and removed every book from its shelves. A day later, the library started a new life as a private volunteer library, run by a newly incorporated non-profit foundation.

“They left us with nothing,” says library trustee Jeanette Hardenburg, “And the building hadn’t been properly maintained for years. Volunteers did everything you see here—refinished the ceiling, donated display cases.”

Palm Springs’s volunteer library now has 8,000 books in its collection—5,000 more than it had as a publicly funded library—and more arrive every day. “Every book in our collection was given to us by the city—I mean by the people—of Palm Springs. I don’t want to give the city any credit,” Hardenburg says.

The city’s public librarian had earned almost \$70,000 annually to tend the 3,000-book collection; Hardenburg and the other trustees each serve as volunteer librarians one day a week. Community members volunteer to help with the Friday afternoon book sales and other fund-raising and outreach programs.

***City of San Diego Estimated FY 2006-07  
Expenditures on Library Services: \$39,424,734***

***Potential Savings from Managed Competition:  
\$3,942,734 - \$9,856,184 (10 – 25 percent)***

## **8. PERMITS**

Municipalities are discovering that hiring private companies to perform permitting activities—such as building code, electrical, plumbing, and mechanical inspections—can generate cost savings to taxpayers and reduce costs to private builders that might otherwise be passed on to consumers. While routine plan checks and building inspections can be carried out by private-sector providers, local governments still maintain the authority to take disciplinary action against a private provider for violations. As illustrated by the Florida case study below, placing this liability risk on the private sector provides the contractor with a greater incentive to be thorough and accurate in its inspections, as opposed to a government agency which may invoke sovereign immunity if a problem arises.

The City of San Diego already has seen the some of the benefits of streamlining initiatives in the area of building codes and standards. According to the National Conference of States on Building Codes and Standards, the city’s project to expedite the permitting process and develop a computerized permit tracking system has been estimated to have reduced regulatory processing time by 60 percent, saving city government over \$10 million over a four-year period; during that same period, the city’s construction industry reported a minimum of \$3.4 million in direct time labor savings. Likewise, contracting with private firms for inspection services could be expected to generate additional savings and efficiencies.

### **Case Study: Forth Worth, Texas Private Inspectors**

In March 1999, the City of Fort Worth began allowing private sector inspectors to contract with developers for plan review and post-construction inspections. This action was taken in response to the increased workload caused by a 50 percent increase in new construction permits in preceding years. According to the Greater Fort Worth Builders Association, developers were experiencing costly

plan approval delays of up to 45 days during which they incurred additional interest on construction loans. Estimated costs ranged from \$1,200 per day/per unit of residential projects up to \$10,000 a day for commercial projects. <sup>123</sup>

City Development Director Ann Kovich proposed the initiative, noting that private inspectors could serve as a “relief valve” on her staff and dramatically improve the post-construction permitting process.<sup>124</sup> According to one local contractor, the city initiative led to a dramatic reduction in the inspection time required for building plan reviews for residential developments of 80-100 homes. The influx of private inspectors resulted in a reduction in review times from 30-40 days down to just 3-4 days. <sup>125</sup>

### **Case Study: Private Inspectors in Michigan**

There are at least seven private, for-profit firms in Michigan that hold contracts with local governments—including Clinton County and the City of Rockford—to provide private inspectors to enforce code regulations. The City of Battle Creek, Michigan, reportedly saved approximately \$600,000 over the first three years of its contract with a private firm that provides supplemental plumbing, electrical, mechanical, and building inspection services. <sup>126</sup> Several cities also contract with private firms to conduct planning and zoning reviews and issue citations for code violations.

According to a recent analysis by the Mackinac Center for Public Policy, if the City of Detroit were to contract with the private sector for inspection services currently performed by the city’s Building and Safety Engineering Department, it could potentially eliminate a \$4.2 million net tax cost currently borne by city residents and perhaps would reap even greater savings. <sup>127</sup>

### **Case Study: Florida Law Changed to Authorize Private Inspectors**

In 2002, the Florida legislature enacted General Law 2002-299 establishing an alternative permitting process that gives contractors the ability to select private providers instead of municipal employees for plan review and building code inspections. According to CAPRI Engineering, a firm that has provided inspection services in over 60 Florida jurisdictions, the use of private providers is gaining popularity statewide, freeing up municipal resources and improving builders’ ability to obtain permits and inspection services in a timely manner. Miami-Dade County and Broward County are just two of the numerous local governments in Florida that have updated local codes to facilitate private providers under the 2002 law.

According to CAPRI Vice President Roland Holt, a former Palm Beach County Building Official, “In jurisdictions where significant growth is being experienced, local building inspectors and plan examiners have workloads that make thorough inspections and reviews nearly impossible. The private provider system can take a significant load off the municipal building department which will result in an improved process for both the public and private side.” <sup>128</sup>

There are additional benefits to using private providers. As Randall Gilbert writes in *The Florida Bar Journal*, “the biggest reason to use a [private provider] is because [they] must carry professional liability insurance. Because of their personal exposure, [private providers] are more likely to be complete, accurate, and thorough than a [municipal official], who has sovereign immunity from liability.” <sup>129</sup> Gilbert also identifies several other key benefits:

- More thorough inspections, leading to increased workmanship quality and fewer defect and warranty claims.

- More efficient inspections and plan checks. Inspection and plan review delays translate into a loss of productivity and lost profits. Faster project reviews reduce owner inconvenience and offer a fast-tracked, turnkey experience.
- An additional level of quality control.
- Reduced exposure to rain, vandalism, theft, and other hazards affecting idle projects.
- Local governments have the authority to take disciplinary action against a private provider for violations.

### Case Study: Sandy Springs, Georgia Planning, Zoning, and Permitting Services

Immediately after its official incorporation in late 2005, the City of Sandy Springs, Georgia (population 87,000), signed a contract with a private company—CH2M Hill OMI—to provide the bulk of community services for the new city, including planning, zoning, and permitting. In the first year since the company began providing these services, the reduction in the average plan review time has reduced from eight weeks to three weeks as a result of creating separate processes for residential and commercial projects.<sup>130</sup>

**City of San Diego Estimated FY 2006-07 Expenditures on Permits: \$35,086,525**

**Potential Savings from Managed Competition: \$3,508,653 - \$8,771,631 (10 – 25 percent)**

## 9. FACILITIES MANAGEMENT

Cost savings from competitively contracting building maintenance and janitorial services typically range from 32 to 40 percent.<sup>131</sup> San Diego already

contracts for some janitorial and security guard services,<sup>132</sup> so it is less likely to achieve savings quite this high, although our 10 percent to 25 percent potential savings range still seems reasonable. According to a 1999 Calvert Institute study,

*Between the years 1987 and 1995, the percentage of cities contracting out for building maintenance services increased by 10 percent, bringing the total percentage of cities contracting out this service to 42 percent. During this same period, the percentage of cities contracting out janitorial services increased by 17 percent, bringing the total percentage of cities contracting out for this service to 70 percent.*<sup>133</sup>

In the early 1990s, the U.S. Government Accountability Office reported on a large-scale study of maintenance of federal General Services Administration Public Buildings Service buildings and found a 25 percent cost reduction through contracting.<sup>134</sup> Table 7 compares the national average for janitorial and maintenance costs in government and in private buildings.

**Table 7  
National Averages of Janitorial and Maintenance Costs,  
Public vs. Private Sector**

Facility	Janitorial/RSF Low-High	Maintenance/RSF Low-High
National Government (BOMA)	\$1.06-\$1.71	\$1.96-\$4.44
National Private (BOMA)	\$0.81-\$1.35	\$1.96-\$4.16

*Source: Building Owners and Managers Association, 2005 Exchange Report.*

### Case Study: Los Angeles County, California Competitive Contracting

Los Angeles County first contracted maintenance and custodial services in 1980. At first, things did not go smoothly. The initial contracts lacked quality-of-service provisions and contractors were not encouraged to hire displaced county workers.

The county learned from its mistakes, however, and improved its contracting process in the second round of contracts <sup>135</sup>. According to a 1999 Calvert Institute study,

- Contracts typically are now five years in length.
- Both quality and low bid are considered in awarding the contract.
- The county currently has 15-20 custodial contracts, each selected on the basis of overall merit.
- Custodial employees now have several options regarding employment:
  - a) they can choose to be retrained in other fields and then transferred to other areas within county government where they have the potential for increasing their salaries;
  - b) they can choose early retirement; or
  - c) they can go to work for the private-sector provider. <sup>136</sup>

As a result, the county achieved savings of 51 percent from contracting, compared to previous in-house operating costs (see Table 8).

**Table 8**

**Before and After:**

**Impact of Privatization on L.A. County Custodial Costs per Square Foot**

Indicator	Before	After	Savings (\$)	Savings (%)
Custodial Costs, 15 Buildings	\$3.79	\$1.85	\$242,279	51%

*Source: Reason Foundation*

### **Case Study: Hamilton County, Ohio Competitive Contracting**

As of April 2007, Hamilton County has over 36 facilities maintenance contracts covering janitorial services, landscaping, pest control, elevator maintenance, and building automation and

controls. The county contracted all \$2.1 million of the Facilities Department's capital projects and nearly \$5.8 million in maintenance expenditures for 2006. <sup>137</sup> This represents 41 percent of the department's total budget. The County estimates a potential savings of 14 percent relative to the costs of in-house provision of these services. <sup>138</sup>

***City of San Diego Estimated FY 2006-07 Expenditures on Facilities Management: \$15,143,790***

***Potential Savings from Managed Competition: \$1,514,379 - \$3,785,948 (10 – 25 percent)***

## **10. INFORMATION TECHNOLOGY SERVICES**

Although outsourcing an organization's entire computer operations hasn't progressed as far in the public sector as the private sector, there has been a considerable increase in information services privatization activity in state and local governments. In a telephone survey of more than 200 state and local officials, 66 percent of respondents indicated they are outsourcing all or part of their information technology today, and 58 percent believed the trend toward outsourcing will gain momentum over the next few years. <sup>140</sup>

Services such as payroll and financial management, ticket and court records processing, traffic controls and municipal records management are

contracted out. Local governments, such as the counties of Orange and Los Angeles, and the cities of Long Beach and Orange, have contracted with private firms for maintaining and upgrading internal systems. Advantages to this type of service include reduced cost of equipment purchase and maintenance (because the systems are leased from the private company), and the enhancement of software and hardware.

Cost savings from outsourcing information technology systems typically range from 10 to 20 percent.<sup>141</sup>

The Illinois Department of Central Management Services began contracting with IBM in 1987 to handle computer maintenance for all state agencies. By reducing paperwork and administration costs and persuading IBM to give a 10 percent annual discount off maintenance fees, the state has saved over \$12 million since 1987. Other benefits include:

- Access to the latest technology without major capital expenses;
- More time dedicated to core business functions;
- More highly trained expertise (because career paths in government generally are very limited for technology specialists);
- More flexibility; and
- Increased user satisfaction (from other departments of government).<sup>142</sup>

## PROBLEMS WITH THE SAN DIEGO DATA PROCESSING CENTER

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The lessons of IT competition are especially germane to San Diego, given the city's struggles over the years with the San Diego Data Processing Center (DPC). The DPC is a nonprofit company owned by the City of San Diego that manages most of the city's computer and telecommunications technologies. It was established in 1979, when many city governments were just switching from paper to computers, to get around civil service and union restrictions and compete with the private sector for top-quality IT personnel. Though these intentions may have been good, the DPC has been plagued with accusations of lack of accountability and oversight, poor customer service, and excessive prices.<sup>143</sup> A 2004 audit concluded:

- DPC lacks a fundamental customer service orientation.
- DPC is not accountable for project costs or poor results.
- DPC's inventory and billing process is complicated and frequently erroneous.
- DPC's entrepreneurial investments have competed with the private sector, resulted in costly overhead expenses, and produced inefficient return on investment.
- DPC staff is unwilling to share detailed overhead cost information with the city.
- DPC senior managers engaged in spending abuses including spending public money on alcohol, dining-club memberships, holiday and Super Bowl parties, travel for spouses, and lavish executive meetings.<sup>144</sup>

The report prompted the resignation of CEO Roger Talamantez and led then-Mayor Dick Murphy and then-City Manager Lamont Ewell to call for the dissolution of the agency, although they subsequently backed off from this proposal.

It is the lack of true competition or accountability that has doomed the DPC to inefficiency. DPC contracts notoriously lack performance measures and penalties, thus reducing its incentives to perform and making contract enforcement difficult. Moreover, the DPC has been unwilling to use outside vendors to provide services, driving up costs and stifling competition. According to Ian Trowbridge, a retired scientist from the Salk Institute and the University of California at San Diego and a critic of the DPC, "Because the city is fragmented, it doesn't use competition to reduce costs and improve efficiency."<sup>145</sup> Adds former City Manager Ewell, "We have inadvertently created a monopoly."<sup>146</sup>

The good news is that the passage of Proposition C and the implanting ordinance provides San Diego with a great opportunity to dramatically improve the provision of its IT services. In short, the DPC has become obsolete because the reason for its forma-



tion in the first place—getting around restricting civil service and labor rules—is no longer an issue now that city employees and private contractors alike can bid for the city’s IT services under managed competition. Given the age and lack of interoperability of the city’s IT infrastructure, elimination of the DPC and implementation of managed competition is the prescription for addressing San Diego’s IT problems.

### **Case Study: Michigan Court System Competitive Contracting/Outsourcing** <sup>147</sup>

The Michigan Court system has taken advantage of more sophisticated technology in the private sector to cut costs and improve service. The private firm, Quad Tran, has created an integrated case management system of more than 700 terminals throughout the state. The system handles more than 300,000 case abstracts, 85,000 driver’s license suspensions, and 55 percent of all Michigan District Court cases.

Quad Tran’s results have been impressive. By contracting with Quad Tran, the courts saved 25 percent in clerical costs, and uncollected revenues increased by 25-100 percent. Service quality also has improved. The accuracy of Quad Tran transactions is 99.4 percent, much higher than state levels. Moreover, processing a driver’s license suspension takes only 60 seconds compared to four to six weeks for the state system.

### **Case Study: Indianapolis, Indiana Competitive Contracting/Outsourcing** <sup>148</sup>

In one of its more complex transactions, Indianapolis contracted out its city and county information systems in December 1995. After more than a year of study and deliberation, a review committee made up of city-county officials, agencies and Information Services Agency (ISA) staff voted to outsource information services to the private management firm of Systems and Computer Technology Corporation (SCT) for a seven-year

period with options for three, one-year extensions. The city expects to save as much as \$26 million over the seven-year contract period.

SCT provides services that include network management, LAN/Desktop/Server management, disaster recovery and security, help desk management, education and training, management of the ISA data center, and technological consulting for the city and county frameworks. A new position, city-county Chief Information Officer, was instituted to manage the contract and perform the duties of the former ISA director. A core ISA staff is maintained to perform strategic planning services.

Of the four companies in the final bidding process, SCT offered the best bid, committing to operate an on-site, seven-day-a-week, 24-hour-a-day help desk, hire all existing information services employees, and provide salaries equal or better than their current pay. City employees were offered the opportunity to compete in the bidding, but opted to become a part of the review process instead.

### **Case Study: San Diego County, California Competitive Contracting for Capital Improvements**

During the late 1990s, the state of San Diego County’s information technology systems was dismal. The IT infrastructure was outdated and the cost to upgrade it was estimated at \$100 million. As a Government Technology article described the problem, “The county’s 50-odd departments each had their own IT staff, systems didn’t integrate and there was no good communication mechanism.” <sup>149</sup>

To improve IT system interoperability and gain access to the capital required to upgrade the infrastructure, the county decided to outsource its IT functions. In 1999, Computer Sciences Corp. won a landmark seven-year, \$644 million contract that is among the largest municipal outsourcing efforts in U.S. history. <sup>150</sup> The contract resulted in several significant improvements:

- 17 separate help desks were consolidated into one.
- Five e-mail systems were reduced to one.
- 800 or more servers—distributed across 300 sites—were reduced to 520 and are now housed in a single data center.
- More than 900 security vulnerabilities were eliminated.
- 800 business applications have been reduced to 600.
- Reliability is up and outages are down.<sup>151</sup>

The contract was not without its rough spots, however. A lack of county staff experience in dealing with performance-based contracts resulted in ambiguities in the contract and accusations that CSC was not meeting numerous service-level agreements. The problems were eventually resolved without legal action through discussions between the contractor and the county.

In January 2006, the county awarded another seven-year contract, this time valued at \$667 million. Although the county ironed out its differences with CSC and claimed that its early problems with the company did not affect its reconsideration, the new contract was won instead by Northrop Gruman. It contains a five-year extension option valued at \$500 million. While the new contract is expected to generate more cost savings than the old one, cost was less of a concern than improved service quality. According to San Diego County CIO Michael Moore, “Most of my comfort doesn’t come from price. It comes from terms and conditions.”<sup>152</sup>

**City of San Diego Estimated FY 2006-07  
Expenditures on Information Technology:  
\$64,282,700**

**Potential Savings from Managed Competition:  
\$6,428,270 - \$16,070,675 (10 – 25 percent)**

## 11. PRINTING AND COPYING SERVICES

Printing and copying services are a prime example of an “internal service” that does not pass the “Yellow Pages test.” Printing and copying service companies are abundant, so it should not be difficult to find bidders. According to a 1995 privatization survey, printing services are the fifth-most common service outsourced by large city governments, with 35 percent of respondents indicating that they contracted for printing services.<sup>153</sup>

The City of Indianapolis saved 30 percent per year by contracting out its printing and copying services.<sup>154</sup> The federal government opened the printing of the federal budget up to competition and the U.S. Government Printing Office (GPO) immediately cut its prices 23 percent, from \$505,000 to \$387,000.<sup>155</sup> The GPO won the bid. The Bush Administration estimates that expanding competition government-wide could save taxpayers \$50 to \$70 million per year in printing costs.<sup>156</sup>

### Case Study: San Diego, California Printing Services in Need of Reform

San Diego taxpayer advocate and former mayoral candidate Richard Rider illustrates the significant savings possible from contracting out printing and copying services:

*The city says it cost [sic] as much as 15 to 25 cents apiece to make copies. That’s what they charge citizens. Yet by looking in the Yellow Pages, we can find a company such as Staples where we can get copies made for 4 cents a copy – cheaper in bulk or on contract.*

*The county of San Diego was doing internal printing that cost taxpayers 5 cents a page – but now they use an outside printing service for only a penny a page.*

*And consider this – June, 2005, the federal government no [longer] prints the postage stamps!*

*The government is saving tens of millions of dollars annually by using a private printing company to produce all future stamps.*

*The city should do the same.* <sup>157</sup>

Rider knows what he is talking about. In 2004, the city published a pension investigation report and offered to sell copies of the report to the public for 15 cents per page (a discount from its normal copying fee of 25 cents per page!), or \$40.25 for the whole document. According to the San Diego Union-Tribune, “Rider started soliciting quotes from private printers. First he found a National City firm

that would print a spiral-bound copy of the report, downloaded from the city’s Web site, at a 40 percent savings. Then he got a quote from Office Depot of 5 cents a page, or one-third of the city’s charge.” <sup>158</sup>

Said Rider, “The city bureaucrats know how to make the private sector look good.” <sup>159</sup>

***City of San Diego Estimated FY 2006-07 Expenditures on Printing, and Copying Services: \$4,355,101***

***Potential Savings from Managed Competition: \$435,510 - \$1,088,775 (10 – 25 percent)***

# PART IV

## LESSONS LEARNED ABOUT HOW TO SUCCESSFULLY IMPLEMENT MANAGED COMPETITION

The purpose of managed competition is to inject competition into the provision of government services. The emphasis is not on outsourcing itself, but rather on driving innovation, better performance and lower costs for taxpayers. This is achieved through the powers of competition—government agencies and the private sector sharpening their pencils and putting their best operational plan forward, all but guaranteeing improved service and costs. As a matter of fact, the federal government has seen a return of \$31 for every dollar spent on managed competitions in the past few years.<sup>160</sup>

What can San Diego put up for competition? At its most basic level, managed competition involves looking at everything government agencies do and determining whether private firms could do the same things more efficiently. Given the potential savings that competition can produce, broad eligibility is important. The city should limit the number of services and functions it exempts from managed competition. Given the fiscal condition of the city, it is reasonable to conclude that all non-policy making, non-inherently governmental, and non-public safety functions should be eligible for managed competition studies.

A good start would be to apply former Indianapolis Mayor Stephen Goldsmith's aforementioned Yellow Pages test and consider the services identified in the preceding section.<sup>161</sup> In addition to Mayor Goldsmith's vision, we can turn to the federal government for guidance. The Federal Activities Inventory Reform Act and the federal Office of Management and Budget Circular A-76<sup>162</sup> have established policy for determining "inherently governmental" and "commercial activities." In short, "inherently governmental functions" are those that only government can provide; whereas, "commercial activities" are readily available in the marketplace and can be purchased. Note that commercial activities are also found within agencies or departments that perform inherently governmental activities (e.g., police department).

***Inherently governmental** services are those involving a core mission of an agency that cannot be shifted to a private entity. An example would be any activity that involves exercising judicial or police powers, or administrative discretion in the granting of licenses and permits.*

***Commercial activities** are not inherently governmental and are widely available from providers in the private sector. This would include a wide range of non-core, secondary, and administrative support services; operation of public facilities; and the like.*

In order to identify appropriate competition opportunities, city officials should develop a comprehensive inventory of government activities, including the services analyzed in this study. Armed with an inventory—broadly establishing inherently governmental and commercial activities—managed competition initiatives will be easier to identify. Furthermore, enterprise-wide opportunities will also become more apparent as like activities are found across multiple agencies.

But identifying the candidates for managed competition is, in many ways, the easy part. The critical issue for most cities is how to ensure that the effort yields benefits for the taxpayers. As we have seen through the experiences of other governments, done properly, managed competition processes can yield great benefits to taxpayers. Poorly constructed processes, however, can set back efforts to produce more value for the taxpayer.

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## KEYS TO SUCCESS

### 1. Trained Procurement Staff

It is essential that a trained and skilled workforce negotiate and manage contracts and memorandums of understanding (MOU). This is an important constraint upon the city since procurement staff often have limited experience and training in how to conduct managed competition

initiatives. One of the key initial steps for the city is to ensure adequate investments in its contracting unit, so that as it moves into the process staff are aware of how best to build in agreements on the level of service to be offered and the monitoring tools that the city will employ.

## **2. Centralized Managed Competition Unit**

To establish success from managed competition, San Diego should develop a core group of procurement officials whose primary function is to assist other departments in developing their procurement and competition documents. This team would build up a critical mass of knowledge and expertise, making certain that lessons learned and best practices were applied across all city departments and in every managed competition initiative.

This team would effectively “own” managed competition initiatives in the city, creating a coordinated process guiding managed competition initiatives. Further, it would be a central point of accountability and responsibility. Private companies, public employees, and citizens would have one place to turn for information about existing and future competition initiatives.

In addition, a centralized unit can open up more reform opportunities. Government agencies largely operate in silos, not interacting with one another, and are not usually capable of influencing policy in other agencies. Without a centralized process or “owner” the city would likely be limited in the types of available solutions. Individual agencies would lack the incentive and the ability to engage in enterprise-wide solutions. Thus, city-wide or enterprise-wide reforms are less likely to be considered or implemented. A centralized unit, however, is best equipped to identify, evaluate, consider and manage comprehensive efforts.

Furthermore, a centralized unit will prevent individual agencies from adopting different standards and processes to carry out managed competitions.

Doing so can lead to confusion among agencies, stakeholders, and competitors.

## **3. Establishing Performance Measures**

One of the most crucial elements is to establish a set of acceptable performance metrics and to measure and monitor the success of a contract post-implementation. Without clear performance goals, it is difficult to communicate and conduct comparisons to identify the bid that provides the best value. It is also difficult to ensure that either the contractor or the municipal department is meeting expectations.

## **4. Reliable Cost Comparisons**

In order to properly evaluate delivery options the city will have to establish formal guidelines for cost comparison. In-house proposals need to “fully allocate” all expenses associated with providing services. This includes all direct full-time and part-time personnel costs, materials, supplies, equipment purchases, capital and equipment depreciation costs, rent, maintenance and repairs, utilities, insurance, travel, operations overhead, and general and administrative overhead.<sup>163</sup> These features, in turn, all go into determining the “unit cost” of providing a service, such as the cost per hour of operating a transit bus, or the cost per beneficiary of administering a health insurance program.

## **5. Implement Performance-Based Contracts**

San Diego should implement performance-based contracts for as many contracts and services as possible. Performance-based contracting is the soliciting of bids based on what results government wants accomplished, rather than what activities it wants conducted. In other words, the emphasis is on outcomes rather than inputs. This requires performance standards to be included in the contract and contractual payments tied to the achievement of results.

The better the performance standards for a given service or activity, the easier it will be to monitor the contract effectively (the next key to success). It is often best to write the performance standards and the monitoring plan simultaneously. Indeed, the federal OMB recommends simultaneous development of performance measures and monitoring plans as a best-practice. <sup>164</sup>

## 6. Monitoring and Evaluation

With managed competition comes greater need to monitor performance. Again, a central specialized unit is best equipped to manage and monitor city wide efforts. As managed competition is rolled out, monitoring and assessing internal MOUs and outside partnerships become vital to achieving the government's goals. While monitoring and measurement systems are becoming more refined, San Diego will need to continuously improve purchasing and oversight of service delivery. Effective monitoring pays for itself by improving the quality, transparency, and accountability of services. <sup>165</sup>

For some contracts, recording satisfactory completion within the time and cost constraints will

satisfy the monitoring requirement. Larger multi-year contracts with complex specifications and performance criteria will demand more extensive monitoring procedures.

Monitoring requirements should include some form of contractor-prepared statements of progress, which provide information on work completed, and information relative to performance standards. These statements of progress should identify problems encountered and any contractual adjustments deemed necessary. The size and complexity of the contract will determine the frequency of reporting but the reports should be verified (audited) for accuracy.

Monitoring plans should focus on quantifiable measures as much as possible, including reporting requirements, regular meetings, complaint procedures, and access to contractor's records (if necessary). As much as possible, plans should focus on monitoring and evaluating the major outputs of the contract and not waste time and resources monitoring routine tasks that are not central to the taxpayer's value.

**Table 9**

**City of San Diego Business Process Reengineering Reviews and Status**

Approved by Council	Included in Proposed Budget	In Progress	Future BPRs
Contracts Human Resource Information Technology Environmental Services	Fleet Services Streets Division Publishing Services Police - Phase I Engineering Metropolitan Wastewater	Development Services Reservoir Program Water Fire-Rescue Police - Phase II Grants and Gifts Facilities Maintenance Park Maintenance Libraries Storm Water	Real Estate Assets Public Information Ethics and Integrity Dispatch Centers Emergency Operations Center Redevelopment Community & Economic Development Planning - Facilities Financing IT&C - Communications General Services - Station 38, Admin Risk Management Finance Park and Recreation

Source: City of San Diego, Office of the Independent Budget Analyst, Review of Mayor's Proposed Fiscal Year 2008 Budget, IBA Report Number 07-46, April 27, 2007, p. 32, [http://www.sandiego.gov/iba/pdf/07\\_46.pdf](http://www.sandiego.gov/iba/pdf/07_46.pdf).

## HOW SAN DIEGO IS TACKLING MANAGED COMPETITION

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The City of San Diego has taken some of the initial steps needed to implement its managed competition process. The first step the city decided to take in the evaluation process is the conducting of a Business Process Reengineering (BPR) study for each city department and function. Once formed, the BPR project team analyzes the targeted city service or department, “maps processes, determines improved methods for completing those processes, benchmarks their methods and performance against other jurisdictions and service providers, and crafts recommendations for improvement.”<sup>166</sup>

The process of conducting a BPR and managed competition are intertwined in a couple of ways. First, since managed competition is one of the process strategies considered in the BPR review, this gives management an opportunity to take an

initial examination of whether soliciting outside bids could be warranted and improve efficiencies. In addition, the development of a BPR can allow city departments to adopt what they think is their “most efficient organization” (MEO), which they may use in submitting a bid to management if managed competition is selected for their service(s). Table 9 describes the status of BPR reviews for various city departments and activities.

There are also steps that, as of the publication of this report, have yet to be completed. The City of San Diego’s managed competition program is to have its own Independent Review Board. According to the implementing ordinance, the board is to act as a “check” on management to ensure that the process of soliciting bids and the selection of the winning bidder is fair, transparent, and done in the public interest. As of this writing, the city has yet to establish the board, but it is expected to do so before the end of calendar year 2007.



## SAN DIEGO'S MANAGED COMPETITION PROCESS

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The following are the steps required before moving forward with managed competition of a function in the City of San Diego under Chapter 2, Article 2, Division 37, of the San Diego Municipal Code (see Appendix 2).

1. Appoint and get City Council confirmation of the Managed Competition Independent Review Board (MCIRB) (section 22.3702.a; 22.3706 through 22.3711).
  - a. The adoption by the City Council of a “conflict of interest” code for the MCIRB (section 22.3706b).
2. City Manager carries out a pre-competition assessment and, if he chooses, transmits to the MCIRB a “statement of work” taking into account provisions laid out in 22.3702.b.
3. Bids are solicited. There is no minimum period in the statute.<sup>1</sup>
4. MCIRB then receives and evaluates the bid. If it finds that the contractor meets the minimum contract standards and provides the best overall value to the City, the MCIRB shall recommend to the City Manager that the contract be awarded to that independent contractor. The MCIRB's recommendation shall include a written explanation providing the rationale for its recommendation (22.3713.b).
5. The City Manager can accept or reject that recommendation in its entirety.
6. If accepting it, the City Manager must notify all labor organizations whose members would be affected by the potential agreement, as well as the City Personnel and Labor Relations departments. Manager must provide the number of City positions by job classification that may be displaced if the contract is awarded to the independent contractor (22.3715.a).
7. If the City Manager accepts it, then he shall forward that recommendation to the City Council. In that transmittal should be the MCIRB's recommendation, the proposed agreement with the contractor, and a transition strategy describing contract monitoring, how to avoid service interruptions, and procedures for any affected public employees. (22.3714).
8. The City Council then has to docket the item.
9. The City Council, at the scheduled meeting, then can accept or reject the recommendation. If it accepts the recommendation, it must make certain determinations.
10. If an independent contractor wins the bid, the contract will be audited every year.

<sup>1</sup> Other state and local laws may dictate a minimum period during which the bid may be open. It is unlikely, albeit conceivable, that some options might qualify as a “project” and could trigger CEQA requirements at some point(s) during the process.

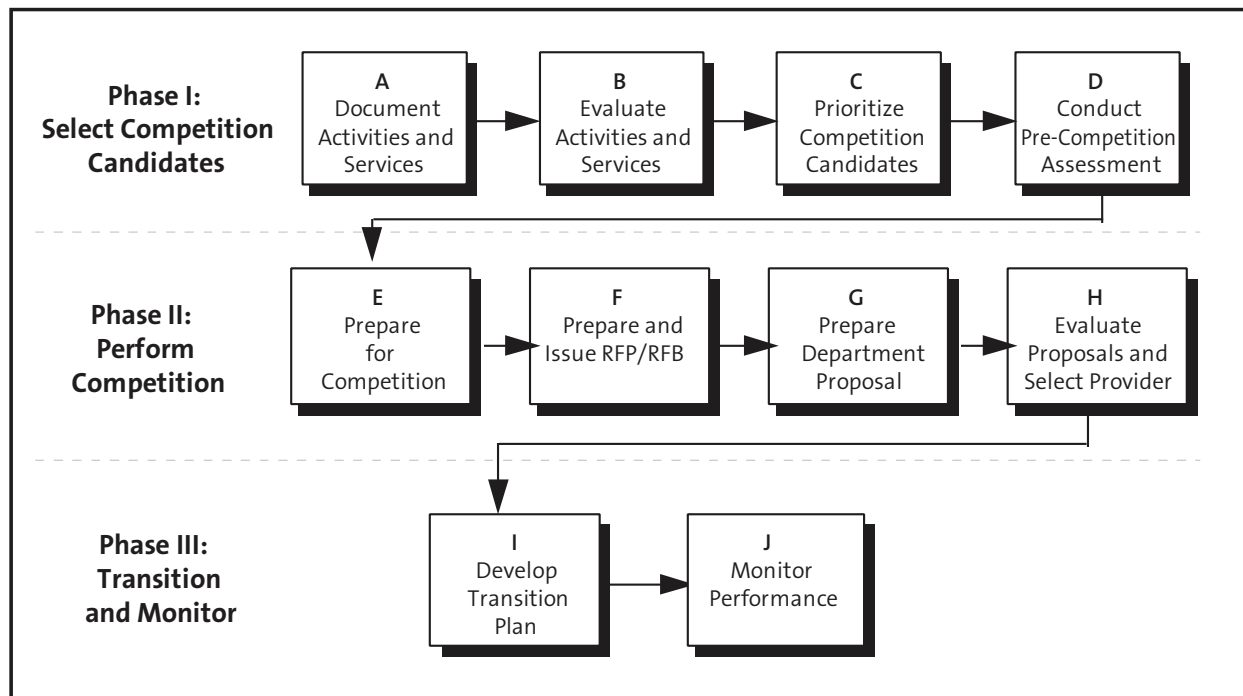
## MANAGED COMPETITION IN SAN DIEGO COUNTY AND LESSONS LEARNED

As noted above, the use of outcome measures, performance-based contracting, and vigilant review and monitoring are keys to the success of any managed competition effort. For further guidance in this respect, and in implementing the competition program in general, the city does not have to look far. The County of San Diego has been running an effective managed competition program since the 1990s. The County Board of Supervisors adopted policies during the 1980s that:

(1) allowed the county to contract with private-sector providers for services if it was determined that the service could be provided more economically and efficiently by the independent contractor and (2) established a competition process. But it was not until the late 1990s that the managed competition program really took off. In 1998, the county published a detailed Managed Competition Guide that describes the competition process and the roles and responsibilities of the Competition & Reengineering Group, competition manager, department work team, department head, Board of Supervisors, consultants, county legal counsel, labor organizations, and other interested parties at each step in the process (see Figure 1).<sup>167</sup>

**Figure 1**

### Overview of the Managed Competition Process in San Diego County



Source: County of San Diego, Competition & Reengineering Group, County of San Diego Managed Competition Guide, August 31, 1998, p. 6, <http://www.co.san-diego.ca.us/cnty/cntydepts/CAR/services/MCG.pdf>.

# PART V

## EFFECTS OF MANAGED COMPETITION ON PUBLIC EMPLOYEES

Despite the resounding success of managed competition across the country, some political interests persist in opposing its adoption, claiming that it hurts public employees. This has generated intense opposition to competition from public employee unions at all levels of government. But well-managed competition initiatives need not put undue burden on public employees.

Comprehensive examinations of competition initiatives have found that competition has resulted in few, if any, layoffs and that public employees can actually benefit in the long term from private-sector management. The literature on employment impacts consistently finds that private contracting mostly shifts, rather than displaces, employees:

- A 1995 study of privatization in Illinois municipalities found that only 3 percent of the 516 responding cities reported layoffs due to contracting. Nearly two-thirds (64.9 percent) of the cities reported no displacement of affected employees, while 10.8 percent transferred workers to other government jobs, 5.4 percent reported that employees were hired by the private contractors, 5.1 percent said the affected employees retired, and 9.8 percent reported a combination of these results.<sup>168</sup> In late 1999, a follow-up survey of 220 Illinois cities of more than 5,000 in population found roughly the same percentage (only 3.8 percent) of cities reporting that employees were laid off as a result of privatization.<sup>169</sup>
- Researchers examining privatization by cities in Wisconsin in 2000 also asked what happened to employees after privatization. The most common response was transfers to other government jobs (42 percent of municipalities), followed by retirement and taking jobs with the private contractor. Only in 6 percent of cases were workers laid off. Roughly two-thirds of municipalities did not keep data on what happened to employee wages and benefits. Of the municipalities that could report on changes in wages and benefits, approximately one-third

reported that private firms paid wages that were higher than the municipality paid, one-third paid similar wages, and the remaining one-third paid employees lower wages than the municipality had paid.<sup>170</sup>

- A 2000 study examining the effect of welfare-to-work privatization on state employees in Arizona found that none of the 160 employees involved were laid off; the contractor hired most of them, while the rest transferred within the state Department of Economic Security (DES). The contractor raised salaries for former DES employees by on average 31.5 percent, and over one-third of former DES employees received at least one promotion in the first year after privatization. One year after privatization, most former DES employees who responded to a survey were satisfied with post-privatization benefits packages—38 percent rated the benefits better than the state's, 41 percent rated benefits the same, and 21 percent rated the contractor's benefits worse. They were evenly split on whether they felt more or less job security with the private contractor. Finally, only 43 percent of former DES employees were "highly satisfied" while working for the state, but 91 percent reported being "highly satisfied" one year after privatization.<sup>171</sup>

Layoffs are a very real concern to public employees when the issue of managed competition is raised. However, there is little evidence to suggest that it results in massive layoffs and hardship for public employees. A 2001 GAO examination of federal competitive sourcing reached similar conclusions:

*... about half of the civilian government employees remained in federal service following the studies, either in the new or another government organization with similar pay and benefits. Most of the remaining employees received a cash incentive of up to \$25,000 to retire or separate. There were a relatively small number of involuntary separations. Further,*

*employees that left government service and applied for positions with the contractors who won the competitions were hired. Pay and benefit minimums offered by contractors are set by law for various geographical areas, which resulted in some employees making less than what they did as government employees and others making more. In many instances, former government employees who accepted employment with the contractors received a cash incentive to leave government service and federal retirement benefits. Contractor benefit packages also differed, but the types of benefits, such as health insurance, vacation time, and savings plans, appeared to be similar to what the government offers.*<sup>172</sup>

It is important to recognize that managed competition may run counter to the interests of public employee union leaders. Fewer members means a decrease in dues which, in turn, can mean a decrease in political influence. Unfortunately, oftentimes this concern has led labor leadership to rally rank and file resistance against managed

competition efforts. Such actions can have serious consequences on the organization, as the process becomes one that is seen as pitting management against rank-and-file, rather than as a tool that can lead to win-win situations and a better relationship between government and taxpayers.

Thus, a critical concern for the city is to effectively communicate early and often in the process with public employees, and to manage employee transitions as part of the managed competition process. There are well-understood procedures for coping with the challenges of employee transitions—best practices and hard lessons learned that should be embraced.<sup>173</sup> A good example is being set by the U.S. Department of the Interior (DOI), which has held competitions between private companies and its own workers to provide the tasks performed by more than 1,800 DOI employees, and through good planning has moved personnel displaced by competition into jobs with contracting firms, other empty positions at DOI, or found them work in other sectors.

PART VI  
CONCLUSION

Over the past decade, more and more government officials have been inviting private firms to compete for contracts to provide services once restricted to public sources. This trend is not confined to any particular region, or to governments dominated by either major political party. The reason for the widespread appeal of competitive sourcing is simple: it works. Given the city's current fiscal crunch, managed competition is an important tool in the toolbox. All public sector entities, including San Diego, must continually seek ways to improve services and increase accountability to their taxpayers.

The keys to success, in many ways, are the rules themselves. A successful process will ensure transparency, accountability, and the delivery of high-performance services. By utilizing best practices and lessons learned from experiences of other governments the likelihood of achieving those results is greatly enhanced. Experience has shown that the following recommendations are vital to a successful managed competition:

1. Seek stakeholder input and establish clear, standard lines of communication with the public to ensure transparency. Agencies should work extensively with stakeholders to explain motivations and goals and how changes will affect them.
2. Establish a core group of procurement officials to assist in procurement planning and decisions.
3. Develop performance metrics and goals; establish them into contracts and other oversight plans. Build these into the contract and tie achieving milestones to payment.
4. Develop strong oversight, monitoring and assessment protocols before entering into a contract to guarantee compliance and performance. Monitoring should focus on

quantifiable measures as much as possible, and the focus should be on achieving results, not on process. Simply put, effective monitoring pays for itself by improving the quality, transparency, and accountability of services.

5. Develop a centralized unit designed to manage initiatives, establish best practices, utilize lessons learned, and present a standard performance-based process. This unit should identify enterprise-wide challenges and possible solutions.
6. Focus on changing antiquated business processes. Competition fosters a new way of thinking and doing business. Don't simply try to do something for less; try to do something better. Contracts should be outcome- and results-orientated, not process driven.
7. Conduct an annual or biannual inventory of all functions and activities performed by government, distinguishing between inherently governmental and commercial activities to create a transparent, searchable inventory of government activities that can be used for a range of management purposes from budgeting, to human resources planning, to identifying competitive sourcing opportunities.

Undoubtedly, San Diego has some of the best public employees in the country. Competition is nothing more than a challenge to excel. Taking this challenge head on will make San Diego a better place to live and do business. The city can become one of the most efficient and effective in the country. Competition will help us get there. When government competes, the taxpayer wins every time.

**Table 10****Summary of Potential Cost Savings from Managed Competition**

<b>Service</b>	<b>FY 2007 Expenditures</b>	<b>Proposed FY 2008 Spending</b>	<b>Low Savings Estimate (07)</b>	<b>High Savings Estimate (07)</b>
Water/Wastewater <sup>1</sup>	\$350,165,778	\$478,984,727	\$35,016,327	\$87,540,818
Environmental Services:				
Trash Collection	\$39,323,442	\$38,514,160	\$3,932,344	\$9,830,861
Landfill	\$25,805,497	\$26,296,990	\$2,580,550	\$6,451,374
Recycling	\$19,600,811	\$19,928,390	\$1,960,081	\$4,900,203
Fleet Maintenance <sup>2</sup>	\$51,018,5941	\$49,635,6931	\$5,101,859	\$12,754,649
Street Maintenance	\$50,681,086	\$68,951,347	\$5,068,109	\$12,670,272
Parks and Recreation	\$95,495,273	\$98,532,648	\$9,549,527	\$23,873,818
Golf Courses	\$11,690,024	\$12,913,763	\$1,169,002	\$2,922,506
Libraries	\$39,424,734	\$38,345,950	\$3,942,734	\$9,856,184
Permits	\$35,086,525	\$31,480,113	\$3,508,653	\$8,771,631
Facilities	\$15,143,790	\$14,886,850	\$1,514,379	\$3,785,948
IT/Data Processing <sup>3</sup>	\$64,282,700	\$86,085,614	\$6,428,270	\$16,070,675
Printing/Copying	\$4,355,101	\$4,196,455	\$435,510	\$1,088,775
<b>TOTALS</b>	<b>\$802,077,855</b>	<b>\$968,752,700</b>	<b>\$80,207,345</b>	<b>\$200,517,714</b>

Source: Expenditures data are from City of San Diego, FY 2007 and FY 2008 (Proposed) budgets.

1. The cost savings projections for water and wastewater **do not** factor in expenditures for water purchases, bond payments, and the bond assurance fund. Note also that expenditures for “municipal wastewater–non activity account” which is a budget line item in the FY 08 budget but not included in FY 07, are excluded for the table. The savings projections also focus only on the municipal budget of the wastewater department, thus excluding metro expenditures (see pages 501-507 and 535-537 of the City of San Diego’s FY 2008 Proposed Budget). Though we have taken a conservative approach in excluding these items for the purpose of determining potential cost savings estimates, it could be argued that because of improved incentives and competition, operators under managed competition would do more to attempt to reduce water losses, including conducting regular audits and taking a more proactive approach, which could result in additional savings. For information on the \$21.8 million the City of San Diego spent in FY 07 on water purchased which was lost before it could be delivered to customers see Rob Davis, “The Case of San Diego’s Vanishing Water,” Voice of San Diego, July 26, 2007, <http://voiceofsandiego.com/articles/2007/08/07/environment/932waterloss072607.txt>.

2. These expenditure figures do not include approximately \$13 million for FY 2007 and \$31.6 million for FY 2008 (Proposed) for the General Services Department’s Equipment Replacement Fund. The city may wish to consider a leasing arrangement under a contract with a private provider instead of owning vehicles. This could result in additional savings from capital costs.

3. Expenditure data for information technology/data processing only includes expenditures from the Office of the CIO (the city’s central IT office) and the San Diego Data Processing Center. It does not include separate information technology divisions established within several city departments. As such, expenditures and cost savings estimates are undercounted.



# PART VII

## APPENDIX 1: DERIVATION OF COST SAVINGS ESTIMATES

In this study we have estimated that the City of San Diego could save between 10 and 25 percent of its current year expenditures for the identified services. We based this estimate from a large body of case studies, including those cited throughout the paper. This potential savings range is intended to be somewhat conservative, and is supported by more than thirty years of academic and government research. We have also based our estimate on practical experience as consultants to a number of government entities that have examined and implemented managed competition processes. Given that each initiative is different and that actual savings depends on many factors including size, scope, condition of existing facilities, and economic conditions, a range of savings is given with both an upper and lower boundary.

The most important studies examining the range of cost savings that government can expect to realize through well-constructed managed competition efforts include:

- In 1993, Reason Foundation examined 100 studies of cost savings from privatization efforts. That meta-analysis found that **cost savings ran between 20 and 50 percent**. [John Hilke, *Cost Savings from Privatization: A Compilation of Study Findings*, Reason Foundation How-to Guide No.6, (Los Angeles: Reason Foundation, 1993), <http://www.reason.org/htg06.pdf>.]
- The Center for Naval Analysis (CNA) in 1996 studied 2,138 competitions undertaken by the Department of Defense between 1978 and 1994. The average cost savings was projected to **be 31 percent**. In 2001, CNA reported on 16 competitions for which the average projected savings was 35 percent. Subsequent analysis showed that savings were closer to **24 percent**. **CNA attributed the difference to changes in contract scope and quantity**. (“Long-run Costs and Performance Effects of Competitive Sourcing,” Washington, D.C., 2001, <http://www.cna.org/research/studies/comsourc.html>.)
- A 1999 study by the Department of Defense’s General Accounting Office looked at 53 completed competitions and projected that taxpayers would save a **total of \$528 million, or 42 percent**. Importantly, savings of this magnitude were realized whether the competition was won by the private sector or by in-house bidders. (General Accounting Office, *DOD Competitive Sourcing: Results of Recent Competitions*, Washington, D.C.: GAO/NSIAD-99-44, February 1999.)
- In 2003, OMB did a major study of competitive sourcing. It found that DOD, with the most extensive program for public-private competition had **realized savings of 33 percent** in the roughly 3,000 competitions held since 1979. OMB also examined reports by the Rand Corporation (which **found savings rates of 41 percent to 59 percent**), the IBM Endowment for The Business of Government, and the GAO. (Executive Office of the President, Office of Management and Budget, “Competitive Sourcing: Conducting Public-Private Competition in a Reasoned and Responsible Manner,” Washington, D.C., July 2003, [http://www.whitehouse.gov/omb/procurement/comp\\_sourcing\\_072403.pdf](http://www.whitehouse.gov/omb/procurement/comp_sourcing_072403.pdf).)
- In May 2007, the Office of Management and Budget showed that federal taxpayers were getting back **\$31 in savings for every \$1 invested in carrying out the competition**. The average net savings per full-time equivalent (FTE) position undergoing the competition was \$25,000, approximately a 28 percent return. (Executive Office of the President, Office of Management and Budget, “Report on Competitive Sourcing Results, FY 2006,” Washington, D.C., May 2, 2007, [http://www.whitehouse.gov/omb/procurement/comp\\_src/cs\\_report\\_fy2006.pdf](http://www.whitehouse.gov/omb/procurement/comp_src/cs_report_fy2006.pdf).)

# PART VIII

## APPENDIX 2: PROPOSITION C IMPLEMENTING ORDINANCE

**Article 2: Administrative Code**

**Division 37: Managed Competition**

*(“Managed Competition” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3701 Purpose**

- (a) The City of San Diego is committed to delivering quality services to taxpayers, residents and visitors in the most economical and efficient ways possible. Under Charter section 117(c), Managed Competition is the process for determining whether City services can be provided more economically and efficiently by an independent contractor than by persons employed in the Classified Service, while maintaining service quality and protecting the public interest. Nothing in this Division shall limit or restrict the City from contracting services under any other provision of law.
- (b) This Division is intended to set forth policies and procedures to implement Charter section 117, subsection (c). The City Manager may also provide for additional policies, procedures and/or regulations consistent with this Division and Charter section 117(c).

*(“Purpose” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3702 Pre-Competition Assessment**

- (a) If the City Manager determines as part of a pre-competition assessment that a City service may be provided more economically and efficiently by an independent contractor than by persons employed in the Classified Service, while maintaining service quality and protecting the public interest, the City Manager may select appropriate services for Managed Competition. If the City Manager intends to submit a City service to Managed Competition, the City Manager will then prepare a preliminary written Statement of Work for that particular City service, and will prepare a report setting forth the rationale for putting a City service into Managed Competition. This report will be transmitted to the Managed Competition Independent Review Board for its consideration.
- (b) In determining whether a City service is appropriate for Managed Competition, the City Manager will consider such factors as the type of service provided, the abilities of the current and projected competitive market, potential efficiencies that could be achieved, the capacity of the City to deliver essential services in the event of contractor default, and the overall welfare of the public. The City Manager will not recommend for Managed Competition, inherently governmental services, or those services so intimately related to the exercise of the public interest as to mandate their performance

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by City employees. Police Officers, Fire Fighters and Lifeguards who participate in the Safety Retirement System will not be subject to Managed Competition.

- (c) A request for qualifications process may be used prior to the solicitation for services in appropriate cases.
- (d) Nothing in this Division shall confer any right to any potential or current independent contractor to bid on a City service for which a solicitation has not been issued.

*("Pre-Competition Assessment" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3703 Minimum Contract Standards and Contractor Qualifications**

- (a) The City Manager shall require that any independent contractor providing services to the City meet minimum contract standards to be contained in the solicitation for services. The minimum contract standards shall include the following:
  - (1) that the independent contractor provide proof that it maintains an adequate level of liability insurance consistent with City of San Diego risk management requirements;
  - (2) that the independent contractor has a policy of equal employment opportunity;
  - (3) that the independent contractor has committed to complying with the City of San Diego Living Wage Ordinance, San Diego Municipal Code Chapter 2, Article 2, Division 42, sections 22.4201 through 22.4245, if required by the terms of that ordinance;
  - (4) that the independent contractor has appropriate safety policies and procedures in place to protect the public and its employees in providing the service;
  - (5) that the independent contractor will comply with all applicable employment and labor laws;
  - (6) performance standards and consequences for non-performance, up to and including termination of the contract;
  - (7) that the independent contractor designate appropriate personnel to monitor contract compliance;

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- (8) that the independent contractor's employees must maintain the same certifications as will be required of City employees performing the same service;
  - (9) that if background checks will be required of City employees performing a particular service, the independent contractor will perform background checks on employees performing those same services;
  - (10) the same regulations and requirements of service delivery necessary to maintain service quality that will apply to a City department shall also apply to any independent contractor;
  - (11) that the City shall unilaterally and immediately terminate the contract if the independent contractor enters into a contract with or employs a member of the Independent Review Board during the term of the contract with the City; and
  - (12) that the City shall unilaterally and immediately terminate the contract if the independent contractor enters into a contract with or employs a former member of the Independent Review Board during the term of the contract with the City, if that former Board member participated in the selection process for that contract.
- (b) In addition, in appropriate cases, as determined in the discretion of the City Manager, the City may require:
- (1) that the independent contractor has provided this service satisfactorily for other comparably-sized cities, counties, districts, agencies or private entities for a sufficient time period, and thereby has demonstrated its ability and expertise to provide the service;
  - (2) that the independent contractor maintain a customer service and customer complaint resolution plan;
  - (3) that the independent contractor have adequate financial resources in order to provide the requested services; and
  - (4) that the independent contractor's employees have the necessary technical qualifications to provide the services.

*("Minimum Contract Standards and Contractor Qualifications" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3704 Resources for City Employees Involved in Managed Competition**

City employees involved in Managed Competition will be provided with resources, such as information, technical assistance and staff support, to develop strategies for optimized efficiency, economy and effectiveness, in order to respond to a solicitation. In addition, in the City Manager's sole discretion, the City Manager may grant a department reasonable time and resources to improve its operations before being subject to Managed Competition.

*("Resources for City Employees Involved in Managed Competition" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3705 City Bid for Non-City Services**

In areas where City workers are consistently productive and cost efficient, a City department can propose to the City Manager that City workers provide a service to other entities, provided that this would be of benefit to the City and its taxpayers, and when such work can increase the City's overall efficiency and effectiveness, while maintaining service quality and protecting the public interest.

*("City Bid for Non-City Services" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3706 Managed Competition Independent Review Board Established**

A Managed Competition Independent Review Board is established pursuant to San Diego Charter section 117(c) to advise whether the proposal of City employees or that of an independent contractor will provide the services to the City more economically and efficiently while maintaining service quality and protecting the public interest.

*("Managed Competition Independent Review Board Established" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3707 Appointment of Members of the Independent Review Board**

The Board shall consist of

- (a) Seven (7) members appointed by the City Manager;
- (b) Three (3) Board members shall be City staff, including a City Manager staff designee, a City Council staff designee and the City Auditor and Comptroller or staff designee; and
- (c) Four (4) Board members shall be private citizens whose appointment shall be subject to City Council confirmation, and who shall serve without compensation.

*("Appointment of Members of the Independent Review Board" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

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**§ 22.3708 Terms of Members of the Independent Review Board**

To promote continuity and organizational knowledge, the terms of the initial appointees to the Independent Review Board shall be staggered as follows: Two private citizens shall serve an initial three year term, and the other two private citizens shall serve two year terms. All subsequent terms by private citizens shall be two years. A member who has served two complete terms shall be ineligible for reappointment for two years after leaving the Board. The three City staff Board members shall not be subject to the above term limits.

*(“Terms of Members of the Independent Review Board” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3709 Qualifications of Independent Review Board Members**

Each member of the Board shall comply with the following qualifications during his or her tenure on the Board:

- (a) No member of the Board shall make a financial contribution to, or publicly support or oppose, a candidate for or incumbent in City office;
- (b) No member of the Board is permitted to act as a lobbyist required to register with the City pursuant to Chapter 2, Article 7, Division 40 of this Code;
- (c) Board members shall not have any personal or financial interests that would create conflict of interests with the duties of a Board member;
- (d) Members of the Board shall be prohibited from entering into a contract with or accepting employment from an independent contractor that secures a City contract through Managed Competition for the duration of the contract. All City contracts secured through Managed Competition shall include a condition that the City shall unilaterally and immediately terminate the contract if the independent contractor enters into a contract with or employs a member of the Board during the term of the contract with the City; and
- (e) Former members of the Board shall not enter into a contract with or accept employment with an independent contractor that secures a City contract through Managed Competition for the duration of that contract after leaving the Board, if that Board member participated in the selection process for that contract. All City contracts secured through Managed Competition shall include a condition that the City shall unilaterally and immediately terminate the contract if the independent contractor enters into a contract with or employs a former member of the Board during the term of the contract with



the City, if that former Board member participated in the selection process for that contract.

*(“Qualifications of Independent Review Board Members” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3710 Removal of Member of the Independent Review Board**

A Board member subject to City Council confirmation may be removed for cause by a vote of the majority of the members of the Council. Before the Council may remove a member of the Board, written charges shall be made against the Board member and an opportunity afforded for public hearing before the Council acts upon such charges. While charges are pending before the Council, the Council may suspend a Board member’s participation on the Board.

*(“Removal of Member of the Independent Review Board” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3711 Confidentiality and Conflict of Interest**

(a) The potential for abuse from knowingly or unknowingly causing or gaining unfair advantage from access to information, or the ability to affect the selection process for personal gain must be understood and avoided by all levels of personnel involved. The City will assist departments to understand, train personnel, and implement safeguards and procedures to avoid the potential for ethical conflicts and abuses. No elected official or City employee shall provide procurement sensitive information to any potential contractor.

(b) A conflict of interest code shall be adopted by the City Council for all members of the Managed Competition Independent Review Board. All members of the Managed Competition Independent Review Board shall be required to complete and file statements of economic interests in accordance with the conflict of interest code.

(c) In the event a service is awarded to an independent contractor through Managed Competition, impacted employees in the Classified Service will not be precluded or hindered from accepting employment with the independent contractor.

*(“Confidentiality and Conflict of Interest” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3712 Solicitation of Proposals and Support for the Independent Review Board**

(a) When it is determined, as a result of the pre-competition assessment, that a Managed Competition process would benefit the City, appropriate acquisition

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actions, such as development and advertising of the solicitation of proposals for the service, will be prepared by City staff.

- (b) City staff will provide support to the Independent Review Board in its consideration of proposals.  
*(“Solicitation of Proposals and Support for the Independent Review Board” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3713 Consideration of Proposals by Independent Review Board**

- (a) In determining whether a proposal of an independent contractor or City Department will provide a service to the City most economically and efficiently while maintaining service quality and protecting the public interest, the Independent Review Board will consider the following factors:
- (1) the Independent Review Board should not recommend awarding a contract to an independent contractor unless there have been at least two bids by independent contractors for the service subject to Managed Competition;
  - (2) whether the bids by the City Department and the independent contractors are responsive to the solicitation and responsible;
  - (3) whether there is reliable information demonstrating that any of the independent contractors bidding on the work have engaged in unethical business practices that would warrant the rejection of their bid;
  - (4) unless the bid of an independent contractor is more than ten (10) percent lower than the bid of a City Department currently providing the service for the proposed term of the contract, the Independent Review Board should not recommend awarding the service in question to the independent contractor. This minimum cost differential is meant to discourage the City from implementing a significant change in service delivery on the basis of marginal estimated savings, and to account for such difficult to estimate factors as the potential costs of reduced productivity and service disruption during transition. In reviewing this factor, the Board will utilize a cost analysis, the purpose of which is to calculate the costs that are saved and the costs that are generated by contracting the service; and
  - (5) which independent contractor or City Department can provide the best overall value to the City. The Independent Review Board will not necessarily recommend the low bidder, as the low bidder may not be

the party that is presenting the most responsible and responsive bid, i.e., the low bidder may not always be the party that can provide the best and most reliable service to the City, perhaps because the low bidder has less experience or lacks the proven track record of a City Department or an independent contractor with a higher bid.

- (b) If the Board determines that an independent contractor meets the minimum contract standards and provides the best overall value to the City according to the factors set forth above, the Independent Review Board shall recommend to the City Manager that the contract be awarded to that independent contractor. The Independent Review Board's recommendation to the City Manager shall include a written explanation providing the rationale for its recommendation.  
*("Consideration of Proposals by Independent Review Board" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3714 City Manager and City Council Consideration of Decision of Independent Review Board**

Upon receipt of a recommendation from the Independent Review Board that a City service should be awarded to an independent contractor, the City Manager shall either accept or reject that recommendation in its entirety. If the City Manager accepts the recommendation, then the City Manager shall forward that recommendation to the City Council. That recommendation shall include the written recommendation of the Independent Review Board, and a transition strategy that addresses contract monitoring, service interruption and affected employee procedures, as well as a proposed agreement with the independent contractor. The City Council shall have the authority to accept or reject in its entirety any proposed agreement with an independent contractor submitted by the City Manager. In order to accept the recommendation to award a service to an independent contractor, the City Council must determine that this City service can be provided more economically and efficiently by an independent contractor than by persons employed in the Classified Service, while maintaining service quality and protecting the public interest.  
*("City Manager and City Council Consideration of Decision of Independent Review Board" added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3715 Notice to Affected Labor Organization and Affected Employee Procedures**

- (a) Before the City Manager recommends to the City Council that it approve a proposed agreement with an independent contractor to perform work for the City which is currently being provided by a City Department, the City Manager will notify all labor organizations whose members would be affected by such an agreement, as well as the City Personnel and Labor Relations Departments, and shall provide the number of City positions by job classification, that may be displaced if the contract is awarded to the independent contractor.

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- (b) City employees who will be laid off as a result of Managed Competition shall be entitled to utilize the layoff procedures set forth in Section L-5A of the Personnel Regulations of the City of San Diego, entitled “Layoff, other than Police or Fire Units”, as well as Rule V of the Civil Service Rules, entitled “Layoff and Reemployment.”  
*(“Notice to Affected Labor Organization and Affected Employee Procedures” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

**§ 22.3716 Monitoring Performance of Independent Contractors**

The City Manager shall have the sole responsibility for administering and monitoring any agreements with independent contractors. The City Manager shall be required to produce annual performance audits for contracted services, the cost of which must be accounted for and considered during the bidding process. In addition, the City Manager shall seek an independent audit every five (5) years to evaluate the City’s experience and performance audits.  
*(“Monitoring Performance of Independent Contractors” added 1-17-2007 by O-19565 N.S.; effective 2-16-2007.)*

# PART IX

## ABOUT THE AUTHORS

### **Geoffrey F. Segal**

is the director of privatization and government reform at Reason Foundation, a nonprofit think tank advancing free minds and free markets. He is also editor of Reason's *Privatization Watch*.

Segal recently served as an advisor to Florida Gov. Jeb Bush's Center for Efficient Government. In addition, his counsel has recently been sought out by South Carolina Gov. Mark Sanford and Indiana Gov. Mitch Daniels, where he is working with the Government Efficiency and Financial Planning group inside the Office of Management and Budget. Segal is also an advisor to the Cost Cutting Caucus in the Virginia House of Delegates and was recently appointed to the Commonwealth Competition Council.

Segal is a highly skilled policy analyst with a strong, diversified background in policy research and project analysis focusing on public-private partnerships, competition, government efficiency, government spending and waste, transparency, accountability, and government performance.

Segal has worked closely with legislators in California, New York, Florida, Indiana, Virginia, Pennsylvania, Georgia, Illinois, Oregon, Kentucky, Ohio, Washington D.C., Colorado, Minnesota, Maryland, Maine, Missouri, North and South Carolina, Hawaii, Arizona, Washington, and Texas in efforts to reduce government spending, improve government performance, and enhance accountability in government programs.

Segal has testified to the United States Senate and numerous state legislatures and agencies. He has written dozens of articles for leading publications including *Investor's Business Daily*, *Atlanta Journal-Constitution*, *Indianapolis Star*, *Orange County Register*, *Houston Chronicle*, *Los Angeles Daily News*, and *New York Sun*. Segal is also a contributing editor to *Budget & Tax News*. A frequent guest on television and radio, he has appeared on Fox News Channel's "Your World with Neil Cavuto" as well as CNBC's "Closing Bell with Maria Bartiromo," "Kudlow & Company" and "Power Lunch."

Segal earned a B.A. in Political Science at Arizona State University and a Master of Public Policy from Pepperdine University.

### **Adam B. Summers**

is a policy analyst at Reason Foundation. He has written extensively on privatization, government reform, law and economics, public pension reform, and various other political and economic topics.

In addition to Reason Foundation, his articles and studies have been published by the *Los Angeles Times*, *San Francisco Chronicle*, *San Diego Union-Tribune*, *Baltimore Sun*, *Orange County Register*, *Los Angeles Daily News*, *Los Angeles Business Journal*, *Contra Costa Times*, Foundation for Economic Education (*The Freeman: Ideas on Liberty*), Ludwig von Mises Institute, American Institute for Economic Research, Maryland Public Policy Institute, and Pioneer Institute for Public Policy Research, among others.

He holds an M.A. in economics from George Mason University and a B.A. in Economics and Political Science from the University of California, Los Angeles.

**Leonard C. Gilroy, AICP**

is a senior policy analyst at Reason Foundation. Gilroy, a certified planner (AICP), researches housing, urban growth, and land issues.

Gilroy designed and manages several Reason Web sites, including [www.Reason.org](http://www.Reason.org), [www.Privatization.org](http://www.Privatization.org), and [www.UrbanFutures.org](http://www.UrbanFutures.org), which has frequently been named one of the Web's best urban planning sites.

Before joining Reason, Gilroy was a senior planner with an urban planning consulting firm in New Orleans where he authored planning and research reports, managed the firm's geographic information systems (GIS) databases, developed and maintained Web sites for public-sector clients, facilitated focus groups, and coordinated public meetings.

Gilroy has also co-authored several research reports through the Virginia Center for Coal and Energy Research at Virginia Tech.

Gilroy earned a B.A. and M.A. in Urban and Regional Planning from Virginia Tech.

**W. Erik Bruvold**

has been the President and CEO of the San Diego Institute for Policy Research since its founding in October 2006. He has overseen the development of SDI's research program, including the initiating of San Diego first regular public opinion poll, the revitalization of a bi-monthly economic bulletin and the production of several widely cited and referenced studies on the region's challenges. Mr. Bruvold has been involved with San Diego politics and policy making for more than two decades. Most recently, he was Vice President of Public Policy for the San Diego Regional Economic Development Corporation (EDC) where he oversaw the organization's public policy efforts on a range of issues impacting San Diego's business climate. Among Erik's achievements at the EDC was his leadership of the successful effort to extend the TransNet sales tax for transportation investment and his leadership of the successful regional response to the 2005 round of military base closures and realignments (BRAC 2005). Prior to joining EDC, Erik was Executive Director for the San Diego chapter of the American Electronics Association where he established the council's local government affairs program, greatly expanded the public presence of the council in the community and authored several studies and editorial pieces on San Diego's high-tech industries. He holds a BA from the University of Denver and MA in Political Science from the University of California, San Diego.

# PART X

## ABOUT THE SAN DIEGO INSTITUTE FOR POLICY RESEARCH

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The San Diego Institute for Policy Research (SDI), LLC is a non-partisan organization whose mission is to improve the efficiency and effectiveness of the public sector throughout San Diego County. Established in 2006, SDI produces high quality policy to help generate debate and discussion amongst San Diego's decision makers and citizens alike.

SDI's policy research focuses on public policy challenges throughout San Diego County and makes extensive use of case studies and lessons learned in the private sector to show how competition, choice, and incentives can improve the quality of life San Diegans enjoy. The Institute also does research on the state of the region's economy and conducts San Diego's first bi-monthly public opinion poll. The views expressed in this and other policy studies are those of the individual authors and not necessarily of the San Diego Institute for Policy Research, LLC or its directors.



## ABOUT REASON FOUNDATION

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*Reason*

Reason Foundation's mission is to advance a free society by developing, applying, and promoting libertarian principles, including individual liberty, free markets, and the rule of law. We use journalism and public policy research to influence the frameworks and actions of policymakers, journalists, and opinion leaders.

Reason Foundation's nonpartisan public policy research promotes choice, competition, and a dynamic market economy as the foundation for human dignity and progress. Reason produces rigorous, peer-reviewed research and directly engages the policy process, seeking strategies that emphasize cooperation, flexibility, local knowledge, and results. Through practical and innovative approaches to complex problems, Reason seeks to change the way people think about issues, and promote policies that allow and encourage individuals and voluntary institutions to flourish.

Reason Foundation is a tax-exempt research and education organization as defined under IRS code 501(c)(3). Reason Foundation is supported by voluntary contributions from individuals, foundations, and corporations. The views are those of the authors, not necessarily those of Reason Foundation or its trustees.

# PART XI

## ENDNOTES

- 1 City of San Diego, Five-Year Financial Outlook: Fiscal Years 2008-2012, November 29, 2006, [http://www.sandiego.gov/mayor/pdf/five\\_year\\_plan\\_11\\_15.pdf](http://www.sandiego.gov/mayor/pdf/five_year_plan_11_15.pdf) (accessed August 21, 2007).
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