

COUNTY OF MILWAUKEE
Inter-Office Communication

Date: May 12, 2004

To: Supervisor Lee Holloway, Chairman, Milwaukee County Board of Supervisors

From: Julie Esch, Research Analyst, County Board Staff
Jerome J. Heer, Director of Audits

Subject: Privatization of Milwaukee County Facilities and Programs (File No. 03-474)

BACKGROUND

On October 30, 2003, the County Board adopted a resolution (File Number 03-474) calling for a report on possible privatization of County facilities and programs. The report was to be prepared by the Department of Audit and County Board Staff with the cooperation of the Department of Administrative Services Fiscal Affairs Division and the Department of Parks, Recreation and Culture (now the Parks Division of the Department of Parks and Public Infrastructure). The resolution highlighted several facilities and programs within the Department of Parks that had been identified as potential candidates for privatization. Further, the resolution called for information regarding the various forms of privatization, advantages and disadvantages of privatizing programs, and revenue and expense information incorporated in privatization decision making.

Several specific Parks operations were designated to be a part of the review. These include: Wehr Nature Center, Mitchell Domes, Boerner Botanical Gardens, Greenhouse Operations, McKinley Marina, Wilson Ice Center, Swimming Pools and Park Maintenance. Golf and concessions operations are two other key activities within the Parks system included in our review.

Discussion on the resolution also indicated an interest in broader information on privatization initiatives beyond the specified Parks items.

DEFINITION OF PRIVATIZATION

Privatization is a process that transfers services, which had previously been performed by the government, to the private sector. The private sector entity can be either a for-profit or a not-for-profit entity. The purpose of privatization is to provide services at a better value to the taxpayers. In many cases, the availability of privatization opportunities may focus on "commercial activities." This is sometimes referred to as a "yellow pages test" in recognition of the fact that the services are commonly available from private businesses. These are activities that the government performs with its employees or resources that could also be performed by the private sector. Examples

of government operations that are often cited as commercial activities include printing, golf, payroll processing and vehicle maintenance. Other types of services may be classified as “inherently governmental.” These are activities that are so clearly and directly related to a public interest without regard to profitability that they are best performed by the government. These may also have a statutory requirement for the provision of the identified service. Examples include law enforcement, corrections, stewardship of natural resources, fire fighting, and judicial functions.

TYPES OF PRIVATIZATION

The following terms describe various types of privatization models. In some cases these definitions are not mutually exclusive.

Asset Sale

An asset sale is the transfer of ownership of a government’s asset, commercial-type enterprises or functions to the private sector. In general, the government has no role in the financial support, management, or oversight of a sold asset. The outright sale of public assets to the private sector can produce a one-time financial windfall to the government in lieu of a former annual income stream or deficit. It may also return the property to the local tax roles, which is a positive outcome.

If the format is a sale-leaseback arrangement, the government sells the asset to a private sector entity and enters a long-term lease for the asset.

Another type of asset sale is an employee buyout. Existing managers and employees of a public unit create a private entity. This is more common in the private sector.

Divestiture

A divestiture involves the sale of government owned assets or commercial type functions or enterprises. After divestiture, the government generally has no role in the financial support, management, regulation or oversight of the divested activity. This is a type of privatization similar to asset sale, but more directly involves discontinuation of a service or program.

Service Shedding

This is a type of divestiture in which the government reduces or terminates the provision of a service altogether. Private-sector for-profit or non-profit organizations may then step in to provide the service if there is a market demand. The government has little or no control over the service or price. The consumer market determines the vendor selection and any fees to be paid.

Subsidization

The government provides a cash or in-kind contribution to a private organization or individual to encourage it to provide a service so that the government does not have to provide the service.

Vouchers

The government provides vouchers to citizens needing the goods or service, but the citizens are free to choose the organization from which to buy the goods and services. The government's financial obligation to the recipient and the vendor is limited to the amount of the voucher.

Outsourcing

This is a general concept in which the government entity remains fully responsible for the provision of affected services and maintains control over policy decisions, while a private entity operates the function or performs the services. This approach includes contracting out, the granting of franchises to private firms, and the use of volunteers to deliver public services.

Contracting

The most common form of privatization is the provision of public services through contracts with private sector firms (contracting out). The government hires private sector for-profit or non-profit organizations to provide goods or services for the government. The government remains the financier and has ultimate control over the type and quality of goods or services to be provided.

Management Contract

A private entity operates a publicly owned facility under a contract with the sponsoring government. Concessions and franchises are to some extent subsets of this concept.

Concessions

The government grants a private firm the exclusive rights to operate, maintain and manage an enterprise for an extended period of time. The government is typically paid on a flat fee or a percentage of revenue basis.

Franchising

The government awards either an exclusive or non-exclusive right to conduct business in a particular market or geographical area. Under most franchises the citizen pays directly for the service rendered. The government may or may not regulate the service level or price, but users of the service pay the provider directly. This model is similar to concessions, but the user pays for the service directly.

Leasing

A way for government to have the use of certain private assets without having to own them. This eliminates the need for capital investment with the cost of the asset spread over the life of the asset. Leasing may also refer to the acquisition of personal services by employment agencies.

Managed Competition

A process in which a public agency competes with private sector firms for the provision of public services in a controlled or managed process.

Public – Private Partnership

A contractual arrangement is formed between public and private sector partners that can include a variety of activities that involve the private sector in the development, financing, ownership, and operation of a public facility or service. Often tax subsidization such as special improvement, incremental and special sales taxes accompany these types of ventures.

Volunteer Ventures

The provision of services is conducted through either a formal agency volunteer program or a private non-profit service organization. The activities are provided all or in part by volunteers and may be organized and directed by a government entity. This concept can also be considered a form of outsourcing.

PAST PRIVATIZATION IN MILWAUKEE COUNTY

In the past, Milwaukee County has implemented a number of privatization initiatives. The following examples provide a track record of previous County privatization efforts and also provide examples of successes and failures in these types of arrangements and relationships.

Doyne Hospital

John L. Doyne Hospital (previously Milwaukee County Medical Complex) was sold in 1995 to another health care provider located on the Regional Medical Center grounds. County expenditures were reduced by approximately \$200 million and the County workforce was reduced by about 1,500 employees. The workforce reduction coincided with an early retirement "window" that resulted in the retirement of 1,130 employees. Further, the School of Nursing was transferred to the Milwaukee School of Engineering, thus reducing the operating budget by \$1.5 million and abolishing 20 positions. The County continued to fund indigent care formerly provided at Doyne Hospital through a separate delivery model using a network of private primary care facilities and local hospitals. These privatizations can be best described as an asset sale or divestiture.

Transit

The model followed for the provision of Mass Transit within Milwaukee County involves contracting with a private sector management company to manage the day-to-day operation of the service. The County retains ownership of the assets. The service is provided by a separate entity with non-County employees. This privatization can be classified as a management contract or a service contract.

County Grounds

As Milwaukee County's presence on the County Grounds decreased, a number of support functions were shut down, including the bakery, laundry and central stores. This situation is best described as a divestiture or service shedding.

Power Plant

This facility was responsible for the provision of electricity, steam, and chilled water to various tenants located on the County Grounds. This plant was sold to the local electrical utility. After the sale, the County was no longer responsible for providing these services. This privatization can be classified as an asset sale, service shedding or divestiture.

Information Technology

Prior to the closing of Doyne Hospital, the hospital's data center was managed by a private accounting and consulting firm. Currently, the Behavioral Health Division and Department on Aging both rely heavily on private companies for technology services.

Ancillary Medical Services

Also prior to the closing of Doyne Hospital, radiology and laboratory services were shifted to a private entity, United Regional Medical Services.

House of Correction Food Service

Effective July 1, 2003 meals for inmates at the House of Correction are prepared by a private firm instead of County employees. A total of 46 food service positions were abolished as a result of this service contract. Five of the former County employees were hired by the new vendor. This arrangement is a straight-forward contracting out for services.

Milwaukee Public Museum

MPM was a County operated recreational and educational institution located in the City of Milwaukee. Previously, significant tax support was needed for the continued operation of the facility. Currently, an annual contribution is provided to the private, not-for-profit organization operating the facility. The County retains ownership of the building and artifacts. This type of privatization can be classified as both a public-private partnership and a subsidy.

Employee Retirement System

Assets of approximately \$1.4 billion are held in the County's pension fund for the provision of retirement benefits for employees. A number of private investment managers are used to manage the investment of the assets of the fund. This type of privatization can be classified as contracting out.

Construction Management

Most major County construction projects have involved the use of private construction management firms, to oversee the work of private construction companies, to ensure that projects are completed on time, on budget and as specified. This practice is best described as contracting out.

Health and Human Services and Aging Services

Each year more than \$200 million dollars is spent in the provision of services by private agencies under contract with Milwaukee County's Department of Health and Human Services and Department on Aging.

Golf Management

Milwaukee County has hired the Wisconsin Professional Golfers Association to manage a number of the County's major golf courses. This is a management contract type of privatization.

Lake Park and O'Donnell Park Restaurants

Private companies have contracts to operate restaurants at these locations. Both are operated as up-scale restaurants. The vendors provided remodeling and physical improvements. A catering company has the exclusive right to provide services in the O'Donnell Park rental space. These may be referred to as concessions/ franchise types of privatizations. O'Donnell Park also contains a parking operation and a children's museum. The museum is operated by a not-for-profit organization that leases space in the building. The parking structure is operated by the County.

County Stadium

In 1992, prior to an eventual transfer of stadium ownership to a Baseball Park District, Milwaukee County transferred County Stadium to the Milwaukee Brewers. Total

expenditures were reduced by more than \$4 million (including more than \$400,000 of tax levy) and 14 County positions were abolished.

Milwaukee County Sports Complex

The Milwaukee County Sports Complex in Franklin was designed for primary use as an indoor soccer facility. It was built through County debt financing. The Wisconsin Soccer Association (WSA) was granted the right to operate this facility with payments due to the County that were to repay the County's construction and debt service costs. Revenue generated by WSA was inadequate to make the required payments. Subsequently, the agreement with WSA was terminated and eventually another operational model involving the Milwaukee Rampage was implemented. With the dissolution of the Rampage, the property is being marketed. This type of privatization was a lease and private/public partnership.

Professional Services

County government utilizes a variety of professional services contractors. These contracted services provide specialized expertise in areas where employment of in-house resources may not be prudent or cost effective. The use of contracts also addresses peaks and valleys in workload by engaging outside resources only when they are needed. Examples include contracts for legal services, audits, accounting, lobbying, architecture, engineering, information technology and others.

Claims Processing

Automated claims processing is provided by private firms for employee health insurance, General Assistance Medical Program charges and Department on Aging Care Management Organization payments for Family Care services. These are examples of contracting out.

REVENUES AND EXPENSES OF PARKS PROGRAMS

During the deliberations on the 2004 Budget, a number of questions were raised about potential park privatization efforts. A review of revenue and expenses associated with park programs illustrates some of the fiscal considerations that arise in assessing privatization. The Parks Division has provided financial data for the specific activities addressed in the resolution. This financial information has not been audited. However, the information can be useful in providing a perspective on the financial elements of privatization decision-making.

The information for the selected activities received from the Parks Division is presented below. In addition to the areas identified in the resolution, we have added details on two other revenue generators; golf and concessions operations. It is important to note that the treatment of overhead, interest expense and depreciation varies significantly in Table 1, 2, 3 and 4. The effect of this condition on the various programs is discussed in the sections following the tables.

Table 1
2002 Revenue/Cost Data for Parks Venues

	<u>Wehr</u>	<u>Mitchell</u>	<u>Boerner</u>	<u>Greenhouse</u>	<u>Marina</u>	<u>Wilson</u>	<u>Pools</u>	<u>Golf</u>	<u>Concessions</u>
Revenue	\$66,463	\$743,560	\$151,958	\$164,646	\$2,100,409	\$353,918	\$1,322,290	\$6,982,396	\$1,561,329
Direct Cost	566,848	1,560,770	917,744	788,779	673,270	633,270	2,343,922	5,202,732	1,531,095*
Overhead					203,333			1,571,744	
Interest					516,215				
Depreciation					657,424				
Net Gain (Loss)	(\$500,385)	(\$817,210)	(\$765,786)	(\$624,133)	\$50,167	(\$279,352)	(\$1,021,632)	\$207,920	\$30,234

* Overhead for concessions is included in Direct Costs.

**Table 2
 2002 Golf Course Detail**

<u>Class</u>	<u>Name</u>	<u>Revenue</u>	<u>Labor</u>	<u>Other*</u>	<u>Overhead**</u>	<u>Total</u>	<u>Gain/(Loss)</u>
Premium	Brown Deer	\$1,161,447	\$698,962	\$408,749	\$334,639	\$1,442,350	(\$280,903)
Gold	Dretzka	594,215	324,067	174,865	150,727	649,659	(\$55,444)
	Oakwood	699,312	279,560	119,741	120,629	519,930	179,382
	Whitnall	795,990	298,788	255,616	167,486	721,890	74,100
Total Gold		\$2,089,517	\$902,415	\$550,222	\$438,842	\$1,891,479	\$198,038
Silver	Currie	\$951,515	\$328,110	\$160,362	\$147,567	\$636,039	\$315,476
	Grant	765,645	388,523	108,104	150,031	646,658	118,987
	Greenfield	787,750	276,090	133,103	123,617	532,810	254,940
	Lincoln	369,013	270,371	91,097	109,200	470,668	(\$101,655)
Total Silver		\$2,873,923	\$1,263,094	\$492,666	\$530,415	\$2,286,175	\$587,748
Bronze	Hansen	\$244,034	\$90,954	\$67,759	\$47,947	\$206,660	\$37,374
	Warnimont	289,082	154,054	40,747	58,849	253,650	35,432
Total Bronze		\$533,116	\$245,008	\$108,506	\$106,796	\$460,310	\$72,806
Oak	Dineen	\$9,324	\$45,963	\$10,362	\$17,016	\$73,341	(\$64,017)
	Doyne	56,562	94,459	39,402	40,439	174,300	(\$117,738)
	Lake	74,712	72,445	16,466	26,860	115,771	(\$41,059)
	Madison	64,937	84,223	12,269	29,150	125,642	(\$60,705)
	Noyes	33,779	48,406	15,367	19,266	83,039	(\$49,260)
	Zablocki	85,079	81,279	12,469	28,321	122,069	(\$36,990)
Total Oak		\$324,393	\$426,775	\$106,335	\$161,052	\$694,162	(\$369,769)
Grand Total		\$6,982,396	\$3,536,254	\$1,666,478	\$1,571,744	\$6,774,476	\$207,920

* Other includes commodities, cross charges, contractual services, etc.

** Excludes depreciation and restaurant operations.

Table 3
Concessions Profit/(Loss)*
By Location for 2002

<u>Location</u>	<u>Revenues</u>	<u>Total Expenditures</u>	<u>Profit/(Loss)</u>
Boerner Botanical Gardens	\$ 4,751	\$ 2,113	\$ 2,638
Bradford Beach	12,771	16,788	(4,017)
Brown Deer Golf	200,727	185,272	15,455
Conservatory (Mitchell)	8,305	5,738	2,567
Cooper	506	0	506
Currie Golf	97,795	117,838	(20,043)
Doyne Golf	6,042	1,844	4,198
Dretzka Golf	79,892	102,600	(22,708)
Grant Beach Concessions	4,005	5,537	(1,532)
Grant Golf	109,031	112,462	(3,431)
Greenfield Aquatic Center	221,222	203,725	17,497
Greenfield Golf	90,966	87,869	3,097
Grobschmidt Pool	4,980	4,343	637
Hales Corners Pool	2,214	1,883	331
Hansen Golf	30,050	20,517	9,533
Holler	596	0	596
Hoyt Pool	19,196	19,301	(105)
Kosciuszko Aquatic Center	17,819	17,777	42
Kosciuszko Center	10,149	7,465	2,684
Lake Golf	2,854	1,320	1,534
Lincoln Golf	28,200	13,400	14,800
Lincoln-Blatz	91	65	26
Madison Golf	1,843	977	866
McCarty Pool	18,386	17,213	1,173
McKinley Marina	57,846	72,497	(14,651)
Mitchell	2,873	901	1,972
North Point	43,645	50,210	(6,565)
Noyes Golf	5,360	997	4,363
Noyes Pool	2,220	3,549	(1,329)
Oak Creek Parkway	777	483	294
Oakwood Golf	119,521	117,381	2,140
Pulaski Pool	5,052	3,040	2,012
Red Arrow	48,179	59,587	(11,408)
Sheridan Pool	17,509	16,146	1,363
South Shore	1,517	787	730
Warnimont Golf	37,875	15,976	21,899
Washington	815	542	273
Wehr Nature Center	495	597	(102)
Whitnall Golf	114,084	114,547	(463)
Wilson Recreation Center	123,137	124,342	(1,205)
Zablocki Golf	8,033	3,466	4,567
Total	\$1,561,329	\$1,531,095	\$30,234

* Does not include overhead, depreciation interest.

**Table 4
 2002 Swimming Pool Detail***

<u>Location</u>	<u>Revenue</u>	<u>Direct Cost</u>	<u>Gain/(Loss)</u>
Greenfield	\$769,084	\$576,192	\$192,892
Grobschmidt**	15,912	66,982	(\$51,070)
Hales Corners	21,298	65,647	(\$44,349)
Holler	4,339	38,397	(\$34,058)
Hoyt	69,775	149,260	(\$79,484)
Jackson	24,565	91,207	(\$66,642)
Kosciuszko	58,419	180,115	(\$121,696)
Lincoln	19,393	86,276	(\$66,883)
McCarthy	63,666	132,600	(\$68,993)
Sheridan	55,780	108,812	(\$53,031)
Washington	8,109	90,861	(\$82,752)
Wilson	18,281	78,651	(\$60,370)
Noyes	89,149	343,907	(\$254,758)
Pulaski	104,519	\$335,015	(\$230,497)
Total	\$1,322,290	\$2,343,922	(\$1,021,632)

* Overhead, depreciation and bond interest not allocated to these operations.

** Revenue of \$15,000 received from South Milwaukee in 3/03 not included.

Greenhouse and Horticultural Venues

For 2004, the new Landscape Management Section under the Parks Division consolidates all horticulture services. The horticulture operation will include the Mitchell Conservatory, Boerner Botanical Gardens, and Wehr Nature Center venues. In 2003, the new Education and Visitors Center at Boerner Botanical Gardens opened under a partnership between the County and the Friends of Boerner Botanical Gardens.

Under this partnership, the Friends contributed 70% of the new center's construction costs and the County contributed 30%. The Center is owned by the County and operated by the Friends with the Friends also participating in the educational aspects of the Center. The new Center will generate revenues from admissions, a privately-managed restaurant, facility space rental and contributions from the Friends.

For 2004, only six of the ten Parks' greenhouses will be operating. The budget also shifts greenhouse staff to the Mitchell Conservatory to allow staff to both grow and show plants. Exotic plants for the Domes and Boerner Botanical Gardens will continue to be grown by the Landscape Management Section. Annual plants for other parks will be purchased from the private sector with

a budget allocation of \$50,000. Also, all Parks mower equipment maintenance previously done at its 68th and State location is transferred to Fleet Division for 2004. When comparing operating costs of these horticulture venues with similar private sector operations, indirect County costs including overhead, depreciation and bond interest must be considered. These are legitimate costs of operation and must be included to provide a fair companion to similar private operations.

Swimming Pools

As reported in the Department of Audit's August 2003 report on Parks Concessions Operations, total attendance at County pools (indoor and outdoor) has dropped from a high of 601,450 in 1991 to 430,541 in 2002, a decrease of 28 percent. All pools showed a loss in 2002, except for the Greenfield Aquatic Center (which would have shown a loss if overhead, depreciation and interest charges were included). In response to declining attendance and projected pool repair costs, the following pool closings have taken place: Carver (1993), McGovern (1995), Gordon (1997), Madison, Dineen, Moody (2002), and Hoyt (2003). Pool losses would be higher if all costs of operations including overhead, depreciation and bond interest were included. For example, if depreciation and bond interest costs for the relatively newly constructed Greenfield Aquatic Center (Cool Waters) were included, the current profitable results of that pool would be negatively impacted. All costs of pool facilities must be considered when making policy decisions regarding the future of pool operations.

Golf Courses

The budget for 2004 golf permit sales was reduced to more accurately reflect declining golf participation. As reported previously by the Department of Audit, rounds for the County's eight major golf courses have decreased 34% from 1985, while par-three golf course rounds have decreased 54% over that same time period. For 2002, Parks reported that the County's eight major courses made \$277,000 while the eight par-three courses lost \$337,000 for a combined golf operating loss of \$60,000. The Department of Parks contracts with the Wisconsin Professional Golf Association (WPGA) to oversee golf operations at the Brown Deer, Dretzka, Oakwood and Whitnall courses. In 2003, the contract with the WPGA was re-negotiated, resulting in \$100,000 in estimated increased revenue. Overall, golf operating costs do include overhead and depreciation costs. As a result, County golf operations can be compared with similar private sector operations.

Marina

McKinley Marina continues to be a Parks Division run operation. For 2004, slip rental rates are adjusted to address price inequities between slip size resulting in a revenue neutral fiscal effect. The Marina Roundhouse restaurant operation was contracted out to a private operator in 2003. Annual Marina operations do include overhead, depreciation and interest costs which provide a true reflection of total costs when comparing to similar private-run operations.

GENERAL CONCLUSIONS ON COST DATA

As previously stated, the financial information provided by the Parks Division has not been verified by the Department of Audit. However, a number of general observations are warranted.

Allocation of Overhead

As can be seen from above, overhead costs are allocated only to a small number of the entities. This was discussed with a member of the accounting staff at the Parks Division who stated that this was the way the reports had been done in the past. The representative stated that there were two components to the overhead, each of which was approximately 15% of direct expenses resulting in a total overhead of slightly more than 30% of direct costs. Applying overhead costs provides a better picture of the true cost of each program.

Recognition of Overhead

Depreciation is an accounting term for spreading the cost of an asset over the useful life of the asset. Government Accounting standards do not include the reporting of depreciation in the General Fund of a government. When comparing a government run program to a private sector operation, depreciation expense should be considered. Depreciation should also be considered when determining the true cost of the program.

Recognition of Interest Expense

The representative of the accounting staff of the Parks Division stated that this interest is associated with debt financing of certain improvements to the marina. Interest costs from debt financing should be included where appropriate when analyzing total program costs and / or when comparing to similar private sector operations.

As can be seen from this discussion, the methods of allocating cost to activities within the Parks Department is not consistent. The model used is a modified Fully Allocated Cost system that is not applied on a consistent basis. This results in the cost data often not being useful for privatization decisions.

A number of key concepts must be included in cost analyses of potential privatization actions. These include the following:

Avoidable Costs- Those in-house costs that will go away if the service is contracted out. Avoidable costs usually include the direct costs involved in providing a service. To some extent, administrative costs may also be eliminated or reduced. Other costs, such as general countywide overhead, may not be diminished at all.

Contracting Costs – The total contracting cost is the sum of the contract cost, plus in-house administration costs, plus conversion costs (spread over an appropriate length of time, depending on the situation) less any new revenue.

ADVANTAGES AND DISADVANTAGES OF PRIVATIZATION

As with any anticipated change there are a number of positives and negatives. Some of the more common concerns regarding privatization are:

Advantages

- Control might be enhanced because the manager is in a position to terminate a vendor contract and seek another provider. In many cases, privatized service arrangements can be terminated or modified with less notice/greater ease than with a public sector, unionized civil service workforce.
- Depending on the cost of fringe benefits and overhead, as well as productivity levels, a government's cost may be higher regardless of the absence of a profit factor. By definition, privatization effort should be implemented only if cost-effectiveness can reasonably be demonstrated.
- Shifting work from a government monopoly to a competitive environment with a public or private winner could yield improvement in service. When there is more than one viable, prospective vendor that can compete for the provision of a service, the County can benefit from those competitive forces in terms of a vendor that is motivated to surpass performance expectations. This may manifest itself in different ways, such as superior customer service, or the private sector's tendency to make better use of cutting edge technology and premium-grade equipment.

Disadvantages

- Managers might lose significant control if much of their work was contracted out because the work would no longer be performed by employees under their direct control.
- Privatized cost may be higher because the government does not charge fees designed to generate profits from its services as businesses do.
- A dependence could develop on sole source vendors. Such dependence could leave the County vulnerable to large price increases until such time as the County could gear up for resuming in-house operations.
- Performance may deteriorate because industry might focus on profits, rather than public needs. While, short of divestiture, the County remains ultimately responsible for the provision of services, it must go through a third party to respond to client/customer concerns.
- Government employees might be laid off.

To address these concerns, there are a number of questions that should be asked when considering privatization of County services.

Does Milwaukee County have complete and accurate figures for costs and revenues associated with the program that can be used to compare County costs to the proposed privatization? The present cost allocation system within Milwaukee County is generally not adequate to make such a determination. In particular, analysis of cross charges and overhead as to their applicability to the provision of a given service is necessary.

What impact will the privatization have on existing employees? Significant numbers of former County employees may be employed by the new provider of the services in the event of privatization. Short term costs may increase if employees retire under a privatization model. Lower long term retirement costs may be achieved if employees retire early because of privatization. In some situations, Milwaukee County has retained responsibility for long-term benefits of employees who are transitioned to a private operation.

In one example, transition of Milwaukee Public Museum employees to the private museum corporation included provisions for continuation of salary, fringe and pension benefits substantially equivalent to their status with Milwaukee County. At retirement, a separate pension is paid by Milwaukee County for years of service prior to the transition. For employees transferred to United

Regional Medical Services, the County retained the pension obligation. The 2004 cost is approximately \$2.5 million.

Will services be solicited through a competitive request for proposals process?

Consideration should be given to competition whenever possible. There may, however, be times when a sole-source approach is appropriate (e.g. Doyne sale, MPM privatization).

Will the current government operation be allowed to compete for the opportunity to provide the service?

This may or may not be a viable option in all instances. When considering this approach, care must be taken to establish an 'even playing field' that does not necessarily follow existing parameters. Allowing current government operations to compete may involve changes in work rules, workloads, procedures, classifications or other aspects of County services.

Milwaukee County has various procurement ordinances that define what is a permissible method of contracting. Dependent on the activities being privatized, the applicable ordinances would either have to be followed, or some waiver of the requirement of the ordinances be granted.

Will all service elements be put out for private bid or will the privatization be limited to specific elements?

In some instances, vendors may only be interested in service areas with the highest revenue potential and/or the lowest cost. For example, contractors might only be interested in operating premium golf courses, not the County's par three courses. Activities that are not viewed as profitable by the private sector could continue to be operated by the County, contracted out with a subsidy, or the need to provide the service could be reassessed.

Does the proposed contract for privatization prohibit near term cost increases? The County would need to be mindful of bids structured artificially low and then adjusted later. Transition costs should also be factored into any analysis of cost savings.

What are the accountability provisions of the proposed privatization? Are there measures of performance?

One of the better methods of privatization would be to require defined outcomes relative to quantity and quality of the services provided. Contract terms can be developed to provide financial incentives / penalties for failure to attain defined quantity and quality outcomes. This should be done irrespective of privatization. These measures could also include provisions for incentives/penalties.

Does the privatization bind the County to the provider in a manner that is difficult to reverse? Extra care should be exercised when the cost of reinitiating the service is excessive. Classic examples are privatization of snow plowing and garbage pick-up, where the government's cost to re-capitalize is high. While the venues identified in this resolution have significant capital costs, depending on the type of privatization considered, short-term reversal of the privatization decision might be possible.

Attachment 1 identifies items to be considered in assessing privatization efforts.

STEPS TO IMPLEMENT PRIVATIZATION INITIATIVES

In a report issued by the General Accounting Office, "Privatization – Lessons Learned by State and Local Governments (GAO/GGD-97-48)" a number of key requirements are identified. These include the following:

PRIVATIZATION REQUIRES A POLITICAL CHAMPION

When introducing and sustaining privatization initiatives, officials should anticipate a need to develop and communicate a privatization philosophy and to garner public, business, and political support. Based on the sample of entities that were reviewed the most common champion was the chief executive officer (Governor or Mayor). In one state, key legislators and the Governor worked together to introduce new privatization initiatives.

IMPLEMENTATION STRUCTURE NEEDED TO GUIDE PRIVATIZATION EFFORTS

Once leaders introduce privatization, they needed to establish a formal structure to ensure effective implementation. A government-wide commission may be helpful to identify privatization opportunities and set privatizations policy, support agencies in their privatization efforts, oversee implementation, and provide a framework for making privatization decisions.

LEGISLATIVE AND/OR RESOURCE CHANGES MAY BE NEEDED TO PROMOTE THE USE OF PRIVATIZATION

Governments may need to enact legislative and/or resource changes to encourage or facilitate the use of privatization. These changes are necessary to signal to managers and employees that the move to privatization is serious and not a passing fad.

RELIABLE AND COMPLETE COST INFORMATION NEEDED TO SUPPORT PRIVATIZATION

Reliable and complete cost data on government activities are needed to ensure a sound competitive process and to assess overall performance. Reliable and complete data can simplify privatization decisions and make these decisions easier to implement and justify to potential critics. Models varied from estimated costs to more formal mythologies.

STRATEGIES NEEDED TO MANAGE WORKFORCE TRANSITION

Moving governments into privatization requires (1) employee involvement in the privatization process, (2) training to provide skills for competing against the private sector and monitoring contractor performance, and (3) creating a safety net for displaced employees. These strategies were necessary to mitigate employees' concerns with, and to bolster their support for, the privatization changes as well as to aid in the transition to a competitive environment.

ENHANCED MONITORING AND OVERSIGHT OF PERFORMANCE IS NEEDED WHEN PRIVATIZATION IS USED

Monitoring and oversight that not only evaluates compliance with the terms of the privatization agreement, but also evaluates a private firm's performance in delivering services is needed when a government's direct role in the delivery of services is reduced through privatization. This is necessary to help ensure that the government's interests are protected and that accountability of both the government and the private party are maintained.

There are three essential components to reaping the benefits of privatization: (1) a well-written contract; (2) a strong County contract administrator to enforce vendor compliance with minimum contractual requirements; and (3) a will to support strict administrative enforcement of contractual requirements.

PUBLIC POLICY CONSIDERATIONS

Policy makers need to consider a range of information and data before deciding whether a public service should be privatized. Such assessment should include (a) a thorough analysis of all relevant, reliable financial data, (b) plausible service delivery alternatives (c) direct advantages and disadvantages of the proposed privatization and (d) the indirect effect of the initiative. In addition to obtaining these facts, it is necessary for decision-makers to understand why certain services are being provided by the public sector and whether community values have changed that would make those decisions different now versus ten or twenty years ago. As such, the values and priorities of the community establish the foundation for a decision-making process that is informed by facts. In this regard, reaching consensus on the appropriate role of government in a particular enterprise is fundamental to a policy discussion on privatization.

Pressure on the public sector to privatize services continues to grow as the availability of public financial and human resources decrease. Therefore, it is even more imperative that decision-makers thoughtfully assess privatization initiatives within the context of what constitutes good public policy. Milwaukee County's operation of an extensive network of golf courses can be used to illustrate this point. Fiscal information may, in all likelihood, show that some courses "lose" money. Alternatives may include privatizing the operation of only the courses that "make" money (i.e., "cherry picking"). Public policy debate may lead to a conclusion that certain unprofitable courses are an important part of a county recreation program for citizens who are young, elderly or disabled. In this example, public policy considerations could conceivably weigh in favor of a decision to continue operation of a subsidized par three golf program.

However, debate may also lead to the conclusion that the decrease in governmental financial and human resources forces a serious look at privatizing or shedding this service because it no longer "justifies" the cost. The historical, community-based context of "public" golf helps to frame the policy discussion. At one time, the County decided that minimal fees should be charged to play a round of golf at the par threes in order to serve the novice golfers and those unable to play at the advanced courses. Because the par three courses are accessible to so many different users, they

have become “feeder” into the larger County golf course system. These may be considered as the values and priorities of the greater community, at some point in time, which could be included in the assessment of any privatization.

Milwaukee County has and will continue to make decisions on whether a public service should be privatized or not. To ensure that policy makers are able to make the best decisions possible, all of the information must be available. In most cases, this goes beyond the analysis of revenues and expenditures.

CONCLUSION AND RECOMMENDATIONS

This report is intended to provide a broad perspective on privatization of Milwaukee County government services. Our analysis should be viewed neither as creating barriers to privatization nor advocating it. In each initiative, some of the factors we have identified will be more relevant than others.

If the Milwaukee County Board of Supervisors believes that there are specific potential improvements to the services provided to County residents, at the same or reduced cost, implementation of a structured privatization initiative is warranted. Each proposal should be thoroughly analyzed on its own merit. This report is for informational purposes. Please refer it to the Committee on Finance and Audit and the Committee on Parks, Energy and the Environment.

Supervisor Lee Holloway, Chairman, Milwaukee County Board of Supervisors
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Privatization Considerations

- Type of privatization.
- Revenues and expenses of current operation (including direct cost, depreciation and overhead).
- Expected impact on revenues and expenses.
- Impact on services.
- Impact on employees.
- Performance measurement considerations.
- Accountability framework.
- Competitive solicitation.
- Long-term and short-term impacts.