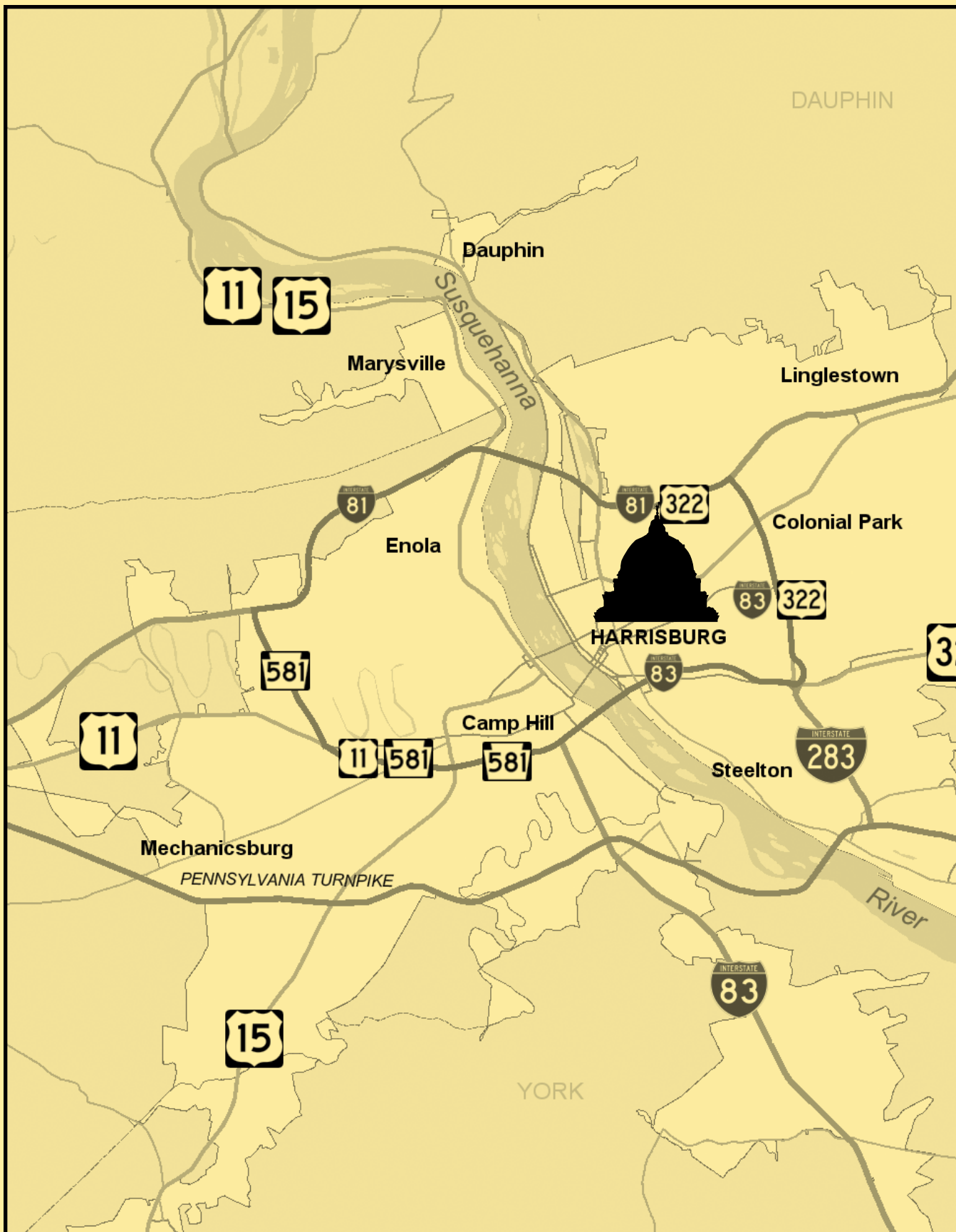


PRIVATIZING



“YELLOW PAGES” GOVERNMENT





PRIVATIZING “YELLOW PAGES” GOVERNMENT

COMMONWEALTH FOUNDATION & REASON FOUNDATION

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EXECUTIVE SUMMARY

Pennsylvania state and local policymakers are facing mounting debt, strained budgets, and underfunded public pension systems. These unprecedented challenges call for new and innovative policy solutions. By applying the “Yellow Pages test,” governments of all sizes have been able to do more with fewer resources. The “Yellow Pages test,” says that if a service can be found in the Yellow Pages of a phone book, government should consider buying it rather than using taxpayer dollars to hire and manage public employees.

The commonwealth is involved in an array of yellow page services. While many Pennsylvanians are aware of efforts to privatize Pennsylvania’s state-run liquor stores and to lease the Pennsylvania Turnpike, this report examines some of the lesser-known government-run businesses. For example, municipalities throughout Pennsylvania own a total of 49 golf courses; numerous local governments operate fitness centers; the Dauphin County Authority owns the Hyatt Regency at the Pittsburgh airport; the Department of Conservation and Natural Resources owns a luxury hotel at Bald Eagle State Park; and about thirty counties in Pennsylvania operate nursing homes.

The reason privatization works is simple: it introduces competition into an otherwise monopolistic system of public service delivery. Too often, poor performers in government are rewarded with budget increases following failure. Competition done right drives down costs and incentivizes good performance.

Diverse leaders throughout the country have embraced versions of the Yellow Pages test with great success. Florida’s former Republican Governor Jeb Bush achieved more than \$550 million in direct savings and avoided more than \$1 billion in future taxpayer costs. Former Indianapolis Republican Mayor Stephen

Goldsmith identified \$400 million in savings and opened up more than five dozen city services to competitive bidding. And Chicago’s Democratic Mayor Richard Daley has privatized more than 40 services and, since 2005, has generated more than \$3 billion in privatization deals for the Chicago Skyway toll road, four downtown parking garages, and the city’s downtown parking meter system.

All forms of privatization are simply policy tools—they can be effective when used well and ineffective when used incorrectly. In well-structured privatization initiatives the government and taxpayers gain accountability they rarely have with public agencies. Privatization is a tool that can lead not only to cost savings, but improve service quality, enhance risk management, and result in greater innovation.

Getting government out of unnecessary services is not limited to auctioning off services and assets; privatization can also involve governments partnering with for-profit firms to deliver services or with nonprofit organizations or volunteers.

This report surveys the scope of Yellow Pages Government in Pennsylvania, looks at examples of state and local privatization throughout the country, and outlines best practices to equip lawmakers to successfully transition government out of unnecessary services by implementing a variety of models.

I. INTRODUCTION

WHAT IS THE “YELLOW PAGES TEST”?

Over the years, governments at all levels have assumed hundreds of services that are commercial in nature. Most of these functions are not inherent or unique to government; in fact, they can be found in the Yellow Pages in towns all over America.

Coined by former Indianapolis mayor, Harvard professor and current chief deputy

for operations of New York City Stephen Goldsmith, the “Yellow Pages test” says that if a service can be found in the Yellow Pages of a phone book, government should consider buying it rather than producing it in-house.¹ Goldsmith put the test into action as mayor of Indianapolis in the 1990s, opening more than 50 city services to competitive bidding between public and private sector entities—driving down the costs of service delivery by \$400 million through competition.

The Yellow Pages test helps government concentrate on delivering “inherently governmental” services—those that should be performed by public employees, like public safety and judicial systems—while contracting with businesses and nonprofit organizations for other services. Ending taxpayer-subsidized competition with private businesses also frees up resources for agencies to complete their mission, and saves taxpayers money.

Leaders as diverse as Florida’s former Republican Governor Jeb Bush, Indiana’s current Republican Gov. Mitch Daniels, and Chicago’s Democratic Mayor Richard Daley have embraced versions of the Yellow Pages test with great success. Bush alone achieved more than \$550 million in direct savings and avoided more than \$1 billion in future taxpayer costs.²

Federal agencies are required by law to implement the Yellow Pages test. The Federal Activities Inventory Reform (FAIR) Act requires each federal agency to submit a list of activities to the Office of Management and Budget classifying federal workers into two broad categories: inherently governmental and commercial. As a result of the FAIR Act, agencies have identified more than 800,000 federal employees engaged in commercial activities—such as data collection, administrative support and payroll services—that could be provided by the private sector.³

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THE RATIONALE FOR PRIVATIZATION

Throughout the last half century, local policymakers in many jurisdictions in the U.S. and around the world have used privatization to better the lives of citizens by offering them higher quality services at lower costs, delivering greater choice and more efficient, effective government.⁴ Recent decades have seen the perception of privatization shift from a radical concept to a well-established, proven policy management tool.

Virtually every local government service—from road maintenance, fleet operations and public works to education, corrections, and public health services—has been successfully privatized at some point in time somewhere in the world.⁵

This trend is not confined to either major political party. The reason for the widespread appeal of privatization is simple: it works. Decades of successful privatization policies have proven that private sector innovation and initiative can do many things better than the public sector. Privatization also boosts the local economy and tax base, as private companies under government contract pay taxes into government coffers and offer employment to communities.

While getting government out of Yellow Page services often involves auctioning off these services, privatization can also involve governments partnering with for-profit firms to deliver services or with non-profit organizations or volunteers.

All forms of privatization are simply policy tools—they can be effective when used well and ineffective when used incorrectly. The reason privatization works is simple: it introduces competition into an otherwise monopolistic system of public service delivery. Governments operate free from competitive forces. Competition drives down costs and incentivizes good performance. Private firms operating under government contracts have strong incentives to deliver quality services. Government managers

and concerned citizens can use privatization to achieve a number of goals:

- **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. A Reason Foundation review of over 100 studies of privatization showed that cost savings ranged between 5 and 50% depending upon the scope and type of service; as a conservative rule of thumb, cost savings through privatization typically range between 5 and 20%, on average.⁶
- **Improved Service Quality:** A competitive process encourages bidders to offer the best possible service quality to win out over their rivals, and performance-based contracting can be used to guarantee minimum quality thresholds, incentivize quality improvements and penalize underperformance.
- **Enhanced Risk Management:** Through contracting and competition, governments may be better able to control cost inflation risks by building cost containment provisions into contracts. In addition, contracting can be used to shift major liabilities from the government (i.e., taxpayers) to the contractor, such as budget/revenue shortfalls, construction cost overruns, and compliance with federal and state environmental regulations.
- **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.
- **Accommodating Fluctuating Peak Demand:** Changes in season, peak demand, economic conditions and the like may cause service staffing needs to fluctuate significantly. Contracting allows governments to obtain additional help when it is most needed so that services are uninterrupted for residents

without permanently increasing the labor force.

- **Timeliness:** “Time is money” if you are a contractor footing the bill or if your contract with the city or state includes penalties for delays. Contracting may be used to speed the delivery of services by seeking additional workers or providing performance bonuses unavailable to in-house staff.
- **Access to Expertise:** Contracting allows governments to obtain staff expertise on an as-needed basis. For example, it may be cheaper to retain architects, engineers, and lawyers on an as needed basis than to hire them as full-time employees.

If poorly executed, privatization, like any other policy, can fail. Taxpayers may be worse off if a service is moved from a government agency to an incompetent or inefficient private business. Fortunately, Pennsylvania can learn from the experiences of governments in the United States and around the world.

APPLYING THE YELLOW PAGES TEST

State and local elected officials often ask: “where can we apply privatization?” One place to start is examining what other governments are doing.

At the local level, the International City-County Management Association (ICMA) conducts a survey of alternate service delivery by local governments every five years, measuring service delivery for 67 local services across more than 1,000 municipalities nationwide. The 2007 survey shows that public delivery is the most common form of service delivery at 52% of all service delivery across all local governments on average (see Figure 1).⁸ For-profit privatization (17%) and intergovernmental contracting (16%) are the most common alternatives to public delivery. Non-profit privatization is next at 5%, and franchises, subsidies and volunteers collectively account for less than 2% of service delivery, on average.

4. For more details on current trends in state and local government privatization, see Reason Foundation's Annual Privatization Report, available at: www.reason.org/publications/annualprivatizationreport

5. This evolution in governance is detailed in Stephen Goldsmith and William D. Eggers, *Governing by Network: The New Shape of the Public Sector*, (Brookings Institution Press: Washington D.C., 2004).

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8. Mildred E. Warner and Amir Hefetz, *Trends in Public and Contracted Government Services: 2002-2007*, Reason Foundation, August 2009.



**TABLE 1. USE OF ALTERNATIVE SERVICE DELIVERY FORMS BY METRO STATUS¹⁰**

| FOR PROFIT CONTRACTING SERVICE | % USE 2007 | | | % POINT CHANGE 2002-2007 | | |
|--------------------------------|------------|--------|-------|--------------------------|--------|-------|
| | Metro | Suburb | Rural | Metro | Suburb | Rural |
| RES. WASTE COLLECTION | 29.0% | 57.3% | 39.3% | -4.6% | 10.4% | 10.0% |
| COMM. WASTE COLLECTION | 39.2% | 63.8% | 52.7% | -2.1% | 14.5% | 18.9% |
| WASTE DISPOSAL | 35.3% | 51.9% | 30.4% | -1.7% | 8.0% | 0.8% |
| HAZARDOUS MATERIALS | 32.4% | 29.1% | 36.5% | -10.1% | -9.0% | 2.5% |
| AIRPORT | 17.1% | 14.7% | 9.0% | -6.2% | -15.8% | -5.3% |
| ELECTRIC UTILITY | 42.6% | 56.7% | 36.8% | 26.0% | 16.4% | 19.6% |
| VEHICLE TOWING | 57.1% | 68.4% | 65.4% | -22.3% | -13.1% | -9.3% |
| DAY CARE | 39.0% | 53.8% | 64.9% | 1.1% | 13.8% | 33.1% |
| CHILD WELFARE | 8.7% | 10.9% | 8.9% | -6.1% | -2.4% | 4.6% |
| TRANSIT SERVICES | 24.4% | 17.7% | 13.0% | -0.4% | -3.4% | -0.7% |
| JOB TRAINING | 9.2% | 7.4% | 2.6% | -5.2% | -3.0% | -5.6% |
| WELFARE ELIGIBILITY | 1.0% | 3.0% | 0.8% | -1.3% | 1.7% | -2.5% |
| HOSPITALS | 35.3% | 38.6% | 43.2% | 24.2% | 8.6% | 11.6% |
| INSECT CONTROL | 14.8% | 24.6% | 19.3% | 1.7% | 3.5% | 8.9% |
| DRUG PROGRAMS | 23.6% | 17.0% | 22.0% | 1.1% | 0% | 10.1% |
| EMERGENCY MEDICAL | 16.1% | 16.6% | 18.3% | 1.4% | 3.9% | 8.0% |
| MUSEUMS | 3.0% | 4.3% | 4.1% | -0.8% | -0.4% | -0.8% |
| FLEET MANAGEMENT | 23.6% | 28.6% | 22.3% | -15.3% | -11.2% | -8.4% |

Trends in levels of for-profit privatization and non-profit contracting have remained relatively steady over the last two decades, though the 2007 survey did not capture any uptick in local government privatization in the wake of the 2008-2009 recession and subsequent proliferation of state and local fiscal crises.⁹

Table 1 shows the percentages of surveyed local governments using privatization across a range of public services. Among the most frequently privatized local government services are waste collection (residential and commercial), waste disposal, vehicle fleet management, hospitals, vehicle towing, electric utilities, drug programs and emergency medical services.

Those services are just a start; City University of New York scholar and privatization expert E.S. Savas identified over 200 government services that have been

contracted out to private firms (including for-profit and non-profit).¹¹ Some of the most prevalent areas of state and local government privatization include:

- Accounting, financial and legal services;
- Administrative human resource functions (e.g., payroll services, recruitment/hiring, training, benefits administration, records management, etc.);
- Information technology infrastructure and networks, web and data processing;
- Risk management (claims processing, loss prevention, etc.);
- Planning, building and permitting services;
- Printing and graphic design services;
- Road maintenance;
- Building/facilities financing, operations and maintenance;
- Park operations and maintenance;
- Zoo operations and maintenance;
- Stadium and convention center

- management;
- Library services;
- Mental health services and facilities;
- Animal shelter operations and management;
- School construction (including financing), maintenance and non-instructional services;
- Park operations & maintenance;
- Correctional services (facility operations and management; health care, medical and food services);
- Child care, child welfare and adoption programs;
- Vehicle inspections and emissions testing;
- Environmental remediation;
- Golf course operations and management;
- Revenue-generating assets and enterprises (state liquor stores, toll roads, parking assets, etc.); and
- Major public infrastructure assets (roads, water/wastewater systems, airports, etc.).

Asking “what can governments privatize” is in many ways the wrong question. A better question is “where can’t governments apply competition or privatization?” Virtually every service, function and activity has successfully been subjected to competition by a government somewhere around the world at some time.

GOVERNMENT-RUN BUSINESSES IN PENNSYLVANIA 555-7524

Applying the Yellow-Pages test to state and local government services and programs in Pennsylvania reveals a great deal of government competition with private businesses. This includes golf courses, parks and recreation, museums, zoos, parking facilities, and more. Most of these services are funded primarily by user fees (and thus more easily privatized), but many are subsidized or guaranteed a profit by taxpayers.

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**GOLF COURSES &
FITNESS CENTERS555-9875**

Pennsylvania has the most golf courses per capita of any other state¹², with more than 810 registered golf courses.¹³ And, more than 60% of these courses are open to the public.

Municipalities throughout the commonwealth own a total of 49 golf courses. The newest addition opened in Montgomery County in 2006—the county's sixth course—the most any one county owns.¹⁴

Subsidized by taxpayers, municipal golf courses are often intentionally priced low to encourage new golfers. According to National Golf Foundation (NGF), the commonwealth's municipal golf courses are among the state's most popular. However with low fees, a saturated market and static demand,¹⁵ these courses can be an unnecessary strain on local governments.

Organizations like NGF can be hired to consult with municipalities and identify areas where it could save money through selling assets, leasing operations and community support. NGF has consulted with over 300 municipalities on golf courses nationally, including eight in Pennsylvania.

Some counties operate fitness centers, offering discounted memberships for county residents. These fitness centers, subsidized by tax dollars, compete directly with private businesses in the community, undercutting membership costs. For example, Derry Township in Dauphin County¹⁶ offers a monthly gym membership for residents that is 16% less than Gold's Gym, and nearly 30% less than The Family Athletics Club of Hershey. Other local governments, like the borough of West Chester, pay the ACAC (Atlantic Coast Athletic Club) to use their facilities¹⁷

for public school fitness. Most community colleges¹⁸ have fitness centers that are in part subsidized by the state.

**STATE PARKS & RECREATIONAL
PROGRAMS555-9734**

Pennsylvania has 117 state parks run by the Department of Conservation and Natural Resource. DCNR has had to shorten park operation hours, consolidate facilities and reduce staff in order to keep parks open. If funding is reduced further, DCNR has threatened it will close nearly 50 state parks.¹⁹

State parks provide a variety of services, for a fee, that private companies already offer, including campgrounds, swimming facilities, bicycle and boat rental, concession stands, ice-skating rinks, and education centers.

State parks receive state and federal funding, along with donations and park fees, with an operating budget of around \$80 million. In addition, park and forest facilities are set to receive \$19 million for site improvements.

Currently, Salt Springs State Park is the commonwealth's only state park managed by a private organization. The nonprofit, Friends of Salt Spring Park, has operated and maintained the park since 1994—offering educational programs and community events. The park, similar to most other state-run parks, charges no entrance fee, using donations and grants to operate the park and restore local historical sites. Last year, Friends leased 137 acres of mineral rights, a nonsurface lease, for more than \$750,000²⁰ to a gas company ensuring fiscal sustainability for future years.

Within parks, the state partners with private organizations to run concessions such as restaurants, watercraft and bicy-

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cle rentals, and golf course operations on state park sites. Approximately 150 concessions are operated by private companies through leasing agreements.²¹

DCNR also provides these services in some parks, including a luxury hotel at Bald Eagle State Park that opened in 2010 at \$7.5 million price tag. Expanding private concessions contracts would help separate public parks viability from tax dollars, placing financial liabilities on private investors, not taxpayers.

**MUSEUMS, TOURISM &
HISTORIC SITES555-3544**

The Pennsylvania Historical and Museum Commission (PHMC) currently own and operate 24 museums or historical locations, many without entrance fees. Over the last decade, state funding for museums has been on the decline. The Historic Preservation Society notes: "Since 2006, the PHMC, has seen its budget reduced by 48%."²²

Some museums have pursued public-private partnerships, such as the Philadelphia Museum of Art. In fact, some of the best historical sites in Pennsylvania²³

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22. National Trust for Historic Preservation, "Pennsylvania," <http://www.preservationnation.org/issues/11-most-endangered/states/pennsylvania.html>.

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are entirely privately owned and operated, including the Shriver House Museum and General Lee's Headquarters Museum in Gettysburg, which are the only museums in Pennsylvania to make the History Channel's "10 Must Visit U.S. Historical Sites."

Privatizing museums could also improve their quality. In a 2010 study, researchers in Italy found that museums that received public funds that were not tied to attendance were significantly less cost efficient.²⁴ One recent example of the lack of good management in state facilities is the 'misplacement' of over 1800 artifacts²⁵ by the Pennsylvania Historical and Museum Commission.

The commonwealth should work to outsource various portions, if not lease/sell whole sites that are currently owned and operated by the PHMC. Grants given by the Council on the Arts should also be analyzed and distributed on merit alone, while non-preferred grants by the legislature should cease.

ZOOS 555-3249

Historically, most of Pennsylvania's zoos began as city- or county-owned and operated entities. Over time, the zoos were privatized or turned into non-profit organizations. Levels of government funding now vary from zoo to zoo.

During the 1980s, the city of Pittsburgh decided to save more than \$1 million annually by closing down its aviary. In response, a citizen group took control of the aviary, receiving 17% of the facility's previous budget from the city and state grants for new investments.²⁷ Due to the successful privatization of the Pittsburgh Aviary, the entire Pittsburgh Zoo went private in 1994. While the zoo has received some state aid,²⁸ it operates profitably, with an almost \$3 million net profit in 2008.²⁹

America's oldest zoo, the Philadelphia Zoo is leased to the Philadelphia Zoological society at a price of \$1 a year since 1859.³⁰ General Fund appropriations for zoos were cut during the Rendell administration and will be eliminated this year by Gov. Corbett. This will be the second year the Philadelphia Zoo has received no state appropriations; however, it still can receive state support through grants, and the city provides free water and trash services.³¹ Memberships and gate fees fund approximately 80% of the zoo's operating budget.

Pennsylvania has many zoological organizations, some partnering with local governments. For example, the Erie Zoo is owned by the Erie Municipal Park Authority, but is leased to the city for operation.³²

Smaller regional zoos may struggle to compete with city zoos and must evalu-


ate their services and costs. Privatization done effectively has already helped to cut costs and raise the quality of some of Pennsylvania's most popular zoos.

PARKING FACILITIES 555-9156

Pennsylvania has 41 special-district governments overseeing parking operations, i.e., "parking authorities;" the rest of the nation has only five such special governments. Annual parking revenue for Pennsylvania totals \$112 million.³⁴

With city budgets running massive deficits and a looming pension crisis, many city governments are looking to cut costs. Privatization of parking provides much needed infusions of cash while residents benefit from better facilities and customer service. Three Pennsylvania jurisdictions—Pittsburgh, Harrisburg, and Allegheny County—have taken tentative steps towards privatization, though none has actually finalized a transaction.

In October 2010, the Pittsburgh City Council rejected a \$451.7 million bid³⁵ from LAZ Parking and J.P. Morgan Asset Management for a 50-year lease of 12 downtown garages and approximately 9,000 metered parking spaces. The lease included plans to spend \$440 million on capital upgrades and create 50 new jobs.³⁶



**PHILADELPHIA
PARKING
AUTHORITY**

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The lease bid was consistent with an independent valuation analysis commissioned by the City Council that found the parking system would yield \$2.35 billion in free cash flow over 50 years, a net present value of \$401 million in today's dollars.³⁷

The city of Pittsburgh, like so many Pennsylvania cities, has a serious pension issue with only 27.5% of their liabilities funded. Mayor Luke Ravenstahl's administration initiated the parking lease procurement primarily to generate approximately \$220 million, increasing the city pension fund's balance to 50% of total obligations by the end of 2010, enough to avoid a state takeover under a law passed by the state legislature in 2009. The Ravenstahl administration has warned that a state takeover would bring a dramatic escalation in mandated pension payments that would necessitate tax hikes, major service cuts, and widespread layoffs of city workers. Lease proceeds would have also been used to pay off \$110 million in city parking-related debt.

City Council attempted to launch an alternative plan authorizing the Pittsburgh Parking Authority to issue debt to raise \$220 million to buy city-owned parking assets, paying off the debt over time through parking rate increases. However, this proposal was denounced as "fiscally irresponsible" by Mayor Ravenstahl and rejected by the Parking Authority board.

One month before a pension takeover—the council began considering several alternative funding plans, including a revised parking lease proposal from LAZ Parking/J.P. Morgan. In the end, a non-privatization approach was approved. On December 31, 2010, City Council approved a one-time \$45 million payment to the fund and pledged more than \$700 million in parking tax money over the next 31 years.³⁸ Today, Pittsburgh's pension plan is in limbo because city leaders chose

to continue borrowing against the future instead of paying off their debts through privatization.

Separately, the Allegheny County Airport Authority rejected a proposal in August 2010 to lease the surface lots and parking garages (13,200 total spaces) at Pittsburgh International Airport. The lease proceeds would have been used to retire \$475 million in bonds used to finance a new midfield terminal in the 1990s.

Allegheny County Chief Executive Dan Onorato became interested in a lease as one potential way to drive down the airport's cost per enplanement, among the highest in the country. Because of the extent of its bonded indebtedness, the airport's airline cost per enplanement last year was \$15.80, making it one of the most expensive U.S. airports for airlines to serve. Debt service is running at \$62 million per year, compared with about \$22 million in annual parking revenue—under a lease the airport could have saved much more in debt service expense than it would have lost in parking revenue.

Parking assets were also a hot topic in Harrisburg in 2010. Despite the Harrisburg City Council's rejection of a proposed 75-year lease of the city's parking garages and surface lots in late 2008, developers continue to show interest in leasing the parking facilities, as the city has entered in Act 47 status as a "distressed municipality" under state law.

The original lease was intended to bring property tax relief and to beef up city services.³⁹ Two years later, the city of Harrisburg is on the brink of bankruptcy—largely due to the challenge of servicing \$310 million in debt incurred to retrofit its waste incinerator in 2004—lease proceeds could have been used to avoid a state takeover, which will jeopardize much more than the city's parking assets. Complicating the

lease discussion, the Harrisburg Parking Authority announced a proposal in October to take on up to \$200 million in new public debt, allocating up to \$60 million to the city to help address its fiscal issues.⁴⁰

The Philadelphia Parking Authority is larger and more complex than most city parking authorities—not to mention full of corruption.⁴¹ The entity enforces parking, runs garages, regulates taxis, and much more that could be performed by a private company. The sale of the Parking Authority could easily net a billion dollars for the struggling City of Brotherly Love.

In 2001, John Perzel, then-Speaker of the Pennsylvania House, engineered a state takeover of the Philadelphia parking authority—making it a haven for republican patronage. From 2001 to 2007, the number of employees on the authority's payroll doubled, and top salaries continue to climb, with the executive director, Victor Fenerty, making more than either the mayor or the Governor of Pennsylvania.⁴² Complaints prompted Governor Rendell to call for an audit of the agency in 2007.

A city audit became a surface examination of the agency because it refused to cooperate with City Controller Alan Butkovitz. Management claimed they could not provide comprehensive lists of contracts because the authority often broke up contracts to get around competitive bidding requirements. The authority's "questionable activities" included contracts with American Traffic, the fixing of parking tickets for family and friends, and the suspiciously small amount of funds going to city schools.⁴³

City and state owned parking garages, meters, and lots should be leased in an open bidding process or assets should be sold separately in the same manner. Governments should do their best to promote the sale to multiple organizations to increase competitive bidding.

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NURSING HOMES555-4698

At one time, 50 counties in Pennsylvania operated nursing homes. Today that number is around 30.⁴⁴ Since 2006, numerous counties in Pennsylvania have leased or sold their nursing homes. In most cases, the privatization of nursing homes occurred out of necessity as county governments faced multimillion dollar budget gaps.

In December 2006, Dauphin County sold the county nursing home. The sale has allowed county taxpayers to save about \$6 million a year and the facility, now called Spring Creek Health Care and Rehabilitation Center, is caring for an increasing number of residents including those on Medical Assistance.⁴⁵ The new owners have also invested in numerous capital improvements. Under county control, the facility continued to run up multi-million dollar deficits.

In Northumberland County, the commissioners voted unanimously to enter into a lease-purchase agreement with Complete HealthCare Resources to sell the skilled nursing facility for \$16.5 million. The sale of the Coal Township nursing home will shrink the county's operating budget by \$14.2 million in 2010, from \$85 million to \$71 million. And the county tax rate of 21.735 mills was reduced by more than 3 mills. Complete HealthCare also agreed to participate in Medicare and Medicaid,

maintaining a minimum Medicaid mix of 65% for residents.⁴⁶

Carbon County commissioners decided to sell the nursing home when it began draining the county of an estimated \$2.5 million to \$3 million annually. Carbon County received more than 40 bids and settled on an \$11,050,000 price tag for the 200-bed facility, which had been county-owned since 1972.⁴⁷ Without the sale, commissioners said they would have had to increase tax millage by two or three mills. County officials used part of the profits to pay off the agreed conditions to union parties including compensation for various benefits accrued.

Counties should evaluate turning the remaining publicly owned nursing homes over to private operators.

HOTELS & CONVENTION CENTERS 555-7165

Hotels and accompanying convention centers are in most cases private businesses, but recently county and city governments have decided that building and managing these complexes is a good way to raise additional revenue.

The Dauphin County Authority owns the Hyatt Regency at the Pittsburgh airport—more than 200 miles away from the county seat of Harrisburg. Unlike the authority's disastrous investment in the Forum Place

office building, the hotel is in the black on the operations side. However, the authority has had to dip into reserve funds to make bond payments. Debt service on the \$64.5 million in bonds floated to build the hotel in 1998 has continued to be a problem. In fact, using reserve accounts is technically a default on bonds.⁴⁸

In a controversial move, the city and county of Lancaster formed the quasi-governmental Lancaster County Convention Center Authority, which was responsible for a \$174.4 million dollar hotel/convention center project. Along with state grants and city backed bonds, the project benefited from a portion of the Lancaster county hotel tax.⁴⁹ In other words, local hotels were forced to send a portion of their proceeds to a build a future competitor hotel.

If these centers are such a good deal, with an above-average rate of return, the private sector would have built them. Instead, local governments borrow millions of dollars to erect a convention center that competes with local private hotels for conferences. By selling these hotels and

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convention centers, counties and cities can reduce their deficits and return to the core functions of government.

PRIVATIZATION CASE STUDIES

PARKS OPERATIONS & MAINTENANCE 555-1945

There are three general approaches to applying privatization in the operations and maintenance of public parks: outsourcing, conservancy, and concession.

Outsourcing is the simplest form of privatization in parks, where a state or local park authority decides to outsource specific services to private vendors, including building maintenance, waste removal, janitorial services, and trail maintenance. Like any service contract, under an outsourcing model government would still own, finance and operate the park, but contract with vendors for discrete services under short-term (typically, 1 to 2 year) contracts. Cost savings from outsourcing recreation facilities operation and management typically range from 20 to 50%, and cost savings from outsourcing park landscaping and maintenance generally range from 10 to 30%.⁵⁰

The conservancy approach utilizes a hybrid model where a nonprofit conservancy organization takes over primary responsibility for park operations and raises revenues to support the park, which are often matched by the local or state government. One of the most famous parks in the country, New York City's Central Park, is run by a nonprofit and was only cleaned up—literally rescued from the rampant crime and poor maintenance—when it was spun off from city government in the 1970s.

The nonprofit 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. As manager of the park, the Conservancy has protected the park by maintaining

and then increasing park staff. 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 generated revenue 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 to bring competition, accountability, and marketplace discipline. It would also minimize city spending on parks and generate funds to be spent elsewhere.

The third type of privatization in parks—and the most powerful—is the concession model, which can be applied in two different ways. A park authority may have a concessionaire operate a retail store or an equipment rental store within a park, returning a set percentage of revenues earned back to the public authority on an annual basis. Independent private concessionaires currently operate in many of the “crown jewels” of the national park system, including the Grand Canyon, Yosemite, and Yellowstone. However, this arrangement affects a limited aspect of park operations.

In the more powerful form, concessionaires are responsible for managing an entire park. Under a “whole park concession” model, a concession would essentially be a long-term (10 to 20 year) lease of the entire operation of a park (or, as is more often the case, a group of parks) under a performance-based contract with a private company. This is an approach pioneered by—and used extensively by—federal agencies like the U.S. Forest Service and Tennessee Valley Authority who recognized that running recreation businesses inside parks was not a core agency competency.

Contracts are usually structured as commercial leases in which the concessionaire collects 100% of recreation fees to fund the park's operations, and pays a set percentage of the revenues back to the public agency as an annual lease

payment, generally between 5 to 20% of annual revenues. Public expenditures on these parks can be significantly reduced—if not eliminated entirely—depending on the level of ongoing activities the parks agency desires.

Concessionaires are only allowed to do what is permitted under the contract, and they cannot change fees, facilities, and operating policies and procedures without approval from the parks organization. The public authority sets the recreation or preservation mission for the park, and the contract requires concessionaires to manage the park with that mission, including adherence to any development restrictions the parks agency chooses to adopt. Fears of concessionaires “cherry-picking” the profitable parks are unfounded, as it is common practice for authorities like the U.S. Forest Service to bundle together money-losing parks alongside break-even or revenue-positive parks in concession agreements.

Though pioneered and used extensively by the federal government—the U.S. Forest Service alone has hundreds of recreation sites run under “whole park” concessions—states have been slow to replicate this model. In one notable example, California ran out of money in the middle of a park redevelopment project earlier this decade at its McArthur-Burney Falls Memorial State Park. California State Parks partnered with a private firm, Recreation Resource Management, who financed and built 24 new cabins and completed several other improvements totaling more than \$1 million, at no cost to the state. To recoup its capital investment, the firm was given a longer term (20 year) concession during which it will operate the cabins, and share revenues with the state.

Perhaps the most important benefit of the concession model lies in the concept of risk transfer—the ability to transfer important and costly risks away from taxpayers and to a concessionaire. Some of those risks include:

- **Revenue/demand risk:** The concessionaire is forced to bear 100% of the revenue risk. This incentivizes conces-





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- **Appropriation risk:** As cash-strapped state's deal with budget crises they are forced to make difficult decisions about the core role of government. Parks often struggle to retain funding in lieu of other expenses such as law enforcement or education.
- **Legal risk/liability:** Under public operation taxpayers bear the risk of insurance, and since states often self-insure, it is difficult to say what the true cost of insuring parks is. Through privatization the concessionaire has to pay for insurance, which removes the risk to taxpayers and reduces cost of insurance for the state as a whole.
- **Project delivery risk:** To the extent that there might be capital expenditure involved in a concession contract (like a visitors center or new trails) the concessionaire assumes the risk associated with the project. This incentivizes the concessionaire to complete the project in a reasonable amount of time, because each day the park isn't open they cannot collect revenue.

The most common misconception associated with parks privatization, regardless of the model used, is that the public will lose control of parks and as a result they will be commercialized beyond recognition. In reality, state and local governments have the authority to dictate every last detail in a contract. Concessionaires cannot disturb

a tree, expand a water or power line, build a restroom or change fees and operating procedures without prior approval from the park's organization.

HIGHER EDUCATION FACILITIES & SERVICES555-6752

Public institutions of higher education are similar to state governments in one important way—they tend to grow into large bureaucracies that expand into non-core, commercial functions and activities, rather than strategically using privatization and competitive contracting to deliver efficiencies and cost savings.

Public university administrators in Pennsylvania should begin looking for new and creative ways to tap privatization and competitive contracting to drive down costs and improve services. Some services commonly outsourced at public universities include facility maintenance, landscaping and grounds maintenance, security operations, parking operations and maintenance, transit services and administrative support functions (e.g., information systems, accounting, payroll services, human resources, etc.)

Savings and operational changes through outsourcing can be significant, as two recent examples illustrate. In July 2010, the final report of the New Jersey Privatization Task Force estimated that colleges and universities in the Garden State could

save approximately \$27.4 million annually through the outsourcing of a variety of facility maintenance functions. Also, the University of Alaska-Fairbanks announced plans in 2010 to contract out the management of its bookstore to Follett Bookstores, the largest national college bookstore operator, citing high operating costs and Internet book downloads as impediments to a sustainable in-house operation. Privatization will return textbooks to the bookstore, improve the online store, and provide new services and a wider array of merchandise.

Policymakers should also embrace the innovative financing of capital projects through public-private partnerships (PPPs). State universities invest a tremendous amount of capital into expanding and constructing facilities—academic buildings, administrative complexes, dormitories and the like. State university systems across the country are beginning to look beyond traditional tax-exempt financing (e.g., bonds, etc.) towards more innovative procurement models that bring private sector capital and expertise to bear on the financing of university facilities.

A recent sampling of innovative PPP arrangements in higher education include:

- **University of California:** The University of California-Davis is using a PPP to deliver its West Village project, a 130-acre project that will provide 343 housing units, 1,980 student beds in apartment housing and 42,500 square feet of retail space. The university will receive income from both the lease payments for apartments and retail uses and payments by resident faculty in the housing units. Using a PPP allowed the university to leverage its small, direct investment of \$11 million into a viable \$280 million project.⁵¹
- **Florida Atlantic University:** In March 2010, Florida Atlantic University (FAU) announced a PPP for a new \$123 million on-campus student housing community on its Boca Raton campus. Under the PPP, Balfour Beatty Campus Solutions and Capstone Development Corporation will oversee the development and



51. Bay Area Council Economic Institute, Public Private Partnerships: Alternative Procurement Methods for Campus Development in the University of California System, June 2010, p. 7.

management of the 1,216-bed student residential project, Innovation Village Apartments, including mixed retail and office uses. Though this project is being financed through a combination of tax-exempt and Build America bonds issued by The FAU Finance Corporation, partner Balfour Beatty Capital has invested in the project by purchasing \$3.4 million of tax-exempt bonds.

- **Northern Illinois University:** The school's board of trustees approved a plan in early 2010 to develop a new, state-of-the art on-campus housing complex to attract more students and have agreed to pursue a PPP model to deliver it. Under the plan, a private concessionaire would finance and construct the complex, which would then be managed by the university.

Given these and other experiences from public higher education systems across the country, Pennsylvania's public universities should evaluate all planned capital projects—and all future projects—for a PPP financing model to generate a better return on investments.

PARKING ASSETS 555-1988

Downtown parking meters and city parking facilities are viewed by many public officials as an important source of revenue. However, often they aren't properly managed or fully maximized, making the operation and maintenance of parking assets a natural privatization opportunity. Further, few public officials would argue that providing municipal parking facilities—garages, surface lots and parking meter systems—is a core function of government.

Rather, parking is essentially a commercial venture, presenting opportunities for private providers to improve operations and enhance revenue. Privatization in parking can take on different forms, from long-term leases of city facilities to multiple leases for competition between garages or parking areas.

Though parking privatization is commonplace in Europe and many other countries, Chicago pioneered leases in the U.S. In 2006, the city announced a 99-year, \$563 million lease of four underground parking garages located downtown, beneath Grant and Millennium parks. The 9,178 spaces made Chicago's system the largest in the United States. In return for the \$563 million upfront payment—primarily used for debt reduction and the establishment of reserve funds—winning bidder Morgan Stanley agreed to rebuild garage infrastructure over the life of the contract.

Chicago was not done yet. In December 2008, Mayor Richard Daley announced the winning \$1.15 billion bid for a 75-year concession (lease) of the city's downtown parking meters, marking the first privatization of an urban parking meter system in the United States. With more than 36,000 meters generating roughly \$19 million per year, Chicago's is among the largest parking meter operations in the country.

In exchange for an upfront \$1.15 billion payment, the agreement grants the operator— Chicago Parking Meters, LLC, a consortium led by Morgan Stanley Infrastructure Partners—the right to maintain and operate the meters throughout the life of the contract. The deal requires the op-

erator to do a wholesale system overhaul, replacing over 30,000 antiquated, coin-based meters with just over 4,000 high-tech, multi-space/multi-pay meters that will facilitate payment via cash, credit and debit cards and potentially other pay systems. Furthermore, the system replacement is occurring at the concessionaire's own expense—separate from the \$1.15 billion upfront payment—removing significant future operations, maintenance and capital expenditure costs from the city's books for decades to come.

The city remains responsible for rate-setting, parking regulation enforcement and fine collection. The deal preserves the city's decision-making authority over the number of meters, hours of operation and the length of time a customer can park. Parking rates will be allowed to rise each year for the first five years of the contract, after which any subsequent rate increases over the remainder of the contract term will require city council approval. Increases in any given year would be capped to increases in the consumer price index.

While glitches in the early implementation of the Chicago parking meter lease—and policymakers' reliance on lease proceeds to close budget deficits in recent years—prompted significant scrutiny of the transaction from local officials and media, the turbulence of the early rollout subsided as operational improvements took hold.⁵² In fact, the concessionaire has reduced the average repair time for broken meters from two days (under city operation) to less than two hours, and the full replacement of the 36,000 parking meters is nearly completed, roughly one year ahead of schedule.

Indianapolis became the first to follow in Chicago's footsteps in August 2010 when Indianapolis Mayor Greg Ballard announced the winning bidder for a 50-year lease of nearly 3,700 city parking meters in the downtown and Broad Ripple areas. Under the lease, a team comprised of Xerox-subsidiary Affiliated Computer Services (ACS) and its local partners Denison Global Parking and Evens Time will take over responsibility for meter system

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operations, maintenance and capital investment, in exchange paying the city \$20 million upfront and a \$600 million share of ongoing revenues over the 50-year lease term. The City-County Council narrowly approved the deal in November.

Under the terms of the lease:

- The concessionaire will take on all of the operating, maintenance and capital costs currently borne by the city today, removing significant costs from the city's books while increasing revenues available for citywide capital improvements.
- The ACS team will undertake an initial upgrade of all of the leased meters, converting them to a combination of solar-powered multi-space and single-space units that accept cash, debit and credit cards. Following the initial modernization, meters would be replaced at least once a decade through the end of the lease, costing the ACS team approximately \$7-10 million over the lease term.
- Having been unchanged for 35 years, the current 75-cent hourly meter rate would rise to \$1.50 over a two-year period under the lease. For the remainder of the term, all rate changes would be subject to City-County Council approval, and any future rate increases would be capped and could not exceed the rate of inflation.
- The lease includes a termination for convenience clause that allows the City to cancel the contract at its discretion every 10 years. The lease agreement specifies the amounts the city would pay to buy out the lease at each ten-year interval, ranging from \$19.8 million in year 10 to \$8 million in year 40.
- The city can permanently remove up to 200 meters without impacting its revenue share, a figure that would increase if the size of the system increases more than 20%. Further, the City retains the authority to relocate an unlimited number of meters in a zone without impacting its revenue share.
- The city would retain control over all parking meter advertising and naming right proposals and revenues would be shared only if the concessionaire sponsors the idea.

In accordance with state law, all city revenues generated from the parking meter lease will be dedicated to street, sidewalk and other infrastructure improvements in the metered portions of the downtown and Broad Ripple areas, effectively allowing the Ballard administration to stretch its existing \$500 million infrastructure repair program even further.

In addition to Indianapolis, Pittsburgh, and Harrisburg, several other U.S. jurisdictions have initiated or are considering procurements for parking asset leases. These include Los Angeles, California; the New Jersey Transit Corporation (NJ Transit); The City of Las Vegas and the Las Vegas Re-development; and Hartford, Connecticut.

HEALTH & HUMAN SERVICES FACILITIES..... 555-7891

States and local governments already make use of extensive partnerships with other government entities, for-profit companies and nonprofits to perform a variety of health and human services, ranging from providing assistance to individuals to complex contracts with private companies to finance, construct and/or operate facilities on behalf of a public agency (e.g., hospitals, mental health facilities, developmental centers, etc.). Given the high capital and operating costs and extensive private sector experience, these types of facilities are a natural arena for privatization.⁵³

Severe fiscal pressures, cost inflation in health-related industries, and federal mandates to shift disabled populations from institutional settings to community-based care are among the many challenges forcing governments to make dramatic changes to the way they deliver health and human services. In the case of public hospitals and other state-run facilities, a conflicting mix of social, political and operational objectives results in weak incentives to control costs. Additional cost burdens come from inefficient accounting, restrictive civil service and procurement rules and regulations, a tangled web of bureaucracy, and a general lack of accountability. All of these factors drive up costs and

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jeopardize care for affected populations. In this context, privatization is increasingly seen as a viable alternative to closing facilities and reducing services. Louisiana has been active on this front in recent years under Gov. Bobby Jindal's administration. Amid a wide-ranging structural reform in its Department of Health and Hospitals (DHH) and the state Medicaid program, the agency has embraced privatization in a variety of ways in fiscal year 2010, including:

- The Louisiana State University-run Charity Hospital System—the only statewide public hospital system in the U.S.—is in the process of being transformed through privatization as part of a transition from a “direct provider” model to a “purchaser” model. For example, the aging, state-run Earl K. Long Medical Center in Baton Rouge will be closed in 2014 and replaced with a public-private partnership with Our Lady of the Lake Regional Medical Center. Similarly, the Interim LSU Public Hospital in New Orleans will be replaced by a new teaching hospital run by a private board.
- The DHH privatized two state-operated community homes in 2010 and has also been transitioning some residents of to privately-run providers for an estimated overall savings of \$7.1 million. Further, DHH plans to privatize an additional 31 state-run community homes in the near-term. According to DHH, “[t]hese efforts are part of the department’s goal of get-

52. See discussion in Reason Foundation's Annual Privatization Report 2009 (www.reason.org/apr2009).

53. For a more detailed review of privatization models and approaches in the area of public hospitals, see Reason Francois Melese, Privatizing Public Hospitals: A Win-Win for Taxpayers and the Poor, Reason Foundation Policy Brief #41, November 2005, <http://reason.org/news/show/privatizing-public-hospitals-1>





ting out of the business of competing with private providers and decreasing the size of government.”⁵⁴

- DHH is discharging 118 people from state-operated psychiatric hospitals to privately-operated community homes, while transferring another 138 institutional beds to a private operator.⁵⁵
- DHH is also privatizing six state-run substance abuse treatment centers.
- These shifts in developmental disabilities, mental health and substance abuse treatment are estimated to save more than \$52 million in 2010, according to agency estimates.

In New Jersey, Gov. Chris Christie created the New Jersey Privatization Task Force in early 2010 to identify viable privatization opportunities across state government. Among their dozens of recommendations were the expanded use of community-based services, supports, and residential options for residents of the state’s seven developmental disability centers, noting that community-based programs can serve a portion of the population now served in state-run centers at a much lower cost (“in many cases less than a third”), while providing appropriate care in a more favorable environment for patients and their families.⁵⁶

Further, the Task Force suggested the privatization of one state-run psychiatric hospital as a step toward privatization of the entire system—estimating this one facility alone would save between \$9 million to \$22 million per year through contracting out operations to a private firm.⁵⁷

While a full review of the types and approaches to privatization in the operation of health and human services facilities is beyond the scope of this paper, state psychiatric hospitals offer a powerful example of the extent to which privatization can be applied.

State-operated psychiatric hospitals have been or are currently being privatized in Florida, Kentucky, South Carolina, Massachusetts, New Hampshire and Texas.

South Florida State Hospital (SFSH)—the first state psychiatric hospital privatized in Florida in the late 1990s—offers an excellent model. The aging facility had never been accredited in its 40-year history and was involved in a major class action lawsuit concerning patient abuse and abysmal conditions before policymakers decided to partner with the private sector. Within 10 months of receiving the contract, the private operator was able to get the existing facility accredited and the lawsuit dismissed, while at the same time financing and building a new, modern facility to replace it.

The annual cost to operate the new hospital plus the annual debt service on construction was less than the state was spending to simply operate the old facility. The private provider designed the new facility and facilitated tax-exempt financing on behalf of the state via a private, non-profit corporation. No state capital dollars were involved and the financing did not involve the state pledging its full faith and credit. The private provider designed and constructed the new facility using construction funding from the bond proceeds. Ownership of the facility reverts from the bondholders to the state upon satisfaction of the debt.

The results have been impressive. Since implementing the partnership, the hospital has reached some significant operational milestones, such as dramatically increasing the bed utilization rate (enabling the hospital’s catchment area to be increased to over half of the state’s population, de-

spite accounting for just 25% of the state’s civil psychiatric hospital beds), reducing the average patient stay from eight years to less than one year, and nearly eliminating the use of seclusion and restraint to manage patient behavior.

Cost savings through privatization have also been impressive. The Florida Department of Children and Families told a legislative committee in 2007 that the average cost per bed in privately operated state psychiatric facilities was as much as 15% lower than at the state-run hospitals. And more recently, the Florida Legislature’s Office of Program Policy Analysis and Government Accountability issued a report in February 2010 finding that SFSH’s per bed costs were 6 to 14% lower than two state-run facilities and that the quality of care was similar.⁵⁸

In this example, the state negotiated a performance-based contract that established care standards and performance mandates (with appropriate financial penalties for noncompliance). The state’s role then shifted to contract monitoring and holding the operator accountable for results. In the case of Florida’s mental health contracts, the state retained the ability to terminate the contract without cause with a mere 30-days notice, a provision clearly aimed at ensuring contractor accountability.

There is no cookie-cutter approach to privatization, and the SFSH-style model will be feasible or appropriate in certain circumstances, while more traditional

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54. Louisiana Department of Health and Hospitals, “Streamlining State Government: Current Streamlining Initiatives,” September 1, 2009, http://www.dhh.louisiana.gov/offices/publications/pubs-81/Current_Initiatives.pdf

55. Jan Moller, “Health care facing huge changes in Louisiana,” *The Times-Picayune*, March 28, 2010.

56. New Jersey Privatization Task Force, p.28.

57. New Jersey Privatization Task Force, p.28.





outsourcing models (services, administration, etc.), facility asset sale/divestiture or private provider reimbursement mechanisms may be appropriate in others.

As a starting point, Pennsylvania state and local policymakers should inventory the hospitals, psychiatric facilities, nursing homes and other health and human service facilities operated by their governments, evaluating where there may be opportunities to transfer residents to existing private sector providers, sell facilities, right-size the system through consolidation, outsource services, or enter larger-scale operating partnerships along the lines of those described in this section.

LIBRARIES.....555-3795

Municipalities across the country have increasingly looked to privatization of library operations to not only reduce costs, but maintain or even expand the quality of library services. Privatization and innovative public-nonprofit partnerships have been used to keep branches open when municipal budgets would otherwise demand cutbacks. Lack of funding is hardly the only motivation for contracting library services; other reasons include improving the quality of management, improving service levels, and acquiring expertise that is lacking in-house.

Riverside County, California became the first municipal government in the nation to contract with a private library operator in 1997, entering a partnership with Library Systems and Services Inc. (LSSI) that is still in place today. In June 2010, the county published a report on the first 13 years of the LSSI partnership, highlighting an array of benefits, including:⁵⁸

- Enhanced services, with operating hours, circulation and staffing more than doubling;
- Decreased operating costs, totaling \$900,000 in the first year alone;
- An expansion in the number of branches from 24 to 33 (a 27% increase) while maintaining a flat 1.15% ad valorem li-

brary property tax;

- More than \$15 million invested in new facilities or major renovations;
- An average 111% annual increase in the collection development budget;
- Enhanced financial accountability; and
- Significant investments in new library technology, including the addition of more than 200 public-access high-speed Internet terminals.

The pioneering privatization has been a model of success, according to report author Gary Christmas, Riverside County's former chief deputy county executive officer:

"We have defied the most outspoken opponents of outsourcing public libraries to a bottom-line-oriented business operation. For the first 86-years of existence of Riverside County libraries, we outsourced the library operations to the City of Riverside. But the effectiveness of that model began to unravel as state funding for public libraries was diverted [...] We had to make a dramatic change in order to save and improve our libraries and gain more control and accountability over policy making and expenditures. And we did so without raising taxes, without massive layoffs, and without foregoing the County's sovereignty. Our libraries remain 100% public and owned by taxpayers and we have more financial accountability and control over our library system than ever before."⁶⁰

In other examples, Chicago Mayor Richard Daley claimed that the city saved \$3.7 million by contracting out management of the city's Harold Washington Library. And in 2009, the Brooklyn (New York) Public Library became one of first libraries in the country to use UPS, rather than a local or internal courier system, to reduce costs and move materials more efficiently throughout its 60 branches. The library's former internal delivery system was frequently backed up, with turnaround times reaching between 7 to 14 days. Under the UPS contract, turnaround time has reduced to 24 hours, taking advantage of the company's overnight service focus,

and former library staffers and truck drivers now work as full-time sorters.

ZOOS & ANIMAL SHELTERS

..... 555-4687

Amid the ongoing budget challenges that local government entities are facing, privatization is one policy option local leaders can apply to ensure that amenities like zoos and animal shelters thrive during the current fiscal crunch.

More than half of the major urban zoos in the country—including world-class zoos in Chicago, Dallas, Houston, San Diego and New York City—are run by nonprofits, often the zoological societies providing supplemental financial support to zoos when they were under public operation. When done properly, the privatization of public zoos can bring a number of benefits, including lowered operations and maintenance costs, improved fundraising and capital investment and better marketing and concessions.

In August 2009, the Dallas, Texas City Council voted unanimously to privatize the Dallas Zoo, turning over operations to the nonprofit Dallas Zoological Society through a partnership expected to save the city \$1.5 million in 2010 and \$16 million over the next five years. Privatization discussions began earlier that year when Mayor Tom Leppert began exploring ways to close a \$190 million city budget deficit. Under privatization, the Dallas Zoological Society is responsible for all zoo management, operations and animals, while the city retains ownership of all related land and the zoo's nearly 200 physical exhibits. In the short term, the city plans to continue contributing operating funds to the zoo, though the level of subsidy is expected to fluctuate over time as the operator implements strategies to increase visitation and self-generated revenues. The agreement also requires the Zoological Society to meet or exceed current operating standards, lest it risk having to return operations back to city control.

58. Florida Office of Program Policy Analysis and Government Accountability, Information on Florida's Civil Mental Health Hospitals, Research Memorandum, February 18, 2010, p.2. Savings range derived on comparative costs per patient day of care provided at the public and privately-operated hospitals.

59. Gary Christmas, The Riverside County Library System: Thirteen Years of Innovation, Experimentation, and Progress, County of Riverside, California, June 17, 2010, http://www.countyofriverside.us/export/sites/default/government/docs/Library_White_Paper_June_17_2010.pdf

60. Library Systems & Services, LLC press release, "New Report Substantiates Successful First Outsourcing of Public Library System in U.S.," June 17, 2010, <http://www.rivlib.net/downloads/LSSIWhitePaper.pdf>.





Another benefit of the privatization is found in the potential for greater private sector support through donations, according to supporters. Michael Meadows, president and chief executive of the Zoological Society, told the Dallas Morning News in 2009 that, “There is a perception when something is run by a public entity, that they don’t have a need for private donations. [The City] found that donors prefer to give to privately funded institutions.”⁶¹ Meadows’ point was later validated after four private donors pledged \$2.25 million to the Zoo within the first four months after privatization.

Animal shelters offer another opportunity to improve services through privatization. For example, officials in Kansas City, Missouri privatized that city’s animal shelter in 2009, and after the first year of implementation all signs indicate that the arrangement has been a major success.

In February 2009, the city signed a contract with Veterinary Management Corporation—a nonprofit created by local veterinarian R. Wayne Steckelberg—to operate the animal shelter. The annual cost of \$626,000 is \$175,000 less than it cost under public operation, representing cost savings to the city of more than 21%. A February 2010 article in the Kansas City Star cited numerous other improvements resulting from privatization, including a tripling in the monthly adoption rate, a 30% decrease in the euthanasia rate and a reduction in crematorium costs exceeding 50%. The private operator has also entered a partnership with Spay & Neuter Kansas City to promote outreach and awareness on the benefits of sterilizing pets to reduce the number of stray and abandoned animals.

Other recent developments in animal shelter privatization include:

- **Southampton, New York:** In January 2010, the nonprofit Southampton Animal Shelter Foundation took over operations of the town animal shelter in Southampton, New York. Under city operation, it cost approximately \$1 million to operate the shelter; under the terms of the contract, the city will pay the Foundation

between \$200,000 to \$300,000 annually to operate the shelter through 2012. No animals in the shelter at the time of privatization were euthanized, and the Foundation is following many of the same guidelines in place when the city operated the facility.

- **Paramus, New Jersey:** The Borough Council in Paramus, New Jersey approved the elimination of its animal control department in April 2010 and moved forward with a \$30,000 annual contract with Tyco Professional Animal Control. The borough spent approximately \$120,000 on animal control in 2009. Under the contract, Tyco will provide animal control and operate the borough’s animal shelter, with an option to use the shelter to house animals from nearby jurisdictions. Tyco currently provides animal control services for nearly 20 other communities in the Bergen County area.

LESSONS LEARNED

PRIVATIZATION BEST PRACTICES

.....555-8871

As is the case in all types of contracting, privatization can be implemented well or can be implemented poorly. A successful privatization process will ensure transparency, accountability and the delivery of high-performance services through a strong, performance-based contract. By using best practices and lessons learned from the experiences of other governments, the likelihood of achieving those results is greatly enhanced. Among them:

- **Rethink the status quo, and ask the “make or buy” question:** Taking a page from management guru Peter Drucker, every “traditional” service or function should have to prove its worthiness and proper role and place within government. Policymakers should ask fundamental questions about what role government should play, such as “if we weren’t doing this yesterday, would we do it today?” Once they whittle the list down to those core functions deemed necessary, they should then ask whether government should “make or buy” those services, opting to contract out

as many services as possible to the private sector to get the best value for taxpayers.

- **Think big:** The central question on the subject of outsourcing should not be “what can we privatize?” but, rather, “what can’t we privatize?” Outside of public safety services, the courts and policymaking functions, the private sector has proven repeatedly that there is nothing in the routine operations of government—those things that citizens interface with most directly—that cannot be privatized.
- **Bundle services for better value:** Governments may find greater economies of scale, cost savings and/or value for money through bundling several—or even all—services in a given department (e.g., public works) or departmental subdivision (e.g., facility management and maintenance) into an outsourcing initiative, rather than treat individual services or functions separately. There have been several instances of governments moving toward this approach since 2008.
- **Focus on building procurement and contract management expertise:** Successful privatization initiatives require good contract negotiation, management and monitoring skills on the part of city managers. The more that state and local governments use privatization, the greater the degree to which public officials’ role will center on contract administration—monitoring and

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enforcing contracts to ensure that the contractor's performance lives up to his contractual obligations. Staff must be properly trained in contracting best practices and, in particular, how to build specific service standards into agreements and monitor provider performance, in order to avoid possible ambiguities, misunderstandings and disputes.

- **Establish a centralized procurement unit:** Global experience with privatization shows the value of having a single independent decision-making body to manage privatization initiatives. Governments should maintain an expert team of procurement and competition officials to guide individual departments in developing their privatization initiatives. This central unit will help to break down the "silos" that departments sometimes operate within and identify city-wide, state-wide or enterprise-wide competition opportunities that might not otherwise be considered. States that have implemented this "privatization center of excellence" model include Texas (Council on Competitive Government), Florida (Council on Efficient Government), Utah (Privatization Policy Board) and Virginia (Commonwealth Competition Council).⁶²
- **Apply the "Yellow Pages Test" through regular commercial activity inventories:** Local government managers should regularly scour all govern-

ment agencies, services and activities and classify each as either "inherently governmental" (services that should only be performed by public employees) or "commercial" (services offered by private sector vendors) in nature. Undertaking a commercial activities inventory helps identify those areas in which government is engaged in the business of business, effectively competing against private sector business and under mining free enterprise and economic development.

- **Utilize performance-based contracting:** It is crucial that state and local governments identify good performance measures to fairly compare competing bids and accurately evaluate provider performance after the contract is awarded. Performance-based contracts should be used as much as possible to place the emphasis on obtaining the results the city or state 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.
- **Establish guidelines for cost comparisons:** State and local governments should 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 in situations in which public employees may bid against private sector firms to provide a given service, as the public and private sectors operate under different rules.

- **Utilize "best value" contracting:** Initiatives that are considered best practices for government procurement and service contracting utilize "best value" techniques where, rather than purchasing based on cost or "lowest bid" alone, governments choose the best mix of quality, cost and other factors in selecting a service vendor. Many privatization failures are linked to a low-cost selection where the allure of increased cost savings negatively impacted service quality.
- **Ensure contractor accountability through rigorous monitoring and performance evaluation:** Regular monitoring and performance evaluations are essential to ensure accountability, transparency, and that the local government's management and the service provider are on the same page. This can help address any problems that might arise early, before they become major setbacks.

PRIVATIZATION MYTHS AND FACTS

.....555-4429

Privatization is an intricate policy tool that is often misunderstood. Countless services or assets have been privatized across the United States, but despite that record of success several myths live on. Three of the most prevalent privatization myths are:

MYTH: Privatization is partisan.

FACT: Privatization is not the domain of any one political party or ideology. Politicians of both parties have successfully applied privatization across the United States. Officials that can apply privatization well prove that they are capable leaders who can bridge the gap between the public and private sector to provide high quality services without sacrificing efficiency. For example, former Indianapolis Mayor Stephen Goldsmith, a Republican, identified \$400 million in savings and opened up more than five dozen city ser-



vices—including trash collection, pothole repair and wastewater services—to competitive bidding. Chicago Mayor Richard Daley, a Democrat, has privatized more than 40 services and, since 2005, has generated over \$3 billion in privatization deals for the Chicago Skyway toll road, four downtown parking garages, and the city's downtown parking meter system. And when Edward Rendell was mayor of Philadelphia, he saved \$275 million by privatizing 49 city services, including golf courses, print shops, parking garages and correctional facilities.

MYTH: Privatization involves a loss of public control.

FACT: This myth involves a fundamental misunderstanding of the nature of privatization—that government loses control of an asset or service once it is privatized. In well-structured privatization initiatives, the government and taxpayers gain accountability they rarely have with public agencies. In fact, the legal foundation of a privatization initiative is a contract that spells out all of the responsibilities and performance expectations that the government partner will require of the contractor. Elected officials can include any number of terms or details to ensure that public resources are not being wasted. Any failure to meet the performance standards specified in the contract could expose the contractor to financial penalties, and in the worst-case scenario, termination of the contract. The potential for a terminated contract forces the contractor to self-regulate and maintain performance. Oftentimes the opposite is true in public agencies, which use poor performance as an excuse for more resources.

State and local government can actually gain more control of outcomes through well-crafted privatization arrangements. Through well-written contracts policymakers can ensure that private partners are held accountable in maintaining service expectations. For example, state officials in Indiana have testified that they were able to require higher standards of performance from the private concessionaire

operating the Indiana Toll Road than the state itself could provide when it ran the road, precisely because they specified the standards they wanted in the contract and can now hold the concessionaire financially accountable for meeting them.

MYTH: Privatization hurts public employees.

FACT: Privatization tends to encounter opposition from public employee unions who view it as a threat to their jobs and influence. This opposition is based in the fear that if a service were privatized they would be put out on the street. However, well-managed privatization initiatives need not put undue burden on public employees. Comprehensive examinations of privatization initiatives have found that they tend to result in few, if any, layoffs and those not retained by the new contractor usually either retire early or shift to other public sector positions.

Research on privatization has proven that public employees can actually benefit from privatization in the long term. The private companies who hire public employees present greater opportunities for upward career advancement, training and continuing education, and pay commensurate with performance. Nevertheless, it is important that management communicate early and often with the public employee unions regarding privatization initiatives. In the event that public employee jobs are at risk, the local or state government should develop a plan to manage public employee transitions.

CONCLUSION

Given the fiscal challenges facing their state and local governments, Pennsylvania policymakers need to use the current crises as an opportunity to transform public service delivery and apply the Yellow Pages test to drive down the cost of government. In considering privatization, Pennsylvania policymakers need to remember the tangible benefits beyond cost savings, including improved service quality, enhanced risk management and business process reinvention. Privatization allows elected officials to utilize the

strength of private enterprise in a way that promotes better governance and services for citizens. When implemented with care, due diligence and a focus on maximizing competition, privatization is an approach that puts results, performance and outcomes first to deliver high-quality public services at a lower cost.

ABOUT THE AUTHORS 555-2655

Leonard Gilroy is Director of Government Reform and Harris Kenny is a Policy Analyst for the Reason Foundation. Katrina Currie is a Policy Analyst and Elizabeth Stelle is a Policy Analyst for the Commonwealth Foundation.

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