An Elected Official’s Guide

COMPETITIVE OPTIONS: FROM MANAGED COMPETITION TO PRIVATIZATION

Government Finance Officers Association
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FOREWORD

Elected officials and administrators are charged with the responsibility of effectively and efficiently delivering public programs and providing services to citizens. Under the pressures of tax limitations, fiscal strains, and stakeholders’ increasing demands, this task poses a perennial challenge to government agencies as citizen expectations for service quality continue to increase as expectations on price continue to decrease.

State, provincial, and local governments are presented with a variety of competitive options that provide fiscal management and alternative service delivery tools capable of meeting demands for more services, at a lower cost, and of a higher quality. Yet, the use of innovations in financing, managing, and delivering services cannot be applied in every case. Mayors, governors, and legislators must follow a diligent path when considering alternative service delivery options.

This Elected Official’s Guide presents an introduction to the use of competition in program and service delivery. The Government Finance Officers Association (GFOA) is deeply indebted to Rowan Miranda, former Director of the GFOA Research and Consulting Center (RCC), for his work on earlier GFOA projects in this area, and for providing valuable guidance and the necessary framework during the early stages of manuscript development. The GFOA appreciates the efforts of RCC staff Barry McMeekin, Senior Manager, and Morgan Shipley, Associate Manager, for finalizing the manuscript and setting forth a balanced presentation of tools and strategies that public officials are using to reinvent government throughout the United States and Canada.

Targeting elected officials and public administrators, the book details the managerial perspective of managed competition and provides useful...
guiding principles and recommendations to practitioners. It reviews the theory and evidence on why involving the private or nonprofit sectors may lower costs or improve the quality of service delivery. Yet the book also highlights the conditions under which it may be preferable for services to be produced through public agencies and describes the questions that must be answered prior to introducing competition.

Presented in a concise question-and-answer format, this book provides clear, understandable explanations to common questions about incorporating competition into alternative service delivery decisions, and in doing so, develops a comprehensive service delivery strategy that can rely on competition when there are benefits from doing so.

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INTRODUCTION

What is alternative service delivery and competitive options?

Responding to fiscal constraints, scarce resources, and demands for high-quality, low-cost services led government to search for alternative sources for delivering vital public services. Alternative service delivery methods are competitive options that present government with an innovative solution for restructuring the process of producing and delivering the services that citizens demand and expect. Without an exclusive example, alternative service delivery includes public, private, and shared delivery options. This Guide explores and highlights the basic concept of competitive options, the utilization of competition to determine the best type of service delivery, and a program for developing and monitoring this process.
Which services should be the government’s responsibility to provide?

Governments choose to pursue competitive options in order to improve the delivery of public services when situations dictate that change may be necessary. It is vitally important that participatory governments properly inventory their own ability to produce and deliver a service before determining which services may be candidates for alternative methods. Not all governments will choose to pursue alternative service delivery, and others will choose competitive options for specific services. Through this process, governments can adequately determine which services should remain restricted to public delivery methods. Such considerations are unique to each government, but may include regulatory agencies, policy-making bodies, police, and decisions and tools regarding economic development.
What is the best method for delivering a service to the public?

Each government assesses its own ability in order to evaluate the best means for properly delivering a public service. Answers may relate to the initial question regarding government responsibility or may lead governments to seek solutions from outside participants. Key considerations include: which services are citizens willing to purchase directly in the marketplace or produce themselves, and are citizens really willing to pay for services that they demand? These questions are recurring ones for the political leadership of most state and local governments and help shape the competitive process.
COMPETITIVE OPTIONS AND MANAGED COMPETITION

Why have governments chosen to use competitive options?

Governments pursue competitive options ultimately to provide the best service, at the best price, for their citizenry. This decision often stems from dissatisfaction with current operating results or the need to compare the results of current in-house services with those provided by the private sector. Cost savings, improved service quality, need to meet regulatory requirements, inability to retain qualified in-house service providers, desire to get out of non-core businesses to focus resources on core business, raise funds for other needs, and inability to raise sufficient capital for needed system improvements all motivate the search for competitive options.
What are the common types of competitive options?

Privatization

Privatization generally refers to increasing the role of the private sector in the delivery of public services. In its most extreme form, privatization involves load shedding—government getting entirely out of the business of financing and producing a service. The term contracting out is a specific form of privatization that relies on delivering a service through a third-party contractor (also called outsourcing). In much of the discussion that follows, the term privatization is equated with contracting out and outsourcing because that is the main form of privatization used in the United States and Canada.

Leasing

Franchises are licenses and agreements between governments and private firms to produce services within a particular geographic area. The principal role of government under this arrangement is a regulatory one—ensuring that firms meet specific price and quality criteria.

Examples of franchises include electric power, taxi service, cable TV services, ambulance services, solid waste collection, and even recreational facilities such as golf courses. Franchises can be exclusive (e.g., a single producer of a service) or non-exclusive (e.g., multiple producers). Public utilities are often arranged on the basis of exclusive franchises. Ambulance services are arranged on the basis of a non-exclusive franchise. Non-exclusive franchises are often favored because they promote price competition among firms and correspondingly increase citizen choices.

Outsourcing

Contracting out has a long history in state and local government and remains the most likely
form of privatization. In its early use, it was limited to specialized areas such as legal and insurance services. Surveys by the International City/County Management Association (ICMA) show that over the last several decades, the use of contracting out has extended to nearly every service that a local government provides and it remains the most popular alternative to government production.¹

Governments generally pay contractors on a lump-sum basis and expect them to follow specific standards that determine the level and quality of a service. The two basic types of payment schemes are fixed-price contracts and contractor cost agreements. Under fixed price contracts, contractors agree to deliver services of a specific quantity and quality for a set price and cost overruns are to be absorbed by the contractor. Cost contracts are used as a last resort because governments are expected to assume most of the risks. Under this arrangement, contractors lack incentives to reduce costs. Governments must undertake audits to verify that only the agreed-upon costs are included in the pricing. If the incentive structure “rewards” firms based on costs, firms might seek to invest excessively in capital equipment, for example, to boost profits.

What is managed competition and how does it relate to alternative service delivery?

Managed competition is a specific process within alternative service delivery that requires government agencies to periodically compete with the private sector to produce public services at the highest quality and lowest costs. The “managed” aspect refers to government continuing to maintain an active oversight role to ensure that the service is satisfactorily provided whether it is done internally or externally. The “competition” aspect reflects the belief that the public or private characteristics of the producer are less important than the extent of competition in service production. The end result is not privatization or outsourcing, but ensuring competitive service delivery. Thus, not all forms of privatization recognize (as does managed competition) that the simple and militant transfer of a service from a public monopoly to a private one is unlikely to yield improvements in either quality or cost savings. Managed competition is the hallmark of the reinvention efforts of several large cities—Charlotte, Indianapolis, Milwaukee, Phoenix, Philadelphia, Los Angeles, and San Diego—whose mayors and managers have received national attention for their work. Some jurisdictions also use the term “competitive contracting” to describe managed competition.

Managed competition is a special case of contracting out. Under managed competition, the process of “tendering” is used to subject government bureaus to competition by requiring them to bid on the service at the same time that the private sector is submitting bids. In theory, after the bid process is complete, it is possible for the government to retain the entire service in-house, have a split or joint arrangement where some of the service is produced internally and the rest through one or more vendors, or private firms may be used to produce the entire service with no governmental involvement.

2. Ibid.
Managed competition may be superior to other alternative service delivery arrangements for several reasons. First, it provides government employees and managers with a yardstick to improve their performance by comparing internal costs to external bid submissions. Second, it grants government agencies an opportunity to compete—simple and militant privatization does not. Third, it lowers the risk facing public managers and citizens who may otherwise be justified in their fears of service disruption. Fourth, in instances where collusion may occur, it is likely to be better if government retains some role in service production so that it can expand its role if private-sector prices get too high. Fifth, through competitive bidding, the process offers citizens the best-value procurement choice. And sixth, managed competition helps break down internal silos that contribute to non-competitive pricing of user department services.
Can all public services be subject to competitive options?

Decisions to pursue competitive options are not universal. Rather, officials must proactively determine the government’s suitability for changes in service delivery and recognize that decisions related to public service delivery can have important consequences for their citizens’ quality of life.

Unfortunately, no simple format exists for deciding on public service delivery. Presumably, any government service that is also available in the private sector could be a candidate for competitive bidding. Yet such conditions do not lead unequivocally to the conclusion that competitive options present the best choice for changes in service delivery. In general, when considering service delivery options and the possibility of introducing competitive bidding into the process, governments should consider the effect on public policy goals and initiatives, the effect on future competition, the ability to maintain critical public services, and the support of stakeholders and the public.
Governments consider competition for several reasons:

(1) *Overall cost reduction* is one of the most pressing reasons why governments consider alternatives service delivery. Governments may issue a request for proposals (RFP) to the private sector to obtain competitive bids. Bidders have an incentive to keep costs as low as possible in an effort to win. Some private firms may benefit from economies of scale that are difficult for the public sector to attain. For example, a multi-national refuse collection firm may be able to invest in the research and development of leading-edge equipment and technology when a city department simply cannot.

(2) *A reduction in labor costs* is another reason governments consider alternative service delivery arrangements. Municipal unionization rates have increased in the United States while private-sector unionization rates have decreased. Powerful unions seek higher wages, benefits, and better working standards while politicians may be pressured to meet union demands in an effort to win political support. The culmination of piecemeal clauses in labor contracts as a result of negotiation and arbitration may lead to contract conditions that increase the overall cost of service production.

(3) *The opportunity to increase revenue without increasing cost* might motivate governments to consider competition. Governments may allow third parties to provide services in an effort to increase revenue. In an age where politicians routinely take “no new taxes” pledges, they may deplete less political capital by allowing third parties to charge and set rates to cover the cost of services. Private third parties may also simply be better at
collecting revenue than government agencies.

(4) *Quality and customer service* can be the direct result of competition. When firms are operating on a cost efficient basis, consumers look to other differentiators such as quality in their choices. A private firm that must periodically win the business based on cost and performance may have a greater incentive for quality and customer service than a public “monopoly” agency.

(5) *Lack of in-house expertise and capacity* are factors to consider when outsourcing, especially in relatively new areas such as information technology management. Governments have difficulty maintaining a pay scale that is as responsive to market conditions for “hot skills” such as technology. Also, the quantity of work for a particular skill may be intermittent (e.g., upgrade of a software product every 18 months). Governments may also have difficulty building capacity to respond to program demands of legislative or oversight bodies or may be ill-equipped to deliver short-term services.

(6) *Maintaining a focus on core business* may be another reason to consider alternatives to public production. Over time, governments find themselves operating all kinds of programs that have little do with their central mission. Management may wish to focus on core services—effective police patrol, for example—and let third parties provide support services such as photocopying or fleet management. Does a city really need its own television station? By narrowing the focus of what they have to manage, it is possible that governments will do a better job.
EVALUATING COMPETITIVE OPTIONS

Are governments at a disadvantage during the competitive process?

Governments choose to pursue competitive options in order to secure the best service at the best cost for all stakeholders. Often such decisions introduce a competitive environment to affected business units for the first time. Such an environment does not necessarily lead to a disadvantage for the government provider or lead directly to outsourcing and job cuts. Rather, as a business unit within a public entity, affected service providers often have a significant competitive advantage due to pricing that does not include taxes or emphasis on profit, and an increased ability to borrow money for capital acquisition much cheaper than the private sector. As a result, although private service providers carry a perception of being better managed and more equipped to compete, being part of a non-profit, public-first government provides internal service providers with a strong base to compete.
How have competitive options been evaluated?

Studies on competitive options, specifically privatization, have examined a broad range of services. One of the most popular services examined is refuse collection. Other services include property tax assessment, electric utilities, school transportation, hospitals, wastewater treatment, police services, fire prevention, welfare services, and computer networks. This list is by no means comprehensive. Also, most of the studies have focused on cost (efficiency), not effectiveness and quality. Consequently, when evaluating services, governments should set meaningful performance measures and targets in advance of pursuing competitive options. By doing so, benchmarks can be developed and compared against external examples, internal services, current outsourced services, private examples, or proposed services.

As a result, it is difficult to get a definitive evaluation answer from available studies. Some studies compare franchises with municipal agencies, while others compare contract and direct municipal production. Some compare a single service within one city (e.g., municipal versus contractor production of janitorial services in two public buildings) while other studies make multi-ser-

vice/cross-city comparisons. Some scholars have carefully examined the literature and attempted to draw some general conclusions.

A recent review of the literature on the effectiveness of contracting out sought to assess the estimates of savings reported in studies. Some 135 studies were found that reported cost savings from contracting to the private sector. The average value of costs saving was about 14 percent. In studies where one government contracted to another (e.g., intergovernmental agreement), savings levels of 22 percent were found. Although this type of review has its limitations—namely, that it does not separate sophisticated studies from simple ones—it does show that contracting is found to be associated with lower costs in many instances.4 But governments wishing to contract out a specific service should seek to find out how other governments have fared that have contracted the service.

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Does private production cost less?

Numerous studies on refuse collection, such as the work by Berenyi, Berenyi and Stevens, Kemper and Quigley, McDavid, and Stevens and Savas are all consistent with the argument that contracting out public services costs less than public production. Berenyi and Stevens note that the differences between the private and public sectors can be attributed to personnel and equipment management practices. Contractors tended to use younger, less tenured workers, who received shorter vacation leaves and lower absentee rates. Contractor organizations were less labor intensive and had more direct control over their manpower and equipment than government. Savas states that these are more immediate causes and that the “ultimate cause is the absence of competition; when a government agency performs the work directly it acts as a monopoly.”

The most sophisticated of the studies, ones which controls for scale, service levels, technology, and environmental factors, find that public production is approximately 35 percent more costly than contract collection, although a range from 14 to 124 percent is reported. Further, the cost differential in favor of private contracting increases once one takes into account fees and taxes paid by contractors to localities with which they contract. Thus, the most sophisticated stud-

12. Ibid.
ies comparing public and private production of solid-waste collection favor contracting out service delivery.

An early study in this literature compared the cost to the City of Scottsdale, Arizona, of providing fire services via private contract with the cost of municipal fire departments. The study found that municipal fire departments provided services at costs between 39 and 88 percent higher than contractors.\textsuperscript{13} A study on housing found costs to be 20 percent higher, per constant quality housing unit, with municipal supply.\textsuperscript{14} A study of Lakewood Plan cities (i.e., a group of cities known for contracting nearly all of their services) in California found budgets to be approximately 20 percent lower than in non-Lakewood cities.\textsuperscript{15} In an extensive review of comparisons of private and public production of services in five countries, the authors summarized their findings by stating that “privatization is cheaper than production in publicly owned and managed firms and given sufficient competition between public and private producers . . . the differences in unit cost turn out to be insignificant.”\textsuperscript{16}

\begin{enumerate}
\item Borcherding, Pommerehne, and Schneider, “Comparing the Efficiency of Private and Public Production,” 127-56.
\end{enumerate}
Does the evidence lead to a compelling case in favor of private production?

In *The Privatization Decision*, the author’s analysis of privatization studies concludes that “Public versus private matters, but competitive versus noncompetitive usually matters more.” A good case for how managed competition might work is described in a famous study on railroads. The study compared the performance and profitability of the Canadian National Railroad to the Canadian Pacific Railroad. When the Canadian National Railroad enjoyed price protection for a long period of time, deregulation led to competition between the two railroads that substantially narrowed the differences in productivity to the point where the government company became marginally more productive.

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What is the impact of competitive options on service quality?

Critics of competitive options argue that private firms emphasize the bottom line more than public organizations and that this focus reduces the quality of service provided by private firms. Quality is difficult to measure for most organizations internally; these measurement problems become more difficult when comparing across organizations. To the extent there is evidence, it suggests that quality differences are minimal. In a careful analysis of ten cities, one study found that overall service effectiveness did not suffer as a result of privatization and in some cases it improved. In another study of 20 cities in the Los Angeles area, the investigators found that quality differences between private firms and government bureaus for eight services were statistically insignificant.

To adequately measure quality impact, governments can utilize the resources at hand. Include service experts with experience in the implementation, delivery, and monitoring of the service under consideration. These service experts provide insight unique to the government and help identify certain quality markers and sources of impact; for example, relevant regulations governing the service, or policy issues such as selecting the lowest responsible bid, choosing a minority vendor, or creating local employment.

For more practical purposes, how can governments use recent studies to structure competitive efforts?

The major limitations in competitive options studies stem from cost and quality measurement and the ability to generalize from specific studies to findings that might apply to state and local government as a whole. Governments seeking to consider competitive options and/or managed competition should not use a single study or a group of studies as a projection of the success they might have. Instead, government staff should try and understand the causal model for why costs were purported to be lower or higher and use this information in their decision process accordingly.

These studies do not represent means to an end, but provide benchmarks, lessons learned, and possible cost and quality comparisons. In structuring competitive efforts, governments must remain diligent to risks associated with opening the service to competition, namely low-balling. Private vendors may engage in loss leaders in order to gain entry into new market. While such efforts may lead to advantages both for the city and the private vendor, using available reports, examples, and cost/savings data to make cost estimates may lead to incomplete costs and inaccurate savings potential. Such conclusions ultimately affect the contract, implementation, total costs, and estimated savings potential.
What is at risk?

The decision to move forward with competitive options is accompanied by foreseeable and unexpected risks. To successfully implement a competitive process requires that governments properly acknowledge risk and incorporate a risk management system into any alternative service delivery initiative. Changes in delivery methods present government with an overarching service delivery risk. As mentioned in the sections on quality and cost studies, no conclusive evidence exists concerning the end results of competitive options initiatives. Maintaining service quality and estimating cost and savings potential are not guaranteed. Results may vary, and implementation may lead to success, continuation of current standards, or failure.

As a result, initial risk assessments should answer the obvious risk question: is the service under consideration a proper candidate for alternative service delivery options? Or stated differently, is the service under consideration better served by the government? The risk associated with this initial question is the ability and/or inability of the government to determine the suitability of the service, and what the government gains, loses, or sacrifices by pursuing alternative service delivery options. This question allows governments to analyze the major risk associated with changing service delivery methods: service interruption. The most common goal associated with changes in service delivery is to deliver a service at an acceptable level of quality while decreasing cost. Intuitive to this decision is the maintained delivery of the service; when pursuing a managed competition project, government must remain diligent both to the process at hand, the continued delivery of the service, and the seamless implementation of new delivery methods without any interruption of the service.

To achieve the stated goals of pursuing a competitive approach, governments must properly identify services that exist within a competitive marketplace and establish processes to create a level
playing field. To implement a program and invite vendors in a marketplace without real competition means that the incentives to keep costs down and quality high are forfeited. Moreover, if the process fails in producing a level playing field, the government risks losing the advantages introduced through competition. Consequently, a general risk is the inability to properly identify services within a competitive environment and the resulting likelihood of using improper benchmarks to estimate the level of competition and the propensity for savings.

Related directly to the risk of competition is the ability to determine full-cost estimates and accounting. Determining the service's actual cost provides the government with the benchmark and evaluation necessary to determine the most cost-efficient service provider. Without properly calculating costs, governments may lose the ability to properly estimate costs, which may lead to problems in implementation and contract adherence.

The stated goal of risk management should be to prevent, avoid, or mitigate risk in order to protect the financial stability, stated goals, and continued delivery of the service. Governments must take a total view of presentable risks and attempt to plan for unforeseen risks to better assess, evaluate, and assign priorities in order to select the best approaches for managing those risks. Such detailed plans also present government with insight into the suitability of the service under consideration. If the risk is too high, it may be wise to consider competitive options for other services.

For standard risks such as workers’ compensation or financial losses due to theft or foreseeable disasters, government can use standard insurance to cover the risk. For risks outside planned solutions, the government should implement a communication program to discuss solutions with relevant parties and articulate responses to affected stakeholders. Effective risk management programs include detailed monitoring and reporting mechanisms in order to properly assess the effects of competitive options, insure the continued delivery of the service, and maintain
accountability. Effective monitoring programs not only review delivery of services, but report on the status of the contract, and address the contractual stipulations placed on the service provider. The monitoring and reporting program should be fully planned and detailed during the contract phase by specifying the level of monitoring and reporting, addressing the responsibilities and tasks of the government and the service provider, and outlining the information necessary from the service provider.

Introducing competition into the delivery of public services presents significant risk to government. No “cookie cutter” approach to pursuing competitive options exists; easing the risks of implementing a competitive process requires government to view all services and delivery methods as different and establish programs around the particular nature of each service. By identifying these risks and establishing responses, government can manage and assuage the potential for risk and move forward with a competitive process.
What criteria should governments use to judge program and service delivery arrangements?

The topic of public-sector program and service delivery is an interesting one because governments are judged both on the basis of ends and means. Getting consensus on ends—quality services and low costs—is sometimes less problematic than getting agreement on means. That is, citizens may want government to use the service delivery mechanism itself to pursue social goals such as job creation, contracts for minority and disadvantaged business enterprises, or assistance to special populations such as seniors and youth. These issues raise an important question: What criteria should service delivery mechanisms be focused on?

Some political scientists and economists have argued that most governments use the criteria of fiscal equivalence in organizing service delivery. Fiscal equivalence is a public finance criterion that is met when citizens “get what they pay for and pay for what they get.” Financing specific services through general taxation can reduce fiscal equivalence and user fees can improve it. Though fiscal equivalence is only one criterion in the decision to provide services, if public officials ignore it problems often result. As noted by the Advisory Commission on Intergovernmental Relations (ACIR):

Individuals are led to distort their own expression of demand for local public goods, either by inflating their demands if others are required to pay or by depressing their demands if they have to pay more than their share. A lack of fiscal equivalence undermines the community interest within a provision unit and generates incentives for individuals to try to improve their own lot at the expense of others, rather than by
joining with others to improve the welfare of the community.\textsuperscript{21}

Thus, communities can lose residents through out migration if policies reduce fiscal equivalence. If the political process supports the provision of specific services, competition is one avenue that governments have toward promoting fiscal equivalence.

Developing comprehensive performance measures from the start helps government evaluate the adequacy of alternative service delivery. Establishing fiscal, quality, and performance benchmarks creates accurate criteria that hold public-sector and private-sector service providers to the same performance standards. This process facilitates the criteria used to judge program and service suitability.

STAKEHOLDERS, PUBLIC POLICY, AND EMPLOYEE CONSIDERATIONS

Who are the major stakeholders?

There are several major stakeholders in service delivery decisions. In the public sector, the most important are citizens and taxpayers who make residential location decisions in part based on bundles of services and associated taxes in specific communities. Inefficient service delivery or poor quality can lead to migration of citizens to other communities. Businesses also face similar incentives as poor services (e.g., access to major transit routes) or high taxes can affect their ability to operate or compete. Municipal unions and employees are also stakeholders as they make their livelihood by performing various tasks that comprise a service. Politicians and administrators also have a stake in service delivery because they are held accountable for government performance.

The primary responsibility of elected officials is to ensure that services desired by citizens are being produced efficiently and effectively. Arguably, elected officials should care less about the production mechanism than the overall outcome. Economists would be quick to point out that having other goals such as social redistribution through the service delivery mechanism (e.g., hiring more workers than needed to provide summer jobs) might be an expensive and inefficient way to improve social welfare (i.e., more efficient mechanisms for redistribution exist).
How do competitive options affect public employees?

Job security is undoubtedly the number one area of concern for municipal employees when a competitive options measure arises. Although there are numerous reasons for undertaking such efforts, including increased efficiencies and increased customer satisfaction, reducing costs is almost always a major reason for introducing competitive options to a government service. Since labor costs, both wages and benefits, account for the majority of spending on government provided services, any attempt to privatize those services will result in decreased spending on labor.

The idea of employee safety net programs such as retraining, reassignment, and early retirement should be developed and made available to affected employees early in the competitive process. Decreased employee morale that leads to decreased service performance is always a possibility when alternative service delivery is discussed. Presenting alternatives to the employees promotes positive labor relations and lessens employee apprehension. Utilizing human resource professionals to design and promote a comprehensive set of employee programs should always take place early in the competitive process.

During discussions of alternative service delivery and managed competitive, employees are likely to feel that they are being mistreated and cast off for the sake of reduced costs. There are many long-time government employees who have expended considerable energy in providing public service. It is important that government treat these employees fairly and show sensitivity toward their concerns. The government may seek their opinion on service issues and oftentimes allow them to compete for the right to deliver the service.
Do competitive options result in layoffs?

Although approved competitive options do not always result in employee layoffs, the possibility of job loss exists whenever service delivery changes from public to private. The transition period between public and private service delivery should be utilized to make employee layoffs an option of last resort. The adoption of a well thought out employee displacement program tends to lessen the effect on government employment and in most cases can serve to totally eliminate the need for employee layoffs.

In Indianapolis, an acknowledged national leader in managed competitive efforts, over seventy initiatives were launched between 1992 and 1996 with an end result of zero employee layoffs. Although officials had promised that the process would not result in employee layoffs, they still needed to devise a plan to absorb employees displaced by competitive options into other areas of employment. This was accomplished through a multitude of human resource initiatives including early retirements, hiring freezes, and employee retraining programs all designed with the aim of locating displaced workers elsewhere in the organization. These programs were the end result of careful negotiations with labor representatives and tended to soften opposition to the competitive options program.

Studies done over the past ten years regarding employee displacement from competitive options arrived at a general figure of between 5 and 15 percent of workforce reduction through layoffs.
What are the major concerns of organized labor?

Despite the lessening role of organized labor in many industries over the past twenty years, unionism still plays a dominant part in the public-sector service industry. Any attempt at turning over public services to private industry is met with great scorn from labor organizations whose role is to protect the rights of employees currently providing the service.

Labor unions generally voice the concern that competitive options initiatives are simply a mechanism for lowering employee wages. For lower skilled services such as landscaping maintenance or janitorial service, employees in the private sector do tend to be paid less than their public-sector counterparts. This disparity is usually a direct result of the collective bargaining process that labor unions fiercely protect. But many studies have shown that the private sector can provide services at a reduced cost without lowering wages. This is especially true in higher skilled areas such as data processing and fleet maintenance. This is usually because private-sector enterprises have more latitude with regards to other management issues.

Collective bargaining agreements address many other management issues and labor unions have serious concerns regarding these matters. These include issues such as scheduling, work rules, leave time, and other employee rights. As mentioned above, the absence of many of these same restrictions in the private sector usually serves to explain the outside vendor’s ability to improve performance.

Because of labor union concerns, competitive options have become a major point of negotiation during the collective bargaining process. Labor unions usually try to negotiate a clause banning competitive efforts, while governments attempt to preserve competition by retaining the right to seek alternative service providers. The end re-
sult in the collective bargaining agreement is generally somewhere in between these two competing interests. In some cases, unions do secure clauses banning competitive options, usually in areas where they have power over the political process. Recently, collective bargaining agreements have included the right for workers to be part of the competitive process. In order to compete, labor unions must be able to protect the above concerns without hindering their ability to submit competitive proposals.
How do competitive options affect management employees?

Management employees affected by competitive options face many of the same issues that concern the employees they supervise. The transfer of services from public to private provision will affect job security, salary and benefits and, in turn, management morale. In the case of management, the government and management employees themselves should have a wider range of options available during the competitive process. These options should be openly discussed. In most cases, management employees possess extensive expertise and knowledge of the subject function that will make them probable candidates for monitoring the contract provisions. Those with superior management skills can probably become assets in other areas of the organization. Those that cannot be moved to other areas or utilized to monitor the contractor should be afforded the same employment safety net programs that are offered to municipal line employees.
How do competitive options affect public policy goals?

Competitive decisions leading to the privatization of public services may have substantial impact on stated public policy goals and initiatives. Prior to competitive options initiatives, current service delivery processes may include provisions aimed at realizing stated public policy ends, such as conservation efforts, subsidies for development, or to create new community jobs. If introducing competitive options negates the likelihood of realizing a desired end, pursuing service delivery alternatives may not be an option for the government. In cases where the implementation of a privatized service conflicts or impedes a public policy issue, governments need to find means for responding to and overcoming such conflict.

An effective transition period builds in considerations regarding public policy goals and recognizes the resulting conflicts that exist between stated goals and new, alternative service delivery options. Possible responses include building stipulations into the service contract to maintain the public policy initiative, separating the goals from the service delivery alternative, and implementing new methods for effectively realizing a government's stated goals. Moreover, the competitive option effort may actually be a means for producing the desired ends. Governments can insert contractual requirements, include subsidies to increase competition, and add evaluation criteria that considers minority-owned contractors or contractors that include equity in hiring standards.
What type of communication process should be used with the governing body?

Any legislative body whose constituents will be affected by a change in mode of service delivery should be kept completely informed of the competitive process. This should be done regardless of the governing body’s ability to vote on the matter itself. In many instances, a city council will have a vote on either the process itself or the contractual arrangement that is the end result of the process. Legislative bodies tend to be quite wary of voting on arrangements for which they have been provided limited information.

It is a political reality that forces opposed to competitive options will try to slow down or stop the process by lobbying members of the municipal legislative body. When the legislative body is not updated regularly, stories of corruption and illegality that are generally nothing more than innuendo can easily gain credence. When undertaking a comprehensive service delivery evaluation strategy, it is good practice to provide the legislative body with updated cost studies, performance measurements, and service effectiveness reports as they are released. It is a better strategy to solicit the opinions of the body and to request that a member of the body take part in any committees that are empanelled to examine service delivery.
What type of communication process should be used with the media?

Because competitive options constitute a major change in service delivery, it remains a controversial subject. News organizations can be counted on to take an interest in controversial matters, especially when they apply to governments. Any attempt to privatize services should be left completely open to the local media. Although the media itself will determine whether an initiative is newsworthy, open communications from the onset will help dispel rumors of favoritism and corruption in the process.

Communications with the media should begin early in the process before any formal procedures are undertaken. The government, through its public information or press relations bureau, should provide local media outlets with news of any formal program analyses, including cost studies and effectiveness measurements. The media should be given access to management employees or outside consultants involved with the program analysis. Any complaints of poor or inefficient service will probably have already reached the news media. The effect of any service analysis will be intensified if service problems have already been publicized. If the news media are made aware of the analysis and results are reported to the public, the competitive process is sure to receive increased taxpayer support.
What type of communication process should be used with labor unions?

In cases where competitive options will affect a labor union responsible for the employees that provide the service, communication should be established early in the process. The communication should start with providing the affected union with the detailed financial and operational reasons for the competitive effort. Appropriate labor relations employees should be brought into the process to provide guidance concerning the collective bargaining agreement in effect and what restrictions it places on alternative service delivery options. The government’s labor representatives should be aware of any notification requirements concerning competitive options that are present in the agreement. Failure of a government to be completely aware of its contractual responsibilities to the labor involved in a competitive effort can lead to both embarrassing and disastrous consequences as the process proceeds.

Many times employee groups and labor representatives stridently oppose competitive options. After all, regardless of employee safety net programs designed and offered by the government, alternative service delivery has an overall diminishing effect on government employment. Even in cases where the alternative service provider is unionized, there is usually a net changeover of representative responsibility. If the sole concern of labor unions is the well being of their members, early negotiations and open communication of programs that will ease worker displacement will aid in soliciting union consent.

All service evaluation reports prepared during the competitive process and presented to the unions must be able to be independently verified. These include cost analyses, performance measurements, and service assessments. Negotiations with labor unions are frequently stalled by the appearance of conflicting numbers and dis-
puted reports. In some cases it may be cost-prohibitive to obtain independent verification of all analyses. If reports cannot be independently verified, then the assumptions they contain and the evaluation methods used should be clearly stated and made available to union representation.

In 1996, Allegheny County in Pennsylvania attempted to privatize two golf courses that had been under government control for over fifty years. Although the initiative presented several economic advantages to the government, including a significant capital investment into the improvement of the infrastructure of the courses, the privatization effort became bogged down in disagreements over cost comparison numbers, especially indirect costs. The rancor and distrust between factions of the government and the labor unions representing affected employees led to the initiative’s ultimate defeat. This occurred despite the government’s assurance that the privatization of the courses would have no net effect on overall union employment numbers.
What strategies can be used to manage human resource issues?

When a government service is slated for an alternative service delivery method, a concerted effort is required to assure that all human resource issues are effectively dealt with. The human resources division should be involved early in the process to begin devising strategies that will ease the concerns of affected employees. This includes detailing alternative job opportunities and programs that will be made available to affected employees, answering pension and benefit questions that will arise during the process, and keeping employees aware of developments as they occur.

The failure to manage human resource issues effectively can lead to extremely unfavorable consequences during the competitive process. A government that is perceived to be unfair in its dealings with employees can be negatively portrayed by the labor negotiation and political processes. There are several human resource strategies available to protect employees and provide a smooth transition to private-sector service delivery. These include employee retraining programs, employee reassignments, access to organization and private job banks, voluntary retirement programs, and employment access guarantees within the privatization contract. The government should utilize all of these processes to protect employee rights during any competitive options venture.
Why might employees wish to work for private entities?

In numerous cases of competitive options, governments have attempted to quell the fears of organized labor by creating right of first refusal and right to be interviewed clauses within the contractual arrangement. These clauses guarantee employees about to be displaced by the private sector the ability to remain employed with, or at the very least gain an interview with, the government contractor.

The change of service delivery from public to private is not always equivalent to lower salaries and decreased benefits. Contractual guarantees protecting the rights of government employees almost always lead to some employee changeover between the public and private sector. For a variety of reasons employees may wish to work for the private contractor; some employees may relish the challenge of a new opportunity, they may have felt constrained in their duties, or they may simply enjoy the work and wish to continue their careers.

In many private-sector organizations, excellent job performance is rewarded with career advancement. Because political favoritism and bureaucratic red tape do not constrict the private sector, some public-sector employees have a better chance at career advancement when a service is privatized.
DEVELOPING A COMPETITIVE OPTIONS STRATEGY

What are the major steps in developing a comprehensive service delivery strategy?

(1) **Inventory and assessment of service delivery responsibility.** In many instances, governments do not know the totality of services they provide. The first step to reexamining service delivery strategy is to identify and create an inventory of services, the level of service provision, and methods of delivery. The second step is to distinguish between services delivered to citizens, services that affect internal operations, and core competencies that should remain within the purview and control of the government (i.e., elections and regulatory bodies).

(2) **Determine operational efficiency of select services.** After the inventory is complete, select services should be analyzed to determine their current operational effectiveness. There are a variety of evaluation tools available to determine the state of current services, including citizen complaints and surveys, cost studies, and performance reviews. Utilizing these methods can provide the government with useful information to focus service delivery redesign efforts.

(3) **Improve the current service or consider an alternative service delivery option.** The performance of service assessments can identify minor inefficiencies or structural problems. Such assessments therefore do not always lead to the conclusion that competitive options are desirable. Often the government can make changes ranging from new policies and procedures to additional capital equip-
ment outlays that can increase service efficiency and effectiveness. It is also possible that a service without operation issues today may be one in which the private sector has significant production advantages. In either case, it is important management problems not be made the sole basis for deciding to pursue competitive options.

(4) *Determine the available service delivery options.* There are numerous ways to deliver a service. Ambulance service can be produced by government agencies, through intergovernmental agencies, through private firms, or by non-profit hospitals. A comprehensive strategy should attempt to identify the most feasible alternatives.

(5) *Continuous monitoring of service delivery.* Evaluating and determining service delivery options should be a continuous process once an overall strategy has been developed. A government must ensure that its stated service objectives are being attained regardless of whether the government or the private sector is providing the service.
What are the main steps used to evaluate a service for competitive options?

As part of a comprehensive service delivery strategy, governments need to determine if a service can be provided more efficiently and effectively by the government or the private sector. The evaluation should include the following steps:

1. **Cost analysis.** The most important step in the evaluation is the performance of a complete and thorough cost analysis of the service that may be subject to competitive options. A government cannot determine the benefits of alternative service delivery without knowing the true costs of service provision. This means that the service costs cannot simply be determined by looking at the bottom line costs of the activity in a line-item budget. A thorough cost analysis takes into account the direct costs of providing the service along with costs not borne by the entity responsible for the service. These indirect costs can include services provided by other government departments such as custodial services or fleet repair. They can also include administrative services such as data processing and payroll. Along with indirect costs there are capital costs involved with most government services. Outlays for machinery and equipment and the associated capital costs must be accounted for in any cost analysis. For true comparison purposes a government must determine which indirect costs will be lessened or eliminated by competitive options along with how capital costs will be redirected. Although the competitive process may eliminate most interdepartmental costs for a certain service, administrative and capital costs can be transferred, but not totally eliminated. A thorough cost analysis will also include:
- Total cost of ownership for a service, which helps determine if it is cost effective to perform capital investments in order to modernize and be internally competitive, or if the cost, life-cycle, and upgrade of equipment makes it cost prohibitive to be competitive with the private sector; and a

- Basic cost allocation system, which develops a method for determining the cost of the service provided to users. The system does not determine the service’s price, but what it costs to actually provide the service in order to fully capture the total cost of service delivery. This reveals direct costs, indirect costs, and overhead service costs, which once revealed, helps to reduce overhead demands, relates the interdependence of departments, and helps develop memoranda of understanding in relation to support services needed to deliver competitive services.

(2) Performance review. Cost is not the only factor that should drive the service evaluation process. How well the government entity provides service in comparison to cost should also be considered in the evaluation process. If the government is providing an effective service at a higher cost, attempts to change the service may be met with citizen contempt, political infighting, and unfavorable publicity. A well thought-out performance review process provides the government with a good measure of the current state of its service delivery capabilities.

Government performance measurement can be a highly complex undertaking that involves significant data gathering, analysis, and technical modeling capabilities, which can be beyond the reach of many local governments. Entire books have been written on the various means of judging government performance. A government should determine the complexity of its evaluation process by its own resource availability and financial position. The desired result of any study, complex or simple, should be to inform the government if it is providing satisfactory services.
In general, inputs such as miles of streets swept or tons of litter removed or outcomes such as overall street cleanliness can be used to evaluate service performance. Most government service departments have at least a rudimentary means of tracking inputs and gathering statistics. Difficulty lies in evaluating outcomes. Usually customer satisfaction surveys or complaint reviews can be used to judge specific outcomes. Statistical analyses are also available to assess some government outcomes. For example, available crime statistics are sometimes used to judge the success of various public safety service inputs such as streets patrolled and citations issued.

There is no guaranteed right or wrong way to analyze service performance. It is entirely up to the government to provide the means of analysis. In the competitive options process, it becomes more important to document the measurement approach and the procedures utilized to provide the assessment. By documenting the overall methods that it utilized to assess the service, the government will be able to defend the results during the subsequent competitive process.

(3) Industry and market analysis. To facilitate review of service suitability, governments should evaluate current market and industry forces. Such an evaluation helps determine the degree of competition, levels of competitive pricing, and number of alternate providers in the local market. Coupled with an evaluation of the level of financial strength and stability of private-sector providers, this industry and market analysis will help government assess its ability to deliver a service versus available options in the private sector. When matched against the cost analysis and performance review, governments are better positioned to begin the discussion of if and how competition could benefit public service delivery.
Who are the major stakeholders in the evaluation and implementation process?

There are several major stakeholders in the process, particularly the citizens and taxpayers who will ultimately be affected by the increased or decreased level of services, which will be the end result of competitive options. The government’s political representatives are ultimately responsible for the services that are provided by that government. Organization management, up to and including the executive-level officer, takes on great risk since the success or failure of any service delivery change will be attributed to their command. Employees will be greatly affected since the process has a direct effect on their job security. The labor unions that represent those employees face a significant loss in representative power when the employees they represent are replaced by the private sector. The service performance and the success of the process will ultimately judge the private contractors. Failure to deliver improved services will not only affect their bottom-line, but because of the controversial nature of competitive options, any perceived problems will result in negative publicity for their enterprise.
Which government agency should oversee the evaluation process?

It is always advantageous to manage the service evaluation process above the user department level. The failure to separate the procurement from the provider functions will almost always result in complaints of unfairness and favoritism. The structure of the government will determine the management of the evaluation process. Because introducing competition is usually an executive-level decision, an entity that reports directly to that executive-level, such as a city or county management office or the office of budget and finance, should be responsible for the evaluation process. These offices cannot only maintain an arms-length separation during the proceedings, they also have greater access to an all-encompassing view of the subject service. This is advantageous in both cost analysis and performance measurement.

Executive-level offices, because of their overall management responsibilities and decision-making powers, can usually compel user-level departments to provide accurate information in a timely manner. This in turn serves to keep the process moving forward instead of becoming bogged down in the pursuit of information. These offices are usually responsible for the labor management and collective bargaining issues that tend to become a major stumbling block in any competitive options process. Union negotiators like to deal with management personnel that can respond quickly to their issues without having to receive answers from a higher authority.

The executive-level offices also have the greatest access to the news media, usually through a government press relations officer or spokesperson. Since many of these initiatives prove to be newsworthy, being able to disseminate accurate information about the process becomes extremely important.
What is the role of the affected department in the process?

Although it may not be wise to allow the affected department to manage the competitive process, the role of that department will still be substantial. The affected department will have extensive knowledge of programmatic costs and outputs. It should also have the subject matter knowledge available to judge the technical merit of the proposals. Failure to acknowledge the expertise available in the user department can lead to morale problems and, in some instances, deliberate sabotage of the process.

Most competitive options experts advocate a separation between procurement and service provision. They also promote a strong role for the management and employees of the government organization that is currently responsible for the service. The department responsible for the overall management of the process has organization-wide access to information, but they usually do not have the day-to-day operational knowledge that is a by-product of service performance. The affected department should be able to provide the expertise to develop the technical requirements of the procurement process. In any procurement process, proper specification development is key to ultimate success or failure. By allowing the user department to play a role in requirement development, the specifications should be similar to the operational procedures of the current service.

In many instances, the affected department is responsible for monitoring the performance of the private-service contractor. Opinion varies widely on the merits of this decision. Many governments create a centralized office outside of the affected department to monitor contract performance. This allows for an unbiased evaluation since the centralized office does not have a stake in the operation itself. Success of this type of monitoring depends on well-documented contract performance measurements and the availability
within the contract office of thorough knowledge of the measurements. When the affected department is responsible for contract monitoring, an independent managerial presence must be responsible for evaluating performance. As stated before, technical knowledge of the service is inherent in the user department and the ability to use that knowledge to provide a fair evaluation of contract performance must also be present.
Why should union leadership be provided the opportunity to participate in the process?

Union leadership will often have great influence over the success or failure of a municipal competitive options initiative. It influences not only the collective bargaining process, but in many instances the actual political process. Since any privatization of public-sector services will greatly affect their rank-and-file, involving union leaders will demonstrate a fair process and establish a smooth transition if responsibility for the service does actually change hands. For this reason, it is often worthwhile to afford the union the ability to take part in the competitive process. As long as the process is designed in a manner that promotes fair competition, private vendors should have little concern with the input of affected labor unions.

Many unions lack the technical knowledge to respond to detailed proposals. They also lack the financial resources to contract with professional consultants to formulate their responses. Since private concerns do possess both the technical knowledge and funding ability, it is usually considered equal treatment for the government to secure consulting expertise for the affected unions.
Are there benefits in using outside expertise?

Throughout the competitive process, governments may choose to hire outside experts to help analyze, structure, and evaluate alternative service delivery options. These outside consultants can help government in a variety of ways by:

1. Performing organizational assessments to determine which services could be delivered more effectively;

2. Providing an objective basis for looking at service delivery alternatives and/or validate the findings of the government;

3. Performing operational checks to determine candidates for managed competition;

4. Helping the internal service provider to compete with the private sector;

5. Reviewing proposals from both the public and private service provider; and

6. Effectively building a wall between the private candidate, the in-house candidate, and the internal, government evaluation team.
Which services are good candidates for managed competition?

Governments often seek competitive options for services that have posed managerial problems. For example, a service where union negotiations have been especially contentious may appear to be ideal for an alternative service delivery method. The elimination of short-term management problems is one of the weaker criteria on which to base a competitive options effort. Instead, services that are good candidates for alternative service delivery and managed competition have one or more of the following characteristics:

1. Scope of the function can be clearly specified;
2. There is extensive competition in the producer marketplace;
3. Performance standards can be defined, measured, and evaluated; and
4. Costs of service are higher than private-sector benchmarks.

As a specific process within procuring competitive options, managed competition may not be suitable in all instances. Some elected officials use the “yellow pages test” when deciding whether to produce a service through government or to contract for it in the marketplace. Photocopying and printing services, for example, are readily available in the marketplace and if the same service can be obtained at a lower cost, the market alternative should be pursued. However, in considering delivery options, governments should not build service delivery considerations around proposed contractors’ options; any initiative should derive from the prevalence of a competitive marketplace for the service under consideration. A managed competition strategy—of letting the government compete against the private sector—is unlikely to be justified for “commodity” type services. Instead, managed competition is more applicable to services that...
governments may well have an edge in but their “monopoly” status has led them to lag in efficiency and/or effectiveness compared to others in the market. A managed competition initiative—where government employees and managers submit bids along side private firms—can lead to improved quality and reduced costs.
What are the major steps involved in developing a managed competition process?

A successfully implemented managed competition program requires a detailed process that supports and properly sets the stage for competition, accounts for all applicable changes, and incorporates the concerns and roles of all affected stakeholders. The steps involved are not uniform, and should be repeated for each procurement process. Moreover, based on the steps below, governments should develop unique checklists for the three general phases of managed competition: selecting competitive candidates, performing competition, and transitioning the service and managing the process. To be a viable service delivery option, managed competition should present a quality-consistent and cost-efficient alternative.

Managed Competition Steps

1. Initiating managed competition: Determining goals and establishing competition. Like any decision concerning possible changes in service delivery, initiating a managed competition solution begins by clarifying the reasons for pursuing this service delivery option. Through explaining the intended outcomes, it concludes by establishing the organizational infrastructure necessary to support, implement, and oversee the process. Typically, the overarching goal in managed competition is to demonstrate that a government recognized and pursued all feasible options for providing cost-effective, efficient, and quality-consistent service delivery options. This emphasis, and any auxiliary goals, should remain jurisdiction-specific, recognizing the unique reasons for pursuing this process and moving forward with competitive options efforts. Achieving these goals starts by creating a process for open and fair competition between private-sector service pro-
providers and in-house options. Governments may consider various alternatives to achieve a level playing field:

− Choosing to ignore the emphasis on fair competition, concentrating solely on cost and quality;

− Creating competitive neutrality insuring neither party has an advantage; or

− Developing a results-based approach where certain requirements may vary, but collectively the process produces fair competition.

A detailed communication plan articulating the goals to stakeholders accompanies this step and leads to decisions concerning the internal, organizational infrastructure assigned to manage the process and establishes goal-specific performance targets. Typically, the CEO, rather than the operating department, oversees day-to-day management. Moreover, governments may choose to incorporate oversight committees consisting of external units to monitor the process and implementation. By engaging in a practice known as uncoupling, the process of creating a firewall between the government purchaser group and the in-house service provider, governments advance the legitimacy and fairness of the process.

(2a) Identifying services for competition. After the goal-setting and management phase, step two develops a method for identifying all available services in order to determine the best mode of service delivery. In this step, each department/unit creates a detailed list of services provided, describing the structure, customers served, quantity, frequency, budgeted costs, and suitability of competitive options for the specific service. To effectively rank service delivery options, a central agency reviews these submitted service reports and initiates a preliminary assessment of managed competition suitability. This process includes evaluation and prioritization criteria specific to the government and its corresponding goals that at a minimum in-
clude: number of providers sufficient to ensure competition; ability to specify service outcomes; establishment and implementation of performance measures and ability to evaluate results; low risk of service interruption or poor performance; cost savings potential; impact on employees; and potential for improvement in service quality. It is essential that the government develop a ranking system related directly to the goals outlined in step one, set individual competitive procurement schedules for each service based on rankings, communicate the schedule broadly to all affected stakeholders and plausible providers, and periodically review and update the service inventory list.

(2b) Competitive evaluation of internal operations. After identifying services and modes of delivery, each department should evaluate the suitability of internal operations to compete with private-sector service providers. Often this evaluation process leads to conclusions that the government’s operations are clearly competitive, making the need to move forward with full competition meaningless and a wasteful exercise. Introducing a competitive process should bring an advantage to the service under consideration; if the internal option leads to the greatest benefit, it will not benefit from further competition.

(3) Preparing to compete. By establishing an inventory of services and determining a competitive procurement schedule, governments set the stage for the units involved, the “purchaser” and the “seller,” to begin the preparation process. During this stage, the team assigned to purchasing the service determines the appropriate competitive strategy, work plan, and timetable. Throughout, the government continues its diligence by notifying stakeholders, including project participants and affected employees. Internal purchasing units may be permanent or unique to each procurement, but need to include subject matter experts and individuals with experience in costing, purchasing, and the service under consideration. The purchasing
group formulates a competitive strategy based on the distinct characteristics of the service to determine the type of competitive options the government will pursue.

If the strategy calls for managed competition, this phase concludes with the establishment of an internal proposal team. The purchasing group and proposal team form two separate processes with complete confidentiality. To effectively facilitate the competitive process, the government must determine and specify the level of support available to the in-house option, including available resources, amount of time allocated for preparing a proposal and reviewing the process, and redesign considerations. The redesign process is not ad hoc; it concludes with detailed descriptions of the proposed changes and improvements, effects on staffing and work processes, changes the provider team will request from internal support services provided by other agencies within the government, and associated costs resulting from the redesign. In responding to the demands for open and fair competition, allocating adequate resources and allowing time for possible redesign increase the ability for the in-house provider to remain competitive.

(4) Conducting the procurement process. A managed competition procurement process should remain consistent with the government’s rules and regulations regarding procurement while incorporating procedures to assure competitive fairness. Such procedures include: confidentiality of all information; equal access to the same information at the same time; standard performance measures for all proposers; full disclosure and equalization of competitive advantages/disadvantages as necessary; and development of a fair cost comparison by including overhead costs in the internal proposal. Prior to the requests for proposals (RFP), the procurement team uses requests for qualifications (RFQs) to pre-qualify prospects. This helps assess the bidders’ qualifications and ability to produce the service, and check available references. RFQs also present the prospective
providers with opportunities to offer feedback regarding RFP components, such as reasonable and competitive fairness, while helping to insure that critical services remain uninterrupted. Managed competition RFPs follow typical government standards, detailing the scope of services, work to be accomplished, and the desired outputs and/or outcomes. The RFP should incorporate performance standards and indicators to assist proposers in understanding the standard of work required and facilitate the government’s development of monitoring and reporting mechanisms. Please see page 60 for a detailed description of the RFP, stakeholders involved, and description of key elements.

The procurement process concludes with an evaluation of all proposals, including an analysis of costs and all technical factors, such as the proposed service provider’s experience, track record, quality of management, and stability of service. Analyzing total costs and savings is a critical aspect of managed competition. A thorough, accurate, and well-documented process should govern this effort. When analyzing costs, governments must remain diligent to the direct costs, proposed prices, and any additional direct and indirect costs or savings a government encounters when changing the mode of service delivery. It is important to properly gauge and analyze the costs prepared by the internal provider, as this price becomes the basis for budgeting the service and cost monitoring if the government awards the in-house provider. An analysis of in-house costs considers the full cost of the internal service delivery and avoidable costs incurred. A thorough cost evaluation also accounts for the total cost of shifting to an outside service provider, including the price proposed by the private vendor, costs avoided by outsourcing, and new costs or savings associated with making the transition to a private-sector service provider.

(5) Transition, implementation, and contract administration. While technically the last step, considerations regarding the transition pe-
riod, the implementation process, and contract administration should start early in order to build related requirements into the RFP and properly estimate costs. Transition planning responds to the effects of change on all affected employees. To smooth this process, governments need to review all affected employees for changes in status (i.e., transfers, layoffs, retirement), changes in benefit status, and incorporate training and/or outplacement services. Including the HR department, payroll/labor relations office, and affected unions eases this transition period and helps identify all areas involved in employee transition. Managed competition also affects the status of assets, which may be used by, transferred, or sold to the new provider. Asset transition entails an inventory of capital assets including documentation of condition, deficiencies, needed repairs, and current value. Governments should also respond to the impact on other agencies as service delivery changes likely affect other service delivery methods, the quality of services, revenues, expenditures, and budgets.

Contract administration essentially starts by assigning accountability, day-to-day monitoring, financial management, and performance reporting responsibilities to an assigned individual or team. Contract administration begins in the RFP stage and continues throughout contract negotiations. Initial efforts consist of establishing monitoring standards, techniques, and schedules consistent with contract terms; clarifying expectations; and introducing systems for educating the service provider and stakeholders on expectations. The group or individual responsible for contract administration develops and utilizes appropriate feedback mechanisms to report on customer satisfaction, fulfill all reporting requirements, and supply regular contract performance reports to the government and affected stakeholders. The contract should specify the service producer’s reporting requirements and appropriate access rights to records consistent with the RFP, the contract, and applicable laws; introduce accountability measures by function for report-
ing, records maintenance, and project management; enact regular reporting schedules; and institute a public access system for records.
Who are the main government staff involved in the contracting process?

There are four distinct governmental roles in the contracting process: specification development, procurement, legal analysis, and contract management. Depending on the organization, these roles may be performed by one department, four separate departments, or a combination of departments. In general, the department that is responsible for providing the service in question should have some, if not all the responsibility for specification development. Since it has provided and may continue to provide some form of the service, it should be able to provide the performance variables, characteristics, and measurements that any prospective vendor will need to develop an effective and knowledgeable service delivery proposal.

The government purchasing office usually handles the actual procurement of an alternative service delivery method. Purchasing officials may also be intimately involved in specification development, but since they usually have vast knowledge of the government procurement policies and procedures, the job of assuring that those policies and procedures are followed is their responsibility.

A number of departments should take part in the negotiation process, including the legal department, purchasing, budget, and the department responsible for project management. All of these departments possess specific knowledge and expertise that help protect the government from entering into contracts that are overly beneficial to the private-sector contractor.

Finally, the government has to determine the department that will be responsible for contract monitoring. The citizens are protected in any competitive options process when adequate and knowledgeable staff is assigned to make sure that the services that are paid for are delivered properly and according to the contract specifica-
tions. The contract monitoring duties are usually assigned to employees of a formal contract management office or to the user department. In many instances, government controller or auditor personnel may also monitor contract performance.
THE RFP PROCESS AND COST ANALYSIS

What is an RFP?

A request for proposals (RFP) is a competitive negotiated bid process that applies several evaluation criteria to a procurement in addition to overall cost. The criteria may include technical factors, such as the ability to perform and prior experience, and responsibility factors, such as company financial status and financial capacity to perform. Because cost is only one variable in the overall evaluation process, an RFP is more flexible than a government formal lowest bid process, which usually awards the contract to the lowest responsible bidder.

An RFP is similar to the more formal bid process in that prospective vendors must respond to detailed specifications. The specifications, along with other criteria, are usually rated using a pre-defined scoring system that includes a score per criteria along with a relevant weighting factor for each criterion. Usually an evaluation team consisting of managers and other employees that possess considerable knowledge of the subject function are assigned the task of rating the proposals.

The RFP evaluation process is usually a phased process in which vendors are eliminated by specific factors at key evaluation points. This is generally referred to as shortlisting and gives the government the ability to further scrutinize proposals considered to be competitive after being judged against the designed criteria. Those vendors whose proposals are considered competitive after preliminary evaluation are usually asked to further clarify cost and other issues. This flexibility in the process allows the government to negotiate the best overall deal for the subject offering.
Which agency should manage the RFP?

Since government structures vary, determining which agency manages an RFP process can change from project to project. Because the use of competitive options has become so common, many governments have formalized offices to oversee RFPs that change the nature of service delivery. In many cases, they may be housed within the government’s purchasing, legal, or budget divisions, but in others they may report directly to the executive level of the local government.

It is almost always advantageous to separate procurement from provision and for this reason the department affected by the change of service delivery should be utilized for technical needs and specification development, but not to oversee the entire RFP process.
Is a consultant needed to develop the RFP?

The need for consultants in the RFP process is dependent upon the level of expertise available within the organization. This can mean both legal expertise and familiarity and experience with the service or operation being procured. In numerous instances the organization developing an RFP may be seeking a potential replacement for in-house provision of the service. In that case, it is quite possible that the expertise for developing the RFP exists in the department currently responsible for the service. It is also possible that the requisite knowledge is available from the organization’s purchasing specialists. It is important to remember that operational experience is not always equivalent to technical knowledge when it comes to designing procurement specifications. The procuring organization needs to determine on a case-by-case basis if the technical knowledge is available in either the user department or the purchasing office.

For some service procurements which are lacking in technical complexity—such as pest control, custodial, and landscaping services—there is a wealth of information available both in-house and on the open market to aid in the development of fairly detailed RFP specifications. The user department or purchasing agent without the help of outside consultants can usually develop specifications for these types of procurements.

Quite a few RFPs are utilized to obtain highly technical and complex services such as engineering design and data processing management. Many governments do not possess the level of expertise and technical knowledge to write specifications for these highly detailed disciplines. There is usually an abundance of consulting firms that possess this type of technical expertise and have vast experience available in the preparation of documents for complex procurements. It is preferable for the government to utilize out-
side expertise as opposed to taking the chance of formulating flawed specifications.

It should always be remembered that the use of consultants for development of specifications for any procurement does not relinquish government from management of the entire procurement process. A contract manager from within the organization will need to provide oversight of the process and act as a quality control agent. This can mean everything from signing off on deliverable documents to authorizing payment for services rendered. The legal authority and restrictions of the government must also be upheld and followed. This is usually the responsibility of the government’s legal personnel. The evaluation of proposals and award of contracts is always the governing body’s responsibility. Management personnel or their designees should carry out these functions.
What are the major elements of an RFP?

Although the actual structure of an RFP may be dictated by the complexity of the service or function being procured, any RFP should contain the following basic elements:

- **Introduction.** An introductory section detailing a high-level summary of the project scope and the background and history of the service or function that is being procured.

- **General conditions.** This section usually details the housekeeping functions of the process such as scheduling restrictions, submission requirements, formatting, required references, insurance provisions, and other terms and conditions.

- **Contract requirements.** Details the overall conditions necessary in any subsequent negotiated agreement. This section can include everything from process controls, vendor performance issues, warranty claims and acceptance, and payment signoff requirements.

- **Technical requirements.** These are the detailed specifications to which the contractor will have to conform. Performance criteria and the actual description of the service to be provided should be completely stipulated within this section.

- **Evaluation methods.** A description of the actual rating methods of the subject procurement. This includes the criteria on which the proposal will be evaluated, and an explanation of the actual evaluation process.

- **Legal appendix.** This section should contain documents such as required insurance, right-to-work papers, disadvantaged business forms, and other legal prerequisite papers that will need to be included with the proposals.
How specific should the RFP be?

Drafting specifications for any proposal for service delivery is not an easy proposition. On the one hand, it is imperative that the technical specifics are precisely detailed. If there is no specific detail, the proposal evaluation process becomes confused and monitoring performance after contract award will be extremely difficult. On the other hand, overly specific proposal standards tend to limit competition and can be construed as being favorable to larger vendors.

In general, an RFP should concentrate on the outcomes that an alternative service procurement seeks. Utilizing this type of approach frees the interested parties to utilize their best business practices to pursue innovative and cost-effective solutions. Mandating how the private sector should do the job tends to repress creativity and lead to the same inefficiencies that are inherent in the public-sector operation.

When soliciting proposals for solid waste services, the specified outcome may be removal of refuse and recyclables from each residence once a week. This allows the vendors the ability to use their industry knowledge to propose an efficient means of providing the service. Narrowing the specifications to include the routes and equipment a contractor must use to provide the service tends to strap the contractor with the same inefficiencies of the public sector. The government may have to set some restrictions on the contractor such as hours of operation, but it still gives the contractor procedural latitude.

This is not to say that the contractor can be allowed to operate indiscriminately without some government restraint. A government that needs a bridge designed should not be expected to solicit proposals with the specification of a designed bridge and nothing else. Obviously there are significant standards and codes to which the contractor must adhere. Public safety will always overshadow the contractor’s ease of operation.
How long should vendors be given to respond to the RFP?

The proposal’s technical complexity will sometimes be a factor in the response time afforded to prospective vendors. However, four to six weeks seems to be a reasonable guideline that can be followed in affixing a response time to most RFPs. Assigning a shorter time period will often limit the number and quality of the responses because some vendors may be limited in the number of staff available to process and create proposal responses. A response time longer than six weeks will obviously elongate the process and may add to the complexity of the responses received. The government’s legal and purchasing divisions should be able to establish if there are any statutory regulations involved with timeframes for proposal responses.
What are the major proposal evaluation criteria?

Although proposal evaluation criteria can change depending on the service or activity proposed for competitive options, several criteria are relatively common for evaluation purposes. These include the overall quality of the proposal, contractor qualifications and experience, technical merit of the proposal, financial stability of the proposer, and the responsiveness of the proposal to the instructions and conditions of the RFP. Often the basis for a fair evaluation relies on a weighting system that uses the importance attached to each criterion by the officials responsible for the procurement.

It is important to understand that the evaluation of proposals is subjective. Government employees that are chosen to evaluate proposal criteria should have explicit knowledge of the service or function that is being procured. It is advantageous to document and clarify the evaluation criteria in a formal plan so that the evaluation team has specific guidelines available to judge the proposals.
What are the major cost factors?

There are several cost factors involved with a competitive procurement. A government should identify the following cost factors to analyze the true costs of competitive options:

- **Procurement costs.** There are transaction costs involved with a competitive procurement. These include the costs of specification design, whether the design is done in-house by the service or purchasing department or contracted to an outside consultant. There are also the legal costs of the bid process itself, including advertisement and contract negotiation.

- **Technical proposal costs.** This is the negotiated final cost of the contract for the service being privatized.

- **Contract monitoring costs.** After an agreement is formalized, the government is responsible for contract management and the costs associated with monitoring should be calculated.

- **Alternative employment costs.** Most governments provide several programs to employees that are displaced by competitive options. The costs involved with these human resource strategies that need to be assessed. A government that guarantees no layoffs may have to create additional positions to accommodate displaced employees. Early retirement and job retraining programs result in additional costs to the government and should be added to the total cost of a competitive options initiative.

- **Unavoidable costs.** Even if the competitive process leads to a private-sector provider, there are certain unavoidable costs that governments incur by introducing managed competition. These remaining overhead costs are the costs previously allocated to the operating business unit, but now dispersed to other cost centers due to competitive options. Examples include salaries of executive management, audit costs, accounts payable, insurance and lia-
bility, legal, pension obligation bonds, and oversight costs. This is not an exhaustive list and governments that choose alternative service delivery methods need to inventory the full range of unavoidable costs and where/how these costs are transferred.
How should costs be analyzed?

Analyzing the costs of alternative service delivery initiatives is highly dependent on the government’s budgetary structure. Assessing service costs from a traditional departmental line-item budget is difficult because many costs are tracked across divisions rather than being tracked to the specific activity or function under consideration for competitive options. In large and medium public works budgets, costs are sometimes assigned by the organization’s geographical breakdown and not by the specific activities that they undertake. Several public works activities can be competitively bid: pothole patching, roadside vegetation control, and snow removal, for example. But tracking costs at the cost center level does not facilitate cost comparison by specific activity. Many governments utilize activity based costing or outcome budgeting to provide a more functional cost assessment.

Activity based costing is an analysis tool that allows governments to calculate the specific costs of the services they provide. Direct departmental spending for wage and salary, equipment, supplies, and materials are allocated to the specific outputs of departmental activity. Some governments utilize sophisticated information systems such as materials management systems and labor tracking systems to track costs to specific activities. Governments that do not have access to these types of systems may require paper-based tracking to show how materials are used and what activities employees undertake. Other governments allocate these costs by predetermined percentages. No matter which type of tracking system is utilized, there is some dependence on government employees to provide accurate costs. The end product of each should be an accounting of the cost per specific output, such as the average cost of a filled pothole. Once the government has arrived at a reliable cost figure for public service provision, a cost comparison can be made against the public service alternative. To provide a true comparison the cost factors of the competitive option process must be analyzed.
Procurement costs and contract monitoring costs are public service costs and can usually be analyzed in much the same way as activity costs. The department responsible for the various programs needs to provide alternative employment costs; a combination of pension administrators and budget officials should develop early retirement costs; and budget officials should determine the costs of added positions. Other safety net programs such as retraining should be available from the human resource employees responsible for the design of the programs.

The technical procurement costs are the actual prices in the contractor proposal. There are several costing mechanisms that governments specify when requesting proposals. These include fixed price, fixed price with escalator, and time and materials contract pricing. Fixed fee simply means that the contractor proposes to provide the service for either a fixed total cost or a fixed unit of service cost. Fixed fee with escalator is the same, but specifies negotiated price increases at specified intervals. Time and materials pricing is usually utilized for building and repair services and allows for set pricing for labor and materials used.

A prudent analysis of costs also factors in the potential for savings. By pursuing competitive options, what costs are eliminated, increased, or transferred to new units within the government? What is the difference between the total cost of the service and the actual, total amount saved if the service is terminated from the government ledgers and completely contracted out? Including factors such as employee restructuring, re-hires, retirement, and training costs leads to a more complete and accurate picture of total costs, costs added or subtracted, and additional costs and/or savings from contracting out a service.

The end result of the above analyses should be firm costs that can provide a fair comparison between public and private service delivery.
Should indirect costs be examined?

In order to have a fair alternative service delivery process, the indirect costs (those costs not borne directly by the service-providing department) should be part of any evaluation that seeks to provide a fair and open competition. Since indirect costing is an inexact discipline and not all governments have the sophisticated financial management tools at their disposal to completely equate these costs, there are several ways in which they can be used in the analysis.

Many governments that lack the sophisticated accounting capabilities to track indirect costs utilize statistical percentage models to establish indirect cost figures. The statistical multipliers are usually obtained from indirect costing studies performed by the budget office or, in some cases, by consulting firms. The figures obtained by using these multipliers are usually adequate for government financial reporting or overall departmental performance reviews. In the context of competitive procurements, indirect costs derived from across-the-board modeling may not provide a figure equitable to judge in-house performance against that of private competitors.

Numerous indirect costs need to be assigned to specific government services. These include interdepartmental service costs such as fleet management or building maintenance. The service department usually provides these costs by means of work order costing. Utility and space allocation are also indirect costs that need to be assessed to user departments. These are usually allocated by space measurements, such as the square footage percentage assigned to a user department. Administrative costs such as payroll processing and purchasing are also costs of doing business. These are usually allocated by usage statistics, such as number of employees or requisitions processed.

Many governmental activities are heavily dependent upon access to capital equipment (e.g., vehicles, heavy equipment, computers, etc). The
cost of the capital used to purchase equipment should be a part of any service cost analysis. These figures are usually available from budgetary personnel and should be included in any service cost analysis.
In any procurement of private-sector services, the proposing vendors will include certain assumptions concerning the government and the service in both the proposal and the contract. These assumptions are usually general issues that the vendor would like to clarify before signing an agreement. The assumptions will then become part of the contract and if they are not upheld or attained during service performance they may become grounds for either contract severance or litigation for damages. For this reason, it is imperative that the government study these assumptions in detail for their impact on overall cost and effect on service delivery.

In many procurements of complex specialized services, such as computer software implementations and infrastructure engineering design, the vendor will assume a certain amount of government staff participation. This participation may be significant and can include everything from testing and modeling to aiding in the project design. Any government participation affects overall project cost and may also affect the government’s ability to function. The government should take into account the salary and benefit costs of any employees needed for the contracted service, along with any residual replacement costs for the employees needed to attain the vendor assumption.

The vendor may also have assumptions concerning the payment structure (i.e., fixed fee, time and materials, incentive based, etc). It is imperative that the government assess the various assumptions regarding payment structure to arrive at the method that presents them with the most value. Other cost assumptions may need to be
analyzed, including, most importantly, the amount of capital investment the vendor assumes it will have to make. In capital intensive services such as garbage removal or street maintenance, the vendor may assume that the government will have equipment available along with capital needed for replacement or repair. All of these assumptions represent either cost or value to the government. If the vendor assumes that the government will provide all equipment, then the overall cost of the service rises by the associated bond fund costs of that equipment. On the other hand, if the vendor assumes that it will be responsible for equipment and other capital costs, the overall value of the service package should increase by the cost of capital investment.
Should vendors be allowed to change their bid during the contracting process?

Governments should always strive for consistency throughout the procurement process. A vendor pre-proposal conference held between the release of the RFP and the deadline date for proposal submission affords vendors the opportunity to question the RFP, the scope of services, and the procurement process itself. Vendors may also be allowed to correct non-material errors or omissions in their proposals for a short period of time following the actual submissions.

Situations arise that may call for resubmission of certain facets of a proposal. Either a mistake in wording or a change in the actual scope of the service may necessitate the need for updated proposals. As long as all vendors are afforded an equal opportunity to update their proposals, these changes can be made. However, the changes should always be requested in advance from the vendors. Vendors should never be able to make unsolicited changes after the proposal deadline date.

In the case of pricing, updated cost submissions may be solicited throughout the procurement process. The procuring government can continue to ask for new cost proposals usually up until the point where it solicits a best and final offer.
How would this process work under a managed competition strategy?

The use of managed competition (the ability for the public sector to compete with private enterprise for government service contracts) has steadily increased throughout the 1990s. As in any competitive procedure, an appearance of fairness must be upheld in managed competition to ensure that an adequate pool of private-sector vendors stay committed to the process. When vendors sense that the process is being slanted to the public-sector entity, their only recourse is to object to the process or withdraw from the competition completely. Vendor objections to the process lead to costly legal procedures and court defenses. Vendor non-participation lessens competition, which invariably leads to higher service costs and inadequate service delivery.

To provide a level playing field between public and private service delivery, procedures must be established and followed throughout the competitive process. A fair cost analysis as described earlier should be performed and equitable performance measurements and service standards need to be instituted for both the public and private sector. There is a vast difference between the methods of cost accounting for service delivery that are utilized by the public and private sectors. An independent and equitable comparison process that sets standards for overhead calculations, capital accounting, and service assessment needs to be established in any managed competition. Once these standards have been developed, the managed competition strategy can be initiated.

There are a number of different approaches to a managed competition strategy. Governments may use an ad-hoc approach where in-house costs are informally compared to service costs of similar private-sector vendors. These comparisons can then be used as standards for improvement of the in-house department or as a means
to enter into a more formal competitive options process. The City of Lake Forest, Illinois, has used this approach by utilizing an independent committee to compare the costs of in-house delivery of solid waste services against those of an outside service contractor in a comparable neighboring government. In the case of solid waste, the government found out that its in-house costs were significantly lower than those of the private sector. The cost comparison process was successful enough to warrant its use on other government services.

Governments may also choose to utilize informal bidding as a managed competition strategy. This strategy involves comparing the costs of in-house service provision against firm fixed costs of formal bids received from private vendors. In many cases, the comparison itself leads to increased efficiency within the government department that is competing for the service. It can also lead to acceptance of the formal bids that provide a more valuable service to the government. Allegheny County in Pennsylvania adopted this strategy in 1996 as a means of comparing numerous in-house service costs to those of the private sector. Although only one service (fleet management) was ultimately privatized, the established benchmarks led to increased efficiency and reduced costs in many other service delivery areas.

Formal bidding can also be utilized as a managed competition strategy. Under formal bidding, the in-house department is required to follow the same procedures as private-sector vendors. It must submit formal bids that include the full costs of service delivery. Many governments utilize outside auditors to ensure that the costs submitted by the in-house department are valid. If the in-house department ultimately prevails in the competition, it is held to its submitted cost proposal and penalized for any cost overruns. A formal bidding, managed competition strategy has been utilized with much success in governments such as the City of Phoenix, Arizona, for solid waste services; the State of Massachusetts for various road maintenance and improvement projects; and the City of Indianapolis, Indiana, for numerous service delivery functions.
Managed competition is a strategy that continues to expand throughout the various levels of government. It has been proven over and over that the strategy can work if all sides follow the same rules and are held to the same performance requirements.
What is the optimal duration of the contract?

Governments may procure contracts for numerous service activities, some simple in nature, while others are extremely complex. Because of the diverse nature of government service delivery, it is hard to determine the optimal length for all governmental contracts. However, including considerations designed to maintain and continue the reasons for competition helps determine the ultimate length of a service delivery contract. There are usually statutory issues involved with acceptable contract lengths and in some areas, the use of long-term contracts may be expressly forbidden. Government purchasing or legal officials should have first-hand knowledge of legalities concerning contract length.

In any service procurement it is beneficial to the government to place minimal restrictions on the private sector and allow it to utilize its ability to propose innovation. Short-term contracts do not always allow for innovative and cost-conscious proposals. Many times vendors may not have access to capital equipment necessary to provide the service. If there is a need for capital outlay by the vendor, a short-term contract tends to restrict competition and drive up costs. Competition is restricted because not all vendors have expensive capital equipment at their disposal and they are not able to risk expensive borrowing without a long-term agreement. Costs are driven higher because vendors have a shorter period to repay capital loans and must set their prices accordingly.

It is sometimes reasonable for governments to enter into shorter-term contracts that contain extension or reauthorization clauses. In these cases, governments agree to revisit the contract at certain periods and extend on the agreement of both parties. These types of contracts may also contain specific performance thresholds or available appropriation criteria. Thus, vendors have some guarantee that the agreement will be ex-
tended if their performance is satisfactory and the government intends to continue funding the service.
What is the objective of the contracting process?

The main objective of the contracting process should always be to provide the citizens with the fairest price for the most effective service. Maintaining a fair and open competition among as many qualified vendors as possible almost always ensures that the main objective will be met. Because the government retains management control in the contract process, there are several measures that can be undertaken to ensure that the objective is met.

The contracting process should guard against creating a private monopoly by way of the competitive process. Lack of competition may serve to eliminate a public monopoly and replace it with a private monopoly. The main objective of the contracting process is to foster competition. Before entering into it, the government needs to determine if there are enough vendors available to guarantee competitive bidding. Determining available competition can be as simple as searching through the local yellow pages or trade journals. The purchasing office may be able to produce a representative sampling of available competition.
What are the major elements of the contracting process?

There are several steps in the contracting process, starting with determining a clear purpose for the contract and the exact services that will need to be performed. The contract should spell out the exact services that citizens are to receive, along with the results that the contract should produce. It should also spell out activities that a contractor must assume to produce the desired results. The government must also decide the most effective means of producing an equitable contract, determined between the bid process and the RFP approach. Along with determining the process, the government should specify the type of pricing that the contractors will need to propose.

When all the purchasing issues have been determined, the procurement element of the process begins. This includes vendor clarifications, evaluation of proposals, and contract negotiation. It is important to maintain a fair contracting process. Prospective vendors should have equal access to all procurement information. They should also have a clear knowledge of how proposal submissions will be evaluated. Those vendors eliminated during evaluations should have access to the evaluation results. This will not only make them aware of their deficiencies, it will foster competition for future procurements. Once vendors have been elevated for negotiations, it becomes the responsibility of government officials to obtain the most favorable terms and conditions. Negotiations should also result in a formal statement of work that clearly defines the contractor’s responsibilities. Once a formal agreement has been reached, the contract should be formalized and brought before the governmental legislative authority.

The final element of the contracting process is contract management. The government contract officer will need to monitor the contractor to affirm that the contractor adheres to the scope of
work formalized in the negotiated statement of work. The contractor should also be monitored for adherence to specifications and performance measurement requirements. Non-performance should be recognized early and brought to the contractor’s attention.

This process also holds true to government units that won the right to provide city services through the competitive process. While largely symbolic, requiring the internal service provider to sign a contract reflects its commitment to perform at the level of service delivery promised during procurement or at the same level a private-sector provider would be held accountable. Such contracts also provide the basis for monitoring the expectations and delivery of a service and create the basis for performance standards and monitoring principles, which helps ensure the process remain open, fair, and ultimately competitive.
What is a parallel negotiation strategy?

A parallel negotiation strategy is based on the principle that maintaining competition throughout the contract negotiation process should result in the best deal for the government. An effective negotiation strategy should fulfill the following objectives:

(1) Mutual agreement between the government and the vendor on what services are being purchased and how those services will be delivered;

(2) Negotiating the most effective services for the lowest price;

(3) Developing service agreements that clearly define the long-term relationship between the government and the vendor; and

(4) Selecting a single vendor that provides the most cost-effective services to the government.

Under parallel negotiations, the criteria developed during the RFP process to grade the various proposals are evaluated to elevate two viable vendors. Because vendors make a significant investment in the process, the government should only elevate those vendors that provide a truly feasible service delivery option. When the government has identified two viable vendor options, a short period of time should be set aside for each vendor to settle any remaining questions they may have regarding the subject service. These “discovery sessions” should provide a basis for refining scope of services and cost proposals and aid in the development of a statement of work.

Once the scope of services has been clarified, the government should begin the negotiation process with the most suitable vendor while maintaining the second vendor as a viable option. It is imperative that the government maintains a good
faith relationship with both vendors remaining in the competition. There are costs involved in any negotiation strategy and merely using an alternate vendor solely as a bargaining chip is not advisable. It should be made clear from the onset that the second vendor is an option only after clearly defined negotiation points have not been attained. This will make it clear to the vendor of choice that negotiations will not be terminated in an arbitrary and capricious manner. This will also assure that a fair but competitive process is maintained up until a contract agreement is reached.
What is a statement of work and how should it be developed?

A statement of work (SOW) is a document developed during contract negotiations to specify the roles and responsibilities of both the government and the vendor. The SOW should clearly spell out what services are to be performed and how they are to be delivered. The SOW should include the specific technical criteria for which the vendor is responsible and how the criteria will be evaluated. The SOW should also define specific maintenance and support plans for the service and provide the final cost and pricing mechanisms that the vendor is to utilize.

A functional SOW describes the work in terms of what is to be performed without constraining the contractor in how the work is to be performed. It contains quantifiable performance measurements such as quantity, quality, and timely service delivery. Because the SOW contains measurable performance and management plans, it becomes an important document for contract management. The government should develop its contract surveillance plans taking into consideration the performance requirements of the SOW.

Careful consideration of the defined SOW is a prerequisite of effective contract negotiations. Questions of what services are to be delivered, where, when, and how those services are to be delivered should all be jointly agreed upon before a final contract is established. These should all be developed in conjunction with the price and value considerations that are the prime factors of contract negotiations. The government’s key motivation during contract negotiations is to receive the most cost-effective service delivery option. A mutually agreed-upon SOW that mandates vendor performance and defines the corresponding costs is a valuable means of protecting the public interest. Because the SOW defines the scope of the contractor’s performance, it is frequently attached as an appendix to the overall service agreement.
Should performance criteria be put into the contract? How should these be developed?

Performance criteria that can be easily monitored are an absolute necessity in most government service contracts. After a contract has been awarded, the government has only delegated provision of the service, not management responsibility. Without fair but specific performance standards there is no basis for determining if the contractor is satisfying the contract terms.

It is important to begin developing performance standards early in the service strategy process and to continue to refine them throughout development of the procurement RFP. Part of the comprehensive strategy is to evaluate the performance of the service as it is provided by the government. Those same performance measurements can be used as a starting point for developing standards to be adopted into the contract document. Holding outside contractors to the same performance standards by which the in-house service has been judged is a way to guarantee fairness in the overall process.

A number of different performance measurements are available to the contracting government. Citizen satisfaction is a key determinant in how an outside vendor is performing. The government can adopt satisfaction survey measurements or complaint tracking mechanisms as means of monitoring vendor performance. The government can also develop service delivery schedules with which the private vendor must be in compliance. The contract management team can then monitor the service to ensure that the vendor is adhering to the required schedules. The government can also build output and outcome measurements into the service delivery contract. A street-cleaning contract, for example, may mandate a certain amount of streets per day as an output while monitoring the overall cleanliness of the streets as a specific outcome of service delivery.
Regardless of which performance standards a government chooses to utilize, the standards should always be measurable and specific. A plan for monitoring those standards should also be developed and should include the vendor’s reporting requirements, a service-assessment meeting schedule, complaint procedures, and the government’s access rights to vendor records.
APPENDIX A

Bibliography


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