United States General Accounting Office

GAO

Glossary

July 1997

Terms Related to Privatization Activities and Processes

GAO/GGD-97-121

ORDERING INFORMATION

Copies of this glossary can be ordered by mail from the:

U.S. General Accounting Office
P.O. Box 6015
Gaithersburg, MD 20884-6015

or by visiting:

Room 1100
700 4th St., N.W. (corner of 4th and G Sts., N.W.)
U.S. General Accounting Office
Washington, D.C.

Orders may also be placed by calling (202) 512-6000 or by fax using number (303) 258-4066, or TDD (301) 413-0006. On the Internet, visit GAO's World Wide Web Page at: http://www.gao.gov to access this glossary.

Privatization and Government Reform

In recent years, various initiatives have been pursued at the federal level that were aimed at rethinking the role of the federal government, initiatives that, in many cases, mirror efforts at the state and local level, as well as efforts in other countries. Some of these initiatives have included outright elimination or sale of a federal function, the devolution of responsibilities to another government, or the restructuring of a particular function's operations to improve its efficiency and/or service quality. Any of these initiatives may bring the private sector into the ownership and/or management of public assets, or into the direct provision of public services—changes that are often broadly described as "privatization."

These initiatives have engendered the use of a wide variety of terms, many of which overlap but may have subtly different meanings. For example, the terms "contracting out" and "public-private partnering" both involve some form of contractual relationship but are different in the requirements that are to be met by the private-sector entity.

This glossary is intended to facilitate a better understanding of privatization-related terms as they are used in the federal government. The glossary provides a working description of different terms, recognizing that the meanings of terms can and do evolve and that specific terms may have different meanings depending on the context in which they are used. Our objective was to describe the most commonly used practices and techniques currently employed to shift governmental functions and responsibilities, in whole or in part, from the federal government to the private sector. We also define some business practices that are not outright privatization but that use approaches that are similar to privatization techniques, as well as some operational practices that are associated with federal privatization decisions.

As we developed this glossary, we relied primarily on four glossaries already in print, as well as on other information published by experts and practitioners. We identified common terms in these glossaries and in the literature, and synthesized these terms to develop working definitions reflecting current federal usage. The four glossaries are (1) Privatization: Meanings, Rationale, and Limits, Congressional Research Service, February 9, 1996; (2) An Action Agenda to Redesign State Government, National Governors' Association report, 1993; (3) The Privatization Primer, National Council for Public-Private Partnerships, 1996; and (4) Glossary, National Academy of Public Administration Foundation, 1995. The Office of Management and Budget's (OMB) revised Circular A-76 and documents from the National Performance Review (NPR) were also used. This glossary is an expanded version of a glossary originally published in our report entitled Privatization: Lessons Learned by State and Local Governments (GAO/GGD-97-48, Mar. 14, 1997).

This document was prepared at the request of Representative Scott Klug. Major contributors to this glossary were John Needham and Don Bumgardner. Please contact me on (202) 512-9039, or John Needham on (202) 512-5274, if there are any questions.

Michael Brostek
Associate Director, Federal Management
and Workforce Issues

Glossary

Activity-Based Costing (ABC)

ABC is a methodology that assigns costs to products or services based on the resources they consume. It assigns functional costs, direct and indirect, to the activities of an organization and then traces activities to the product or service that caused the activity to be performed. ABC gives visibility to how effectively resources are being used and how all relevant activities contribute to the cost of a product or service. Such information may be key to making decisions about whether to restructure or privatize an activity.

Asset Sale

An asset sale is the transfer of ownership of government assets, commercial-type enterprises, or functions to the private sector. In general, the government has no role in the financial support, management, or oversight of a sold asset. However, if the asset is sold to a company in an industry with monopolistic characteristics, the government may regulate certain aspects of the business, such as utility rates.

Commercial Activities

The term commercial activity is used in the governmental context to identify those activities that the government performs with its employees or resources but could obtain from private-sector sources. Commercial activities are in contrast to “inherently governmental” activities.

Competition

Competition occurs when two or more parties independently attempt to secure the business of a customer by offering the most favorable terms or highest quality service or product. Competition in relation to government activities is usually categorized in three ways: (1) public versus private, in which public-sector organizations compete with the private sector to conduct public-sector business; (2) public versus public, in which public-sector organizations compete among themselves to conduct public-sector business; and (3) private versus private, in which private-sector organizations compete among themselves to conduct public-sector business.

Contracting Out

Contracting out is the hiring of private-sector firms or nonprofit organizations to provide goods or services for the government. Under this approach, the government remains the financier and has management and policy control over the type and quality of goods or services to be provided. Thus, the government can replace contractors that do not perform well.

Divestiture

Divestiture involves the sale of government-owned assets or commercial-type functions or enterprises. After divestiture, the government generally has no role in the financial support, management, regulation, or oversight of the divested activity.

Employee Stock Ownership Plans (ESOP)

Under an ESOP, employees take over, or participate in, the management of the organization that employs them by becoming shareholders of stock in that organization. In the public sector, an ESOP can be used in privatizing a service or function. For example, in 1996, the Office of Personnel Management established an ESOP for its former employees who perform personnel background investigations.

Franchising of External Services

Under the franchising of external services, the government grants a concession or privilege to a private sector entity to conduct business in a particular market or geographical area—for example, operating concession stands, hotels, and other services provided in certain national parks. The government may regulate the service level or price, but users of the service pay the provider directly.

Franchising of Internal Services

Under the franchising of internal services, government agencies provide administrative services to other government agencies on a reimbursable basis. Franchising gives agencies the opportunity to obtain administrative services from another governmental entity instead of providing them for themselves. In the federal government, these arrangements are often called interservice support agreements (ISSA).

Government Corporations

Government corporations are separate legal entities that are created by Congress, generally with the intent of conducting revenue-producing commercial-type activities, and that are generally free from certain government restrictions related to personnel and procurement.

Government-Sponsored Enterprises (GSE)

GSEs are federally established, privately owned corporations designed to increase the flow of credit to specific economic sectors. GSEs typically receive their financing from private investment, and the credit markets perceive that GSEs have implied federal financial backing. GSEs issue capital stock and short- and long-term debt instruments, issue mortgage-backed securities, fund designated activities, and collect fees for guarantees and other services. GSEs generally do not receive government appropriations.

Inherently Governmental Activities

An inherently governmental activity is one that is so intimately related to the public interest that it must be done by federal employees. These functions include those activities that require either the exercise of discretion in applying government authority or the making of value judgments in making decisions for the government. Governmental functions normally fall into two categories: (1) the act of governing, i.e., the discretionary exercise of government authority, and

(2) monetary transactions and entitlements.

Joint Ventures

See public-private partnership.

Managed Competition

Under managed competition, a public-sector agency competes with private-sector firms to provide public-sector functions or services under a controlled or managed process. This process clearly defines the steps to be taken by government employees in preparing their own approach to performing an activity. The agency's proposal for providing the service, which includes a bid proposal for cost-estimation purposes, is useful in competing directly with private-sector bids.

Most Efficient Organizations (MEO)

In certain circumstances under OMB Circular A-76, agencies that are considering contracting out an activity must first conduct a cost benefit exercise to identify the MEO. The MEO refers to the government's in-house organization that would most efficiently perform a commercial activity after a managed competition under A-76. It may include a mix of federal employees and contract support and is used as the basis for measuring all government costs (direct and indirect) and performance against competitive contractor or interservice support agreement (ISSA) offers. To determine the MEO, the in-house activity may reinvent, reorganize and restructure itself, including making capital investments, in order to arrive at the agency's most efficient method of performing the commercial activity.

OMB Circular A-76

OMB Circular A-76 sets forth federal policy for determining whether commercial activities associated with conducting the government's business will be performed by federal employees or private contractors. Recent revisions to the A-76 Supplemental Handbook were designed to enhance federal performance through competition and choice, seek the most cost-effective means of obtaining commercial products and support services, and provide new administrative flexibility in agency decisions to convert to or from in-house, contract, or ISSA performance.

Outsourcing

Under outsourcing, a government entity remains fully responsible for the provision of affected services and maintains control over management decisions, while another entity operates the function or performs the service. This approach includes contracting out, the granting of franchises to private firms, and the use of volunteers to deliver public services.

Performance-Based Organizations (PBO)

Under a PBO, policymaking is to be separated from service operation functions by moving all policymaking responsibilities to a presidential appointee. The service operations are moved to an organization to be headed by a chief executive officer (CEO) hired on a competitive contract for a fixed term. The CEO's contract defines expected performance, and in exchange for being held accountable for achieving performance, the CEO is granted certain flexibilities for human resource management, procurement, and other administrative functions. As of March 1997, several PBOs had been proposed, but no PBO had been authorized in the federal government.

Privatization

The term privatization has generally been defined as any process aimed at shifting functions and responsibilities, in whole or in part, from the government to the private sector.

Public-Private Partnership

Under a public-private partnership, sometimes referred to as a joint venture, a contractual arrangement is formed between public- and private-sector partners that can include a variety of activities that involve the private sector in the development, financing, ownership, and operation of a public facility or service. It typically includes infrastructure projects and/or facilities. In such a partnership, public and private resources are pooled and responsibilities divided so that the partners' efforts complement one another. Typically, each partner shares in income resulting from the partnership in direct proportion to the partner's investment. Such a venture, while a contractual arrangement, differs from typical service contracting in that the private-sector partner usually makes a substantial cash, at-risk, equity investment in the project, and the public sector gains access to new revenue or service delivery capacity without having to pay the private-sector partner. Leasing arrangements can be used to facilitate public-private partnerships.

Service Shedding

Divestiture through service shedding occurs when the government reduces the level of service provided or stops providing a service altogether. Private-sector businesses or nonprofit organizations may then step in to provide the service if there is a market demand.

Subsidies

The government can encourage private-sector involvement in accomplishing public purposes through direct subsidies, such as the funding of low-income housing, or tax subsidies, such as research and development tax credits.

User Fees

User fees require those who use a government service to pay some or all of the cost of the service, rather than having the government pay for it through revenues generated by taxes. The fees charged for entry into public parks are an example of a user fee.

Volunteer Activities

Volunteer activities are conducted through either a formal agency volunteer program or a private nonprofit service organization. An activity in which volunteers provide all or part of a service and are organized and directed by a government entity can also be considered a form of outsourcing.

Vouchers

Vouchers are government financial subsidies given to individuals for the purchase of specific goods or services from the private or public sector. The government gives individuals redeemable certificates or vouchers to purchase the service in the open market. Under this approach, the government relies on market competition for cost control and on individual citizens to seek out quality goods or services. The government's financial obligation to the recipient is limited to the amount of the voucher. One form of voucher is a federal grant given to a state or local government, which then may use the funds to buy services from the private sector.