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SECTORAL ACTIVITIES PROGRAMME

Working Paper

Privatization of municipal services: Potential, limitations and challenges for the social partners

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Working papers are preliminary documents circulated
to stimulate discussion and obtain comments

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Foreword

In the context of public service reforms, decentralization is regarded as an important means to achieve improved efficiency and quality of services. One of the challenges in this context is the financing of such services, since tax and fee systems are often not changed simultaneously or sufficiently. Consequently, municipalities and local government institutions opt for a variety of approaches to privatizing services provided in the public interest. Decentralization affects the terms of employment and working conditions of municipal workers, as well as labour-management relations, in a number of ways. Moreover, public employees from government agencies at district, regional and national levels are often transferred to local authorities. Such developments are common to different services that are provided in the public interest, such as education and health services as well as utilities and transport. Despite the differences between these sectors, there is a case for discussing jointly the implications of decentralization on the municipal services. Responses to the challenges arising from decentralization might be found jointly or through alliances between some of the sectors.

The ILO report on “Human resource development in the public service in the context of structural adjustment and transition” of 1998 and the subsequent Joint Meeting have already set out some direction in relation to the public service in general. A further report of the ILO will study the developments more specifically in view of the municipal services and provide the background for the discussions at a Joint Meeting in 2001 on the “Impact of decentralization and privatization on municipal services”. In preparing this report the ILO Sectoral Activities Department is undertaking a wide range of research in various municipal sectors, which include health services, education, transport and utilities.

The present working paper by Brendan Martin on the potential, limitations and challenges of privatization of municipal services is one of several studies which will be taken into consideration for the report of the ILO. It endeavours to set a frame for the discussion of a very complex and multifaceted theme which is at the centre of the changing role of the State and the role that the private providers of public services may assume. The focus of this survey is on labour and social issues in health services, a focus which warrants, however, to introduce the origins, main trends and developments in privatization in a variety of countries worldwide. As a Sectoral Working Paper, the study is meant as a preliminary document and circulated to stimulate discussion and to obtain comments. Earlier drafts of the paper were intensively discussed at the ILO, the opinions expressed are nevertheless those of the author and not necessarily those of the ILO.

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Contents

List of acronyms

AAET	American Anglian Environmental Technologies
AFSCME	American Federation of State, County and Municipal Employees
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of South East Asian Nations
BOT	build-operate-transfer
CCT	Compulsory Competitive Tendering (in the United Kingdom)
CFD	Caisse Française de Dévelopement
DKK	Danish Confederation of Municipal Employees
EPSU	European Federation of Public Service Unions
EU	European Union
FOA	Union of Public Employees (in Denmark)
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
IFC	International Finance Corporation
ILO	International Labour Organization
IMF	International Monetary Fund
IPP	independent power producer
ISS	international service systems
ITF	International Transport Workers' Federation
NAFTA	North American Free Trade Agreement
OECD	Organisation for Economic Co-operation and Development
PFI	Private Finance Initiative (in the United Kingdom)
PPA	Power Purchase Agreement
PSG	Professional Services Group, Inc.
PSI	Public Services International
RPI	Retail Price Index (in the United Kingdom)
TRIPS	Trade-Related Aspects of Intellectual Property Rights
USAID	United States Agency for International Development
UW	United Water
WTO	World Trade Organization

1. Introduction

1.1. Introducing the paper

This paper explores the potential and limitations of privatization to tackle the range of challenges faced by public services in general, and municipal services in particular. It was commissioned by the ILO for the Joint Meeting on the Impact of Decentralization and Privatization on Municipal Services with a remit to explore the subject with particular reference to a range of employment issues – specifically labour relations, workers' rights, productivity, human resource management and working conditions – and service delivery issues, specifically quality, service outcomes and democratic accountability, as well as productivity. These were to be discussed in the context of the impact of globalization on the challenges facing public services, and the relationship between globalization and privatization. In addition, the terms of reference required some exploration of alternatives to privatization.

The paper begins with this introductory section 1, which looks at privatization in general, its definition, forms and trends, before locating privatization of public and specifically municipal services in that context. Section 2 explores the relationships between globalization, privatization and public services. It examines the range of pressures on public services which have fuelled the privatization trend, focusing in the course of this also on the perceptions of the various stakeholders – government, service consumers, public service workers, business – and on the roles of various international institutions. Section 3 explores the impact of privatization on public services in terms of the employment and service delivery dimensions identified above, while section 4 attempts to draw some brief conclusions and to identify challenges and opportunities facing the social partners in relation to the subject. There are also eight boxes, each examining a particular case, selected to illustrate the range of themes addressed in the paper in the detail enabled by case studies. Although these cases have been located within the paper in a way designed to illustrate in particular the themes discussed in the sections of the paper in which they are located, each case also cuts across the sections by illustrating also the themes of the paper as a whole.

1.2. The origins of privatization

Few international political issues have aroused such passions over the last two decades as privatization has done, and yet the term's meaning remains imprecise. It is a very young term, but has acquired in its short life a range of usage much wider than that of terms many times its age. This breadth of usage not only reflects the variety of contexts in which privatization has occurred, but also the variety of political and economic projects which – as a policy instrument, if not as a policy – it can serve.

Although privatization as a systematic policy of macroeconomic structural reform informed by a strong ideological view about the roles of the State and the market became an international phenomenon only in the 1980s, following the example of the Thatcher administration in the United Kingdom, it was the Pinochet military dictatorship in Chile a decade earlier that had been responsible for the first comprehensive national experiment. Privatization as a policy instrument of more marginal significance to macroeconomic policy began earlier. The first reference recorded by the Oxford English Dictionary (OED) is attributed to the Erhard Government in West Germany in 1959 (in connection with a mining concern), while the first usage mentioned by the OED in connection with public services is drawn from Canadian press reports of 1976. [1]

Private provision of municipally organized public services pre-existed the term "privatization" by centuries. "Private firms had contracts to clean the streets of what is now New York City as early as 1676", an ILO publication has noted, and "municipalities have been contracting with the private sector for the provision of services and infrastructure ever since". [2] As a movement, however, privatization is as recent as the term. To a small extent in the 1970s, much more in the 1980s and very much more in the 1990s, first a few national and local governments and later many began to divest state-owned enterprises on an unprecedented scale, to contract out public service provision and in a variety of other ways to transfer responsibility, ownership, financing, operation and/or management from the state to private businesses or individuals. By 1995, well over 100,000 enterprises had been divested and more than 80 countries had fully fledged privatization programmes. Privatization had transcended its origins as a policy instrument to become a policy in itself.

1.3. The meaning of "privatization"

The OED defines privatization as "the policy or process of making private as opposed to public", a formulation which begs more questions than it answers. Although typically used in connection with the changing size, role and activities of the State, the term is sometimes used to capture the effect of restricting access to and authority over "the commons" (that is, assets held in legally protected common, as distinct from state, ownership). Moreover, the term "privatization" has also been used in connection with arrangements which result in non-state but also non-profit ownership or control of assets or activities previously the property or responsibility of the State. In addition, in some countries, privatization has been seen – or, at any rate, presented – as a means to make ownership and control of assets more rather than less public. Sri Lanka's privatization programme was at one time known as "peoplization", for example, while, in the United Kingdom, the term "people's capitalism" was coined to describe the results of the mass share flotations which privatized utility services. The acronym "plc" does, after all, stand for "public limited company", a form of joint stock ownership, and anyone with the means to do so is entitled to buy shares in such a company if there is a willing seller.

However, there is clearly a fundamental difference between rights of ownership and influence which arise from financial status and commercial transactions, and those which arise from citizenship within a State. It is that distinction, rather than less precisely defined distinctions between "public" and "private", that is at the heart of the privatization debate, and which principally concerns us here. We are chiefly concerned, that is to say, with privatization as a transfer from the civic to the commercial sphere.

However, another question immediately arises: transfer of what? At its narrowest, privatization denotes transfer of ownership, but the term is also used in connection with contracting-out, private finance for public infrastructure, and many other instruments. "Nevertheless," one study has commented, "the lowest common denominator of all types of privatization policy is some transfer of productive activity from the public sector to

[1] *Oxford English Dictionary*, 2nd edition, Clarendon Press, 1989, p. 821.

[2] D. Rondinelli; M. Iacono: *Policies and institutions for managing privatization: International experience*, ILO, 1996, pp. 4-6.

privately owned enterprises”. [3] Even that does not embrace the full scope of privatization’s forms, however, since some entail transfer of responsibility – from the collective to the individual, for example, in the case of user fees – rather than of productive activity.

Bearing all those points in mind, privatization *is defined* in this paper as *the transfer of ownership, responsibility, financing, operations and/or management from the State to non-state organizations or to individuals*.

There have been countless definitions of “privatization” and that one is broader than some, as we have seen, and narrower than others. It is narrower, for example, than that of another ILO paper, which defines privatization as a “transformation or participation process designed either to secure involvement of private investors or to introduce more market like spirit into public activities”. [4] This would include various forms of commercialization and marketization in relationships between the State and private business, between the State and its citizens and within the state sector itself. Such forms include competitive tendering between in-house operations and outside contractors (not necessarily leading to contracting-out); the introduction of vouchers as a form of currency to enable public service users to choose between rival service providers; reconstitution of state-owned enterprises into corporate forms, as has recently occurred in the United Kingdom post office; restructuring to create internal markets within the public sector, associated with division of purchasing and providing (or client and contracting) responsibilities; and even the reprioritization of the objectives of public service providers in favour of commercial considerations. Mechanisms such as those can be closely related to privatization in various ways, such as by paving the way for it, but they can also be viewed as alternatives to privatization. For both those reasons, this paper’s definition of privatization excludes them.

1.4. Forms of privatization

This paper’s definition of privatization nevertheless incorporates many forms. Privatization of responsibility can involve, amongst others, liberalization or deregulation of a sector; liquidation, termination or reduction of state production/provision; and transfer to individuals of financing responsibility (not only in the form of direct user charges, but also in the form of, for instance, private medical insurance).

Privatization of ownership can lead to various structural outcomes, related to the various means by which it can be accomplished, such as share flotations, direct sales to operating companies, sales to investment funds, mass privatization through vouchers, restitution to previous owners, management and/or employee buy-outs, transfer to cooperatives or other forms of collective non-state but also non-profit bodies, and disposal of land or other assets. Many of those forms can also be total or partial, and, if partial, can involve a majority or minority stake (although some commentators believe that to be worthy of the name, privatization must involve transfer of control).

The major forms of privatization of operations and/or management are contracting-out and (usually longer-term) concessions, with or without competitive tendering in either case. Concessions are often linked to privatization of capital finance for public

[3] G. Yarrow; P. Jasinski: *Privatization: Critical perspectives on the world economy*, Routledge, 1996, Vol. 1, p. 2.

[4] C. Oestmann: *Privatization of public services and public utilities*, ILO, 1994, p. 5.

infrastructure development or renewal, through such mechanisms as build-operate-transfer (BOT) schemes.

Some forms of privatization are peculiar to countries of a particular type, or more common in some types of countries than in others, for reasons arising from a variety of factors, such as prevailing national levels of economic and capital market development. Some forms of privatization are also employed more in some sectors of public service than in others. For examples, the long-term concession, often linked to a BOT scheme, is the typical form of water privatization (the United Kingdom being exceptional in having privatized ownership of water and sewage assets as well as operational and investment finance responsibility), while for other municipal services, such as solid waste collection, shorter term contracting-out is the more typical form. But the precise design of each mechanism also varies, as does whether or not a particular privatization applies to the whole of a service organization or to specific parts of it.

1.5. Privatization of public services and municipal services

In most countries, depending on the range of state ownership and operations at the time, privatization started with divestiture of small state-owned enterprises in potentially competitive markets, moving into utilities and other public services later. [5] By now, public services are the main arena of privatization throughout the world, although the scale of their privatization continues to vary significantly between and within continents. For example, whereas in the European Union, privatization of water and electricity distribution remains highly exceptional, it is becoming almost routine (partly as a result of International Monetary Fund (IMF) and World Bank policy) in Africa and Latin America. [6]

Box 1
The Philippines privatization programme

The privatization programme in the Philippines, first conceived during the presidency of Ferdinand Marcos under the influence of the IMF and World Bank, is managed by the Committee on Privatization (COP), an agency within the Office of the President. Implementation began after the overthrow of Marcos and his replacement by the Cory Aquino administration in 1986, and gathered pace under the presidencies of Fidel Ramos and Joseph Estrada in the 1990s.

The programme has had three overlapping phases, starting with divestiture of government-controlled corporations, moving on to utilities and most recently encompassing also a range of other public services, including municipal ones. Its five-point rationale is to:

- improve efficiency and provide better-quality service;
- focus government energies and resources on provision of basic public goods and services;
- create a more favourable investment climate;
- broaden the base of property ownership and develop the capital market;
- generate revenues for priority government projects, including land reform and development of public infrastructure.

[5] R. Ramamurti: “The new frontier of privatization”, in R. Ramamurti (ed.): *Privatizing monopolies: Lessons from the telecommunications and transport sectors in Latin America*, John Hopkins University Press, 1996, p. 1.

[6] L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998.

From 1987 to 2000, some 470 industrial, service and banking enterprises were sold to private buyers, raising around 194 billion Philippine pesos (around US$4 billion at January 2001 exchange rates), some of which has been earmarked to finance the country's agrarian reform programme. During the 1990s, privatization was extended into the electricity sector, in the form of 42 independent power projects (IPPs), while the activities of the National Power Corporation (Napocor) were commercialized. The privatization programme was also extended into water, with the responsibilities of Manila Water and Sewage Services being transferred to two long-term concessions each run by a consortium linking established Philippine businesses with transnational partners specializing in the sector.

More recently, the focus has shifted to privatizing local government operations in various ways, including BOTs, contracting-out and other forms of what are seen as public-private partnerships. Sectors affected include public markets, slaughter houses, cemeteries, fish ports, electricity distribution, water supply and waste management. Further sectors to be brought into the programme include land reclamation, fisheries, forestry, parks and wildlife management, and education facilities, while the expansion of a private health care sector is being promoted.

The Committee on Privatization has carried out no systematic evaluation of the programme's effects, in terms of either its declared objectives or broader considerations such as employment and labour impacts. [1] The programme has been criticised for its failure to combat (and, indeed, for its contribution to consolidating) the corruption and nepotism which are acknowledged features of the both state and business, and of the relationship between them, in the Philippines. The programme has also aroused controversy because of some perceived differences between its rationale and its effects. The fact that new owners typically include already dominant business interests is seen as clashing with the objective of spreading ownership of productive assets in the country more widely, for example, while the programme's extension into local public services is criticised on the grounds that the proceeds from earlier privatizations were supposed to enable the State to invest in those.

A major recent controversy has concerned the terms under which Napocor is obliged to pay IPPs (in US dollars, following rapid devaluation of the Philippine peso) for power it does not need. Although the 42 IPPs led to the construction of much-needed new electricity generating capacity through private finance, the capital was secured on the basis power purchase agreements (PPAs), which are "take or pay" deals under which Napocor (with guarantees from the State) pays for a certain amount of power at predetermined prices whether or not it can be economically retailed to municipal and other distribution utilities. It is estimated that this arrangement has produced losses of more than $9billion, transforming Napocor's healthy financial position into growing deficits. Consumers and potentially taxpayers are now carrying that burden but "will not get anything in return – no new service, quality improvement, or any asset of value". [2] The problems arising from this allocation of risk have prompted the new Government of President Gloria Arroyo-Magacapal to review plans for Napocor's privatization, which had been one of the conditions for future International Monetary Fund (IMF) support.

[1] The most complete evaluation of the social and labour impact so far carried out was conducted by the present author in August 2000 for the Philippines Civil Service Commission, as part of a project in which three of the four union confederations representing public employees were also partners. Fuller details of the programme and its effects are contained in that report which, although not intended for publication, might be available from the Civil Service Commission of the Republic of the Philippines, Constitution Hills, Batasang Pambansa Complex, Diliman, 1126 Quezon City, Philippines. [2] R.V. Vicerra: *NPC stranded costs: How to prevent the adverse redistribution of people's incomes*, Congressional Budget and Planning Committee, Philippines, 2000.

Source: B. Martin: *In the public service*, Zed Books (forthcoming).

There are difficulties with identifying cross-national trends in privatization of specifically municipal services, not least among them that the constitutional, institutional and structural context varies between countries. Public health care services are delivered through municipalities in some countries but not in others, for example, and the same can be said of education, public utilities and other sectors. The nature of the constitutional relationships between the two tiers also varies, and in many countries the picture is additionally complicated by an intermediate tier of regional government, and/or by the existence of ad hoc bodies responsible for particular services in diverse relationships with national, regional and local government.

A further complication is that, as well as varying between countries, the constitutional, institutional and structural context is changing within countries. Indeed, a feature of public service reform over the last two decades has been change in the relationship between central and local government. While decentralization of responsibilities (though not necessarily of the budgets previously allocated to them) has been a salient feature of this trend, there has also been in many countries a concurrent process of centralization of powers in some respects, which has had a bearing on the course of privatization in municipalities.

In addition, and significant in the context of this paper, some municipal privatization – especially contracting-out – is by nature on a smaller and more local scale than that of utilities or nationally organized state enterprises, and has been comparatively under-reported.

The salient national example of the way in which privatization of municipal services can be accompanied with centralization, rather than decentralization, of power is that of the United Kingdom, which has been more systematic than any other country in contracting-out municipal services (see box 2). The United Kingdom pattern has no replica elsewhere, but privatization of many municipally provided services – especially in the forms of concessions and contracting-out – has been on the increase internationally throughout the last two decades, not least as a result of structural adjustment programmes in countries borrowing from the IMF and World Bank. Those institutions' policies have been influenced, as one would expect, by their largest shareholder, the United States, where there has been a rapid increase in the range of municipal services put out to tender and privatized.

Box 2
Privatization and marketization of municipal services in the United Kingdom

Decentralization and municipal privatization are often assumed to be bedfellows, but in the United Kingdom systematic contracting-out of local authority services required centralization of power to a very significant degree. Under a regime called Compulsory Competitive Tendering (CCT), it became unlawful from 1989 onwards for any local authority to operate its own service in six specific sectors without having first sought bids from private companies. A similar regime had been imposed on hospitals, then governed through dedicated local bodies, from 1983. The local government services initially affected were building cleaning, refuse collection, street cleansing, school and other catering, grounds maintenance and vehicle maintenance. Later, sports and leisure management was added to the list, and later still the regime was extended to a proportion of "white-collar" functions such as housing management and legal services.

Except by special dispensation from central Government, municipalities were obliged under CCT to accept the cheapest bid. Even the rules governing how the tendering should be carried out and evaluated were written into the legislation, which gave central Government sweeping powers to change the rules and extend CCT to new services by order, without the need for further discussion in Parliament. The tendering rules specifically outlawed local authorities taking into account, when awarding the contract, any "non-commercial" considerations. The legislation defined a number of these – including the pay rates, employment practices, health and safety records and equal opportunities commitments of companies submitting tenders – but also empowered the Government to continually redefine the meaning of "non-commercial" by adding to the list of specific considerations which were outlawed. In addition, the law required local authorities not to do anything to "distort, restrict or prevent competition", and passed to the Government the duty of deciding whether any particular act of commission or omission fell foul of that requirement.

The scale of the transformation CCT brought about in local government can be measured by the fact that while in 1989, before the legislation took effect, there was estimated to be £100m worth of local government work under contract, that figure had risen to £2,280m by the end of 1994. Around four of every five contracts had been awarded "in-house", to the local authority's own workforce, but typically this was accomplished only as a result of substantial reductions in jobs, pay and conditions of service. Several studies indicate those effects, although estimates as to their extent vary. Local authorities responding to several surveys carried out soon after the beginning of the regime cited productivity improvements as the sources of cost reductions more than any other factor. One showed that, on average, costs were cut by 22 per cent following contracting-out (and by 17 per cent when the work was retained in-house following tendering), with better use of equipment and labour cited as the explanation in both cases.

The Equal Opportunities Commission – an official body – reported in March 1995 that CCT discriminated against women, because such effects as loss of jobs, increased reliance on temporary and casual employment, and deterioration in terms and conditions of employment impacted disproportionately on them. Based on a study of the impact of CCT in 39 local authorities, the research showed that women's employment fell by 22 per cent while men's fell by 12 per cent. In building cleaning and education catering – both female-dominated workforces – male employment actually increased while female employment fell by 31 per cent and 11 per cent respectively in the cases examined. In refuse collection – a male-dominated service – pay levels increased on average, contractual hours remained the same and employment fell by 23 per cent. In building cleaning, a female-dominated service, hours fell by 25 per cent and "pay rates have not generally increased and in some cases have declined, particularly for part-time workers", while employment declined by 29 per cent. The most severely affected workers across the board were part-time women employees, and many had their weekly hours of employment reduced to below a key threshold level (16 hours) for protection of employment rights.

There is some evidence that there was a further tightening of productivity after the first round of contracts expired and a second round of tendering took place in the early 1990s. By the end of the 1990s, however, this was ameliorated to some extent by legal judgements, following cases brought by unions, that workers transferred under CCT were covered by the European Union's Acquired Rights Directive, under which jobs, pay and some other conditions (but not pension entitlements) are protected in the event of take-overs. This was later overruled as a result of a case brought by employers, and there was some legal confusion throughout the late 1990s, as court verdicts see-sawed.

Following a change of government in 1997, CCT was abolished and replaced by a scheme, also compulsory, called "Best Value", under which local authorities are required to review all services, whether provided in-house or by the private sector, on a five-year rolling programme, and to reduce costs by 2 per cent per annum. According to the United Kingdom's main public employees' union, UNISON, there is some evidence of a trend towards reversal of privatization following the replacement of CCT with Best Value, although in some sectors – notably home care services – there appears to have been more contracting out since the introduction of the new rules. More than half of all home care services provided through local authorities were privatized by the beginning of 2001. In addition, UNISON reports that the Best Value requirement to make year-on-year savings is intensifying in-house pressure on workers to drive up productivity, and the union reports the emergence of "two tiers" of employment terms, with privatized workers "invariably" offered, for example, no pensions.

The latter trend has been fuelled not only by the cumulative effects of CCT and Best Value, but also by another significant development in the United Kingdom since 1997, which has been the rapid expansion of public-private partnerships through a mechanism called the Private Finance Initiative (PFI). Under this scheme, public bodies, including local authorities, engage private companies to design, build, finance and operate facilities and then buy services from them under long-term (typically 25 years) contracts. This has had the effect, among others, of transferring the workforce to private sector employment, although the possibility of combining PFIs with continued public employment of the affected workforce is now under consideration in the health service.

Source: Documentation provided by the organizations quoted, and personal interviews with UNISON officials.

2. Globalization, public services and privatization

2.1. International economic integration and privatization

International economic integration, in the forms of both globalization and regionalization, has been among the most powerful of the forces driving change in the roles and relationships of state and market, and in the structure and organization of public services, and has in turn been further facilitated by privatization. One investment consultant, with the firm Scudder, Stevens and Clark, made the point succinctly quite early in the period in which the major focus of privatization was switching from industrial enterprises to public services. "Privatization is being driven by the shift of important economic sectors to operation on a global scale", he told a conference for potential investors in developing countries' utilities. [1] His point was echoed at around the same time by a leading official of the United States Agency for International Development (USAID), which was then devoting considerable resources to privatization, who explained the growth of her agency's involvement by noting: "Industries such as telecommunications, finance and energy are being restructured to respond to the needs of an integrated world economy. The global structure of these industries demands their participation in the privatization process." [2]

Globalization has also shaped the development of public services in many other ways. One general way has been through its contribution to downward pressure on public spending and investment, as countries compete for foreign investment and promote the international competitiveness of domestic business. Until quite recently it might have been quite contentious to claim – as many, including labour unions, have done – that transnational corporate interests held more sway with national and local governments than domestic social interests. Now it is fast becoming a commonplace. As the European Editor of the *Financial Times* has put it: "It is not politicians who are driving change in Europe – it is the private sector. This has been true for 15 years as Europe's single market has moved into full swing. But the trend has accelerated as a result of the launch of the euro [the new single currency shared by several European Union (EU) members], privatization, the explosion of information technology and telecommunications, and globalization." [3] It is in this context that the terms which have shaped regional economic integration can be understood. For example, the EU has required convergent reductions in external debt and fiscal deficits – to 60 per cent and 3 per cent of GDP respectively – in preparation for entry into the euro, under the terms of the Maastricht Treaty. This has added to and focused the more general pressures on municipalities to find ways to reduce their costs, which in turn has helped to fuel privatization at the municipal level.

[1] L.Y. Rathnam: "Investment in the privatization of state-owned industries by institutional investors", a paper presented at the International Privatizations: Investment Opportunities Conference, International Business Conferences, New York, 20 February 1991.

[2] Speech to Adam Smith Institute, Fifth International Conference on Privatization and Commercialization, London, 24-25 June 1991.

[3] L. Barber: "Europe seeks a third way to prosperity", in *Europe reinvented*, a *Financial Times* supplement, Jan. 2001.

The regional dimension of international economic integration has also applied some more direct pressures to privatize public services. For example, the North American Free Trade Agreement (NAFTA) has encouraged convergence in the gas and electricity markets of its three member States, which has influenced the nature of structural change in those sectors. [4] It is also encouraging privatization in the Canadian health services. [5] Similarly, the Asia Pacific Economic Cooperation (APEC), which links 18 countries, has "increasing significance for future policies relating to utilities" according to an ILO publication, which adds: "Water, electricity and gas utilities are all covered by APEC policy on infrastructure, which is for competition, full cost pricing and removal of subsidies, and private investment, with some attention given to environmental issues." [6] The EU is also requiring liberalization – and, in effect, encouraging privatization and transnationalization – of a steadily expanding number of public services. However, unlike other regional institutions of economic integration, the EU also has a social dimension, reflected, for example, in emerging policy about the obligations of public service providers, whether public or private sector. In September, 1996, the European Commission (the EU's executive body) adopted a Communication on "Services of a general interest in Europe", which set out certain principles which providers of the services covered by it should adhere to, including an imprecisely worded commitment to universal access.

2.2. Pressures for greater efficiency and quality

Pressure on the national and local state to make more efficient and effective use of public finance has come not only from business interests, however, but also from society more broadly.

In richer countries, electors appear to support political parties committed to lower taxes, while citizens have also expected public services to meet changing and growing areas of need more effectively, and have become less prepared to tolerate inefficiencies, poor quality, rigidity and lack of responsiveness. Not only economic changes but also a range of cultural changes – such as decline in deferential attitudes to the State and to professions – have influenced these trends. Awareness has grown that, however noble in its intentions and suited to its time might have been the earlier widespread public administration model of providing standard services through monolithic institutions and organizations, it needed to adapt to modern conditions. As the private sector demonstrated increasing willingness to provide in different ways for different segments of their customer bases (differentiated by varying ability to pay, among other dimensions), many people increasingly wanted more choice and flexibility from public services too. Privatization has been seen by many governments as a way to respond to these pressures at the same time as lowering the cost of public service provision.

In many poorer countries, on the other hand, incapacity of the State, especially at municipal level, has produced a growing gap between economic, social and environment need, on the one hand, and service provision, on the other. In circumstances in which there is also under-employment and, to varying extents, substantial community self-

[4] B. Martin; N. White: "Privatization and restructuring of electricity, gas and water utilities in the United States and Canada", in L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998, p. 211.

[5] C. Fuller: *Caring for profit*, New Star Books, 1998.

[6] M. Paddon: "Restructuring and privatization of utilities in the Asia Pacific region", in L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998, p. 45.

organization, decentralization of responsibility for service provision to non-state bodies has been seen increasingly as a way to close the gap.

These pressures on governments have been exacerbated by other trends, not least among them being demographic change, which has not only added greatly to the burden on public finance generally but also forced a rethink of the extent of the state's responsibility for social welfare. While many (mainly the richer) countries are dealing with ageing populations, and others (mainly the poorer countries) are experiencing population growth particularly among lower age groups (facts, it is worth mentioning, for which the success of public services as well as economic growth can take credit), all have been pushed in part by these demographic trends into narrower targeting of what the State does and pays for, and wider engagement with the private and "third" sectors in service delivery.

A range of other pressures from society has also helped to drive the privatization trend. These have included increasing concern about the environment, which has forced national and local states to rethink the way some services – such as electricity supply, water supply, sewage disposal and solid waste disposal – are provided. These pressures do not necessarily point towards privatization, but they have combined with other pressures, especially financial pressures, in ways which have pushed national and local states to look to the private sector for affordable solutions to growing challenges.

2.3. Technological change as a driving force of privatization

As well as being a contributory factor to the social, economic and cultural trends mentioned above, technological change has also contributed more directly to the privatization trend. Its significance in driving privatization varies across sectors, but was undoubtedly particularly great in the case of telecommunications, which is a highly important sector not only for obvious intrinsic reasons but also because its privatization, and the techniques developed in the course of it, have paved the way in many countries for the application of the lessons of that experience to other utility services.

In telecoms and in some other areas of public service, as well as creating new markets and facilitating convergence between economic sectors, technological development has enabled the emergence of a competitive environment in some fields which had previously been natural monopolies. This has encouraged the disaggregation of some areas of public service. For example, while electricity transmission remains, like the fixed network parts of other utilities, a natural monopoly, generation and distribution have become contestable. [7] Perceived as being consistent with consumer interests, by enabling choice, the trend has been to open up such sectors to competition, which has, in turn, fuelled the emergence and growth of companies focused on the new markets.

[7] This is explained not only by technological development, but also by other sources of change in ideas about how public services should be run. Those ideas continue to change, however, on the basis of privatization experience. While the conventional definition of "natural monopoly" was based on market failure arising from economies of *scale*, it has become increasingly accepted that market failure also arises from economies of *scope*, which arise from the cheaper cost of providing a range of services, both contestable and non-contestable, than of providing each separately.

2.4. New business interests and privatization

Many firms have been eager to enter or expand their interests in these growing markets. Indeed, privatization has itself created a new and growing business interest in the form of (increasingly transnational) companies in sectors previously largely the preserve of the State. In addition to banks, accountancy firms, management consultancies, legal practices and other businesses which profit from their involvement in privatization (and, therefore, have much incentive to promote it), each utility sector is now dominated on a world scale by a handful of companies. They form a significant lobby on governments, and on international finance institutions and aid agencies, for the release of new markets through further privatization. There is, in fact, a discernible spiral effect, characterized by the spread of privatization in public services, the resulting expansion of transnational business involvement in delivering them, the growing economies of scale enjoyed by these companies, and, as a result of that, some undermining of much of the original logic for state investment.

New commercial opportunities have opened not only *in* those areas of public service in which competitive markets have been created, but also *for* the market in those areas of public service which remain natural monopolies. In addition to increasingly favouring privatization of contestable areas of public service, governments have also increasingly privatized monopoly parts of public services, using contracts or regulation to attempt to reconcile the public interest with the commercial interests of private providers.

2.5. Privatization as a vehicle for capital investment

The spiralling trend discussed above has been fuelled by the growing capital demands of public services and their infrastructure. As well as needing to modernize technologically, public services have also suffered from growing investment backlogs, which have fuelled general dissatisfaction about the performance of state-owned enterprises because of the effects of under-investment on efficiency and quality of service. “During the 1980s and early 1990s, the average waiting period for telephone installation in Indonesia was nearly eight years, in the Philippines seven years, and in the former Soviet Union and in Pakistan ten years”, report Max Iacono and Dennis Rondinelli for the ILO, adding: “In Thailand customers had to wait an average of three years to receive telephone services and by 1989 the waiting list in Bangkok alone had grown to more than 300,000 applicants. Moreover, even when telephones were installed, service was often poor. Call completion rates were extremely low in many developing and socialist countries because of faulty equipment and lack of switching capacity.” [8]

A widening gap between the capacity of public service organizations and the needs and expectations of their business and social users has been evident in other sectors too. Indeed, the scale of the telecommunications under-capacity mentioned above in Bangkok has been dwarfed by the problems such rapidly growing urban centres have experienced in other areas of economic and social infrastructure, such as energy and water supplies, sewage and solid waste disposal, and public transportation and roads. Such problems have been experienced in even the wealthiest countries; a major element of the rationale for water and sewage privatization in the United Kingdom, for example, was that the infrastructure was so old and neglected that public authorities did not even know the location of many of their assets, much less their condition.

[8] D. Rondinelli; M. Iacono: *Policies and institutions for managing privatization: International experience*, ILO, 1996, p. 11.

2.6. Public finance deficits and privatization

The capacity of government spending to invest in technological modernization and to tackle investment backlogs in the 1980s and 1990s was undermined in many countries by high levels of external debt and fiscal deficits, hanging over from the oil price shocks and other developments of the 1970s. "The crisis came almost universally in the early 1980s", reports one account. "The terms of trade suddenly worsened, exacerbated for non-oil exporting countries by the exogenous second oil price shock of 1978, causing drastic deterioration in the balance of payments." [9] At the same time, politicians have become increasingly convinced that people will not vote for parties which openly increase tax levels, and have devised many ways to reduce or even eliminate corporation tax, on the grounds that investment would be repelled otherwise. The combined effect of these and other pressures has been to prompt governments to seek ways to secure investment in infrastructure and service provision without increasing public debt, and to drive up productivity.

Those problems confronted municipal leaders in highly indebted countries especially, and privatization as a solution to them offered the additional benefit of bringing in foreign exchange or swapping debt for equity. Privatization became a standard component of conditionalities attached to loans and other financial assistance from international financial institutions to countries tackling structural economic and fiscal challenges. However, similar financial pressures on a lesser scale have challenged municipal politicians and public service managers in even the richest countries. In the United States, for instance, scarcity of public capital has combined with higher environmental standards (resulting from campaigns by consumer groups and environmentalists) to fuel the rapid spread of privatization of wastewater treatment. As one mayor has put it: "I need capital to finance improvements in my old plant, I'm being fined daily for not meeting environmental regulations, more stringent standards are on the way, and the private firms are willing to take over my operation for 15-20 years, make the necessary capital improvements, and stabilize rates. This is a hard deal for a mayor to turn down." [10] However, the capital demands of public services globally remain much greater than can be satisfied by private sources, and, in the context of ever tighter public finance, this has strengthened the private companies' bargaining position, affecting the terms on which privatization has taken place.

2.7. International financial institutions and aid agencies and privatization

The IMF and World Bank have been highly influential in promoting privatization of public services and in the design of mechanisms, programmes, measures and implementation strategies for nearly two decades. Privatization in various forms became a standard component of conditionalities attached to structural adjustment loans during the 1980s, and continuing into the 1990s, in a way that was colourfully, if contentiously, described in an open letter of resignation from his job with the IMF, dated 10 January 1989, by the Trinidadian economist Davison L. Budhoo: "About five years ago", he wrote, "President Reagan effectively told us to go out and make the Third World a new bastion of free wheeling capitalism, and how we responded with joy and with a sense of mission! ... Everything we did from 1983 onward was based on our new sense of mission to have the south 'privatized' or die; towards this end we ignominiously created economic bedlam in Latin America and Africa in 1983-88."

[9] P.M. Jackson; C.M. Price: *Privatization and regulation: A review of the issues*, Longman, p. 239.

[10] Quoted in a briefing by the United States public service workers' union AFSCME.

That was a minority viewpoint among IMF-World Bank staff, and few would express misgivings in the same robust language even now, but its content, tone and language resonates with how many at the receiving end of the agencies' prescriptions experienced both the processes by which their governments adopted new policies and the effects of those policies. The approach of the institutions has become more consultative and less dogmatic since then, and there has also been considerable reconsideration of the respective roles of the State and the market in development. However, if the IMF and World Bank have learned much about the need for consultation as part of endeavours to tailor public service policies more to national conditions, they remain strongly convinced of the benefits of privatization and committed to promoting and facilitating it, in the belief that it forms an indispensable part of programmes to create stable conditions for economic growth and to alleviate poverty in the long term.

The institutions' role in relation to privatization has, in fact, not only changed but also expanded greatly in recent years, from that of promoting privatization through conditionalities and providing corresponding technical assistance, to increasingly underwriting and arranging privatization deals and funding mass retrenchments. The World Bank did the latter for the first time openly with the dismissal of 90,000 railway workers in Argentina in 1995, while the Bank's changing role in bringing private capital into public service investment and delivery has been reflected in the growing involvement of its private sector arm, the International Finance Corporation (IFC), in arranging and financing privatizations, in the cases of water supply and sewage disposal in Buenos Aires and Manila, for examples. Indeed, during 2000, the World Bank's Private Sector Development Department was effectively transferred to the IFC.

Regional development banks have also played a considerable role in promoting and facilitating privatization of public services, while some bilateral aid agencies have performed a similar role, as mentioned earlier in relation to USAID. The rapidly increasing number of concession contracts involving French transnational water and utility companies (which dominate the world water market) and the French state-owned EdF electricity supply company in Africa, for example, has been achieved with the financial support of the country's bilateral aid agency, the Caisse française de développement. [11]

Parallel to the changing political approaches and roles of both multilateral and bilateral aid agencies in relation to privatization has been a changing focus of their technical advice. There has been a growing interest and involvement in the design of state institutions appropriate to the privatization context, such as regulatory bodies, reflecting a rehabilitation in the thinking of the institutions about the important role of the State. In preference either to the pre-privatization role of the state as planner, investor and provider, or to its subjugation to the market in the later neo-liberal model, it is now seen more as enabler, facilitator and monitor of development through the private sector.

Box 3
Water privatization in Buenos Aires

Privatization of the water service in Buenos Aires was promoted and facilitated by the IFC, which provided most of the resulting investment and also took an equity stake in the company, Aguas Argentinas, which was awarded the 30-year concession beginning in 1993. The company's dominant owner is a French transnational, Suez-Lyonnaise des Eaux. The IFC has promoted this case as an international model. According to an IFC report on the project:

[11] P. Plane: "Privatization of water and electricity in Africa", in L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998, p. 21.

> Assisted in part by broad-based assistance from the World Bank and IFC over an extended period, Aguas Argentinas has engineered an extraordinary turnaround of a state enterprise in decay into an efficient, viable private company. The residents of Buenos Aires have been the main beneficiaries. For the first time, chronic water shortages have been eliminated. Both the quality and quantity of potable water have been increased. Water tariffs paid by consumers have been cut. An ambitious capital expenditure programme is being carried out making it possible for the first time to extend water and sewerage services to the poor with accompanying improvements in the environment and public health. [1]

As that testimony suggests, there were strong social and environmental cases, as well as economic reasons, for radical change in the city's water services. While the city's wealthy were able to overcome water shortages by constructing storage tanks, the poor had to live with them, or worse. Untreated sewage was dumped into the River Plate and drinking water was contaminated with high concentrations of nitrates, bacteria, arsenic and heavy metals. Three million people had no choice but to draw upon wells which were polluted, or had to buy water from street vendors at prices which, typically, demanded a far higher percentage of their income for supply than the better off had to pay for better supply.

It is estimated that nearly 80,000 annual cases of water-borne disease, leading to more than 100 fatalities a year, were resulting from these deficiencies. The State's capacity to tackle them was undermined by the fact that Argentina was spending a large proportion of its tax revenue on servicing external debt, and was exacerbated by the water utility's failure to collect bills even from many of those able to pay, apparently as a result of inefficient management and financial systems.

According to the IFC account, Aguas Argentina renegotiated a number of contracts, changed certain systems, cut clandestine connections, collected more bills and installed more meters, at the same time as reducing average (but not all) tariffs. Around half of the 9,000 workforce were retrenched, while pay and training for the remainder were improved and there was a great increase in subcontracting.

Less than three years into the 30-year concession, however, the deal was being renegotiated. A serious problem had arisen which challenged the central social rationale for the project. Although the terms of the concession required the provision of infrastructure to poor neighbourhoods – the IFC itself provided more than half of the US$930m planned capital investment – it was becoming clear that the poor would not be able to afford the projected tariffs. "Although ability to pay for water and sewerage services is not a constraint for those above the poverty line", states the IFC report, "evidence indicates that it is for those classified as poor ... and although the poor potentially are to be the major beneficiaries of the investments to be carried out under the concession agreement, existing incentives favour expansion of service to those with the ability to pay."

The scale of this problem, and its implications in terms of social justice and political instability, was demonstrated when riots broke out in one poor neighbourhood of the city, where the concession – with a monopoly protected by law – began to provide piped-water services to residents who had been buying from street vendors at prices amounting to about a tenth of the average Aguas Argentinas bill. [2] In early 1997, Aguas Argentinas initiated a renegotiation of the concession contract which was finally approved in 1998 and which led to the creation of a new tariff structure including some cross-subsidy. The social and environmental impact of the Aguas Argentinas experience remains, however, to be fully evaluated.

[1] F. Jaspersen: "Aguas Argentinas", in *The private sector and development: Five case studies*, International Finance Corporation, 1997, pp. 15-16. [2] T.M. Solo: "Competition in water and sanitation: The role of small-scale entrepreneurs", in *Public policy for the private sector*, World Bank, Washington, DC, Dec. 1998.

2.8. The OECD and privatization

Another international institution which has been influential in shaping and promoting reform of public services has been the Organisation for Economic Co-operation and Development (OECD), which has a dedicated Public Management Department. The OECD has advocated a "new paradigm" characterized by a greater focus on results and increased value for money; devolution of authority and enhanced flexibility; strengthened accountability and control; a client and service orientation; strengthened capacity for developing strategy and policy; introducing competition and other market elements; and changed relationships with other levels of government. [12] The OECD expects reforms in those categories to continue and to produce "in the decades to come", a "well-performing

[12] *Governance in transition*, OECD, 1995, p. 25.

public sector" that "will be radically different in appearance and behaviour" and which, typically, will be less involved in direct service provision.

2.9. The World Trade Organization and privatization

The role of the World Trade Organization (WTO) in relation to privatization has been less prominent than that of other global intergovernmental organizations, but this is changing, chiefly as a result of the General Agreement on Trade in Services (GATS). Through various of its agreements and associated institutions, the WTO has already had a major impact on public services. The roles of the Agreement on the Application of Sanitary and Phyto-Sanitary Measures (affecting, in particular, food standards regulation) and of the Trade-Related Aspects of Intellectual Property Rights (TRIPS) have been especially significant.

GATS, negotiated during the Uruguay Round of trade talks and finalized in 1994, established a framework for liberalizing international trade in services for the first time. It extended to services the approach historically applied to trade in manufactured goods and commodities under the General Agreement on Tariffs and Trade (GATT). Initially, GATS provided for no more than a general "standstill" agreement under which WTO members agreed not to implement any new tariffs, quotas or other restrictions on the international trade of services. However, it also authorized negotiations among subgroups of WTO member governments to liberalize trade in specific service sectors, a provision resulting in two 1997 agreements covering the financial services and telecommunications sectors. It also mandated further rounds of negotiations about other services, the first of which, now underway, is supposed to be completed in 2002 (but probably will not be, because of slow progress so far).

Under the GATS as it stands, member countries negotiate "schedules" in which they "commit" to certain principles. Among these are the right of foreign enterprises to engage in commercial activities in a country's market (the right of establishment); equal treatment of foreign and national enterprises under domestic law (national treatment); and non-discrimination in the treatment of enterprises from all WTO member nations (most-favoured nation, or MFN, treatment). Each WTO member decides which sectors are covered by or exempted from their GATS commitments and the degree of liberalization in each. However, the overriding purpose of the GATS is to liberalize trade in services and to promote effective market access to all sectors for business enterprises of all nations. There is no special provision for "public services" – indeed, GATS recognizes no intrinsic distinction between public services and other services. It does enable exemption from the application of WTO rules of any activity deemed to be governmental rather than commercial, but the existence in a member country of *any* private commercial operations in a particular sector could have the effect of exposing that *whole* sector to unlimited international competition, on the grounds that the existence of commercial operations in the sector is in itself proof that it is not exclusively governmental. Therefore, privatization in any public service sector could have the effect of opening the whole of that sector to privatization under WTO rules. [13]

[13] For a more detailed description and analysis of the significance of GATS in public services, see *Great expectations*, published by Public Services International and Education International, at www.world-psi.org, where links to other sources on this subject are also made.

2.10. The ILO and privatization

In public services, as well as for other economic sectors, the ILO monitors trends, complementing the existing body of information with policy-oriented research on specific aspects. It also organizes regularly international sectoral meetings at which representatives of governments, workers' and employers' organizations discuss topical issues and formulate conclusions and resolutions. [14] In the nature of the changes that have been occurring in a number of sectors in recent years, the ILO's sectoral activities have increasingly addressed privatization.

In addition, the ILO has organized a number of research projects focusing specifically on privatization, such as, in the early 1990s, an Interdepartmental Project on Employment and Structural Adjustment, which investigated more than 20 cases of privatization in seven countries, and, in the late 1990s, an Action Programme on Privatization, Restructuring and Economic Democracy, which produced a number of specially commissioned research documents, one of which focused on electricity, gas and water, and another on health care services. The Action Programme investigated employment impacts of privatization on an unprecedented scale.

"There are two major reasons why the ILO is particularly concerned with the process of privatization", according to a report which emerged from the Interdepartmental Project mentioned above. "First, the ILO has a special responsibility to ascertain that privatization takes place within the context of internationally acceptable agreements on labour standards and labour rights in relation to workers' rights, collective bargaining and social security. The second reason relates to ILO's objective of striving for increased employment and reduction in poverty." [15] The introductory chapter of one of the Action Programme research reports stated that "two basic ILO beliefs" had emerged, namely: "First, that positive measures to provide employment and income security are consistent with restructuring to increase competitiveness; and second, that social partnership and constructive dialogue are prerequisites to identify the appropriate transformations and implement them fluidly". [16]

2.11. Public employees and their unions in the context of privatization

Much of the rationale for privatization has been based upon the idea that private companies and management are capable of producing higher quality and greater efficiency than public sector organizations, all other things being equal, particularly in competitive conditions. The logic behind this idea is that the market and the profit motive produce incentives which are absent in public sector organizations, while the nature of incentives within the latter militate against innovation and experimentation, and, therefore, against competitiveness. This is underpinned by two related bodies of theory – principal agent theory and public choice theory – which combine to produce the conclusion that public servants, motivated primarily by their own interests rather than those of their state

[14] L. de Luca (ed.) *Labour and social dimensions of privatization and restructuring (public utilities: water, gas, electricity)*, ILO, 1998, p. ix.

[15] R. van der Hoeven; G. Sziraczki: *Privatization: A subdued first assessment*, World at Work, No. 10, 1994, p. 10.

[16] L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring (public utilities: water, gas, electricity)*, ILO, 1998, p. xvii.

employers and the people they serve, cannot be trusted to promote the public good. Rather, the public interest is best served through the creation of market structures and/or regulatory environments which provide incentives for private companies (or, as a second best, arms-length commercially run organizations within the public sector) to deliver public service outputs defined so as to achieve public policy goals.

Unions representing public service managers and other employees have long challenged that logic, arguing that the pursuit of private profit tends to be incompatible with the public interest in public services, and that regulatory institutions and market mechanisms have often proved ineffective at reconciling the two. Unions have also argued that public choice theory misunderstands the nature of incentives among public service workers, who are often motivated by vocation and/or professional ethics, and inspired by collective and cooperative rather than individualistic and competitive values. Whilst acknowledging the existence of corruption and patronage in public services, they attribute these characteristics to departure from the public service ethos as a result of poor leadership, systems and/or management, rather than to intrinsic deficiencies in public provision, and they point out that privatization can legitimize and create corruption rather than eradicate it. Unions also argue that low labour productivity in public services is often the consequence of inadequate capital investment, insufficient staffing, low pay and/or inadequate resources for training.

In addition, public service workers and their unions, reflecting wider societal trends, increasingly seek higher quality of working life in addition to pursuing their traditional concerns about employment, employment security and freely negotiated terms and conditions. They increasingly recognize that, in order to reconcile these goals, structural and systemic changes to introduce greater job flexibility into a context of employment security, as well as more decentralized decision-making and "flatter" organizations, are required. Consequently, unions have increasingly urged reform of public service organizations while remaining suspicious about the motivation behind much and probably most privatization, and determined to fulfil their basic mission of protecting their members' interests. They often believe they are insufficiently consulted about public service reform, and that their own increasingly large body of experience, knowledge and examples of efficient and effective alternatives to privatization are not given due consideration by international, national and local policy-makers.

Most public service workers' unions also see themselves as custodians of a wider public interest in relation to the services in which their members work, believing that they have a responsibility to warn of the hazards and costs of privatization and other policies which they see as undermining public services, and to promote alternatives, if and when necessary. In this regard, they are working increasingly closely with representative and advocacy NGOs, from local to international levels, concerned about the impact of public services and privatization on poverty, social justice and the environment, and about the long-term implications for concentration of wealth and power of the increasing domination of public service provision by transnational corporations. They are increasingly advocating alternative approaches which they believe a growing body of evidence demonstrates are capable of combining innovation, flexibility and dynamism with public service values more effectively than privatization tends to achieve.

Public service unions have, nevertheless, been quite pragmatic in their responses to privatization. Many have changed their constitutions to enable them to follow their members into the private sector, and have sought to protect them in the new environment whilst maintaining their arguments of principle in relation to privatization as a policy. In an increasing number of cases, sometimes supported by the legal environment, they have succeeded in negotiating agreements with private providers of public services.

3. The impact of privatization of public services

3.1. Tension between private profit and public interest

A distinguishing feature of public services is that their ethos is informed by a wider range of objectives and responsibilities than that of commercially driven business. Indeed, they owe their existence to market failure of various kinds. Rather than their mission being to maximize shareholder value, they exist to meet a range of economic and social needs in accordance with public policy. For this reason, they are also subject to public accountability and to ethical standards peculiar to their context. They have responsibilities to use public money in efficient and effective ways, which demands disciplines similar to those of private business, but must do so at the same time as meeting standards of fairness and social responsibility not expected of private business. These wider responsibilities extend to employment issues; as well as providing jobs, society in many countries has expected public services to set an example for the rest of the economy in their employment practices.

For many people, these features of public services are precisely their strength, while for others they are sources of weakness. The privatization trend has been associated with rethinking the role and modi operandi of public services. At its extreme, this has taken the form of eradicating the differences between them and other parts of the economy, so that, like profit-oriented business, public services are expected to pursue unambiguously commercial missions. In this context, it is relevant that there is no clear internationally accepted distinguishing meaning of the term “public service”, a fact which takes on increasing significance in the context of GATS (see section 2.9, second paragraph, above).

In the main, however, governments other than those gripped by market fundamentalism do acknowledge, if only implicitly, that there are some services whose role cannot be determined, and whose performance cannot be judged, by commercial criteria alone, even if they are not provided directly by public employees. For this reason, in the context of privatization, they seek to regulate the behaviour of privatized public services through a range of mechanisms and institutions designed to reconcile, or at least balance, commercial objectives and the wider public interest. State ownership has represented one approach to regulation, but in the context of privatization new approaches have necessarily been developed.

3.2. Regulation of privatized services

The challenge of regulating privatized public services is, as one account has put it, “to configure the economic system so that individual economic actors achieve allocative efficiency for the wider society”. [1] (Allocative efficiency is a measure of the extent to which resources are distributed in accordance with their optimal return, whereas operational efficiency is a measure of the extent to which they are then managed in accordance with their optimal return.) Arrangements for enforcing compliance with rules and standards held to be consistent with public policy fall into two main categories: oversight of private providers by state agencies; and contracts. There are, broadly, two

[1] P.M. Jackson; C.M. Price: *Privatization and regulation: A review of the issues*, Longman, p. 12.

distinct approaches to regulation by state agency (as distinct from contract). One is a participatory approach, as modelled by the public utility commissions at state level in the United States, in which open hearings enable interested parties to cross-examine company representatives and expert witnesses as part of a process through which the public interest is defined. The other is a bureaucratic approach, in which public policy, rather than being shaped through the regulatory process, is broadly defined by law and government, and interpreted and enforced by officials of the responsible agency.

In defining the differences between regulatory approaches in that way, this paper departs from the conventional distinction made between "rate-of-return" and "price cap" regulation, and it does so for three reasons. The first is that, especially in the context of the ILO's structure and concerns, it seems important to highlight the distinction between bureaucratic and participatory approaches which is overlooked by the conventional distinguishing criteria of alternative mechanisms. The second is that the difference between those mechanisms – "rate-of-return" and "price cap" regulation – is in any case steadily eroding. And the third is that, while participatory approaches can be designed to regulate not only prices charged to service users but also other aspects of the behaviour of private providers of public services, bureaucratic approaches typically involve separate agencies regulating the various aspects (prices, environmental impact, safety, and so on). The consequence of the latter approach is either a multiplicity of regulatory agencies, a state of affairs which can be both inefficient and ineffective, or undue neglect of aspects of corporate behaviour other than prices.

That said, the main focus of regulation of privatized public services has indeed been on prices. The aim is to combat monopoly abuse by controlling the revenue of private providers to some extent by controlling the prices they are permitted to charge. This is done by setting prices at levels which optimize the balance between commercial viability and public interest considerations, such as environmental protection, universal access to services, and public safety. Rate-of-return regulation involves arrangements (possibly including, as in the United States model, public hearings) through which a range of factors, such as necessary levels of investment, are taken into account before a permitted rate of return is set and tariffs determined accordingly. Price cap regulation of the kind pioneered as part of the process of privatizing utilities in the United Kingdom does not specify permitted rates of return. Rather, its focus is on setting upper limits on packages of prices by allowing them to rise at the same rate as prices generally (Retail Price Index (RPI), to use the British term), less an element (x) predicated on productivity improvements (hence RPI – x), plus (in some cases) an element (y) allowing for investment finance (hence RPI – x + y).

A weakness of rate-of-return regulation which has long been acknowledged in the literature is its tendency to provide incentives to overcapitalize without applying downward pressure on costs, and these perceived deficiencies produced the rationale for the creation of a new approach in the context of privatization. Price cap regulation was the result. Inevitably and increasingly, however, price cap regulators have had reasonable rates of return in mind in the course of setting prices. As Catherine Price has commented, while price cap regulation is cheaper to administer and provides incentives to reduce costs:

> Such benefits remain however only so long as the determination of the level of price cap is exogenous to the industry and the firm cannot affect its level. If the industry believes that the regulator will choose the cap according to the firm's performance then it will adapt its behaviour accordingly. Since regulators have few criteria other than rate of return to determine the appropriateness of

price levels, the necessity to review the price cap induces the firm to reduce rate of return, and introduces the familiar incentives to overcapitalize. [2]

The dynamic which has emerged in the process of price cap regulation is one in which, driven to make efficiency improvements, but expecting these to be passed on to consumers by the regulator over time by means of a tighter price cap at the next review, "the constraint becomes a hybrid with some elements of the costs and advantages of both price cap and rate-of-return regulation". That is why the difference between the two approaches has eroded.

Contracts between the State and private providers of public services are also designed to enable the latter to meet the former's requirements whilst remaining commercially viable, and balances are struck accordingly. Typically, they impose upon the providers a range of targets arising from public policy and include agreements defining limits on price increases or arrangements for setting prices. These agreements can prevent providers from imposing price increases except by agreement with the state body to which they are contracted. However, like regulation by agency, these arrangements, as the Buenos Aires water case (see box 3) demonstrates, develop their own dynamic over time.

3.3. Evaluating the impact of privatization on public service performance

In the context of regulation of privatized services, therefore, as well as in wider evaluation of the impact of privatization, a key issue is how productivity, efficiency and other categories of achievement are defined, and in accordance with what criteria, information and techniques of measurement. Definitions of terms such as "efficiency" and "effectiveness", and of the distinctions between them and the relative priority accorded to each, are, therefore, of central importance, especially in the context of evaluating the impact of privatization on the "quality" (another key term with contentious meaning) of service.

The challenges associated with these issues have been highlighted by productivity specialist Evan M. Berman, who defines productivity as "the effective and efficient use of resources to achieve outcomes". [3] Yet, as an example of "outcomes" – another key term – the author offers "the number of arrests made by police officers". Other commentators (myself included) would define that as an "output", as distinct from a corresponding "outcome" of crime levels. Lucy Gaster, commenting on the British scene, has pointed to a similar problem: "In the early 1980s", she has written, "it was a struggle to get anything other than 'value for money' on to the public agenda. The ideals of economy (least cost inputs) and efficiency (highest outputs in proportion to inputs, or unit costs) were apparently displacing public sector values such as fairness and altruism. 'Effectiveness' can be defined as the achievement of objectives and (possibly) increasing the 'public good'. However, it was a less powerful value than the first two, largely because of the (continuing) difficulty of devising suitable measures for it." [4]

This discussion might appear to be straining at gnats, but the distinctions being stressed here, and the way in which difficulties of both definition and of measurement have

[2] P.M. Jackson; C.M. Price: *Privatization and regulation: A review of the issues*, Longman, p. 82.

[3] E.M. Berman: *Productivity in public and no-profit organizations*, Sage, 1998, p. 5.

[4] L. Gaster: *Quality in public services*, Open University Press, 1995, p. 13.

influenced policy, have significant practical impact. For example, some privatized utilities in the United Kingdom have reduced greatly the number of people disconnected from supply for failure to pay their bills, after public disquiet in the period soon after privatization when the number of consumers being disconnected from water supply rose sharply, especially in relatively poor areas. However, they have also greatly increased the number of people whose homes have pre-payment metres, and who effectively cut off their own supply by failure to pay for it in advance. Thus can a performance indicator – the number of consumers disconnected from supply for failure to pay their bills – distort the reality of the extent to which the intended outcome – that the poor should be able to afford to pay for water supply – is achieved. Regulatory rules can have a similar effect. For example, price cap regulation typically limits not particular charges but the average of a package of tariffs, thus allowing companies to "rebalance" their tariffs between consumers. In telecommunications, this has tended to enable companies to reduce prices in competitive parts of their services, such as long distance, while increasing them well above the average in monopoly parts, such as local calls. That in turn has applied downward pressure on demand for those services, enabling companies to claim truthfully that they have cut waiting lists for supply.

In addition to challenges of defining what should be measured and devising criteria by which to measure, there are practical problems about how to measure performance in relation to those criteria. There are many confounding variables because privatization generally takes place in the context of other developments and policies. As a result, even to the extent that it is possible to measure the pre- and post-privatization realities, it is much more difficult to specifically link cause and effect. In addition, even to the extent that they can be measured, a comparison of pre- and post-privatization realities is an unsatisfactory methodology, since a truer comparison would be with counter-factual possibilities. An argument can often be made that, in the context of tightening public finance and even virtually bankrupt enterprises, the alternatives to privatization would have produced worse outcomes, while an equally strong case could be made in other circumstances for arguing that alternative approaches to reform would have produced better results.

Resort to more easily defined measurement criteria, allied to the change in ethos which (unless effectively corrected through regulation) would be expected to occur when a public service is transferred to a profit-seeking company, has certainly had an impact on the way on which the performance of privatized services has been evaluated, and, indeed, on the way in which the case for privatization has been made and its implementation designed. As Berman has noted: "There is consensus that efficiency is typically a more important goal in the for-profit sector, whose success tends to be singularly defined as profit. Some business texts even define productivity as efficiency." [5]

The way in which these issues have found expression in privatization policy has been demonstrated by Sunita Kikeri of the World Bank, who has written in relation to Mexican telecommunications before privatization that "by the end of 1990, labour productivity was about half the international standard (10.5 workers per 1,000 lines)", and added:

> Overstaffing is rampant in other infrastructure sectors as well, at both national and municipal levels. Power utilities in many African countries, as well as in India and Pakistan, are severely overstaffed, with fewer than 50 customers per employee (compared to more than 200 in countries such as Chile, Indonesia and South Africa). Production per employee is also low, with a median of 379 megawatt-hours per employee (compared with about 3,000 in industrial countries). ... Overstaffing is also common in water and ports. In Pakistan's water system for Islamabad, for example, there are 45 staff per 1,000 water

[5] E.M. Berman: *Productivity in public and no-profit organizations*, Sage, 1998, p. 7.

supply connections, compared with three staff per 1,000 water connections in efficient water companies in Latin America. [6]

Whilst statistics of that kind can be of great value in benchmarking performance, to the extent that they drive policy without regard to context they can lead to perverse outcomes, since differences might be explained by factors other than relative levels of efficiency.

3.4. Privatization's impact on productivity

Measuring financial efficiency and labour productivity in the above manner, as a ratio of outputs to inputs, there is no doubt that privatization has been associated with dramatic increases, but the causes vary. In some cases, renegotiation of contracts with suppliers has been a highly significant cause. Ravi Ramamurti reports that Argentine telecoms slashed its procurement costs by as much as half as a result of a threat to buy from an alternative source. [7] In the United Kingdom, post-privatization electricity generators had dramatically lower costs than they had had under state ownership, but this had little to do intrinsically with privatization. Much of the reduction was the product of a flood of imported coal after a change of government policy which followed the defeat of the British miners' strike in 1985. [8] However, the other key factor in overall productivity increases in United Kingdom electricity was that "among the non-fuel costs, it is clearly in employment terms that the new companies have made their major efforts to reduce costs".

On an international scale, Ravi Ramamurti reports an "explosive growth in labour productivity" following privatization of utilities. He identifies the causal factors as: freezing the size of workforces while output increased; cutting the workforce (by 50 per cent or more), while also recruiting younger workers with more modern skills; greater labour flexibility; and reduced pilfering. "Unlike the Government, private owners did not regard employment creation or its preservation as an objective of the enterprise". [9] The privatized utilities were "ruthless" with white-collar jobs as well as manual ones, according to Ramamurti, with departments closed or consolidated. The result was a 13 per cent increase in lines per employee in the first three years after telecommunications privatization in Mexico, and a 19 per cent increase over the same period in the same sector in Argentina.

ILO research reveals similar findings in electricity and water services, all over the world, although the detail and the factors influencing the productivity changes vary. [10] These factors will be discussed in subsection 3.5, while the relationship between productivity increases and service outcomes will be explored in subsection 3.6. Evidence

[6] S. Kikeri: *Privatization and labor*, World Bank, undated, p. 4.

[7] R. Ramamurti: "The new frontier of privatization", in R. Ramamurti (ed.): *Privatizing monopolies: Lessons from the telecommunications and transport sectors in Latin America*, John Hopkins University Press, 1996, p. 27.

[8] G. MacKerron; J. Watson: "The winners and losers so far", in J. Surrey (ed.): *The British electricity experiment*, Earthscan, 1996, p. 202.

[9] R. Ramamurti: "The new frontier of privatization", in R. Ramamurti (ed.): *Privatizing monopolies: Lessons from the telecommunications and transport sectors in Latin America*, John Hopkins University Press, 1996, p. 28-29.

[10] See, L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998.

about the impact of contracting-out of other municipal services reveals similar impacts, which are also explored further in subsections 3.5 and 3.6, as well as in box 2 above.

Box 4
Restructuring, privatization and labour in Côte d'Ivoire railways

Côte d' Ivoire railways employed 6,000 workers in 1985, a number reduced by 10 per cent by 1988, as part of a restructuring exercise. This was followed by a change in senior management and a further restructuring programme, carried out with no consultation with the workers' union, which resulted in a third of the workforce leaving. However, it soon became clear from operational difficulties that there had been too many redundancies in some key areas, notably signalling and security. Moreover, investment in infrastructure and rolling stock did not increase, and the company had to pay some of its remaining workforce overtime as a result of the impact of capital deficiencies on labour productivity.

In March 1993, a new stage of restructuring began, in which the union was involved, and this led, according to company documents, to more commercial attitudes among staff, a reduction of fraud by 30 per cent and a 60 per cent increase in availability of locomotives (a good sign of maintenance efficiency).

In 1995, the railway system was privatized as a company named SITARAIL, led by the French transnational SAGA, and was awarded a concession to run services and to rehabilitate the infrastructure. Three per cent of its equity was allocated to staff. However, SITARAIL further reduced its workforce by more than half, from around 4,000 to 1815. The unions asked for information as to how further labour restructuring would be carried out, but the government ignored the request. This led to a strike, and workers displayed such tactics as blocking the centre of the capital, Abidjan, with a locomotive. Negotiations started a few days later. Eventually, details were provided and the union argued up the severance terms to the equivalent of 14 months of wages, double the initial offer. Also conceded by SITARAIL was an agreement to favour companies created by former employees when looking for subcontractors; track maintenance, company car fleet management and printing of timetables and tickets have been contracted out to such firms as a result. SITARAIL also agreed to give preference to workers made redundant in 1995 when recruiting new staff. However, those workers are treated as new employees for the purposes of pay determination, which is a significant condition, because SITARAIL has abandoned the pay scales in operation before the concession began, replacing them with a new system in which there is a lower basic wage but more allowances and bonuses, some related to performance. The overall impact on pay levels is not clear. Average pay has increased, but the sharp increases awarded to managers to raise their salaries to private sector market levels distorts the average considerably.

The company health insurance programme enjoyed by the workers before privatization was privatized through a contract with a separate company, financed by contributions from both the workers and SITARAIL. Although on paper it is a worse arrangement for the workers than the social protection provided to them and their families through their employment prior to privatization, in practice the state employees' funds had come to be heavily in debt as a result of the Government failing to pay its contributions, and most employees no longer even applied to the fund for reimbursement of medical expenses. In effect, therefore, according to their union, the new health scheme is better, and working conditions have also improved since privatization.

According to officials at the Comité de Privatization, out of the CFA fr.40 billions planned investment in rehabilitation of the railway, SITARAIL itself has been obliged to raise only CFA fr.8 billions, of which CFA fr.3.5 billions is a loan from the Caisse Francaise de Development (CFD), the French bilateral aid agency. The rest is state-guaranteed loans provided by multilateral and other bilateral aid agencies.

Regulatory oversight of SITARAIL has proved difficult, according to officials at the agency established for the task, who admit that it is technically very difficult for them to control the company's activities because they have insufficient capacity, especially human resources, to check the accuracy of information.

Source: B. Martin and M. Micoud: *Structural adjustment and railways privatization: World Bank policy and government practice in Ivory Coast and Ghana*, ITF.

3.5. Privatization's impact on labour relations, pay and working conditions

A study of the effects of contracting-out in a range of municipal services in several United States cities and towns shed some detailed light on the factors which increased productivity following privatization. It found that:

> Generally speaking, the productivity gains through contracting do not result from low wages; they result from more work performed per employee per unit of time. ... The observed cost difference is accounted for by the fact that contractors: (1) provide less paid time off for their employees (less vacation time and fewer paid absences); (2) use part-time and low-skilled workers where possible; (3) are more likely to hold their managers responsible for equipment maintenance as well as workers' activities; (4) are more likely to give their first-line managers the authority to hire and fire workers; (5) are more likely to use incentive systems; (6) are less labour intensive (i.e. they make greater use of more productive capital equipment); (7) have younger workforces, with less seniority; and (8) have more workers per supervisor. [11]

If the relevance of those factors is general across cases, the extent to which each applies is more particular between cases. Therefore, the consequences of privatization for labour relations, pay and other terms and conditions varies greatly.

Other studies have also shown a similar pattern – that is, a consistent set of factors affecting the impact on labour, but great variation in the extent to which those factors apply, and, therefore, in outcomes in particular cases – with other forms of privatization. [12] Circumstantial factors which influence the outcomes for labour include the terms of national labour codes and other aspects of the legal background; labour productivity levels, scope for expansion and other variables specific to the organization or sector concerned at the time of privatization; the prevailing labour relations climate and balance of forces (including the organizational strength and strategies of unions); the attitude of government and the content of agreements made with unions in connection with privatization; the approach taken to human resource development by the privatized management; and the regulatory environment, including the attitude of regulatory bodies.

An example of the way in which the legal environment affects the impact of privatization on labour is that of the European Union (EU), where transnational companies above a certain size have to form consultative works councils, which has resulted in such councils being established in major companies holding contracts and concessions for municipal service provision, such as Suez-Lyonnaise des Eaux. [13] In addition, the jobs of workers in the EU are protected, along with many of their terms and conditions, in the event of contracting-out, because they are covered by the terms of the Acquired Rights Directive, which was originally designed to give protection to workers whose companies are taken over by others (see also box 2). In the case of the water service in Guinea, by contrast, the entire workforce was laid off, albeit with the opportunity (except for those dismissed for "gross negligence") to apply for completely new contracts which were awarded, or not, on the basis of aptitude tests. Many failed and many others, anticipating failure, did not reapply. [14]

[11] E.S. Savas: "Privatization in state and local government", in A.H. Raphaelson (ed.): *Restructuring state and local services*, 1998, p. 95.

[12] See, L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998.

[13] D. Hall: "Restructuring and privatization in the public utilities – Europe", in L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998, p. 137.

[14] P. Plane: "Privatization of water and electricity in Africa", in L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998, p. 33.

The attitude of the leadership of the private companies concerned can also be a significant factor affecting the outcome of privatization for labour, and such attitudes are, in turn, shaped in part by the national context in which the company has developed. An ILO study found that, while companies tend to adapt to the environment in which they are operating as a result of privatization, firms based in the United States are more likely than others to resist doing so. [15] The mindset of some was vividly expressed by the straight-talking Jeffrey Skilling, president of energy company Enron, when he told an industry conference in Phoenix, Arizona, that the future belonged only to those utilities which "get rid of people" because "they gum up the works". [16] However, other companies take the view that good employment practice represents good business.

Box 5
Relations between UNISON and ISS in the United Kingdom

ISS is a transnational cleaning company, based in Denmark but operating in 32 countries. In recent years it has grown rapidly through acquisition, with 53 take-overs in 2000 alone, and increasingly diversified into other support services. With 265,000 employees, it is one of Europe's ten largest employers. In the United Kingdom, it has more public sector contracts than any other cleaning company. Only 53 per cent of the company's employees have full-time contracts, but ISS plans to increase that percentage to 80 per cent by 2005. UNISON is Britain's largest union, with 1.5 million members across all grades in local government, health care, education, utilities and transport, of whom many now work in the private sector, as a result of nearly 20 years of privatization in the United Kingdom's public services. In the 1980s, UNISON amended its constitution to enable it to organize in the private sector. However, the union remains opposed in principle to privatization, believing that the ethical basis and quality of public services is undermined if they are a source of private profit.

In 1994, ISS and UNISON signed a Recognition and Procedure Agreement for "mutual benefit", in which the company recognizes and accepts "the desirability of eligible employees being members of the union" and the union recognizes the "right of the company to manage its establishments" and the "constraints placed upon the company by its terms of contract". The agreement covers terms and conditions of employment; procedures for engagement, suspension, termination and duties of employment; negotiation and consultation machinery; discipline; and provision of facilities, including time off for training, for union representatives employed by the company.

A Memorandum of Understanding between ISS and UNISON states that it is in their "joint interests to recognize each other as partners in the workplace", that the company "recognizes and agrees that good terms and conditions of employment for its employees will help in providing quality services in the public sector", and that "wherever ISS obtains contracts, both parties will work to make the contract a successful enterprise".

The relationship between ISS and UNISON operates at both national and local levels. Some policies and procedures, including those covering health and safety, operate across all contracts, and some terms and conditions, including working hours and sick pay, are negotiated nationally. Pay rates are determined locally, although the proportion of UNISON members covered by national wage negotiations with ISS has been growing and the union intends to submit a formal national claim in 2002.

On the basis of the agreement, the partners have entered into a number of joint initiatives, including nationally supported training projects tailored to local needs identified at workplace level. The major goal for the union at present is the introduction of a pension scheme at ISS. Currently there are no pension arrangements for the company's British employees, and the two parties are together exploring the possibility of establishing one. Recent legislation promoting and enabling "stakeholder" pensions has provided more favourable conditions for doing so.

[15] ibid.

[16] C. Parkes: "Power groups face brutal future", in the *Financial Times*, London, 14 Mar. 1997.

The ISS-UNISON agreement is unusual in the British context, because it was signed more than three years before the Labour Government came to power there in 1997 and some six years before new legislation restored the right of workers to have their union recognized by employers where the majority of a workforce are in membership and vote to bargain through the union. In other respects, however, the union is frustrated that the prevailing national environment continues to impede its efforts to improve the remuneration package available to its members. A UNISON official commented: "ISS deserves a lot of credit and in some respects our relationship with them is a model of partnership working. But the terms and conditions it offers new staff are not good, and the company says this is because they cannot afford to be too far out of line with competitors, or else they would price themselves out of the market. ISS is not so obsessed by its share price as some contractors, but it does have to pay some attention to it, and we understand that." For this reason, UNISON believes government action is needed to restore some form of "fair wages resolution", a device setting minimum pay standards in particular industrial and service sectors which was abolished in the 1980s by the then Conservative Government. The union believes that restoration of this provision in some form would enable employers which wish to invest more in their workforces to do so without loss of competitive advantage.

Source: Documents provided by UNISON, and interviews with UNISON officials.

There are many cases in which large-scale employment reductions and change in pay and conditions of employment preceded privatization, directly or indirectly in preparation for it, so that analysis of what occurs later would produce misleading conclusions about the relationship between privatization and employment. There are also many in which job reductions are offset by employment creation as activities are contracted out, in which case the impact on terms and conditions varies depending upon labour market conditions.

As with other dimensions of the impact of privatization, there is variety not only between but within particular cases. "The productivity gains from employment cuts often have resulted in wage improvements for employees who remained", as Sunita Kikeri has pointed out, adding: "In Argentina, the real wages and salaries of employees of Entel [telecoms] and the Buenos Aires water concession increased by 45 per cent in the three years following privatization." She notes similar improvements in Chile, Malaysia and Mexico, and goes on: "In exchange for higher wages, rigid labour contracts often have been revised. In Latin American countries, for example, inefficient work rules and conditions of service were renegotiated to provide managers greater flexibility with respect to decisions on content and pace of working conditions, labour allocation, and subcontracting of support and administrative services to non-unionized firms and subsidiaries." [17]

On the other hand, the regulatory regime can have a major influence on labour relations in the post-privatization context, and this, over time, can begin to undermine improvements secured by employees in the initial stages. For example, UNISON, in the United Kingdom, reports that, as well as applying general pressure for productivity increases, there is a growing tendency for the energy regulator to study companies' operations in detail and identify particular areas in which labour costs could be reduced.

Among other factors influencing the course of labour relations and other employment matters after privatization is structural change among the companies in the privatized sectors. There is a merger and acquisitions trend not only within each sector but also between utility sectors and between them and other areas of public services, while those companies often also outsource many of their activities. The labour relations challenges arising from this are magnified by the take-over of companies by transnationals based overseas. For example, 11 of the 12 privatized electricity supply companies in the United Kingdom were taken over by United States firms in a trend that also began to reverse the horizontal disintegration which had been part of the rationale for privatization. United

[17] S. Kikeri: *Privatization and labour*, World Bank, undated, p. 7.

Kingdom unions report also a proliferation of companies in the electricity sector since privatization, making the organization and bargaining environment totally different not only from when the service was state-run but also from when it was initially privatized. They say that as a consequence of outsourcing, some of the protection afforded by legal obligations and agreements which apply to a privatized company can be lost to sections of the workforce. [18]

Moreover, as with other commitments made at the time of privatization, the extent to which agreements concerning labour are honoured can be a function of the balance of forces in the post-privatization context. In Hungary, electricity workers' unions reached an agreement with their government which protected employment levels and their collective labour contract as part of the terms of privatization. In the event, the privatized companies tried to withdraw from the commitment, but the unions campaigned not only at home but also with the support of other Public Services International (PSI) affiliates in France and Germany (the base countries of the service's new owners), and pay rises due under the contract were honoured. [19]

Box 6
Building the labour dimension into the privatization process in Buffalo, United States

Municipal politicians and managers, and their employees' unions, can exercise considerable influence on what happens after privatization by shaping the terms on which it takes place. For example, in 1996, intending to privatize its wastewater treatment service, the United States city of Buffalo, NY, invited proposals from United Water (UW), American Anglian Environmental Technologies (AAET) and Professional Services Group, Inc. (PSG), and required the bidders to set out what they would do with the existing labour force if they won the contract.

UW's submission stated that the company "is committed to employing existing staff and making significant investment in the greater advancement of each of its team members" and that they would extend the one-year no lay-offs pledge required by the city to five years, improving productivity instead through "our innovative approach to providing service level enhancements, and through 'in-sourcing' of minor capital improvements work, major corrective repairs and other services currently 'outsourced' by the board". [1] In addition, the company proposed to implement an extensive training programme on process control, maintenance, safety, warehousing, purchasing and cost control measures. However, they made no promises about union recognition, bargaining rights or maintenance of pay levels.

AAET also undertook to embark upon a comprehensive programme of employee training and development and to maintain employment and terms of employment at then current levels throughout the period of their five-year plan, as a result of a planned extensive meter installation programme. While promising to meet all the financial costs of these commitments, the company's submission declared its assumption that all employees with over 25 years of service, and therefore able to retire under the terms of the municipality's pension arrangements, would be enabled to take early retirement.

PSG appeared to anticipate the need for some redundancies, stating that it would seek to eliminate "no lay off" language in existing labour contracts in the course of negotiating terms and conditions with the union, which it undertook to recognize as its workers' bargaining agent. The company also said it would budget for a 3 per cent pay increase; maintain medical payments for up to 18 months; provide training even for redundant employees; and offer other benefits.

Significantly, the more the commitments on employment made by the rival companies, the higher their proposed charge for the contract to the city, so that the city itself was faced with the cost of the trade-off.

[1] United Water price proposal for the City of Buffalo.

Source: Documents provided by AFSCME, the United States public employees' union.

[18] Personal interview with Sol Mead, UNISON official, Jan. 2001.

[19] Information from Public Services International, the labour federation linking 25 million public services workers, in public and private sectors, worldwide.

3.6. Privatization's impact on quality and service outcomes

"There is no agreed definition of quality, yet it is this that anyone wanting to improve their service hankers for", Lucy Gaster has written, in the context of European public services.[20] As already discussed in the context of efficiency, effectiveness and productivity, the quest involves several challenges. One is to define objectives, another to determine the criteria by which to measure results against them, and a third to determine measurement methodology.

Despite these complexities, some studies of privatization have been robust in their findings. Philip K. Porter and James F. Dewey insist: "There is substantial evidence that private firms in competitive markets outperform government bureaus in the provision of goods and services. In many cases, the gains from privatization are quite substantial."[21] Paul Seidenstat, writing about the experience of municipal contracting-out in the United States, goes further: "The preponderance of evidence suggests that competently designed privatizing almost always leads to lower unit cost, improved service quality, or both."[22] And E.S. Savas goes further still: "There is by now a lengthy array of studies which demonstrate quite conclusively that, in general, contracted service cost less and are at least as good in quality as corresponding services produced in-house by government agencies."[23]

A brief review of the research reveals, however, that the picture is more varied and nuanced than those American claims would suggest. One evaluation of contracting-out municipal services was made after research sponsored by the United Nations and World Bank and carried out by a team led by Richard Batley of the School of Public Policy at the University of Birmingham, in the United Kingdom. On the basis of their own case studies in Brazil, India, Malaysia, Mexico, Uganda and Zimbabwe, as well as 50 already published assessments of experience elsewhere, Batley concluded that "the evidence of greater efficiency and effectiveness through privatization or contracting-out of public services remains slim, particularly for developing countries".[24] He presents a mixed picture: "There are strong cases of effective public water supply, public electricity supply, public housing, refuse collection and disposal, and even (in Malaysia and perhaps Mexico) primary education." In particular, "public refuse collection systems (in Mexico and Zimbabwe) and education systems (in Malaysia and in Mexico) were among the best performers in the cross-national comparison", while "purely public water supply systems were among the best-performing services overall".[25] At the same time: "The clearest case of improving performance through contracting-out appears to be the privatized refuse collection system in Recife, Brazil. In another case of competitive public and private provision, the private

[20] L. Gaster: *Quality in public services*, Open University Press, 1995, p. 2.

[21] P.K. Porter; J.F. Dewey: "The political economy of privatization", in A.H. Raphaelson (ed.): *Restructuring state and local services*, 1998, p. 71.

[22] P. Seidenstat: "Theory and practice of contracting out in the United States", in P. Seidenstat (ed.): *Contracting out government services*, Praeger, 1999, p. 20.

[23] E.S. Savas: "Privatization in state and local government", in A.H. Raphaelson (ed.): *Restructuring state and local services*, 1998, p. 93.

[24] R. Batley: "Public-private relationships and performance in service provision", in *Urban Studies*, Vol. 33, Nos. 4-5, 1996, p. 723.

[25] R. Batley, ibid., p. 749.

education in Ahmedabad and Anand in India is clearly more effective than the public. But there is also negative experience: contracting-out of solid-waste management in Penang Island, Malaysia, has presented certain problems and failures ...", while Calcutta's entirely privatized transport system has brought neither efficiency nor choice. [26]

The United Kingdom Electricity Association has concluded that there is no correlation between ownership form and fuel prices, [27] while another study, based on exhaustive international empirical research, found that in the long run, in electricity generation, "better investment planning leads to lower operating costs", while in transmission and distribution, there was "no evidence" that privatization would bring lower costs in the short or long runs. "In the ESI [electricity supply industry] as a whole it is likely that the biggest gains are from restructuring and better government management of state owned electricity assets", the report commented. [28]

A study of Australian telecoms concluded that "it is clear that privatization is not a necessary condition for improved productive efficiency of publicly owned enterprises", [29] while an account of Malaysian privatization concluded that "in most cases, the transfer of ownership from public to private hands has not involved reduced user costs or significantly enhanced quality of services". [30]

Even within the same service, the results vary greatly, as the generally positive accounts of privatization of Japanese railways (that it has been a success) in contrast to the consensus about railways privatization in the United Kingdom (that it has been a disaster) demonstrate. Heterogeneous outcomes emerge even from within the *same* case. One account of the impact of privatization on Mexican telecommunications reports improved public telephone facilities and more rural services, but also that: "Customers complained about billing errors, repair delays, unfriendly service and of course high prices. As one Mexican observer put it, 'Consumers are complaining that they have to pay First World prices for Third World service.' " [31]

Other studies reveal similar discrepancies. Some indicate that the availability of choice between providers, and of choice between tariff structures from the same provider, can bring benefits to consumers, including lower prices. Several studies suggest, however, that it brings illusory benefits or even costs to consumers because of a form of market failure often overlooked in privatization design, arising from the inability of consumers, through lack of time or capacity, to gather information and effectively evaluate it. As one study has put it: "Residential and small business electric customers have little time and

[26] R. Batley, ibid., p. 739.

[27] D. Hall: "Restructuring and privatization in the public utilities in Europe", in L. de Luca (ed.): *Labour and social dimensions of privatization and restructuring*, ILO, 1998, p. 146.

[28] M.G. Pollitt: *Ownership and performance in electric utilities: The international evidence on privatization and efficiency*, OUP, 1995, p. 189.

[29] A. Brown: "Australian telecommunications", in M. Hossain and J. Malbon (eds.): *Who benefits from privatization?*, Routledge, 1998, p. 95.

[30] W. Goh; J. Sundram; "Privatization in Malaysia", in M. Hossain and J. Malbon (eds.): *Who Benefits from Privatization?*, Routledge, 1998, p. 196.

[31] R. Ramamurti: "The new frontier of privatization", in R. Ramamurti (ed.): *Privatizing monopolies: Lessons from the telecommunications and transport sectors in Latin America*, John Hopkins University Press, 1996, p. 27.

modest economic incentives to become skilled in the art of electric service analysis. Their primary interest is in receiving a reasonably priced, reliable and non-discriminatory electric service. ... For these customers, the effort required to judge and compare rate options does not result in savings large enough to justify the effort.” [32]

While, as we have noted, some studies make general claims about efficiency and/or quality improvements always arising from privatization if it is carried out competently, none of the literature suggests that privatization is never followed by quality improvements. Studies which do show such results do not necessarily attribute them to privatization per se, and some stress that competition is the key factor rather than private ownership or management. Even that is open to dispute, however, as Batley, for example, has found: “The best-all-round case identified in the present research was that of the Hermosillo [Mexico] municipal services department, which has been exposed to no competition at all. This is a case of firm management, a strong investment policy, light administration and strong political (mayoral) support for improvement of the service.” [33] Other studies point to a similar conclusion.

Some evaluations of the tendering and contracting-out of municipal services have suggested that in so far as they produce efficiency and/or quality improvements, this is attributable to the preparatory process of carefully analysing and specifying costs and services in detail, rather than the product of either competition or privatization per se (although the prospect of those consequences might well have stimulated the close examination of the inputs and outputs of services). Some even say that those benefits can be lost if privatization then goes ahead, as one labour union report on contracting-out in Australia implies: “Evidence suggests that failure to meet contract conditions or specifications and problems with contracts which may ultimately lead to termination are higher where contractors are used than with in-house providers. In other words, the quality of service declines.”

Box 7
Competition and cooperation in the city of Indianapolis

In 1992, an ambitious young politician called Stephen Goldsmith became mayor of the United States city of Indianapolis, a Republican stronghold. During the campaign, Goldsmith had boldly declared that he would run the city with a team of four purchasing agents – everything else (other than the police and fire departments) would be done by private contractors. In addition to being ideologically committed to this plan, Goldsmith wanted to reverse migration by residents and businesses to suburbs beyond the city limits. His aim was to improve the quality of the city’s public services without tax increases, while encouraging inner-city regeneration.

The city’s workers, organized in the American Federation of State, Country and Municipal Employees (AFSCME), had opposed his election and planned to resist his privatization plans, with militant action if necessary. The union also proposed an alternative based on the idea that if the workers were given a fair shot at putting into practice their own ideas about how to improve services while spending public money less wastefully, they could compete with the private contractors and win. Goldsmith was sceptical, but when he went and talked to the front line workers in one of the departments concerned, he was impressed by what they said. He became convinced, in fact, that they were the true experts in how the operations in which they worked could be run more effectively and efficiently, and he decided to take their knowledge and experience seriously.

[32] M. Shames: “Preserving consumer protection and education in a deregulated electric services world”, in M. Hossain and J. Malbon (eds.): *Who benefits from privatization?*, Routledge, 1998, p. 127.

[33] R. Batley: “Public-private relationships and performance in service provision”, in *Urban Studies*, Vol. 33, Nos. 4-5, 1996, p. 744.

However, the workers knew they could never compete with the private contractors if they were also expected to carry the huge overhead represented by an unnecessarily deep layer of politically appointed managers – patronage sinecures would have to go, the union insisted. "By normal political standards, the union's demand would have been a show-stopper", Goldsmith wrote later. "The supervisors were all registered Republicans. These managers, and their patrons in our party, had supported my election. The union had supported the opposition and campaigned strongly against me." But the union's case was unanswerable. For 94 workers in the street-repair division alone, there were 32 politically appointed supervisors – "most of them highly paid", as Goldsmith pointed out. "If I had blinked and shielded my fellow Republicans, the message would have been clear: we were not serious about competition." [1]

Consequently, the politically appointed managers were dismissed, but the union had a further condition for their cooperation in plans to reorganize work processes to drive up labour productivity: that there would be no compulsory job losses among their members. Goldsmith came to agree with that, too. "No matter how committed a workforce is to the public weal", he says, "you cannot say to them please come up with some good ideas so that we can put you out of work. So it would have been extraordinarily difficult to achieve what we have achieved without the commitment on employment security". [2] It would also have been impossible to do so, however, without reducing the workforce in some departments. Therefore, the city established a labour pool, to which surplus workers were transferred, and from which other departments of the city, and private employers, could recruit. Training was provided for these workers.

Indianapolis has cut its annual budget by $12m while fewer services are now contracted out than when Goldsmith took office, although more than before are subjected to market testing on a regular basis. Services have improved so much that the city and the workers' union were jointly awarded an Innovations in American Government Award by the Ford Foundation and the John F. Kennedy School of Government at Harvard University. Earnings have greatly increased because of a gain-sharing agreement under which workers are awarded 25 per cent of the savings their efforts achieve below already reduced budgets.

In addition to mobilizing their knowledge, the workers have been able to focus it effectively as a result of being trained in Activity Based Costing, which measures the costs of particular outputs, such as filling a hole in a road, through breaking down inputs into constituent parts – equipment, material, labour, depreciation and overheads – and counting the cost of each. Whereas, in the past, only a division's overall budget was visible, now financial information is much more transparent and openly available, and this has contributed greatly to the successful reorganization of work processes.

[1] S. Goldsmith: "Can-do unions: Competition brings out the best in government workers", in *Policy Review*, Mar.-Apr. 1998, p. 24. [2] Personal interview, Apr. 1998.

Source: B. Martin: "In the public service" (forthcoming).

3.7. Privatization and democratic accountability

A fundamental argument against privatizing public services has long been that services run by private companies cannot also be democratically accountable, by definition, since their providers' chief concern – or, in the case of "public" companies, legal obligation – is to maximize profits. The main counter-argument is that democratic accountability is satisfied so long as policy and strategic decisions are taken at a level which is susceptible to periodic judgement by voters, and provider organizations – whether publicly owned or not – are accountable to that level. The better the design of the regulatory or contractual arrangements linking the "purchaser" or "client" side with the "provider" or "contractor" side, the more democratically accountable services will be (provided, of course, that the relationship between citizens and government is also democratic). By contrast, public organizations prone to weak internal control, leading to divergence between the interests of the "principals" and their "agents" are, as a consequence, also less accountable democratically.

Another line of pro-privatization argument would challenge the democratic accountability argument against privatization more directly, by asserting that loss of democratic accountability is a positive outcome of privatization, on the grounds that our collective welfare is best served by minimizing the interventions of political processes and enabling the market to allocate resources and make decisions about their use. The application of this outlook into the heart of public services might be regarded as market fundamentalism, and it characterized the approach to privatization taken by the first government to develop a systematic programme, the Chilean military dictatorship led by General Augusto Pinochet from 1973 into the 1980s. Obviously, that regime was not at all concerned with democratic accountability in general, owing its existence to a military coup which deliberately and violently overthrew an elected government and destroyed or suppressed institutions through which democratic accountability could be exercised. It was precisely the anti-democratic nature of that regime that enabled it to pursue so fundamentalist an approach to public policy, but even elected governments have been guided by the same outlook in their approach to privatization, even if the pressure of democratic accountability itself has prevented it being taken to such extremes as in Chile.

Not only issues of regulatory and contract design but also the more fundamental issue about whether democratic accountability is appropriate to public services continue to find expression in privatization policy-making. A topical example illustrating the range of these issues is that of the electricity supply services in California. Commenting on the debacle which has followed his state's experiment with regulatory reform and privatization, Governor Gray Davis spoke of the need to "face reality", and added:

> California's deregulation scheme is a colossal and dangerous failure. It has not lowered consumer prices. And it has not increased supply. In fact, it has resulted in skyrocketing prices, price-gouging and an unreliable supply of electricity. In short, an energy nightmare. … We have lost control over our own power. We have surrendered the decisions about where electricity is sold – and for how much – to private companies with only one objective: maximizing unheard-of profits. [34]

Those comments are especially interesting in the context of this paper in that they make an association between service quality outcomes and loss of democratic accountability. Their significance is heightened by the fact that the only part of the state to have escaped power cuts, steep price increases, or both, has been Los Angeles, where an integrated electricity supply service has been retained within the municipality.

The experience in California has prompted some commentators to suggest that authority over energy supply decisions there should be returned to the Public Utility Commission, strengthening democratic accountability. Others have argued that the energy crisis in the state has arisen from deregulation having not gone far enough (some price limits and other restrictions on the power utilities' activities remain in force), and that if market forces were to be truly liberated, reliable and cheap supply would follow. Both positions are problematic. On the one hand, while the fortunate citizens of Los Angeles might feel that they are benefiting from reliable and cheap energy supplies because they retain democratic accountability over their service, people elsewhere are entitled to point out that most of the externalities of the cheap fuel enjoyed in the city (and throughout the United States) are paid by people far away. Energy prices kept artificially low through political pressures produce market distortions which are paid for by others excluded from the democratic processes which produce the decisions. On the other hand, the "price gouging" to which Governor Davis referred is a product of not a free market but the kind that actually exists, in which dominant interests can influence market structure and outcomes in self-serving ways.

The latter problem is not necessarily overcome by regulation or contracts, no matter how well designed. On the contrary, a charge frequently levelled at regulatory institutions in the context of privatization is that they are subject to capture by the growing market power of the industry they are regulating. The same can certainly be said of contract-based

[34] State of the State Address, California Governor Gray Davis, 8 Jan. 2001.

regulation, as we have seen in the case of Buenos Aires water. Imbalances in resources, capacity and power between the two sides can have a larger impact than the formal arrangements alone would suggest. As one recent academic commentary, written from an ethical and legal standpoint, has put it, privatization involves "an abdication of power by state institutions and its assumption by individuals and large corporations". It adds: "Once given away, it is very difficult to take back. The power assumed will be used to resist its retaking or its limitation. Indeed it may well be used to seek extensions of that very power." [35]

This transfer of power favours not only of transnational corporations but also, in developing countries especially, local elites, as the experience of privatization in South-East Asia and Latin America has demonstrated. As one commentary has claimed:

> In many ASEAN countries, people have the feeling that privatization indeed reduced the burden of government, but it has increased the burden of the consumers ... The common people are to pay unreasonably higher prices and higher tariffs even for public utilities. Moreover, it is strongly felt that privatization in many cases has not led to more competition, but it has generated monopoly power in the hands of a few joint owners of privatized utilities like telecom and electricity generation. Privatization has indeed converted public monopoly into private monopoly. And the growth of crony capitalism is said to be one of the direct consequences of privatization where the benefits are enjoyed by the relatives and friends of political bosses. [36]

In those countries, and in poorer ones, there is another aspect of the democracy dimension of privatization, namely the continuing influence of external international finance institutions. This issue was highlighted by a letter written from the IMF mission in the Philippines to a member of that country's Congress on the subject of the pace of passage of the electricity privatization legislation there. The letter expressed a thinly veiled threat to withdraw financial support for the Philippines Government unless the legislation paving the way for NPC's privatization was passed without further delay.

What these experiences and many others suggest is that there is a real crisis of democratic legitimacy in public services internationally, and that profound change in the way they are run is required in order to resolve this, as well as to resolve challenges associated with efficiency, quality and employment. The fact is that the status quo is not an option for municipal services; therefore, the issue is not whether there will be change, but what kind of change is to occur. In that context, alternatives to privatization – of which there is a growing body of theory and practice, as with privatization itself – deserve as much consideration by policy-makers and social partners as do the benefits and costs of privatization.

[35] C. Sampford: "Cautionary reflections on the privatization push", in M. Hossain and J. Malbon (eds.): *Who benefits from privatization?*, Routledge, 1998, p. 256.

[36] B.N. Ghosh: "Privatization: The ASEAN experience", in *Privatization: The ASEAN connection*, Nova Science Publishers, p. 9.

Box 8
Building a learning organization in Danish health and social care

The largest responsibilities of Frederiksborg county, which lies just north of Copenhagen, the capital city of Denmark, are health and social care, in which it employs more than 10,000 people. Faced with an increasing challenge to raise the standards of its services in response to the rising expectations of users, at the same time as cutting costs in response to problems of public finance in the context of increasing internationalization of the economy, Frederiksborg considered contracting out many of the ancillary services. However, while believing this would successfully reduce costs, the county was not convinced that industrial relations and job satisfaction would be improved in that way, and believed that tackling those issues would lead to improvements in long-term financial efficiency and service quality. Among other difficulties, the county wished to reduce its very high rate of labour turnover – about a third of the workforce annually – among the ancillary staff, and especially among the cleaners, most of whom were women.

In these circumstances, the Union of Public Employees (FOA), allied with the Danish Confederation of Municipal Employees (DKK), proposed a solution to which they gave the name the “Service Project”. Ironically, Frederiksborg’s declared short-term need to save 15m DEK per year was actually met thanks to the high rate of staff turnover, by leaving new vacancies empty, rather than by contracting out or by the Service Project. Employment reductions among cleaners alone in the end accounted for about two-thirds of the budget reductions achieved by the council. A smaller staff led, however, to a larger work burden on the remaining staff and greater dissatisfaction among them. This in turn heightened the workers’ enthusiasm for change.

The concept of the Service Project – involving initially more than 1,000 cleaners, porters, domestic helpers, kitchen assistants and general workers – was based on four pillars: the concept of an all-round service employee, rather than specialism; self-managing teams; training to develop a “learning organization”; and leadership as a guiding managerial principle. As a result of the changes introduced through the project, each self-managing team, organized either within or across departments, is responsible for carrying out a range of duties agreed with doctors and nursing management, but organizes its own work plans and allocation of tasks, based on multiskilling and flexibility. The teams are encouraged to suggest ways of improving their own working methods and register their specific needs for training. All team member have equal status.

The first stage of reform comprised a 15-week training programme involving all the self-managing teams. During the first six weeks, the teams concentrated on issues such as team building, developing inter-personal communication skills and conflict resolution. Only when these issues had been thoroughly tackled did retraining for new daily tasks begin. In place of the previous demarcation between ancillary jobs – between cleaners (mainly women) and porters (mainly men), in particular – all workers involved are now able and expected to move flexibly between the roles assigned to their team. In addition to the financial savings, the project has greatly increased labour productivity. It also brought pay increases for most, because all ancillary workers were regraded to the same level as porters. In this way, gender inequalities in pay and status have been eradicated, resolving a long-standing grievance of the majority while bringing considerable cultural challenges to all and especially to the minority.

Source: B. Martin: *European integration and modernization of local public services*, European Federation of Public Service Unions (EPSU), Brussels, 1996.

4. Challenges and opportunities for the social partners

Municipalities face a great and growing challenge to meet the changing economic, social and environmental needs and expectations of the communities they serve within the constraints of budgets and policies determined at national and international level. In practice, this means they are being expected to provide for economic infrastructure, environmental protection and renewal and social need within parameters shaped not only by their own electorates but also by processes and institutions over which they have little if any influence. This calls for great resourcefulness, which the evidence of the experience of privatization and other reforms in municipalities in recent years suggests can best be mobilized through participatory processes in which all stakeholders are enabled not only to influence policy but also to contribute their capacities to implementing it. To the extent that solutions such as privatization are imposed from above and outside, these capacities – and, indeed, the capacity to devise local solutions to local problems at all – is undermined. Therefore, the rights and responsibilities of municipalities must be clearly defined. A fundamental challenge for municipalities and the social partners linked through them, therefore, is to work, in conjunction with others elsewhere (for example, through national organizations linking municipalities) for a constitutional, policy and fiscal framework suited to the exercise of their legitimate roles within the international and national arenas.

That said, municipalities have no choice at the same time but to work within restraints as they are, a reality which adds to their responsibilities to use resources as efficiently and effectively as possible to achieve desired outcomes. Many have turned (not necessarily of their own accord, but sometimes under direct national and/or international pressure or even instruction) to privatization in order to bridge the gap between aspiration and available resources. The results have been highly variable, depending on a complex range of factors associated with the context in which privatization takes place – factors such as the constitutional, legal and political environment, relative availability of public and private finance, access to skills, training and other labour market specifics, and so on. It can be said neither that privatization is always the appropriate solution, nor that is never so. Therefore, when municipalities are considering how to tackle the public services challenges which confront them, a thorough analysis is essential. This, too, is a challenge, but also an opportunity to develop the required capacities.

By what process should such an analysis be conducted? In democracies, municipalities are accountable to their electorates, but in modern democracies that is no longer the full extent of public participation in their decisions. Again, the issue of participatory process is a fundamental one. Moreover, precisely the limitations on the resources at the disposal of municipalities demands the mobilization of all capacities – business, non-governmental organizations, workers – within communities served by municipalities, and experience suggests there is much to be gained from enabling each to contribute what they can to the development and improvement of services. As the conclusions which emerged from the ILO’s 1995 Joint Meeting on the Impact of Structural Adjustment in the Public Services (Efficiency, Quality Improvement and Working Conditions) put it: “Public sector reforms and macroeconomic structural adjustment measures should aim to enable all citizens to participate equitably in their society’s economy, as producers and consumers, and share fully in its cultural life.” [1] The conclusions added:

[1] Conclusions concerning the impact of structural adjustment in the public services on efficiency, quality improvement and working conditions of the Joint Meeting on the Impact of Structural

Public sector reforms are most likely to achieve their objectives of delivering efficient, effective and high-quality services when planned and implemented with full participation of public sector workers and their unions and consumers of public services at all stages of the decision-making process. Continuing dialogue between government and the citizenry as a whole, including public sector workers, should be ensured. Effective communication, consultation and negotiation with a view to reaching agreement with workers and their unions, are essential during restructuring. [2]

Given that the context is one of attempting to match growing need for more and better service outcomes with continuing and often tightening restraints on resources, it follows that a first step in such a participatory process of analysing whether or not privatization offers the best solutions, and if so how it should be carried out, is to establish goals and identify available resources. On this basis, an analysis can be made of the extent to which demand for resources is matched to capacities, and, to the extent that it is not, consideration can be given to how the gaps can be closed. For examples, if capital is required, from where can it come and with what opportunities and risks attached? If management expertise of a new kind is required, on what terms can be it acquired? What knowledge is available within the workforce which could be mobilized through suitable participatory processes and training, and how might it impact on performance? Such an approach can prevent existing resources from being wasted, and might lead to a conclusion that the potential benefits and risks associated with privatization in this case are less favourable proportioned compared to alternative strategies. It can also more effectively target the next step of acquiring absent resources, which can affect judgements and decisions about what kind of privatization goes ahead, bearing in mind the definition of privatization used in this paper (see section 1.3), the variety of its forms (see section 1.4) and its extent.

An important aspect of this analytical and decision-making process will be to evaluate the various options for monitoring and regulating the performance of whatever service delivery organization might emerge from these considerations, since the extent to which that can be done in the various scenarios will affect judgement as to which scenario to create. How can accountability through internal controls be improved in ways which also release initiative and allow innovation among in-house workforces? What capacity is required to manage the regulatory mechanism through which, in the event of privatization, it would be intended to reconcile the public interest with the commercial interests of private service companies? To what extent are the advantages of scale and experience associated with engaging a large transnational company offset by the imbalances this might create in the ability of the municipality to regulate its behaviour? Conversely, would small or medium-sized locally based companies, which might be more easily regulated, be otherwise less reliable and effective in investing in and providing services to the levels required? Those are the kinds of questions the social partners would need to consider.

In order to consider those issues, the social partners will also need to give attention to the questions of measurement discussed in section 3. How can the proposed outcomes for service efficiency and quality improvements be converted into measurable outputs? By what criteria should they be measured, and through what processes?

Adjustment in the Public Services (Efficiency, Quality Improvement and Working Conditions), 30 May 1995, p. 1.

[2] Conclusions concerning the impact of structural adjustment in the public services on efficiency, quality improvement and working conditions of the Joint Meeting on the Impact of Structural Adjustment in the Public Services (Efficiency, Quality Improvement and Working Conditions), 30 May 1995, p. 3.

In the course of these processes, and as extensions of them depending on the whether or not (and if so, how) privatization goes ahead, many labour-related issues also need to be considered. Are there labour or skills shortages, and how can they be overcome? What are the implications for training and for budgets for training? In the event that labour reorganizations and/or retrenchments are required, what steps need to be taken to deal with the consequences?

All of this will be taking place, as already mentioned in 4.1, within parameters far from entirely within municipal control, but that does not mean the social partners at municipal level can exercise no influence over the changing nature of their wider policy environment. Constitutional and legal provisions relating to the powers of municipalities, labour protection and other matters have an important bearing on the outcomes of privatization. Therefore, the national and international links developed and maintained by the social partners – both independently of each other and through national and international institutions in which social dialogue takes place – are of great importance. At those levels, it is possible for the social partners to influence the policies which shape the environment in which their own decisions must be made.

As section 1.1 in the introduction to this paper noted, this paper was commissioned with a remit to address the subject of privatization of public and especially municipal services with particular attention to a range of employment issues – specifically labour relations, workers' rights, productivity, human resource management and working conditions – and service delivery issues, specifically quality, service outcomes and democratic accountability, as well as productivity. The evidence explored in the paper suggests that to some extent these issues can be reconciled through decisions about privatization and (where privatization takes place) its design, while in others they can at best be balanced in ways which maximize good whilst minimizing harm. The evidence suggests that privatization can play a useful role in overcoming deficiencies in municipal services in ways which combine economic efficiency, social justice, democratic accountability and environmental sustainability, but that it does not necessarily have that effect, often does not have that effect and is certainly no panacea. It is for that reason that the challenges for the social partners have been addressed in this concluding section of the paper in a strategic and pragmatic way, and the evidence suggests that privatization can contribute most to the development of municipal services if it is approached in a similar fashion. The overall challenge which runs through the various issues addressed in the paper is to accurately identify the factors (and configurations of factors) which tend to produce particular outcomes, and to form policy and take action accordingly, as opposed to expecting privatization to produce predictable results regardless of circumstances.