

**PRIVATIZATION
IN THEORY AND
PRACTICE**

By

Dr Madsen Pirie

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'In every great monarchy of Europe the sale of the crown lands would produce a very large sum of money, which, if applied to the payment of the public debts, would deliver from mortgage a much greater revenue than any which those lands have ever afforded to the crown... When the crown lands had become private property, they would, in the course of a few years, become well-improved and well-cultivated.'

Adam Smith, The Wealth of Nations,
Book V, Chapter II, Part I.

FOREWORD

By Dr Eamonn Butler

This report represents the most comprehensive review so far of the remarkably extensive replacement of state activities by private-sector alternatives that has occurred in recent years. But its main strength is not merely its listing of the countless examples of where private involvement - with its associated benefits of consumer choice and the stimulus of competition - has been introduced into areas once thought to be the sole prerogative of the state. Its principal contribution is to collate that wide experience into a unifying theoretical framework which helps us to identify and to understand the strategy and tactics of privatization.

The author explains that privatization arose not as a conscious strategy but as an approach to practical problems for a government that originally supposed budgetary restraints and the excision of waste to be its main policy tools. Such macropolitical ideas, says Dr Pirie, are doomed to failure: insensitive cuts remove vital services instead of administrative waste, and interest groups from within the bureaucracy, from the beneficiaries of existing programmes, and from the service providers themselves all combine to make the political obstacles overpowering. The privatization strategy, on the other hand, is a micropolitical approach which applies one of a number of techniques to each specific problem, making provision for the concerns of each interest group as it transfers activities from the public to the private sector. It is an approach which produces creative and innovative solutions to each problem, not a single solution that is imposed on each case.

From the wide range of innovative solutions that have been tested, Dr Pirie makes an impressive identification of twenty-two different techniques of privatization, and shows in the form of practical examples the numerous variations that have occurred upon each theme. The result is to clarify our thinking on what the strategy of privatization involves, the purposes and range of benefits it is expected to achieve, and how future problems might be tackled by its use.

1. INTRODUCTION

Although the term 'free enterprise' is conventionally used to describe the economic systems of the United Kingdom and other Western countries, the salient characteristic of all such economies is the size of the public sector. In the United Kingdom, as elsewhere, the government is the largest single element in the system. It is the biggest consumer, the biggest employer, and far and away the biggest spender. Besides being the largest element in the economy, government also exerts a distorting effect on such freedom of action as survives in the private sector.

In the free enterprise portion of the economy, people express themselves through personal decisions. They reveal their priorities with spending decisions. They seize entrepreneurial opportunities. They take chances, and they run the risk of winning or losing. The public sector prevents these activities. Instead, it responds to political (rather than economic) pressures. It pre-emptes the funds which citizens would have used to make their own choices. It spends, for the benefit of special interest groups, those funds which could have sustained entrepreneurial activity.

Although people talk of the public sector as though it expresses choices made by the public, it in fact expresses the priorities of legislators and bureaucrats. The property and capital which are called 'public' are administered by these individuals as if it were their own. Ultimately, this means that the public sector takes resources out of the area in which the beneficial disciplines of the market operate. It takes them away from the trial and error activities, and from the choices by which people introduce their preferences into the system. It removes resources from the progressive and growth-generating sector, and locks them into programmes which satisfy political constituencies.

If a dispassionate observer looked at the history of the United Kingdom, he or she might conclude that the gradual growth of the public sector was part of the life cycle of a free enterprise economy. Looking at the steady and remorseless increase in the proportion of the economy falling under the government's grip, the observer might well suppose this trend to be inevitable, and one which would culminate in the extinction of the remaining free enterprise activities.

Commentators have already noted a 'ratchet effect' which sustains the public sector. Like an industrial cog-wheel which can turn in one direction only, the size of government increases but never diminishes. Free-spending administrations can always increase the scope and extent of their activities, but more cautious legislators are unable to decrease them in times of stringency. The political system makes it very easy for elected representatives to vote for increased spending, or to legislate

automatic increases in spending. That same system makes it almost impossible to cut spending. New projects can be taken on without difficulty, but older ones cannot be jettisoned.

The cumulative effect over the decades has been to increase the size of the public sector year by year until it now limits the spontaneous society - the realm of private decision-making - to a small part of the whole. A regimented and regulated society now forms the dominant element and people in many countries speculate on how long the growth of the public sector can continue before it so restricts the market sector that it completely absorbs it.

From time to time administrations have been elected amid much rhetoric about cutting public spending. None of them has succeeded in doing so. At best there has been no more than a temporary holding action, perhaps only a slowing down of the rate of increase. Although political mythology has it that these politicians were not tough enough, the evidence suggests they were simply unable to fulfill their brave words. Intentions alone are insufficient to curtail public spending.

Given the history of these attempts, the prognosis for free societies cannot be described as optimistic. These societies seem to face the prospect of ever-greater burdens on the productive sector to support an ever-increasing number of beneficiaries of state largesse. Industry, saddled with the additional costs of government, seems destined to produce goods and services more and more expensively. The outlook is for a constant and increasing export of jobs to developing countries whose lower costs promise to help them capture the markets of the advanced economies.

This, in turn, raises the spectre of protectionism. A wall around the EEC and other developed countries might allow them to produce and sell expensive goods to their own captive markets by keeping out the competition. Unfortunately, this promises an international grouping of independent fortress economies, all stagnating under high costs. The simultaneous eclipse of economic freedom and economic prosperity is not an attractive combination to look forward to, but to many there seems no other way to relieve the legislature from the mounting pressures to sustain and increase the growth of the public sector.

A new approach

It is onto this landscape that the word 'Privatization' is making its appearance on the political horizon. The idea involves transferring the production of goods and services from the public sector to the private sector. At its lowest common denominator, it means having done privately that which was previously done publicly.

Close to the heart of the case for privatization lies the recognition that private programmes are subject to economic dis-

ciplines, and respond to choices made by the beneficiaries of these programmes. While it might be impossible to control the cost and scope of a public programme, if such a programme can be moved to the private sector it automatically becomes subject to market-based pressures.

In effect, privatization controls the public sector by gradually replacing it. Thus, it offers a 'reverse ratchet', a means of systematically reducing the public, government-directed part of the economy. Once a programme is operating successfully outside of the state sector, subject to consumer inputs and responding accordingly, it can stay there. Each piece of privatization can thus permanently diminish the overall scope of state involvement in the economy.

Privatization is not something peculiar to the British economy. Although the trail was blazed in the United Kingdom, and perhaps was most needed there, its fire is spreading rapidly. West Germany, Belgium, and other European economies are witnessing it. In the Pacific, it is beginning to dominate Japanese thinking. Malaysia, Singapore, and Taiwan already have major privatization projects under way; and even Communist countries such as Vietnam and the People's Republic of China have been affected by its progress.

Part of the universal appeal of privatization lies in the fact that it is not a policy but an *approach*. It is an approach which recognizes that the regulation which the market imposes on economic activity is superior to any regulation which men can devise and operate by law. It is an approach which also recognizes that the market measures, and responds to, the choices and preferences of people more accurately than the political process. A programme performed in the private economy can be done more efficiently, more cheaply, and with greater satisfaction to its beneficiaries than its counterpart can achieve in the public sector.

While privatization is not a policy, it still less is an easy formula. It requires creativity to devise policies appropriate to each public sector problem. Solutions which have been successful in one country often will not succeed in another. Even within a country, policies which successfully deal with one problem cannot necessarily be applied to another.

Experience has shown that not only is each country different, but each problem is different. The process of privatization requires policies to be tailor-made to deal with each particular issue. Each part of the public sector generates different interest groups and different political problems. Each distinct programme requires a distinct approach.

Nonetheless, the British experience shows what can be done. It illustrates the battery of privatization techniques which have been developed and applied already. It serves as an incentive to policy analysts elsewhere in the world to devise creative solu-

tions which are relevant to their own case. If they respond to that challenge, then privatization offers the first real chance to reverse the growth of government and restore to individuals the freedom and the choices which government has usurped.

2. THE PERFORMANCE OF THE PUBLIC SECTOR

Attitudes toward the public sector of the economy often have coloured the way in which its performance has been evaluated. While the private production of goods and services has been assessed in terms of normal commercial criteria (profitability, efficiency, consumer satisfaction, etc.), state activity has been viewed as a public service which is different in kind and which requires a different standard of judgement.

As a result, private undertakings have been judged by comparing their performance with that of their rivals. Public activities, on the other hand, have been judged against what was intended. In socialist economies this reaches its ultimate point when economic performance is assessed in terms of whether the targets of a five year plan have been attained. Even in mixed economies, there has been a strong tendency to judge the success or failure of public undertakings against some concept of what 'ought' to have been achieved.

A central assumption has been that public sector operations cannot be judged by normal economic criteria such as the rate of return on capital. On the contrary, it has been widely supposed that government activities operate in a league whose performance is assessed by non-economic factors. Thus, the quality of service is often gauged against what can 'reasonably be expected' from the labour force, or from the available funding. A parallel but less explicit assumption has been that readiness to serve the public provides motivation in the public sector workforce that is equally as strong as the profit motive in the private economy. This assumption has been particularly prevalent in the areas of public activity which involve regulation and administration, as opposed to the production of goods and services.

The measurement of performance against expectations, and the assumption of a selfless workforce, have provided a formidable combination against objective assessment of the public sector. These assumptions have worked to insulate the public sector from comparisons in cost-effectiveness or quality of service. Had the public economy been treated as simply another way of organizing the production of goods and services, it might have been evaluated dispassionately against its alternatives. Had there been no assumption of selfless public service, ways might have been developed to link the aims of the producers with the satisfaction of public needs.

Recent analysis

Only recently have analysts stood aside from these assumptions and produced studies which evaluate public performance by more conventional and realistic standards. The comparative efficiency of production and delivery of public goods and services has been judged in two ways. First, the use of foreign examples has

enabled assessments to be made even in cases of national monopoly. Although largely invulnerable to any unfavourable contrasts within a country, a national monopoly can be compared with the performance of its private counterparts in other countries. The quantity and quality of service which is achieved for each given input can be measured, as can less obvious criteria including the extent of technological improvements and the variety of services offered to the consumers.

The second type of comparison which has been employed recently is comparison with private sector counterparts within a country. Even in cases of local or national monopoly, there are often comparable private sector activities with which to compare performance. In fields as diverse as transport and housing, education and health, there are private sources of production that enable comparisons of cost and productivity. Even in such areas as transfer payments and regulation, there are equivalents lying outside the public sector which can be used for critical comparison.

Once we overcome the assumptions that the public sector is different in kind, and that it is entitled to a different standard of evaluation, these alternative assessments become admissible. To some extent, it is the visibly poor performance of the public sector which has contributed to the abandonment of those benign but faulty assumptions. It is the result of hard-nosed, more realistic comparisons which have transformed the intellectual perception of the public sector.

In place of the image of a beneficial and helpful arm of society, the public sector is now largely perceived as afflicted by a number of serious economic and institutional problems. A systematic examination of these problems leads to a new picture of the public sector, and a new recognition of its limitations.

TEN PROBLEM AREAS

There are ten basic problem areas which emerge from an examination of the public sector. These problem areas merit close inspection because, when taken together, they cast doubt on the use of public sector organization to produce and deliver goods and services. These problems are not simply adverse tendencies which need to be monitored and corrected. Rather, they are structural weaknesses which undermine the whole basis on which the public sector is established.

1. Production costs

Several major studies have compared the costs of producing the same goods and services in both the private and public sectors, and all have concluded that on average, the public sector costs are much higher. The margin of saving achieved by the private sector varies with the type of good or service being produced.

It also varies from country to country. Despite these variations, comparative studies all point in the same direction, and identify a range of cost savings to be expected where private enterprise is used. On average, private industry in Britain has costs of production that are about thirty-three per cent lower than in the public sector. In the United States, the figure is nearer to forty per cent and in West Germany, private business produces goods and services at fifty per cent of the cost of production by its public counterpart.

It is important to compare like with like. The costs of public sector operations are often very difficult to calculate because of the difficulty in distributing overhead expenses. A valid comparison must count the cost of central administration, of buildings and insurance, of recruitment and training, and of fringe benefits. Even more important, it must count the cost of capital. These calculations, long routine in private business, are by no means the norm in public activity.

The strikingly lower cost of the private alternative emerges in study after study where like-with-like comparisons are drawn. It appears that market-induced pressures to keep costs down and profits up acts as a better discipline on the private sector than does the desire for economy in the public sector. Private businesses seem able to achieve cost-cutting and productivity gains which the public sector cannot match.

2. Efficiency

The comparisons made for similar types of operations all point to greater efficiency as the source of private business's lower costs. The studies indicate that public operations tend to use higher manpower levels for identical operations, and make much less efficient use of their machines.

Typical are the studies on refuse collection. The private operators were found to use fewer employees per vehicle, and to have the vehicles in active use for a greater number of hours per week. Single-man or two-man operations were the norm in the private sector, whereas the public operations frequently featured five-man operations. Turn-around time for vehicle repair was faster for private businesses, and the time spent on the road was greater.

The implication, once again, seems to be that the disciplines of competition and the need to earn a profit keep private businesses leaner and more efficient than their public counterparts. A private firm can go bankrupt if it fails to keep up with the competition; public sector activities rarely face a similar prospect. The different penalties which they face seem to produce a difference in performance.

3. Labour costs

Labour costs are often the key to differences in efficiency between the private and public sectors. Public sector activities appear to be more vulnerable to the pressures which increase labour costs. The key factor here seems to be the ability in the public sector to pass on the results of working agreements directly to the taxpayers who finance the activity. A private business does not have the same freedom, since prices have to be kept competitive. Thus, within the private sector there is a greater propensity to negotiate working agreements with more concern for the effect on costs.

Private businesses are characterized by labour agreements which, for the most part, allow flexible use of labour in terms of skills and time. It is primarily in the public sector that restrictive work practices abound, that agreements specify that only certain classes of employees shall perform certain types of tasks, and that unions are able to limit work at unpopular hours for their members. Although the unions and the administrators are on opposite sides in labour negotiations, in the public sector it is easier for each to meet the other's needs. In the private sector, the consumer is a tacit party to such agreements. If consumers do not accept the higher costs reflected in higher prices, they can take their trade elsewhere. In the public sector, the consumer is normally captive, having no other option to turn to.

The tendency towards uneconomic working practices is a consequence of the monopoly which normally characterizes public operations, and the leverage it gives to unions. There are sectors of the private economy notable for unrealistic and uneconomic labour agreements. But these, too, tend to be in areas where monopoly or other special circumstance gives unions unusual power.

4. Capital costs

The degree of capitalization in the public sector depends on how much government has available to spend for this purpose. This depends, in turn, on the state of the national economy, on the levels of taxation which government thinks will be acceptable, and on other demands on the public purse. Political pressures tend to deny public operations the degree of capitalization which they require.

For example, there is considerable political pressure to squeeze capital spending in order to expand current spending. This is because the political pressures on current spending are huge. The labour force must be assuaged, and there must be few visible cuts in the services provided by public enterprise. Inevitably, the capital side of the ledger suffers. Capital spending is less visible, and has fewer interest groups to defend it. A capital cut only postpones the maintenance or acquisition of buildings and equipment. It is easier for legislators to raid

the capital accounts.

The public sector is thus characterized by a tendency for current spending to rise as a proportion of total spending, and for the share devoted to capital to diminish. This means that the public sector of the economy often makes do with obsolete equipment. It is denied new, labour-saving and cost-cutting technology. The provision of improved and more valuable services are delayed, and the existing capital stock is made to last much longer than its planned life.

Against this standing tendency to skimp on capital spending in the public sector is the practice of capital renewal in the private sector. Unless firms keep up-to-date with developments, a rival may step in with a cheaper operation or a more valuable good or service and capture the market from those who lag behind. Sound business practices always involve adequate funding for the maintenance and acquisition of capital equipment. This is one reason why public operations often seem to be the poor relatives of their private counterparts.

5. Consumer input

The consumer is able to exercise a degree of control on private firms by deciding whether to shop with them or seek satisfaction elsewhere. The goods and services have to be oriented toward consumer satisfaction in order to attract customers and make profits. Where the public has no choice but to pay and take what is provided, as is usually the case in the public sector, this degree of control is absent.

Various expedients have been tried to achieve some substitute control. Boards representing consumers are often established with the statutory right to be consulted, or local committees of consumers may be part of the decision making process. In neither case does this give consumers the same power that the threat of withdrawal of trade does. In the absence of any effective input from consumers, public sector operations become producer-oriented and have their activities directed more towards meeting the interests of those engaged in production than towards those who receive the service.

Some public sector activities clearly are serving the interests of their workforce more than the interests of their customers. Often, the hours of opening or availability of the service are directed toward accommodating the wishes of management and labour. Price and quality similarly reflect producer interests. In the case of public sector manufacturing, the central aim of the activity is often shifted from the production of goods for consumers to the provision of jobs for workers.

It is sadly ironic that private businesses are more under the control of the general public than those businesses which are 'publicly owned'. The former can be influenced directly and

immediately by consumer decisions. The latter can only be influenced, if at all, over the vast distance of electoral control, and that in a diffuse and disorganized way.

6. Innovation and flexibility

When goods or services are produced under central direction, there is always a need to cope with the problem of control. Methods of production and distribution must be found which enable management to deal in manageable units. Not surprisingly, customers have to be dealt with in broad categories, rather than in terms of each consumer's individual preferences.

Where a number of competing firms vie for the attention of customers, much more variety is found, and the consumer is more likely to find a service tailored to his or her individual needs. Private firms are constantly seeking new products and practices to give them a competitive edge. They adapt swiftly to changing market conditions, knowing that failure to do so might lead to bankruptcy.

The rate of innovation in public operations is much lower, and public services appear to change only very slowly over time. During the time when a private sector good or service may change beyond recognition, the public sector seems to turn out the same products year after year. The low rate of innovation in the state's postal services, for example, contrasts sharply with the innovations of private postal services. Many other public sector activities also illustrate this point.

The desire to stretch public capital beyond the limit of its useful life, the reluctance of powerful public employee unions to accept change, and the absence of reward for entrepreneurial innovation all make for a public sector that is slower to adopt new ideas, more hidebound in its accustomed ways, and less adaptable to changing circumstances.

7. Decision-making

Decisions in the private side of the economy are based heavily on economic factors. The choice of when to expand and where, the choice of a level of production, the choice of a price - all of these decisions are made on the basis of economic criteria. Firms have to gear their decision-making to the market. They have to deal with the level of demand and with the price and availability of capital. And they have to use their knowledge of the market.

In the public-sector many of the important decisions are made on political grounds. Private business inhabits the economic world, but state business lies in the political world and is governed accordingly. Decisions are made on the basis of factors such as the popularity of the government and how the decision

will affect it. The number of marginal voting districts affected by a programme can provide the basis for a decision to expand or contract it. Public tolerance of tax levels can determine the level of funding. Voter response to a price increase is an important factor in the management of public sector industries.

What this means is that public sector decisions are divorced from the realities of supply and demand. Even a decision about the quantity to be produced is likely to be determined according to political judgements and without reference to what is genuinely wanted. This, in turn, means that public sector services are not allocated to areas of greatest need, or where they will generate the greatest economic returns. Political objectives can only be pursued at the expense of economic ones. Inevitably, the public sector does not operate with the degree of efficiency achieved by the more market-directed private sector.

8. Condition of equipment

Public sector equipment, being 'publicly' owned, is not owned by anyone individually. As a result, few people treat it with the care and attention that they give to their own property. People protect their own property, and tend to keep equipment in good repair before damage allows it to deteriorate further. The obvious motive is the desire to avoid loss and expense. This motive is absent in respect of public sector property.

It may be sad to reflect that people will not care for common property as well as they care for individual property, but it seems to be a fact of life. It is one which militates against public equipment being in a good state of repair: too often, public equipment seems shoddy and badly maintained. Citizens who would object strongly to attacks on private property seem resigned to accept vandalism and ill-use of common goods. Again, there are the added effects of under-capitalization and a captive market. Both contrive to produce outdated equipment in poor repair.

Private businesses tend to keep their equipment up to standard. To the private firm it is capital to be protected. Its condition affects both its use and the demand for it. Clean, modern and well-kept equipment is likely to increase sales and profit. This is why there is often the dramatic contrast between a private firm's gleaming facilities, clean and attractive, and the seedy, down-at-heel look of the public facilities.

9. Interruption of service

Although many goods and services were taken under the public wing in order that the supply might be guaranteed, a clear look at performance shows that the opposite is achieved. The public sector operation is more vulnerable to interruption.

Concentration of power provides the explanation. Public sector services in Britain are usually supplied by a public monopoly, with no alternative source of supply permitted. This, in turn, means that any interruption can shut down all sources of the service to consumers. In the private sector, a labour dispute in one firm threatens only its own customers; a labour dispute in a public monopoly threatens everyone. This gives great power to the labour force. Given the many interests competing for public funds, it is almost inevitable that this power will be deployed from time to time as the labour force seeks to pursue its own financial interests.

In the private sector, the workforce always has to consider the effect of such actions on their jobs. A strike might cause a permanent loss of customers, forcing the firm out of business. In any case, the public always will be able to turn to non-striking competitors. Public sector monopoly, on the other hand, prevents a situation in which a strike is more attractive. The job is less at risk, the shutdown is total, and there is always the hope of public pressure on the employer (the government) to back down and restore the service.

Private sector delivery, then, promises considerably more security of service to the consumer than does public sector delivery. This applies to essential services just as much as to other services. Food distribution in Britain would be difficult to interrupt, because food is privately produced under conditions that are diverse and competitive. Water distribution, on the other hand, was recently interrupted by industrial action. Water, for the most part, is distributed by the public sector.

10. Responsiveness to cost control

Private sector costs are controlled competitively. They are not, in any case, financed out of taxation. A rise in the costs, and therefore in the price, of private goods or services leaves us the choice to turn to cheaper competitors, to take up substitutes, or to consume less. Private businesses have to be ever alert to cost-cutting opportunities in order to attract financial capital. Investors put their money where the market indicates that a high return will be achieved. In the private sector, funds are not diverted away from profitable and successful concerns and into inefficient or loss-making ones.

The public sector shows an immunity to cost controls. Its budget is nominally under the control of government, to be raised or lowered according to political decision. Yet government after government has attempted to control public sector costs without achieving any result commensurate with the effort expended.

The truth of the matter is that public sector costs are made up of a variety of factors, many of which are outside the control of government, even though technically within the legislative domain. Public servants have little interest in reducing costs.

In fact, many have interests in the opposite direction. Groups which benefit from public operations form vociferous and effective lobby groups with high media visibility and the power to sap the will of an economy-minded administration. The savings realized by cutting public sector costs rarely benefit those bureaucrats who are expected to do the cost cutting. Moreover, those who ultimately pay for public programmes are neither as self-conscious nor as visible as those who benefit from them. All of this makes public sector costs very difficult to control. Attempted savings are more likely to result in the closure of the most popular and necessary aspect of the service, rather than achieve any savings from the elimination of administrative fat or from belt-tightening measures which improve efficiency.

The tendency in public sector operations is thus for a remorseless annual rise in costs, a rise which is beyond the powers of most governments to restrain, much less reverse. This brings in its wake a constant pressure on taxation, with funds needed for the expansion and development of successful private concerns being diverted and consumed by the inefficient state operation.

3. THE ATTEMPTS TO OVERCOME PUBLIC SECTOR PROBLEMS

Faced with the growing evidence of the deficiencies of public programmes, governments have attempted a variety of expedient remedies. The structure of public monopoly often means that government must attempt to represent the interests of the consumer as well as those of itself, as producer. Since the consumer cannot go elsewhere if dissatisfied, government is obliged to take due note of complaints, and to attempt remedies.

The problem arises from the fact that any proposed improvements in public services always seem to be those which cost more money. The industry itself goes to great lengths to show that only a large influx of new public money would enable it to deal with its shortcomings. Government thus finds itself in the position of attempting to stem the drain on taxpayers' resources, yet facing demands for improved services which would consume yet more funds.

If services become poorer because funds are restricted, the level of complaints will rise. On the other hand, if more money is allocated, there will be a greater burden on taxpayers, including the wealth-creating private economy. Government finds itself caught in the jaws of a vice which severely restricts any freedom of action.

For many years, there was a tendency in the advanced economies to respond to social problems by allocating more money to public programmes. In some countries, this practice continues. The comparison of public and private operations suggests, however, that there are weaknesses inherent in public sector organizations which lead to comparatively ineffective use of funds. The tendency to skimp on capital spending provides a case in point. As their capital is depleted, public programmes appeal for more capital funding. Unfortunately, the forces which lead to unbalanced current spending are still there, and any new funds are subject to the same one-sided pull. As a result, the proportion of any new allocation which reaches the capital account will be small. The logic that directs the system will cause much of the new funding to go towards relieving the pressure and allowing a continuation of an excessive use of labour and a top-heavy administration.

PROBLEMS OF PRESENT TACTICS

There are four tactics used from time to time by governments to deal with the escalating costs of public programmes. Unfortunately, none of these poses a solution to the inherent problems.

1. Efficiency drives

When governments become aware of the inferior performance of public sector supply, the attempt is sometimes made to graft on

to the public programme some of the efficiency-making expertise of the private sector. Typically in Britain, a senior management executive will head an efficiency programme, promising to use in the public sector the same methods which bring success in streamlining private companies. Sometimes, a group of observers with considerable private sector expertise will conduct an investigation and study, identifying areas where efficiency could be improved and making the appropriate recommendations. Whether the private manager is brought in from outside to run it, or whether he is asked to examine and report in the role of outside observer, the attempt is the same. It is an attempt to use the methods which the private sector induces spontaneously because of its need to remain competitive and profitable. Yet these methods are not induced in the same way in the public sector because it is non-competitive and not profit-making by design.

The effort is commendable, but of temporary effect. Such campaigns have achieved limited success, and that only during a short period of public pressure. When the novelty has died, the orthodox practices of the public sector gradually reassert their effects. The history of the public sector in Britain is littered with the names of 'whiz-kids' who brought a beneficial but short-lived influence from the private sector.

The reason for the transient nature of any improvement lies in the fact that streamlined business practices are an outgrowth of streamlined business. One can introduce bulk buying, better cash-flow control, and various short-cut procedures, but the one thing difficult to introduce is the incentive which will sustain and extend those practices. In the private sector, it is the pursuit of profit itself which ultimately serves that end.

It might be possible to introduce into bureaucracies schemes designed to substitute for the profit incentive. Ways might be found of linking the fate and fortunes of individual administrators with the performance of their area of responsibility. But the practice calls to mind the habit in socialist economies of allowing a miniscule market to survive in order to establish prices, or of paying a production bonus to factories and workers who exceed the government-imposed quotas. In neither case is this as effective as the real thing. It resembles the private enterprise economy only as a candle resembles the sun.

2. Drives to eliminate waste

A frequent tactic employed by a cost-conscious government is the initiation of procedures to identify and eliminate waste within public operations. An outsider is brought in, as with the efficiency drive. But in campaigns against waste, another civil servant is often employed to take a detached look at spending. The aim is to eliminate flagrant sources of abuse, some so habitual that they no longer can be recognized as such by those within a government department.

In the drive to cut waste, attention often focuses on trivial items, such as requiring bureaucrats to stay in three-star hotels instead of five-star hotels, or requiring the re-use of standardized envelopes. The more serious aim of these reviews is to pare down the administrative fat which adheres to the meat of public programmes, without cutting the service itself. If more productive use can be made of administrative personnel, then the hope is that spending can be curbed without risk to the programme's output.

Broadly speaking, such reviews have a propensity to instate a freeze on hiring, and to merge several departments so that one establishment can take responsibility for several activities.

As with efficiency campaigns, the drive against waste achieves temporary results. The larger department can indeed handle more areas and in the short term might reduce overhead costs. The problem is that the new, enlarged department has more authority and importance than its predecessors, and has more ability to direct increased responsibility, and increased funding, to itself. Inevitably, it acquires enhanced status with each new responsibility, and its administrators move up the scale of prestige and salary. Being larger, it often becomes even more difficult to manage and control.

There is another effect which the anti-waste drive shares with the efficiency campaign. Both try to bring in a fresh look from outside. In doing so, both undermine administrative morale by having key decisions taken outside of the department's own structure. Civil servants speak of 'riding out' these campaigns, waiting for less stringent times to return or for a government more relaxed about public spending.

3. Eliminating unnecessary programmes

Governments seeking to cut taxes look for areas of public sector supply rendered obsolete and unnecessary by changing social circumstances. A body set up half a century ago might no longer be required, given the new levels of affluence. The steam laundries and public bath-houses of Victorian England might be no longer needed, now that most homes have bathrooms and washing machines and that coin-operated laundries are easily accessible.

A possible source of public sector saving might be found in the complete elimination of unnecessary services. The problem for government lies in the determination of what is or is not necessary. Administrations which embark on such a course are frequently surprised to discover just how passionate and vociferous is the defence for any public programme, no matter how useless it might now seem.

The point is that every public service has its beneficiaries. There are some who have a locational advantage in a tax-funded programme of little general benefit. There are regular users who

prefer the free or cheap service, even though they could afford the private sector alternatives. The steam laundries and bath-houses provide examples. Whenever there are moves to close any of them, a public outcry is always the result.

Every public programme also has its losers. These are usually the general taxpayers, whose standard of living is lowered to provide the service which benefits others. These losers are neither well organized nor very visible. Those who benefit from public programmes know themselves to be beneficiaries. They are a visible group ready to lobby and attract media attention. Very rare is the general taxpayer who is prepared to chain himself to the railings of a bath-house demanding its closure to save public funds. Pressure upon legislators thus is heavily loaded in support of public programmes, no matter how little good such programmes create.

Administrators themselves, although expected to administer the dissolution of unnecessary programmes, have no interest in seeing this done successfully. On the contrary, it threatens their status and even their job to have their area of responsibility diminished. Not surprisingly, all kinds of bureaucratic obstacles and impediments appear in the way of policies which would phase out public programmes.

These effects take their toll. Governments which embark boldly on elimination of useless activities soon find there are none to be agreed upon. Every programme is fought for bitterly, with losses in prestige and goodwill sacrificed in return for only meagre gains. The steam runs out of the government drive long before it successfully shuts down the publicly-funded Victorian laundry.

4. Cash limits

The policy of cash limits is the outcome of an intelligent attempt to cut the Gordian knot of departmental spending. In annual budget preparations, governments have seen each element of the public sector fought for by its own administrators, with the cumulative effect being an overall increase in spending.

The cash limits strategy tries to do two things. By imposing an overall budget limit on a department, it encourages some areas within the department to oppose spending by others, since this is the only way their own can acquire additional funds. The hope is that in this way, essential services will be guaranteed but that administrators will join forces with each other to vote down increased appropriations to unnecessary activities. The second aim of a cash limits policy is that the administrators themselves will introduce efficiency and anti-waste campaigns to continue operation under the constraint of an overall limit on spending. Here too, the assumption is that what is not needed will go, leaving an altogether more cost-effective programme.

Neither attempt succeeds as intended, leaving the policy of cash limits much less successful at controlling public spending than its proponents hoped. In the first place, within any government or any individual department, it is not the most necessary programmes which corner the funding, but the ones with greatest political pull. Departments of government are no less vulnerable to office politics than other organizations. The difference here is that public money is tied up in it. Sometimes the large bureau has more influence because it is larger; so the effect of cash limit campaigns is to improve the position of the big bureaucratic operations at the expense of the smaller ones.

Secondly, the effect of the overall limit on each operation is by no means that which is sought. Instead of the savings coming from the elimination of inefficiency and waste, spending cuts tend to be applied directly to the delivery of valuable services. Administrators asked to economize do not do so with their own jobs and salaries. They come forward instead with proposals to cut out certain parts of the service, albeit without significant reductions in overhead costs. The effect of cash limits, therefore, can be to make the public sector less efficient. Capital spending is cut first, being the easiest option. Then important services are dropped, leaving roughly the same overhead establishment operating on a smaller capital base with lower output.

The other aspect of cash limits which is distressing to government is the degree to which media manipulation is used to undermine the campaign. Those inside and outside the bureaucracy who oppose limits on spending know which are the most popular and sensitive services. These are the ones put at risk first or characterized as most vulnerable. Savings on the welfare budget can only be achieved, it seems, by closing schools for handicapped children and by throwing dependent old people out onto the street. Naturally, enough, these horror stories are extensively covered by the media, ably assisted by leaked memoranda showing more atrocities on the way. Government supporters in the legislature wilt under the hail of fire, and the cash limit campaign has its fangs pulled.

CONCLUSION

The failure of these four tactics suggests that government is unable to control public sector spending, except temporarily in a few selected areas and at great cost in political support.

Although criticisms of administrations abound from those opposed to public sector spending, lack of effort on the part of the administration is not usually a just charge. Complaints that the government 'was not tough enough', 'should have done more', or 'ought to have done it all on the first day while it was still popular', all assume that government can control public sector spending. Failure to do so, it is assumed, must involve a failure of will. Yet the above analysis suggests that public spending is pushed by factors outside the control of government.

It is the critics who are at fault, adhering to the myth of legislative omnipotence. A careful and sympathetic examination of the forces which thwart the intentions of government might point the way to policies which could overcome them.

4. DISMANTLING THE STATE

All of the traditional policies that attempt to control public sector costs operate at the macro level, attempting to secure solutions from the top. All of them operate on the supply side, seeking to alter the conditions under which public sector goods and services are produced. All of them seek wide-ranging benefits secured by a series of changes imparted through central planning. All of them fail, to a greater or lesser extent, to achieve the chosen objectives.

There is, however, an alternative approach which was hardly featured in the manifesto of the Conservative government elected in Britain in 1979, but which has nonetheless achieved major successes. This is the policy of moving state operations towards the private sector, instead of merely attempting to restrain their costs. The thinking behind this approach is that only the private sector itself can impose the economic disciplines and create the incentives which are desperately needed.

The policy of privatization, of transferring public activities wholly or partly into the private sector, derives from a recognition that the weaknesses of the public supply are inherent. It assumes that any temporary grafting of private enterprise attributes onto the state sector will be temporary, and that the gains will be whittled away as the characteristics of the public economy reassert themselves. Such attempts to make the public sector more cost-effective and more responsive to demand are ones which will have to be continually remade, at great cost in political goodwill, and with no permanent success.

The actual transfer to the private sector, on the other hand, can take the service into the purely economic world and out of the political world. It can expose the service to the perpetual effects of competition and cost controls. It can give consumers choice and input. It can leave capital spending and price decisions free to be determined by straightforward economic logic, instead of by an anticipation of what the public might tolerate.

The transfer of resources

From the point of view of government, perhaps the most attractive feature of this solution is its permanence. It needs to be done only once, whereas the cost campaigns need to be fought and refought, year after year. Once the service is in the private sector, it is outside the direct area of government responsibility. Its costs no longer have a direct impact on taxation; its labour force no longer works for the state; and its level of service is determined by demand.

Of nearly equal importance to government is that cost-cutting campaigns are normally equated with cuts in services, whereas the

movement of a public operation into the private economy need not involve any deterioration in quality of service. On the contrary, many of the forces which contribute to sub-standard performance by state enterprises will cease to operate after the transfer is made, and an improvement in quality can be expected. In political terms, this means that a government which adopts this approach faces less public criticism and media denigration than one pursuing economy campaigns perceived as a threat to essential services.

The policy of transferring operations from the public to the private economy is much more oriented to the demand side than to the supply side. It asks the fundamental question of a state activity: can public demand for this service be satisfied by the private market? If the answer is yes, then a variety of measures are available for effecting that transfer. Many of the actual methods of making the change occur piecemeal, allowing separate decisions to build up gradually to the transfer of an entire sector.

None of this should imply that privatization is easy. Just as there is no shortage of people urging the government to cut costs, so there is no lack of those recommending privatization. There is no such profusion of people explaining how costs can be cut, or how tasks which have for many years been performed in the state sector can suddenly be incorporated into the private and competitive economy. In practice, the shift of supply from state to private sector requires a battery of sophisticated techniques which take full account of the political and social problems of the public sector, as well as of its economic shortcomings.

The Conservative government in Britain, which was elected in 1979 and re-elected in 1983, has used more than twenty-two different methods of transferring public operations wholly or partially into the private sector. In doing so, it has achieved the largest transfer of property since the dissolution of the monasteries under Henry VIII, a transfer from the state to its citizens. This transfer has meant that large and increasing areas of public supply are now subject to the economic disciplines brought by the private market. From the government's point of view, costs now are being controlled more securely than could ever be achieved through economy campaigns.

The transfer is almost certainly permanent. It has been achieved using a variety of ways which make it difficult to reverse. New groups have a vested interest in the new status quo, and a public accustomed to regarding the public sector as a drain on its resources is unlikely to give endorsement to a campaign for re-appropriation. The transfer is ongoing. A small part of the total public sector has been privatized, but the techniques which have worked on one area are constantly being prepared for application elsewhere. The progress is remorseless and one-way.

These continuing changes have some similarities with the great

retreat of government which was set in motion in the first half of the nineteenth century in Britain. Under the influence of the ideas expounded by Adam Smith, a succession of administrations dismantled much of the regulatory apparatus of state over a period of half a century, culminating with the repeal of the corn laws in 1846.

In recent times, the year 1979 appears to have denoted the high water mark of the public sector in Britain. Since then, the huge machine of state industries, regulations and transfer payments has systematically been dismantled, to be replaced by more efficient and more responsive private sector alternatives.

What this means for Britain, among many other things, is that the potential for future governments which are less economy-minded is being severely restricted. An administration which merely holds down the growth of government for a time is easily replaced by another big spender. This time, however, there has been a permanent transfer of resources, and a momentum generated which will be difficult for successor governments to withstand. Britain may well be entering upon the early stages of another long retreat by government.

Wide range of methods

One reason for the success of this strategy has been the wide range of techniques used to execute the transfers. It is not simply a question of 'selling off the state.' On the contrary, there are very few parts of the public sector which are appropriate for direct sale. It is a question of regarding each part of the state as an individual problem requiring appropriate treatment.

The successful methods have been those which deal with the entrenched forces, with the interest groups and with the political pressures which devolve on the state sector. For every state programme there are the administrators whose job is enhanced in status by the responsibility for it. There are the public sector trade unions which thrive on the power of a public service monopoly. There is the workforce with a guaranteed job, who have often been able to secure comfortable conditions without the risks of bankruptcy to restrain them. There are those who benefit from a subsidized operation, and those who thrive by representing and lobbying for those recipients. There are the media, ever-ready to see government failing in its responsibilities.

These groups have the potential to oppose a transfer to the private sector, just as they are able to thwart cost-cutting exercises. The successful methods of transfer involve a recognition of the role played by each of these groups, and the inclusion of provisions which neutralize or outweigh the adverse effect they might have. If, for example, circumstances are contrived in which the beneficiaries do even better under a private system, their voice will be muted, alongside those of

their lobbyists and the media. Their embrace of the new system may be sufficient to outweigh the objections of the bureaucracy and the trade unions. Alternatively, ways might be devised to ensure that the change was accompanied by an improvement for the workforce. Each of the methods employed successfully has its own variation for coping with the realities.

For government, a very important factor in the change from public to private is the need for assurances that the most vulnerable and dependent groups will be protected during the turn-over. The vocabulary of trade union opponents of privatization abounds with terms which imply that the weakest will go to the wall. Profit-seeking entrepreneurs will move in, it is claimed, 'skimming off' the lucrative and profitable parts of the service, leaving those without power without a service. The concept is erroneous because it takes no account of the remarkable ability of private businesses to move in and make money from services which cost the state a heavy loss. Yet it still leaves government seeking to build in assurances that dependent groups will not suffer because of the transfer. Some of the techniques therefore involve the acquisition by dependent groups of effective buying power, either by direct grants to needy individuals, or through the use of publicly-paid contractors to guarantee the service for them.

In the case of utilities and services deemed essential, a government contemplating a switch to private sector supply might need to give considerable attention to the problem of outlying consumers, and take steps to ensure that supply can be guaranteed to these consumers after the change. Sometimes, the removal of unnecessary regulation suffices to ensure that new types of service will evolve that can profitably serve even remote or scattered customers. Sometimes, more active assurances might be built into the charter terms of private companies permitted to operate.

It is by careful examination of the processes of the public sector that government is able to anticipate the response of the various parties involved, and to make the necessary adjustments to the techniques to be used. The process of privatization is not one which depends only on the will of a government. There must also be considerable creativity in policy innovation. New and sometimes intricate techniques are required, each to be tailored to the particular problems caused by individual areas of public supply. Public ownership cannot be dealt with by the same methods as public regulation. State-produced goods require quite different techniques for transfer than those needed for the transfer of state-produced services.

The operations of the public sector have to be regarded as processes, and examined minutely to track down the way in which their elements motivate individuals involved as producers or consumers, as taxpayers or beneficiaries. Policy creativity is needed to ensure that the new reality will be willingly supported by enough of its participants to make it a success, and to

guarantee its permanence. *Micropolitics* is the art of generating circumstances in which individuals will be motivated to prefer and embrace the alternative of private supply, and in which people will make individual and voluntary decisions whose cumulative effect will be to bring about the desired state of affairs. The process of transfer from public to private economy is most securely achieved when its progress is evolutionary, arising from free decisions.

The following analysis of the various methods employed to dismantle the state sector shows how each of them deals in a different way with the problems posed by various interest groups. The analysis covers many different types of public operations, and, as might be expected, reveals many different types of solutions.

5. THE TECHNIQUES

METHOD ONE: SELLING THE WHOLE

There are cases of public sector activity in which government is able to sell, as a unit, the whole of a specific operation. Relatively small organizations which deal with a specialized product or service are often suitable for this very direct treatment. Alternatively, units which have been acquired by chance, as subsidiaries of larger concerns which were nationalized, can sometimes be returned to the private sector by this method.

Large parts of the state economy are not suitable for direct sale, however. Those involving regulation or transfer payments cannot be run as profit-making enterprises, and many of those engaged in the production of goods or services have a long history of financial losses and labour troubles which render them unattractive to buyers. The argument is sometimes advanced that government enterprises which make losses cannot be sold, while charges of 'asset-stripping' are levelled at attempts to sell enterprises that are profitable.

The argument is more valid if it is inverted: operations which make profits can be sold, and those which make losses must be sold in order to stop the constant drain on resources. While some state operations make money, this is usually temporary, and should prompt the legislative to move quickly toward their disposal while conditions are good.

A sale, skillfully handled, creates a new interest group in the new owners. This group constitutes a lobby which can be counted on to oppose moves towards subsequent expropriation. With the prospect of private capital coming in to develop and renew the operation, the workforce may have any initial misgivings allayed, and come rapidly to prefer working for a successful private concern rather than for an ailing, capital-starved public organization. The bottom-line security in the state system may be shown to be worth less to them than the opportunities for advancement which a streamlined, modernized private company can bring them.

In a similar way, any initial doubts felt by the public concerning the possible risk to supply can be replaced by a conviction that the new service is better, more varied, and more responsive. In any event, the areas where total sale is appropriate are often those in which the consumers form a highly visible special interest group. The effect on the general public may be minimal with respect to their role as taxpayers. The proceeds of the sale go to relieve the pressures on the public purse: they can be deployed to reduce the public borrowing, to narrow a deficit, or to reduce taxes.

In light of these incentives taxpayers, and legislators can be

added to the groups who can gain substantially from the sale of a public operation. Under the right circumstances a direct sale can be achieved with political as well as financial success, and it can be made practically impossible to reverse.

Amersham International

A good example was afforded in Britain by the sale of Amersham International, the small radionics firm. Previously known as the Radiochemical Centre, Amersham International had dealt for forty years in the supply of man-made radioactivity obtained from nuclear reaction (or atom-markers). More recently, it had developed strong links with the market for extremely sophisticated medical equipment.

Until the offer for sale on 15 February 1982, the shares were held by the government's Atomic Energy Authority. The price per share was set at 142p, and the offer for sale was oversubscribed 24.6 times, with applications from both employees and the general public. The employees were allocated 1.8 million shares (representing 3.6% of the issue share capital), with 99% of them taking the government offer of £50 worth of free shares. Furthermore, over 80% of employees took up the one-to-one share offer, whereby their own investment would be matched by an equivalent number of free shares up to approximately £250 per applicant. Also, 40% of the employees applied to buy under a preferential application scheme.

In the end, the sale raised £71 million, taking into consideration the £310,000 that was paid for professional advice. Of this £71 million, £5.7 million will eventually go to the company while the remainder will go to the government.

Amersham International was thus wholly sold off and is now fully within the private sector of the economy. The method of sale was criticized in Parliament, with allegations that the low offer price had enabled City friends of the government to 'make a killing'. This may have precipitated subsequent moves towards sale of shares by other methods.

METHOD TWO: SELLING COMPLETE PARTS OF THE WHOLE

Even where the whole of a public operation cannot be sold, there are instances in which distinct sections of the whole may be sold off independently. Even though the main body may be in no condition to attract buyers, it may be possible to separate out parts of the organization which have better prospects of finding purchasers. In some cases, two or more parts may be effectively packaged, making a parcel that is a viable proposition for a purchaser.

When the whole of a public sector organization is sold, it tends to be sold by the issue of shares on the stock market.

Thus, when a public enterprise is sold en bloc, there is a great deal of attention paid to the method of issue, the ways of bidding for shares, and the diversity of ownership which is sought.

When a complete part of the whole is offered for sale, it is usually done by finding a single private buyer. For this kind of sale it is usual for negotiations to be undertaken with interested parties, such as corporations already active in similar fields. Price and conditions are agreed, and the transfer is effected in exchange for payment from the company to the government. In this way, complete parts of state activities are taken over by corporations operating within the private economy. Very often, these activities were anomalous to the main activity to which they originally belonged.

Sometimes the government has actively sought buyers, and carefully prepared packages for the purpose of enticing sales. In other cases, with a government known to be sympathetic to the concept of privatization, the initiative has come from the potential buyer. In this case, a corporation may approach the government with a suggestion for take-over.

When parts are sold to a single buyer, the outcome for the employees, including those at management level, is of the utmost importance. Without a diversified ownership, there is no broad-based new interest group to defend the new status quo. In this case it is advantageous to have a management and workforce who perceive the new arrangement as beneficial to themselves. This at once removes a possible source of opposition to the transfer, while simultaneously helping to make the change permanent. The new owners, of course, have an interest in protecting the new arrangement, and the taxpayers benefit from the proceeds of the sale.

As with the sale of entire operations, the expectation for the sale of a part is that the service will improve as it is modernized and recapitalized, and that consumers will prefer it in its new setting, offering yet more resistance to any attempted or proposed reversal of the change.

Range of examples

The success of this method is illustrated by the wide variety of state operations which have been returned to the private sector by its use. The following list shows the diversity of its application.

(1) **British Rail hotels.** It seems strange to think of a state-run railway being in the hotel business, but British Rail had found itself operating twenty-nine hotels. By March 1983, twenty-seven out of the twenty-nine hotels had been privatized by the British Rail Board subsidiary, British Rail Investments. Three Scottish hotels were placed into a new company, Gleneagles Hotels Ltd, which started to trade in June 1981. The British

Rail Board received £10.35 million - part of it in deferred payment - of which £4.5 million was used to buy loanstock and shares in the company.

In February 1983, bids for a total of £25.85 million were accepted for ten hotels and then another nine were sold soon after for £8.7 million. (The two remaining hotels have been let on short leases and not sold, because they were in the immediate locality of stations shortly awaiting development.)

(2) English Channel ferry services. Shipping ferry services across the English Channel were another subsidiary of British Rail. When they were formed into a separate state-owned company in 1979, the name 'Sealink' was chosen. It was one of Europe's largest ferry groupings, operating forty ships on twenty-three different routes, and owning seven major harbours, together with several smaller harbours and piers.

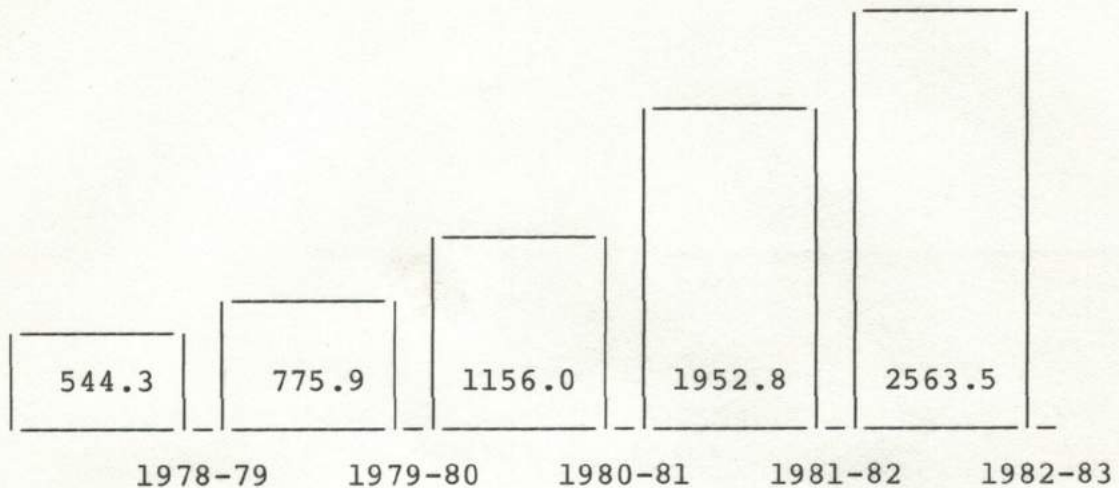
The British government decided to sell Sealink to a single buyer, and in 1984 it was sold to Sea Containers, a Bermuda-based American company, for £66 million.

(3) The Manpower Services Commission. The Manpower Services Commission has responsibilities which include job advertising and some industrial training. A number of the restaurants in its training centres have been sold off, thus taking them outside the public sector. The Commission is to close large numbers of its job centres, and to use kiosks in private premises such as supermarkets to take their place.

(4) North Sea oilfields. The North Sea oilfields which were government-owned through the state-run gas corporation were formed into a state company called Enterprise Oil. Stock was offered to the public in June 1984, at 185p per share, representing a total valuation of £392 million. Investors took only 65% of the stock issue, but the government received all its money because the underwriters took the rest. The low demand was put down to several factors, including a low prospective yield, an unsettled oil market, and rising interest rates.

(5) Government land and buildings. Sales of land and buildings by both the British government and the various city and district governments have taken place at an increasing rate.

Table 1
Sale of land and buildings by central
and local government (£ million)



Source: Parliamentary Question: *Hansard*, 26th April 1983.

(6) **Tractors and trucks.** The state-run car industry in Britain, British Leyland, sold its forklift truck subsidiary, and its tractor line at Bathgate in Scotland.

(7) **Refrigerators.** British Leyland also ran a state-owned refrigerator company called Prestcold. This was sold to Suter Electrical, a private company, for £9 million.

(8) **The National Coal Board.** The National Coal Board sold land, vehicles, and buildings to the tune of £19 million.

(9) **British Airways.** The state airline, British Airways, sold off a subsidiary communications company, called International Aeradio, for £60 million. This was while British Airways itself was being prepared for privatization.

(10) **Motorway service areas.** The Department of Transport has sold thirty-eight state-run motorway service areas which provided motorists with car service, refueling, and catering facilities. They were sold on fifty-year leases to the Rank Organization, Granada, Trusthouse Forte, and Imperial Foods for roughly £50 million.

(11) **Oil stockpiles.** Government-owned oil stockpiles were sold in 1982-83 for a yield of £33 million.

(12) **Oil and gas exploration licences.** For the eighth round of offshore licensing for oil and gas exploration, the British government decided to sell licences for fifteen of the 184 offshore areas. Offers for seven of these raised nearly £33 million.

(13) **Water authority land.** The Regional Water Authorities in Britain sold off £3 million worth of land in 1979-80.

(14) **Property Services Agency.** The Property Service Agency administers state-owned estates in Britain. It sold land and buildings worth £5 million 1979-80, and a further £4 million in 1980-81.

(15) **British Steel.** The government-run steel industry, British Steel, sold a subsidiary steel company called Redpath Dorman Long to Trafalgar House, a private corporation.

(16) **British Sugar.** The state's holding of 24% of the stock in British Sugar was finally disposed of in 1982, with the government gaining £44 million from the sale to the private sector.

(17) **Crown Agents.** The Crown Agents, responsible for administering overseas property held by Britain, sold over £16 million worth of assets in Australia.

(18) **National Health Service land.** The National Health Service is reckoned to be Europe's largest employer. It also holds large amounts of land. For the two years ending in March 1981, it sold 1,460 acres for a total of £25.5 million. A further 4,000 acres are currently awaiting sale back to the private sector, since the National Health Service has declared it no longer needs them.

(19) **British Petroleum.** British Petroleum is an oil company which formerly had the British government as a majority stockholder. However, in November 1979, the government reduced its holding from 51% to 46%. This meant that the company was now technically in the private sector, and could raise capital without it being counted as government borrowing. A subsequent stock issue of 1981 lowered the government holding to 39%, and the government sold some of its stock in 1984 for £565 million, bringing its holding down to 31.7% of the stock.

(20) **Property in the new towns.** Britain's 'new towns' were set up as government-sector corporations, mostly after the second world war. Since 1979, the first year of the Thatcher administration, the new towns have sold £400 million worth of industrial and commercial assets. In addition, the new towns have sold large quantities of land for residential use, as well as actual homes. For the years 1981-83, sales amounted to 75 hectares, land made available under licence came to 580 hectares, and dwellings sold totalled 13,960.

(21) **Local government residential land.** Local authorities similarly disposed of residential land. Over the same period, 1981-83, they sold land for private housing of 1,615 hectares, and made a further 470 hectares available for disposal under licence.

(22) **Shipbuilding.** The state shipbuilding company, British

Shipbuilders, sold off its biggest loss-making yard, the Scott-Lithgow Shipyard. It was sold for £12 million to Trafalgar House, with payment being made in installments. The government had to spend £71 million to 'wipe the slate clean', writing off debts and honouring commitments. This sounds like a bad deal until one appreciates that Scott-Lithgow lost £66 million in 1982-83 alone. It was a case of short-term spending to free the state from long-term losses.

(23) Suez Finance Company. In 1980-81, the government received £22 million from the sale of its shares in the Suez Finance Company.

(24) The Forestry Commission. The Forestry Commission is responsible for huge state-owned forests in Britain. It has sold tracts of land and property, including residential properties. The 1981 Forestry Act allowed it to sell both planted and unplanted land.

METHOD THREE: SELLING A PROPORTION OF THE WHOLE OPERATION

Where it is inappropriate to offer the whole activity for sale, or even dispose of distinct parts of it, it is sometimes feasible to offer for sale a proportion of the operation. In common parlance, this means allowing people to buy in on a state business, while retaining a proportion of it in public ownership. Instead of offering 100% of it for sale, the government offers a smaller percentage, often 51%.

There are clear advantages to the government in following this course of action. In the first place, it makes money from the sale. Secondly, it spreads ownership and reduces the size of the public economy. By the Treasury's own regulations, if the state holding drops below 50%, future capital raising by the business is exempted from the public sector borrowing requirements and capital may be raised on normal commercial considerations. But even if only 10% is sold to the private market, the business becomes subject to many of the laws which protect the owners of private corporations.

From the government's point of view, this can be a very effective method of gaining value for money when releasing government assets. A state corporation with an unhappy history behind it might not command a very high price. By selling a percentage, especially a controlling percentage, the state returns it to the private sector even when it retains a significant holding. As the disciplines of the private sector assert their effect on the operation, it becomes more cost-effective and more profitable. The value of the state's holding increases, and can be sold for a higher price.

The sale of a proportion of the total ownership brings in immediate cash to the government, and to the business itself for recapitalization. It sometimes turns what is in most years a

liability to the government into a substantial asset. There is a reasonable expectation that the improved performance will increase the worth of the state's remaining percentage to one which approaches or exceeds that of the original whole.

Naturally enough, the new shareholders who have bought stock form a group opposed to subsequent expropriation. Management and workforce can be brought to appreciate their improved prospects under an influx of private capital. Legislators gain in many of the ways outlined. As with other methods of sale, it is the public sector unions - leadership rather than membership - which form the single group which can be expected to oppose the measure. They stand to lose the power which their position in the public sector gives them, and which will be limited by all kinds of commercial considerations in the private sector.

Britoil

A British example of this type of exercise is afforded by the sale of 51% of the shares in Britoil. This was the state activity dealing with the exploration for, and production of, oil and gas from the North Sea.

Britoil's assets included six producing oil fields and one producing gas field. In addition, it held three more oil fields with very good potential, but still under development. At the time of its share offer (1983) it had the largest acreage of licence interests in the United Kingdom Continental Shelf area and was responsible for approximately seven per cent of the total oil production from that area.

The sale offer for Britoil, of up to 255,230,028 ordinary shares of 10p each at a minimum price of 215p per share, was made on 19 November 1982. This represented 51% of the shares in Britoil and led to applications being received for around 70 million shares. This undersubscription left the remainder, 185 million, in the hands of the underwriters and sub-underwriters.

Of all applications received, 99% came from small investors and employees, with over 35,000 applications being for 2,000 shares or less. This may be explained partially by a small shareholder bonus scheme which involved the 'gift' of further shares if the individuals concerned retain at 30th November 1985 at least the number of shares originally allocated to them. Over 92% of eligible employees bought shares.

Although undersubscribed, the total share issue grossed over £548 million, and the gross proceeds to the government will eventually reach around £640 million when £88 million debenture is repaid by Britoil.

The commonly accepted reasons why the share issue was undersubscribed are the considerable uncertainty over oil prices, the belief (since proven correct) that they were about to fall from

1982 levels, and the fact that the method of sale - inviting bids on the basis of price - is far too inflexible. Doubts about the method explain why subsequent sales have been by fixed-price tender.

Despite the undersubscription for the stock, the government (and hence the public) did receive their money from the underwriters. The sale was successful insofar as it is desirable to have satisfied investors participating, but also in that it was the smaller investors who gained more from the privatization operation. To involve smaller investors has been a key objective of the government in all its privatization programmes.

Cable and Wireless

A second example of a partial sale is that of Cable and Wireless. Under the provisions of the 1981 Telecommunications Act, the British government was empowered to sell shares in Cable and Wireless, a group of companies who, in the main, operated overseas, supplying telecommunications services and facilities. However, since its semi-privatization it has attempted to shift towards the British market. To that end, it provided forty per cent of the initial finance for Mercury, the newly licensed telecommunications firm who are establishing an independent system in competition with British Telecom. Cable and Wireless had interests in the provision and operation of the public telecommunications services of thirty different countries and territories.

Following the offer for sale, the government had 50.53% of the issued share capital of the company. Meanwhile, over 99% of the workforce decided to buy 3,785,833 shares - equivalent to 5% of the proportion of total issued share capital. However, the government's share fell to 45% when a subsequent issue to existing stockholders in March 1983 was not taken up by the government, thus increasing the proportion of Cable and Wireless shares held in the private sector to 55%. This state of circumstances did not last very long. On 27 October 1983, the government announced that it intended to sell even more of its remaining shareholding in Cable and Wireless plc - about half, representing 22.2% of the company's issued ordinary share capital.

The sale was made at a minimum price of 275p a share, with a total of 100 million shares on offer. The government was guaranteed a minimum of £275 million following the completion of the underwriting on 25 November 1983. A further 25% of the government's holding in Cable and Wireless was sold in early 1984, raising £262 million. This means that the government now retains only 25% of the total share issue.

Associated British Ports

The state-owned harbours were sold by a similar method. The

British Transport Docks Board operated the following ports: Southampton, Hull, Grimsby, Immingham, Goole, Swansea, Port Talbot, Barry, Cardiff, Newport, King's Lynn, Lowestoft, Plymouth (Millbay Dock only), Garston, Fleetwood, Barrow, Silloth, Ayr, and Troon - a total of nineteen in all, dealing primarily with freight traffic.

After its conversion into Associated British Ports, a total of 21.3 million shares were sold in February 1983. This represented 51.5% of the total shares of the company, with the remaining 48.5% being retained by the government. All in all, 91% of the workforce became shareholders, buying a total of 1,736,545 shares (12.2% of the total). The government offered shares at 112p each, but they were oversubscribed thirty-three times. Nevertheless, it received £21.95 million from the sale as gross proceeds, plus a further £25 million in cash from the Associated British Ports group. The government finally dissolved itself from ABP when, on 18 April 1984, it sold 19.4 million ordinary shares of 25p representing the remaining 48.5% of the issued share capital. Gross proceeds were £53 million.

British Aerospace

British Aerospace (BAe) was established as a state-owned corporation in 1977, involved in aircraft manufacture. By 1980, BAe had established itself as a sizeable concern, with capital assets of about £700 million, a current-cost profit in the same period of around £65 million, and a workforce of 75,000 people.

BAe is mainly involved in the civilian side of the industry, with interests in Airbus Industries, the A310 aircraft, and the older, better-known models, such as the BAe 111 aircraft. Significantly, the Airbus family has been said to represent the only credible competitor to the American giant civil aircraft manufacturers, such as Boeing, McDonnell-Douglas, and Lockheed. However, BAe is also involved on the military side of aircraft production, with its highly profitable aerospace and missile interests plus its joint ventures such as the Tornado, the Harrier Jump Jet, and the Anglo-French Jaguar aircraft.

In 1981, on 13 February, the Secretary of State for Industry offered for sale up to 100 million shares (representing 51.6% of the total number of ordinary shares available) at a price of 150p each. Over 27,000 employees bought shares (40% of the total workforce) applying for around 10.6 million, although receiving only 7.1 million. This represented an employee over-subscription in the region of 50%.

The gross receipts from the sale were approximately £148.6 million, but after deducting the expenses of the sale (£5.6 million) and payments to the company of £100 million for the new shares subscribed for by the Secretary of State, the total net receipt was £42.9 million.

Jaguar - British Leyland

Britain's state-owned carmaker, British Leyland, announced that 177.9 million shares in Jaguar, its luxury division, would be sold at 165p each, valuing the company at £294 million. It announced its intention to expand annual output by 4,000 cars, equivalent to an eleven per cent increase in output, and take on a further 530 workers across Britain. The share issue was heavily oversubscribed, and there were traffic jams and fights in the street as potential buyers struggled to enter their applications for stock. It was voted as one of the most successful share issues in the history of the London market.

British Telecom

By far the largest floatation of a public corporation so far is that of the sale of 51% of the stock in British Telecom, for which the government realized some £4,000 million. Once again, a great deal of effort was put into ensuring that small investors played a part in the new company, and there were generous allocations for those applying for small numbers of shares, and for workers in the company. Vouchers, offering a discount on telephone bills, were available to individual shareholders who retained their holding for six months. A national TV and newspaper advertising campaign made the general public aware of the floatation and how to acquire shares.

The result was that when the shares were offered for sale in November 1984, they were oversubscribed by five times: over a million people applied for the shares. A number of the larger investing institutions were disappointed to find that they were allocated only around half of the shares they wanted to take up; members of the public were limited to a maximum of 800 shares, even if they had applied for more; and when trading started in early December, activity was brisk.

Although opponents of the transfer argued that the shares had been sold too cheaply, the wide involvement of the general public made it an undoubted success. Furthermore, careful conditions were put into the operating licence arrangements for Telecom which helped to counter opposition. These included conditions that the new company:

- (a) would continue to provide a comprehensive telephone service where reasonable demand exists;
- (b) would maintain emergency and rural telephone services; and
- (c) would connect its system to competitors such as Mercury.

Conclusion

The Thatcher government has given considerable attention to pre-

paring government-owned industries for privatization. Whether the sale is a whole enterprise, or separate parts of it, or of some of the shares in it, there are many government operations rendered unattractive to buyers by long years in the public sector. Bad business practices, depleted capital stock, feather-bedding at both management and labor levels, uneconomic working practices and poor production quality do not appeal to investors seeking high rates of return.

By subjecting bloated state enterprises to a strict regimen, however, the government has brought many of them nearer to the point where they can become viable private sector operations. Managers have been appointed to bring about major changes by cutting down on loss-making activities and on feather-bedding practices. In some cases, the removal of protective monopoly privileges has permitted competition to prompt similar moves. The overall result has been to increase the options for privatization through some form of sale.

METHOD FOUR: SELLING TO THE WORKFORCE

For some government activities, it may be possible to sell the operation as a complete entity to the workforce. The obvious merit from the government's viewpoint is that this secures the co-operation of labour and management during the transition. The reasoning behind this method points to the importance of motivation.

For most public sector activities, there is no strong link between employee performance and reward. Only recently in Britain have bonuses for increased productivity been used genuinely as a major element in employee compensation. All too often there have been so-called 'incentive payments' whose real function has been to save face for a government forced to concede a higher wage increase than its current wage guidelines called for.

Workers who participate in the ownership of their company, on the other hand, have a real incentive to recognize their own interests within those of the firm. In employee-owned firms, restrictive practices stop and the quality of service leaps forward when the employees gain personally from reduced costs and increased sales. Workers are often in a good position to assess what effect on productivity and production would result if they become the owners of the firm. They can thus assess the viability of a privatized co-operative.

Just as the public expects better service from a manager who is also the owner, so it can expect better treatment from a firm whose workforce owns it. In this way the two large groups who are potential opponents of such a move - consumers and workers - both have their interests bound up in the change.

This is an appropriate method for privatizing the public sector

when independent buyers might doubt their ability to achieve full-hearted co-operation from the employees under private management. The employees, as owners, know that they will do what is required. In this way it is possible for a loss to the government to be transformed into a profit for the workers, with the government receiving the proceeds of the sale in the bargain.

The National Freight Corporation

Britain's National Freight Corporation was sold to its employees, at their suggestion, and provides a remarkable case history of successful transfer.

The National Freight Corporation was established in Britain in 1969, in an attempt to bring together under one roof all the road freight transport interests that the government had acquired. It was set up with an initial capital debt (excluding any payment of interest) of almost £100 million.

The government's plans for sale were outlined in a press notice of 22 August 1979. It was felt that National Freight's poor financial performance would prevent its sale by a straightforward flotation. In May 1981, a proposal for an employee buy-out was put to the government from within the NFC; and by October 1981 a conditional sale agreement had been signed. On 19 February 1982, the National Freight Company Ltd became a wholly-owned subsidiary of the National Freight Consortium - owned jointly by employees, pensioners of NFC, and four banks.

The deficiency in NFC's pension schemes was to be funded by the government, and this had a considerable effect on the price which the government received. NFC was sold for £53.5 million, but, after deducting the contribution to the pension funds and miscellaneous expenses incurred in the sale, the government made only about £6 million net.

The sale of the NFC to its employees has been a spectacular success. A company whose poor financial performance was felt to stand in the way of a sale has been transformed into a highly profitable enterprise. The first annual shareholders' meeting following privatization attracted considerable press attention. At the end of its first trading year it transpired that the company had made good profits. Shareholder-employees thus had the double satisfaction of seeing their investment pay dividends, and enjoying a considerable capital appreciation.

Their comments to the media were revealing. One summed it up by describing the new working conditions as a different world from that of employment by the state. Gone were the demarcation disputes, and in their place was a determination to get on with it and make a success. The NFC has continued to prosper, and is a major example of privatization by means of sale to the workforce. It provides a dramatic contrast with the highly-subsidized workers in the state sector.

Redhead

A second worker buy-out took place at the Redhead shipyard. In 1977, the government took over the main private shipyards and established British Shipbuilders as a state concern. Since that time, it has continually faced one problem after another, with losses reaching £109.7 million in 1979. Despite an improvement in productivity of 15% between 1981 and 1982, and a reduction in the workforce from 86,700 when nationalized in 1977 to around 60,000 by 1982, it continued to make losses.

The British Shipbuilders Bill, first introduced in late 1982, was intended not to be a direct privatization attempt, but more of an enabling measure giving the Secretary of State the necessary powers to direct the corporation to dispose of assets by forming and then selling subsidiary companies. British Shipbuilders comprised no less than nineteen shipbuilding companies, five companies involved in the manufacture of slow-speed diesel marine engines, and three training companies.

The Minister of State for Industry, Mr Norman Lamont, was obviously thinking of something like the Redhead shipyard when he said in 1983 that he was looking for 'an opportunity to allow a breath of private capital' and enterprise into the state-owned industry. The Redhead ship repair yard at South Shields was closed by British Shipbuilders in October 1982, whereupon some eighty of the workers came together, pooling £110,000 of their redundancy payments, and bid for the yard. Within the state sector there were fears that the new operation might siphon work away from them. An impossible price of £300,000 was set, but this was reduced after the 1983 election, and the deal was closed.

The workers' group is paying off the cost over eight years at four per cent above bank rate, and have the option to buy out at any time without further interest. The private yard opened in October 1983, with twenty-two of the eighty shareholders at work, seeking the orders that could put the rest of them to work. By January 1984, 110 men were at work, with the expectation of the total soon rising to 150.

As with the National Freight Corporation, the notorious inter-union disputes have vanished; and the new firm's brochure advertises a 'guarantee of no strikes, no overtime bans, no demarcation disputes, sensible flexibility, and minimum lost time'.

The Redhead move is not yet a success story, but is well on the way to becoming one as the orders come in. It illustrates the value of the technique for even the most depressed and difficult industry. In a field of chronic labour disputes, it is revealing to hear the words of one of its founders, shop-floor director Jim Todd: 'It's a long time since I've heard singing and laughing in a shipyard'.

Victualic

The plastics firm Victualic provided a case of another successful buyout. In early 1983, British Steel sold Victualic, a firm making plastic pipes and joints and rubber gaskets and seals, to its workforce. Out of a total of 885 workers, 634 put up a total of £838,000 for a forty per cent share in the company - British Steel retains thirty per cent with Barclays Bank and various holding the balance. The average holding is £400 per worker, but some spent as much as £5,000 on buying a share in their company.

The exercise appears to be succeeding beyond anyone's dreams. In fact, each share bought for £1 just over a year before is now valued (according to a recent report) at £1.98, meaning that each worker who bought shares has effectively doubled his money in the space of twelve months.

METHOD FIVE: GIVING TO THE PUBLIC

There may be elements of the public sector where a sale is inappropriate, but where an outright gift can be made. For firms which have experienced large losses over the years, it would be more accurate to talk of disposing of public liabilities than of handing out state assets. Since the public sector is already technically in 'public ownership', the only difference made by a gift to the general public is that people receive an assigned and specific share instead of having a notional claim on the whole. But this makes a big difference, because once their share is identified it becomes alienable, meaning it can be sold or otherwise disposed of.

It may be feasible, for certain public operations, to distribute to the general public the shares which they already own notionally. In some cases, those who worked in the industry might be given additional shares, but the expectation in either case would be that shareholders would be represented eventually by a management group with plans for turning a profit through reorganization. After a period of time, one would expect to see a company operating as part of the private sector, albeit with a very diversified ownership.

This is similar in many respects to the method used to dispose of the Volkswagen company after the second world war. Its obvious advantage is that it ends public liability, while restoring the operation to the private sector. In cases where everyone receives their piece of the company, the acquiescence of the general public is gained. Workers in the company might face an increased risk to their jobs, so it may be advisable to grant them additional shares to put them high on the list of the direct beneficiaries from any improvement in productivity.

In cases where specific individuals receive benefits from a costly public sector activity the beneficiary group can be counted on to oppose the distribution of the 'assets' if a loss

of their benefit results. It might be appropriate in such cases to make the beneficiary group the recipients of the gift, to counter the loss which would otherwise be incurred.

There is still no clear-cut example of the British government actually giving away to the general public a 'publicly' owned asset in its entirety. There are numerous examples of some shares being given to workforces or the public who buy shares in a firm - usually on a one-to-one basis with the purchaser getting a certain number of free shares on the condition that he buys some of his own.

One minor example of a gift to the public is worthy of note because it represents a break from the more conventional privatization methods. It concerns the sale of British Telecom. Because of the size of the sale - most estimates suggest a value of £4 billion - there was a fear that it would swamp the market and not achieve its 'true' value. So, in order to encourage far wider share ownership and overcome the problems that might occur with such a large sale, the government chose to go ahead with a voucher incentive scheme whereby those buying BT shares received a discount on their telephone bill. This took the form of giving individual investors vouchers of a fixed amount which can be offset against their quarterly telephone bills over a limited period ahead. The number and value of the vouchers received by an investor was related to the amount invested at the time of flotation and held over the period, subject to a maximum.

Cases of whole industries being given to the public have not occurred yet, although this has been suggested by many Conservative thinkers, and by Dr David Owen, leader of the Social Democratic Party.

METHOD SIX: GIVING TO THE WORKFORCE

There may be areas of state supply suitable for transformation into worker co-operatives by an outright gift to the employees, together with the writing off of any capital debt. This treatment is suggested for operations in which a history of public subsidy points to the need for major reorganization, and the possibility of sale to the workforce is unlikely.

There are undoubtedly some areas of the public sector where the industrial power of the workforce and the history of labour relations are sufficiently discouraging to outweigh the value of capital, land, stock, equipment and other assets. To anyone except the workforce, the operation might have a negative value and pose the prospect of a continual drain on future resources. For the workforce, however, the prospect might be viewed quite differently, as an opportunity to restructure and make the business a success. Working for themselves in a co-operative might lead them to change their attitudes and work habits more than any management from outside could. The workers' own leaders might be quite different if they were elected on some basis other

than their ability to drive tough bargains with government. As with several of the other methods of dealing with public sector problems, this one takes advantage of the propensity of workers to do better when they work for themselves than when they work for others.

In practice, such a form of transfer could take place only with the full agreement of the workforce. The employees might well prefer the prospect of remaining public employees, confident of their power to exact continuous subsidies and to achieve better rewards for themselves at the expense of the rest of society. Only if there were serious prospects of that state of affairs not continuing would there be any incentive for serious consideration of a workers' co-operative. Part of the price which government might have to pay is the continuation of certain subsidies which are withdrawn on a gradual basis over several years as the new co-operative grows. By continuing subsidies on a short-term basis, government might find itself with a solution to even the most intractable loss-making areas of the public sector.

There is obviously a limited number of cases in which this method of privatization is appropriate. One factor to be considered would be the possibility of placing an essential service entirely in the hands of a militant union (insofar as it is not already in such hands). Another would be the desire to avoid substituting a private monopoly for a public one.

Hovercraft services

There is a case history in Britain of a public sector enterprise being given over to its workforce. This was done with the English Channel hovercraft ferry service, formerly owned by British Rail in association with a Swedish firm, as a result of a previous merger.

In mid-February 1984, British Rail sold its 50% share interest in Hoverspeed for a nominal sum of £1 to a staff consortium, with the co-owners doing likewise. Thus, Hoverspeed was given away to its management and workforce, and is now wholly owned within the private sector.

METHOD SEVEN: CHARGING FOR THE SERVICE

Charging prices for public services is a variety of partial privatization. Just as the production of goods and services may be in the public or in the private sector, the *finance* of production also may be in either sector. Charging prices for public services involves taking the finance into the private sector, while leaving the production in the public sector.

The reasoning behind this tactic is that a system of direct pricing can bring some economic disciplines to bear where there were none before. For goods or services which are 'free' - that

is, financed out of general taxation - the demand is potentially infinite. It is in everyone's interest to consume individually as much as possible of goods which are paid for collectively. In practice, this involves considerable economic dislocation, with all kinds of services hopelessly oversubscribed and rationed either by waiting lists or by political influence.

The switch to finance through consumer charges immediately inhibits frivolous demand, and directs funds to those areas where real value for consumers is demonstrated. It tends to limit over-production and over-supply, and to act as a restraining influence on costs.

There are some operational difficulties to taking the finance of public services into the private sector by means of charging for services. While some areas, notably the public utilities in Britain, have long featured direct charges, there has always been public resistance to price increases, and such increases have always been politically sensitive. Where charges have not been traditional, there is considerable resentment to their imposition by recipients of the 'free' service. These recipients enjoy a good deal of media sympathy, accompanied by graphic portrayal of real or apparent hardship caused by the charging of prices.

Where successfully introduced, the practice of charging prices puts pressure on legislators to support uneconomically low prices, and to maintain artificially low prices by means of subsidies. The general taxpayers are insufficiently organized or visible to counter these pressures. Every year, legislators risk unpopularity if they keep the charges at a level which reflects true costs. Therefore, charging prices cannot be part of a permanent movement from public to private sector, but it is certainly better than having both production and finance in the public domain. Its best use is perhaps in limited areas as a step toward a fuller transfer and as a means of bringing in the economic disciplines which will make complete privatization possible later.

Examples

Charges for some of Britain's National Health services provide case histories. Charges for spectacles, dentistry, and prescriptions serve to illustrate its application.

Prescription charges were introduced at a rate of 1/- (5p) per prescription form in 1952. By 1956 the charge was 1/- per item and in 1961 it had risen to 2/-. They were abolished in 1965 but reintroduced in 1968 at a rate of 2/6 (12.5p) subject to a number of exemptions. The current charge is £1.40 per item, so a single prescription with two different drugs will cost twice as much.

The charge represents only a small fraction of the cost of many prescriptions, and political pressures have led to some groups

being exempted in an attempt to prevent hardship. There are many exemptions, but the main groups are: men and women beyond retirement age; children under 16; pregnant women and those who gave birth within 12 months; people receiving family income supplement or supplementary benefit; and those suffering from certain medical disorders.

Dental and optical charges were first introduced in 1951, and currently there is a maximum charge for routine dental treatment of £13.50, while the most that can be charged for all forms of treatment is £95. For spectacles the maximum charge is £30, though most are less than this. All check-ups are free. At the moment there are no charges for: the examination of teeth; the arrest of bleeding; repairs to dentures; and essential home visits.

The government attempted to introduce a £2.00 fee for eye tests but dropped the idea.

The exemption groups are the same as for prescription charges. Government policy is to make charges increase in line with costs.

METHOD EIGHT: CONTRACTING OUT THE SERVICE TO PRIVATE BUSINESS

A further method of partial privatization involves keeping the finance in the public sector, but moving production over to the private economy. Instead of using in-house direct labour to produce goods and services, independent businesses are paid from public funds to perform the task. Successful changeover to contract services involves inviting competitive tenders from companies seeking the work.

This method involves a recognition that government can still be responsible for guaranteeing a supply, even when it does not produce that supply itself. The immediate advantage to government and taxpayers is the saving, normally in the 20%-40% range. The public usually gains an improved, more up-to-date service. The workforce is usually reduced, because private firms use labour more efficiently.

Resistance by unions and employees is weakened by the fact that private businesses often give workers better opportunities and incentives. In Britain, private pension benefits tend to be lower than price-indexed government pensions, but basic pay, bonuses and other fringe benefits are often as good as or better than their state counterparts. The unions, which stand to lose public sector powers of leverage, are the main groups opposed to the use of contractors. In Britain they have spent millions, unsuccessfully, in an attempt to curtail contracting out.

An intelligent use of private business under contract normally will specify that the successful bidder give preferential treatment to existing employees before taking on new labour. It will involve pre-selection of bidders, so that only businesses known

to be reputable and stable will be involved in the performance of essential work. It will involve penalty clauses for non-delivery of service, often with bonds being lodged to guarantee payment. Every effort needs to be made to placate possible sources of anxiety as to whether private business will be sufficiently reliable. The above measures, together with careful specification of tasks in the contract, will allay such worries.

The general advantages are enormous. With production in the private sector, economic disciplines are re-introduced. An entire history of restrictive practices and union-controlled services is wiped out overnight and replaced by a competitive climate. Attempting to win the contract, and to retain it when it is renewed, keeps firms competitive in price and quality. Costs go down because men and machinery are used efficiently.

If it chooses, government can seek to cover some of the costs of terminating the service by selling capital equipment to the new private supplier. In this way the initial costs of lay-off pay to discharge employees can be covered.

The use of private contractors on a growing scale to perform local government services in Britain, provides a whole range of case histories. It has been an astonishing success, and continues to gain momentum.

Local government services

Even though the private sector handles 98% of all hazardous waste disposal in Britain, it is surprising that no major local refuse service was put out for bid until 1980. In that year, Southend-on-Sea invited tenders for the provision of refuse collection, street sweeping, and lavatory maintenance, and of the six bids submitted, the winning offer by Exclusive Cleansing and Exclusive Cleaning led to a total saving of £492,000.

The overwhelming success of this venture led to a trickle of local authorities following Southend's example. This trickle turned into a flood as the cost-saving and improved service became more apparent. The flood has now turned into a torrent with hardly a day going by without the report of one more local authority privatizing another part of its services.

Statistical information has tended to underestimate significantly the number of local authorities who contract out their services, since few records are kept centrally. Nevertheless, information provided through surveys by independent organizations indicates how explosive the growth has been.

In Summer 1984, *Public Service Review* provided a list of thirty-one different authorities who had privatized a service. By December 1983 this had increased to forty-six authorities and rose to fifty-five by March 1984. Not only is this figure expected to continue to rise, but the phenomenon of councils

contracting out more than one service, once they see the advantages it brings, is also expected to continue its increase.

The government has also introduced and extended certain measures of compulsory bidding, mostly for local authority construction and maintenance work. Under amended competition regulations approved on 30 March 1982, 30% (by value) of maintenance works less than £10,000 per job have to be put out to competition if the total annual value of such work exceeds £300,000. In addition to this, the threshold for competition for highway works was lowered from £100,000 to only £50,000.

Presently, all maintenance work above £10,000 per job, and 30% of the work below that figure, has to be put out to bid. In addition, any new building work above £50,000 per job plus one third below it has to be put out for bid. There are motions in the pipeline to introduce a compulsion to bid for 60% of the new building work below the £50,000 threshold, though a decision has yet to be made. These reforms have enabled private contractors to carry out more than half the local authority work on highways, construction, and general maintenance. Direct labour organizations carry out 61.2% of general maintenance, 53% of highway work, and between 16% and 24.4% in construction.

Such a huge range of services have been successfully privatized, that each week now sees the privatization of yet more services somewhere by more local authorities. So far the policy has been an enormous success with immense savings to ratepayers already recorded nationwide.

Table 2
Local government services contracted out to private industry

Local authority	Operation	Annual savings
Bath City	public lavatory & street cleaning & refuse collection	£300,000
	catering in council & sports halls	£63,000
Birmingham City	school cleaning	£670,000
Boothferry BC	pest control	£14,390
Bromley BC	street cleaning	£200,000
Broxbourne BC	public convenience cleaning	£11,000
Cambridgeshire CC	school cleaning	£700,000
Chiltern DC	refuse collection	£160,000
Christchurch DC	public convenience cleaning	£16,000
Croydon DC	public convenience cleaning	£70,000
	pest control	£20,000
Dover DC	public convenience cleaning	*
Dudley BC	school cleaning	£600,000
	further education college cleaning	£130,000

Ealing BC	street cleaning	£600,000
	school meals	£695,000
East Staffs DC	meals on wheels	
Eastbourne BC	electrical contractors	£3,000
	street cleaning	£500,000
Edinburgh DC	refuse collection	
Epping Forest DC	architectural services	*
	pest control	£2,000
	delivery/collection of polling equipment	£365
	vending service	£7,000
Fareham BC	public convenience cleaning	£22,000
Gedling BC	office cleaning	£12,000
Gillingham BC	public convenience cleaning	£36,500
Gloucester DC	horticultural produce	£24,000
Gt Yarmouth BC	office cleaning	£6,114
Humberside CC	meals on wheels	£43,000
The Royal Borough of Kensington & Chelsea	refuse collection	£100,000
Kent CC	school cleaning	£1,100,000
Kingston BC	grass cutting	£46,000
Lewes DC	public convenience cleaning	£7,000
Lothian RC	car parks leased	£220,000
Maldon BC	street cleaning	£1,180
Mendip BC	refuse collection	£126,000
Merton BC	school meals	£833,270
	school cleaning	£250,000
	refuse and waste paper collection	£750,000
Milton Keynes BC	refuse collection	£488,000
North Norfolk DC	refuse collection	£175,000
Penwith DC	public convenience cleaning	£30,000
St Albans DC	public convenience cleaning	£20,000
St Edmundsbury BC	golf course leased	£15,000
Salisbury DC	pest control	£12,000
	office cleaning	£28,000
Solihull BC	school cleaning	£108,000
South Bucks DC	pest control	£7,000
	office cleaning	£2,000
South Kesteven DC	public convenience & street cleaning and refuse collection	£320,000
South Lakeland DC	grass cutting	£1,500
South Oxfordshire DC	refuse collection	£200,000
Southend-on-Sea BC	street cleaning	£600,000
	refuse collection	
Surrey Heath DC	street cleaning	£12,000
Sutton BC	cleaning of libraries	£3,500
	laundry	£14,000
Tamworth DC	refuse collection	£200,000
Tandridge DC	refuse collection	£160,000
Taunton Dene BC	refuse collection	£42,700
Vale of White Horse DC	street cleaning & refuse collection	£290,000
Wandsworth BC	street cleaning	£670,000

	refuse collection	£1,130,000
	garden maintenance	£200,000
	housing repairs	£151,000
	vehicle maintenance	£297,800
	community centre cleaning	£120,000
Waverley DC	golf course leased	£2,000
City of Westminster	architectural services	£235,000
Wirral BC	street cleaning & refuse collection	£1,400,000
Wycombe DC	office cleaning	£3,455
Yeovil	office cleaning	£21,500

Notes: * Authority unwilling to give figures
 BC = Borough Council DC = District Council
 CC = County Council RC = Regional Council

Source: *Public Service Review*, No. 3, 1984.

Hospital ancillary services

The use of contractors in the National Health Service is not entirely new. The recent expansion in the numbers involved, especially for catering and cleaning in hospitals, is new.

In previous years, the use of contractors has been handicapped, not only because there was no obligation to go out to bid, but also because a health authority employing direct labour would not have to pay Value Added Tax (VAT). Conversely, if outside contractors were used, VAT had to be charged. Despite this, out of the ninety area health authorities in England in 1981-82, many contractors were good enough to overcome this tax burden, and still gain the contracts in twenty-four authorities to provide catering services, and in eighty-eight authorities to provide domestic cleaning services. The total value of these, including laundry was over £17 million.

The savings by taking private business bids to perform services can be both direct and indirect. On the one hand, if the private contractor is better and cheaper, then costs are lowered; on the other hand, even if the service is still retained 'in-house', then the mere threat of competition can produce savings. Any savings on a bill of almost £800 million per year can be re-allocated into additional patient care and medical equipment.

In a recent Department of Health circular, the government asked 'health authorities to test the cost of their support services in order to discover whether savings can be made and resources released for improved patient services' and it also tackled the tax problem: 'the government is making arrangements for this VAT to be refunded to health authorities from 1 September 1983'. But while it concentrated on domestic, catering and laundry services, the circular did encourage some contracting, and all in all, eighteen hospitals were revealed to have sought tenders.

Privatizing the services of health authorities does include certain examples less well known than those mentioned in the circular. For example, Southern Derbyshire Health Authority are considering estimated savings of £24,000 a year by closing down four oil-powered boilers and buying steam from a private contractor. Certain regional health authorities contract out their abortion services to private agencies. Private firms are being used in Somerset to take surgical waste to incineration, and many health authorities are either renting mobile operating theatres or are just sending patients to private hospitals, in a successful attempt to reduce waiting lists.

Meals in British schools

Most local authorities provide midday meals for British schoolchildren, and traditionally this has been done by employing their own labour. In view of the high cost of this, it is not really surprising that some education authorities have attempted to obtain the advantages of privatizing their school meals service. It was left to the London Borough of Merton to make the first move and as the local paper reported, 'it has proved popular with the children'. The service is now provided by Sutcliffe Catering Company (South) Ltd, who started preparing 6,500 meals a day from 5 September 1983. The general reception to the change was summed up by a local headmaster, Mr Hugh Streeter who said: 'We are delighted. The meals are presented on very colourful and attractive trays and the children love them.'

Innovation by private firms, such as the provision of vending machines at Hillcrest School in Dudley (W Midlands), is an obvious advantage that keeps the children happy, and at the same time saves money. But as with local authority contracting out, there are problems of calculating how extensive the privatization programme is. This is not made any easier by the fact it was only tried for the first time in September 1983. Nevertheless, indications are that the success of Merton is being duplicated elsewhere. East Sussex County Council recently announced that it is inviting tenders for the provision of meals in its 40 schools, and Hereford and Worcester set up an innovative workers' co-operative scheme.

Whatever the result, one thing is sure; the provision of school meals by private contractors is expanding.

Other examples of contracting out

(1) **Testing of trucks and public vehicles.** The 1982 Transport Act allowed for the annual testing of heavy goods vehicles and public service vehicles to be transferred to the private sector.

(2) **British Telecom - coin collection.** British Telecom has contracted out coin collection from public payphones to Pritchard Security Ltd for an undisclosed sum.

(3) **Pollution emergencies.** The Ministry of Defence and the Ministry of Transport have transferred the task of maintaining and storing emergency cargo transfer equipment to the private sector. Specialized equipment for dealing with pollution emergencies is now stored centrally and maintained by United Towing Ltd.

(4) **Government buildings and maintenance.** Of the many thousands of construction contracts and design commissions that the Property Services Agency handles each year, it has become policy that 'all new construction and over eighty per cent of maintenance work is carried out by private contractors. In 1982-83, forty-two per cent of project design was done by private consultants.

(5) **Grass cutting in Northern Ireland.** In 1981, the Northern Ireland Housing Executive contracted out the cutting of grass.

(6) **Health authorities - auditing.** By November 1983, nine firms of accountants held contracts to undertake audits of fourteen District Health Authorities previously audited by staff at the DHSS.

(7) **Road construction units - design.** By 1981, the road construction units (mainly designing roads and motorways) had handed over to private consultants virtually all their work, amounting to schemes worth approximately £2,000 million.

(8) **Civil service catering.** Mr Barney Hayhoe, the Civil Service Minister, announced in December 1983 that more than half of the 654 civil service restaurants and cafeterias have been operated by private contractors in recent years.

(9) **Ministry of Defence cleaning.** There are some 920 defence and armed forces units in Britain with a requirement for cleaning. Of these, 672 are currently cleaned by private contractors and a further 72 have agreed contracts.

(10) **Southern Electricity Board - cash security.** Pritchard Securities won the offer from Britain's Southern Electricity Board for what is says is its biggest cash-handling security service. The exact value has yet to be disclosed but the work covers the collection of cash and cheques, and wage distribution for the Board's 120 shops and offices from Yeovil and Cirencester to Bognor Regis and the Isle of Wight.

(11) **British Steel - contract labour.** Initial Services has been supplying British Steel with contract labour for twenty years, including a new ingot dressing service where the Initial men burn the impurities off the steel which is produced.

(12) **Central Office of Information - film unit.** From 1st April 1982, the work of the Central Office of Information film unit was transferred to private film-makers.

(13) **National Bus Company.** The National Bus Company has contracted out catering, building repairs and cleaning, maintaining of tyres, and cash security services. The hire of other operators' vehicles to enable the company to meet peak commitments amounted to 5.6 million miles of operations in 1982.

(14) **Government departments.** All government departments in Britain use private firms in one way or another. The most common form of contracting out appears to be to private security firms to safeguard buildings and the transportation of valuable or potentially dangerous items. However, other examples include cleaning, training, catering, construction work, maintenance, architectural work, surveying, and even the deck chair service in royal parks.

(15) **Post Office - parcel mail.** The Post Office invited tenders for the carriage of parcel mail to Paris for a period of one year commencing during the summer of 1984.

(16) **British Rail - miscellaneous experiments.** There are a total of seventy private franchises operating in stations, and while there is delay in privatizing some on-train catering, experiments with private companies on minor train services has begun.

(17) **Servicing of ships and aircraft.** The Ministry of Defence is currently proceeding with the handing over of the major servicing of Royal Navy ships and Royal Air Force front-line aircraft to private contractors.

(18) **Army laundering.** With the exception of those sections of the army facilities in the British Army on the Rhine and the Falklands, all laundering for the Army is contracted out. The total contract is worth approximately £3.5 million a year.

(19) **Prison services.** Most of the work concerned with the design and construction of prisons is performed privately, as well as the domestic catering and night security services at two staff training establishments.

(20) **Arms trials overseas.** The Ministry of Defence is currently organizing the contracting out of support activities for overseas trials undertaken by the Aeroplane and Armament Experimental Establishments.

METHOD NINE: DILUTING THE PUBLIC SECTOR

For parts of the public sector where there is no possibility of moving existing operations towards the private sector, it may be possible to have maintenance and expansions done privately. The effect of this is to lower the proportion represented by the public sector without touching the existing network.

Chronic capital shortage is a standing weakness of the public

economy. At all times, but especially in an economic recession, extension of a network of services presents a problem. One solution is to find ways of bringing in private enterprise to the task. The injection of private capital into the work of restoration and expansion of the public network can take the pressure off the public purse, bringing the much needed improvement in service without further burdens on the taxpayer.

Private capital always seeks a positive return, and intricate devices are sometimes required to establish genuine risk-capital ventures in the public sector. If private firms put up the money and perform the work for a guaranteed return from government, this is simply public sector borrowing by another name, and fails to take the pressure off public spending. What is required is a means of allowing private entrepreneurs to take risks based on the anticipated use of the new or rebuilt parts of the network.

When risk is built into the system, two important results emerge. The first is that the private funding is then not regarded as public sector borrowing, but private investment. The other result is that only those parts of the public network which are most certain of a demand will be renewed or extended. The introduction of risk, in other words, serves to direct private funds to where the need is greatest. Whether the public network involves roads, water facilities, or other types of public systems, the private capital to develop or renew public facilities has to seek its returns through customer usage. In this way, the money will be attracted to where entrepreneurs think it will most likely serve an unsatisfied need.

The attraction for legislators of bringing private capital to the aid of a traditionally public network is that it enables work to be done with a minimum of public outlay. It is often noted how infrastructures suffer when there is a squeeze on public money. With this type of approach, however, an infrastructure can be maintained and extended without massive outlays of public funding. The repayment is made over the years according to use.

Private building, engineering, and contracting firms are natural allies of government in the introduction of such schemes. The employees of these companies welcome the extra jobs which the work brings, and the public gains the benefit of the new or improved service. As the attractions of using this method spread, more and more renovation and extension projects will be done in the private sector. The size of the public sector thus will diminish without direct cuts in public funds or jobs. The effect is to dilute the proportion of a service which is done in the public sector.

Private road funding

Britain has recently developed road construction schemes which use private capital on a risk basis. Privately-funded road projects give an example of how the performance of essential new

work by the private sector, without altering the status of the existing network, can dilute the public holding.

When appointed by the British Government to investigate potential road construction employing private capital, Charterhouse Japhet suggested the 'Black Country route' near Wolverhampton.

The plan has been top priority on the County Council (West Midlands) structure plan for some years, with the intention that an access road to the industrial area (mostly an eleven-mile area west and north-west of Birmingham) would help unemployment which averaged 19%, but went as high as 30% in certain areas.

A consortium of National Westminster Bank plc, Tarmac Construction Ltd and Saturn Management Ltd, (known as TNS) became involved during Easter 1983. The Federation of Civil Engineering Contractors became interested and eventually started lobbying for the scheme. 'The basis of the proposals is that TNS will provide a road to the design and specification of West Midlands County Council who will make payments based on actual traffic flows and actual commercial and industrial space developed within a specified area. These payments will commence when the road is open to traffic and cease twenty-five years later,' said the West Midlands submission to the Transport Department.

It was the prospect of the road being privately funded that offered hope for the project to proceed in a fast, flexible, and efficient manner. When coupled with the competitive tendering procedures adopted for actual construction work, this could mean that the road might be completed in five years. State funding, the Council estimate, would make it unlikely for the road to be finished in less than ten or twelve years. The reason for this is that the funding for the project will be divided into two stages: interim funding for the construction period and long-term funding for the operating period. By having private funding, total finance would be in place before construction starts, while state funding would be on a yearly basis according to use.

The Department of Transport rejected the first proposal put before it, after long consideration, on economic grounds. Meanwhile, the West Midlands County Council is going ahead using state funds in the shape of the Transport Supplementary Grant to start construction. Other privately-funded plans are under consideration.

Development of council estates

With local authorities having to reconsider expenditure commitments over the last few years, privatization has become a high priority. The year 1983 saw the introduction of the private development of public housing estates in Britain. In Priesthill, one of Glasgow's problem areas of low-quality housing, Barratt (the housebuilding firm) is taking over 190 council houses. It

will then upgrade and sell them. In the case of Priesthill, they will be on offer for £18,000 for a two-bedroomed apartment. Other councils, such as in Liverpool, where the Stockbridge Village Scheme on Merseyside has been successful, are taking on board the idea.

It appears to have greatest appeal in those areas where there are large numbers of poor-quality council houses, and the authority concerned has little or no money available to carry out the necessary improvements. The net result is that councils can improve the quality of housing within their area at no extra cost. The much needed repair of housing goes ahead, and the tenants even get the opportunity to buy the house after redevelopment.

Other areas known to be considering the idea include: Tower Hamlets in London, who are looking at the possibility of this form of privatization for the Teviot Estate in Poplar; Kilmarnock and Loudon District Council, which is considering using Barratt in the Ardbeg Crescent Area; and at Craigshill, where Barratt hope to buy 72 apartments for refurbishment from the Livingston Development Corporation.

National Bus Company

The National Bus Company welcomed the possibility of involving private capital in improving facilities. As a result, the NBC set up National Bus Properties Ltd. They also became involved in joint ventures with the private sector in express and coach holiday business.

British Steel Corporation

British Steel has been involved in the 'Phoenix' companies. The first of these was Phoenix I, set up by British Steel with the private firm of GKN in February 1981. It traded independently under the name Allied Steel and Wire Ltd. Phoenix II was to have been a subsequent joint operation between BSC and the private sector, this time in the engineering steels sector, but remains stalled in negotiations.

High-tech industrial parks

These are attempts to bring together state-run universities and private industry on a common location - usually involving well laid-out industrial areas, sited near universities or polytechnics - to develop formal and informal links between private business and the state higher education establishment. The first park opened at Cambridge in 1970, but since 1979, a total of ten parks have been established, two are awaiting the date to be announced for their establishment, and a further eighteen sites are being considered.

METHOD TEN: BUYING OUT EXISTING INTEREST GROUPS

When existing special interests have the power to thwart a move to the private sector, it may be possible to use a technique which alters the pattern for the future, even while continuing to benefit the present beneficiaries. In this way the service can be phased into the private sector over a period of years, and without threat to existing interests.

For example, proposals to abolish rent control and restore a private market in rented property seem unable to make headway in the face of opposition from those who live in artificially low-priced housing and their supporters. Proposals to end rent controls for new properties and new leases, however, will not face the same level of opposition because they allow existing tenants to continue to enjoy their subsidies. Such proposals in a sense 'buy out' the present generation in order to phase in a new system.

There are parts of the public sector in which long-term commitments have been entered into, and in benefits have long been enjoyed. In some of these areas the beneficiary group forms an identifiable and politically active group, ready to defend its privilege. Clearly there is a case for continuing to honour existing commitments, while shutting off the route whereby new beneficiaries can enter the system. The present generation has its opposition allayed by the continuation of its benefits. Yet this group forms a diminishing band if their numbers are not renewed.

This method sets in motion a chain of events whose process gradually but inexorably diminishes the publicly-controlled supply, and gradually enhances the proportion covered by the private market. It culminates in the extinction of yet another seemingly intractable part of the public sector.

The Thatcher government's introduction of new shorthold tenancies and assured tenancies serves as an example of the technique of withdrawing public sector participation for newcomers into a system, while allowing those already within the system to continue in the benefits they receive from it.

Shorthold tenancies

The 'protected shorthold tenancy' is a form of renting between private landlords and their tenants. It is designed to deal with some of the problems generated by rent control. Brought into effect on 28 November 1980 under the 1980 Housing Act, the main feature of the shorthold lease is that it allows landlords to rent property for a period between one and five years, while retaining the right of repossession at the end of the tenancy. There are certain safeguards for tenants, and other requirements, before a letting can qualify as a shorthold:

- (a) the lease must be to a new tenant;
- (b) tenants have security of tenure during the period of the tenancy;
- (c) the landlord must give due notice both to prospective tenants when a shorthold is being offered, and to the sitting tenant of his intention to repossess the property; and
- (d) for all shortholds outside Greater London before 1 December 1981 and for all shortholds in the Greater London area after 28 November, the dwelling must be registered for a fair rent with a Rent Officer.

Assured tenancies

The same Act created the 'assured tenancy' scheme. This permits bodies approved by the Secretary of State to let recently-built homes in England and Wales, without coming within the provision of the Rent Acts. In many ways, it is similar to the shorthold tenancy scheme, such that the landlord has to give notice of the end of the tenancy, unless the tenant breaks one of the conditions of the tenancy. A significant difference is that the assured tenant can apply to the county council for a new tenancy, whereas no such right exists with a shorthold. To qualify, the landlord must be an approved body, construction of the building must have started on or after 8 August 1980 (even extensively altered property since that day cannot qualify), and if previously rented, it must only have been an assured tenancy. Therefore, the scheme is for newly-built properties, and by exempting them from the Rent Act, allows the establishment of a freely negotiated market rent.

On 28 November 1983, a government spokesman announced that there were 121 bodies approved under the assured tenancy scheme, representing a 300% increase since November 1982. Estimates of the number of homes they intended to provide are in the process of being re-assessed upwards, as the number of approved bodies has since risen significantly.

METHOD ELEVEN: SETTING UP COUNTER GROUPS

Many of the ways which make it possible to have state-provided goods and services transferred to the private economy involve assuring interest groups that they will not lose in the process. Their potential opposition is neutralized if they stand to gain from the move. However, it is not always possible to ensure that every single interest group will benefit. Indeed, there are some groups enjoying power and privilege at public expense. If the general public is to benefit, it is sometimes necessary to transfer the powers and privileges from the few, and distribute them to the many.

The task of scaling back the public economy, therefore, sometimes involves a careful balancing of interests to ensure that there are more who gain from the process than lose by it. One type of proposal involves the creation of new groups of vested interests to counter-balance those whose benefits are linked to public sector supply. If the bureaucrats who administered a public programme are to lose their power and status, for example, it is important that a new class of private managers see their own future tied up in the new order of things. The new people act as a counter-group to outweigh the old. Those who once administered public operations and enjoyed the power of controlling state assets are balanced by a new group of owners in the private sector. The new owners will not willingly surrender their acquisition, and will form a group whose interests are tied to the new reality. Similarly, individuals who enjoy the choice and variety which private sector operation often brings the consumer will not willingly forego the new freedom in order to return to the take-it-or-leave-it approach of state monopoly supply. They thus form an effective group whose interest is clearly aligned with the continued success of private supply.

There are specific cases in which the forces keeping an activity within the state sector can gradually be countered by the creation of a new interest group which recognizes its own gain from going private. In such cases, the element of gradualism becomes important. An overnight change would not allow time for the new group to perceive and appreciate benefits that are only potential future gains. Actual experience of the private sector and its benefits creates a self-conscious group aware of its gains and prepared to oppose their elimination.

The creation of counter-groups normally takes time, and is more appropriate to cases where privatization can be introduced gradually. The success of privatization spreads and secures the allegiance of beneficiaries until there are enough enjoying its benefits to outweigh those who object to the systematic diminution of the state's role.

Counter-groups were created in Britain by the sale of state housing to existing tenants, and the new property-owners have proved to be a powerful group in support of the new reality.

Council house sales

The disposal of public housing in Britain into private hands provides a case history of establishing a counter-group. The houses were offered for sale to the current tenants at discounts of up to fifty per cent.

More public sector housing in Britain (a total of 589,000 units) transferred to the private sector between 1979 and 1983 than in the whole of the period since 1945. Central to this has been the introduction of the 'right to buy'. This came as a result of the 1980 Housing Act and the Tenants Rights (Scotland)

Act 1980, which gave tenants of local authorities, new towns, and non-charitable housing associations the right to buy the home they live in, the right to a mortgage, and the right to a discount off the open market value of the home, between a minimum of 33% rising to a maximum of 50%, contingent on the time spent as a tenant.

A recent survey by the Nationwide Building Society indicated that the typical former council tenant who buys his own home is significantly older than other buyers and more likely to live in Scotland, Northern Ireland, or the North of England. More important, though, is that the survey shows that he is also relatively poorer than other house-buyers. However, if a tenant is unable to afford to buy outright then by paying £100 he can have the option (for two years) to buy at the price at which the home was originally valued. If the tenant buys in that time, then the £100 goes towards the price of the house; otherwise it is refunded in full. For those who are unable to buy at the full value of the house, there is the option for shared ownership. A tenant can buy a long lease of a house or flat for only a proportion of the dwelling's value (for example 25%, 50%, or 75%) and that becomes the proportion which the tenant then owns. The rest is owned by the landlord, e.g., the local authority, and on that part the tenant still pays rent.

Table 3
Right to buy: progress of applications: 1980 to 1 July 1983

Requests received	860,600
Acceptances issued	804,400
Sales completed	526,380

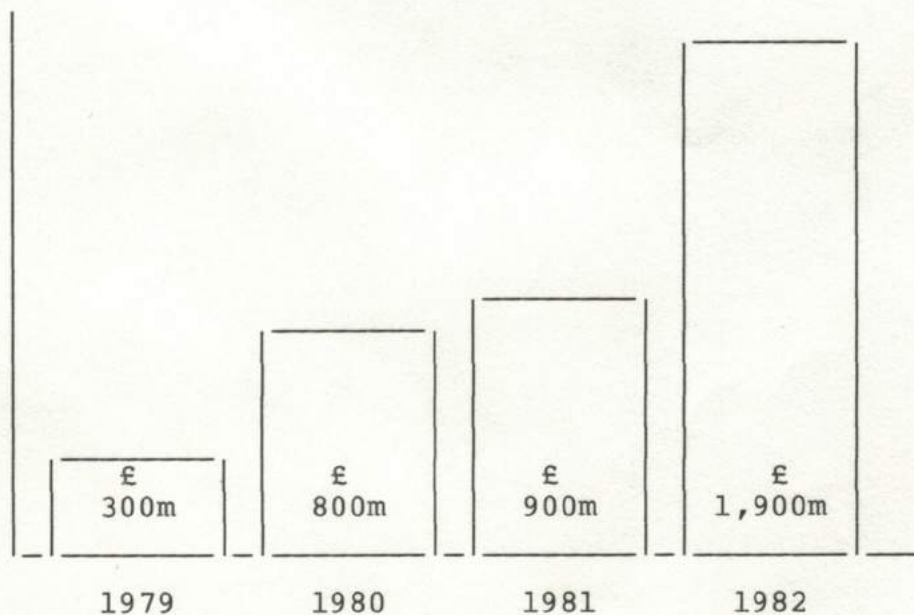
Shared ownership is aimed at those whose income is not big enough to qualify for a large enough mortgage. It allows the home owner to part own and part rent his home. Some local authorities will offer discounts, but this is at their discretion, and it is not uncommon for shares to be worked out on the 'sale price of the house'. The shared ownership scheme had £40 million allocated to it in April 1983, through the Housing Corporation, and it has proved to be a runaway success with almost 2,700 buyers being granted help, with thousands more inquiring. Unfortunately, the funding ran out after only three months, owing to the success of the scheme, and unless more funding is given the Housing Corporation say that there will be no shared ownership scheme next year.

Initially there was considerable opposition from many Labour councils toward council house sales but this has largely died down since the local authority in Norwich was taken to court in 1981.

The Housing and Building Control Act 1984 extends the right to buy. Its main purpose is:

- (a) to extend the right to buy to allow tenants to buy long leases (up to 125 years) where their landlords do not own the freehold. (At the moment the sale can only take place if the landlord owns the freehold of the dwelling, and in some areas leaseholds are more common);
- (b) to increase the maximum discount available from 50% for tenants of twenty or more years tenancy, to 60% for tenants of thirty or more years tenancy;
- (c) to increase the Secretary of State's powers to assist tenants experiencing difficulties in exercising their right to buy; and
- (d) to introduce the 'right to repair' for council tenants, under which they can have certain repairs performed privately and charge the local authority.

Table 4
Receipts from council house sales



Source: Lords Hansard, V.446 c.916.