

June 2001

**LEAGUE OF WOMEN VOTERS OF NEW ORLEANS**  
**A GUIDE TO PRIVATIZATION OF GOVERNMENT SERVICES**  
**AND**  
**AN ANALYSIS ON THE PROPOSED PRIVATIZATION OF THE NEW**  
**ORLEANS SEWERAGE AND WATER BOARD**

**The League of Women Voters of New Orleans became aware of the proposed Request for Proposals (RFP) and Request for Qualifications (RFQ) being developed for the New Orleans Sewerage and Water Board in July, 2000. Based on the League's Good Government positions, the procedure being followed by the Board was flawed. The public and other significantly affected parties were being by-passed in the process to approve a massive privatization plan. The S&WB planned to adopt the draft documents on February 21, 2001. The League, followed shortly by the Bureau of Governmental Research (BGR) and others, requested more time to review the proposals and also a procedure for including the findings in the final procurement plans.**

**In response, the S&WB moved adoption of the draft proposals to the end of June, and are accepting comments from the public, and are accepting comments from the public until June 15. An executive summary of the proposal was made available in print and on the website. A printout of questions from the public and answers provided by the S&WB's consultants has been made available on request.**

**Considering the potential impact of the proposed privatization and the imminent decision before the Sewerage and Water Board, the League Board voted that the situation constituted an emergency and that the League should develop positions on the issue of privatization of government services. Information was gathered from the S&WB documents released to the public, the Sewerage & Water Board (S&WB) meetings, the S&WB staff and the BGR report released in April, 2000. In addition, a privatization study guide compiled by the Montana League of Women Voters was utilized. The League hosted a public forum on April 2, held at the University of New Orleans. In May, interviews were conducted with a vice president of United Water, an international water company, and Councilmember Eddie Sapir and his consultants.**

*"Whatever the issue, the League believes that efficient and economical government requires competent personnel, the clear assignment of responsibilities, adequate financing, coordination among levels of government, effective enforcement and well defined channels for citizen input and review."*

(From: LWVUS Impact on Issues 2000-2002: A Guide to Public Policy Positions, Public Policy Positions, p. 3)

The following material is excerpted from Privatization Study, Montana League of Women Voters, January 2000.

### **PROS OF PRIVATIZATION**

- Where the private sector can provide the service profitably and at a lower cost, the government is spending citizens' tax money unnecessarily.
- When the government has a monopoly on provision of services, the lack of competition can give rise to higher levels of political intervention and bureaucracy and legal constraints, leading to inefficiency on the one hand or one-size-fits-all services.
- Both the public and the private sector can benefit from privatization. For example, if the private sector achieves higher productivity, government resources are freed up to address other policy issues of major concern.
- In certain cases, citizens' needs can be most expeditiously or efficiently served by the private sector because market competition has been enabled. According to John Hilke (of the Reason Foundation) over 100 independent studies found privatization programs carried out by state and local governments have realized between 20% to 50% cost reductions. The increases in productivity result from the power of the profit motive to encourage innovation, more productive equipment, and in some cases, economies of scale.
- Potentially, private firms are more responsive to the public in offering services, with flexibility, speed, and continual service-improving innovation.
- Studies have shown that the effect of privatization on unemployment is not a major problem, although some layoffs do occur. Some of the tools that have proven effective with labor in privatized firms are employee safety nets, retraining, job placement, early retirement, and attrition.

### **CONS OF PRIVATIZATION**

- One frequent problem is a lack of sufficient competitive bidders. Competition is usually needed to attain a satisfactory contract.
- Even with sufficient competition, problems often arise if the winning contractor has won with a "low-ball bid." This creates two significant risks for the government: the contractor will fail to complete the work (which usually results in an increase in costs for the government) and because he is on the job, the low-baller will have an advantage against remaining contractors.
- A simple comparison between expenditures before and after privatization is not sufficient for judging whether privatization has been a success. The reduction in government expenditures may be due to the contractor providing his employees with lower wages and benefits than the government employees, in order to show a significant profit. For instance, if health benefits are not provided, the cost of health care may fall on others.
- Privatization advocates have a tendency to overstate the benefits from privatizing. In one survey of 63 cities, the estimated cost savings, as reported by the cities, ranged from 16 to 21 percent, much lower than the advocates suggested. Reported costs may not include the hidden costs of privatization, e.g., of originating the contract and overseeing the contractor's performance.
- There can be employee problems involving unionization. Privatizing government services is almost sure to have a negative impact on the morale not only of the employees who are directly affected but on the other employees as well.
- Inadequate analysis of costs before privatization affects the final cost savings.

## **LWVNO POSITIONS ON PRIVATIZATION OF GOVERNMENT SERVICES**

1. Privatization of a government utility is justified only when it can be demonstrated that services will be increased or there will be an improved cost/benefit ratio, and these goals cannot be reasonably achieved within the existing structure.
2. In the bidding and contracting process, there should be policies to prohibit potential contractors and affiliated corporations from giving campaign contributions, providing jobs or loans, or contracting with public officials who are involved in the process, or their family members.
3. The contract should provide for scheduled and periodic independent audits.
4. Any private company operating public services must be subject to the public records laws.
5. Following the transition, the government agency should fulfill the role of regulator, have sufficient expertise and staff to monitor the performance of the contractor, and manage the responsibilities that are not included in the privatization.
6. Proposals for privatization of government services in Orleans Parish should meet certain criteria:
  - a) The plan provides full cost information, including indirect costs, for both the privatization proposal and the actual cost of the government agency to provide the service.
  - b) Civil Service Commission rules should be followed throughout any privatization process and the impact to employees clearly defined.
  - c) There will be no diminishment in the quality of services delivered to the citizens.
  - d) There is independent oversight of contract performance with measurable factors for evaluation and agreed upon periodic review.
  - e) The working relationship between the private sector and the government agency is clearly defined in all aspects, including facility and equipment usage, access, and areas of responsibility.
  - f) Sufficient competition exists from potential providers.
  - g) Penalties for performance failure are clearly stated.
  - h) There is a back-up plan if privatization fails.

Adopted June 2, 2001

# PROPOSED PRIVATIZATION OF THE NEW ORLEANS SEWERAGE AND WATER BOARD

## BACKGROUND:

As a result of public dissatisfaction with ever escalating waterline breaks and delayed repairs causing structural street damage, and questions raised by incoming city council members, the Sewerage and Water Board (S&WB) began considering privatization. The initial premise was that service could be improved while keeping rates down. Precedent for privatization already existed within the system, as the operations of the wastewater treatment plants were under contract to U.S. Filter.

During this same period, the City Council and the S&WB, agonized over raising rates for the citizens. The increase was necessary to cover the costs of replacing the leaking sewage lines throughout the city. The leaking lines were allowing wastewater to enter the storm drainage system and the resulting contaminated water had been entering Lake Pontchartrain. After years of litigation with the EPA and the U.S. Department of Justice, the City and the S&WB are under a Consent Decree by the federal court to repair the lines. (*The LWVNO was an intervenor in the suit which brought the matter to settlement and resulted in the Consent Decree.*) The expense of the repair is not optional and cannot be delayed. The resulting fee increase only covers the initial expense of line repair and further increases can be expected.

The structure and membership of the S&WB, a state agency, was created to remove those vital operations, essential to the health and safety of New Orleanians, from political influence. However, over the decades the Board itself has become politicized and closely connected to city government. Three of the thirteen members are city council members, and the Mayor is the current Board president. The Mayor appoints two of the members from the Board of Liquidation, a city department. The Mayor, with the approval of the City Council, appoints the other seven members. The mayoral appointees serve staggered nine-year terms.

Decisions are made by recommendations from the S&WB six committees and issues are passed from committee to committee for consideration. This results in long delays. A large number of staff and consultants assist the committees. Consequently, the administrative employees of the Board are burdened with a slow decision-making process. State law requires the S&WB to set user fees, subject to the City Council's approval. However, the decision to privatize can be made by the S&WB and it is not subject to the City Council's approval. **Privatization will not change the structure of the S&WB, nor will it address the decision-making process.**

The annual budget for the S&WB consists of three separate cost centers for the functions of wastewater collection and treatment, drinking water treatment and distribution and drainage. They have dedicated revenue sources and separate capitalization plans. The total operating budget for 2000 was \$99.3 million. In order to satisfy the Consent Decree in up-grading the sewer lines, it is estimated that \$455 million is needed through 2010.

The Request for Proposals (RFP) from potential contractors for privatization does not include the drainage system, the Consent Decree up-grades or any capitalization projects that cost more than \$10,000. The draft RFP will cover the operations of the drinking water system and distribution and the wastewater collection and treatment. It will be for a period of twenty (20) years. In 1997, the IRS began allowing government agencies to contract for longer periods in order to obtain better contracts and financing. **This is the largest privatization proposal in the United States.** It has an estimated value of \$1 billion dollars.

As it was recently pointed out in an article in the *Gambit* and League members learned during a meeting with one of the potential bidders, one of the incentives for a private firm to enter into a contract for privatization would be the opportunity to sell water and services outside the system. Water is a merchantable commodity, and especially potable drinking water, that is becoming increasingly valuable. Laboratory services and wastewater treatment are also marketable to other customers. With an abundant water source and excess capacity, the New Orleans system would be a very desirable acquisition, even with its antiquated infrastructure and inefficiencies. In addition, the mega companies have been operating privatized water systems in Europe for some time. If they can create a successful operation in New Orleans, they will be able to sell contracts to other American cities.

## REASONS FOR PRIVATIZATION:

The commonly perceived reasons for considering the privatization of the operation of the Sewerage and Water Board functions and the more significant reasons may not be the same.

- **A guaranteed contract with a set cost for an extended period of time for a private company to operate certain functions of the Sewerage and Water Board would give the Board an equity holding that enables them to seek bond money to fund necessary major capital improvements, such as the replacement of the leaking sewer lines required by the federal consent decree.** Private companies are generally expected to bid the contract for operation at a lower amount than the government agency. This will free up funds the Board can then use for other purposes. This guaranteed source of income provides backing for bond money. Re-engineering, re-organization or other methods of internal saving cannot achieve the same result, because a promise to save is not considered equity in the bond market.
- **It cannot be assumed that privatization will keep fees charged for services from being increased; however, privatization may offset some of the expected increases.** A private company is not committed to certain operating restrictions placed on government agencies. Measures such as the economy of scale in purchasing, personnel changes, more productive equipment, better maintenance and improved inventory management will hold down costs. For example, the 1999 Annual Report figures show a donation of over one billion gallons of free, metered water allotted to various city departments, agencies and institutions, and over 29 billion gallons in unmetered use and leakage loss. In that same period, nearly 25 billion gallons were sold to ratepayers. A private company would have the incentive to slow the loss of treated water.

On the other hand, there are built-in costs faced by a private company that are not faced by a government agency. The pass-through costs that will be passed to the ratepayers will be taxes, insurance, and the cost of re-fitting facilities to meet OSHA standards. As a government agency, the S&WB facilities are self-insured, not subject to sales taxes, and not subject to OSHA rules.

In addition, there are two foreseeable reasons the Sewerage and Water Board could incur major expenses that would have to be absorbed by the ratepayers. One, major capitol expenses, such as planned replacement of drinking water delivery lines, a charcoal treatment addition for the East Bank water treatment plant or installation of some of the newer microfiltration technologies, will remain the responsibility of the S&WB. The decisions to make capital expenditures will be made by the S&WB and not the private operator. If the private operator cannot meet EPA standards due to antiquated equipment, the Board may be forced to assume capital costs. Two, the S&WB will still bear most of the risks with EPA fines and penalties. First, if the conditions of the Consent Decree are not met for any reason, the court ordered fines are very hefty and not subject to most challenges. Second, the private operator will pay fines and penalties due to their own failure to meet EPA permit requirements and regulations. However, if the failure is due to antiquated equipment, or an uncontrollable circumstance such as flooding or natural settling of the soil, the risk could pass to the S&WB.

- **The claim that privatization of the Sewerage and Water Board will solve the pervasive problem of broken water lines and potholes in the streets is limited to an improved schedule for repair to problems as they occur.** The contract with the private operator can be written to require line and street repairs within a specified time frame whenever a water or sewer line break occurs that causes street damage. This will partially help New Orleans motorists who must dodge potholes and barricades and suffer damage to their vehicles from the uneven streets. A privatization contract will not solve the underlying problem of the shifting soil and old lines. The soil supporting the lines shrinks and swells due to subsidence from the recent drought and subsequent expansion when there is adequate rainfall. When subsidence has been substantial, the street can sink several inches leaving manhole covers above the road surface.

### **THE EMPLOYEE MANAGEMENT OPTION:**

In addition to privatization, there is another alternative before the Sewerage and Water Board. It is called managed competition and would allow the employees to bid on the proposed contracts. The Managed Competition Employee Committee (MCEC) is coordinating the development of the employees' bid. There would be significant differences in the final outcome if the employee group obtains the privatization contract compared to a private firm. Management and/or operations of the S&WB by the employee group would still be considered a government agency, not a private entity. The Jefferson Parish Water Department is employee operated.

The employee group would not be subject to sales taxes and would not be subject to OSHA requirements. They would continue to be self-insured. They could argue that as current employees, they have intimate knowledge of the system and would be in the best position to streamline operations to achieve savings and expedite repairs. There would be no stockholders to satisfy. However, giving the operations contract to the employee group would not create the financial bonding capacity the S&WB is seeking.

### **SOURCES**

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New Orleans Sewerage & Water Board, Draft Request for Qualifications/Request for Proposals, prepared by Financial Advisory Team, February, 2001.

Appendix A: *Agreement for Management Services*

Appendix B: *Memorandum of Understanding for Management Services*

Appendix C: *Agreement for Management, Operations and Maintenance Services*

Appendix D: *Memorandum of Understanding for Operations and Maintenance Services*

("Agreement" refers to a contract with a private company. "Memorandum of Understanding" refers to a contract with a public employee group.)

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