

PRIVATIZATION STUDY

Forms of Privatization: excerpted from Government Privatization: history, Examples, and Issues issued by the Commission on Government Forecasting and Accountability, Springfield, IL; October 2006

Forms of Privatization

Five forms of privatization are identified by Richard C. Brooks in his paper “Privatization of Government Services: An Overview and Review of the Literature.” These five forms of privatization are:

- Complete Privatization
- Privatization of Operations
- Use of Contracts
- Franchising
- Open Competition

Complete Privatization

Complete privatization is the outright sale of government assets to the private sector. This type of privatization not only confers assets but also related responsibilities of ownership to the private sector. Government run industries and assets have generally been completely privatized through one of three main ways. The first way is share issue privatization. The government sells shares of the government run company which can then be traded on various stock markets. Share issue privatization has been the most prevalent method used, though a developed secondary market is necessary. The second method is through asset sale privatization. In this method, the whole firm or asset is sold to an investor. This is usually done by auction. The final method is voucher privatization in which shares of ownership are distributed to all citizens for free or for a very low price. Complete privatizations have been seen mostly in the transition economies of Central and Eastern Europe in recent years.

Complete privatization has been somewhat rare in the United States due to the market driven economy and federal regulations associated with the sale of public assets that were built using federal grants. An example of this kind of transaction in the U.S. can be seen in the sale of the Fairbanks Municipal Utilities System for \$R100 million in 1996. The company was sold by the City of Fairbanks under provisions that kept utility rates within certain ranges and provided for stable employment.

Privatization of Operations

The privatization of operations is the turning over of managerial and operational responsibilities of publicly owned facilities to private sector firms. This kind of privatization is often seen with

the running of sports and concert venues. Under this arrangement, the private sector firm generates revenue through the collection of fees from individual customers of the government asset. For example, the sports stadiums in New York City are managed by the baseball teams that use the facilities during the baseball season but are run by the New York City Department of Parks during the off season. This kind of arrangement can also be seen in transactions concerning the operation and maintenance of toll roads and toll bridges.

Contracting Out

Contracting out is the production of designated services by a private firm under a contract. Under this scenario, the private sector firm is paid directly by the government for their services. The government finances these services through the taxes of the collection of user fees. This type of arrangement is commonly used for the collection and disposal of solid waste. Other types of services that have been privatized through this type of agreement include security services, data processing services and consulting services for numerous professions.

Franchising

Franchising is the awarding of exclusive rights to perform services within a specific geographic area to a private firm by a governmental unit. The private firm generates revenue by collecting user fees. Cable television is the most common example of this kind of privatization. Utilities such as electricity, gas, and water service could also fall under this category.

Open Competition

Open competition is the last form of privatization under this classification. Open competition is similar to pure competition as many private firms are allowed to compete for customers within a governmental jurisdiction. This type of privatization can potentially be seen in telephone and internet service providers. This type of privatization is not appropriate for some services as it most likely would not be efficient to have multiple suppliers of electricity, gas or water service.