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ISSUE BRIEF

Efficiency: Effective or Extractive?

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The idea of making government more "efficient" is not new. Before Elon Musk's Department of Government Efficiency, there was Reinventing Government, the drive by Vice President Al Gore during the Clinton Administration to speed up the gears of a government that was often seen as sluggish and inefficient. "Government should run like a business" has been the campaign talking point of candidates from both major political parties.

Every organization – public or private – should always be seeking ways to do things more efficiently and effectively. But public institutions, with outsized missions and democratic mandates, have a particular responsibility to taxpayers to use their dollars well.

But what is efficiency? It means different things from different perspectives.

Efficiency typically refers to doing more with less—have a greater output with fewer inputs. But it's the input part that is most attractive to elected officials. If they can cut costs and either do more for the extra money or return it in some way to taxpayers, they have material for their next campaign ads. But it is also simply good government to handle the public's money with care, to get the biggest bang for the buck.

Smart efficiencies can identify and implement new innovations while cutting costs. Engineering advancements can lead to greater fuel efficiency for cars. Hiring of employees with greater knowledge and experience—or training them—can lead to higher quality work produced more quickly. Electronic toll booths can save travelers time, while smart phones have enabled all sorts of activities to be done faster and more accurately, from ordering takeout for dinner to getting driving directions to a new location. Greater efficiencies can result in positive outcomes, including greater convenience or time saved—much of which leads to cost savings.

"Efficiency," reduced to cost savings alone without consideration of effectiveness, doesn't lead to "more and better" service – whether within public agencies or outsourced private contractors.

Advocates for outsourcing or privatizing public services currently offered by governments often argue that the private sector is "more efficient" and a better deal for government—and taxpayers.

When governments turn to the private sector to provide greater efficiency in the provision of public functions, it is often based on an assumption that the contractor can provide the public good or service for a lower cost. But, outside the smart efficiencies already mentioned, what would make the private sector provider offer the good or service at a savings to government? That is the central question that must be asked during every conversation about whether to privatize or outsource a good or service. If a private contractor promises to provide the same service for less money, what gets lost? What is reduced and where? Given that a private company must also make a profit in order to stay in business, that puts an additional strain on the calculus.

In other words, something's got to give. What might that include?

To deliver on promised cost savings, contractors often resort to cutting corners. This can mean that a contractor may use inferior materials, making the final product perhaps cheaper in the short run, but require earlier replacement, expensive repairs, or unsafe or unhealthy outcomes for the long run.

Contractors might provide lower wages or fewer benefits to their workers than might be available if the service was kept in the public sector. Not only can this have the effect of reducing the quality of the service or goods offered because it would lead to hiring lower-skilled workers, it can also have ripple effects through an entire community, as lower wages can lead to less retention and higher unemployment, not to mention fewer dollars to put into the rest of the economy.

Contractors might also reduce labor costs by hiring fewer workers or reducing overall work hours, leading to fewer hours of service or a greater workload for each worker, another factor that can chip away at the quality and availability of a service.

Contractors might achieve cost savings by skimping on thoroughness or quality of service provision, or failing to serve everyone who needs the service, instead cherry-picking those who would help the contractor make the best return.

To make matters even more challenging, despite cutting corners, sometimes the promised cost savings in outsourcing still fail to materialize, resulting in cost overruns or renegotiations to increase the price of the contract. By then, continuing or renewing the contract is often the route of least resistance.

Efficiency and Timeframes

Government contracting necessarily focuses on the provision of public goods and services for the time-bound life of the contract. This makes decisions about the public good or service more likely to be shorter-term focused, and any efficiencies achieved are through the lens of short-term gains. This approach can be at odds with the long-term nature of public goods and services. True improvements and smart efficiencies need to be long-term focused and adaptable with the changing needs of the public and the specific communities that rely on the good or service. Contractors seeking to quickly achieve immediate and short-term efficiencies and cost savings may compromise the long-term goals of public goods and services.

Often, some aspect of the public good, such as service quality, is reduced to produce the promised cost savings. These types of efficiencies are extractive in nature, as they take away from the public good to produce the "efficiency."

It is important to point out that endeavors in the private sector have different functions, purposes, and measures of success than those in the public sector. The goal of a private company is to generate and maximize profits while providing a good or service. This may be an appropriate primary focus for the production of private market goods, such as computer chips or light bulbs, but public functions and services are not private market goods. Public goods exist to fulfill the function of serving public needs, not make or increase profits. The primary focus for most public goods should be metrics related to quality, reliability, availability, and/or accessibility. For public goods, using profit as a lens to view efficiency can degrade the quality, reliability, availability, or accessibility of a public good.

Unfortunately, many governmental entities do not find out how private sector promises of efficiencies and cost savings will impact other dimensions of the public good or service until it is too late. When important aspects of public goods are compromised or reduced in the name of efficiency, the overall good or service is not provided in a way that meets the government's goals or the public's needs.

Types of Efficiencies

Smart Efficiencies

Smart efficiencies occur when implementing or improving an input to the service or operation results in better outcomes for the service or operation. Note that the goal of smart efficiencies is to improve outcomes or make it easier to deliver the service but does not necessarily have to result in cost savings. This is especially true in the delivery of public services and goods, where outcomes like the number of people served or the time it takes for a service to be delivered are often greater priority than minimizing cost. Some examples include:

- **Innovative technologies:** The implementation of new technologies or the innovative use of existing technologies may help an operation or service increase timeliness, serve a greater number of people, or make more accurate decisions, etc.;
- **Improved processes:** The implementation of new or improved processes may remove operational bottlenecks or barriers, allowing for better outcomes for the operation or service;
- **Expertise:** Employing and/or involving people who have expertise or specialized knowledge or providing robust training to a workforce to develop expertise and knowledge, can result in greater accuracy, increased timeliness, and other improved outcomes for the operation or service.

Extractive Efficiencies

Extractive efficiencies, especially in the context of contracting, are often used to produce cost savings. This type of efficiency consists of reductions in services, which can occur through the measures listed below. Employing extractive efficiencies may minimize costs in the short-term, but often result in outcomes that ultimately hurt the service or operation, including increased workforce turnover, decreased service availability, and decreased service quality. Some examples include:

- **Staffing levels:** Reducing the number of employees, or reducing the number of employee work hours, or reducing the number of shifts, etc.;
- **Workforce compensation levels:** Reducing the pay and/or benefits of the workforce or particular segments of the workforce;
- **Service availability:** Reducing the availability of the service, through measures such as reducing hours of service availability, reducing methods for receiving the service, reducing the locations where people can receive a service, etc.;
- **Service levels:** Reducing the amount of service provided or reducing the amount of output created;
- **Asset maintenance:** Reducing the amount/level or quality of maintenance and performed on equipment, tools, technology, and other assets needed to provide the service;
- **Material inputs:** Reducing the quality or quantity of materials, supplies, tools, equipment, etc. used in the operation or service;
- **Service levels:** Reducing the amount, scope, or duration of service provided.

Ultimately, the keepers of the public trust need to keep their eyes just as much on what gets lost as what goods and services might cost in any efficiency project whether internally by agency cost cutting or by outsourcing or privatizing schemes. A careful examination of how public agencies or contractors will achieve efficiency will help the public truly decide the best way forward.

Recommendations for preventing extractive efficiencies in government contracting

It is critical that governments understand and evaluate a contractor's promise of efficiency and have ways to hold contractors accountable for their performance. Unfortunately, the pervasive idea that the private sector is more efficient than the public sector means that claims of efficiency often go unchecked and unscrutinized. Below are several responsible contracting best practices and policies that can help governments reduce the risk of extractive efficiencies and poor contracting outcomes.

Conduct an "efficiency analysis" for contracting proposals

Governments often do not perform the analysis needed to understand whether contracts are truly efficient, cost effective, and able to improve the good or service. Too often, governments do not require or perform any analysis of proposed contracts to understand details about how promised cost savings or other outcomes will be achieved and/or never investigate corporate claims that contracting will be more efficient, save money, and improve quality. This lack of proposal analysis increases the chance that a jurisdiction signs a risky contract or outsources a public function that is better performed by public sector staff. Before a contract is signed, localities and states should conduct an efficiency analysis to understand whether and how a contractor working under a proposed contract plans to achieve greater efficiencies and/or cost savings. In other words, does the contractor plan to implement smart efficiencies or simply cut corners to achieve cost savings.

An efficiency analysis should include a review of a company's track record with similar contracts in other jurisdictions. Contractors that have had problems in delivering on their promises on other contracts should be a signal to jurisdictions to carefully analyze the contractor's current claims and promises related to the proposed contract.

An efficiency analysis should also include a cost comparison to compare the costs of a proposed contract and in-house service provision. This type of analysis allows governmental entities to dig into how proposed contracting cost savings or promised efficiencies will impact each expense associated with the good or service. For example, if labor costs vary between the public and private delivery options, governmental decision-makers should explore why those costs are different and how those differences might impact the provision of the public good or service. Analyses should account for all expenses associated with contracting, such as operational, material, labor, and overhead costs, as well as costs incurred by the governmental entity, such as costs associated with contract administration, on-going contract oversight and monitoring, transition costs, and the contractor's use of public equipment and facilities. This type of analysis can help governmental entities understand whether outsourcing the public function is truly efficient and cost effective, and whether outsourcing is a preferable service delivery option over public provision. For more information about this type of procurement cost analysis, see ITPI's brief, "Procurement Cost Analyses and the Decision to Contract."

Additionally, governmental entities should perform an impact analysis that examines the social, economic, and environmental impacts of a proposed contract, especially for contracts that could have broad impacts on the community. When a government contractor cuts corners, these impacts can ripple beyond immediate service provision. For example, if a janitorial contractor plans on using cheaper cleaning products, it is important to identify and understand the potential health and environmental impacts. If the contractor plans to reduce compensation for its workforce, it is important to understand the impacts of the reduced money flowing to the local economy. This process must be transparent to ensure that critical impacts are captured in an analysis, and to determine whether the broader impacts for a given proposal are acceptable, especially to those most impacted.

Ensure contractors that have poor efficiency track records do not receive future contracts

It is important that governments engaging outside entities ensure that only law-abiding companies with positive efficiency track records receive public dollars. Localities and states should bar companies that fail to abide by federal, local, and state laws, including tax, labor, civil rights, environmental, and other types of laws, from participating in the contracting process. Governments can and should also bar contractors that have failed to live up to their contractual promises from receiving future contracts from the jurisdiction.

In 2023, San Antonio, Texas made changes to it procurement process to root out low-road contractors on public works projects. The city passed a new ordinance that allows city staff to refuse bids from contractors that previously did not meet expectations on a project, did not adhere to deadlines, or owe the city money. Previous problems with several city projects prompted the new law, with the goal of giving the city a tool to hold contractors accountable for their performance. A project team will evaluate each project, and score the contractor based on six weighted factors: meeting contract requirements, staying on schedule, quality of work, responsiveness, keeping within budget, and finalizing or closing out the project. The city will not award any new contracts for city projects to contractors with a score below 70% for a three-year period.[1]

An additional benefit of this type of policy is that it necessitates a post-contract review to evaluate whether the contractor fulfilled their promises and responsibilities. Government contract outcomes are often not evaluated and reviewed in a systematic manner. While local or state auditors may audit a contract or groups of contracts, this is often an exceptional occurrence, instead of a regular review of contracting outcomes. This type of methodical and straightforward review ensures an evaluative step that is often left out of the contract close-out process.

Ensure that governments have the ability to choose high-road contractors

There may be situations where legal constraints prevent jurisdictions from selecting more responsible contractors, forcing the selection of contractors more likely to cut corners to achieve extractive efficiency outcomes. For example, in 2022, in a survey about school lunches, parents and students in school districts across Illinois overwhelmingly complained about the taste of the lunches, the lack of food quality, and freshness. Many reported that their children begged for a sack lunch to avoid eating the hot lunch. Unfortunately, many of these school districts contract out their food service operations and Illinois state procurement code required districts participating in the National School Lunch Program to select the lowest-bid in the bid selection process. As Sharon Desmoulin-Kherat, superintendent of Peoria Public Schools explained, "Being forced to accept the lowest bid constrains school districts from selecting the best-qualified contractors to meet the nutritional needs of students."[2] By forcing school districts to accept the lowest bid, contractors compete solely on cost, creating conditions that are ripe for cutting corners and skimping on important aspects of service provision.

Concerned lawmakers introduced a bill to remove the lowest bid requirement for school districts which passed in June of 2022.[3] Schools can now choose contractors that may not be the lowest bid, but provide fresher, tastier, and healthier food options. School districts can also improve their procurement processes by involving students in the decision making, allowing them to make their voices heard by testing food and giving feedback.[4]

Hire and train efficiency monitoring staff

Localities and states should employ sufficient contract oversight staff to ensure that contractors do not utilize extractive efficiencies that result in comprised public goods and services. Such staff should be able to monitor how contractors deliver the good or service and hold them accountable for their performance. Real-time oversight of contracts can prevent, or at least decrease the severity of, contract problems, especially those that arise from extractive efficiency measures.

Cities and states should have laws and/or rules and procedures related to contract oversight. These rules should clearly specify who is responsible for various aspects of oversight before, during, and after a contract term, and requirements for contract oversight. Additionally, contracting agencies should adopt rules that provide additional guidance related to their specific mission -- for example, oversight of a technology contract will be different than oversight of a waste pick-up contract.

All staff involved in contract oversight, including formal contract managers as well as other positions that may include this responsibility or act as de facto contract managers, should receive training. Well-qualified contract managers should have substantive knowledge of their agency's service and mission as well as contract management skills. Managing contractors requires a unique skillset, including specialized knowledge about contracting best practices, applicable rules and laws around contracting, incentive structures, how to identify the use of extractive efficiency measures, and monitor performance of the contractor.

Maintain accurate and transparent public records about government spending

State and local governments should track how much money is spent on private contracts, how many workers are employed by those contracts, and what worker wages are. This information should be readily available to the public. While researchers estimate that total state and local procurement may be roughly valued at $2 trillion,[5] it is difficult to know exactly how accurate this figure is and importantly, difficult to know how much contracting takes place and how much public money is diverted from the public good to corporate profits. Moreover, important details about these contracts are often unknown since many governmental entities do not systematically collect and make this information public. It is essential that jurisdictions understand how much of its budget goes toward contracting and how much public money is taken for corporate profits. This lack of financial transparency and contract data makes it difficult to evaluate whether contracts are truly bringing smart efficiencies to governments, or whether they are extractive.

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1 https://sanantonioreport.org/san-antonio-contractors-road-projects-accountability-ordinance/

2 https://www.pjstar.com/story/news/education/2022/02/09/new-legislation-illinois-underway-to-improve-school-lunches/9299690002/

3 https://www.ilga.gov/legislation/billstatus.asp?DocNum=4813&GAID=16&GA=102&DocTypeID=HB&LegID=139272&SessionID=110

4 https://www.pjstar.com/story/news/education/2022/02/09/new-legislation-illinois-underway-to-improve-school-lunches/9299690002/

5 Donald Cohen and Allen Mikaelian, "The Privatization of Everything," 2021, pg 290.

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