

Other outsourcing experience



Massachusetts

In 1994 Legislative audit finds political nature of the contracts led to lax state oversight, poor performance, and 35% of contracted work completed by state forces. The State auditor finds meaningful cost comparisons cannot be made. The pilot program is canceled and original plans to expand the program are abandoned.

Florida

A 2003 legislative audit indicated that Florida DOT could not prove overall agency savings

Virginia

Cost analysis and savings questioned in 2001 legislative audit.

Oklahoma

After asset management contract collapsed over service issues, in May 2002, the Oklahoman Senate voted that it was opposed to contracting out highway maintenance.

Texas

Results through 2002 for two pilot outsourcing contracts showed significant drops in performance quality compared to prior state exercise of maintenance responsibilities.

For more information:

www.wsdot.wa.gov/publications/folio

www.wsdot.wa.gov/maintenance/outsourcing.htm

www.wsdot.wa.gov/maintenance/default.htm



With permission: George Price, Published in The New Yorker June 3, 1939

What needs to be considered long before any outsourcing program is undertaken?

- Scoping and planning.
- Asset management complexities of highway maintenance service delivery (including the dynamic of least life cycle costs).
- Economic analyses.
- Asset inventories and level of service trends.
- Service delivery and activity or unit costs.
- Contract administration responsibilities and costs (including liability and insurance analysis);
- Cost savings based on actual cost comparisons.
- Contracts specifications.
- Performance measures and evaluations with financial incentives/disincentives based on service thresholds.
- Competitive market analyses.
- Political direction.
- Public expectations.
- Exit strategies and contingencies.
- An experienced management team to administer, manage and evaluate contracts.
- Lessons learned can be used to inform future public policy and improve the delivery of highway maintenance.

WSDOT Secretary MacDonald continues the lonely fight to disentangle myths and misstatements on the cost benefits of "outsourcing."

January 2005



**Washington State
Department of Transportation**

Douglas B. MacDonald
macdond@wsdot.wa.gov

Secretary of Transportation
Washington State Department of Transportation
www.wsdot.wa.gov

The evidence continues to be developed on whether outsourcing of highway maintenance is a strategy that really saves money.

"We found that while the Ministry's systems and procedures ensured that contractors bidding on routine maintenance and minor capital projects were qualified and that the services were acquired competitively, they were not sufficient to ensure that the province's highway assets were being maintained cost effectively. In particular, we noted that the Ministry's systems and procedures: did not ensure effective oversight and evaluation of the performance of contractors engaged to maintain provincial highways and that appropriate corrective action was taken when required..."

Office of the Provincial Auditor of Ontario, 2004 Annual Report, 19, 334-5.

Ontario: Highway Maintenance Outsourcing

"As has been done in several other jurisdictions, the Ministry outsourced almost all maintenance work on provincial highways and bridges to the private sector between 1996 and 2000."

A table of total highway maintenance expenditures shows:

Pre-outsourcing:

	Total maintenance costs	Lane kilometers maintenance (thousands)	Maintenance costs (\$) per lane kilometer
1996-97	\$216 million	56	\$3.9
1997-98	203 million	53	3.9
1998-99	211 million	46	4.6

Post-outsourcing:

2000-01	\$222 million	45	\$4.9
2001-02	236 million	45	5.2
2002-03	252 million	46	5.5
2003-04	241 million	46	5.3

"We found that the Ministry had appropriate controls over the contracting and payments processes. Specifically, the Ministry ensured that contractors bidding on Ministry work were financially sound, a competitive number of bids were received for each contract, and the best bids were accepted. Despite the competitive acquisition of services, costs have continued to rise, as the table above shows. The Ministry informed us that higher costs are due to a number of factors, such as above-inflation increases in salt prices, a requirement that contractors make use of advances in winter maintenance equipment, new safety regulations governing road maintenance, and increased traffic."

Georgia

Georgia DOT, with the assistance of Georgia Tech, is undertaking a detailed assessment of the feasibility of maintenance outsourcing. This timely and important study includes:

- Cost effectiveness and quality analysis of current GDOT maintenance activities to establish a base line for cost comparisons.
- Analysis of vendor activities in other states and a compilation of maintenance services and performance standards and warranties offered to determine the level of and benefits from existing market competition.
- "True costing" of contracting out including the cost of contract negotiation, oversight, lost department capability, and contract failure.

Stephen Henry, "Georgia Maintenance / Public-Private", personal communication, January 5, 2005.

There is no credible demonstration from case studies that "public-private partnerships" show a 6 to 40% reduction in highway construction costs.

Snapshots of Innovative Contracting

"In February 2003, Battelle, on behalf of Koch Industries, compared the use of traditional methods of constructing to the use of innovative construction methods. Although data comparing the use of innovative contracting is rare, the case studies reviewed by Battelle found that the use of performance based contracting, a form of public-private partnership, can result in cost savings ranging from 6 to 40 percent..."

U.S. DOT, Report to Congress on Private Public Private Partnerships December 2004, 42

The Battelle report lists sixteen examples of highway construction projects with innovative contracting approaches. *U.S. DOT, Report to Congress on Public Private Partnerships*, Appendix A. All but four projects show no cost information at all or report that the project is "on budget." The four projects that show "savings" are the four Koch "warranty" projects: New Mexico 44 (see details at rights); another warranty project completed for the Commonwealth of Virginia (Virginia 299) and for two small street rehabilitation and construction projects completed by Koch in Aspen, Colorado and O'Fallon, Missouri.

State DOT Experience With Design-Build Contracting:

"State DOT experience with design-build contracts under SER-14 varies widely. Some projects noted significant cost savings while others experienced increased costs." (A forthcoming FHWA report was said to promise additional information).

U.S. DOT, Report to Congress on Private Public Private Partnerships December 2004, 45

New Mexico SR 44

- Original state highway department estimate and budget for four-laning NM 44 was \$180 million.
- After Koch Industries proposal was accepted, a gold-plated outsourced design was prepared. A very high bid on first of four contracts suggested four contract total would be \$50 million or more over estimate and budget.
- State highway engineers redesigned the project to bring costs down. Total award cost for four contracts was \$193 million. Overruns on contracts brought final construction cost to \$215 million. Overruns mostly resulted from asphalt price escalations, the risk of which were not shifted to the contractor, but were left with the state. At about \$1.8 million per lane mile, the lane mile cost was approximately twice as high as a conventional four-laning of NM 44 south of the project performed earlier by the state highway department.
- Additional project costs also included \$46 million for design and \$49 million for construction management.
- Public financing with tax-exempt debt through New Mexico Finance Authority insisted on by state legislative leaders achieved interest rate savings of 275 basis points over private financing originally proposed by Koch, sparing New Mexico taxpayers millions of dollars of further cost on the project.
- The \$62 million up front warranty pavement made to Koch shifts no risk to Koch because Koch's liability is limited to the amount of the payment (the "heads I win, tails you lose" bet). An economic analysis commissioned by the state highway department and FHWA by the Volpe Center concluded that savings were in the range \$7 – 27 million. A different report prepared at the request of the New Mexico Legislative Finance Committee concluded there was no way to establish whether the warranty had been cost-effective given the lack for support for the "benchmark" expected state maintenance cost over twenty years used as the basis to calculate "savings."
- Serious pavement heaving problems have occurred on some sections of the corridor. Legal disputes ensued about Koch's obligation to reimburse the state highway department for required repairs. Details on these issues are not readily available.