



## YIELD TO THE MARKET

### How Prosperity Districts Would Competitively Furnish Municipal Services

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The Prosperity District concept envisions a local community in which government is greatly limited to a level of involvement in peoples' everyday lives and exchange interactions reminiscent of that which existed in early 19<sup>th</sup> century America. Regulation would be minimized. State government would play a role only to the extent absolutely necessary to meet constitutional requirements. Local government within a District would take on a completely different character compared to local governments today, with a purposely hands-off philosophy and purposely minimalistic to the point that local government would directly produce little in public services. Local government would act primarily as a contracting authority, arranging with private companies to build and manage traditionally publicly-provided assets and services through public-private partnerships (PPPs) or otherwise outsourcing services to other existing governmental bodies through managed competition.<sup>1</sup>

This concept is not at all far-fetched... Communities have long experimented with privatized public services.

#### **An Extension Of Existing Examples**

This concept is not at all far-fetched. Economist Gabriel Roth wrote a book entitled *The Private Provision of Public Services in Developing Countries* about the phenomenon throughout the globe.<sup>2</sup> Sandy Springs, Georgia, a previously unincorporated community that got frustrated with poor service from the county, is famous for having privatized virtually every aspect of city management (the chief exception being public safety) from the very beginning of its incorporation.<sup>3</sup> Another community, Johns Creek, Georgia, followed suit a year later, although it has not gotten as much attention as Sandy Springs.<sup>4</sup> Communities have long experimented with privatized public services, especially refuse collection (generally a money saver),<sup>5</sup> fire services,<sup>6</sup> ambulance services,<sup>7</sup> and municipal building maintenance.<sup>8</sup> Roads have long been subjects of privatization efforts.<sup>9</sup>

The Prosperity District concept would expand on the Sandy Springs/Johns Creek example of total privatization, possibly expanding it to include public safety services. In principle, there is no reason to exclude public safety from being privatized except for cultural considerations; however, managed competition in law enforcement services is recommended for all but the most sophisticated districts.

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## Introduction

What follows is a discussion of the traditional model of public service provision wherein government internalizes the production of services, looking at its strengths and weaknesses from a public choice point of view, focused on incentives inherent in such a system. The same type of analysis is done with respect to PPPs. Then, separate discussions of the advantages, disadvantages and possibilities for the contracting with private entities by a Prosperity District for public services, specifically roads, water/sewer, electricity, fire services, police, refuse collection, and public education.

The Prosperity District concept to which this paper is written contemplates a polity in which the establishment of monopolies is prohibited. However, most PPPs are contracted for services that are, for all intents and purposes, monopolized by government. The competition enters into the picture through careful construction of the PPP contract, holding the provider to strict standards with the possibility that the contract can be renegotiated with someone else. Most of the discussion that follows presumes this type of PPP. However, many of the services discussed in this paper could have more than one PPP operating simultaneously, if that is what is required in order to keep from violating the Prosperity District's principles of organization. However, two different PPPs for water supply, for example, are not likely to serve the same territory simultaneously.

The privatization of the services just mentioned above could individually constitute a paper dozens of pages long. Such detail is beyond the scope of this paper. Instead, the discussion is focused on the possibility of privatizing each service in the context of the Prosperity District proposal wherein eminent domain and monopolies are prohibited, and taxes will be limited, necessitating greater dependence on user fees.

## The Traditional Model of Service Provision

The traditional model of public service provision purposefully conceives a top-down approach wherein elected officials dictate policy and dedicated public servants seek to carry it out. Services are directly provided by government. Public servants are presumed to be blank slates on whom are written the express desires of their elected bosses. Elected officials are assumed to have the wisdom, foresight, listening skills, clairvoyance, and technical knowledge to know and understand the desires, needs, and priorities of the general public. Public servants are assumed to always tell their elected bosses the truth and to have no ambition but to carry out the explicit and

implicit instructions of their bosses in the form of laws, and rules derived from statutes, that can be decades old. Discretion on the part of public servants in the traditional approach to public service provision is supposedly allowed only to the degree that they pursue the policies and policy priorities that have been dictated to them. This implicit assumption is made despite the fact that policy makers often know only a fraction of what public servants know.<sup>10</sup>

Max Weber is often credited with articulating the theoretical foundations of the traditional model of public service provision. But, he arguably simply described management forms that already existed in Prussia. Woodrow Wilson is also credited with popularizing the idea that policy setting and administration can be treated and conceived as two separate spheres, with the inherent assumption that administrators will carry out dictated policies in good faith, with efficiency, and perhaps even enthusiasm.<sup>11</sup> Today, the traditional model is often viewed as hopelessly idealistic and naïve, if not simply ideological, by economists and others who have come to understand that every individual acts in his own self-interest and according to incentives. Nevertheless, there continue to be made theoretical justifications of Weber and Wilson even though the traditional model is quite old.

The strengths of the traditional model include: 1) the potential of direct accountability to top government officials, 2) ready standardization of services across many polities in a federal system, 3) the use of eminent domain (and consequent ease of action on the part of government, which is not necessarily best for all property owners), 4) ready access of citizens to services, and 5) ease of taking action on the part of bureaucrats who have been granted authority.

As will be discussed below, some of these advantages can also be viewed as weaknesses, but for now, consider how they are strengths. First, the top-down system, at least theoretically, provides accountability for the bureaucrats who are tasked with carrying out policy. They answer to officials who, in a system like that employed in the United States, are answerable to the people through regular elections. Indirectly then, bureaucrats are answerable to the people who they serve, and at least in the case of agency heads, bureaucrats are fairly easy to replace, should the executive elected official decide such action is necessary.<sup>12</sup>

Second, governments generally do not have proprietary interest in their methodologies and systems. Thus, there is no issue with sharing how they accomplish their tasks. As a result, there is no real hesitancy in sharing knowledge and stan-

standardizing methods as well as systems across jurisdictions. In fact, government officials commonly form associations for the offices they occupy that represent all jurisdictions. Thus, county assessors have a county assessors association. Mayors have an association. So do school superintendents. When they meet, they share knowledge and jurisdictions become similar in ways that allow citizens to know what to expect from jurisdiction to jurisdiction.<sup>13</sup>

Third, government's ability to fall back on eminent domain as a way to keep costs low and prevent hold outs to assemble properties needed for important public infrastructure investments is a definite advantage for governance. While resentments on the part of property owners whose land has been condemned and legitimate uncompensated harm cannot be

all government-provided services, even one as important as water, allow for universal access.<sup>14</sup>

Finally, traditional government service provision theoretically enjoys a relative ease with which those in charge can take action. Though executive authorities face legal constraints, there is a degree to which they can direct, expedite, and expect immediate action when changes are made due to new ideas or circumstances. It can be much harder to make changes when contractual, arm's length, formal agreements are involved.

The traditional model also has its disadvantages, which are significant. In fact, virtually any of the advantages for the traditional model can be a disadvantage. For example, universal access to public services can be an advantage for a polity, if competing polities do not provide universal access, but it can

## Disadvantages of Traditional Government Service Provision

- Poor incentives for efficiency and effectiveness
- Overuse of resources
- Budget cycling encourages waste
- Potential for corruption
- Taxpayers "Left Holding the Bag"

completely eliminated, improvements and projects proceed with relatively little interference and lower overall costs to the community. The downside, of course, is the fact that force is ultimately involved with the exercise of eminent domain and its use can result in projects of excessive size and scope. No matter how much due process is involved, eminent domain arguably makes government projects less expensive than they would otherwise be and has the potential of leading to an inefficient allocation of resources.

Fourth, the traditional model of public service provision allows for universal access of services. Often, this is true regardless of how much one helps to cover the expenses of government services. For example, in most communities everyone can avail themselves of police and fire services as well as access to streets whether one pays a million dollars in taxes or nothing at all. Sanitary sewer is not even designed to be denied to a structure once it is attached to the system, except that it can be non-existent, and even then, traditional government requires that sanitary measures be taken by property owners. Water service, however, is deniable based on lack of payment with valves that can be turned off and locked. So, not

also be a disadvantage when its citizens treat a valuable resource as if it is costless, as people generally do with roads. Congestion during rush hours is the result, often with excess capacity during other hours of the day, which is wasteful.

The disadvantages of the traditional model of public service provision include: 1) poor incentives for efficiency and effectiveness, 2) overuse of resources, 3) budget cycling that encourages waste, and 4) potential for corruption. Oftentimes, these problems are characterized as "government failure," in contrast to "market failures" that are often used as justifications for government provision in the first place.<sup>15</sup>

First, there is generally a significant disconnect between consumers of a government-provided good or service and those who produce it. This can be true of markets, too, but consumer service is incentivized in the private sector as much as possible because if consumers are discouraged from buying from a producer, the producer loses money. The government does not lose money when service is poor because the bulk of government revenue comes from taxes, which are extracted by threat of the legitimate use of force. Where a government service results in revenues through fees, government is almost



always a monopolist, as is generally the case with trash collection, water delivery, and sometimes even electricity. Monopolists concern themselves relatively little with consumer service unless there is a chance that another producer could enter the market. Governments have their monopolies by law which gives the government monopolist all the more a tendency to ignore consumers complaints.

Second, while on the one hand, universal access to government services can be viewed as a strength, it is also a weakness. A zero price produces very high demand, as in the case of roads during rush hours. Uniform pricing makes no distinction between those who have genuine need versus those who simply can pay. In other words, due to a lack of pricing, or inefficient pricing due to the lack of a profit motive, the traditional model results in resource waste.

Third, a presumption of the traditional model is that government agents (bureaucrats) have an incentive to faithfully carry out the wishes of the peoples' representatives. In reality, there are many conflicting pressures on bureaucrats. They have their own ambitions, which are often pointed at empire-building for their agency. Sometimes, ambitions are turned toward looking forward to a related and lucrative position in the private sector. This often leads to excessive spending and inefficient action, especially when these two motivations do not conflict, which is often.<sup>16</sup>

Fourth, officials in charge of accomplishing tasks under the traditional model of government provision often do not have extensive experience. There is a tendency to accomplish tasks and organize operations the way they have always been done. This is human nature. Due to a lack of competition, there is little incentive to experiment and discover greater efficiencies and effectiveness.

Ultimately, the biggest disadvantage for the traditional model of government provision is that taxpayers – the people in general – are left holding the bag. Government's errors and inefficiencies, whether intentional or not, cost people wealth, income, and opportunity. Obviously, costs must be considered in light of benefits. None of this is to say that government represents a net negative, just that the net benefits could be larger. This is the hope and promise of the public-private partnership (PPP) model of public service provision.

### **The Public-Private Partnership Model**

Public-private partnerships, as the term is used here, are an alternative to the traditional model of public service provision. The term is often used to describe instances where

## **PPP Advantages**

- Private sector efficiency and effectiveness
- Flexible budgeting
- Transferring risk to contractor
- Blunting downstream political influence

government subsidizes private industry, often to attract industries that elected officials and politically connected elites in a community consider desirable. Occasionally, the term is used to characterize situations where government seeks to piggy-back on private development and extort a developer to provide something normally financed through taxes, like a park. A PPP in the context of this paper is when government arranges to have the private sector provide a good or service that government normally provides through a contractual arrangement that, hopefully, exploits the many positive incentives inherent in competitive private enterprise.

The private sector, due to the profit motive and competitive enterprise, has a strong incentive to economize on resources and, in so doing, increase the net benefit of an endeavor for business owners and their customers by innovating to undercut competitors' prices. Private producers also have an incentive to add consumer value to their product to make it more desirable compared to competitors, increasing net benefit all the more. PPP arrangements of the type proposed under the Prosperity District concept seek to capture private sector incentives to add net value of public services for citizens.

Through proper competitive contracting under a PPP, citizens can benefit from the extensive experience that private companies accumulate in providing services in a variety of settings with a variety of expectations, sometimes all over the world.<sup>17</sup> Such extensive expertise is lacking in most local government administrations. If contracts are properly written to provide correct incentives and then rigorously administered and enforced, citizens can enjoy a great deal of added value from government-provided services. Potentially with PPPs, incentives align better with the interests of citizens in that the self-interest inherent in human exchange interactions – the profit motive in commercial transactions – simultaneously



creates net value for citizens. Too often, the traditional model relies on the hope that government officials will simply do the right thing when self-interest dictates otherwise.

Another strength of the PPP model is that budgeting can often be more flexible. Government budgeting tends to be all-or-nothing. Once yearly budgeting is completed, say for road maintenance versus construction and reconstruction, the relative amounts can only be altered by going back to the budgeting authority. This can be very problematical when meetings do not occur frequently and unforeseen events arise. With a PPP, flexibility can be written into a contract with overall system metrics used to judge performance and the private contractor allowed to respond accordingly. In addition, competitive forces push bidders to offer marginal unit pricing for their services over the course of a contract as opposed to the lumpy pricing that occurs with project-by-project contracting that occurs when government entities hire private contractors for individual projects.

With skillful and proper contracting, a PPP agreement

a favored political connection but not the community as a whole, it would also tend to intrude on a PPP road contractor's bottom line. The contractor has an incentive to push against purely political considerations.

On the other hand, PPPs have their own drawbacks. If these drawbacks are recognized from the beginning, they can be successfully guarded against. However, there will doubtlessly be unforeseen circumstances that arise which will occasionally challenge the advantages of PPPs. Contracts must be constructed in a way that anticipates as many of the foreseeable issues as possible and rigorous, dedicated effort on the part of government authorities is part of the PPP contracting process.<sup>19</sup>

First, there is a lack of experience among government officials in PPP contracting. Europe has used PPP methodologies for many years, especially with respect to roads.<sup>20</sup> In general, however, there has been relatively little interest in this type of provision of services that are traditionally government provided in the United States. Expertise is therefore relatively

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can transfer a considerable amount of risk to a private entity and away from taxpayers. In so doing, superior incentives over the traditional model can result. For example, if a private company is provided a long term PPP contract to maintain a road network and it is determined that a new road to relieve congestion is required, the company will have an incentive to build the new road well and to locate it to relieve as much congestion as possible. Under the traditional model, road contractors' only incentive is to maximize profit, which can lead to cut corners and absolutely no concern about good design and location. A PPP contract can be constructed to measure traffic flows and reward the contractor for improving movement. A contractor also has an incentive to keep maintenance costs low if the contract is long-term, so roads get built to last.<sup>18</sup>

A not so obvious benefit of risk transfer with PPPs is that PPPs have an incentive to push back when political considerations would result in inefficiency. For example, if a politician were to propose a new road located in a way that benefits

scant on the governmental side. On the other hand, some U.S. firms have partnered with foreign corporations to provide services elsewhere under PPPs. Also, private companies can rely on legal expertise that has specialized in serving the private sector side of PPP deals.

Local governments are especially at a disadvantage in the back and forth of PPP contract negotiation. They often cannot afford the high-powered legal and consulting services often necessary to aid in avoiding being bested at the negotiating table. Nevertheless, PPP contracting is common enough now that entities like the Reason Foundation have built enough connections and expertise to aid interested government officials in avoiding the worst pitfalls of PPP contracting.<sup>21</sup> The World Bank serves as a PPP resource as well.<sup>22</sup>

Because PPP contracts are often long-term, they can represent large money streams, the sort of money that can attract the sort of bad actor that might do anything, including committing fraud or bribery, to get the contract. Thus, PPPs are



not a slam dunk to solve corruption problems that might arise with the traditional model. In fact, a system of checks and balances using lawyers, auditors, and consultants in negotiating PPPs would be wise to establish.<sup>23</sup>

Finally, when government services are produced “in-house,” there are intangibles in managing service production directly as opposed to an arm’s-length arrangement like a PPP contract. For example, there are some circumstances that a contract might not have foreseen. Unless a contract is written in a way that gives the contracted party a great deal of flexibility, an unforeseen contingency would force a renegotiation of the contract, which can be time consuming. Direct control by governmental authority, on the other hand, allows for quick decision-making when new and unexpected contingencies occur. Contracts must therefore be written to allow for quick communication with the contracting authority in order to react to unforeseen contingencies.

### **Why Some Services are Provided by Government**

Several services are commonly provided by various levels of government. For many, it is unimaginable that they could be provided in any way other than directly by government. To be clear, PPPs do not completely remove a central authority from the provision equation. Instead, PPPs turn the central authority into a contracting entity, with full authority to negotiate, administer, and enforce the contracts with private entities who directly provide the services. Nevertheless, many are uncomfortable with private entities directly providing/administering water and sewer services, law enforcement to include police and incarceration services, roads, fire and emergency, electricity infrastructure, and education services.<sup>24</sup>

Oftentimes, people who object to PPPs are reacting from an emotional or instinctive level. They object to changing more than anything else and simply cannot imagine that any other way of doing things could work as well as what they already know. Economist Walter Block has written of an American’s experience who, while visiting Great Britain, once suggested that phone services in Europe would be better if they were provided by private companies rather than by the government. The reaction was shock that such an important service could possibly be privately provided, even as he could attest how much better phone service was in the United States, where private companies provided it.<sup>25</sup>

On the other hand, economists often cite technical reasons as to why some services must be provided by government. Natural monopoly is one reason. In simple terms, this

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is a condition where average costs fall continuously as scale of production increases, even as output rises to large levels. To put it another way, one producer can produce more cheaply than two since duplication of effort would halve the scale of each producer and increase average costs. This implies that a monopoly is better than competition, except that economists know monopolists have a tendency to overprice and underproduce. Two methods have been used to solve this dilemma – regulation of a single private company by government while granting that company exclusive rights to serve a region, and direct government production. Both methods of control are supposedly carried out in “the public interest,” however that is defined. Both also entrench those who carry out production, making it nearly impossible to transition to some other producer.

Another issue is externalities. When people bring up health and safety issues, they are, from an economic perspective, talking about externalities. The concept of an externality is simply the idea that one’s actions don’t just affect one’s self, but also affect others. So, in the third world, when people throw raw sewage in the street, they are protecting their health inside their home, but they are simultaneously harming everyone else who has to move about on the street. This is an example of a negative externality and why government is almost inevitably intimately involved in providing for sanitary sewers.

Another reason government provides services is that certain services, once produced, benefit everybody, whether everybody pays for them or not. National defense serves as the best example of this phenomenon. Once produced, national defense protects everyone within a nation regardless of whether they helped pay for its production. Taxes are assessed to force everyone to pay since the incentive is to free-ride (en-



joy the benefits without paying). Under such circumstances, it almost seems natural that government would directly provide that for which it demands everyone's money. In economic parlance, services everybody benefits from even if they do not pay are public goods.

A public good, to economists, is not merely something government has decided to finance or directly provide. If someone hires a service to keep them safe in their neighborhood, to some extent, others benefit from the increased security. It's impossible to keep others from so benefiting, meaning the service is nonexcludable. But, just because one person benefits, this fact does not diminish how much anyone else benefits, which means the service is also nonrival. These are the two characteristics of a public good and these characteristics make it easy and desirable on the part of others to free ride. But if people free ride, it's unlikely desirable public goods will

tary services is included in the health care category. Only basic education can be thought of as a public good, and that is arguable.<sup>26</sup>

Refuse collection is not truly a public good except to the extent that it benefits general public health. Refuse collection does not offer much in the way of economies of scale. Clearly, the main justification to have government collect refuse is to protect public health and to make sure all refuse is collected regardless of who produced it or whether they can pay to have it removed – again, for public health. Refuse collection, however, is not that expensive, and has a long history of being privatized. Public health can be protected by requiring refuse to be collected at each address and fining anyone who does not do so.<sup>27</sup>

Water and sewer services lend themselves to natural monopoly, with sewer being a public good to the extent that it

## Avoiding PPP Pitfalls

- Negotiate through expert analysts, lawyers and accountants
- Establish a transparent system of checks and balances involving independent auditors to prevent corruption
- Write PPP contract for flexibility and quick communication with the contracting authority in order to react to unforeseen contingencies

be produced at all, unless government steps in.

Few services that government provides are pure public goods. Foreign diplomacy is one. Prisons are as well, since everyone benefits from having criminals off the streets. Other services provided by government see differing degrees of rivalry and excludability. Individuals can be easily excluded from consuming road, police, and fire services with fences and the simple refusal to answer calls. Also, no two vehicles can occupy the same spot on a road. Similarly, a policeman or fireman cannot be two places at one time. So though road, police and fire services are considered public goods, this is mainly because it is so common for government to produce them. Education and health care are hardly public goods at all, unless disease prevention through pest control and sani-

is a public health issue. Although it is often the case that a city might have several zones or territories of separate pipeline networks, it would be more costly to have multiple pipelines servicing the same area. Water and sewer services, as alluded to above, also solve externality problems by preventing the filth from one household or business from impacting another. Clean water delivered sanitarily through community-provided pipes also prevents road congestion from delivering water by truck and guards against contamination and mosquito infestations where a few households might attempt to store and provide for their own water supply.

In order to provide for a pipeline network, it is sometimes necessary (or at least it is difficult to cheaply avoid) routing sections through private property. In so doing, this has often



led to the exercise of eminent domain since a private property owner can effectively extort exorbitant sums from the community. A good rule of thumb is that eminent domain should never be exercised to benefit a private party. Were water and sewer provided by private companies, assembling a pipeline network at reasonable cost could be difficult without eminent domain, but allowing private companies to exercise eminent domain is almost unthinkable in a polity that understands the value of private property. Thus, one reason for having government provide services that require the assembly of tracts of property rights like roads and pipelines is to avoid turning private property over to private entities through the use of eminent domain.

Police and justice services are not pure public goods, but they come close. The free rider problem and the possibility of under-provision are quite possible were these services not government-provided. In addition, it is difficult to conceive that laws would be consistently enforced were law enforcement privately and individually financed and provided by a plethora of firms. Policies would be arbitrarily determined by private individuals paying their private security services' bills. It is also inconceivable by concepts of justice today that private individuals could, by their own authority, incarcerate other individuals. This is a job for a collectivized justice system, at some level, that enjoys the moral authority and support of the community as well as constraining rules, along with an adversarial advocacy system. Finally, equipment and property needs create some economies of scale for policing and incarceration services, giving public safety some degree of natural monopoly.

Roads are not public goods. However, there is a degree of economies of scale in road construction and maintenance due to the heavy equipment needs to efficiently do the work. Although the technology exists today that will allow individual road users to be charged for every individual mile of different types of roads they use, this is a very recent development. Roads have historically been a job given to government in order to provide ready, low cost access to private property by individuals and in order to facilitate trade and other types of human interaction. What's more, government has the authority to establish rules and standards of road construction and conduct on the roads. Were roads privately owned, it would be difficult for individuals to cooperate to maintain them, individuals could be excluded from using a road to access his own property, and rules and standards would be more difficult to enforce. Finally, eminent domain becomes an issue as well,

as it is against the foundations of liberty to transfer property from one private party to another using eminent domain.<sup>28</sup>

Fire and emergency services are not public goods, either. It's easy enough to exclude someone from these services and while a fire crew is putting out one fire, it cannot simultaneously put out another across town. However, the equipment required to provide these services – expensive vehicles and places to store them – as well as the employment of specialized personnel, creates economies of scale to some degree. Externalities are also an issue, especially with fire services. Fire has a tendency to spread, so if one person's house catches on fire, it is often likely to spread to others. When a fire is put out, it is not just the people whose property is engulfed who benefit.

Electricity is often provided by government directly by cities and through cooperatives. Economies of scale again come into play. Eminent domain also comes into play in the need to provide for transmission lines and substations, although much like pipelines, access is through easements which do not require complete property ownership transfers. This was especially true in the dawn of the electric era when no one had planned for the need to make room for electrical equipment. Electricity generation and transmission, given current technology, also leads to natural monopoly due to lower average costs from large-scale generation plants and transmission territories as well as the benefits of not doubling up on transmission lines. Transmission networks, more than generation, are a source of significant economies of scale. Finally, due to the role scale has historically played, electricity transmission is highly integrated across state and community lines, partly to make electricity provision stable and reliable. Standards have had to be created and enforced by government in order to maintain that stability and a level of standardization that helps make it possible to use the same electrical appliance anywhere in the nation.<sup>29</sup>

Finally, public education is almost universally provided by government entities in the United States, namely school districts, county and city-level governments, all usually under state supervision. Externalities and the need to standardize education are the two most common arguments in favor of government provision of education. Another has to do with a notion of fairness to children in providing a modicum of equal opportunity by providing each child with the chance to easily gain at least a minimum amount of knowledge regardless of how much in resources a child's family possesses. In addition, most believe that there are externalities associated with poor education with the familiar notion that a commu-





## Natural Service Candidates for PPPs

- Roads
- Water and Sewer
- Electricity Transmission and Generation
- Fire and emergency services
- Refuse collection
- Education

nity can spend money now educating an individual or spend money later incarcerating that same individual.

### Advantages of Privatization of Government-provided Services

While it might be necessary for government to finance some services through taxation and forced fees, the perceived need for government to integrate bureaucracies that directly provide those services into the governance structure is simply incorrect. For example, when the State of Texas created a highway department in 1917 in order to comply with the first Federal Aid Road Act, the Texas Highway Department purchased equipment and its employees directly constructed roads.<sup>30</sup> Later, partly due to the ease with which the system could be corrupted with all operations done in-house, the Texas Highway Department switched to contracting with private companies to build and reconstruct roads.<sup>31</sup> Private companies are also contracted to do heavy maintenance and repair work with the department now carrying out only light maintenance.

Today, Texas' modern highway department, whose mission has since been broadened and has been renamed to the Texas Department of Transportation, is learning to rely on PPPs to accomplish its mission. Texas Highway 130, a toll road running north-south east of Austin as a relief route for Interstate 35, is a prime example. Much of that highway has been constructed as a result of a pure public/private agreement wherein a private company financed its construction in exchange for the right to manage the road and collect the tolls for a period of decades.<sup>32</sup>

#### Roads

The advantages of a PPP in limited-access roads like the U.S. interstates are manifest. First, a private company will demand at least some say in the routing of the road in order to

maximize its use and the revenue stream it will generate. Instead of political considerations such as making sure the road runs near the property of someone who is politically connected, the road will tend to be routed in a way that moves a lot of traffic, which is exactly what roads are intended to do.

Under a properly structured PPP for roads, the privately contracted entity also has an incentive to build the road to be durable so as to minimize long-term maintenance costs. Another incentive is to attract and keep traffic on the road. A road that is poorly maintained and rough will be avoided by drivers. Consequently, the private road provider will maintain the road in good shape.

Road durability and location are not the only aspects of road design. There are other issues that a private road provider will consider in order to make sure drivers who use the road will continue to do so. These elements include signage, banking of curves, and adequate road markings. Also at issue for the private provider will be liability issues that government road authorities often avoid simply by virtue of being part of the government and enjoying the rights of sovereignty. Overall quality of service from a road under a PPP should be significantly better than if the road were built and maintained by a government road bureaucracy.

In cases where a private road administrator controls pricing on a road where drivers directly pay tolls, the private provider will have an incentive to price according to real-time demand in order to minimize congestion and keep traffic moving. Profit is maximized by keeping traffic moving, with throughput at its highest possible level.

While government road agencies are often run by individuals who have long experience, it often is not that broad. While states like Texas and Arizona have a variety of climates, soils, and urban versus rural conditions, many states do not. Texas and Arizona do not have to deal with every challenging geographic condition that is possible, either. Private companies



like Zachary, one of the companies with the PPP on Texas' Highway 130, have an international, globe-wide reach. Consequently, their engineers and employees often have more varied experience of circumstances and have been able to learn from a larger worldwide pool of other engineers.

PPPs in roads see the private road contractor taking on financial risk instead of taxpayers. If a road agency builds a road in an undeveloped area in anticipation of development that never occurs, or if the agency locates a road due to political considerations so that net benefit from the funds spent on the road could have been much higher spent elsewhere, taxpayers bear the cost. They bear it financially out of their pockets and they bear it by foregoing roads that could have produced better value. If a private road contractor makes this sort of mistake, it suffers financially and might even go bankrupt. Were it to go bankrupt, the road will not disappear. In fact, such contracts see government retaining ownership of the road itself. What it sells is the anticipated cash flow. Thus, the incentive for a private party to a PPP to locate and build roads well, is very strong. Also, given the ownership rules, even if a private road management company goes bankrupt, the road does not disappear. Nor does cash flow.<sup>33</sup>

An advantage of a road PPP is that performance measures for roads are well-established. Road quality measures are well-known and understood. Contract administrators can easily observe whether construction standards are being met. Private firms can even be engaged to aid in making observations for performance checks.

PPPs in roads can be financed in a variety of ways, and private companies interested in gaining such a lucrative contract have an incentive to propose any number of them. Consequently, there is potential for a great deal of innovation in determining the financing of road PPPs, whether the roads are of the limited-access variety or if they constitute a local grid. Direct tolls are an obvious source of revenue for limited-access highways. Another system, one that does not require drivers to pay directly, is shadow tolls. With this system, government pays a toll for each vehicle that uses the road. Traffic counters determine the amount of traffic. The incentives for the private contractor under such a system are very nearly the same as for one with direct tolls. Shadow tolls, however, produce very different incentives for the consumers of roads since congestion pricing is not possible.

The technology exists whereby every vehicle could have a GPS-enabled unit installed that would determine road type and for every mile traveled by the vehicle. Drivers would then

be billed accordingly. This technology, however, is not widely accepted and would require some refinement to make it effective for congestion pricing.<sup>34</sup>

Under a road PPP, lines of accountability are clear. While it is possible that the private contractor could blame problems on the PPP contract and the contracting authority it deals with, for the most part the buck will stop with the contractor. Government direct provision of roads, on the other hand, is often like dealing with a committee arranged in a circle with everyone pointing toward the middle. In other words, blame for issues like poorly maintained roads is assigned by one party in government to every other party and it is rare that any one individual or subdivision in government actually takes responsibility. This is especially true at the state level where federal policies play a role in determining how roads are allocated and built.

While road PPPs, in principle, transfer risk from taxpayers to private providers, this depends greatly on the contracting skills of the governmental road authority. Contracting activity on the part of either the public authority or private entity is not a job for amateurs. There must be highly competent negotiators on both sides with expertise in road provision as well as in legal issues. Very often, the amateurs are on the government's side of contract negotiations, for the obvious reason that private companies have often negotiated many contracts in a variety of jurisdictions. Government authorities must exercise humility and hire outside expertise for contract negotiating if necessary.<sup>35</sup>

Administration of the contract over time is an issue as well, especially as a contract's duration is coming to a close and there is less and less for the private company to lose in failing to live up to the standards promised in the contract. Even though the intention behind PPP contracts is to incentivize the private entity to act in a way that is generally beneficial to the polity, it is difficult to cover every eventuality and nearly any contract can be gamed if one party develops bad intentions. Therefore, it is necessary for the governmental contracting authority to have expertise on staff in order to look over the shoulder of the private contractor with authority to enforce the contract and, if necessary, to impose sanctions specified in that contract or even to abrogate the contract if necessary.<sup>36</sup>

One of the problems government contracting authorities have is continuity, especially in democratic republics with periodic elections and executives who often make changes in the top echelons of agencies. Government, once it adopts PPPs as a policy, must commit to it regardless of partisanship. One



of the strengths of the Prosperity District concept is that the commitment to PPPs as a policy is made from the very beginning so that authorities within such a district will be committed by default.

An ever-present risk with government is corruption. So much money is at stake that it poses a large temptation. Road expenditures are often a large part of government budgeting and there are any number of ways to exploit the system for illicit gain, everything from substituting a substandard but cheaper mix of concrete compared to what is specified and paid for, to awarding contracts to friends instead of the most qualified. Road operations tend to be taken for granted by regular citizens, so it is possible to get away with such shenanigans.

With PPPs in roads there are two keys to counter temptations toward slacking or outright corruption. First is a culture of honesty and toughness within a governmental contracting authority. This requires the governmental authority to initially hire an executive into the road authority who is above reproach to set a standard, not only for the present, but for the

worthwhile to go to the government authority and push for an abrogation of the old contract to re-bid. A PPP contract should have provisions whereby the government authority is free to re-bid at any point in the duration of the contract when enough third-parties come forward with cost-saving proposals while still repaying the original party for the cost of its original investment.

### *Water and Sewer*

Water and sewer services would seem to lend themselves to provision through PPPs. Both involve an initial investment in a pipeline network with access available to make new connections. Water service involves treating water to make sure it does not carry pathogens in addition to securing reliable water supplies. Water must also be delivered at an adequate pressure. Sanitary sewer involves treatment of an entirely different type and can result in a solid product that has value for improving soil fertility.

While it is unusual to see common sanitary sewers run by private companies, it is quite common in rural areas to see

While it is unusual to see common sanitary sewers run by private companies, it is quite common in rural areas to see quasi-private water supply companies in the form of utility districts providing water.

future.<sup>37</sup> Second, transparency is key. Regular, open reporting, in writing and posted on the internet, with information on key expenditures and performance measures is vital. For one thing, this encourages potential alternative private providers of road services to monitor the situation and bring issues to the attention of authorities in order to encourage them to make a change where contractual arrangements allow them to do so.

Transparency is also key to mitigating the tendency toward monopoly pricing where roads are tolled. PPP contracts generally contain price-restraining provisions, but to the greatest extent possible, a private party to a PPP should be free to price in order to cover marginal costs and adjust to congestion conditions. Governmental authorities are generally not going to have the best information about actual costs. However, with full transparency, potential competitors who would like to undercut the PPP contract holder can have the fullest possible information to determine if this is possible and whether it is

quasi-private water supply companies in the form of utility districts providing water.<sup>38</sup> Water flow to a residence or business is easily measured and transparently charged. Smart metering technology using cell communications technology makes it possible to ping meters to get readings without having to employ personnel simply to read meters.<sup>39</sup> Sewer volume from a given location is impossible to measure since it is not purely a liquid and biomass tends to choke any automatic measuring device. Common practice has been to charge patrons of centralized sanitary sewer on a proxy basis based on water usage.

Sanitary sewer does not have to be centralized. Or, depending on a community, it can be centralized in certain districts and distributed in others, especially in residential areas that are not highly dense. Older septic systems require enough space to allow effluent, piped underground, to soak into the ground with adequate rain drainage to prevent flooding of the septic field. New aeration systems produce an end-product of



## An Aside on Eminent Domain in the Prosperity District Context

Because ribbons of property must be assembled for road, water, sewer, and possibly other infrastructure, careful planning is necessary in order to avoid constant corrections, additions, and expansions that potentially interfere with private property. However, the Prosperity District concept is substantially about avoiding central planning, relying on private interactions instead of government in order to determine the best and most efficient deployment of resources. The concept is relatively simple and easy to envision where goods and services are relatively flexible in how they are produced, easily divisible in nature, and quickly consumed. However, infrastructure is relatively permanent, lumpy, and once in place, relatively inflexible. This has not changed even with thousands of years of innovation in materials, methods, and other technology.

Despite the relative inflexibility of infrastructure, there is a great deal of flexibility in how a given parcel (or parcels) of land can be used. Once a piece of land is used to site a car dealership, there is no guarantee that it will stay a car dealership. A large office building can, in the future, be laid low into a parking lot or a production facility. Therefore, to some extent, there is a need for some flexibility in infrastructure in order to accommodate unforeseen, changing needs over time.

Eminent domain, while disallowed by a Prosperity District's authority, is not completely eliminated as a tool within a Prosperity District for tasks related to infrastructure to be accomplished. The

Prosperity District concept includes a provision for governmental units contiguous to a District to exercise eminent domain for transportation and power transmission purposes. Provisions to protect private property from arbitrary takings are included. This considerably reduces any possible perceived need for a Prosperity District's governing authority to have the ability to exercise eminent domain. Still, there are imaginable circumstances where, depending on how and for what overall purposes a Prosperity District is constituted, a District could conceivably be limited in its growth potential without the power of eminent domain. This is likely to be rare, however.

Changes in technology, changes in preferred, legitimate private uses of property, unforeseen circumstances that require unforeseen infrastructure expansions in unexpected directions, are all issues that, at some point, see an almost inevitable conflict between an individual's property interests versus the infrastructure needs of the community as a whole. However, allowing the exercise of eminent domain is somewhat anathema to the prosperity district concept, and the concept is, after all, a laboratory for innovation to get around the perceived need for its use.

One reason for disallowing the use of eminent domain in a prosperity district is that there is no doubt that eminent domain is regularly abused by government today. Its limits at the federal level are only subject to a few words in the U.S. Constitution requiring an undefined level of just compensation.<sup>41</sup> States have raised their hurdles

non-potable clear water effluent that does not smell and that is sprayed onto a lawn, requiring very little room for disposal. Thus, a Prosperity District could minimize the need for centralized sanitary sewer facilities by allowing for modern aeration septic systems and requiring residents to keep them in good repair.

In a Prosperity District, where property owners are intended to have as many degrees of freedom as possible, and where zoning and the creation of distinct residential and commercial

areas is not imposed, it is debatable whether allowing aeration systems yields the greatest long-term flexibility. Nevertheless, developers should have the ability to exploit whatever type of sanitary sewer system they deem cost-effective and competitive, especially as long as this does not increase the expense or spoil the economies of scale of any traditional municipal system existing in parallel, which will be necessary if any part of a Prosperity District is developed as a high density urban environment.

to eminent domain since the Kelo decision,<sup>42</sup> but their hurdles are not nearly as high as what Richard Epstein, has proposed where he would require property owners to be compensated for such intangibles as a sense of community and loss of close access to friends.<sup>43</sup> This, in fact, is what the elimination of eminent domain within a Prosperity District effectively implements. Without eminent domain, the only way to accomplish public infrastructure investments that conflict with private property is through peer pressure from the community as a whole and buy-in to the community by individual property owners. This in itself is a strong incentive for sound, consensual governance.

Of course, with a little creative thinking, the lack of eminent domain power at the district level would likely prove to be an illusory problem. Because a Prosperity District is initially formed with 100% consent of all affected surface landowners (along with 100% of qualified resident electors), the founders of a district could easily anticipate the need for infrastructure flexibility by including a contractual “buy-out” clause as an affirmative covenant that would run with the land. The terms of the covenant could give the managing board of the district an option to purchase land in the district for infrastructure uses; thereby enabling it to mimic the power of eminent domain through a voluntary contract. Market forces incentivizing the landowners to preserve the value of their property for future users would likely make the terms of any such buy-out clause far more reasonable than the typical procedural protections afforded targets of eminent domain.

Another possible solution to the eminent domain problem is proposed by economist Mark Lutter in his dissertation. He proposes the establishment of “Proprietary Cities” wherein all land and infrastructure would be owned by a single entity. Residents would not own the land. The owner would have an incentive to maximize the value of the land by making such a city desirable to live in, providing infrastructure and other public services so that residents could be safe and carry on peaceful enterprise.<sup>44</sup> This could be a solution to the problem of eminent domain for Prosperity Districts, but it also appears to fly in the face of the Prosperity District’s concept of private property, which is a Lockean concept of freedom that is associated with individual property ownership. However, Lutter would allow the individual ownership of structures. He seems to envision a system not dissimilar to that envisioned by Henry George.<sup>45</sup>

Ultimately, it is difficult to believe that a lone holdout problem will arise in the case of a Prosperity District for the simple reason that it is voluntary in a way that general government elsewhere is not. This could change over time if a community develops and individuals are born into the Prosperity District contractual situation and inherit land. However, as long as there are mechanisms by which people voluntarily, knowingly sign up to the Prosperity District concept, they are unlikely to hold hostage the community and put it at risk for lack of truly necessary infrastructure.

In principle, water and sewer provided through a PPP will have all the positive incentives that PPPs in roads produce.<sup>40</sup> One or more private companies could be engaged to construct the initial infrastructure with the right to administer the system and collect the revenues, as with roads. It could be left to private contractors to determine the size of the initial core system and whether to expand it over time, based on perceived need in cooperation with a Prosperity District’s initial organizers. Thus, there are incentives to build durably, if the

contract is of sufficient duration. There is also an incentive to locate network extensions where they are truly needed and to anticipate such need on a rational basis since costs will be borne by the provider. Incentives to price close to marginal cost in at least a semi-competitive fashion can be built into the contract with both adequate and vigorous oversight as well as a credible threat to abrogate and renegotiate the contract when other potential vendors present viable options.

As with PPPs for roads, risk is transferred significantly



from taxpayers to vendors. Accordingly, decision making moves away from pure politics as motivation and toward pure economics, which is preferable in a world of opportunity costs. Private vendors will have an incentive to use the latest cost-effective innovations in materials, methods, and technologies in order to keep costs low and service quality high at the same time. Innovative pricing will be encouraged as well. Already, water authorities regularly price water higher during droughts. Given Arizona's unique position vis-à-vis water supply, drought pricing is not as likely or necessary, but a Prosperity District with a privately-managed water supply could become a model for the rest of arid, western states.

A potential advantage with privatized road, water and sewer systems under a PPP is that there will be less likelihood of streets being permanently damaged by water and sewer servicing and repair. This is because a private road authority will have an incentive to demand full compensation for digging up parts of roads under which water and sewer lines pass, as well as to compensate for the time the road is out of service. This will give water and sewer providers an incentive to be timely with repairs and expansions that interfere with others' private property rights. This is in marked contrast to common practice when government controls these systems, taking their time, always with excuses, in making and keeping infrastructure serviceable. It is also not uncommon for a newly paved road to be dug up to service water and sewer lines simply because road and water authorities within government do not communicate. There will be a pecuniary incentive for firms managing these systems to communicate.

On this last point, it might be wise for the authorities in charge in a Prosperity District to at least consider issuing a single PPP contract that integrates road, water, and sewer infrastructure under the control of a single vendor. There is, after all, a reason that water, sanitary and rain sewers, as well as conduits for phone, electricity, and fiber optics, are often located within road rights of way and under road surfaces. It reduces the need to impose on private property rights with easements and reduces the likelihood that private property will have to be affected when repairs and new construction take place. This can actually reduce delays in dealing with property owners who understandably do not want to lose investments of their own.

A PPP fully integrating some of the most important infrastructure government traditionally provides would eliminate communication problems as described above. It would encourage durability even more so than independent PPPs

for each infrastructure element. It would also encourage the broadest possible innovation. It also makes sense to fully integrate these various infrastructure elements because they are all projects traditionally carried out by civil engineers. As with road PPPs, a PPP in other forms of infrastructure creates clearer lines of responsibility and accountability, but with a fully integrated PPP, this could be even truer. Some might object that these different types of infrastructure are already fully integrated under the traditional, centralized, governmental model. However, as noted earlier, it is all too obvious that the various hands of government rarely speak to each other. This is simply because, other than citizen complaints, they have little incentive to do so, and there is no pecuniary incentive to do so.

As with roads, there is a risk that government contract administrators will be out of their league in negotiating PPPs for water and sewer infrastructure and ongoing provision. Third party expertise is likely to be a must in negotiations. Governing authorities should allow their imaginations to run wild and welcome imaginative proposals on the part of private entities submitting proposals. But, hard-nosed realism and practicality must prevail once negotiations begin. Here too, the community must commit to the concept of PPPs without partisan differences on ideology cycling a hot and cold relationship with vendors and the concept of PPPs.

### *Electricity Transmission and Generation*

Electricity and the infrastructure associated with it have long been provided privately. Thomas Edison's first-of-its-kind electrical grid was entirely owned by private investors.<sup>46</sup> Many utility companies, their generation facilities, and their transmission systems, are privately owned. These exist in parallel and are somewhat integrated with municipally-owned systems and non-profit, quasi-governmental cooperatives that have historically served rural areas. In the United States, the many disparate electrical generation systems are integrated into two interstate grids, the western and eastern grids. Then there is one single-state grid in Texas.<sup>47</sup>

Electricity regulation is complex. While generation is not characterized by a great deal of economies of scale, transmission obviously is. Unquestionably, it is cheaper to provide a region with one set of wires than it is to provide it with two or more sets of wires. Consequently, municipalities and states have historically awarded exclusive territorial franchises to electricity companies to generate and transmit electricity to individual structures. Due to their granted monopoly sta-



tus, electricity delivery companies are regulated as utilities, with governmental authorities charged to make sure quality of service, universal service, and something reasonably close to marginal pricing are maintained. Private water companies have seen similar regulation, as do roads under PPP agreements. State governmental authorities do the lion's share of regulating, although municipalities often play at least some role, especially in determining transmission line location. The federal government also gets in on the act since the western and eastern grids involve interstate commerce and it is important from a national perspective to maintain grid stability.

Over the last twenty years, there has been some move to recognize that since economies of scale are in transmission and not generation, it would seem that generation should be organized more competitively. Texas has probably moved farther in this direction than any other state, although Pennsylvania has made significant moves in this direction and California has made some attempt as well. In territories served by private companies, Texas has maintained the privately-owned and monopoly transmission grid as a regulated utility. At the same time, it has legally separated and delineated the retail electricity and wholesale electricity markets. Individual electricity consumers may choose among a number of retail electricity providers who, themselves, may purchase electricity from a number of wholesalers who actually generate electricity. Each retailer, and in turn, each wholesaler, is obligated to make sure they supply the grid with enough electricity to cover the consumption of their consumers.<sup>48</sup>

In Texas, the entire competitive system is integrated through a quasi-governmental authority called ERCOT which operates to some degree as regulator, but mostly as a centralized market system that measures electrical outputs and demand and makes sure the system is balanced. It is through ERCOT that suppliers' generation obligations are measured and where it is made sure that they pay up at predetermined rates when they fail to contribute the amount of generation they are obligated to provide. Large, usually long-existing generation companies are charged with making up the difference when other generators fall short since, in order to be reliable, the grid's voltage must be maintained at a constant level.<sup>49</sup>

A Prosperity District will likely have to tap into one of the nation's western grid in order to provide for its residents' power needs. Thus, it is not practical to think that the highest ideals of independence with respect to electricity will be achievable for some time when a Prosperity District is first organized. Perhaps from the beginning a Prosperity District can

**Fire and emergency services are relatively easy to imagine being privately provided. In fact, fire service PPPs, of a sort, have existed in the past, through subscription.**

obtain state and local permission to allow residents who can to live independently of the electric grid with distributed electric generation systems, wherein individuals or small groups provide for their own electrical needs, usually using renewable energy sources. However, it is likely that unless independence is alone the overriding consideration, most will opt to be part of the grid for its reliability and relatively low cost. The Prosperity District could conceivably insist that generation be provided on a competitive basis, but it could be a challenge to insure reliable power inexpensively given the relatively small initial scale involved with a newly developed area.

Realistically, a Prosperity District might be able to enjoy the benefits of a PPP with respect to the transmission system while initially connecting to an established utility for generation. A long-term agreement for the supply of electric generation service could include a provision that once the Prosperity District has enough customers, an ERCOT-like entity will be organized and competitive electric generation will commence.

As already alluded to, the real PPP opportunity for electricity supply in a Prosperity District is in the transmission infrastructure. Assuming transmission and generation can be separated in the first place, which is likely to be difficult in many states, there is no reason transmission cannot be administered as a PPP with consumers paying for the grid from which they draw electricity at least partly on the basis of the amount of electricity consumed through it, but independently of generation. Once again, the incentives inherent in road and water/sewer infrastructure PPPs exist with respect to electricity infrastructure.

Another advantage of a start-from-scratch development, likely with a Prosperity District, is that a decision can be made relatively easily and at relatively low cost whether to run electricity transmission lines above or below ground. Above ground, hung on poles, electric lines present safety hazards and are vulnerable to damage from storms and wayward ve-



hicles as well as interference with trees. Nevertheless, running transmission lines above ground is generally inexpensive relative to trenching and burying lines. Above-ground affords greater flexibility for expansion both in terms of the logistics involved as well as the costs. On the other hand, to some extent, electricity transmission infrastructure can be integrated or at least piggy-back on road and water/sewer provision. Electrical, and for that matter, fiber optics and other wires, can easily be snaked inside PVC pipe conduit under the ground. Such wiring, as technology and/or need develops and dictates, can be replaced easily when it runs through pipes instead of being buried directly into the earth.

Authorities considering issuing a PPP call for proposals from a Prosperity District should consider including a set of conduits in a possibly integrated PPP for road, water and sewer infrastructure. Regardless, careful consideration should be given to anticipating the possibility of placing much of the community's electricity transmission infrastructure underground.

Administration of an electrical transmission infrastruc-

ture being privately provided. In fact, fire service PPPs, of a sort, have existed in the past, through subscription. There are several problems with subscription services, however. Subscription services only respond and help with the emergencies of subscribers. This can potentially lead to ambulance/EMT services ignoring the plight of a non-subscriber who is having a catastrophic health event or who has been in an auto accident. Or, emergency services might aid a subscriber but charge an exorbitant amount of the service. In the case of fire service responses, subscription fire departments have actually stood by while a non-subscriber's house burned to the ground while wetting down subscribers' houses in order to prevent the spread of the conflagration. Publicity surrounding such circumstances inevitably leads to outrage and these arrangements rarely last as a result.<sup>50</sup>

Under the traditional model of providing for emergency and fire services, especially in urban areas, crews consisting of government-employed specialists take part in days-long shifts, maintaining equipment to a high shine and doing some training, ready on a moment's notice to respond to emergen-

In a PPP for fire and emergency services that does not rely on subscriptions, careful thought must be given to how the contractor will be compensated.

ture PPP contract will potentially suffer many of the same pitfalls of administration of other infrastructure PPPs. One advantage of the usual regulated utility system for electrical services is that the electric provider has an incentive to at least somewhat efficiently provide for infrastructure, making sure that wires, for example, are adequately durable given the probability of their being destroyed by storms or other catastrophic events. A regulated transmission-only utility has an incentive to cut corners in order to reduce costs. There will therefore be a need to carefully monitor and administer the PPP contract. One ace up the sleeve of a Prosperity District's contracting authority will be that the infrastructure provider only gets paid over time subject to adequate performance. In this case, performance should include the durability of transmission cables, transformers, and substations.

### *Fire and Emergency Services*

Fire and emergency services are relatively easy to imagine

cies. Historically, there has been a tendency for personnel to unionize, with plenty of idle time on the clock to discuss grievances and ideas for gaining better compensation. Although there is no denying that most emergency personnel are dedicated and genuinely desire to contribute to their community, many minor emergencies see over-responses with large fire trucks and multiples of personnel over and above what is truly needed responding to the event.

A private company contracted to provide emergency services and free to organize so as to be as efficient and effective as possible is likely to organize things quite differently. Stations, trucks, and other investments are likely to be more carefully matched to the emergencies that are regularly seen and expected within a community. Imaginative work arrangements using part-time personnel and even volunteers are more likely as well, assuming that the contractor is not constrained by a union contract. Trucks might not be quite as shiny, but their maintenance is more likely to be carried out



when it is truly needed.

In a PPP for fire and emergency services that does not rely on subscriptions, careful thought must be given to how the contractor will be compensated. The PPP's contracting authority will likely learn from proposals submitted by private companies, but contract administration will have to be expertly carried out. The tendency will be for contract administrators to form close relationships with the contractor and fail to hold the contractor fully responsible. Performance measures, regularly audited by outside third parties, will have to be carefully thought out. These should include measures for proper maintenance of fixed assets like fire stations as well as proper maintenance of vehicles so that they are in proper running order. And of course, response times as well as effectiveness in carrying out services will have to be evaluated on an ongoing basis.<sup>51</sup>

A fire and emergency services PPP contractor will have to be paid on the basis of necessary scale given the size of the community, with periodic adjustments as growth occurs. Revenues for the contractor should not be fee based because such fees would be accrued only when bad things happen and nobody should be incentivized to make bad things happen. In order to incentivize high performance levels, a system of bonuses should be devised based on superior accomplishment of performance measures. At the same time, financial sanctions can be applied when readiness audits are found wanting and performance does not measure up. Clearly, in order to make sure emergency services perform well to minimize costs to life, limb, and property of emergencies in the community, it will be critical to measure and monitor readiness on a regular basis. Hopefully, this will be the main means of measurement since ideally, performance in actual emergencies would be rare due to few emergencies.

Ambulance and EMT services would be contracted, measured, and managed similarly to fire services and possibly integrated into a single PPP contract with the provider of fire services. Private ambulance service already occurs in Arizona, but it is not managed in a PPP arrangement and suffers somewhat from rent-seeking. Nevertheless, there are lessons to be learned from the Arizona experience.<sup>52</sup>

### *Refuse Collection*

Little will be said here about refuse collection because it is already so widely privatized and there is so much experience with it. In fact, there is little if anything a Prosperity District actually has to do other than to require residents to have their

refuse collected. This will ensure demand and private companies will rise to the occasion. Issues do arise with completely open competition in refuse collection, however. Complaints about excessive truck traffic and trash containers always out on curbs, although in front of different houses from day to day, have occurred. Although the Prosperity District concept does not allow for monopolies to be established through exclusive franchising, the District could regulate scheduling for trash pickups.

### *Education*

Finally, primary and secondary education services might, depending on how negotiations go with the state and whether such authority is granted, be provided under the authority of the Prosperity District. More than likely, though, public education will be organized in the territory of the District according to school district boundaries and administered independently of the District.

If the Prosperity District is granted the authority to separately constitute its own school district, the district will have the right to separately collect its own property taxes with additional revenue from the state and possibly even the federal government. The best use of these funds is to encourage a private education system with parents choosing schools for their children. The most efficient funding method to accomplish this with the most superior incentive structure is Educational Savings Accounts whereby parents control a yearly grant made to each child to be spent on a variety of possible educational services. Although limited in availability, these are already law in Arizona, where they are called Empowerment Scholarship Accounts. Economy on the part of parents is encouraged by allowing any savings accumulated over years to be used toward a child's post-secondary education in college or trade school. Methods are currently being devised in Arizona and Nevada, among others to monitor expenditures authorized by parents to make sure they are properly educationally related.<sup>53</sup>

The literature on privatized education, charter schools, vouchers, and Education Savings Accounts is extensive and readily available. Therefore, no more will be mentioned of it here. Besides, it will be a difficult concession to gain from the state to move to a completely independent education system within a Prosperity District.

### **What about Law Enforcement?**

Law enforcement services are usually the most difficult for



people imagine being privately provided although the first modern police force in Great Britain was not established until 1829 in London.<sup>54</sup> Elected constables and sheriffs, as well as privately hired security were the precursors to today's police forces. These offices speak to the fact that police are expected to be close to, indeed part of, the community, so it is understandable that a remote corporation that might not even be part of a community would seem the worst sort of entity to be entrusted with the community's safety and security. Police, of all community services, should be locally managed and controlled, for the good of the community, to protect it from abuse by those who are supposed to be protecting the population from illegal activities. What's more, each community has its own expectations and standards of conduct. Surely, only local management and control of police can insure that law enforcement is fully integrated into the community.

These concerns seem overwrought given recent history and concerns over everything from asset forfeiture to the militarization of police services.<sup>55</sup> Police personnel, unless a community is relatively remote, do not necessarily hail from the community they are specifically hired to police, either. It is not at all uncommon for police chiefs to move from city to city, even across state lines, much like city managers and school superintendents do.

A private firm engaged to administer law enforcement in a community under a properly constructed PPP contract will have an incentive to minimize costs. But, if police output is properly measured, that same company can be incentivized to perform well for the community. It's not as if such a company is going to hire foreign mercenaries to police a community. Instead, in order to be effective, such a company will hire local personnel who live in the community, if for no other reason than to ensure a stable workforce that is familiar with the community and its culture. The real issues lie in administration of a law enforcement PPP contract, appropriate performance measures, and proper third party audit work that does not unnecessarily add to costs.

A distinct likely advantage to hiring a private company to police the Prosperity District under a PPP contract is that the private company's chief personnel are especially likely to have wide experience, perhaps in a variety of environments. The principals of such a company are likely to have had military experience, policing populations in other parts of the world, as well as experience policing large cities. The combined experience of principals willing to take on a contract to police a community is likely to be quite extensive.

**Increasingly, effectiveness measures for police officers have been devised and used in cities. Response times can be measured, monitored, and audited. Crime rates can be measured and checked through surveys.**

Again, looking at recent history, it is obvious that government run and administered police forces suffer from empire-building and costly preparation for highly unlikely scenarios. The likelihood of public unrest in Chicago is quite different from that of Dallas or of Phoenix. Yet, we see urban police forces across the nation preparing as if they all face equivalent threats and threat levels. A privately managed police force, however, will be much more cost-conscious. For example, armored vehicles available as surplus from the U.S. Army are unlikely to be accepted as needed hardware merely due to the local police chief's desire to keep up with police chiefs from across the nation whose force have armored vehicles. Such vehicles are costly to maintain while serving little to no purpose, not to mention the cost of training personnel in their proper use and operation.

Just how to compensate a private company to administer police under a PPP is an important question. Police personnel will be employees of the company and deputized under the authority of the Prosperity District as negotiated with the state and adjoining local governments. Police uniforms will not indicate that the police are privately employed. Once they are trained and deputized, this will not matter. Compensation to the private contractor should not be predicated on the number of personnel. The number of officers necessary to get the job done as well as equipment needs should be under the discretion of the contractor so that costs are minimized both to the contractor and the community.

Increasingly, effectiveness measures for police officers have been devised and used in cities. Response times can be measured, monitored, and audited. Crime rates can be measured and checked through surveys.<sup>56</sup> As a starting point, a PPP for police services will initially pay a contractor sums approximately equal to the budgets of similarly-situated cities and communities around the nation. Provision should be made in

the contract that assessments will be made periodically and the overall fee adjusted in accordance with legitimate manpower and equipment needs. A system of financial awards and penalties must be devised to create proper incentives for the PPP contractor to properly train and equip personnel to do their jobs in an excellent and professional manner. This will not be easy. There will be a learning curve on the part of both vendor and government administration.

Another aspect of policing in a Prosperity District will be the freedom of resident citizens and businesses to hire their own security personnel, either individually or in a collectively with others for a neighborhood. With freedom to be maximized under a Prosperity District arrangement, there should be an expectation that residents should be free to hire their own security personnel. It might be necessary for the Prosperity District to require liaison meetings and common communications between the District police and other security personnel with the ability to disqualify a separately hired security personnel who do not cooperate. However, keeping in mind that the District force will have an incentive to disqualify alternative security personnel in order to minimize the possibility of future competition for the larger contract, the district force should not be the final authority on whether alternative personnel can continue to operate.

Nevertheless, due to the novelty and potential controversy of furnishing law enforcement services privately, it is recommended that all but the most sophisticated Prosperity Districts instead consider managed competition whereby law

enforcement services are procured by competitive outsourcing to existing public policing agencies, such as the County Sheriff, State Police, or nearby municipalities.

## Conclusion

While some will object to the notion of privatizing traditionally government-provided services in a Prosperity District through PPPs, this paper shows that there is no practical reason not to do so. There is a great deal of evidence that PPPs in providing a variety of public services can succeed. If there is a reason to object to the Prosperity District concept, it is not because of privatization. The demonstrated practicality of privatization and PPPs, does not mean, however, that PPP privatization is a simple matter. Dedicated hard work will have to go into fully conceptualizing and fleshing out PPP proposals and contracts. Hard-nosed negotiations will have to take place, and once the contracts are executed and in place, the hard work has not ended. Dedicated, ethical contract managers will have to be employed to monitor contractors and administer the contracts fairly and ethically. Third party auditors will have to be vetted and selected. Real and relevant information will have to be forthcoming, and sound judgment will have to be exercised.

The rewards of all the hard work are likely to include improvements in quality of service over the traditional model of provision, as well as cost savings,<sup>57</sup> and ultimately a prosperous, harmonious, and growing community.



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Made possible by a generous grant from:

