

# THE CHANGE IN OWNERSHIP STRUCTURE OF LOCAL PUBLIC UTILITIES PROVIDERS: THE CASE OF WATER AND WASTEWATER MANAGEMENT IN SLOVENIA

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**Abstract** The paper analyses the effect of Public Private Partnership Act on the ownership structure of local public utilities' providers in Slovenia. The Act affected the legal status of public enterprises, where solely public ownership was prescribed, and therefore demanded the reorganization of existing public enterprises. The paper aims to evaluate the reorganization of the existing public enterprises, the motives of reorganization and the advantages and disadvantages of the reorganization under the new legislation. The paper presents results based on the primary data collection through a detailed on-line questionnaire sent to the Slovenian local public utilities' providers in the area of water and wastewater management, in the period from 2018 till 2020. The collected data is used in the comparative analysis which gives evidence about the final outcomes of the reorganization process. It is evident that policy proposal contributed to the increased public ownership in local public utilities provision.

**Keywords:**

local public utilities, public enterprise, water and wastewater management.

## 1 Introduction

The trend of privatization and out-sourcing the provision of local public services has during the twentieth century turned back to reverse privatization and contracting in or remunicipalization (Gradus et al., 2019, p. 1; Gradus & Budding, 2018, p. 2). A shift back from private to public ownership, a trend towards remunicipalization of local public services can be detected also in Slovenia. In Slovenia, public enterprises have become principal form of local public services provision. To enable and encourage mutual help and cooperation between entities from the public and the private sectors, which would lead to economical and efficient provision of public services, Slovenia adopted the Public-Private Partnership Act (PPPA) in 2006 (Bauby & Similie, 2010, pp. 116-117). This Act also prescribed the transformation of existing public enterprises, which in the specified period should made the appropriate changes in their organizational status or should their founders consider adaptation of their current status to the new legislative conditions.

It is evident that public ownership and control has increased, and that the majority of providers retained their public status even after the new legislation. However, the results of the reorganization process are not so evident in full, like whether buyout was implemented in full, and what motives guided municipalities in buying the ownership shares, which was necessary for the reorganization of existing public enterprises into public enterprises with 100% ownership of municipalities. The paper therefore focuses on evidence and aims to evaluate the reorganization of existing public enterprises, the motives of reorganization and also the advantages and disadvantages of reorganization under the PPPA.

The paper presents results based on the primary data collection through a detailed on-line questionnaire, sent to Slovenian local public utilities' providers in the area of water and wastewater management. The results of the research give general evidence about the final outcome of the reorganization process. It is seen that policy proposal contributed to the increased public ownership in local public utilities provision, however, the results also reveal the motivating factors that contributed to increased municipal buying out of private investors from (public) enterprises.

## **2 Literature review on remunicipalization trends**

Market liberalization has led to outsourcing and privatization of local service provision, as a reform to promote efficiency of municipal service delivery. However, in the last decade a trend towards remunicipalization has increased, where municipalities take the provision of local public services back in their own hands (Gradus & Budding, 2018, pp. 2-3; McDonald, 2019, p. 61; Wollmann, 2018, pp. 426). With remunicipalization, municipalities strive to achieve greater municipal democracy and autonomy. This is also a strategy to deal with pressing social, economic and ecological problems. Public ownership has benefits for local communities, such as lower costs for consumers, more access for underserved populations, providing social services etc. Besides that, public ownership can support economic development, provide jobs, enhance local control and participation in economic decision-making (Hanna, 2019, p. 45-46).

On one hand, remunicipalization can be intentional and is done by ending contract with private provider, very often due to dissatisfaction with private provider (higher costs, bad service quality, public mistrust of private provider, corruption, not achieving infrastructure promises etc). On the other hand, municipalities can also be forced into remunicipalization, even though policy makers would prefer to retain private service provision. This is a consequence of high costs of monitoring and regulating private contracts, reducing efficiency gains and last but not least insufficient number of private-sector bidders for a contract. In this context we can include large, long-term concessions and small, short-term contracts, where sophisticated and expensive regulatory management is required in both cases (Berlo et al., 2017, p. 1; McDonald, 2019, p. 62).

Remunicipalization can be proceeded in two ways, by repurchasing shares that were previously sold to private companies and by reinsourcing services that were previously outsourced. When the concession is expired, municipalities decide about remunicipalization, as an opportunity to bring services back in-house without transaction costs incurred with termination of contract. When the concession has not expired yet, there can be difficulties with the outgoing private provider about the compensation (Hall et al., 2013, p. 206; Wollmann, 2018, p. 422). The remunicipalization process, however, varies according to local context, the condition of public service, the involvement of the local government, the

duration of the contract, the degree of private participation etc. (Valdovinos, 2012, pp. 115-116).

As already mentioned, a trend towards remunicipalization of local public services can be detected also in Slovenia. In Slovenia, important changes happened in the field of transformation of existing public enterprises with the implementation of the Public-Private Partnership Act (Official Gazette of the Republic of Slovenia, No. 127/06) (Brezovnik, 2009, p. 180; Trpin, 2007, pp. 5-6). The Act was adopted in 2006 and entered into force in March 2007. The Act strongly influenced the legal status of public enterprises, especially regarding further organization and operation of the public enterprises providing public services and it has determined the rules of transformation of existing public enterprises (Brezovnik, 2010, p. 24).

The legal status of public enterprises has been defined by the Act. This definition enables the differentiation between “true” public enterprises that shall remain exclusively publicly owned to perform public service activities, and other public enterprises that shall be transformed into commercial companies. Public enterprises with the private equity stakes have two options of reorganization. First, a public enterprise can be transformed into a commercial company in accordance with the Companies Act, and second, a public enterprise status can be retained, meaning that the private equity stakes are in a way nullified (Kocbek, 2011, p. 86). Therefore, public enterprises where private investors kept shares, needed to be transformed into commercial companies, and public enterprises that wanted to remain public had to transfer the private ownership to the state or local community. The decision about either of two options had to be taken by the founder of the enterprise within three years from the adoption of the Act (by March 2010). The new regulation determines that a public enterprise may only be an enterprise which is 100% owned by the state or local government. Besides legal status and to that related ownership, the Act also regulates awarding concessions to public enterprises, which are transformed into a commercial companies. First, the founder shall award concessions without public tender to the commercial companies that were created out of the public enterprises with no stakes of persons of private law. This had to be done within one year, by March 2008. Second, public enterprises transformed into commercial companies must obtain a concession in compliance with the legislation. The concession

should be awarded within one year by the founder of the enterprise as a result of the bidding process on the public tender (Hrovatin, 2010, p. 102; Brezovnik, 2010, p. 24; Trpin, 2007, pp. 6, 13).

To summarize, the Public-Private Partnership Act (PPPA) demanded reorganization of the existing public enterprises and awarding concessions to public enterprises which had transformed into private law companies. In the following section, the paper therefore focuses on evidence of reorganization of existing public enterprises, on the motives of reorganization and on the advantages and disadvantages of reorganization under the PPPA.

### **3 Methodology and research**

#### **3.1 Research design and research sample**

A study on reorganization of Slovenian public enterprises in the field of water and wastewater management was done with primary data collection through a detailed on-line questionnaire, sent to Slovenian local public utilities' providers in the area of water and wastewater management. The answers were collected in the period from 2018 till 2020. The questionnaire was developed by authors, and pre-tested to get relevant insight into the topic.

An on-line questionnaire is divided into 5 thematic units, covering the basic data of the respondents, the provision of public utilities in the area of drinking water supply and wastewater treatment, the ownership structure of the public utilities providers before the adoption of the new legislation, the changes resulting from reorganization of existing public enterprises and the compliance with the applicable new legislation, and the price setting of the local public utilities in the area of drinking water supply and wastewater treatment, using a combination of multiple choice answers, open ended questions and Likert scale 1 – 5. The results shown in this paper do not cover all 5 thematic units, but as already mentioned focus mostly on changes and outcomes of the reorganization process.

The scrutinized research population included all public enterprises in the field of water and wastewater management in Slovenia, more specifically, public enterprises providing drinking water supply, sewage and wastewater discharges and urban wastewater and sewage treatment. Given the fact that Slovenia is a small country, this enabled the analysis and evaluation being focused on the entire population of public enterprises in this industry. The total population included 72 public enterprises for water and wastewater treatment in Slovenia. 55 public enterprises are providing both drinking water and wastewater treatment, 11 providing only wastewater treatment and 6 providing only drinking water treatment.

As seen from the Table 1, in total 30 public enterprises (41.67% of total sample) responded to the on-line questionnaire, but only 21 public enterprises completed the survey in full or almost in full. The actual respond rate (fully and almost fully completed surveys) is 29.17%, which enables the insight and comparison of answers to survey questions and therefore gives the whole picture of the outcomes of the reorganization process of public enterprises in the field of water and wastewater management in Slovenia. The relatively low response rate might be attributed to the fact that questionnaire is rather long, since it is aimed towards holistic evaluation of the effects of the law. Given the context that we want to evaluate the outcomes in the comprehensive manner, this input should be considered in a sufficient manner to extrapolate the field experiences. The data analysis and results, which are presented in the paper, consider all the available respondents' answers, from incompleting to fully completed questionnaires, therefore the total number of responses differs between the presented results in the tables.

**Table 1: Research sample**

| <b>Public enterprises</b>                          | <b>Number</b> | <b>% of total sample</b> |
|--|---------------|--------------------------|
| <b>Sample total</b>                                | 72            | 100.00%                  |
| <b>Provision of water and wastewater treatment</b> | 55            | 76.39%                   |
| <b>Provision of only water treatment</b>           | 6             | 8.33%                    |
| <b>Provision of only wastewater treatment</b>      | 11            | 15.28%                   |
| <b>Total no of responses</b>                       | 30            | 41.67%                   |
| <b>No of (almost) completed surveys</b>            | 21            | 29.17%                   |
| <b>No of in-completed surveys</b>                  | 9             | 12.50%                   |

source: Questionnaire, 2018-2020

Most of the public enterprises from the research sample (almost 86%) are established as a Limited Liability Company and only 14% as a Publicly Limited Company (Table 2).

**Table 2: Legal status of public enterprises**

| <b>Legal status</b> | <b>No of responses</b> | <b>% of total responses</b> |
|---------------------|------------------------|-----------------------------|
| <b>LLC</b>          | 24                     | 85.71%                      |
| <b>PLC</b>          | 4                      | 14.29%                      |
| <b>Total</b>        | 28                     | 100.00%                     |

source: Questionnaire, 2018-2020

### **3.2 Results overview and discussion**

The majority of responding public enterprises (77%) had 100% public (municipal) ownership already before the adoption of PPPA and have retained their legal status of public enterprise also after the adoption of new legislation. After the adoption of PPPA the share of 100% public ownership has risen to 91%, which shows that in the process of reorganization some enterprises with mixed ownership (public and private) have transformed into 100% publicly owned public enterprises. Before the adoption of PPPA, such mixed public enterprises represented almost 23% of all respondents, which has decreased to just under 9% of responding enterprises with mixed ownership after the adoption of new legislation (Table 3).

**Table 3: Ownership before and after PPPA**

| Ownership          | Ownership before PPPA |                      | Ownership after PPPA |                      |
|--------------------|-----------------------|----------------------|----------------------|----------------------|
|                    | No of responses       | % of total responses | No of responses      | % of total responses |
| <b>100% public</b> | 17                    | 77.27%               | 21                   | 91.30%               |
| <b>Mixed</b>       | 5                     | 22.73%               | 2                    | 8.70%                |
| <b>Private</b>     | 0                     | 0,00%                | 0                    | 0.00%                |
| <b>Total</b>       | 22                    | 100.00%              | 23                   | 100.00%              |

source: Questionnaire, 2018-2020

After the adoption of PPPA, the founder of a public enterprise (a municipality) has retained 100% public ownership in almost 86% of researched cases and only in 9.5% of cases the process of transformation into 100% public ownership has happened. In one case the founder has left ownership shares as own shares of public enterprise (Table 4).

**Table 4: Retention of or transformation into 100% public ownership after PPPA**

|  | No of responses | % of total responses |
|--|-----------------|----------------------|
| <b>Retention of 100% public ownership</b>        | 18              | 85.71%               |
| <b>Transformation into 100% public ownership</b> | 2               | 9.52%                |
| <b>Other</b>                                     | 1               | 4.76%                |
| <b>Total</b>                                     | 21              | 100.00%              |

source: Questionnaire, 2018-2020

Respondents with 100% municipal ownership also gave information, whether the retention or change in the ownership structure was a consequence of the adoption of PPPA. Around 30% of responding public enterprises confirm that the decision about ownership was due to the adoption of PPPA. Around 60% of respondents did not have this information and some of the respondents (approximately 10%) stated that there were never doubts about 100% municipal ownership, with no regards to new legislation.



The ownership structure of mixed public enterprises that retained mixed ownership even after the adoption of PPPA has not changed significantly. The average public capital share has decreased from 66% to 59% and the average private capital share had increased from 34% to 42% (Table 5).

**Table 5: Ownership of mixed public enterprises before and after PPPA**

| Ownership      | Ownership before PPPA |                 | Ownership after PPPA  |                 |
|----------------|-----------------------|-----------------|-----------------------|-----------------|
|                | Average capital share | No of responses | Average capital share | No of responses |
| <b>Public</b>  | 66%                   | 5               | 59%                   | 2               |
| <b>Private</b> | 34%                   | 5               | 42%                   | 2               |
| <b>Total</b>   | 100%                  | 5               | 100%                  | 2               |

source: Questionnaire, 2018-2020

Retaining mixed ownership in mentioned public enterprises after the new legislation and consequently transformation into a commercial company was in one case due to incapability of municipality to provide budget funds for the purchase of ownership shares; and in other case, it was due to the interest of owners and employees.

One of the aims of the analysis was also to elaborate on the motives that might have guided municipalities in buying the ownership shares, which was necessary for the reorganization of existing public enterprises into (pure) public enterprises. The most important motive for 100% municipal ownership of a public enterprise was management problems in a mixed-ownership enterprise, closely followed by simpler regulation of the service provider, greater control over the service provider, more possibilities for influencing the business activities and greater rationality and efficiency of business activities. These are the classical reasons for remunicipalization. Therefore, we can argue that legal amendments have promoted those trends towards remunicipalization in Slovenia. On the other hand, to avoid employee dismissal was the less important motive and also to avoid public tender for concession was not an important motive. However, avoiding public tender for concession did not prevail as an important motive, because most of the respondents retained 100% public ownership and they don't need public tender for concessions.

The reorganization process brought advantages and disadvantages. The respondents see the biggest advantage that municipality can monitor the business activities of the enterprise under the decree, followed by the advantage that institutional, corporate and governmental rights are prescribed by a municipal decree; better co-operation between the enterprise and the local community; and that municipality has full control over the performance of public utilities' providers. In contrast, also some disadvantages of the reorganization process can be observed, but they are less important and of smaller magnitude than advantages. The respondents find the biggest disadvantage in the arrangement of a concession relationship, which requires the regulation of many legal acts. They agree that lack of experiences of the municipalities in providing control over the concessions can be observed and that regulatory price policy can present a disadvantage. These exposed disadvantages explain the fact that high costs of monitoring and regulating private contracts drive municipalities to remunicipalize and that remunicipalization is a better option than privatization or contracting out.

#### **4 Conclusion**

As Slovenia faced the reorganization of existing public enterprises with the adoption of PPPA, which has influenced the legal status of public enterprises and brought significant changes in their ownership, the paper tries to reveal the final outcome of the reorganization process, what specific institutional changes and experiences has it brought. The analysis is based on the primary data collection through an on-line questionnaire, sent to Slovenian local public utilities' providers in the area of water and wastewater management, in the period from 2018 till 2020.

The results of the analysis indicate that the majority of the responding public enterprises have retained their legal status of public enterprise with 100% public ownership and that also some public enterprises with mixed ownership have transformed into 100% publicly owned public enterprises. Mixed public enterprises, retaining mixed ownership after the new legislation, transformed into a commercial companies, have taken this decision due to incapability of municipality to provide budget funds for the purchase of ownership shares and due to the interest of owners and employees.

Results also indicate that the most important motive for having 100% municipal ownership of a public enterprise was management problems in a mixed-ownership enterprise, closely followed by simpler regulation of the service provider, greater control over the service provider, more possibilities for influencing the business activities and greater rationality and efficiency of business activities.

Results also indicate that the reorganization process brought mostly advantages, e.g.: municipality can monitor the business activities of the enterprise under the decree; municipality has full control over the performance of public utilities' providers; institutional, corporate and governmental rights are prescribed by a municipal decree and better co-operation between the enterprise and the local community.

To summarize, the implementation of PPPA contributed to the increased public ownership in local public utilities provision and most of the existing public enterprises retained or transformed into 100% municipal ownership. At this point it is only questionable whether solely public (municipal) ownership is economically rational due to minority market competitors in acquiring the rights to provide the utilities.

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