

Regulation and public ownership in local public services

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public property, political regulation and independent regulation for the public services

1. Public services: definition, development
2. The history of public ownership
3. Network services
4. The rise of regulation
5. Are uniformity or coordination necessary?

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What is “public service”?

- Traditionally, a public service has been understood as **any service provided by a public entity**.
- A more satisfactory definition refers to contents: we are interested in services characterized by being:
 - **necessary or very useful to life** (of individuals, of the community), so they fall under some **public responsibility (or “general interest”)**,
 - usually **not provided** by private, profit oriented entities under **normal market conditions**,
 - yet **not necessarily provided by public entities**.

Why are services of general interest not being provided under normal market conditions?

Because:

- due to **inequalities** in income and wealth, part of the population will not be able to pay for these services (health, education),
- some services provide **benefits to the community** (e.g. clean air) and not specific benefits to individual citizens who can be called to pay (the case of “public goods” in technical sense, i.e. non-rival, non-excludable),
- some services (e.g. collective transport, waste collection) benefit both the individual citizens directly interested and the whole community interested in clean air and clean streets (**externalities**), so the cost must be shared,
- some services can be sold in the market but need **collective infrastructure and planning** (airports, rail and road networks, communication infrastructures).

Public services: development trends

- Needs for many services **grow**, expenditure (private and public) for services increases
- This applies also to “public” services such as health, education, networks, transport, communications
- Direct public provision is **shrinking**
- Services are increasingly provided by private companies,
 - **often in competition**
 - **under concession if “natural monopolies”**

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2. The historic role of public ownership: the reasons in favour

- a. a substitute for missing private initiative and an engine for development
 - (the “infant industry” theory, basic industries)
- b. a provider of public goods, externalities
 - (water systems)
- c. a remedy to monopoly, externalities,
 - (Italian constitution art.43: nationalisation for “essential public services, energy sources and monopolies where preminent general interest”, no mention of antitrust)
- d. a remedy to “natural” monopoly
 - (network services: railways, highways, electricity)

There is a choice

- Public ownership justifies a monopoly (benevolent?)
- Most objectives may be attained with other means:
 - Legal obligations, limitations
 - Public procurement for public goods, subsidies for externalities
 - Competition among suppliers enforced by an Antitrust authority
- An “ideologic” debate:
 - “public is always better”: the market is simply bad, an engine for inequality
 - “private is always better”: it is efficient while the public sector is inefficient, corrupt

The basic weaknesses of public ownership

- A public enterprise is shielded from competition and may control its controller
- It has conflicting goals: maximise profits and implement political directives: how can managers be evaluated?
- A burden on public finance from losses and from investment: a vicious circle of lacking funds – bad service – low tariffs
- State aid is contrary to trade agreements (and to EU law)

Privatisation often has a bad name, consequently it may be badly managed

- Half-hearted privatisation
 - from Government need for revenue or inability to fund company growth,
 - without a programme for improvement
- Sale of minority shares maintaining public control:
 - limited advantages of greater transparency, possible conflicts remain

The alternatives to public ownership

- To promote national development: good rules, infrastructures
- To provide public goods: contracting out
- To correct externalities: taxes, subsidies
- To correct inequalities: obligations to serve, differentiated tariffs,
- To contrast monopoly: open and large markets, an antitrust law and a competition authority
- To set rules and monitor compliance: a regulatory authority

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3. Network services

In presence of a network, competition may be impossible or uneconomic: a classic case of “natural” monopoly

- Traditional consequence: a legal monopoly and a concession of the whole service to a public-owned or to a private-owned company
- Traditional bundling of a whole service (tracks and trains, grid and electricity, pipeline and gas)

objections

Even a public monopoly does not escape the monopoly's weaknesses:

- no contest, no incentive to efficiency, no choice, no room for entrepreneurship
- moreover: political interference, investment is a burden on public finance
- size of company limited by political boundaries

Alternative (a): maintain an integrated (bundled) service and run it better

- Prices (tariffs) set by a public body
- ... also setting quality levels, environmental standards
- This is the traditional notion of “regulation”

- Although a regulated monopoly is better than an unregulated monopoly, some important faults remain:
 - **No choice**
 - **Little room for initiative and entrepreneurship**
 - **Risk of political patronage**

Alternative (b): maintain an integrated service and tender it out

- Tendering introduces competition among bidders
- The service is provided under (a temporary) monopoly
- Monopoly power is limited by terms of tender and by contractual obligations
- Monitoring of tariffs and of performance is required

Difficulties and Requirements:

- duration of contract and incentives to invest
- sufficient competition in bidding is necessary
- tendering and monitoring may be beyond the capabilities of a local administration: help required
- local preference for local company may distort tendering

**Alternative (c):
unbundle network from service,
keep the network under (a) or (b),
open a competitive market for the service**

Networks (monopolies) regulated and accessible:

- Unbundling (accounting, legal, ownership)
- Contents of network regulation: tariffs, rules for access
- A role for both industry regulator, competition authority

Problems:

- Interest links between network company and on service company
- Brand names

Competition for services works well if ...

- a sufficient number of competitors and ...
- a market large enough to allow optimal size of company.
- Transition in liberalisation: divesting the public company or parts of it is controversial, may create conflicts
- Transition problems in pricing: from regulated tariffs to free market prices
- Protection of low-income or otherwise disadvantaged customers requires special provisions

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4. The rise of regulation

- the US tradition of regulation
 - **Public Utilities Commissions since early 20th century**
- in Europe
 - **public (or semi-public) ownership made regulation seem unnecessary**
- a revolution started around mid-1980s
 - **deregulation, opening of markets, privatisation**
 - **objectives: efficiency through competition, shrinking and re-orientation of State functions**
 - **an independent authority has been seen as necessary**
 - **rise of regulatory authorities 1990-2005**

Political regulation vs. independent authorities

- reference case: the rise of independent central banks
- the case for “tying one’s hands” in the regulation of public services
 - useful as a defence against demagogic temptations
 - necessary in presence of Govt-owned companies
- the importance of independent regulation in transnational investment in infrastructures (view of the World Bank)

The task of a regulator

- set tariffs for monopolistic services
- promote competition where possible
 - access to networks
- set technical standards for safety, interoperability
- promote development of infrastructures using obligations and incentives
- protect weak consumers
- advise Government

Many institutions in charge of local regulation

- The local area is often too small for setting up a local regulatory authority
- The local administration may be weak in contracting out the service, in designing and managing a tender
- Difficult cooperation in the Triangle: national government - local administration - national regulator (plus national antitrust authority)
- A special case: cooperative enterprises running local services

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5. Are uniformity or coordination necessary?

- the extreme cases:
 - high uniformity needed in financial markets
 - low uniformity needed in local services
- instruments for coordination
 - top-down: treaties, legislation, institutions
 - bottom-up: cooperation, information, best practices
- Problem: the “regulatory gap” between multinational companies and national (local) regulation

Public services in the European Union



- 1957: the Treaty of Rome (6 countries) established the European Economic Community (Common Market)
- 1987 Single Market Act
- 1991 the Maastricht Treaty established the European Union (12 countries)
- 2007: Lisbon Treaty reformed the EU
- Now 28 countries have a Single (Internal) Market

Public services in the European Union

The treaties refer to “services of general interest” **identified by the Member states**, and distinguish:

Economic services (services of general economic interest, SGEI)

- Economic activities that public authorities identify as being of particular importance to citizens and that would not be supplied (or would be supplied unsatisfactorily) if there were no public intervention
- Examples: transport networks, postal & social services
- SGEI are **subject to the rules of the EU Treaty**: open market, competition or competitive bidding

Non-economic services of general interest

- Usually provided by public entities, not subject to specific EU legislation, except basic principles such as non discrimination

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