

PUBLIC SECTOR VERSUS PRIVATE SECTOR:
A MODEL FOR PRODUCTIVITY

By

CHARLES D. HESLER

Bachelor of Science

Oklahoma State University

Stillwater, Oklahoma

May, 1981

Submitted to the Faculty of the
Graduate College of the
Oklahoma State University
in partial fulfillment of
the requirements for
the Degree of
MASTER OF SCIENCE
May, 1988

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CHAPTER I

PREFACE

When a service is provided by a federal, state, or municipal entity, accountability and responsibility for that service is accepted. Any service performed by governmental agencies should be provided as cost efficiently and effectively as any service purchased from the private sector. If a service cannot be provided equally or more cost efficient and effective, then it becomes an obligation of a governmental agency to eliminate those inefficient and ineffective internal service operations and purchase the service from a private purveyor.

Problem

Increasingly governmental agencies of the 1980's are being held accountable for their efficiency and cost effectiveness. This trend is being felt from the highest levels of the federal government down to local municipalities. Never before at any time in history have federal, state, county, and municipal agencies found themselves being examined and compared with the private business sector for efficiency and effectiveness.

One could assume that governmental agencies would have some way of evaluating the services that they provide to the taxpayer. Unfortunately, the majority of governmental agencies, especially those at state and local level, do not evaluate their services except as a budgetary comparison with the previous year's historical expense.

Purpose

The purpose of this study is to identify a viable, realistic model that agencies can use to measure cost efficiency and effectiveness of their

delivered services.

Objective

The objective of this study is to develop a workable and realistic instrument that can be used by city and county governmental agencies to measure the productivity of their service against an identical service provided by the private sector.

CHAPTER II

REVIEW OF LITERATURE

There is substantial difficulty in trying to determine the proper cost comparisons of services delivered by cities or counties versus the contractor in the private sector. The literature reviewed points up the various areas of local jurisdiction, city/county governments that lend themselves to cost comparisons and the possibility of outside bids to the private sector.

Until 20 years ago, few dared to compare private industry with governmental business endeavors. Today, and into the future, governmental agencies must stand the same productivity rules as private business. Productivity has become a common word in society's vocabulary. Productivity is "Doing more within a given period of time." According to Dolce (1984), an authority from the private sector on commercial fleet management, the basic purpose of productivity is to produce more with fewer people and at less cost. In contrast, there has been a steady increase in manpower in governmental agencies to accommodate the normal level of services provided to the constituency. In the private businesses of fleet and heavy equipment management, when peak work loads occur the excess is performed by an outside provider. On the other hand, governmental entities tend to staff for peak loads, rather than for normal work loads thereby creating expensive overstaffing. This is illustrated by the steady growth of support staffs local governmental agencies during the last 30 year. This has resulted in their services being more expensive than that of the private sector

Besides being overstaffed, the wages and fringe benefits of governmental employees are in many instances in excess of a comparable wage and benefit

package in the private sector (Stevens, 1984). Stevens stated that surveys have shown that eight local municipal government performed services were more expensive than the same services of another municipality with the only difference--it was performed by private contractors. The private contractors performed to the same standards that the municipal employees did and were more cost effective in providing the same services. These services included street sweeping, janitorial services, refuse collection, payroll operations, traffic signal maintenance, asphalt overlay, street tree maintenance, and turf maintenance.

Local agencies (city and county) are bureaucratic in nature and are slow to change their operating policies as noted by the Energy Task Force (D.O.E., 1980) Report. However, local agencies are being forced to become more efficient because "local jurisdictions are faced with rising energy and labor costs and the already stretched tax revenues are being further threatened by adverse taxpayer reaction to the cost of government" (p. 11).

With higher costs and fewer tax dollars to provide services, both cities and counties are being forced to acknowledge the taxpayer's demand. The taxpayer requires local governments to give value (services) for the taxpayer funds, to be innovative in hiring practices (Stevens, 1984), and to emulate the private sector in fiscally sound business practices. If the taxpayer feels ignored and local jurisdictions are not responsive to demands of competition to services performed, a loss of credibility or confidence may occur.

The credibility gap that local jurisdictions are experiencing might be the direct result of their inflexibility in improving productivity (Department of Commerce, 1978). This study involved a department of a local jurisdiction (city) and the related problems in defining and measuring its purchasing

department's productivity. The measurability of productivity in such a complex area was finally achieved using qualitative and quantitative measurement techniques.

Any function of a local jurisdiction that bills or charges for its services can have its productivity, efficiency, and a cost comparison of rates that it charges, verified, defined and measured (Moore, 1986). By taking into account such factors as man hours available for work per month, appropriate rates can be developed. The efficiency level is the total of the revenues divided by the man hours available. For an area to be able to fund equipment replacements and have in a positive cash flow condition, a 60 percent efficiency level is needed. The national average, however, is between 35 percent to 40 percent in the private sector (Moore, 1986).

There are progressive local jurisdiction entities that are at the leading edge of the growing movement of public/private competition for delivery of municipal services. Jensen (1986), for example, stated:

In Phoenix, Arizona, competition is the name of the game. Since 1979, the city of Phoenix has developed and refined a highly competitive process of bidding on a number of city services. This unique process provides a competitive environment in which the city bids against private contractors in order to determine who can provide the most cost effective service to the taxpayers (p. 7)

The key to this innovative and competitive process lies in the City of Phoenix's form of government. According to Jensen (1987), the form of government in the early days in Phoenix, encouraged croneism and corruption. This condition lasted until the mid 1950's when business people in the community became incensed with the graft and corruption and voted a new form of city government.

Jensen (1987) suggests Phoenix's new form of government encouraged

innovative approaches to city problems. One innovation was that of private companies providing contract custodial services to the city.. Upon the bidding of custodial services to the private sector, there ensued a multiplicity of problems and misunderstandings which were eventually ironed out. The key lesson learned in resolving the problems was to include provisions in the vendor contracts that allowed the City of Phoenix to deduct a sum of money from the vendor's monthly check for non-compliance with contractual obligation. This provision quickly brought shoddy and sloppy work to an end thereby eliminating complaints about the bid services.

The most innovative plan by far was to allow various departments to bid on the services that were offered to the private sector businesses. The team work between labor and management became the biggest bonanza of the bidding process when the departments that had performed the services were allowed to bid on recovering those services. This team work, according to Jensen, greatly improved labor relations with the unions. The rank and file employees were also challenged to look for ways to become more competitive and even regain services that had been lost to the private sector.

At one time in Phoenix, there were 11 areas of city services performed by the private sector. There have been other local governments that came to realize the benefits of competition for delivery of traditional city provided services. One such city was Newark, New Jersey. The leading proponent of Newark's privatization was A. L. Zack, Director of Departments of Engineering. Zack (1986) stated "...contracting or privatization is defined to mean the use of the private sector to deliver services historically provided directly by government employees" p. 3.

Jensen stated that the major obstacle in the initial bidding came from the employee labor unions. This problem was overcome when management and

union staff worked together to increase productivity to make the city provided services more efficient. The city eventually became able to compete with the private sector and actually underbid private firms to regain those previously lost operations and jobs (Jansen, 1986).

Privatization of traditional public services for Newark accomplished several purposes and they all involved money. For every contracted service provided with a private sector employee, the city saved 40 cents per salary dollar that would have been paid as fringe benefits for a city worker to have performed the same task. In 1986, Newark paid \$25,000,000 or \$1.00 of contract labor for every \$2.00 of city employee salaries, excluding police and fire department expenses for performed city services.

Another benefit received from Newark's privatization was the flexibility that it allowed to secure specialty skills that were not available in the local workforce. Another benefit was that of the 27 city services that were contracted, there were none that were 100 percent. With less than 50 percent of the total service advertised for bid, smaller more competitive private companies were large enough to perform the needed work. Zack proposed that when only a portion of the service was bid, a healthy competition was created between the public sector and the private sector employees.

Jensen (1987) stated "A rapidly growing method of providing municipal services is the public/private partnership that utilizes the advantages offered by both the public and private sectors" p. 1. According to Jensen, the many benefits that privatization gained for the community have continued to grow. Delivered municipal service in a competitive environment made team players of labor and management because they learned that it took both sides to remain a viable service provider.

Chapter III

RATIONALE FOR THE RESEARCH

This chapter will discuss (1) who and at what administrative level in governmental agencies would support productivity enhancement of public sector employees by privatization; (2) areas of internal resistance to the privatization concept in public agencies; (3) the type of information needed to evaluate effectiveness and efficiency, (i. e., productivity of public agencies and where to find the information); and (4) the development of an instrument that can identify costs, efficiency levels, staffing, and labor rate comparisons.

The purposes of this research was to gather data and develop an instrument to measure competitive productivity. If such an instrument were developed, it would provide a valuable tool for use in productivity comparisons between public and private sector support functions. The review of literature has suggested that active competition is a significant factor between the public and private sector for delivery of support services. The instrument this research will develop will present a criterion that could be applied to support services of public agencies thereby allowing comparison and evaluation with private sector services.

As Jensen (1986) stated in his City of Phoenix privatization effort, support for privatization must come from the highest level of administration. Privatization decisions involve funding, long-range planning, and the commitment to change an existing management policy and therefore the necessary follow-up for compliance status. In the case of Phoenix, the mayor, city council, and city managers as well as agency heads were supportive of the

privatization concept.

The opposition to privatization, according to Jensen, came from middle and lower level management as well as the service personnel who performed the services that were privatized. Labor unions also responded negatively because of loss of union members. The resistance that service personnel offered was understandable, according to Zack, in that it involved employee's fear of loss of employment.

It is essential that those groups who resist the privatization plan be communicated with because they hold the key to solving the resistance problem. As Jensen noted, the problem was not solved until there was active participation of middle and lower level management, service staff and union locals.

When a service is provided, whether public or private, expenses are incurred and revenues are earned. An expense is the total amount of funds expended to achieve a goal. A revenue is that money earned by an entity for the service performed which was the goal achieved. In business, either public or private, all factors included in financial statement are generated using basic accounting principles. In the public sector this information is mandated monthly by governmental agencies. At fiscal year-end, the total of the year's expenditures are compiled into the final yearly accounting ledgers. Governmental agencies receive financial reports of the previous months historical activity concerning expenses and revenues.

The private sector is not mandated by law to provide financial reports on a monthly basis, but good, sound business practice demands them for use as management tools. The financial report is critical for a successful business to monitor and track expenses and revenues of a given operation or service from the smallest department all the way to the total corporation.

CHAPTER IV
INSTRUMENT DEVELOPMENT AND VALIDATION

The instrument (Appendix A) is essential to any organization, public or private, in that it will show what a business or agency must charge to recover employee costs. When the phrase "employee costs" is used, it means total employee costs. In the private sector, a business can look good on paper and still become bankrupt for lack of funds. The inherent danger of public agencies is that they do not declare bankruptcy, they simply ask for greater amounts of appropriations. Inefficiency may go unnoticed or even be tolerated by an agency manager who knows that his superiors will not be pleased with notoriety that labor problems or lawsuits brought by employees dissatisfied with the work changes. The instrument will allow this manager to determine his rate of efficiency and then be the judge of what needs to be done. The instrument will show what labor rate should be charged for services rendered on a per hour basis as well as the measured percentage of efficiency of the agency.

In order to utilize financial information to analyze the effectiveness of a public sector business, Moore (1986) states that one must look at three areas: (1) total costs versus total revenues; (2) revenue versus the total potential for revenue; and (3) rate of labor versus the rate charged for comparable services.

Total costs for an agency consists of the following:

- A. Total salaries and fringe benefits of technicians and service staff.
- B. Total salaries and fringe benefits or percentages of, for managers, clerical, janitorial, and other support persons
- C. Building costs, utilities, equipment, depreciation, supplies, repairs and maintenance.

Effectiveness comparisons of potential versus actual invoice generated revenue necessitates the use of this type of formula:

- A. Number of invoice generating revenue (production) staff (1) times the number of hours worked per day (2) times the number of hours per year worked normally adjusted (3).
- B. Total number of revenue producing hours available (1 + 2 + 3)
- C. The labor rate or charge per hours for invoice generating revenue (production) staff
- C. Total of revenue available per year divided by
- E. Total of actual earned revenue per year to reflect percentages of effectiveness.

Labor rate comparisons for the services performed can be compared to competitive delivered services in the private sector. Chaiken and Dormont (1975) stressed the utilization of delivered services efficiency while Jalali-Yazdi (1977) encouraged linked formulas in evaluation. This instrument (Appendix A) contains 16 distinct but interlinking parts providing a formula that can be applied to any business or service to identify evaluation needs or steps in the search for productivity and efficiency of delivered services.

Stevens (1984) promoted efficiency and comparison of efficiencies, involving actual costs of services compared with competitive or non-traditional service delivery costs. Zack (1987) favored effectiveness percentages. Jensen (1986) stressed the importance of historical data comparisons of the potential of service costs for delivered services versus actual service delivery costs. The instrument represents some aspects of the various author's points of view taken from the review of literature. The instrument also includes the writer's formulation of those points into a business oriented, measurable work sheet of accepted business procedures from both the public and private sector.

To test the instrument, a panel of subject matter experts in various service oriented businesses were contacted and agreed to allow sampling using

the instrument. Of the four business critiquing the instrument, two were from the private sector and two were from the public sector. Seeking the widest variety of services possible, a security force service company, a custodial and building maintenance company, an automotive repair facility, and a food service operation were used. The findings gathered from these various service delivery firms validate the final version of the instrument to its present 16 level evaluation format.

In the private sector, businesses with a rate of 60 percent are accepted as healthy. The information needed to survey the agency is easily arrived at from the financial records that all governmental agencies receive monthly from their accounting section. When information is needed, go to the agency in question and request access to them as they are public records and open to the review by anyone.

Support for the privatization or productivity enhancement of public sector services comes from two primary sources. The first and most important ally is the taxpayer who lives and works in the private sector world and believes that delivered services should be delivered efficiently and effectively. The second most powerful ally is top management of the very agency or collection of agencies that one seeks to privatize. Middle level administrators and lower in the agencies will possibly not be much help initially because they will feel the brunt of the changes.

In conclusion, research has shown that in an unchecked monopolistic situation in which governmental agencies exist, services delivered tended to go up in cost and down in efficiency. However, introduce good quality competition from the private sector and watch productivity increase in public sector services.

SUMMARY

With the advent of the 1980's, the literature becomes more challenging by advocating that traditionally performed service functions of governmental agencies be placed on the cutting block of commerce to be sold to the "lowest" bidder. Early literature avoids the brashness and bold statements of the 1980's and talks of procedures and programs of very specific areas of productivity. Dolce (1984) spoke of productivity but did not get too deep into the subject. Stevens (1984) got closer but he too failed to delve into the specifics. Jensen (1987) and Zack (1987), however, showed that if given the opportunity and incentive, the public sector could become a viable producer of needed services.

CONCLUSIONS

The idea is forwarded that society is about to see an enhancement of traditional roles in the private and the public sectors. Competition and the privatization of those service functions that lend themselves to privatization will benefit from the process. Civil government authorities must be convinced that the change in process means no harm to their positions. In fact, if anything, their positions will be enhanced. It especially pleases this researcher to find from the literature, the need of competition to gain pride and respect for their job function in the public sector.

RECOMMENDATIONS

A. Offer incentive plans for public sector employees for their suggestions about ways that their service areas could be made more productive. Private

sector corporations such as Phillips Petroleum Company as well other organizations offer their employees cash awards based on a percentage of the dollar amount the idea saved the company in a year's time. Such an incentive plan could be judged by a committee of agency directors and function in the same manner as the Phillips Petroleum Company plan. The key to employee interaction in local government operation is to allow the employees a chance to receive recognition as well as a cash award as an extra incentive for their participation to provide more cost efficient governmentally provided service.

B. Annually review the effectiveness and efficiency of delivered support services of the public sector agency. At the first evaluation, any agency found below minimum standards of effectiveness and/or efficiency would be given one year to bring efficiency up to an acceptable level. If at the end of that probationary period the deficiencies had been overcome, the agency heads would receive both recognition and a one-time cash bonus. The agency head would also be placed in a program to allow he/she, along with the total staff, to receive a portion of the money saved from a more productive operation. Thus, each employee might work harder each year to remain productive.

C. Each agency head should be given the opportunity to bid against the private sector contractor to perform the delivered service that their respective agency performs. If the agency is the successful low bidder, all employees in that agency would share in the recognition and a percentage of the savings to the taxpayer as a one-time bonus. If, on the other hand, an agency did not raise its productivity at the end of the initial probationary period, that agency would have 25 percent of its assigned function bid to the private sector contractor. At the end of the first contract period the agency would submit the needed information to the comptroller who would prepare

specifications and solicit bids on the next contract for the agency. If the agency was not competitive, they would lose another 25 percent of their support function for a total of a 50 percent reduction in their assigned work function. If the agency's management failed to be the successful bidder on the third contract interval, new management would be brought in.

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SERVICE EFFICIENCY AND EFFECTIVENESS SURVEY

Cost Efficiency

- 1. Total salaries and fringe benefits of technicians and service staff A \$ _____
- 2. Total salaries or percentages of for managers, clerical, janitorial, and other support persons B \$ _____
- 3. Building costs, utilities, equipment, depreciation supplies, repairs, and maintenance C \$ _____
- 4. Total cost (A + B + C) D \$ _____
- 5. Number of technicians or service staff that actually produced invoiced revenue E _____
- 6. Loaded labor rate of technicians or service staff (D -- L) F \$ _____
- 7. Labor rate average for competitive comparable delivered services G \$ _____
- 8. Comparison of your labor rate differences (high) (low) H \$ _____

Cost Effectiveness

- 9. Number of technicians or service staff (E) times the number of hours worked per day (J) times the number of hours per year worked normally* adjusted (K) I _____

* (2080 hours less vacation (80 hours), less sick leave (40 hours), less 250 hours for two 15 minutes rest breaks a day = (1710 production hours per year)

- 10. Total number of revenue producing hours available (E x J x K) J \$ _____
- 11. The labor rate or charge per for technicians or service staff K \$ _____
- 12. Total of revenue available per year L \$ _____
- 13. Total of actual revenue per year M \$ _____
- 14. Effectiveness percentage (N 0) N % _____
- 15. Effectiveness ranking Scale

30 35 40 45 50 55 60 65 70 75