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**MICHIGAN**

# Privatization

A Publication on Privatization Initiatives

Volume 10, Number 1 / Fall 2005

**REPORT**

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- Survey: School Outsourcing Grows • Privatization Update: Hamtramck
- Competitive Sourcing on an Individual Basis • Privatizing Libraries
- State Park Privatization and more!

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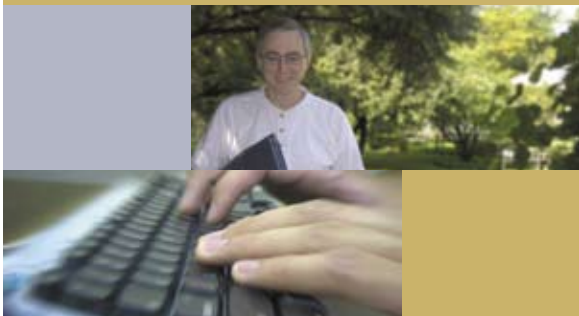
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## Privatization REPORT

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# Privatization

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**MICHIGAN**

## REPORT

### FEATURES

4

#### Survey:

#### School Outsourcing Grows

School districts face the same cost pressures as companies in the private sector in trying to deliver a quality product at the best price. Michigan schools are contracting out more ancillary work than ever before, according to the Mackinac Center for Public Policy's 3rd biennial school privatization survey.

5

#### Competitive Sourcing on an Individual Basis

Outsourcing is a fact of life in public schools. Big contracts with private,



for-profit vendors in areas such as food service often get the most attention, but districts are starting to increase their focus and contract out for individual positions.

7

#### Hamtramck Update: Will City Thrive Without Emergency Financial Manager?

Seasoned business executive Louis Schimmel recounts his experience as Emergency Financial Manager for the city of Hamtramck.

8

#### Booking Privatization: Why Not Privatize Government Libraries?

Public libraries are fixtures in many communities across the state, yet



many are struggling recently to fund their operations. Officials at both the state and local level may wish to consider some private alternatives to strictly government libraries.

9

#### State Parks Privatization

The State Park System today has expanded into something quite different than what lawmakers envisioned when the system was created in the early part of the 20th century. Generating revenue was never the original purpose, and the State Park System will ultimately be stronger if it is comprised of only parks that represent the most important natural and historic treasures of our state.

10

#### Privatization Means Significant Savings

Jeff Siegel, superintendent of the Berrien County Intermediate School District, made the case in April for competitive contracting in the St. Joseph Herald Palladium.

12

#### Governing by Network: The New Shape of the Public Sector

A book review of "Governing by Network: The New Shape of the Public Sector" by Stephen Goldsmith and William D. Eggers.

16

#### 'End of the Line' for Amtrak Subsidies? Think Again

Despite promised reforms, Amtrak has never turned a profit in more



than three decades of operation. Since 1997, Amtrak has absorbed more than \$6.5 billion in government subsidies. Privatizing the service could mean better service and additional revenue for the government.

### DEPARTMENTS

13

#### AROUND THE STATE

An update of privatization initiatives, opportunities and controversies from around the Great Lakes State.



#### ADVERTISERS:

Earth Tech Operation Services	2
MichiganVotes.org	2
Educlean Services	6



# Features

## Survey: School Outsourcing Grows

by Michael D. LaFaive  
and Daniel J. Smith

School districts face the same cost pressures as companies in the private sector in trying to deliver a quality product at the best price. One method used by firms in both the public and private sectors to achieve greater efficiency is the outsourcing of ancillary business operations. Michigan schools are contracting out more nonessential work than ever before, according to the Mackinac Center for Public Policy's 3rd biennial school privatization survey.

This year the Mackinac Center successfully interviewed a representative from every one of Michigan's 552 school districts to determine how many of them use outside vendors for three primary noninstructional services: food, janitorial and busing. The number of districts that contract out rose from 34.0 percent in 2003 to 35.5 percent currently. Today, 196 of the state's school districts outsource at least one of these three functions.

By far the most popular area of school privatization is in food services: 156 Michigan school districts (over 28 percent) contract out with a private company for some type of food service delivery. While janitorial outsourcing occurs much less frequently than in the food services arena, there is a growing interest in it. Janitorial services are now outsourced in 8.7 percent of districts, up from 6.6 percent just two years ago.

The survey also asked respondents about whether outside vendors had saved the district money, if the district was satisfied with its contracting experience, and what barriers (if any) existed to thwart privatization. Almost 80 percent of the districts reported savings through privatization, though some had difficulty quantifying precisely how much had been saved.

Only eight districts reported no savings, but this number should be interpreted carefully. Over the years some districts have reported to us that they didn't care about saving money as much as they were seeking to get out of a particular business — such as busing — so they could concentrate on their mission of educating kids.

The most significant barrier to privatization, according to 25 percent of those respondents willing to answer this question, was employee and union

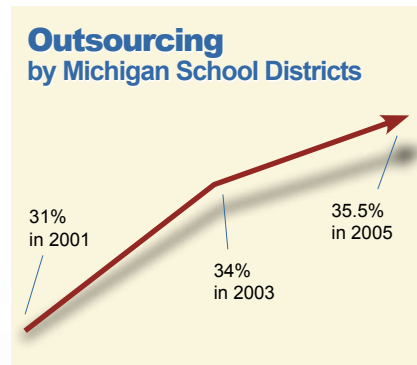
services reports that contracting with Chartwells, a popular food service company, has meant that "We are better off and the students are better off." According to Loock, the district went from paying a \$100,000 subsidy to the food program to posting a profit of up to \$25,000 after Chartwells took over. He also added that Chartwells gave them a better quality food product and more selections.

Notably, food service for the entire Iron Mountain school district in Dickinson County is provided by the 144-student Dickinson Area Catholic School. The public school district is reportedly happy with their services, though not surprisingly they can't get meat on Friday during Lent.

While the purpose of this survey was to specifically investigate contracts that districts held for basic noninstructional services, we found that many districts are using competitive contracting in other areas. For example, the Birmingham Public Schools maintains a comprehensive list of more than 60 services for which it utilizes outside contractors. The district is saving more than \$50,000 annually by outsourcing 80 percent of its lawn mowing needs from April through November.

Done correctly, privatization can and does save money and often improves the quality of services for school districts willing to adopt this cutting-edge management technique. Best of all, the savings realized can be invested in efforts that more directly impact the classroom experience of our children. **MPRI**

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School districts around the state of Michigan are finding that outsourcing services such as janitorial, busing and food operations helps schools meet their budgets and direct more dollars into the classroom.

opposition. This opposition should not surprise even the most casual observer. Members pay hefty dues to unions that fight the type of competitive bidding that has saved many districts money while improving services. The Michigan Education Association has long opposed contracting out, even though it has in the past contracted for various support services at its own headquarters — and in some cases with non-union firms.

On July 11 Kent City schools became the most recent district in the state to privatize its food service program. Another addition to the Center survey is the Avondale school district in Auburn Hills. Timothy Loock, assistant superintendent for business

Michael D. LaFaive is director of fiscal policy, and Daniel J. Smith is a research assistant, both with the Mackinac Center for Public Policy, a research and educational institute headquartered in Midland, Mich.



# Competitive Sourcing on an Individual Basis

by John R. LaPlante

Regular readers of Michigan Privatization Report know that school districts use competition to obtain food service and student transportation needs. A company provides the employees, who then provide the service. But can that model be used for even more specialized needs? Recent experience suggests that it can.

Following the example of the private sector, schools are starting to rely on people who come to work, and perform a job, but who are actually employees of a third party employee-leasing firm.

In Michigan, four major companies serve the education market. ContractED, based in Ann Arbor, lists nearly 25 schools on its client roster. Professional Contract Management of Marine City counts over 80 school districts and intermediate school districts as its customers. Thumb Educational Services of Kinde also boasts clients across the state.

All three organizations are headed by individuals with extensive experience in education administration, including terms as superintendent. All offer a wide range of professional employees to school districts, including building managers, curriculum directors, and a variety of central office employees.

Kelly Educational Staffing, a division of Troy-based Kelly Services Inc. provides substitute teachers, administrative assistants, and custodians on an individual basis. It screens and trains its own employees, freeing districts up from those burdens. Since 1999, it has placed over 8,000 substitute teachers worldwide.

School districts benefit in several financial and non-financial ways.

The most obvious advantage to the school is cost savings. For example, when using contract employees, schools do not have to pay into the state school employees' retirement system for contracted employees as they do with district employees. According to The Times-Herald, in the 2003-2004 school year, that would have saved schools 12.99 percent of an employee's pay. Currently the rate is 14.7 percent, and it's slated to increase to 18.7 percent in the 2005-2006 year.



*Outsourcing specialized services is a growing strategy which schools are employing in order to cut costs and improve operations.*

Schools also save because they are no longer responsible for employee health insurance premiums, which can easily exceed \$10,000 per year. And employee organizations, not schools, shoulder the burden for unemployment tax, workers compensation payments, and many other fees.

It's little wonder then, that schools find this an attractive arrangement.

Money not spent in these areas can be used in the classroom. Cass City schools, for example, estimated that it will save \$32,000 per year by using an outside employer to provide secretary positions.

But the benefits to schools extend beyond cost savings. Obtaining employees through an outside organization saves the school the time and expense of

a talent search. Some searches, though infrequent (assistant superintendent) can be stressful, while other more routine assignments (substitute teachers) can easily snowball. Paperwork normally handled by school employees is handled by the employing organization. The school district also gains the flexibility of having employees in an at-will employment status, making it easier to dismiss poor performers. Relying on an outside vendor to provide personnel can help schools concentrate on their main mission: educating kids.

Anecdotal evidence suggests that many people who choose this arrangement work as contract employees at a school district from which they retired. The chief benefit to employees is that they can start collecting retirement income and still draw a paycheck, which is a perfectly legal option.

Employees can also find the arrangement a way to serve a district in which they have worked for a long time, while benefiting themselves. Said Lavonne McCallum of the Sandusky Community Schools, "I'm not really ready to retire, and I felt this was a way to save the district some money." After working for over 23 years as a district employee, McCallum is now an employee of Thumb Educational Services.

Throughout the business world, companies are focusing on what they do best, and relying on other businesses to provide specialized services. Schools have been following this example by outsourcing entire departments. By hiring from firms that lease employees on an individual basis, however, schools are taking the logic of specialization to the next level. **MIPRI**



*John R. LaPlante is an adjunct scholar with the Mackinac Center and an education policy fellow with the Flint Hills Center for Public Policy in Wichita, Kansas.*

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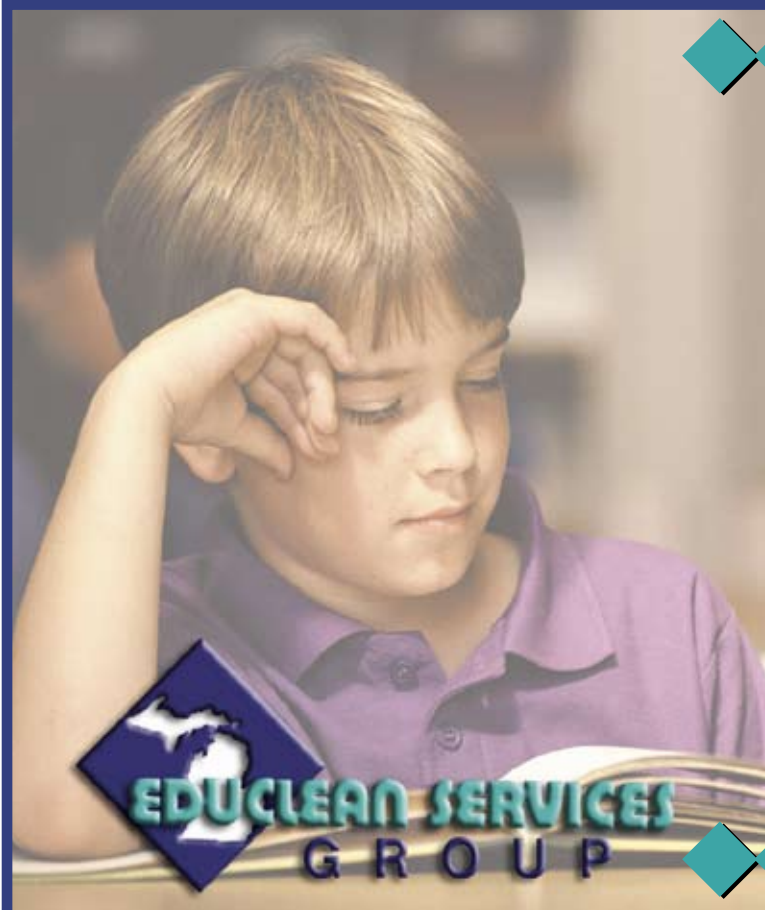
**Cass City schools, for example, estimated that it will save \$32,000 per year by using an outside employer to provide secretary positions.**



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# Hamtramck Update: Will City Thrive Without Emergency Financial Manager?

by Louis Schimmel

When I was asked in November 2000 by the Michigan Emergency Loan Board to take the job of “emergency financial manager” for the City of Hamtramck, the city was faced with several mounting financial problems that past mayors and council members had been sweeping under the rug for years. The city’s general fund deficit had grown to \$2.9 million and financial record-keeping was in total disarray. Computer technology was close to non-existent, and there were hardly any knowledgeable department heads or financial staff in any department of the city.

Other major problems facing the city included a dysfunctional Department of Public Works operating out of a poorly maintained facility, a police department housed in a dilapidated unsafe building with dinosaur technology, an underfunded library operating out of a building needing major repairs, and outdated non-working or poorly working water meters throughout the entire city. The city’s labor contracts had expired, and the city was also about to lose a major grant and other funding for a streetscape project due to the city’s inability to put a streetscape plan together.

In addition, the city had numerous unresolved legal matters. Some of the biggest legal problems confronting the city included inaction for 17 years on a brownfield site remediation case, inaction for 32 years on building court-ordered housing resulting from a segregation case, and a suit brought by retired firefighters and policemen for unpaid pension benefits that was ultimately settled for \$8.1 million. This case alone resulted in an extra city property tax levy of 14 mills for three and one half years.

I believe that an emergency financial manager has to take one of two strategic options. One approach is to

manage the crisis; the other is to fix the problem. I made it clear to state officials that, if appointed, I would not be a babysitter and would aggressively pursue changing how the city operated in order to permanently fix the city’s financial problems.

And so I began the venture by consolidating departments and hiring a controller and other key personnel to run the city. This small but dedicated staff of department heads helped bring about a complete change in how the city now does business. Unnecessary services and employee positions have been eliminated. Essential services have been, for the most part, contracted out to private companies on a lowest bid basis. Contracting out has greatly improved services and has and will continue to save the city substantial sums of money.

Contracting out DPW services meant that the city no longer needed the DPW building and all of its poorly maintained equipment (garbage trucks, snow plows, water meters, street sweepers, etc.). The former DPW building was sold and is now the site of a very successful charter school.

A former three-story hospital owned by the city has been completely renovated and houses all city offices, the 31st District Court and a modern updated police department. Major building improvements have been made to the library and a millage passed to make it self-funding.

All water meters have been replaced, and meter reading is done by a state of the art system. A private contractor does the billings. A private contractor was hired to repair or replace 110 fire hydrants that were not working. Several streets have been completely repaved.

Labor contracts were negotiated with all unions providing substantial savings to the city. The above mentioned

brownfield site was remediated which produced \$1.9 million for the city’s general fund. The infrastructure has been completed for the court ordered housing case. The downtown streetscape, including a newly repaved parking lot, has been completed.

As a result of the above, and of numerous other improvements, the city’s cost of doing business has been greatly reduced. For example, the city’s annual insurance premium dropped by over \$600,000 in the past year by hiring an outside private legal firm to be the city’s attorney for numerous lawsuits that were resolved, saving the city several million dollars.

So is everything in Hamtramck fine now? That is not exactly the case. The only reason Hamtramck is temporarily out of financial trouble is because of four years of hard-nosed professional management provided by a state-appointed emergency financial manager. Because of the absence of professional management, past Hamtramck mayors and councils have given the city labor unions excessive pension, healthcare, days off, and numerous other benefits that are far beyond the city’s ability to pay. In addition, the lack of good management has cost the city millions of dollars in lawsuits.

On November 1, 2004 the town was turned back to the system of governance that created the financial mess. However, in February 2005, the city adopted a new charter, which provides for a city manager form of government. Hopefully, the new city manager will be able to provide the necessary leadership and professional management which can prevent the city from falling back to its old ways of cronyism and fiscal irresponsibility. MPRI



Louis Schimmel is an entrepreneur and emergency financial manager in charge of labor negotiations for the city of Hamtramck.

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# Booking Privatization: Why Not Privatize Public Libraries?

by Laura J. Davis and Michael D. LaFaive

Public libraries are fixtures in many communities across the state. Some communities have expanded or built new facilities to house their libraries, yet others struggle and grasp for more public funds. Any plans to address these issues should recognize that throughout history civil society — free people working outside of coercive government mechanisms — have created novel ways for libraries to flourish without state intervention. The state of Michigan should end its subsidies to local public libraries across the state and let the institutions be financed locally.

The first established libraries were private collections dating back nearly 5,000 years to the society of the ancient Mesopotamians. Even after the inception of the first public library in the fourth century B.C., private libraries continued to be more prevalent. Following the fall of Rome, it was the libraries — or scriptoriums — of monasteries that assumed the task of preserving a wide range of books. Some monasteries even began systems of inter-library loans. During the Renaissance, families, universities, and the Vatican City all built their own libraries.

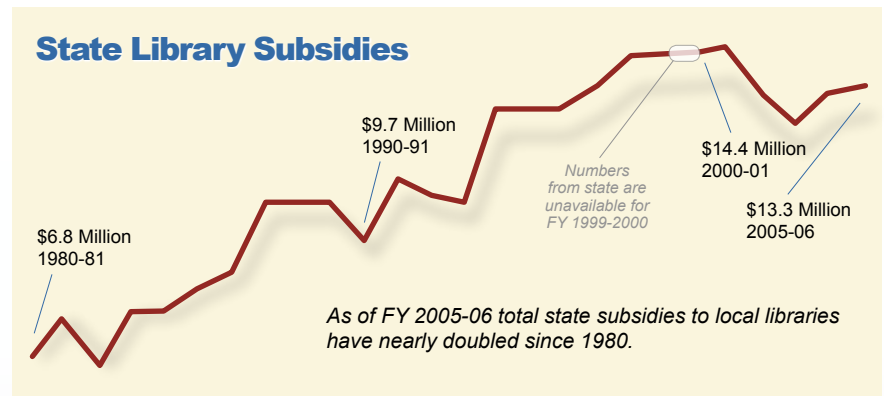
In America the first library dates to 1638 when John Harvard donated his own collection of books to the divinity school that later adopted his name. Benjamin Franklin also famously started a subscription library, the Library Company of Philadelphia, to which members paid dues in order to sustain the library. It was not until the nineteenth century and the beginning of public education that the first public libraries were opened.

There are 384 public libraries and 305 branch libraries spread across Michigan. Most of these libraries are subsidized through the “State Aid to Libraries” line item in the Michigan

Department of History, Arts and Libraries. The proposed fiscal 2006 line item will account for about \$13.3 million in funds. Interestingly, Detroit and Grand Rapids libraries used to enjoy their own line items in the state budget and a portion of the “State Aid to Libraries” subsidy, but have recently been rolled into the overall budget line as part of recent budget reforms.

service that proponents claim would not occur if government were not providing it. Public libraries have been expanding into services that for-profit companies would or do effectively provide. Video tape rental, coffee shops, and “free” Internet access are three examples. Lastly, there remains justifiable public criticism as to how a public library uses its funds. Some libraries have had to contend with

In an informal survey by state officials, last November there were 15 ballot measures before voters in communities across the state for library related millage requests. Seven failed to pass.



Today budget problems still trouble public libraries, and their operators have responded by shaving hours of operation, reducing the purchase of new materials, and laying off personnel. The Warren Public Library closed the Edgar A. Guest branch in 2004 to save money, and Birmingham recently delayed a proposal to expand its library. According to an informal survey by state officials, last November there were 15 ballot measures before voters in communities across the state for library related millage requests. Almost half — seven — failed to pass.

There are a number of problems associated with publicly subsidized libraries. First, they make demands on taxpayers to provide a service that they do not use. Second, they are unnecessary. Just because a government library doesn't exist doesn't mean that people will be deprived of reading material. Third, government entry into particular businesses crowds out the very private sector

questions relating to internet filters, politically correct book purchases and what does or does not constitute acceptable displays of artwork.

As in many areas of the public and private policy arena there are alternative solutions that can address these problems in whole or by degree. Libraries are no exception. Here are a few options:

1. Stop subsidizing public libraries at the state level. This will relieve taxpayers in Ishpeming, for example, from being forced to subsidize the library habits of Detroiters. Services that are provided and funded publicly from a local millage may be tailored to constituents. It is likely that the people of Holland, Mich. will have different literary tastes than those in Ann Arbor.
2. Stop subsidizing public libraries at every level. A sea change in policy see “Library” on page 11



# Privatization in Michigan State Parks

by Russ Harding

Michigan's state park system has expanded into something quite different from what lawmakers envisioned when the system was created in the early part of the 20th century. The Natural Resources and Environmental Protection Act states that the purpose of the Michigan state parks is to "preserve and protect Michigan's significant natural and historic resources."

It was not the intent of the original lawmakers to set aside areas as state parks merely as an alternative to outdoor recreation opportunities provided by the private sector. Rather, state parks were intended to be special places representing the best Michigan has to offer in natural and historic resources. Most would agree that parks like Ludington State Park, with its beautiful Lake Michigan beaches, and Porcupine Mountain State Wilderness Park, meet the most original definition of what was supposed to be protected.

However, Michigan has acquired many state parks over the years that are not unique in either their natural resources or their historic value. Michigan's state park system consists of 97 parks, encompassing 265,000 acres — a far cry from the humble beginnings of the system when D.H. Day and Interlochen, the first two parks, were acquired by the newly created State Parks Commission in 1919.

The state should sell a number of state parks. Returning these parks to private ownership would provide several benefits:

1) The cash-strapped state would realize a considerable windfall from the sale of these properties, which often contain waterfront and other features prized by private citizens.

2) The liquidation of these properties would allow state park managers to focus their limited resources on protecting the state's truly outstanding natural and historic sites.

3) Taxpayer-subsidized competition with private campgrounds would be reduced significantly.

4) The privatized properties would be placed back on local tax rolls.

The following parks may be good candidates for private ownership:

• **Aloha State Park**, 107 acres. The park provides campers with access to Inland Lakes Waterway, a benefit that could be attractive to the private sector.

• **Baraga State Park**, 56 acres. The park is one-quarter mile from Baraga, Mich., making it convenient. It does not provide unique value, however.

• **Dodge #4 State Park**, 139 acres. This site does not possess unique characteristics.

• **Hayes State Park**. Hayes does contain three lakes, but much of the visitation is due to the park's proximity to Michigan International Speedway and other tourist attractions.

• **Hoeft State Park**, 301 acres. Hoeft is a stopover for visitors to the Mackinac Straits area.

• **Interlochen State Park**, 187 acres. Interlochen primarily supports activity at the adjacent National Music Camp. The Music Camp might be a good candidate to operate the park.

• **Mears State Park**, 50 acres. Located near Pentwater, Mich., Mears should be sold to the private sector.

• **Muskallonge Lake State Park**, 217 acres. The park is northwest of Newberry, Mich., in the Upper Peninsula.

• **Newaygo State Park**. Newaygo contains 99 rustic campground sites, but no important or unique natural resources.

• **Otsego Lake State Park**, 62 acres. This park is located along Otsego Lake and contains 155 campsites.

• **Straits State Park**. Located in St. Ignace, the park is used primarily by campers who visit attractions in the area. This park could be sold to the private sector.

• **Twin Lakes State Park**, 175 acres. Twin Lakes is primarily a staging area for campers visiting attractions on the Keweenaw Peninsula.

• **Wetzel State Recreation Area**. Wetzel is used primarily by enthusiasts of radio-controlled airplanes.

• **Wilson State Park**, 36 acres. Wilson, located in Harrison, Mich., is not very unique.

The sale of any state park will generate political resistance. Park officials will resist a sale simply due to turf protection.

But creating revenue and competing with private campgrounds are not the reasons the state Legislature created the state park system. The system will ultimately be stronger if it is comprised only of parks that represent the most important natural and historic treasures of our state. <sup>MIPRI</sup>



Russ Harding is a former chief of Michigan state parks and is senior environmental policy analyst for the Mackinac Center for Public Policy.

The system will ultimately be stronger if it is comprised only of parks that represent the most important natural and historic treasures of our state.



# Features

## Privatization means significant savings

by Jeff Siegel

*Reprinted with permission of the Herald Palladium in St. Joseph.*

Over the past several years Michigan has undergone a significant economic downturn, and, as a result, funding for education has been slashed. Michigan schools have been left with the huge problem of continuing to provide quality educational programs and services to our students with fewer dollars. Proposal A (approved in 1994), which helped narrow the gap between wealthy and poor districts, took away school districts' ability to raise taxes for operations.

The Berrien County Intermediate School District, in its role as a service agency, provides programs, services and funding to local school districts. These funds help local districts offset their costs for operating special education programs and for providing special services to their students. Thus, dollars saved by the BCISD result in increased funding, programs and services for local district operations.

With local district options for raising new money through taxes limited, discussions have turned toward reducing expenses. In 1994, PA 112 was amended; allowing schools to privatize non-instructional services without going through the collective bargaining process. In fact, the amendments went beyond removing the necessity to negotiate on this issue and made it an illegal subject of bargaining. As a result, the past decade has seen many local and intermediate school districts outsource their food service, custodial, transportation and certain administrative services to reduce costs without directly impacting instructional programs to students.

The BCISD has privatized the food service program and the trans-

portation system for students attending the Lighthouse Education Center (formerly North Lincoln School) for many years with great success. More recently the district also privatized some administrative and consulting services, resulting in more than \$200,000 in savings this past year. Since the transportation system at the Blossomland Learning Center is a high-cost item, privatizing has been discussed for several years. In the fall of 2004, the BCISD met informally with various potential vendors to gather information about the services they might offer and the potential savings the district might realize.

In December 2004, requests for proposals (known as RFPs) were sent to possible transportation vendors. In March the district received firm bids from three private carriers. The most attractive (and lowest) bid was submitted by Laidlaw Education Services and, if implemented, would save the BCISD nearly \$1 million for each year of the five-year proposal. Laidlaw is the largest private contractor of student transportation services in the country with more than 40,000 buses; the company also provides services to more than 1,000 school districts.

Given that school districts now have the right to privatize these services, the more difficult question becomes: "Is it the right thing to do?" Arriving at the best answer involves significant discussion, critical analysis of bids (focusing on safety and quality issues) and a detailed check of references including on-site visitations.

The safe and efficient transportation of our students is, and always will be, the most important consideration. This holds true both for regular students and for students with special needs. Jeopardizing their safety and quality of care would not be an option, regardless of the amount of

dollars saved. Currently, many Michigan districts, ISDs and local districts outsource all or a significant portion of their transportation services. Nationally, more than 40 percent of student transportation is provided by private carriers. While it is easy to become caught up in discussing whether the private contractor or the public employee would provide more safety and quality, the fact is there is no evidence to support that either one meets a higher standard of quality, care or safety than the other.

While this decision is about students and cost savings, the BCISD remains sensitive to the anxiety this causes for our transportation staff. These employees have performed admirably over the years and are sensitive to the needs of the students. The district has required that any successful bidder provide the first opportunity for employment to our current staff. Although the benefits would be reduced if employed by a private contractor, hourly compensation would be commensurate with their current wages.

The mission of the Berrien County Intermediate School District is "to provide programs and services to our constituent school districts which enhance learning opportunities for all students." If the BCISD can provide private transportation services to our students while meeting the same or higher standard of quality and safety, and realize a significant cost savings that would provide enhanced educational opportunities to the students in our local districts, it would be fiscally irresponsible to do otherwise. MPRR

*Jeff Siegel is superintendent of the Berrien County Intermediate School District*

**Nationally, more than 40 percent of student transportation is provided by private carriers.**

## “Amtrak” continued from page 16

subsidy, however, because the federal government foots part of the bill for the Port Huron and Grand Rapids routes.

Amtrak should prepare itself for privatization. There are a few primary types of privatization: competitive outsourcing and commercialization are two of the most popular forms. In competitive outsourcing, a unit of government hires a private firm

## “Library” continued from page 8

of this nature would likely result in many creative responses to keep libraries open to some degree in communities. Philanthropists may donate money to keep libraries open, fundraisers may be held by a “friends of the library” association, volunteers may replace paid staff, and other libraries may start charging a variable fee to rent a book based on the length of the rental and popularity of the title. Other libraries may just close and sell their assets to other libraries.

3. Government may maintain ownership of the asset but contract out for its total operation, as has occurred in Southern California.
4. Public libraries may split the duties between a local, publicly paid staff and a private, for-profit management company for very specific duties, such as cataloging, technical and book-buying services, and janitorial and grounds maintenance. In Metro Detroit, libraries are contracting with private agencies to collect library fines. According to an August Detroit News article, half of Metro Detroit’s 65 libraries employ collection agencies. Clearly, libraries are familiar with contracting for services.

to operate a particular service under contract. Commercialization occurs when a government gets out of a particular business entirely. If Amtrak were commercialized, for instance, the government could sell everything from its trains to access to its stations and repair equipment.

Passenger train privatization would not be a novel concept in much of the

One such company is Library Systems and Services Inc. (LSSI). The company has provided expertise in library management for federal agencies such as the Library of Congress, the Department of Energy, and the Smithsonian Institute, in addition to running entire libraries at the local level in such states as California, Texas, Kansas and Tennessee.

In one instance the company won a contract with Riverside County, California to run its entire 28 library system. LSSI outbid two public units (a county and a school district) for the contract. The company has been providing library management services in Riverside for eight years. Its newest contracts are in Shelby County, Tennessee where LSSI is managing four libraries under four separate contracts.

There is nothing about local libraries that make state involvement a necessity. Local units (and their taxpayers) should make decisions as to whether or not they wish to support a library without subsidies from Lansing. MPRI



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world. According to Joseph Vranich, author of “End of the Line: The Failure of Amtrak Reform and the Future of America’s Passenger Trains,” 55 nations around the world are “privatizing, devolving, or regionalizing their national rail services.”

Britain has one of the more exciting reforms to consider. According to Vranich the increase in ridership in Britain alone since its 1993 rail privatization is larger than the total number of annual Amtrak passengers annually. Indeed, passenger use of railroads in Britain is higher today than at anytime back to 1947, when the rail network was far more extensive. The British experience is based on a system of franchises awarded to 12 corporations that have won the right to provide passenger rail services throughout the United Kingdom. The brash entrepreneur Richard Branson of Virgin Records owns one franchise. The trains are all owned by a different company and leased for use to the franchisees.

Ending Amtrak subsidies completely and selling off the corporation’s assets would not end passenger travel altogether; it would simply make transportation alternatives more affordable by leaving additional resources in taxpayers’ hands. It is time to make this archaic entity part of America’s and Michigan’s past.

(Author’s Note: As MPR went to print in September, Amtrak’s future was still being debated. However, a Sept. 21 news report indicated that Amtrak has conceded a willingness to let private companies bid to operate some routes. “Private operators need to be given a shot,” said Amtrak’s chairman, David Laney.) MPRI

Michael D. LaFaive is director of fiscal policy for the Mackinac Center for Public Policy.

**Ending Amtrak subsidies completely and selling off the corporation’s assets would not end passenger travel altogether; it would simply make the alternatives more affordable.**



# Governing by Network: The New Shape of the Public Sector

by Lawrence W. Reed

The following is a book review of “Governing by Network: The New Shape of the Public Sector,” by Stephen Goldsmith and William D. Eggers; Brookings Institution Press, Washington, D.C.; 2004.



Garnering attention in many halls of government including Lansing in recent years is a book by David Osborne and Peter Hutchinson titled “The Price of Government: Getting the Results We Need in an Age of Permanent Fiscal Crisis.” Billed as a “step-by-step roadmap for change,” the book offers a mixed bag of suggestions for budgeting, restructuring and consolidation — some good, some questionable, but few that are truly as “radical” as the authors claim. As some reviewers have noted, the book dusts off and repackages a lot of ideas from the “reinventing government” craze of the 1990s, an effort that largely fizzled in the face of resistance from entrenched bureaucracies and status quo politicians.

A more recent book offers new promise. “Governing by Network: The New Shape of the Public Sector” by Stephen Goldsmith and William D. Eggers centers around the premise that Big Government is here to stay and needs to be better managed. It deserves a prominent place in the libraries of every officeholder who wants to succeed in an era of fiscal stringency because it plainly argues that good government doesn’t mean more of it. Rather, it means redefining what government’s responsibilities are and performing them by directly involving both the private for-profit and nonprofit sectors — even to the point where the government’s “customers” enjoy the provision of government services without coming into contact with a government employee. Take the best of Osborne/Hutchison, add this book, and you have a recipe for some real, positive change.

Goldsmith and Eggers challenge the reader to think of government less as the actual *provider* of certain goods and services and more as the *facilitator* of them. By encouraging networks of private and nonprofit individuals and organizations, government can often get its job done better, quicker and cheaper. If customer satisfaction is to be a cornerstone of better government — and too often in the past, it just hasn’t been high on the list of government priorities — then this book deserves the high praise it is eliciting across the political spectrum.

This concept of “networking” central to the book’s thesis is more than theory. The more forward-looking, customer-oriented, cost-conscious governments — primarily state and local — are already moving in this direction. In a review of the book for the Democratic Leadership Council’s *Blueprint* magazine, Marc Porter Magee notes that the advantages of the networking approach “include greater specialization to handle America’s increasingly complex public problems, greater speed and flexibility to explore alternative solutions, and increased reach to implement broad-based alliances and make government funds go further.” Goldsmith and Eggers provide a rich collection of revealing examples, drawing lessons and offering advice for future finely-tuned improvements.

Community-based nonprofits in Florida run the child welfare systems in dozens of counties, “and the state’s entire child welfare system is slated for eventual privatization.” For-profit firms are managing some public schools. The National Park Service has teamed up with a nonprofit group to refurbish the Golden Gate National Recreation Area in San Francisco. Goldsmith himself, when he was mayor of Indianapolis in the 1990s, saved millions of dollars and improved dozens of city services by creative outsourcing with private groups and networks.

Nonetheless, notions about improving government should not be seen as arguments for government to be involved in anything as long as it gets better at it. Indeed, with government combined at all levels consuming a portion of personal income many times what it ate a century ago, strong arguments exist for governments to do less by withdrawing from certain activities altogether. By its tax burden alone, it can crowd out private initiative even when it contracts with it.

As an extreme hypothetical example, the fact that a city-owned pizza parlor could be improved by contracting out to private pizza makers instead of using taxpayer-paid government employees shouldn’t distract us from the conclusion that no level of government should be baking pizzas at all. One wishes that Goldsmith and Eggers had said more on this issue, but if one starts with the assumption that a given service is indeed a proper one for government, their book points the way to getting it accomplished with the welfare of the taxpaying and service-consuming public being the top priority. The authors devote considerable space to the problems of networking with nongovernmental groups, and explain numerous ways to anticipate and preempt those problems. If you are a public official, those are precisely the details you need to know.

By empowering private people and their networks, government can move beyond merely tinkering with old ways of doing things and genuinely reform itself. Done properly, “governing by network” can treat festering public sores with cures instead of band-aids. That ought to put the Goldsmith and Eggers book at the top of every public official’s 2005 must-read list. [MPPI](#)



Lawrence W. Reed is president of the Mackinac Center for Public Policy.

# Around the State



## Traverse City Debates the Future of its Zoo

TRAVERSE CITY — A July opinion column in the Traverse City Record-Eagle called on the city to privatize its Clinch Park Zoo. The zoo has long been located on prime real estate along Grand



Traverse Bay in downtown Traverse City. According to the author, Karl DeFoe, taxpayers have paid out \$3.4 million in subsidies since 1990 to keep the zoo afloat. Revenues generated by the zoo have only provided about 30 percent of its annual cost, noted DeFoe.

The Clinch Park Zoo is hardly the first government zoo to require subsidies. DeFoe mentions a few by name, including the Saginaw Children's Zoo. Years ago the Mackinac Center for Public Policy did a review of this zoo's transition to private status. The Center found that as a result of its conversion to private ownership and the hiring of a maverick zoo leader, the zoo increased in size, attendance, and in the population of healthy animals. Since 1996 there has been an 80 percent increase in the number of animals that can be viewed. To read more about the Saginaw Children's Zoo privatization visit the Mackinac Center for Public Policy's Web site at [www.mackinac.org/1654](http://www.mackinac.org/1654).

While DeFoe's article mentioned the cost savings that could be realized by eliminating Traverse City's subsidy, it failed to mention the other financial benefits of zoo privatization. The city could get out of the zoo business altogether by selling off the land to a private owner and pocketing the proceeds. It would then have a new tax revenue-generating property on its rolls.

## Privatization Not on Ice in Redford

REDFORD TOWNSHIP — In May, Redford Township officials voted to get out of the ice rink operation business by contracting with Family Entertainment Properties. The contract began in June and is expected to save Redford money while improving services.

According to the Detroit News, the ice arena had been expected to lose \$70,000 in fiscal 2005. By contrast, under the new contract, the arena is expected to generate \$30,000 in annual profit for the township. Family Entertainment Properties is also expected to make needed capital investments and to provide more services.

Michigan Privatization Report has long followed municipal recreation and recreation privatization in the state, recommending privatization of non-essential municipal services — such as golf, wave pools, and ice arenas. In 1999 the Mackinac Center dedicated an entire issue to privatization of government recreational facilities. Entitled, "Entertaining Privatization" the issue addressed everything from park, zoo, and state fair privatization to ending public subsidies for professional sports stadiums and the arts. The issue can be accessed on the World Wide Web at: [www.mackinac.org/1849](http://www.mackinac.org/1849).

## Livonia Swimming Toward Privatization?

LIVONIA — The city of Livonia and many other municipalities have been grappling with a decline in revenues over the past five years. One way Livonia has tried to manage this decline is by making use of competitive contracting. In June, Livonia Mayor Jack Engebretson told The Detroit News that he was looking at a number of options — including privatization — for the city's three municipally owned and managed swimming pools.

In a conversation with Michigan Privatization Report Editor Michael LaFaive, Engebretson detailed how the

city owned three pools, one of which had been operated by the local YMCA. When the YMCA returned its operation to the city a year early, the cash-strapped city was left with few options and closed the pool. The mayor has had some dialogue with local civic associations that use the pools about these groups taking over the pools' operation.

No group has yet expressed an interest but that may change when the city tries to finalize its next budget and considers closing the remaining pools. There are some case precedents for allowing local nonprofit groups to operate city facilities. For example, the Livonia Hockey Association operates all three of the city's ice sheets and does so without a subsidy. An added benefit is that the city is no longer exposed to liability suits associated with running municipal ice arenas.

As MPR went to print the Detroit News reported that two of the Livonia pools may continue to be operated in 2006 under the auspices of the city — barring an absence of additional revenue sharing cuts from the state.

## Municipal Golf Deficits Spark Privatization Talk in Lansing

LANSING — A Lansing State Journal feature on Sunday, August 2 reported that Lansing's four municipally owned golf courses have lost an average of \$641,500 annually — "a deficit covered by taxpayer subsidy," according to Journal writer Todd Schulz.

City council member Carol Wood told Schulz that something had to be done to stem the financial losses and



that could include selling off courses in their entirety, closing any number of the four, or contracting with a private company for management. The city's park director opposes any such moves

*continued on next page*

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**The ice arena had been expected to lose \$70,000 in fiscal 2005. Now, under the new contract, the arena is expected to generate \$30,000 in annual profit for the township.**

# Around the State

and has argued that some public-private golf management contracts have fared poorly for the municipalities that enter into them. Wood cited unspecified examples of companies turning back golf operations to municipalities in worse shape than when the companies took over management of them.

Michael LaFaive, senior editor of Michigan Privatization Report, believes that such bad experiences can be mitigated by careful contracting. "It takes two to tango," said LaFaive. "The world now has a lot of experience with privatization and precautionary steps can be taken by every unit of government to minimize poor performance and the abandonment of duties on the part of a vendor. It is vital that government does everything it can to facilitate successful partnerships otherwise they may give privatization a bad name."

For more on golf privatization, see "Golf Privatization: Fieldstone Should be Private" on the Web at [www.mackinac.org/6502](http://www.mackinac.org/6502).

## Auditor General Report Riles Prison Contractor

LANSING — The Michigan Information Research Service, a Lansing-based political newsletter, reported in late July that the Geo Group, a private for-profit contractor that operates the Michigan Youth Correctional Facility in Baldwin, criticized an Auditor General review of its work.

The audit was sparked by a recommendation from Gov. Jennifer Granholm that the contract with Geo Group be canceled. Geo Group spokesman Bill Nowling told MIRS that canceling the contract was effectively a gift to the Michigan Corrections Organization, a Service Employee International Union that represents state corrections workers. Nowling criticized the report for excluding important information, not addressing the value of having a youth-only facility and for neglecting the negative economic impact that closing the facility might have on Lake County.

The Auditor General's report is available online at [audgen.michigan.gov](http://audgen.michigan.gov).

## Intergovernmental Contracting Inspires Lawsuit

MOUNT CLEMENS — Mount Clemens officials last April voted to contract out for police protection with the Macomb County Sheriff's Department, thereby eliminating the city's 118-year old police force. The \$2.1 million contract, which began July 1, is expected to save the city \$600,000 the first fiscal year of the agreement and then \$1 million annually thereafter.

According to a June 16 Detroit News article, the move did not sit well with the union that represents the city's 26 police officers. The officers' union sued the city to prevent the change, arguing that it is against the law. In what may be the first anti-privatization "poison pill" in American history, the Sheriff's Act of 1846 actually prevents a replacement of city police with "sheriffs, unless the city maintains the highest level of staffing over the past 36 months," union attorney Douglas Guscher told The News.

Because current staffing is not at its high point, the sheriff would have to add officers to the payroll, thus increasing the actual cost of the contract. The term "poison pill" is often used to describe mechanisms for publicly-traded corporations to thwart hostile takeovers from outside parties. Mike Murray, a lawyer for the city, told Michigan Privatization Report that the union attempted to obtain an injunction preventing even a temporary takeover. The request was dismissed and the dispute between the parties may go to court.

The Mackinac Center for Public Policy has addressed both intergovernmental and private police contracting in the past. For more on these subjects see "State Police Can Patrol Highway for Less" at [www.mackinac.org/5373](http://www.mackinac.org/5373) and "Privatizing the Long Arm of the Law" at [www.mackinac.org/796](http://www.mackinac.org/796).

## Will It Pay(roll) to Privatize?

LANSING — Legislation to privatize the state's payroll processing system was approved in the state House last March and is expected to be taken up in the state Senate this Fall, once budget negotiations for fiscal 2006 have been completed. The House vote was primarily along party lines, passing by an eight vote margin. To see how your legislator voted visit [www.michiganvotes.org/2005-HRC-34](http://www.michiganvotes.org/2005-HRC-34).

The Mackinac Center recommended that the state consider contracting out for human resource activities in its Winter 2003 edition of Michigan Privatization Report. The article argued that the state could reasonably project savings of \$5 million annually through privatization of its human resource functions (not just payroll).

The focus of the MPR article was Florida's new contract with Convergys, Corp., a public, for-profit group headquartered in Ohio. Since publication of that original article, Florida state officials have tussled over forecast versus actual savings expected from the contract with Convergys. According to a February St. Petersburg Times article, the original contract was to have saved \$93 million over seven years but is now expected to save only \$25 million over nine years.

Supporters of the contract, including Convergys, dispute the revised figures, arguing that the new accounting does not consider savings generated by the contract that have been diverted to other uses. In addition, say Convergys officials, critics are not counting the estimated \$80 million the state saved by not having to purchase new human resources software and implementation services for their own aging system.

## Federal Outsourcing in Michigan

Employees of federal hatcheries located in Michigan were reportedly worried early this year about a Bush

Lansing's four municipally owned golf courses have lost an average of \$641,500 annually — "a deficit covered by taxpayer subsidy,"

Administration plan to “competitively source” the work they do in the Great Lakes State. Competitive sourcing requires certain bureaucracies or federal agencies to compete with private-sector rivals through the bidding process for the right to provide services.

The “President’s Management Agenda” was introduced in the summer of 2001 and included proposals to use competition between government agencies and the private sector to improve the cost-effectiveness of services being provided to the public.

In late July of this year, the administration issued an update on its previous report about the results of Pres. Bush’s competitive sourcing initiatives. The report stated that in fiscal year 2004 agencies underwent 217 competitions involving 12,500 federal job positions that are expected to save taxpayers about \$1.4 billion over three to five years. The report also argued that an increase in fiscal 2004 savings is largely attributable to competitions between larger bureaucracies and private-sector rivals, and a better, more frequent use of a management process that enables the agencies and businesses to compete on a more level playing field.

According to the administration’s report it is competition that is the main driver of savings. The authors found that if two or more bids were submitted by the private sector to perform a service, savings of more than \$30,000 per full-time federal employee might be derived. By contrast, if no bids were submitted but the public agency undertook a reform of its own practices to operate more efficiently, only \$18,000 in estimated savings per FTE was found.

Some positions that had been considered for competitive sourcing were here in Michigan and were part of the federally owned and operated fish hatchery system. There are 70 national hatcheries with operations that may be competitively sourced, three of which are located in Michigan: the Jordan River operation in Otsego County, and the Sullivan hatchery and the Pendills Creek

hatchery in Chippewa County.

Those involving animal husbandry were at one time up for competitive sourcing but the Bush Administration has since withdrawn these positions from the prospective outsourcing. Some administrative and maintenance positions may still be put up for bid.

Not everyone is thrilled with the competitive sourcing policies of the Bush Administration. In 2003, Paul Light of New York University and the Brookings Institution testified before the U.S. Senate and reported that competitions may “never be more than a minor lever in allocating headcount constraints more systematically.” Light considers competitive sourcing to be a “blunt instrument” and suggests as an alternative a more “performance-centered system” that would allow government bureaucracies to “achieve the effects of competition more naturally.”

In 2002 Michigan Privatization Report recommended in its article, “Legislators Should Spawn Hatchery Privatization,” that some type of privatization occur for state-owned and run hatcheries, noting that private companies were capable of doing the same work, and for less. The hatchery privatization article can be accessed at [www.mackinac.org/4742](http://www.mackinac.org/4742).

### Possible Pontiac Privatization Causes Protest

PONTIAC — Oakland County school officials were treated to a public rally and protest July 11 over the intention of Pontiac board of education members to pursue privatization of services that may affect union-held positions in the district.

The Oakland Press covered the protest and noted that the district faces a \$12.5 million deficit. As part of her duty to balance the school’s budget, School Superintendent Mildred Mason is looking at competitive contracting options that might trim 300 employees from the official district payroll, including 42

security officers and 83 secretaries. As of August 22 the plan was officially on hold because the unions that represent these employees may agree to concessions with the district.

### Chesaning Union School District May “Substitute” Privatization

CHESANING — The Chesaning Union School District is exploring options for contracting with a private firm to provide substitute teachers. According to Tom Daluca, the district’s director of finance, the research is necessary to ensure that money saving options are available to the district. In an August interview with Michigan Privatization Report Daluca said that the district had been presented with “one brief overview” by an individual who explained services that could be provided under contract with the district. If the board chooses to contract for substitute teachers says Daluca, the plan will likely be implemented in January 2006.

### Corrections

In the previous Michigan Privatization Report “Privatize Parking Garages” the author described Ann Arbor parking garages as being owned by the Downtown Development Authority. Technically, they are owned by the city which contracts with the Authority for their operation. The Authority then contracts with Republic Parking System for day-to-day operations. Parking meters are not enforced after 6:00 p.m. though Republic does work after 6 p.m. operating public structures and attended lots.

In the article, “Cobo Hall: It’s Time to Sell,” Novi Center Expo executive Blair Bowman was incorrectly identified as a “she,” instead of a “he.” MPR regrets the error. MPRI

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The report stated that in fiscal year 2004 agencies underwent 217 competitions involving 12,500 federal job positions that are expected to save taxpayers about \$1.4 billion over three to five years.



# Feature

## “End of the Line” for Amtrak Subsidies? Think Again.

by Michael D. LaFaive

In 1970, Amtrak — a federal, quasi-public corporation — was created by the federal government to help increase passenger use of trains. Taxpayers were promised a profitable system within three years. More than three decades have passed and Amtrak has yet to turn a profit in any year, despite promised reforms.



*Amtrak trains continue to operate, despite the corporation's repeated failures to meet ridership targets or become profitable.*

Since its creation, Amtrak has absorbed more than \$29 billion in subsidies and more than \$6.5 billion since 1997 alone. It was in 1997 that a federal reform board mandated that Amtrak either become profitable by 2003 or be liquidated. Both the federal government and the state of Michigan must stop providing cash subsidies to this unnecessary and expensive intervention in the transportation marketplace. Taxpayers would be better off with some sort of privatized version of

Amtrak, but that does not look like it will happen in the short run.

President Bush attempted to prompt needed reforms of Amtrak when he introduced his fiscal 2006 budget, which would have removed all operating funding for the system unless needed reforms were made. Last June Congress reinstated hundreds of millions of dollars in funding to ensure that money-losing routes outside the Northeast corridor would remain operational. Initial reform proposals might have resulted in the elimination of 17 of the most expensive routes outside the Northeast corridor.

Bush's Amtrak reforms had three components, according to Ron Utt of the Washington, D.C.-based Heritage Foundation.

- Transfer the NEC (Northeast Corridor operations) to the Department of Transportation, which in turn would lease it to a newly created entity that would operate NEC trains on behalf of a compact formed and financed by the eight states that the NEC serves.
- Reduce federal operating subsidies for Amtrak's 17 long-distance routes by phasing in, between 2005 and 2008, incremental increases in the share of the Amtrak subsidy that states pay for routes in their regions. In the first year, states would have to cover any losses over 40 cents per passenger mile;

in 2007, losses over 10 cents per passenger mile; and in 2008 and thereafter, all losses.

- After three years of operation, contract out all Amtrak routes that are still in operation (except the NEC) to private operators on a competitive basis.

Doing so could save hundreds of millions of dollars annually. According to the Wall Street Journal, the Bureau of Transportation Statistics collected information on federal subsidies in four areas of transportation: rail, bus, flight, and highways and then divided these figures by passenger miles traveled. This allows researchers to make cost comparisons among different modes of transportation. Amtrak had the largest subsidy at \$186.35 per thousand passenger miles versus just \$6 for airlines.

Amtrak maintains three routes in the state of Michigan: Detroit, Port Huron, and Grand Rapids, all of which roll to Chicago. The Port Huron and Grand Rapids routes are subsidized by the state of Michigan. In fiscal 2006, Michigan taxpayers may directly contribute more than \$7 million to cover the shortfall in revenues necessary to maintain these routes. Granholm's budget recommendation for 2006 was \$7.1 million but it appears that the house will remove \$1 million as part of its overall budget trimming exercise. This is just a portion of the total  
*see "Amtrak" on page 11*