

Liberalisation of local public companies and its effects on the industrial and technical content of water utility companies

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1. Regulatory framework development in public utilities

More than ever before public utility services in recent years have undergone a profound process of reorganization that has placed them at the focus of interest of the more important economic and financial operators.

All this, from the concentration of municipal utilities into new companies, to the extension of the range of services supplied, quotation on the stock exchange and the presence on the international market, took place in a comparatively short space of time, the hallmark of a transformation that has very few equivalents in the panorama of national enterprises.

As is often the case in this country [¹], the regulatory framework does not always precede changes in the operating and institutional framework, and sometimes comes to the fore only when the latter has already begun to change and then follows, generalizes and stimulates this evolutionary process.

Ever since the late '90s it has become increasingly clear that there is a need to change the reference framework regarding local public utilities.

A mix of factors ranging from the need imposed by European treaties to open up the market also in these sectors to the shortage of resources available to the local authorities that contributed to enhance the economic value of the respective enterprises. It also gave rise to a widespread opinion that the time had come to put an end to what had now become an unsustainable equidistance between various management forms (from special company to third party concession) expressed at the time in arts. 22 and 23 of law 142/90 (then incorporated in decree 267/2000).

Moreover, law 34/94 on water services refers, although indicating no preferences, to the forms of management (except management on a time and materials basis and the institution) provided for in law 142/90.

In this (attempted) overhauling operation, in the space of a few years, we have witnessed the appearance of DDL 1388 (the so-called Napolitano law, dating to 1997), DDL 4014 (the so-called Vigneri-Bassanini of 1999), ultimately leading to DDL 7042 which, after a number of evolutions, even though approved by one of the houses of parliament at the end of 2000, failed to be definitively passed before the end of the XIII Parliament. The intense discussion accompanying the development of these regulatory projects, although

¹ It should be recalled, for instance, that the first municipalization legislation (L.103 of 29/3/1903) was passed in Italy much later than the first municipalizations, which took place around the year 1880.

fruitless from the purely regulatory standpoint, nevertheless enhanced the increasingly widespread awareness of the need to rapidly proceed beyond those configurations that find in a monopoly their only reason for being, and to develop instead the capacity to meet the demands of customers who are now served in a different and more competitive fashion than in the past. Moreover, the citizen, who represents the ultimate user of the service, cannot be expected to shoulder all the burden, in terms of quality and/or cost of the services, of any shortcomings in the managing company.

In this connection it may be claimed that this fresh awareness has been more instrumental than law 36/94, which has often been obstructed by vetoes, local power politics and red tape, in inducing companies to convert into joint-stock companies and in some cases to be quoted on the stock exchange. In the meantime other public utility services, such as gas supplies, were characterized by a much more advanced regulatory organization than that of water utilities.

This organization was actually characterized by the establishment of an independent regulatory authority (law no. 481/95), by free access to the network, competitive management and lastly by the adoption of the joint-stock company as the compulsory institutional form for the management entity, all of which are elements that for example we find in the decree law no.164/2000 (the so-called Letta decree) governing natural gas.

The 2002 budget law (no. 448/2001), the first budget of the XIV parliament, resuming the ideas and themes treated in the preceding debate, but also adding new or relatively undeveloped elements (such as the separation between ownership and management and the distinction made with respect to services of comparatively low industrial value), provides a first important response in art. 35 to the laboriously pursued need to reform the now outdated scheme provided for in law no. 142/90.

2. Art. 35 of law 448/01 and opening up the market

A central element of art.35, in this case fully reiterated in DDL 7042 is, after a transitional period of management/territorial consolidation, that of compulsory bidding to assign to third parties services deemed to be of industrial significance (such as the integrated water service). All the other forms envisaged in DLgs 267/2000, also including the mixed joint stock company, even with a private partner selected by calling for tenders, are thus superseded.

It should be pointed out in this connection that it is precisely the mixed public-private company that was the most preferred form in most of the plans developed at the ATO level [2].

The loss of any kind of autonomy by the local and regional authorities in the identification of the form of management of public utilities in their area of competence was certainly one of the most controversial aspects of art. 35, to the extent of rendering the national legislation unique at European level and beyond.

² As shown by the "Annual Report to Parliament on the state of water services for the year 2001" published by the Comitato di Vigilanza sui servizi idrici (Rome, June 2002), of the 19 ATOs that had identified the management form prior to the introduction of art. 35, in only two cases was third party concession adopted. ATO means "Ambito Territoriale Ottimale" (Optimal managing area)

Moreover, with reference to the recently performed competitive bidding for the management of the water services of the larger European capitals, it is seen that none involve outright concession to third parties (reminiscent of the 19th century), but rather the use of mixed public-private companies in which the private partner is selected following publicly visible procedures [3].

It should be recalled in this connection that during the same period the European Commission commissioned a study [4] on the management models used in water services which showed that in no Member Country of the Union did any national legislation exist that allowed the formula of third party concession exclusively for water services management.

Conversely, in the case of the water services of the Member Countries, a very low level of contestability (practically zero in some member countries), emerged from the study. In any case in the European scenario a wide range of management/institutional mechanisms: from 'in-house' concession to local public subject, and affermage contracts, and mixed public/private companies or direct concession to private companies quoted on the stock exchange, etc..

This does not mean, with reference to general principles of the Treaty and after specific appeals were made, that the European Commission has not acted [5] in the sense of identifying a series of limitations vis-à-vis the general principles of the Treaty itself imposed by the above-mentioned art.35, thus placing the Italian State in a position to have to initiate a Community-wide confrontation to enforce those criteria on which the assignment of local services should be based.

After confrontation with the Commission lasting more than one year involving the department of Community Policies, in the second half of 2003 a scheme was defined to overcome Community objections in which, in addition to the assignment of third parties by means of competitive bidding, also 'in-house' assignment and mixed joint-stock companies with competitive bidding used to identify the private partner.

The establishment of three different mechanisms for the assignment of services has thus led the national legislation to (for once) become aligned with the practices adopted by practically all European countries. Furthermore, it is a fact that the European Union while, on the one hand, implementing a policy constantly directed towards guaranteeing the principles of free competition, on the other has never obliged any Member State to carry out forced liberalization of local utilities with a generalized competitive bidding obligation and in any case the EU directives issued on the subject of local public utilities for the time being do not concern water services.

It must be added in any case that the recent Green Paper on services of general interest [6] represents a first step that the European Commission itself intends to take to encourage a wide-ranging reflection on the topic in order to subsequently proceed, if deemed advisable, to adopt definite initiatives in this field, while

³ For example, Prague (2001), Budapest (1997) and Berlin (1999), where a private capital quota of 25% to 66% is envisaged.

⁴ B.Antonioli and G.Bognetti "Modelli di offerta dei servizi pubblici locali in Europa" Working Paper n.07.May 2001

⁵ In this specific case we are referring to the letter of the European Commission of 26 June 2002 concerning the warning received by the Italian government on a number of points in art.35 of L.448/01. The Department of Community Policies set up in the Presidency of the Council immediately contacted the Commission itself in order to ascertain the measures to be taken.

⁶ This is the "Green Paper on Services of General Interest" COM(2003) 270 Brussels, 21 May 2003

the Italian lawmakers, in the framework of the 2004 budget, do not rule out possible future developments in the area of market opening up [7].

3. Water services management: from the “pensée unique” to a fresh awareness

To an attentive observer following the recent developments in the water market over a broad horizon, the solution proposed by DL 269/2003 concerning the multiple nature of reference management models comes as no surprise. It may actually be said that it is precisely the wide-ranging debate that in recent years has been refined at the international level – a debate that is beginning to take account of the acquired (positive and above all negative) experiences - that reveals, particularly in the case of water services, that the forms of funding, managing and assigning the service must be varied and diversified.

Several studies [8] show that, particularly for this type of service and in any case the widespread conviction of the need for private capital intervention, it is not possible to identify a management model that is per se superior to the others; on the contrary, dogmatic approaches referring to ideal theoretical models (or that in any case require ideal conditions in order to work properly) often lead to sensational failures.

The final conclusions of the recent World Water Forum of Kyoto (18-23 March 2003) themselves are significant in this regard.

They indicate that a wide spectrum of solutions must be available in the case of institutional and management forms; in the final document signed by the Ministers of the countries participating in the Forum, it is stated that: “*. we should explore the full range of financing arrangements including private sector participation in line with our national policies and priorities. We will identify and develop new mechanisms of public-private partnerships for the different actors involved....*”

This represents in essence a rejection of the theory of the “pensée unique” that, in the field of public utilities, regarded outright concession to private subjects as the only possible model to be used in all contexts and all situations, a hypothesis that had been dominant in other international fora. It is also significant that, again in this forum, important private groups operating at the international level deemed it of interest, in recounting their experiences and making proposals, to refer not to a single model but to a wide range of solutions ranging from conventional concession, to BOT and even as far as public-private joint-ventures. A part of the proposed models may be included in the so-called PPPs (Public-Private Partnerships).

This fresh awareness that tends to reject dogmatism and precooked solutions (valid for all cases and at all times) emerges also in the new approach to global market regulations and policies displayed by the institutions involved [9].

⁷ To art.4 para. 234 of law 350/2003 has been added “Regulations in this sector, in order to move beyond monopolistic forms, can introduce rules to guarantee free competition in the management of the services they govern, envisaging, with full respect of the provisions of para. 5, gradual criteria for the way the service is assigned”

⁸ International Water Association (IWA) “Alternative Models and Elements of Effective Public-Private Participation” Public Private Partnership Panel, 3rd World Water Forum of Kyoto, March 2003.

⁹ In this connection see the IMF analysis :“Effects of Financial Globalization on Developing Countries: Some Empirical Evidence” of 17 March 2003 and the summary/comment published in Sole24ore of 7 January 2004.

This recently led, for instance, the IMF (International Monetary Fund) to abandon its exaggeratedly laissez-faire approach associated with the now superseded “Washington consensus”, which failed when actually put to the test, in favour of more realistic and pragmatic approaches as emerge from the recent “Monterrey consensus” [10].

4. Final considerations

More than at any previous time, in recent years public utilities have undergone profound reorganization which now places them at the focus of interest of the more important economic and financial operators. From the concentration of local utilities into new companies, to the expansion of the services provided, to quotation on the stock exchange and activity on the international market, all this has taken place in a short space of time which is a visible sign of a transformation that has only very few precedents in the sector of national enterprises.

At the same time, awareness has increased concerning the nature and objectives of water services, also in view of the strong environmental and social implications. In the wake of the experience gained in the different international environments, both European and extra-European, and in the development of the debate on these services, there is a growing conviction that it is necessary to embrace a wide range of solutions in order to more effectively satisfy the needs and specific requirements of the various local situations.

The regulatory developments needed to attain a high degree of industrialization and quality in water services in Italy cannot in any case be considered complete; the recent amendments to art.35 introduced in the 2004 budget are important but are not sufficient; they merely represent an indispensable precondition.

Opening up the market in terms of liberalization and participation of private capital actually makes it necessary also for the regulatory configuration, the rules governing tenders and pricing criteria to be adjusted beforehand to satisfy the need for transparency, equidistance and enhancement of (public and private) entrepreneurial capacities present in this country, a situation that is still far from having been attained. Also recent comparative analyses of the attractiveness of capital investment in water services in the EU area [11] point to the absolute inadequacy of the rates applied in this country, which ranks last in Europe. Moreover, the limited number of participants bidding for tenders regarding water service management (in one case – Sarnese Vesuviano- there were no participants) represents a clear signal that the underlying economic regulations are still inadequate [12].

In any case, if the political authorities have the determination to encourage the growth of a strong and competitive system of national enterprises, it matters little at this stage whether public, private or mixed, operating in the sector of water service management, it is necessary to make clear-cut decisions to update

¹⁰ This is the intergovernmental agreement adopted at Monterrey (Mexico) in the framework “*Summit Segment of the International Conference on Financing for Development*” containing 63 theses, which replaced, at least as a programmatic reference, the model of the ultra laissez-faire Washington Consensus model of 1989.

¹¹ European Environmental Bureau “*A Review of Water Services in the EU under liberalisation and privatisation pressures*”, Brussels, July 2002

¹² R.Drusiani “*Prime considerazioni sui bandi di gara relativi all'affidamento del servizio idrico integrato*” Rivista Trimestrale degli Appalti, num.1 2003.

law 36/94, many parts of which are now obsolete, by promoting the enhancement of existing entrepreneurial prerogatives.

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