

Relations between Local Authorities and Public Utilities Companies

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Abstract

The development of public utilities (supply) has led to a change in needs, thereby influencing the functions that the local public administration is asked to perform.

Globalisation has caused profound socio-political changes (just think of the formation of the European Union, the introduction of the single currency, the fall of some regimes) and has strongly influenced national and local goals.

The development of the socio-political context and the development of new technologies have changed the meaning of public service, and local authorities (i.e. elected administrations) have been able to benefit from this discretionary power, demonstrating their sensitivity to the matter as well as their vision.

Keywords: Public Utilities; Local Authorities; Local Communities; Local Public Administration; European Union; Global Markets

1. Public Utilities in the New Competitive Context

What role have public utilities assumed over the past twenty years?

It might reasonably be claimed that evolving public needs have led to a reassessment of the values assigned to public utilities. Nevertheless, it might also be claimed that the development of public utilities (supply) has led to a change in needs (demand), thereby influencing the functions that the local public administration (the offerer) is asked to perform.

In addition, this dynamism has caused a change in driver markets. Regulations have been updated by implementing requests received externally, and have often disrupted past competitive (or better, uncompetitive) systems, in effect promoting the growth of competition¹. Globalisation has caused profound socio-political changes (just think of the formation of the European Union, the introduction of the single currency, the fall of some regimes) and has strongly influenced national and local goals².

Heterogeneous situations in the public utility service sector derive from geographic-cultural as well as from legal-administrative factors. Therefore, socio-economic systems may be characterised by³:

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- closed competition;
- elementary competition;
- oligopoly-based competition;
- very heavy competition.

Parties that once played major roles as grantors or suppliers in this sector (municipalities, municipal corporations, consortiums) have been replaced by public or private companies, special enterprises or institutions. This does not mean that local authorities have abdicated a role that regulations continue to assign them; it means that such role has changed radically. The so-called ‘Testo Unico degli Enti Locali’ (Local Authority Consolidation Act) (Decree Law 267/2000) consolidated – and added a number of important innovations to – past measures concerning local authorities. Specifically, it redefined aspects regarding their autonomy, organisation and accounting system, and imposed new rules for managing services⁴.

Art. 112 of the Decree (entitled ‘Local Public utilities’) states that: ‘Local authorities, each within its respective jurisdiction, are responsible for managing public utilities that produce goods and assets to be used for social purposes and for the economic and social development of local communities.’

The Decree’s significance is clear as it:

- acknowledges the existence of various public needs, subject to constant adjustment due to changes in the environment (social, cultural, economic, demographic, etc.);
- confirms a function that local public administrations are called to fulfil, i.e., the realisation of social goals and the economic and environmental development of the communities for which they are responsible;
- identifies a means by which such function can be performed: public service.

The authorities are given wide discretionary powers: the national law, as general as it is specific, does not (despite its length) provide any clear definition of public service or of local public service.

Whenever the law does use such terms, there is never an unequivocal definition that could prevent differences in interpretation.

The development of the socio-political context and the development of new technologies have changed the meaning of public service, and local authorities (i.e., elected administrations) have been able to benefit from this discretionary power, demonstrating their sensitivity to the matter as well as their vision.

The government’s only (and recent) worry is revealed by the provision that divides local public utilities into two macro-categories:

- those of economic significance, and
- those without economic significance,

marked by two specific legal-administrative systems that do not detail the basic features of the services⁵.

From the 1903⁶ regulations up to today, this development has demonstrated that the concept of public service has changed from the:

- ‘construction of aqueducts and fountains and distribution of drinking water;’
- ‘supply and operation of public and private lighting;’

- ‘making and sale of ice;’
- ‘drying and storage of corn’ and from other cases specified by the older regulation (which, moreover, is still in effect with regard to the first two services listed);

To:

- The ‘management of building heat;’
- ‘remote heating;’
- ‘data transmission.’

The second part of the list, similar to the first, is incomplete. However, as opposed to measures in the older law, the current law no longer identifies or details the activities that make up public utilities⁷. Government policy confirms this: the discretionary power granted to local authorities is extremely ample and must be exercised to satisfy the functions (the realisation of social goals and economic and social development) that such authorities are called upon to perform. Consequently, the means (public utilities) are affected by political decisions made by administrations as well as by technical-productive potential and opportunities for actual supply.

2. Safeguarding the Interests of Local Communities

The interests of local communities, i.e., the interests of their residents as well as those of all parties associated with them in any way (such as a shop owner who lives in one town but runs his shop in another), must be safeguarded by local authorities.

A business set up to provide public utility services may have one of the following legal statuses:

- *direct management* (so-called ‘time work’), used for services without economic significance, such as public education, public works (maintenance), most activities in the social field (home service, services for minors, etc.);
- *special enterprise*, i.e., the former ‘municipal enterprise,’ resorted to for managing services without economic significance. This status is currently limited to environmental/cultural services and management of real estate assets and cemeteries, mostly of small size and without the need of partners;
- *institution*, introduced by the 1990 reform (Law 142/1990). The reform had difficulty taking root because it was rigid and probably unable to cope with changing contexts. This status has found limited use: for example, in social services for management of nursing homes for the elderly or in the cultural sector for management of museums or art collections;
- *stock company*, considered the most ‘modern,’ which the law specifies as necessary for services with economic significance. This status is gaining popularity as it is the only one that allows third parties to become involved in the business initiative (for example, a private foundation in the management of a museum complex, etc.). In addition, corporate status guarantees – even if not exclusively – recourse to the financial market for access to funds temporarily paid-in by third parties. This category also includes consortiums, which unite several parties (only public or also

private) for services normally provided in areas governed by more than one local administration.

Direct management does not involve relations with any third party, whereas all of the others require the authority to assume (along with the role of granting party) the role of protector of the public interest, for whose development a specific public service is provided.

Setting aside *institution* (which does not enjoy legal status but only managerial independence⁸), relations with a special enterprise or with a stock company authorised to provide a public service must be examined with awareness that when the:

- stock company is controlled (if not wholly owned) by the local authority, aside from purely legal aspects (budget system, by-laws, etc.) there are no marked differences from ownership of a special enterprise: the local authority exercises full control;
- company consists mainly of local public capital but the authority does not hold an absolute majority, relations with other stakeholders must be defined. The participation of local administrations is not a financial investment. It is based on a need to benefit from services provided by the company. Different local needs must be delineated, and therefore an agreement among all of the public stakeholders must be reached before relations are defined between the company and the stakeholder authorities;
- local authority has a minority stake and one or more private stakeholders has an absolute majority stake in the stock company, a corporate agreement must be drafted with these third parties (aside from the service contract) to specify stakeholder conduct at times of important decisions;
- stock company has been listed on the stock exchange, despite the fact that the local authority continues to hold a majority stake (absolute or relative, and if relative with significant controlling power), there is greater rigidity due to strict regulations on listed companies. In addition, any decision by the stakeholder authority may have an effect on share value.

In all cases, the granting local authority may not abdicate its role as protector of the public interest, and therefore the corporate governance model adopted for each legal status is a fundamental aspect. The corporate governance model significantly influences how activities are managed and, therefore, affects the supply of services and the benefit received by the public.

The local administration must be aware of the consequences of granting a service: the mayor (elected directly by the citizens pursuant to Law 91/1983) cannot presume that public consensus is related only to activities performed directly by the authority and not also to activities that the authority has delegated to third parties. Political attention is focussed on the assessment expressed by consensus, traceable to a systemic viewpoint⁹ interested in ensuring 'the economic and social development of local communities.'

3. Market Competition and the Development of Local Communities

The changed environmental context and new market domains in the public utilities sector are leading to a review of strategies and policies that have formed the basis of company management for decades. Similar to markets suffering from over-supply¹⁰, we are gradually witnessing the development of an 'economy of intangible supply and enterprise which, on the one hand, emphasises the role of multi-market and multi-business companies and, on the other, reduces the competitive significance of the business sector. As a result, traditional analyses based on maturity/novelty of the sector give way to corporate activities with a high degree of competitiveness, for which the creation of new value presupposes the destruction of previous values'¹¹.

One must therefore define adequate strategies and consistent corporate policies, because factors such as corporate culture, structure, the production and supply system and corporate communication are essential elements in the management of local public utilities.

This challenge involves local authorities directly. The need to form and maintain good relations with licensed entities, pursuant to the function that authorities have to provide, requires the development of adequate professional skills within the public administration so that the consequences of decisions and actions by parties who actually provide services may be assessed. In essence, this involves the formation of technical-organisational structures for communication¹² and consistent training policies so that the authority may have a system to manage such relations and to assess the results achieved by the service companies. In relation to its mission and to its (public) corporate situation, the local authority can be focussed on the three elements that define market-driven management:

- an outward-looking *culture* based on principles, values and conduct aimed at the continuous search for new sources of competitive advantage;
- *distinctive abilities* in perceiving and relating to the market and in formulating anticipatory strategies;
- a *structure* that sustains the company's ability to anticipate and respond to the changing needs of customers/users and to changing market conditions¹³.

A local authority, a 'vital system' on a par with any company, must therefore work hand in hand with third parties that can have major significance for and influence on the local authority itself¹⁴. The critical nature of these relations demands the definition of a 'relationship policy' consistent with the local authority's stated goal: development of its community.

4. Managing Relations with Public Utilities in a Competitive Context

The legislature has recently provided an instrument aimed at managing relations between local authorities and public utilities: the service contract. In addition to traditional contract terms and conditions (duration, compensation, revocation, etc.) this instrument can be used to define qualitative and economic/financial criteria, office locations and hours, etc., as well as to identify methods for managing relations with customers.

With regard to services of economic significance, Art. 113 of Decree Law 267/2000 states that: 'relations between local authorities and service providers and between local authorities and companies managing networks and systems are regulated by service contracts (attached to the tender specifications), which must specify the levels of service to be guaranteed and appropriate means to confirm the respect of such levels.'

With regard to services without economic significance, Art. 113 ext. of Decree Law 267/2000 is less specific. Nevertheless, it still provides that 'relations between local authorities and the service providers referred to in this article are regulated by service contracts.'

Disregarding all purely legal aspects, attention must be directed toward substantive matters in line with the function that the law assigns to local authorities: the grantor must be interested in the quantity and/or frequency of services, the prospect of expanding the customer base, operational flexibility, managerial elasticity and increased communication with users.

Consider as well that the Decree Law, coming to the aid of local authorities, has also made mandatory another instrument: public service plans, introduced by Prime Ministerial Directive on 27 January 1994¹⁵. These plans are mandatory for all suppliers of public utilities, regardless of their status (public or private).

These documents should represent a 'declaration' by suppliers, serving to protect users and containing precise assumptions of responsibility (in essence, standards of conduct for public utilities) with regard to the characteristics of services provided, service quality, invoice methods, and payment collection.

Public service plans must be based on the following fundamental principles:

- equal rights for all users;
- impartiality;
- continuous supply;
- the right to choose (where possible) among various suppliers;
- the user's right of participation;
- effectiveness and efficiency of activities conducted,

and must also:

- specify the qualitative and quantitative standards of services;
- promote the simplification of procedures;
- keep users updated continuously;
- specify rules of conduct in relations with users;
- specify methods for assessing the services provided;
- specify reimbursement methods,

in addition to guaranteeing the protection of customers and their right to make complaints.

In light of the above, one may legitimately state that legal instruments are not lacking (nor are they anachronistic or overly dispersive). Therefore, an authority's ability to adequately perform its role can only depend on:

- administrative culture;
- expansion of the market concept from a competitive point of view;
- sensitivity to needs;
- technical skills and training;
- the ability to co-operate with all of the local authority's stakeholders.

That is why formal respect for the law (for every activity granted to third parties: drafting of a service contract and approval of a public service plan) cannot even be questioned by local authorities. On the other hand, the assessment of an administration's work must be focussed on how well the administration performed its task of developing the local community. In this perspective, it is essential for authorities to implement policies that view the market in a competitive context so that they may understand the most critical aspects of demand, the market, direct and indirect competition, in addition to adopting technological advances that may change the services offered to the public.

Managing relations with utilities cannot be classified as one of the negligible duties of a local authority. An updated management model could allow authorities to retain only coordination and support activities, thereby assigning other aspects to third parties (perhaps linked to the authority: for example, a stock company) that can provide greater flexibility.

The complexity of and constantly changing legislation, the decline in national government funding and growing tax autonomy are elements that lead one to favour an authority with a lean structure, but still able to coordinate relations with local communities on the one hand and with various utilities on the other.

Lastly, in the presence of special enterprises or of stock companies in which the authority is the majority stakeholder, corporate governance also identifies a system based on the separation of policy-making/control activities and management activities. Conversely, in companies where the authority does not contribute risk capital, or holds a minority stake, it may be unable to dictate policy, whereas it should (or better, must) perform control activities.

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Notes

¹ See R. Mele, who identifies four developmental stages of public utilities:

- a. creation and initial development (1850-1900);
- b. public regulatory stage (1900-1945);
- c. promotional stage (1945-1985-1990);
- d. deregulation and development of competition and privatisation (since 1985).

In addition, he notes that public utility transformation has been oriented toward a model definable as 'quality of life or of services,' in R. Mele, *La nuova regolamentazione del settore*, in *Economia e gestione delle imprese di pubblici servizi tra regolamentazione e mercato*, Cedam, Padua, 2003, pp. 1-4.

² See C. Leys, who notes that 'most people now work for private companies, and what remains of the public sector has been remodelled on 'business' lines, with 'profit centres', performance-related pay, annual 'market-testing', 'outsourcing', 'downsizing', and 'productivity savings' targets – and in sectors like hospitals and the arts, appeals to charities and companies for donations. Conversely, people now bought their phone services, water supplies, gas and electricity from other private companies. Buses, trains and train stations, airlines and airports were also now all privately owned and operated, as more and more government offices and, imminently, hospitals and clinics..... Official terminology had been changed to encourage the shift from a 'producer' to a 'consumer' culture: 'customer' replaced 'passenger', 'client' replaced 'patient'.', *Market-Driven Politics*, p. 53, Verso, London-New York, 2001.

³ See S.M. Brondoni, *Comunicazione pubblica e 'soddisfazione dell'utente'. I paradigmi relazionali di efficacia e di efficienza*, in S.M. Brondoni (ed.), *La comunicazione nell'azienda pubblica. I paradigmi di efficacia e di efficienza*, Giappichelli, Turin, 1999, p. 16.

⁴ Art. 13 of the Local Authority Consolidation Act provides that 'municipalities are responsible for all administrative functions that relate to the public and the municipal territory, with particular regard to sectors that provide services to individuals and to the public; to the organisation and use of the territory and its economic development, except as expressly delegated to other parties by national or regional law, according to their respective jurisdictions.' A similar provision (obviously for different specific contexts) governs other types of local authorities (provinces, metropolitan cities and mountain communities).

⁵ See articles 113 and 113ext. of the Decree Law, recently amended, which distinguish between 'local public utilities of economic significance' and 'local public utilities without economic significance,' however without explicitly defining either term.

⁶ Royal Regulations of 1903 (better known as the 'Giolitti law,' no. 103 of 29 March 1903), later included in the Consolidation Act referred to in Royal Decree no. 2578 of 15 October 1925.

⁷ The measure instituting supervisory authorities for sectors deemed critical identifies 'services of public utility' as only those regarding:

- electricity,
- gas,
- telecommunications.

Paragraph 1, Art. 1 of Law no. 481 of 14 November 1995, which instituted regulatory authorities for public utilities, states that '*The provisions of this law aim to ensure the promotion of competition and of efficiency in the public utility sector, hereinafter called 'utilities,' as well as adequate levels of quality in such utilities under low-cost profitable conditions, ensure their homogeneous availability and distribution throughout the nation, stipulate a clear, transparent rate system based on pre-defined criteria, and safeguard the interests of users and consumers, taking into consideration community regulations and general policies formulated by the Government. The rate system must harmonise the economic-financial goals of utility companies with general goals regarding social concerns, environmental protection, and the efficient use of resources.* All other utilities except for water, transportation (and pharmacies) are not regulated by special administrative laws.

⁸ The regulation (Art. 113bis of the Decree Law) states:

1. *The special enterprise is an auxiliary body of the local authority with legal status, entrepreneurial autonomy, and by-laws, approved by the municipal or provincial council*
2. *The institution is an auxiliary body of the local authority for the exercise of social services, with managerial autonomy.*

⁹ Regarding systemic analysis, see the article by G.M. Golinelli, *L'approccio sistemico al governo dell'impresa*, Vol. I, *L'impresa sistema vitale*, Cedam, Padua 2000.

¹⁰ See S.M. Brondoni, *Comunicazione, risorse invisibili e strategia competitiva d'impresa*, in *Sinergie*, n. 43-44, 1997.

¹¹ See Lambin J.J., Brondoni S.M., *Ouverture de Market-Driven Management*, in *Symphonya. Emerging Issues in Management (symphonya.unimib.it)*, n. 2, 2000-2001

¹² See G. Rebori, M. Meneguzzo, *Strategia delle amministrazioni pubbliche*, UTET, Turin, 1990.

¹³ See G.S. Day, *The Market Driven Organization*, The Free Press, New York, 1999.

¹⁴ See G.M. Golinelli, M. Gatti, who note: '*Significance is therefore the primary differentiating factor for entities that make up the vital system. The enterprise system forms a variety of relations and interactions with these entities, making permanent or temporary contributions and creating conditions that may be harmonious and significant from time to time. The significance of these third parties can be classified on the basis of two attributes:*

- *the 'influence' exercisable by the entity;*
- *the critical level of the resource contributed to the enterprise system.'*

This permits an initial distinction between 'significant systems' (characterised by being influential and simultaneously possessing a critical resource) and merely 'influential systems,' so defined because even though they may be able to exercise influence, they do not have exclusive possession of a specific resource,' in The Firm as a Viable System, in Symphonya. Emerging Issues in Management (symphonya.unimib.it), n. 2, 2000-2001.

¹⁵ The preamble of the Directive offers further help in circumscribing public utilities, even if, once again, a definition is lacking: 'For purposes of this directive, services that ensure the enjoyment of constitutionally protected rights to health, social services, social security, education, freedom of speech, personal freedom and safety, and freedom of movement for purposes of Art. 1 of law no. 146 of 12 June 1990, and those ensuring the distribution of electricity, water, and gas, are hereby considered public utilities, even if exercised pursuant to a licence or an agreement.'