

# The Politics of Government Outsourcing in the American States

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## Abstract

Government outsourcing of services to private sector entities is increasingly common. Given the connection to market principles, common understandings of this trend center on its connection to conservative leadership. However, outsourcing is regularly championed by leaders of different ideological orientations, suggesting other factors may be at play. I point to an underappreciated way by which potential losers—bureaucrats organized into public sector unions—affect the decision to outsource. To test the argument, I construct a new measure of service outsourcing at the state level. While I find little connection to ideology, the results show that states with strong unions are less likely to rely on private actors. I bolster these findings with a synthetic control analysis of a state law that sapped union power. Overall, these results highlight how public sector unions stem the outsourcing tide and suggest that policies that circumscribe unions have downstream implications for service provision.

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Facing the nation’s highest rate of children in foster care—17 out of every 1,000 children—in 1995 the state of Illinois decided to privatize its child welfare program. No longer would state employees directly administer foster care and adoption services; instead, these functions were to be carried out through contracts with private companies and non-profit organizations. Illinois was not alone; Kansas, New York, and Oklahoma followed suit with large-scale outsourcing of their own child welfare systems. Such contracts have become increasingly common; today state governments routinely offload information technology, medical patient services, park management, prison management, maintenance of roads, bridges, and water treatment facilities, and numerous other government functions to the private sector. This trend is replicated at the federal level, where contractors help fight wars, run prisons, collect taxes, write regulations, render benefit decisions, and shape policy.

Debates about whether the public or private sectors provide particular services more effectively or efficiently have been around since the Founding of the republic (Michaels, 2017).<sup>1</sup> Yet, the trend toward private sector provision of government services has quietly gained momentum in recent years, leading one prominent scholar to declare the current state of affairs “Leviathan by proxy” (DiIulio, 2014, 6), another to describe the network of contractors employed in the government service as a “shadow government” (Light, 1999), and still others to bemoan it as the “hollow state” (Milward and Provan, 2000). Yet while the trend toward privatization of government services is ubiquitous, scholarly discussions about government outsourcing decisions remain largely abstract and focused on the consequences of this trend, rather than its root causes.

How do political factors shape government decisions to outsource services or keep them

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<sup>1</sup>This article focuses on the outsourcing of *government services*—meaning that a service that has traditionally been performed by government is reallocated to a private sector entity, which can be a for-profit or a non-profit organization. Outsourcing is one component of privatization, a broader term which also describes a government’s reliance on the private sector, but which encompasses other activities such as asset sales and public-private partnerships.

in-house? Because outsourcing relies on market forces, it is often assumed to be a tool that is primarily pursued by Republican or conservative leaders. I demonstrate, however, that the impulse to outsource has become nearly universal for political leaders of all stripes. Instead, the variation in outsourcing rates that we observe comes not from differences in the desire to implement it from the top, but rather from the concerted efforts of organized interest groups with a vested stake in outsourcing decisions. Adopting this “policy-focused perspective” (Hacker and Pierson, 2014), I focus on the role of public sector unions. Recent research highlights the political power of public sector unions (e.g., Anzia and Moe, 2014, 2016, 2019; DiSalvo, 2015; Flavin and Hartney, 2015; Marlow, 2013), and blocking outsourcing is a matter of self preservation for these political actors.

The states provide the ideal venue to empirically assess this argument. Not only is there considerable variation in outsourcing levels among the states, there is also variation in their economic health, political leadership, and the extent to which public sector unions have clout. To leverage this variation, I develop a new annual measure of state government outsourcing decisions over a 23-year period (1992–2015). However, while I develop evidence at the state level, the argument readily extends to other levels of government.

This paper proceeds in several parts. The first section describes the largely normative literature on government outsourcing and privatization. I then explain the incentives facing public sector unions when it comes to outsourcing decisions, and the strategies available to them to influence these decisions. An introduction to the new measure of outsourcing follows, with an explanation of how it is derived and validation of its use. The next sections test the expectations in a large-N empirical setting and also assess alternate explanations for outsourcing. I then turn to a case approach, applying the synthetic control method to a legal change that sapped public sector union strength in Wisconsin. These analyses provide additional evidence of the influence of union strength on outsourcing decisions. The final section concludes with a discussion of the normative implications of this study, particularly in light of recent court decisions regarding public sector unions.

## The March Toward Marketization

Most scholars agree that reliance on the private sector to perform government tasks has been on the rise in recent years (DiIulio, 2014; Light, 2008; Michaels, 2017; Verkuil, 2017). DiIulio (2014) points out that although the number of federal bureaucrats has remained relatively constant since 1960, the amount of dollars each one oversees has increased nearly fivefold in the intervening years. This disjuncture can be explained by a decided turn to contracting out government work to both for-profit and non-profit contractors. Light (2008) estimates that there are four contractors for every one federal bureaucrat. Although less often evaluated at a systemic level, the trend is mirrored at the state and even the municipal levels (Verkuil, 2017).

Contemporary theorists often focus on the deleterious consequences of this trend. One prevailing concern is that outsourcing reduces accountability, as contractors bear no direct connection to voters. This concern is exacerbated by the extent to which contracting has become entrenched: at one defense contracting agency, more than half of the procurement specialists—who oversee the management of contracts—were themselves contractors and the government’s online database used to track contracts is also outsourced (Stier, 2009). Others note the diminished transparency associated with outsourcing, since contractors are not bound by the same restrictions as government, such as judicial review, freedom of information and disclosure laws, and sundry laws designed to promote participation and rationality in decision-making (Freeman and Minow, 2009). Finally, some worry about the broader societal impacts associated with outsourcing, such as the ability of private contractors to “cream” the easiest to serve beneficiaries of social services (leaving the harder-to-serve to an uncertain fate) or the welfare losses associated with more workers employed in the private sphere, where wages are lower, benefits are less generous, and job security is more tenuous than for those in the public employ (Donahue, 2008).<sup>2</sup>

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<sup>2</sup>However, the effects of privatization may not be as deleterious as some have feared; recent work suggests

Most political accounts trace the origins of the outsourcing trend to the presidency of Ronald Reagan, who famously proclaimed that “government is not the solution to our problem; government is the problem.” Reagan kick-started the outsourcing revolution with grandiose rhetoric, yet most of the actual outsourcing that was achieved during his tenure was primarily related to “mundane and ministerial responsibilities” (Michaels, 2017, 98). Instead, the real movement toward outsourcing gained momentum under a Democrat. President Clinton’s “Reinventing Government” initiative promoted privatization based on the belief that government should “steer” and the private sector should “row” (see Osborne and Gaebler, 1992). This push was accompanied by a government-wide National Performance Review, which evaluated each individual agency’s steering progress. President George W. Bush further entrenched outsourcing with a “competitive sourcing” initiative—which required some bureaucrats to compete with the private sector to retain their positions—along with other programs like his faith-based initiative, which encouraged reliance on private religious organizations.

The link between outsourcing and Republican leadership is logical since arguments in favor of outsourcing often hinge on market principles and limited government, two cornerstones of conservative ideology.<sup>3</sup> Yet, this link has rarely been subjected to empirical scrutiny. And, upon closer inspection, there are reasons why ideology is not a satisfying explanation for the trend. Foremost among these, on an aggregate level, outsourcing has increased in recent decades, while aggregate liberalism in the states has remained stable (Caughey and Warshaw, 2016). Additionally, conservatives and the Republican Party by no means “own” outsourcing as a governance or management tool, as President Clinton’s high profile push for privatization demonstrates. Indeed, some recent studies suggest that, while outsourcing may have had conservative roots, its ideological connection may have weakened over time

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that privatization—of charter schools at least—is not associated with lower levels of political participation (Cook et al., 2019).

<sup>3</sup>Meanwhile, liberals and Democrats are more closely associated with labor and unions.

as the method’s reputation for efficiency and cost-savings have grown (Brudney et al., 2005; Gunderson, 2018). This points to an alternative logic for the incentive for political leaders to privatize that has little to do with ideology.

Other work that takes outsourcing seriously often focuses on individual sectors, such as the military and defense settings (e.g., Avant, 2005; Stanger, 2009), “e-services” and information technology (e.g., Ya Ni and Bretschneider, 2007), or individual services provided at the local level (e.g., Becker, Silverstein and Chaykin, 1995; Chandler and Feuille, 1991; Jerch, Kahn and Li, 2016). Given the idiosyncrasies associated with individual sectors or agencies, it is difficult to generalize these findings to a broad trend that is occurring across all levels of government. The result is that we have a limited understanding—particularly in an empirical sense—of the political and institutional factors that give rise to, and perpetuate, the tendency for governments to turn to the private sector.<sup>4</sup>

## How Public Sector Unions Counter Outsourcing

Public sector unions are a powerful political force in American politics. As membership in unions in the private sector has declined markedly in recent decades, membership in public sector unions has held steady and in some areas has even increased (Wolfe and Schmitt, 2018). An emerging literature highlights the skill these entities exhibit in a range of domains, including corralling their members to vote (Moe, 2006; Rosenfeld, 2010, 2014) and to participate politically (Flavin and Hartney, 2015). The organizing power of unions is effective too; for example, some studies suggest that unions can influence the outcome of elections through both increased turnout and endorsements of specific candidates (Moe,

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<sup>4</sup>One notable exception is a study by Brudney et al. (2005) that relies on state bureaucrats’ evaluations of outsourcing at their agency, as established in a survey. They find that individual agency factors relating to the agency’s budget or to past experiences with contracting, and not institutional state-level factors, do a better job of explaining agency-level outsourcing decisions. However, agency level explanations do not speak to the broader trend happening across the states.

2006, 2011).

Government spending is a key focus of scholarship on public sector unions. But the question is usually whether public unions affect the overall *size* of government or, more specifically, whether strong unions lead to bloated government spending. Empirically speaking, the findings are mixed, with some arguing that unions are associated with higher spending levels (e.g., Anzia and Moe, 2014) and others suggesting they are not (e.g., Crowley and Beaulier, 2018; Paglayan, 2018). However, decisions to outsource are independent of the size of government; the decision to outsource is a decision about who will perform work, rather than whether the work will be performed in the first place.<sup>5</sup>

Ultimately, outsourcing is a choice between government bureaucrats and contracted workers in the private sector. When a task is outsourced there are clear winners (private sector contractors) and clear losers (bureaucrats who would otherwise have performed the work). Unionized public sector workers thus have an incentive to fight to keep their jobs and to prevent the government from further outsourcing work.<sup>6</sup> In the words of Anzia and Moe (2019), these groups function as “interest groups on the inside.” Operating from a vantage point *within* bureaucratic agencies, they are uniquely positioned to advance their particularistic interests.

For their part, unions pay close attention to outsourcing and consider it central to their policy agenda. There are several avenues by which these actors can potentially influence decisions to outsource. First, when unions negotiate contracts with government management they can include provisions that limit when government services can be contracted away from

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<sup>5</sup>To wit, the measure of outsourcing I deploy later in this paper enjoys a relatively low level of correlation with total government spending ( $\rho = 0.28$ ).

<sup>6</sup>Of course, public administration scholars have long argued that unions provide an important counter-pressure to contracting out services, particularly at the municipal level (Becker, Silverstein and Chaykin, 1995; Chandler and Feuille, 1991; Ferris and Graddy, 1986). Yet these observations are disconnected from broader arguments about ideology and political power.

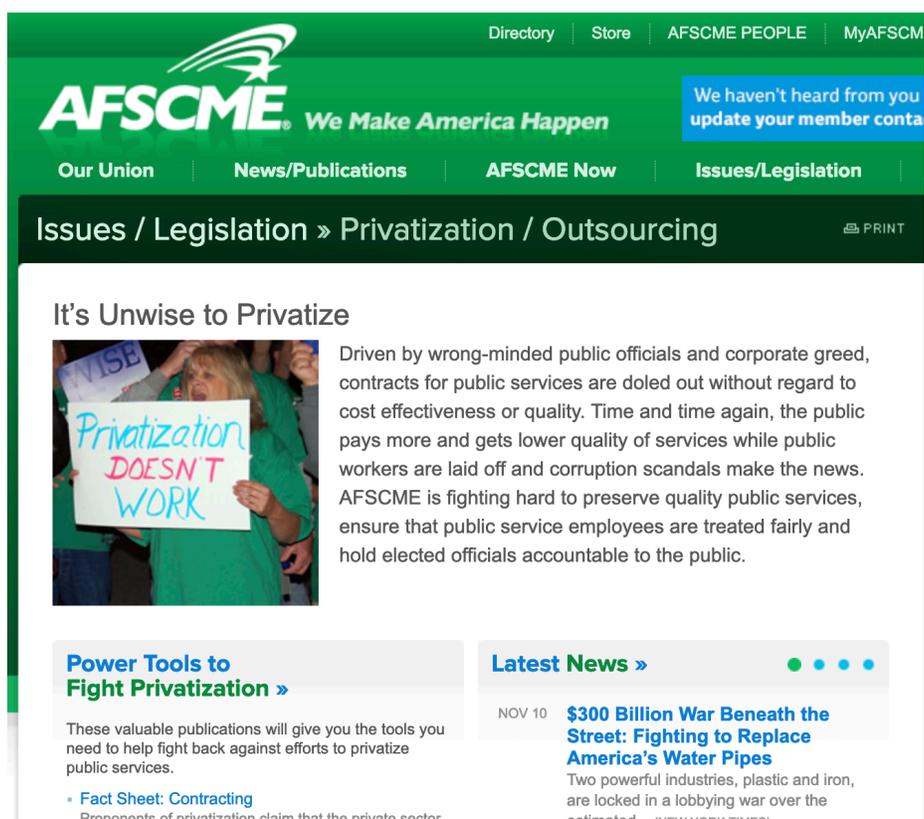
public employees, such as stipulations that grant unions special access to the government’s decisionmaking process. For instance, the current contract between the Defense Finance and Accounting Service (DFAS), a federal agency, and its union, includes seven provisions pertaining to the contracting out of work. These provisions require the agency to allow the union to participate in any studies of the commercial potential for union work, to notify the union in advance of its decision to contract out, to alert the union about site visits by potential bidders and allow the union to participate in such visits, and, if work is contracted out, to give union employees the right of first refusal for employment openings created by the contractor (DFAS, 2014). These kinds of provisions are fairly standard in union-agency contracts.<sup>7</sup>

A second avenue by which unions can affect outsourcing decisions is through member mobilization. Many public sector unions consider fighting job outsourcing to be a key member action item. Figure 1, a screenshot of the webpage for one of the largest public sector unions, illustrates the position of unions with regard to outsourcing—one section heading reads “it’s unwise to privatize” and includes a photo of a woman holding a sign stating “Privatization doesn’t work.” In addition to including links to facts sheets and news articles, the page also states the union’s position on outsourcing: “contracts for public services are doled out without regard to cost effectiveness or quality. Time and time again, the public pays more and gets lower quality of services while public workers are laid off and corruption scandals make the news.” Union members can take these agenda items and information points into rallies, meetings with government managers, agency officials and legislators, or interviews with the press.

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<sup>7</sup>On an individual level, public employees may use their influence to steer government away from the private sector. Previous research suggests that public sector employees are disproportionately opposed to government privatization (Fernandez and Smith, 2006, but see Bhatti, Olsen and Pedersen (2009)). The personal beliefs of these employees may potentially infiltrate their professional activities, such as when they oversee contracts or engage in strategic organizational planning.

Figure 1: Public Sector Unions Actively Lobby Against Outsourcing



*Note:* Screenshot of webpage from the American Federation of State, County and Municipal Employees, one of the largest public sector unions, showing member tools available to fight privatization.

Lobbying and campaign contributions present other avenues for public sector influence. For instance, public sector unions regularly endorse candidates and give money in elections where their interests are at stake. As Crowley and Beaulier (2018) explain, “political contributions in support of candidates are perhaps the most direct method for influencing elections available to public unions; in other words, it is the union’s way to ensure a preferred candidate is elected.” While unions have historically been associated with Democrats, public sector unions do give to legislators of both parties who sit on key committees relating to budgets and agency affairs (CRP, 2019). In turn, legislators that receive support from unions may be more inclined to oppose the outsourcing of services.

Finally, unions can rely on the courts as a way to stymie outsourcing efforts. Fer-

nandez and Smith (2006, 360-1) explain, “the courts have awarded monetary damages and back pay to displaced employees when they have found that the government acted illegally or improperly when contracting out a service or function.” The threat of a “prolonged and costly legal challenge” may therefore lead government to avoid pursuing further outsourcing opportunities if the threat of a union suit is likely.

Stepping back, the implication is clear: public sector unions have the means and the motive to counter outsourcing. However, these actors may not always have the same opportunity to engage in these activities. Not all workers can join or choose to join unions and, even then, cultural norms or legal restrictions in the states may limit the power of unions. Thus, only when their strength is relatively robust will public sector unions be in a position to effectively block outsourcing.

Of course, when states keep service provision in-house, actors in the private sector who would have benefited from contract awards lose. In contrast to public sector unions, however, this is a diffuse set of actors, including both for-profit and non-profit organizations. As a result, while these actors have an incentive to pressure states to engage in more outsourcing, this pressure may come in the form of lobbying on individual issues or contracts, rather than via a unified effort to counter outsourcing per se.

## Measuring State Outsourcing of Services

To evaluate the political components of outsourcing, I create a new annual measure of service outsourcing levels by state governments from 1992-2015.<sup>8</sup> Specifically, I extend the

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<sup>8</sup>While this measure has many advantages, what it lacks is consideration of the *numbers* or *types* of services that are being assigned to the private sector. With respect to type, recent work finds that state government spending is increasingly allocated toward redistribution and welfare-oriented goals (Grumbach, 2018), suggesting that the growth in outsourcing may also be concentrated in these areas. Identifying particular sectors and services where outsourcing is more likely is a promising avenue for future research.

“chipping away” approach developed by Minicucci and Donahue (2004). Starting with a slice of annual state government expenditures, the measure deducts any spending not associated with services, as expressed in the following equation:

$$\text{Service Outsourcing}_{it} = \frac{\text{Operating Spending}_{it} - \text{Compensation}_{it} - \text{Goods}_{it}}{\text{Operating Spending}_{it}} \quad (1)$$

where  $i$  indicates a state and  $t$  a particular year. The intuition behind this approach is that the residual represents the proportion of all state spending on services, or “outsourcing.” The Organisation for Economic Cooperation and Development uses a variant of this approach to compare government outsourcing cross-nationally (OECD, 2011).

The base of current spending on operations includes consumption spending for employees, as well as spending on goods and contractual services.<sup>9</sup> It excludes spending on items like interest payments, inter-governmental transfers, construction and other investment spending. From this base, I deduct spending on salaries and benefits of state employees ( $\text{Compensation}_{it}$ ), as well as spending on durable and nondurable goods, which removes purchases of things like fuel supplies and non-capital equipment. While the equation itself is intuitive, it relies on the collection of data from a variety of sources, including the Census Bureau, the Bureau of Labor Statistics, and the subsequent analysis of this data (e.g., determining the appropriate amount of funds spent on state employees including both benefits and wages); further details about the data and the measure can be found in the Supporting Information (SI).<sup>10</sup>

By way of illustration, consider how the transition from having a traditional public

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<sup>9</sup>The operating spending figure is from the Census of Governments. Specifically, it includes “direct [expenditures] for compensation of own officers and employees and for supplies, materials, operating leases, and contractual services except amounts for capital outlay.”

<sup>10</sup>All dollar amounts are expressed in real 1992 dollars.

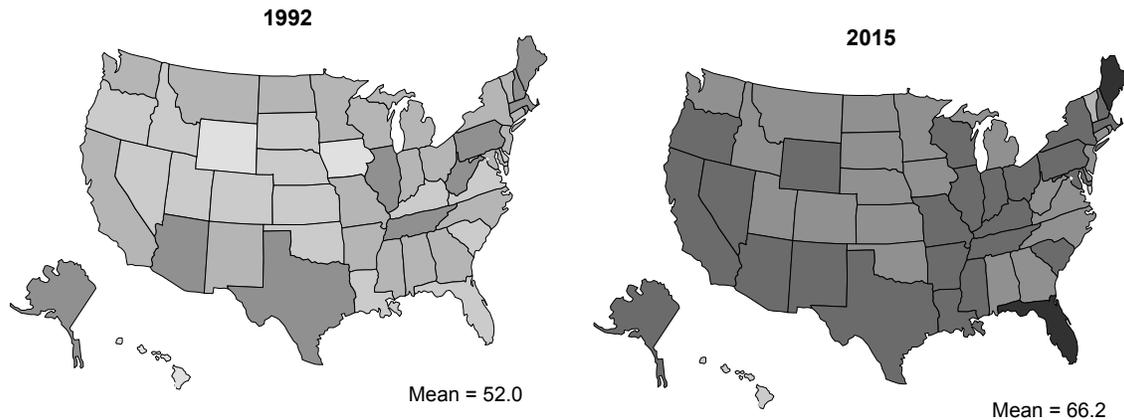
school to having a charter school—one form of outsourcing—is treated in this method. If a state opts to keep the school public, meaning that the teachers remain public employees, then their salary and benefits will be deducted from the base (i.e., they will be counted under the Compensation term). Spending on textbooks and desks, for example, will also be deducted from the numerator, as durable goods under the Goods term. Now, consider what happens if that same school becomes a charter school. The teachers and other service providers are no longer public employees (strictly speaking), but now are private employees of the organization operating the charter. Under Equation 1, their salaries are no longer subtracted from the spending base, but instead are captured by a higher level of outsourcing. Similarly, the relevant goods spending would move to the lefthand side of the equation.

The resulting measure shows that states engage in a considerable amount of service outsourcing; the mean level of outsourcing across all states and years is 61.1% of services (std. dev. = 8.25%), with a low of 28.6% in Delaware in 2004 and a high of 86.3% in Nevada that same year. Figure 2 shows outsourcing levels across the states at two distinct points in time. As anticipated, the trend across the states is toward increasing levels of outsourcing over the study’s time period, a finding that comports with that of many observers (DiIulio, 2014; Michaels, 2017; Verkuil, 2017).<sup>11</sup> This provides some reassurance in terms of face validity.

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<sup>11</sup>See Figure A-1 in the SI for individual state-level trends.

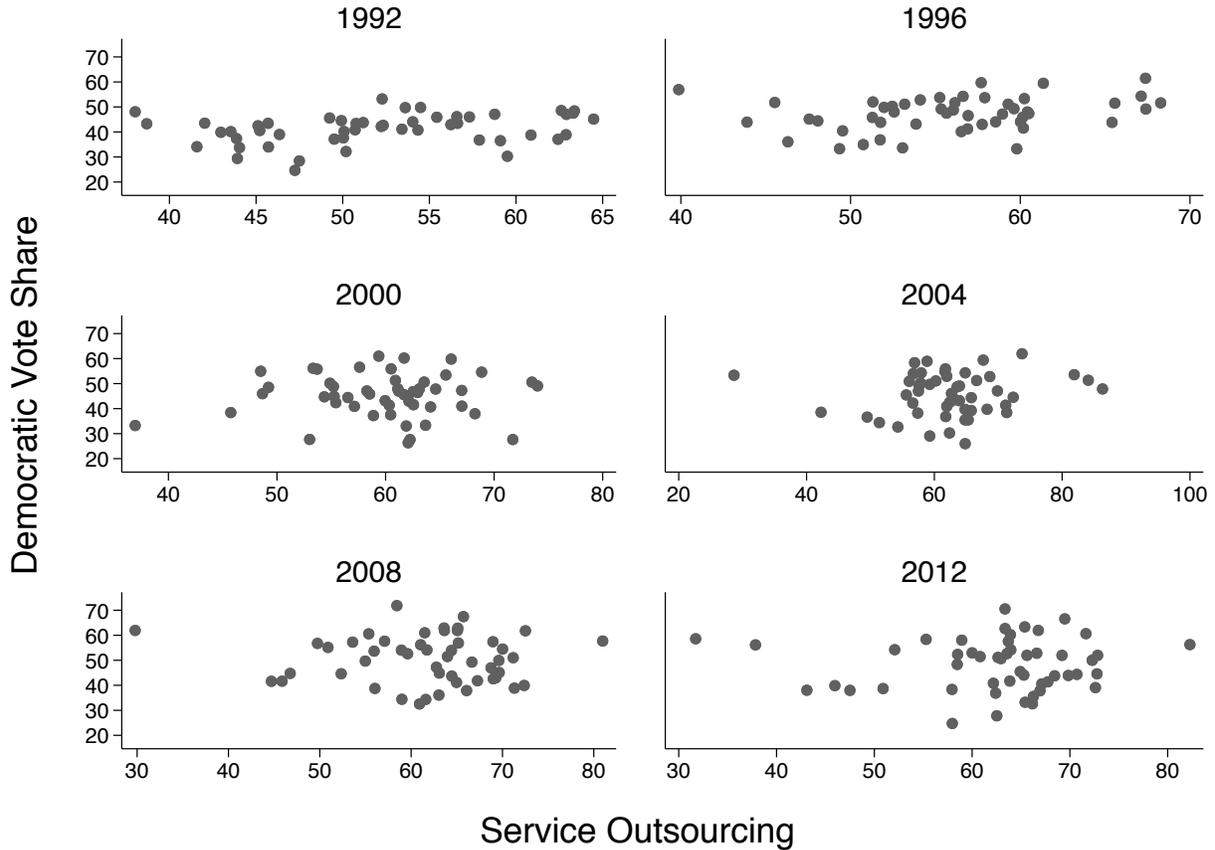
Figure 2: Service Outsourcing in the States, 1992 and 2015



*Note:* The left map shows outsourcing levels in the states in 1992, while the right map shows levels in 2015. Darker shades indicate higher levels of outsourcing.

Figure 2 also reveals an interesting pattern with regard to service outsourcing. So-called “red states” are not the only bastions of outsourcing. For instance, in 2015, Florida and Maine engaged in the highest levels of outsourcing; the following year, the former voted for President Trump—by only a 1-point margin over Hilary Clinton—and the latter chose Clinton over Trump by a 3-point margin. Additionally, as shown in Figure 3 there is no systematic relationship between presidential vote share for Democratic presidential candidates and the level of observed outsourcing in a state in that year. This point is further reinforced by evaluating the relationship between the service outsourcing measure and other policies that might be considered liberal or conservative; there is very little correlation ( $\rho = 0.02$ ) between *Service Outsourcing* and Caughey and Warshaw’s (2016) measure of state economic policy liberalism, which is based on an aggregate evaluation of more than 150 individual state-level policies.

Figure 3: Outsourcing by Democratic Presidential Vote



*Note:* Scatterplots showing no systematic relationship between Democratic vote share and Service Outsourcing for each of the presidential elections in the time series.

The regions have broadly followed the same pattern of increasing outsourcing, with some slight variations, as Figure A-2 in the SI illustrates. States in the Northeast were early adopters of outsourcing, while western states were late adopters and have lagged the other regions in more recent years. Notably, the South—which is often given special consideration in American politics and might be considered ripe for outsourcing given its conservative ties—does not stand out in an appreciable way.

Although there are few alternate measures of service outsourcing and none on the scope of the one introduced here,<sup>12</sup> the measure comports well with those that do exist.

<sup>12</sup>There have only been a handful of attempts to measure the outsourcing of government services. With

For example, in 2012, the State of Nebraska commissioned a comparative study to examine state outsourcing of government services (Goss and Morse, 2012). The measure employed in that study relies on similar formula to the one employed here although it is based on total agency expenditures and focuses only on salary (excluding benefits and payments for goods). Nevertheless, as shown in Figure A-3, the two measures correlate reasonably well.

## Unions and State Outsourcing Decisions

With the measure of service outsourcing in hand, it is possible to evaluate the effects of unions on outsourcing decisions. All states have public sector unions, but the strength of those unions varies in terms of the number of workers they represent. Unions that represent a greater proportion of workers are believed to exercise more clout. The primary measure of union strength that I include is *Union Coverage*, the proportion of a state’s public sector workers who are covered by a collective bargaining agreement. However, as an alternate measure, in some models I include *Union Density*, which is the proportion of public sector employees who are members of the union compared to all public sector employees in the state.<sup>13</sup>

To systematically evaluate the role of unions in outsourcing decisions, I estimate the following two-way fixed effect model with lagged dependent variables:

$$y_{it} = \beta \text{Union}_{i,t-1} + \sum_{l=1}^L \delta_l y_{i,t-l} + \alpha_i + \xi_t + \epsilon_{it}, \quad (2)$$

where subscript  $i$  denotes the state, and  $t$  denotes the year. Here,  $\beta$  is a regression coefficient,

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the exception of the Nebraska study discussed here, the extant measures focus on individual agencies or individual sectors (e.g., Cook et al., 2019). Often such studies rely on methods that are not replicable on a broader scale, such as surveys of bureaucrats (e.g., Brudney et al., 2005) or proprietary estimates of the number of contractors employed (Light, 1999).

<sup>13</sup>The data underlying both measures are from Hirsch and MacPherson (2003); see [www.unionstats.com](http://www.unionstats.com).

$y_{i,t-1}$  is a state’s level of outsourcing in the year prior to  $t$ , the  $\alpha_i$  are state fixed effects, the  $\xi_t$  are year fixed effects, and  $\epsilon_{it}$  is an error term. I include a lagged measure of union strength, since I assume it may take time for political actions to be reflected in state contracts, given the slow pace of the government contracting process. This specification can be interpreted as comparing different years within the same state and estimating the difference in the yearly change in outsourcing with respect to whether the public sector unions are relatively strong or relatively weak for that state. I use ordinary least squares to estimate the models and cluster the standard errors by state to correct for autocorrelation within states over time.<sup>14</sup> This dynamic panel model approach offers an advantage over a model that includes state fixed effects alone since past levels of outsourcing are likely to vary within state in ways that state-specific fixed effects cannot capture.

The results are shown in Table 1, which shows the models with and without a set of state-level covariates.<sup>15</sup> A substantial proportion of the variation in the data is absorbed by the inclusion of both the state and year fixed effects, as well as the two lag terms. To interpret the substantive impact of *Union Coverage*, it is therefore necessary to consider the within-unit variation (i.e., how much *Union Coverage* typically varies within, rather than across, states). Following Mummolo and Peterson (2018), I consider a plausible counterfactual scenario that takes into account the average within state-year variation in this variable.<sup>16</sup> This approach suggests that a change from one adjusted standard deviation below the mean level of *Union Coverage* to one adjusted standard deviation above the mean results in a reduction of approximately 1.2% in terms of *Service Outsourcing* (Model 1). This change accounts for

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<sup>14</sup>One potential concern with this approach is that the dependent variable *Service Outsourcing* is bounded between 0 and 100. Yet, these bounds are not binding, as in no case does the measure approach them, making OLS an appropriate modeling technique.

<sup>15</sup>I omit a substantive discussion of the control variables here, since there is little by way of systematic patterning that emerges from the analysis.

<sup>16</sup>In other words, I adjust the calculation of the standard deviation to consider the types of movement in *Union Coverage* that occur within states, an adjustment which substantially narrows the variance compared to an analysis that considers the variation across all states and all years.

about 25% of one standard deviation in the outsourcing measure. While these effects appear small on their face, they represent potentially major policy changes and financial windfalls. For example, in a big state like California, a change of this size in an average year is equated with approximately \$6.6 billion moving from the public to the private sector; in a smaller state like Vermont, however, the change is much more modest in scale, amounting to about \$26 million in any given year.<sup>17</sup>

Table 1: Effects of Union Strength on Outsourcing Decisions

	(1)	(2)	(3)	(4)	(5)	(6)
Union Coverage	-0.099*** (0.036)	-0.099*** (0.037)				
Union Density			-0.071* (0.035)	-0.073* (0.036)		
Labor Contributions					-0.001*** (0.0003)	-0.001 (0.0002)
Outsourcing t-1	0.750*** (0.044)	0.748*** (0.046)	0.753*** (0.044)	0.751*** (0.046)	0.746*** (0.046)	0.743*** (0.049)
Outsourcing t-2	-0.085 (0.043)	-0.081 (0.043)	-0.085 (0.044)	-0.081 (0.044)	-0.110*** (0.047)	-0.105*** (0.047)
Observations	1,100	1,100	1,100	1,100	966	966
R-squared	0.814	0.817	0.813	0.817	0.799	0.803
Controls	NO	YES	NO	YES	NO	YES
State & Year FE	YES	YES	YES	YES	YES	YES
States	50	50	50	50	50	50

*Note:* \*\*\* p<0.001, \*\* p<0.01, \* p<0.05. Robust standard errors clustered at the state level are in parentheses. FE = fixed effect. For full models showing the control variables see Table B-1 in the SI.

Models 3 and 4 employ the *Union Density* measure. The results here suggest a somewhat smaller, but still substantively meaningful effect; a change from one adjusted standard deviation below the mean level of *Union Density* to one adjusted standard deviation above the mean results in a reduction in *Service Outsourcing* of approximately 0.5%.

The final two columns of Table 1 explore the role of campaign contributions as a

<sup>17</sup>Figures calculated based on mean values of *Operating Spending* for each respective state; see Section A of the SI.

mechanism by which public sector unions can influence outsourcing decisions. Specifically, I include *Labor Spending*, which is the change in campaign contributions made by the labor sector to candidates for state office in the state over the prior year, according to the National Institute on Money in State Politics. While this measure includes financing by private sector labor unions in addition to public sector ones, private sector unions often work to counter the political influence of business interests (Witko and Newmark, 2005), suggesting that in terms of outsourcing decisions both types of unions may share interests. Here again the substantive effect is small but meaningful; moving from one within-unit standard deviation below the mean level of *Labor Spending* to one within-unit standard deviation above the mean results in a reduction in *Service Outsourcing* of approximately 0.3% (Model 5).<sup>18</sup>

All told, these models suggest that public sector unions are influential in convincing state governments to keep work in-house. As I show in the SI, these findings are robust. The results do not hinge on the inclusion of lags of the dependent variable or the inclusion of year fixed effects (Table B-2), or to excluding the South from the analysis (Table B-3). Additionally, the results relying on labor spending are consistent with campaign contributions as one way that groups can affect change, although I do not rule out a role for member lobbying, contract provisions, or litigation as alternate routes of union influence.

## Alternative Explanations for Outsourcing

Historically, public sector unions have not been an important focal point in studies of outsourcing. The focus instead has been on other sources of pressure, often with little explicit discussion of how those forces are expected to contribute to more or less observed outsourcing. Below I articulate the rationale and develop empirical tests for three of the chief explanations—party and ideology, fiscal need, and divided government. While these are by no means the only factors associated with the decision to outsource, they represent

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<sup>18</sup>In Model 5, the coefficient for *Labor Contributions* is significant at the  $p < 0.1$  level.

the most commonly offered explanations for the broader trend.

## Party and Ideology

The logic connecting outsourcing to conservatives and the Republican party is straightforward. Republican (or, depending on the argument, conservative) leaders pursue private sector relationships based on a belief that a smaller government modeled on market principles is more desirable than public sector provision.

In considering how partisanship and ideology might infiltrate state outsourcing decisions, the governor is a logical focal point. As a state’s chief executive, the governor is influential in affecting policy, and spending decisions in particular (Kousser and Phillips, 2012; Berry and Fowler, 2018). Since prior research suggests that the partisanship of leaders also can affect aggregate levels of spending (de Benedictis-Kessner and Warshaw, 2016), it is not a stretch to extend that logic to how monies are allocated. Indeed, one government report on privatization found that across a slew of states the governor was the “political champion” of outsourcing efforts (General Accounting Office, 1997, 9). This leads to the expectation that when states are led by a Republican governor, levels of outsourcing should increase, as these governors pursue private sector solutions.

Model 7 in Table 2 tests this expectation. It shows the relationship between *GOP Governor*, a dummy indicating whether the governor was a Republican, and outsourcing. The sign on the coefficient is negative, suggesting that Republican governors engage in *less* outsourcing—although this result is not statistically significant. Model 8 takes a different tack by including *Governor Ideology*, a continuous measure of each governor’s ideology as indicated from Bonica’s (2013; 2014) campaign finance (CF) scores.<sup>19</sup> Here, a large and positive CF score indicates a more conservative leader, and a negative one indicates a more

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<sup>19</sup>Bonica’s widely-cited CF measures of ideology use millions of campaign finance contributions from across the political landscape to generate estimates of ideology for leaders at numerous levels of government.

liberal leader. Again, *Governor Ideology* carries a negative sign—suggesting that more conservative governors are associated with lower levels of outsourcing—and again it fails to achieve statistical significance.

Of course, in a separation of powers system the governor must contend with other actors in the political system. For instance, the governor can work with the state legislature to pass legislation that either promotes (or inhibits) outsourcing. As Ya Ni and Bretschneider (2007) explain, “the dominant party affiliation of a legislative body can affect contracting out decisions as legislatures with more conservative values representing stronger ties to private sector businesses tend to favor contracting out, while political parties representing low-income workers and unions tend to oppose the practice.”

Accordingly, in Model 9 I incorporate measures indicating the partisan control of the state’s upper and lower chambers, respectively *GOP House* and *GOP Senate*. I also include a dynamic state-year measure of the economic policy liberalism of the mass public. This measure, developed by Caughey and Warshaw (2018), is based on hundreds of public opinion polling questions and captures the extent to which a state’s population is more supportive of economically liberal policies. If pressure to outsource is coming directly from voters themselves, we should see a negative and statistically significant coefficient for *Mass Economic Liberalism*. Despite the strong theoretical priors with respect to other actors in the political system, the results in Model 9 do not provide support for the expected effects with respect to *GOP House*, *GOP Senate*, or *Mass Economic Liberalism*.

In Table B-4 in the SI, I consider the possibility (introduced previously) that the ideological roots of outsourcing may have decayed over time. I split the time span covered by the analysis into three equal periods and interact the partisanship of the governor with each of the time periods. If outsourcing has become less ideological over time, then one might expect it to have a positive and statistically significant coefficient in the earlier period, and a declining or null effect in later periods. I find no support for this hypothesis.

Table 2: Alternative Factors Affecting State Outsourcing Decisions

	(7)	(8)	(9)	(10)	(11)	(12)	(13)
GOP Governor	0.076 (0.293)		0.156 (0.287)				
Governor Ideology		0.011 (0.207)					
GOP House			-0.071 (0.480)				
GOP Senate,			0.224 (0.340)				
Mass Econ Liberalism			-1.121 (1.534)				
Debt % GSP,				0.047 (0.133)			
Unemployment Rate				-11.881 (21.261)			
Unemployment % change				-0.122 (1.253)			
Income per capita				-0.000 (0.000)			
Income per capita % change				-3.394 (9.894)			
Budget surplus				0.152 (0.083)			
Fraction of ARC paid					0.039 (0.137)		
Business Bias						-0.200 (1.011)	
Divided Government							0.166 (0.310)
Union Coverage	-0.099*** (0.038)	-0.104*** (0.042)	-0.086*** (0.037)	-0.099 (0.051)	-0.111*** (0.054)	-0.089 (0.046)	-0.100*** (0.038)
Observations	1,100	1,031	1,078	850	683	900	1,100
R-squared	0.817	0.813	0.816	0.818	0.795	0.824	0.817
Outsourcing t-1	YES	YES	YES	YES	YES	YES	YES
Outsourcing t-2	YES	YES	YES	YES	YES	YES	YES
Controls	YES	YES	YES	YES	YES	YES	YES
State & Year FE	YES	YES	YES	YES	YES	YES	YES
States	50	50	49	50	49	50	50

*Note:* \*\*\* p<0.001, \*\* p<0.01, \* p<0.05. Robust standard errors clustered at the state level are in parentheses. Model 9 excludes Nebraska, which has a unicameral legislature. Model 11 excludes Utah (all years) and Indiana (some years) since ARS reporting data was not available. Control variables include: state population, the partisanship of the governor (omitted in Model 9), divided government (omitted in Model 8), and the state unemployment rate; omitting these controls does not change the substantive takeaways. FE = fixed effect.

## Fiscal Need

A second alternative explanation is tied to state financial factors; outsourcing is often associated with cost savings and, as a result, governments may turn to it more during times of fiscal distress. As Freeman and Minow (2009, 8) explain “private companies are simply more effective than government—more ‘nimble’—and therefore more capable of responding to rapidly changing events.” The logic of cost savings is tied to the competition that occurs before a service is outsourced; by holding a procurement competition, getting bids from an array of vendors, and awarding a contract to the lowest bidder, market forces ensure that the government is getting a good deal for its money. It follows then that governments may farm out work in times of fiscal crisis as a way of capitalizing on private sector efficiencies.

In Model 10, I include several indicators of a state’s economic condition: debt as a percentage of GSP, the unemployment rate, the percentage change in the unemployment rate, income per capita, the percentage change in income per capita, and a lag of the state’s budget surplus.<sup>20</sup> None of these indicators of fiscal stress achieve statistical significance. While there may be some concern about the collinearity of these variables, modeling them individually does not affect the results.<sup>21</sup>

In recent years, retirement plans for public sector workers have become more underfunded, placing increasing pressure on state budgets (Anzia and Moe, 2019). In Model 11, I consider whether the financial stress imposed by state pension liabilities may deter states from additional reliance on bureaucrats. The variable *Fraction of ARC paid* represents the Annual Required Contribution (ARC)—the amount that the state must pay to amortize the existing pension obligations plus its outstanding pension debt—as a percentage of the state’s

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<sup>20</sup>Measures of state economic health follow Table 5.2 in Kousser and Phillips (2012)

<sup>21</sup>In some specifications, the budget surplus variable is positive and statistically significant, suggesting that having excess funds is associated with an increased tendency toward outsourcing. While not a robust relationship, this is worth exploring in terms of the types of services that get outsourced and whether outsourcing can be thought of as a luxury good in some contexts.

revenues.<sup>22</sup> If daunting pension obligations make private sector options more attractive, then this variable should have a positive sign. While this expectation is realized, as the results in Model 11 shows, the coefficient is not statistically different from zero.

Finally, I consider whether some states are just more open to business than others and whether that predilection explains outsourcing decisions. Model 12 includes a measure of the bias of a state's campaign finance system towards more organized and monied interests. This measure, developed by Witko (2017), is based on the difference in the number of for-profit high-income groups that gave campaign contributions to candidates for state office and the number of non-profit and labor groups that participate in that same way. Higher values of *Business Bias* suggest that a state's campaign finance system is more biased towards the former groups. Again, however, the results fail to provide support an interpretation that bias in a state's campaign finance system results in greater outsourcing.

In Table B-4 in the SI, I explore whether there is a conditional relationship between governor ideology and the fiscal measures on the logic that perhaps only Republican governors turn to outsourcing in the face of this pressures. However, I find no evidence of an interactive relationship between the governor's party and any of these indicators.

## Divided Government

Divided government is another factor to consider in the outsourcing environment. Prior research suggests that under divided government, legislatures are more likely to delegate work to independent agencies and commissions, whereas under unified government legislatures delegate more to executive agencies (Epstein and O'Halloran, 1999). To the extent that legislatures are a driving force in outsourcing decisions, this logic extends cleanly

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<sup>22</sup>The ARC is calculated according to standardized accounting rules. Data are from the Public Plans Database from the Center for Retirement Research at Boston College. See Anzia and Moe (2019) for more insight into the politics of pension liabilities.

to the outsourcing domain and we should see greater reliance on the private sector under divided government. To test this, I include a dichotomous measure of whether or not the state's government was divided in a given year. Model 13 in Table 2 shows the results; while the coefficient carries the expected positive sign, it fails to achieve statistical significance.

In sum, across all of these specifications the null results do not support the idea of a robust and systematic role for Republican or conservative leadership, for financial pressures or biases, or for divided government as explanations for outsourcing trends. Of course, these results should be interpreted with caution. The time series for this analysis begins in 1992 and it is certainly possible that outsourcing had stronger connections to these influences in earlier years. Additionally, it may be the case that these institutional factors all have a more nuanced relationship with outsourcing levels, a possibility that future work should seriously consider. Nevertheless, in contrast to the results on union strength, little evidence emerges of a strong and consistent direct effect for these alternate explanations.

## Analyzing Union Retrenchment Laws

One potential concern with the results presented to this point is that the strength of a state's public sector unions is correlated with many other aspects of that state's policies and politics. It is thus difficult to disentangle whether union strength—or some other unknown, omitted factor—underlies a state's outsourcing decisions. To further assess the effects of public sector union strength on outsourcing decisions, I therefore consider legal changes that affect the relative power of a state's unions.

In recent years, numerous states have adopted laws that rescind or limit the powers of public sector unions. For example, during the time period under study two states—Indiana and Michigan—adopted “right to work” (RTW) laws for their public sector unions, a legal change which prohibits unions from forcing all workers covered by a union agreement to

join the union or pay dues.<sup>23</sup> Another two states—Indiana and Wisconsin—passed laws that prevented public sector unions from engaging in collective bargaining.<sup>24</sup> These types of legal changes drain unions of their strength, by reducing union membership and sapping the organizing power of members (e.g., Ellwood and Fine, 1987; Eren and Ozbeklik, 2016), and that their passage should be associated with higher levels of outsourcing to the private sector in the affected states.

To probe the effect of legal changes regarding union power on state outsourcing decisions, I give close scrutiny to “Act 10,” Wisconsin’s union restricting law. In 1959, Wisconsin became the first state to offer collective bargaining to its public sector employees. However, in 2011, Republican governor Scott Walker proposed to rescind these protections, as part of a platform intended to balance the budget and reform the way government works (Walker, 2011). The proposal gained sustained national attention, as state employees, who were strongly opposed, staked out the capitol in Madison and engaged in weeks-long protests involving more than 100,000 protestors. In the end, Walker and a unified Republican legislature succeeded in passing a law that not only removed the public sector employees’ collective bargaining rights, but also further circumscribed union power by mandating annual recertification elections and eliminating automatic paycheck deductions for dues collection. If these legal changes weakened the state’s unions, then following my earlier argument this change should be reflected in Wisconsin’s aggregate outsourcing levels after the law’s passage.

To evaluate the impact of this shift, I rely on the Synthetic Control Method (SCM), a causal inference technique that allows the researcher to systematically select comparison units

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<sup>23</sup>An additional two states—West Virginia and Kentucky—adopted RTW laws in the years after the close of the study’s time period.

<sup>24</sup>For a variety of reasons, it is not possible to evaluate all of these union retrenchment cases using the analytical approach deployed in this section. For instance, Indiana eliminated collective bargaining for its state employees in 2005. However, the Indiana case is not a viable case because the state suffered a considerable post-treatment change to its outsourcing program following a widely publicized scandal involving a large contract with IBM (see Erickson, 2011).

in order to estimate the effect of a specific intervention (Abadie, Diamond and Hainmueller, 2010, 2015). Using this method, it is possible to construct a counterfactual scenario wherein one estimates the level of outsourcing *had Wisconsin not changed its collective bargaining law*. If union strength is indeed an important impediment to state outsourcing decisions, the level of outsourcing in Wisconsin should be lower under the synthetic counterfactual (where unions retained their strength) than under the actual level of outsourcing (where union power was sapped via the changes in the bargaining law). Wisconsin is an ideal case to evaluate the effect of this legal changes, since Act 10 was passed in the latter-half of the outsourcing time series, allowing for considerable time in the pre-treatment period.

Specifically, the treatment in this case is Wisconsin’s legal rescission of collective bargaining rights for public sector unions and the pool of donor cases is restricted to a set of donor pool states in which collective bargaining was legal during the entirety of the study’s time period. For public sector workers, collective bargaining is often granted on a sector-by-sector basis. To develop a list of appropriate states, I thus rely on the set of states for which collective bargaining was legal for firefighters, police, and teachers, which results in a set of 33 comparison states.<sup>25</sup> Building on a set of covariates for each state, the SCM approach identifies similarities between the treatment state and the donor states during the pre-treatment period. These similarities are then used to generate a synthetic counterfactual unit for the treatment state that is a weighted combination of the component control states.

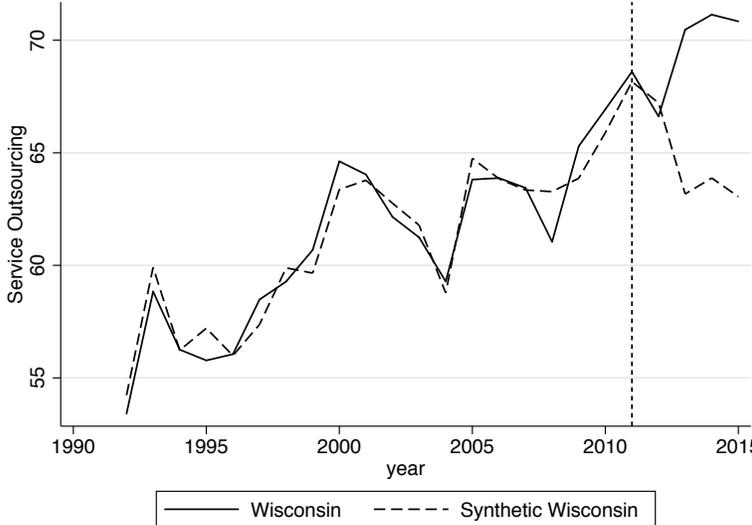
Figure 4 shows the results of this approach, illustrating the synthetically generated level of outsourcing in Wisconsin pre- and post- adoption of Act 10, in contrast to the actual

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<sup>25</sup>See Table 1 in Sanes and Schmitt (2014) for a list of collective bargaining by sector for each state. In addition, following general SCM practices, I exclude an additional five outlier states. The states in the donor pool are: Alaska, California, Delaware, Florida, Hawaii, Idaho, Illinois, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Minnesota, Missouri, Montana, Nevada, New Hampshire, New Jersey, New Mexico, New York, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Dakota, Utah, Vermont, Washington, and West Virginia.

levels of outsourcing observed in Wisconsin during these periods. Notably, had Wisconsin not adopted this law, based on a control group generated by peer states, it is predicted to have experienced a drop in outsourcing levels. However, the state actually saw a substantial increase in outsourcing following the adoption of Act 10, a pattern in keeping with the expected effects of this policy change. The differences between synthetic Wisconsin and real Wisconsin are not statistically different in the initial two years, but after the third year these differences become distinguishable (see Figure C-2). The implication is that it may have taken a short time for the effects of Act 10 to achieve a meaningful effect; this lag period makes sense given that it takes time to complete existing public sector projects, initiate the procurement process, and undertake new contracts with the private sector.

Figure 4: Evaluation of Wisconsin’s Act 10 Using SCM



*Note:* The dotted line shows the results from synthetic Wisconsin, while the solid line shows actual outsourcing levels in Wisconsin.

Overall, these results suggest that outsourcing in Wisconsin increased considerably in the period after the adoption of Act 10; specifically, over the period from 2012-2015, outsourcing increased 3.1% per year on average, which amounts to an increase of 5.7% over the 2011 baseline.

Following Abadie, Diamond and Hainmueller (2015), I adopt a different year for the intervention, assuming that Act 10 had been adopted approximately halfway through the time series. The results of this in-time placebo test are shown in Figure C-3, and demonstrate that there is not a clear break in outsourcing levels. I also conduct an in-space placebo test where each of the donor states is iteratively treated as having had the same legal intervention. Each treated donor state is then compared with an iteratively constructed synthetic counterfactual and the effects, shown in Figure C-4, demonstrate that in no state is the effect as large as in Wisconsin. Finally, Abadie, Diamond and Hainmueller (2010) recommend evaluating the distribution of the ratio of post/ preintervention mean squared prediction errors (MSPEs). If the ratio for Wisconsin is unusually large, then we can infer that Act 10 had an impact on outsourcing levels. The ratio of most states is less than 1, whereas in Wisconsin value is closer to 3; the probability of obtaining the ratio as large as Wisconsin is therefore  $1/33 = .03$ . These analyses help to increase confidence that the results shown for Wisconsin's are attributable to the adoption of that state's collective bargaining law.

The evidence from the removal of collective bargaining protections in Wisconsin shows that moves that weaken union power have exacerbated the tendency for states to rely on the private sector for service provision. Overall, this suggests that although strong public sector unions can stem the outsourcing tide, they are not infallible. When states take action to limit these unions' power, outsourcing levels respond in kind.

An important consideration for future research is why states adopt these laws in the first place. Of the eight anti-union state laws discussed earlier, all but one were adopted under a Republican governor. This introduces the possibility that these types of policies may gain more traction with Republican leaders, offering a different perspective on the null findings with respect to ideology and partisanship reported earlier. Rather than a systematic pursuit of all Republican governors, outsourcing may be addressed by individual governors that make big policy changes with respect to unions that considerably alter a state's outsourcing

trajectory. Indeed, as (Moe, 2011) documents, the rise of teachers unions in many states was associated with a concerted effort by Democratic groups to enact collective bargaining laws; it may be the case that business interests concerned about outsourcing issues work through Republican leaders to adopt major policy shifts pertaining to public sector unions and, by proxy, to outsourcing.

## Discussion

Whether individuals employed by the government or those employed by the private sector perform government functions is fundamental to questions of both government performance and government accountability. This article takes government outsourcing of services seriously, examining the contribution of public sector unions to this phenomenon. Through both large-N regression analyses and a synthetic control analysis of one state's law designed to weaken unions, I find that public sector unions play a critical role in countering pressure for governments to outsource services to the private sector. Preliminary evidence suggests that campaign contributions may be an avenue through which unions channel their influence. Although earlier arguments link outsourcing to a conservative ideology or times of fiscal distress, I find little systematic evidence to support these explanations. These results suggest that outsourcing stands apart from other policy issues; while states have increasingly polarized their stances on a host of policy issues (Grumbach, 2018), outsourcing is happening across all 50 states and it does not appear to be strongly affiliated with one party in particular.

While there is ongoing debate about the ability of public sector unions to affect top-line government spending figures (Anzia and Moe, 2014; Paglayan, 2018), this research suggests that at a minimum unions are effective at influencing the allocation of monies within the public sector. It follows that when organized into public sector unions, unelected bureaucrats can have a powerful influence over the direction of public policy. Of course,

public employees do not have homogenous interests when it comes to contracting out (Bhatti, Olsen and Pedersen, 2009), and this homogeneity is likely to be reflected more in some agencies and in some political contexts. Future work would do well to explore the conditions under which unions oppose outsourcing efforts and those where they work in tandem with government to pursue effective public and private partnerships.

The findings about unions have at least three broad implications. First, state business climates that are considered friendly to business are often inversely related to the strength of public sector unions in the state (Marlow, 2013). This research suggests an underappreciated mechanism—pressure not to outsource—by which union presence can contribute to this outcome. Second, public sector unions are often vilified for producing generous pay packages and pensions for their members at the taxpayer’s expense (e.g., DiSalvo, 2015). Yet, unions may play an important role in providing counter-pressure against private sector lobbying. While private sector contractors lobby to keep and extend individual government contracts (Witko, 2011), public sector unions offer a countervailing force to keep spending in-house. If unions indeed provide a counterweight against private sector lobbying, then a third implication of this research is that policies that scuttle public sector union power—such as the recent Supreme Court ruling in *Janus v. AFSCME*<sup>26</sup>—stand to augment the ongoing trend of government reliance on the private sector to perform services.

While the results are robust, there are nonetheless important caveats to consider. First, union targeting of outsourcing decisions may not translate equally to all sectors of the economy. For example, in studying state prisons, Gunderson (2018) finds that high rates of prison guard unionization have little systematic association with state decisions to privatize their prisons. Additionally, while the results have broad implications for both the federal and the municipal level, other considerations surely factor in differently in those contexts, such as agency structure at the federal level or the form of government at the local level.

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<sup>26</sup>See *Janus v. American Federation of State, County, and Municipal Employees, Council 31*, No. 16-1466, 585, U.S. \_\_\_\_\_ (2018).

Looking ahead, government outsourcing of services promises to be a core governance issue in the years to come. This article offers an important advance in understanding the politics of outsourcing; quite simply, public sector unions are a critical component of this governance decision. Future work should continue the conversation.

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