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Water LPEs in Cities: Three Case Studies

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Water LPEs in Cities: Three Case Studies

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Canada – Montréal

Germany – Stuttgart

France – Brest

SOMMAIRE

GENERAL SUMMARY	**3**
THE CASE OF MONTREAL	**10**
THE CASE OF STUTTGART	**49**
THE CASE OF BREST	**84**

Water LPEs in Cities: Three Case Studies

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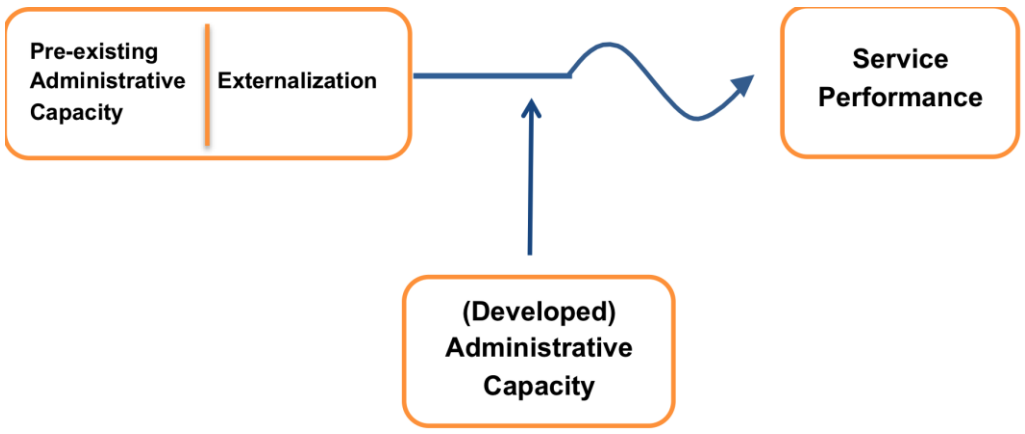
Administrative Capacity and the Organization of Water Services

Despite the acknowledged importance of administrative capacity, its meaning and measurement remain hard to fathom (OCDE (2012), Charbit (2011)). A bibliometric content analysis by Christensen and Gazley (2008), reviewing four decades of scientific research in various fields, showed that not only is capacity a multidimensional concept, but it has also developed independently across fields. Although there are many overlaps, this has led to a proliferation of diverging conceptual frameworks. For instance, while 'Management Science' research stresses external dimensions like financial capital and market forces, internal dimensions like human resources and leadership play a minor role in this area of research.

An unequivocal result is, however, that depending on the governance structure envisioned by a local government, the necessary set of skills can differ considerably. The failure or success of providing public services like drinking water through different institutional arrangements may depend crucially and in a non-trivial way from the administrative capacity. A strand of literature deals with this question and what administrative capacities are required for governments to adapt to these situations (Brown and Potoski (2003)). Initially, pre-existing administrative capacities will impact on the decision to organize a public service through direct public management or otherwise. In addition, administrative capacities developed through the provision process, once the governance structure is decided, will also impact on the service performance and at the end, on the willingness to switch from one governance structure to another (See Figure 1).

Figure 1: Administrative Capacity and Service Performance



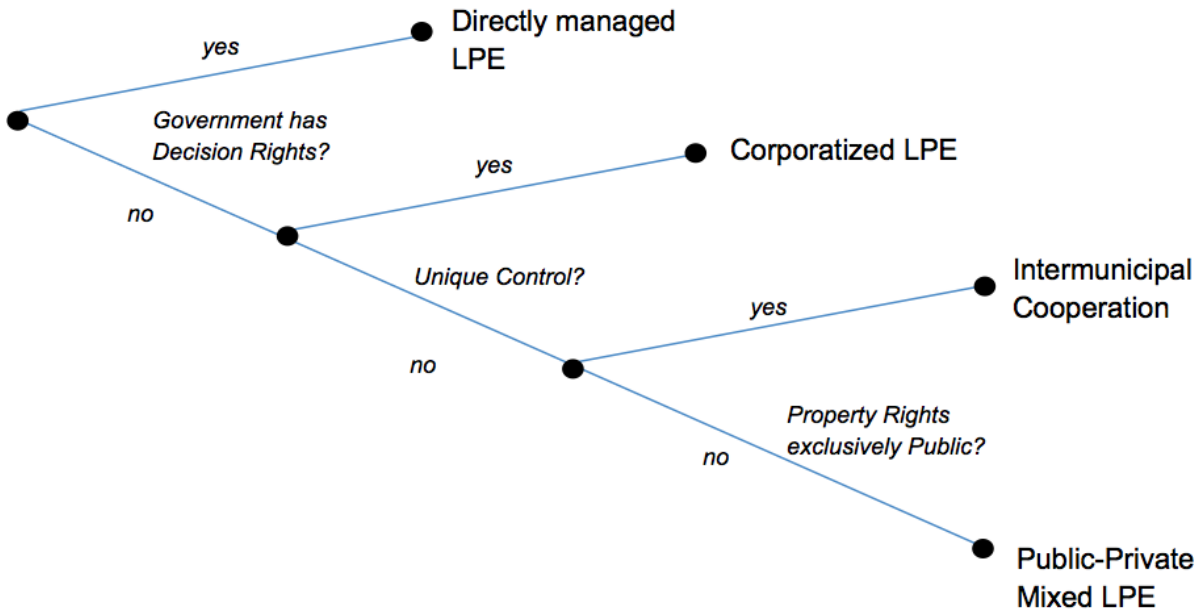
The objective of the three case studies, looking carefully at three cities (Stuttgart - Germany, Montréal - Canada and Brest - France), is to highlight key features of such relationships between administrative capacity and choices made by cities to organize their water public services.

A Starting Point: Taxonomy of LPEs

In order to propose a taxonomy of the different governance structures that might be implemented by cities to provide water services, the question of decision rights is key. Unless the government is ready to give up some decision rights, which requires the creation of a separate organizational entity, alternative types of LPEs are ruled out. Second, apart from the decision rights of an LPE,

the issue of joint vs unique control is helpful to distinguish corporatized LPEs, which constitute a separate legal entity but are owned by a single municipality, from the remaining types of LPEs. Third, if a local government shares control over an LPE, the question of whether this involves public or private partners is the final step to distinguishing public-public partnerships, i.e. inter-municipal cooperation, from public private partnerships in the form of public-private mixed firms. Figure 2 below summarizes the different possible types of LPEs (i.e. different types of governance structures).

Figure 2: Taxonomy of Local Public Enterprises (Source: Klien & Saussier 2013).



The three case studies we selected for this report concern cities that 1/ did not choose the same governance structure and 2/ that decided to switch from one governance structure to another.

Montréal: Locked in an Inefficient Choice?

From a historical perspective, the city of Montréal experienced only few changes in the way water services are provided (See Table 1). Since the 70s, water services have been provided through direct public management, either in a distinctive municipal department or within the public works department (between 1979 and 2010). Even if numerous indicators of service quality had pushed for change (i.e. underinvestment, leak ratio, etc.), this case shows how difficult it can be to move from one kind of LPE to another without a consensus among stakeholders.

Table 1: Montréal

Montréal *Citizens pay for water services through their municipal taxes – no user charges*	**Bef. 1979**: Direct public management (Aqueduc service) **1979**: The aqueduc service merged with roads, parks and building services within a new Public Work Department
	80's and 90's: Water dedicated staff and investments decreased. Expertise loss and low maintenance level **90's**: Move from direct public management to public-private LPEs is discussed but abandoned at the end of the 90's
	2000's: Transition period of amalgamation process. Proposition to create an autonomous water LPE but abandoned. **2003**:Following several reports pointing out the advanced deterioration of water infrastructures, creation of a water fund
	2010: Creation of the MWD that is a directly managed LPE : it brings together all water-related operations into a municipal department distinct from the Public Works Department

The creation of the MWD did not follow trends observed elsewhere in OECD countries, such as corporatization, organizational autonomy, or even marketization of water services management. On the one hand, the importance of trade unions in Québec and the strong popular opposition to any form of delegation of services makes it difficult to achieve organizational autonomy, even in a publicly managed form (i.e. Corporatized LPE or Public Private Mixed LPEs are not possible – See Graph 2). On the other hand, abundance and quality of raw water resources and the high tenancy rate in Montréal do not favour the development of a user-pays system. Finally, political tensions between local municipalities on the Island of Montréal make it difficult to establish an inter-municipal board.

As the case of Montréal shows, the goals to achieve a better balance between management autonomy and political and democratic control can prove very challenging. In the view of water services managers, the political process of setting priorities interferes with the technical requirements of a long-term plan. The events of the past decades show that it is indeed a political challenge to allocate resources to sectors that are less visible, taken for granted, and for which neglect has consequences mostly in the long run.

In addition, another challenge is the rebuilding of a trustful relationship between politicians and their public servants so that they can work together to achieve efficiency.

The MWD that was created in 2010 has made progress in recent years but still faces many challenges to fully catch up the past decline. The greatest of these challenges is without much doubt the reconstruction of internal expertise and knowledge. Since 2009, the Water Department has greatly increased hiring to rebuild its workforce and improve its ability to execute the service in-house and to manage contracts with external partners. However, this new generation still has to gain grounded experience that will only come in time.

Brest: Moving from Private Provision of Water to an LPE with Inter-municipal Cooperation

After a long period of private provision of water services (25 years long concession contract with Veolia), in 2010 the city of Brest decided to switch back to public management (See Table 2). This case is interesting because it demonstrates that such switch is possible and permits to identify the targets followed by the city. It is, however, too early to conclude whether it is a success or not.

Table 2 : Brest – Eau du Ponant

Eau du Ponant *Citizens pay for water services through user charges. Bills pay the LPE in charge of water services. "Water pays water".*	**90's 00's**: Water services are provided through long-term concession contracts with Veolia and through direct public management depending on which municipality involved in the LPE is considered Transparency of and involvement in the water services are an issue.
	2010: Creation of the LPE "Eau du Ponant" regrouping 4 local authorities – supplying water to 24 municipalities both urban and rural ones. The capital of the LPE is entirely public coming from those four local authorities. - A concession contract is signed between the LPE and each municipal authority without call for tenders - Still contracts with Veolia to operate 6 water treatment plants and associated reservoirs.

When "Eau du Ponant" was created, 90% of the local staff working for Veolia were transferred to the new SPL. Very little competence and know-how were therefore lost in the re-municipalization process, creating a rather smooth transition. However some specific competences were missing in the new structure. Employees had to be recruited for the call centre, for the invoice department and for the communication department.

The budget of the SPL is strictly distinct from municipal and inter-municipal budgets and it is funded directly by the customers water invoice. There is no contribution made by the municipal or inter-municipal budgets. The water price is revised yearly for each of the four water services according to a price revision formula embedded in the service provision contracts. SPL pays taxes and VAT as a private company. The budget of "Eau du Ponant" is discussed during the commission of resources where representatives of the four shareholders are present. The accounting of the SPL is controlled by independent auditors as well as by the revenue Court.

Before and during the switching process, a specific communication campaign has been implemented to explain the rationale of the SPL creation. An information brochure was sent along with the customer invoice. Public notices were posted and press conferences were held.

The reasons invoked for switching back to public management is the willingness of the city to increase the transparency of its management, the control capacity of its shareholders, the decision making processes which ensures the autonomy of tariff and investments policy for each contract and each water service.

On the downside, the fact that LPE did not have to face competition to be awarded the water services contracts has been questioned by some of the partners.

Each year, the SPL "Eau du Ponant" provides the four inter-municipal authorities with the technical data necessary to produce the regulatory annual report on water service quality and price, which each and every French water service is legally required to produce. However, these statutory performance indicators have been complemented with specific indicators agreed upon by the contractual partners. As of now, performance assessment is not used by the four local public authorities to reward or penalise their service provider "Eau du Ponant". It is used as a steering tool to manage efficiently the service rather than a real target driven incentive scheme. However, in the upcoming years, it is planned to use performance assessment, reporting and monitoring more concretely to achieve incentive compatibility. It will be interesting to see if such incentive schemes are actually implemented as it is questionable that cities, who own the Eau du Ponant LPE, would penalize themselves in case of bad performance.

Finally, a consultative water council has been set up. Once every three months, it gathers 12 local stakeholders such as consumers associations and environmental associations. It ensures public participation as it provides an opportunity for discussions on specific themes such as social tariffs or water supply security.

Stuttgart: Moving from Private Provision of Water to Direct Public Management

The case of Stuttgart city is highlighting that some shifts from one governance structure to another might be driven by other considerations than observed performance of public services. Following a referendum in 2009, this city is planning to move from private provision of water services (through a concession contract) to direct public management (See Table 3). Hence, in less than 20 years, the city will have experienced three different governance structures: corporatized LPE, private provision and directly managed LPEs (See the taxonomy provided in graph 2).

Table 3: Stuttgart

Stuttgart	**1933-1997**: Direct public management by the city of Stuttgart through a corporatized LPE
From Corporatized LPE to public-private partnership to non corporatized LPE.	**1997-2003**: Direct public management through a corporatized LPE named NWS AG (intermunicipal cooperation)
	2003-2014: Concession contract with EnBW that bought NWS AG
	January 2014: The municipality is expected to provide the service itself again, by expanding the existing directly managed LPE responsible for wastewater, forming a general provider for both water and sewage.

Maybe one of the striking points of the Stuttgart case is that it appears unlikely that the drivers of the programmed switch in 2014 are connected to public discontent with the provided service characteristics: water losses and service disruptions decreased during the concession period and water prices increased slower than in the decade before.

Potentially the most important driver was a shift in public attitude against privatization, which materialized, in the public movement the 'Stuttgarter Wasserforum'. After some initially successful campaigns, e.g. against the use of cross-border-leasing, in 2009 the organization launched a petition for referendum with the goal to re-municipalize water provision. Local elections in mid-2009 increased the momentum further as the topic became a major issue for the opposition parties to criticize the government. As a result, even before the end of the petition for referendum and just before the election, the governing party announced that it would support the re-municipalization.

Despite initial plans to keep EnBW, the private company involved in the service provision, pressure by the public movement and opposition parties ensured a complete privatization reversal, buying back not only the infrastructure but also integrating the service into the municipal administration.

However, two factors led to complications and slowed down the re-municipalization process. Firstly, the city was unable to take over the water provision immediately due to the lack of skilled personnel and expertise. Although EnBW was initially ready to assist during the transition period, it put the city government at a disadvantage in the negotiations. Secondly, after it was clear that

the concession contract would not be renewed, the city and EnBW were unable to reach an agreement about the buyback of the infrastructure. The different valuation methods led to a difference of several hundred millions of Euros. As a result, the city has taken legal action against EnBW to force a buyback.

Conclusion

The three cities selected for the case studies differ in many dimensions. However, we believe that several lessons might be learned from them. First, because water services involve investments in infrastructure that are partially not visible by the public, an underinvestment situation, degrading the service in a way that is not visible for the consumers (e.g. leak ratios) can prevail for a long period without any consequences for the governance structure in charge of the service. This aspect is reinforced in the case where users do not pay for the service, as it is the case in Montreal where payment is effected through taxes independently of consumed quantities. The consumers' willingness to pay appears essential.

Second, essential drivers, in addition to bad quality services, are the consumers and more broadly the citizens' willingness to be involved in the public service process. Hence, increasing transparency and reducing asymmetric information are often arguments pushing for re-municipalization of water services, as it is the case in Brest (and also as it has been the case in Paris on 2010). This driving force is present increasingly in recent years and not only in situations that are characterized by an initial absence of transparency.

This is also the third lesson coming from the Stuttgart case. More transparency and more involvement in the provision of water services may become very soon the rules rather than the exception. One open question is therefore to know if this is pushing for more direct public management, as it is the case in Stuttgart, or if other governance structure can adapt in order to achieve those newly imposed targets. The development in France of new contractual relationships between cities and private providers as well as the creation of a new entity – a LPE with mix capital (public and private) dedicated to one public private contract ("SEM à operation unique") show that governance structures are always evolving, raising the question of administrative capacity that must evolve with them.

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Local public enterprises

Canadian case study

Water provision in Montréal

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Case Study : The Montréal Water Department (MWD)

Executive Summary

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Local Public Enterprises in Québec[1]

In Québec, there is little talk of local public companies. Nonetheless, there are some "semi-autonomous and uni-functional local organizations, outside municipal councils." (Hamel, 2004: 339). These types of service providers are mostly found in sectors such as public transport, waste management and social housing. Some small municipalities join to provide water through an intermunicipal board (*régie*).

Local water services management in Québec

Drinking water and sanitation services management is a responsibility of local municipalities or agglomerations. Two provincial ministries are particularly relevant for the water sector: the Ministry of Environment, Sustainable Development, Wildlife and Parks (MDDEFP) and the Ministry of Municipal Affairs, Regions and Land Occupancy (MAMROT). In most Québec municipalities, municipally-owned facilities are operated by municipal employees. Operating costs and investments are covered by the general budget, which mainly comes from property tax revenues. There are few cases of water commercialization and metering in the province.

Local administrative structure: the City of Montréal and the Montréal Agglomeration

At the infralocal level, the City of Montréal is divided into 19 boroughs. Decentralization of powers to the boroughs was meant to counter opposition to the 2001 municipal amalgamation. In accordance with the City of Montréal Charter, local responsibilities are shared between the city council and the borough councils. The Montréal agglomeration brings together the 16 local municipalities on the Montréal Island territory, that is to say, the City of Montréal and 15 “linked cities” which have been de-almagamated and reconstituted in 2006. The agglomeration council is the democratic body responsible for common services, among which water.

Historical background

After a period of major investments in Québec province and in Montréal during the 1960s and 1970s, the 1980s gave way to a fiscal crisis. In 1979 the City of Montréal makes reorganized its services focusing on municipal employees' versatility. The aqueduct service was then merged with the roads, parks and buildings services within the new Public Works Department. In the meantime, wastewater collection and treatment were still a responsibility of the supra-local Montréal Metropolitan Community (CMM), later abolished during the 2001 mergers.

During the 1980s and 1990s, Montréal reduced capital expenditures in underground infrastructures and started to neglect maintenance and renewal. The water-dedicated staff decreased significantly and the effects of the expertise loss and lower maintenance levels were later confirmed by many expert reports, as well as spectacular water leaks.

[1] We exclude from this section directly managed LPEs (Under the proposed OECD taxonomy on local public enterprises table 2 p.22), that is to say, municipal departments, which remain by far the most common form of local public services provision in Québec.

The 1990s and 2000s saw various attempts to tackle the degrading infrastructures and need for investment. These were projected firstly under the leadership of politicians, for financial reasons. Popular opposition put an end to these delegation projects at the end of the 1990s. Secondly, during the transition period of the amalgamation process in 2001, a vision for water services management was elaborated by a group of managers that proposed the creation of an autonomous water LPE to the Transition Committee, which integrated this idea in its final proposal to the newly elected local officials. However, the managers' proposal was never discussed publicly and water services were entrusted to the Public Works, Transport and Environment Department of the new amalgamated city. However, the City did proceed to have numerous reports prove the advanced deterioration of its infrastructure, which led to the creation of a water fund in 2003 and major public works projects and contracts.

Agglomeration, local municipality and borough responsibilities for water in Montréal

The Montréal agglomeration is responsible for drinking water production, wastewater interception and treatment, as well as maintenance of primary networks and mains. The agglomeration delegates these operations to its local municipalities and most operations are thus carried out by the MWD. The MWD manages six primary water networks. One of these networks is connected to both Montréal factories and five other networks are connected to five other drinking water production plants on the territory of the linked municipalities.

The secondary water supply and sewer infrastructure falls under local municipalities' jurisdiction. Within the City of Montréal, these are under borough responsibility. Boroughs collaborate with the MWD for public works planning, data management, and financing. In fact, boroughs act like sub-contractors: they are paid by the MWD to perform works (or have them performed) according to centrally-defined priorities.

The MWD Governance and Operational Structure

The MWD is a *directly managed LPE*[2] established in 2010. It brings together all water-related operations into a municipal department distinct from the Public Works Department for the first time since 1980. The MWD is an entity operating under the City of Montréal's General Directorate. It manages operations for the City of Montréal, some in partnership with the boroughs, as well as for the Montréal agglomeration. Decisions are taken by the local government, that is to say, by the City Council or the Agglomeration Council. The Water Department is funded from the municipal central budget. Some works are financed by higher levels of government through grants or programs paid to local municipalities. The Water Department has no independent income directly related to the use of the services it provides. Indeed, citizens pay for water services through their municipal taxes and not by user charges. The Water Fund established in 2003 by a tax surcharge played an important role in the Water Department's ability to develop its activities and staff in recent years, within the municipal structure and despite the changing organizational context.

The MWD is organized into four operational directions (drinking water, wastewater, strategic networks management, and sustainable water management, corporate and emergency measures) and one administrative direction.

[2] According to the OECD proposed taxonomy on LPEs (table 2 p.22) and not to the local legal status.

Challenges for the MWD

The MWD did not follow trends observed elsewhere in OECD countries, such as corporatization, organizational autonomy, or even marketization of water services management. On the one hand, the importance of trade unions in Québec and the strong popular opposition to any form of delegation of services makes it difficult to achieve organizational autonomy, even in a publicly managed form. On the other hand, abundance and quality of raw water resources and the high tenancy rate in Montréal do not favour the development of a user-pays system. Finally, political tensions between local municipalities on the Island of Montréal make it difficult to establish an intermunicipal board, even if this idea has been discussed since the 2006 disamalgamation.

In this context, it is a challenge to achieve a better balance between political and democratic control and management autonomy. In the view of water services managers, the political process of setting priorities interferes with the technical requirements of a long-term plan. The events of the past decades show that indeed it is a political challenge to allocate resources to sectors that are hidden, taken for granted, and for which neglect has consequences mostly in the long-run.

Interestingly, Québec's local democracy faces the dominant vision of an apolitical municipal sphere. According to this view, municipal issues are more about effective management of technical services, for which values are not taken into consideration during decision-making. (Bherer et Breux, 2011: 4) "Municipal democracy in this context boils down to a question of local public services management, and is not the expression of a political agenda." (Collin, 2011: 343) Surely another challenge is the rebuilding of a trustful relationship between politicians and their public servants so that they can work together to achieve efficiency.

The MWD has progressed in recent years but still faces many challenges to fully catch up its past decline. The greatest of these challenges is without much doubt the reconstruction of internal expertise and knowledge. Since 2009, the Water Department has hired many people to rebuild its workforce and improve its ability to execute in-house and to manage contracts. However, this new generation still has to gain grounded experience that will only come in time.

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Contents

1. NATIONAL OVERVIEW ON LOCAL PUBLIC ENTERPRISES 15

1.1 Local public enterprises in Québec 16

1.2 Local public enterprises in Montréal 19

2. SETTING THE SCENE FOR THE CASE STUDY: FOCUS ON QUÉBEC'S WATER SECTOR 20

3. MONTRÉAL WATER DEPARTMENT GOVERNANCE 24

4. SWITCHING CONTEXT FOR THE MONTRÉAL WATER DEPARTMENT 28

4.1 The decade 1990-2000: privatisation projects and national water debate 29

4.2 The decade 2000-2013: Municipal reorganizations and projects towards an autonomous water organization 31

5. CHALLENGES FOR THE WATER DEPARTMENT 33

5.1 The City of Montréal's gradual loss of water expertise: still a challenge today 33

5.2 Managerial autonomy, political control and intermunicipal coordination 34

ANNEX I - THE QUÉBEC LOCAL ADMINISTRATION 37

ANNEX II - THE MONTRÉAL LOCAL ADMINISTRATION 40

REFERENCES 44

Local Public Enterprises
Case Study : The Montréal Water Department

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Introduction

This paper discusses the case of the Montréal Water Department. Montréal is the metropolis of Québec Province and the second largest agglomeration in Canada. The "water sector" in Canada and in Québec is not structured the way it is in European countries. In Europe, water utilities are organised in national associations, some of which have been established for decades. (EUREAU, 2009) Dutch, French, German and UK water associations and regulators, for example, are leaders in their field and provide extensive annual data on their respective water sectors.

We hope this case study will provide useful insights into a different kind of water-sector organisation, one that is less often discussed than its European counterparts. The water sector in Canada is more about an administrative public service provided by "municipal organisations" and less about "water utilities", in the sense of legally-distinct industrial and commercial enterprises.

Canadian local municipalities are not recognized in the constitution. Under section 92 of the *Act of British North America*, Canadian provinces have full jurisdiction over local institutions (UMQ, 2013: 11). "From a legal point of view, the municipalities' existence and the powers vested in them depend on the provincial government." (Collin *et al.*, 2010: 1) The case study presented here refers specifically to the context of Québec, which may differ from other Canadian provinces.

Because of the central role played by local administrations as the direct operators of water services, we have included a description of the Québec and Montréal local administrations in annexes at the end of this report, to which the reader can refer.

1. National overview on local public enterprises

1.1 Local public enterprises in Québec[3]

In Québec, unlike in Europe, there is little talk of local public companies or local public enterprises. Nonetheless, there are "semi-autonomous and uni-functional local organizations, outside municipal councils." (Hamel, 2004: 339) These organizations can be public, private or mixed, for-profit or nonprofit. They include paramunicipal, périmunicipal or supra-municipal organizations, boards (*régies*), intermunicipal boards and public transport enterprises. (Coulombe *et al.*, 2010) Paramunicipal and intermunicipal companies "are thriving in sectors such as wastewater treatment, regional transport, social housing and other services that municipalities choose to provide collectively." (Hamel, 2004: 343)

Local mixed enterprises

Local mixed enterprises (ME) are unifonctional agencies involving both private sector and municipal or supramunicipal organisations, most often a Regional County of Municipalities (RCM). Four ME projects were authorized by *ad hoc* laws in 1994 and 1995, and a framework law was adopted in 1997. The Act provides that the public shareholders must remain controlling and that MEs be considered public organisations in matters of access to information. (Hamel, 2004: 351) Despite this, Québec had only one operating ME in 2004. (Hamel, 2004: 349) Some MEs have been created since, especially in the field of waste management.[4] ME projects have not materialized more broadly in Québec because "Québec's transparency requirements uneasily answer the legitimate needs of the private sector." (Hamel, 2004: 349)

Some local Mixed Enterprises in Québec	
2004	**Compo-Haut-Richelieu** is the only operating ME in the province, owned 60% by the RCM du Haut-Richelieu and 40% by the company Compo-sortium, a former member of Suez-Lyonnaise des Eaux and later of Services Matrec Inc.
2004-2006	The **Société de développement durable d'Arthabaska Inc.** is created by the RCM d'Arthabaska and Gaudreau Environnement Inc.
2009	**La Sémer** is created by the RCM de Rivière-du-Loup and Envirogaz to do the conception, implantation and operation of a biomethane plant.
2012	The **Société d'Économie Mixte de l'Est de la Couronne Sud (SÉMECS) Inc.** is created by the RCM de Marguerite-D'Youville, the RCM de La Vallée-du-Richelieu and the firm Biogaz EG Inc. in order to process organic waste.

Paramunicipal organizations

Paramunicipal organizations are those that "the law declares officers or agents of a municipality and any organization whose board of directors is composed mainly of municipal council

[3] We exclude from this section municipal departments, the most common form of local public services provision in Québec.

[4]

members, as well as any organization whose board of directors is composed at least of one elected municipal official serving as such and for which a municipality or a metropolitan community approves the budget or contributes to more than half of the funding." (Coulombe et al., 2010: 13) These organisations must be audited by the municipality's auditor general.

Perimunicipal Organizations

A "perimunicipal organization" is controlled by at least one local municipality and is included in the municipal reporting entity. For example, a municipal enterprise, a public transport company, a leisure corporation or a local development center (LDC) are perimunicipal organizations. (MAMR, 2007: 7) A LDC is not, however, a municipal enterprise "because its revenues are derived primarily from sources within the RCM reporting entity." (MAMR, 2007: 16)

Municipal enterprises

A municipal enterprise is a form of intermunicipal or perimunicipal organization that:

- is a separate legal entity;
- possesses financial and operational powers to carry on commercial activities;
- has for main activity the sale of goods or the provision of services to individuals or organizations which are not included within the municipal reporting entity;
- may continue its operations and meet its liabilities with revenues not included in the reporting entity of the municipal organization.

"Ultimately, what essentially characterizes a municipal enterprise is its high degree of financial autonomy." (MAMR, 2007: 4) A commercial partnership between a municipal organization and another party to manage either assets, a business or an organization can be considered a municipal enterprise. "An intermunicipal board or an intermunicipal board of transport (CIT) is usually a partnership." (MAMR, 2007: 14)

Intermunicipal agreements and Intermunicipal boards (*régies*)

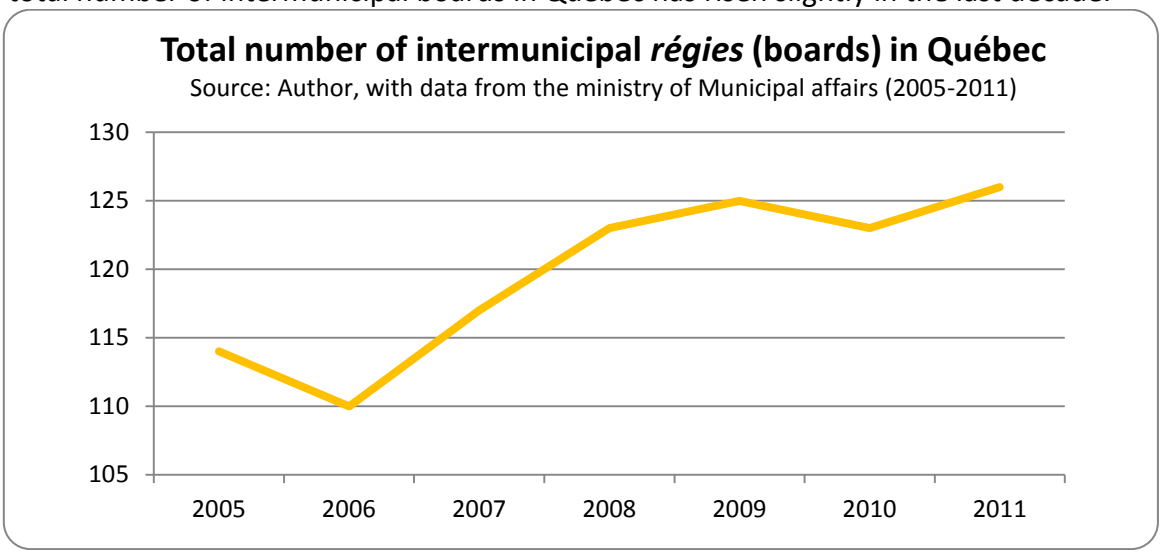
Intermunicipal agreements allow municipalities to share goods and services. Municipalities determine cost-sharing arrangements and decide which will be the operator: either one of the local municipalities party to the agreement, a supramunicipal organization (eg, RCM) or a separate legal entity established to manage the service (eg, an intermunicipal board). (MAMROT, 2013b) An intermunicipal board, when it is a commercial partnership, is considered a municipal enterprise as described above.

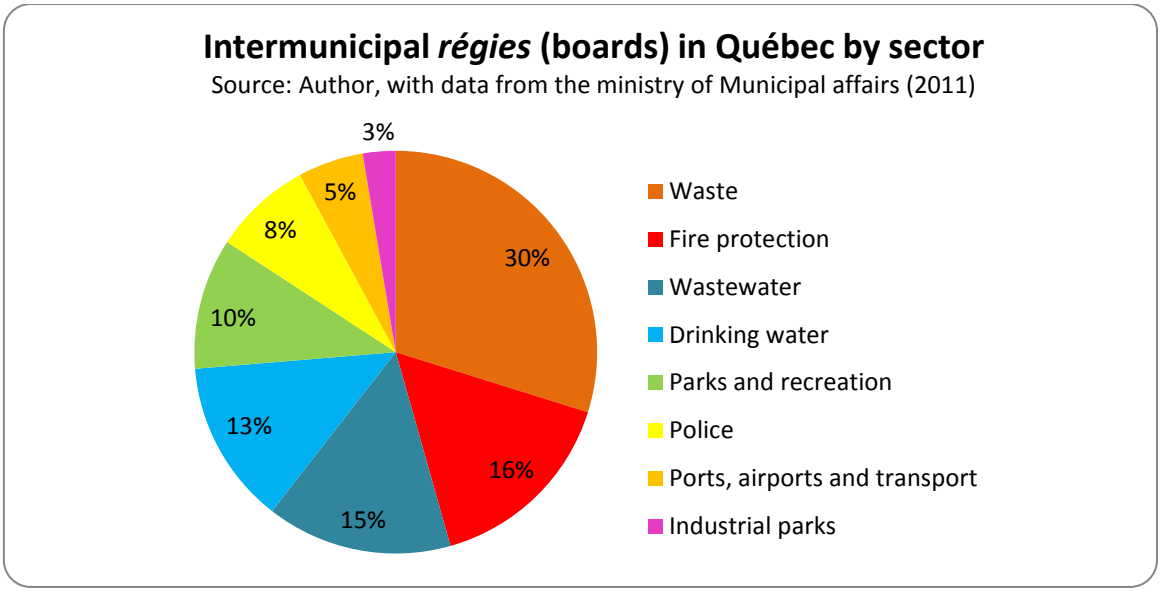
Drinking water supply and wastewater treatment are an exception, since the criteria for cost sharing are set by law: "Capital expenditure payments are proportional to each municipality's maximum consumption capacity. Operating costs are paid according to the actual consumption of each municipality, so long as it does not exceed, where applicable, the specified maximum capacity." (MAMROT, 2013b) The creation of an intermunicipal board is subject to the approval of the Minister of Municipal Affairs.

> "The intermunicipal board is a public law legal entity established for the joint management of the service covered by the agreement and is administered by a board where each participating municipality is represented. Intermunicipal boards are especially useful when the pooled services involve significant capital, affect a large number of municipalities and a significant population or are regional in nature. The Board of Directors is composed of representatives of the municipalities on whose territory the board has jurisdiction. The number of delegates from each municipality is determined in

the agreement and mentioned in the Minister's Decree establishing the intermunicipal board. Each municipality chooses its delegates among members of its council." (MAMROT, 2013b)

The total number of intermunicipal boards in Québec has risen slightly in the last decade.





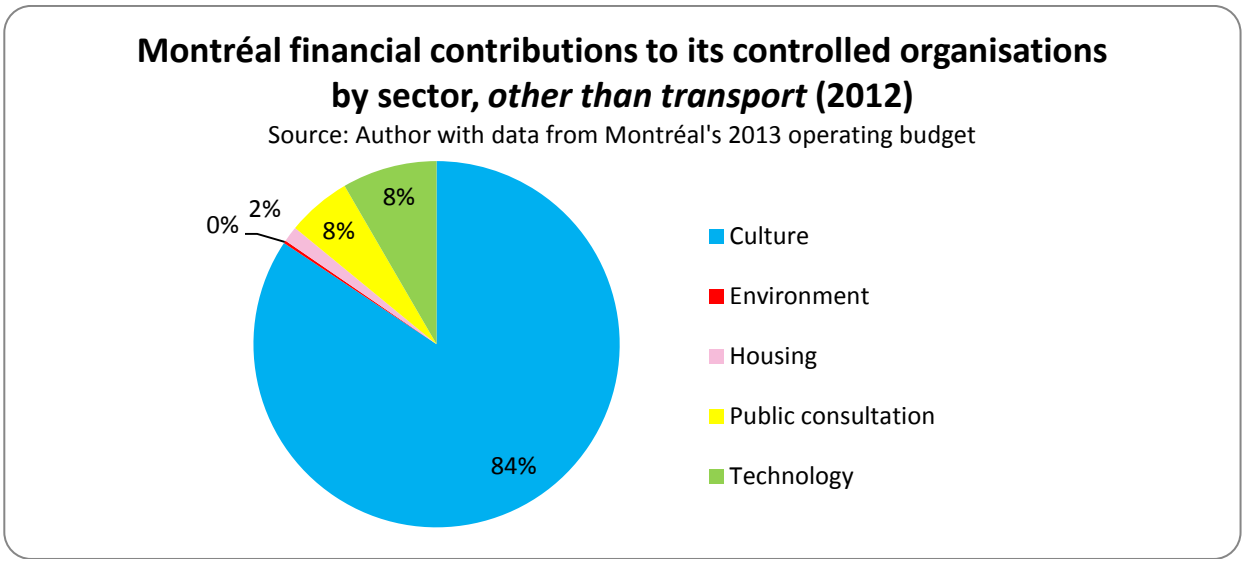
This form of intermunicipal collaboration is mostly used for waste management operations, followed by water and wastewater operations which account for 28% of intermunicipal boards. Given that these boards are usually created by small municipalities and operate small-scale operations they represent a very small portion of services rendered throughout the province.

According to 2011 and 2012 data from MDDEP and MAM there are 15 intermunicipal boards in charge of drinking water production and/or distribution. This is a very small proportion of water operations in the province: about 1% of drinking water production plants are operated by an intermunicipal board and about 0,27% of the municipally-served population is served through distribution networks managed by an intermunicipal board. These municipalities sometimes count only a few hundred or a few thousand inhabitants.

1.2 Local public enterprises in Montréal

In 2012, Montréal contributed 536.25 million $CAD to different organisations., some of them being "associated organizations", "paramunicipal enterprises" or "municipally-controlled agencies". Paramunicipal enterprises are mandated by the City and report to the Executive Committee annually. Municipally-controlled agencies are those included in Montréal's consolidated financial statements.

The City's financial participation in its controlled organisations by activity sector is shown in the following graph. We excluded Montréal's participation in the local public transit company, the Société des transports de Montréal (STM), its biggest beneficiary: the STM accounts for 74% of the City's financial contributions to outside organisations and 93% of the City's contributions to its controlled organisations.



The STM is a public corporation governed by a board of directors composed of elected officials and two public transit users' representatives. Nearly half of its revenues come from user fees, although it is also funded by the agglomeration of Montréal as well as government grants. The STM has its own staff and management but is included in the City's consolidated financial statement and organizational chart.

Montréal also controls the *Société de vélo en libre-service*, a commercial organisation providing user-financed bicycle services in Montréal and other cities around the world. It can be considered a "municipal enterprise" as defined in section 1.1.

As shown in the table below, the governance and management structures of Montreal LPEs are diverse. Some have their own staff and publish independent financial reports while others are very small and "borrow" all their employees from City of Montréal staff. Many have City Council or Agglomeration Council representation on their boards, while others are independent bodies. Some organisations in all of these categories are included in the City's organizational chart, but not all of them (see Annex II).

Categorization of the different types of LPEs in Montréal Source: Author with data from City of Montréal		
Paramunicipal enterprises (Report to the Executive Committee annually)	**Municipally-controlled agencies** (Consolidated in Montréal's financial statements)	**Associated organizations** (Autonomous management)
Corporation d'habitation Jeanne-Mance (*1958 - City represented on the Board*) Office municipal d'habitation de Montréal (*2002 - Non-profit organisation with board members appointed by Agglomeration Council*). Société de gestion Marie-Victorin (*1998 - Board members appointed by the City and by the government, no employees of its own*)	Société de vélo en libre-service (*2009 - user-financed bicycle service*) Fiducie du Technoparc de Montréal (*1987*) Montréal Arts Council (*1956 - Non-profit independant organisation*) Montréal Intercultural Council (*2003 - Independant organisation and consultative body to the City Council*) Office de consultation publique de Montréal (*2002 - Independant agency with mandates fromMunicipal Council or Executive committee*)	Electrical services Commission (*1910 - Included in City budget*). Société du musée d'archéologie et d'histoire de Montréal, Pointe-à-Callière (*1992 - Non-profit Corporation with City representatives on its board*). Société locale d'investissement dans le développement de l'emploi (*Non-profit organisation supporting businesses*)
Corporation Anjou 80 (*1979 - Non-profit organisation*) Société du parc Jean-Drapeau (*2006 - Non profit organisation*) Société d'habitation et de développement de Montréal (*1980 - Board members appointed by Montréal Executive Committee*) Société de gestion du port de plaisance de Lachine (formerly Société de gestion NauBerges de Lachine)	Société de transport de Montréal (STM) (*1951 - Autonomous commercial enterprise partly financed by the City and with City representatives on its board*) Société en commandite Stationnement de Montréal (*1995 - Subsidiary of the Metropolitan Montréal Chamber of Commerce*)	

Appart from the public transit and the bicycle companies, Montréal LPEs are mostly NGOs operating small-scale activities such as parks, museums and housing units.

2. Setting the scene for the case study: focus on Québec's water sector

In Québec, drinking water and sanitation services management is a responsibility of local municipalities. Water utilities are mostly municipal departments, or directorates within bigger municipal departments such as Public Works.

In most municipalities, municipally-owned facilities are operated by municipal employees. Operating costs and investments are covered by municipal revenues, mainly from property

taxes. The operator being the municipality itself, we do not speak of water LPEs. However, municipalities can jointly manage equipment or services through intermunicipal water boards as discussed in section 1.1.

The 11 Québec agglomerations have authority over water services in their territory. The agglomeration delegates operations to one or more of its constituent local municipalities. In the case of larger cities, infra-local borough administrations are responsible for secondary network maintenance.

Municipalities can delegate water operations to the private sector through contracts. In the wastewater sector, where the private sector is more present than in the drinking water sector, 153 municipal treatment plants are operated by a private company and 679 plants are operated by municipalities or intermunicipal boards.[5]

Drinking Water Supply in Québec Source: Author with data from MDDEP			
Type of drinking water supply	**Municipal drinking water production plant**		Other type of supply (i.e. private well)
	Surface water	Groundwater	
% of the population	70 %	15 %	15 %
Number of production plants	236	717	n/a

The following chart describes roles and responsibilities of provincial ministries and other water-sector relevant organisations.

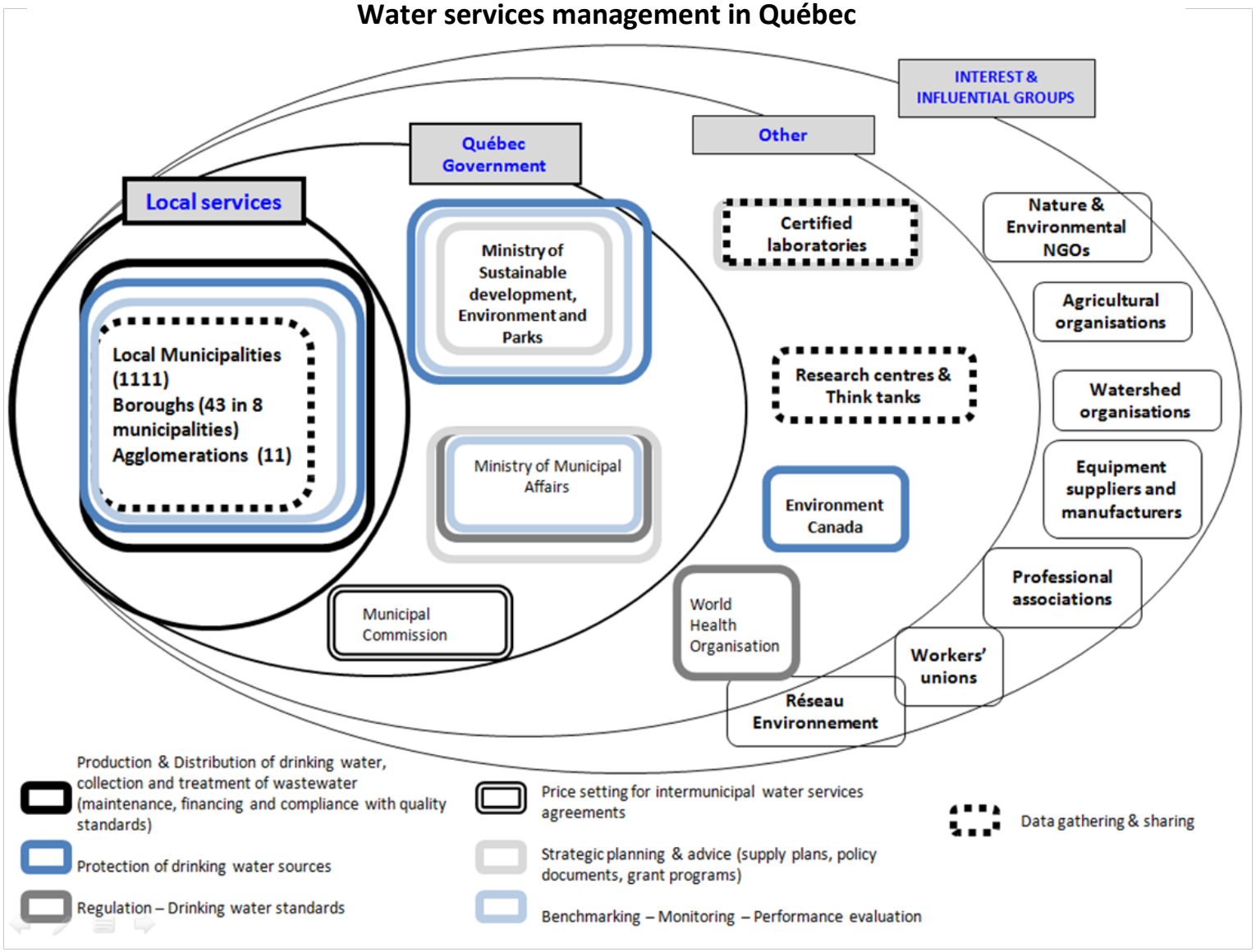
Ministry of Municipal Affairs, Regions and Land occupancy ("MAMROT")
Regulates and monitors local municipalities. Manages infrastructure programs in support to municipalities. Ensures that infrastructure projects satisfy norms and by-laws. Responsible for the Québec Strategy for reducing drinking water use. Has responsibilities regarding National Water Policy implementation. Manages a database on municipal wastewater treatment.
Ministry of Sustainable development, Environment and Parks ("MDDEP")
Regulates drinking water standards (by-law on drinking water quality)[6] Regulates wastewater treatment and discharge standards. First interlocutor of water utility operators in water non-conformity or emergency situations. Controls utility operators and laboratories to ensure they meet their obligations.

[5] Unfortunately, the MDDEP could not provide similar data for drinking water utilities operated by the private sector.

[6] http://www.mddep.gouv.qc.ca/eau/potable/brochure/

Monitors water quality through by-law enforcement and surveillance programs. Manages the program that certifies laboratories. Centralizes and manages water quality data. Government interlocutor for the Association of Québec watershed boards. Has responsibilities regarding the implementation of the National Water Policy.
Municipal organisations
Responsible for water provision and wastewater treatment. Set strategies and operations to comply to regulation and norms. Must send water samples to certified laboratories.
Certified laboratories
Report promptly out-of-norm analysis to utility operator, MDDEP and local Health Departments. Report electronically all water analysis results to the MDDEP.
Ministry for Employability and Social solidarity
Capacity building: Offers a certification program to water utility employees.
Ministry of Education, Sports and Leasure
Capacity building: Approves professional and technical education programs in the field of water treatment and distribution.
Ministry of Agriculture, Fisheries and Food
Controls bottled water quality. Ensures that food establishments implement appropriate measures during boil advisory situations.
Québec Municipal Commission (QMC)
Government agency which acts as tribunal, investigation, administration and counselling organization. Fixes rates in intermunicipal sale of water or sewer services.
Environment Canada
Regulation and legislation at the Federal level for environment protection and boundary waters.
Réseau Environnement
Is a platform for technical exchange and capacity building between water utility professionals, private sector consultants, equipment manufacturers and suppliers, researchers and governments. Provides input to ministries, government agencies and legislators.. Is the Québec chapter for the American Water Works Association, the Water Environment Federation and the Canadian Water and Wastewater Association.

Water services management in Québec



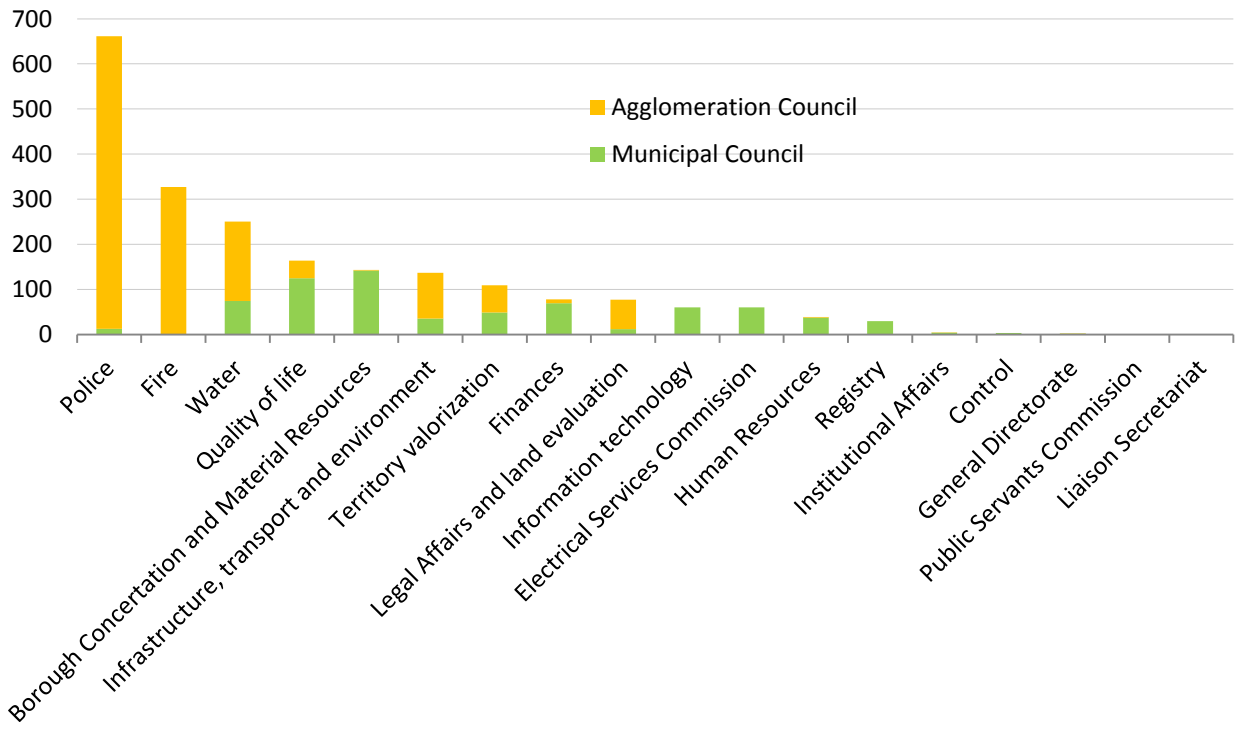
3. Montréal Water Department Governance

The Montréal Agglomeration is responsible for drinking water production, wastewater interception and treatment, as well as maintenance of primary networks and mains. The City of Montréal, as the main city in the agglomeration, is responsible for operations. The Montréal Water Department (MWD) is an entity operating under the City of Montréal's General Directorate. It manages operations for the City of Montréal, some in partnership with the boroughs, as well as for the Montréal agglomeration.

The City of Montréal's operations are divided in its budget by whether they are achieved under local responsibilities or under agglomeration responsibilities. However, it is the same administration providing the services. The MWD is the third biggest *central* (excluding borough-level) service in terms of expenses, after public security departments, with annual operational costs of approximately 250 million $CAD (see Annex II for the corresponding Montréal organizational chart).

Montréal Central Services Operating Expenses by Business Structure (2012, million $CAD)

Source: Author with data from Montréal's borough and central services operating budget 2013



Primary drinking water infrastructures

The MWD manages six primary drinking water networks. One of these networks is connected to both of the Montréal drinking water production plants and five other networks are connected to five other plants on the territory of the related municipalities. "Although certain primary network assets (including plants) may have (or have had in the past) a local vocation, these are

now considered an agglomeration jurisdiction, and not a local one." (Ville de Montréal, 2011: 103) This centralisation of water production plants management has had a positive impact on water services management by pooling expertise and allowing technical support between civil servants of Montréal and other cities. This was not the case before amalgamation when each administration functioned independently: for political reasons, employees turned to private consultants instead of to their neighbouring local counterparts.

The MWD also manages the primary sewer networks and the island's wastewater treatment plant.

Secondary drinking water and sewer infrastructures

The secondary water supply and sewer infrastructures fall under local municipalities' jurisdiction. (Ville de Montréal, 2012: 41) Within the City of Montréal, these are under borough responsibility. (Ville de Montréal, 2011: 35) Boroughs collaborate with the MWD for public works planning, data management, and financing. In fact, boroughs are like sub-contractors: they are paid by the MWD to perform works (or have them performed by a contractor) according to the priorities defined centrally.

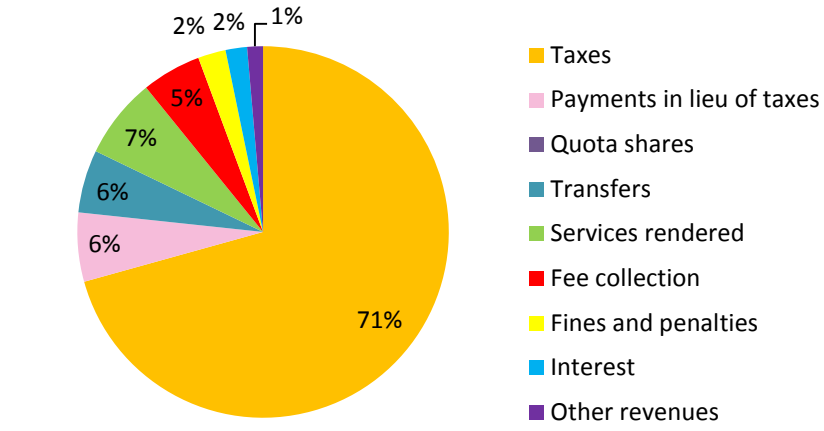
To categorize infrastructures as "primary " or "secondary" many technical factors must be taken into consideration, such as pipe size or strategic importance for network loops. Local municipalities tend to advocate for their infrastructures to be classified as "primary" as much as possible to pass the financial burden to the agglomeration. Distribution of infrastructure responsibilities between local "related" municipalities and the agglomeration is not always transparent.

Municipal revenues

The MWD' operating expenses are covered by the City of Montréal or Montréal Agglomeration central consolidated budgets. In both cases, revenues come mostly from taxes and transfers. Taxes are mainly property taxes based on land and real estate value. Municipal revenues from fees are very low, as shown below. The Water Department has no independent income directly related to the services it provides. Montréal's revenues from intermunicipal water services agreements (i.e. drinking water sale to related municipalities) are pooled in the consolidated municipal budget and are not MWD revenues.

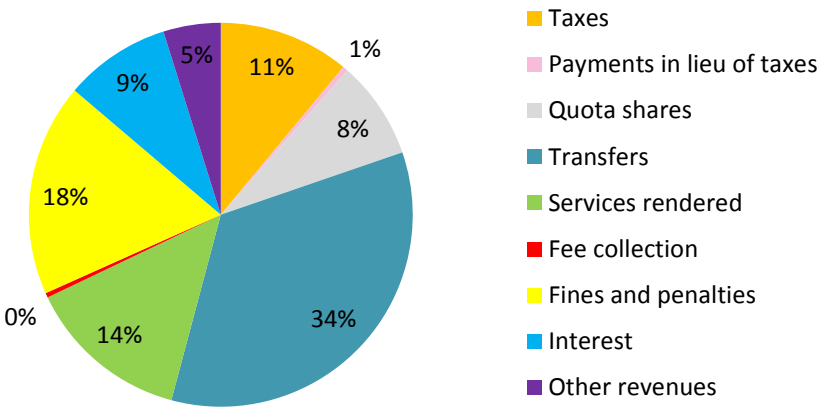
Sources of muncipal revenues for local responsabilities

Source: Author with data from Montréal's 2012 financial report



Sources of muncipal revenues for urban agglomeration responsabilities

Source: Author with data from Montréal's 2012 financial report



Government grants

Some infrastructure works are financed by higher levels of government through grants and programs administered by the MAMROT. Since the adoption of the Québec National Water Policy in 2002, admissibility to government subsidies became conditional to having a municipal water infrastructure *intervention plan*. The MWD has completed its intervention plan in 2010. (VGVM, 2013: 177-185)

The Water Fund

The Water Fund, paid for by a property tax surcharge, was established in 2003 by the municipal administration. This fund played an important role in the MWD's ability to develop its activities

and staff during the past decade, within the municipal structure and despite the changing context (which will be discussed later):

> "Over time, (...) the initial vision of the Water Fund - and even the use that has been made of it - has expanded. It stopped concerning only the financing of major works. It gradually started to cover the financing of activities, even those internal and preparatory to the great works, and, ultimately, all revenues necessary to finance the entire water management. In short, what was originally an *ad hoc* tool associated with a specific program (catching up) has become a *de facto* tool for all water management." (Ville de Montréal, 2011: 114)

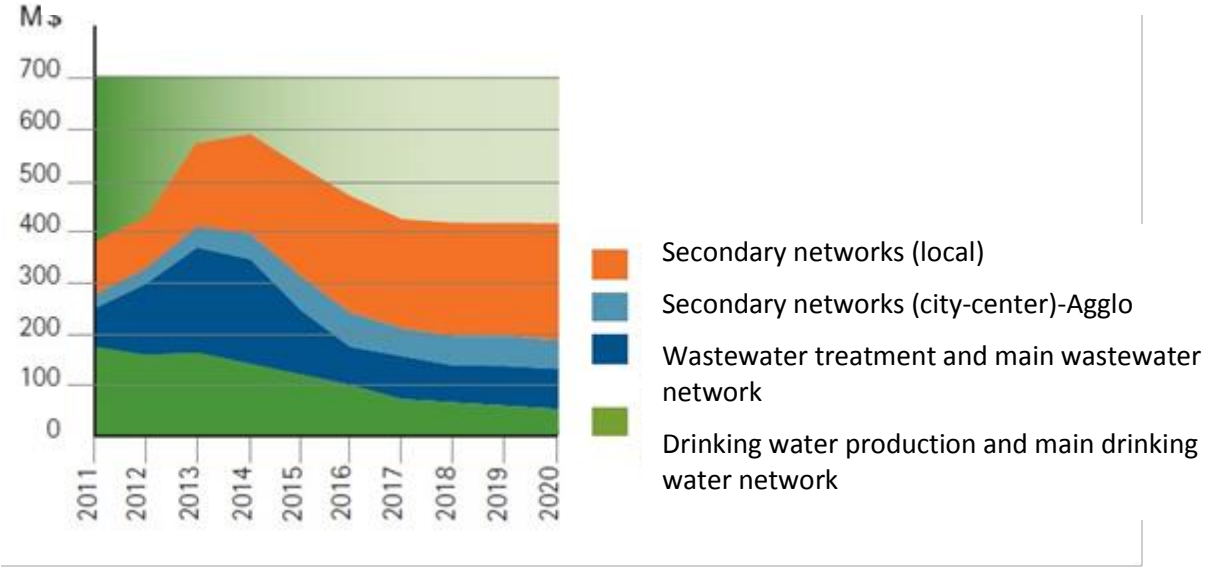
Investment needs

Water sector investment needs were theoretically estimated in 2003 by consultancy firms at 200 million $CAD a year during 20 years, or 1,5 billion dollars, in order to recover accumulated investment deficit and renew assets at the target rate of 1%/year. (VGVM, 2013: 201) Between 2004 and 2011, Montréal did not reach the 200 million investment target and the cumulated deficit kept rising. In the meantime, construction work and more precise information gathered on the network itself led the MWD to declare in 2010 that investment needs had been under-estimated by half in 2003. The revised cumulated deficit was calculated to be 3,6 billion dollars at the end of 2011.

In 2012, the Agglomeration Council approved the MWD's 10-year strategic plan and 2011-2020 financing plan of 4,6 billion dollars. However, many points of this plan's execution remain uncertain, as the municipal triennial capital investments are approved yearly. Moreover, the agglomeration council did not raise the water tax surcharge as proposed in the investment plan for 2013. This led the City's Auditor General to state that the municipal council and agglomeration council must determine what level of service they want to achieve, as well as the corresponding levels of long-term investments and a realistic long-term funding method. This is essential for the MWD's managers to be able to set intervention priorities. (VGVM, 2013: 208)

Investment needs in Montréal Agglomeration Water Infrastructures

Source: Ville de Montréal, 2011, p. 99



Operational Structure
The MWD is organized into four operational directorates and one administrative directorate.

MWD operational structure	
Drinking Water Directorate	Production and distribution of drinking water. Management of water mains and reservoirs.
Wastewater Directorate	Manages the main sewer network and the wastewater treatment plant.
Strategic Water Networks Management Directorate (SWNMD)	Manages the secondary networks in partnership with the boroughs.
Sustainable Water Management, Corporate and Emergency measures Directorate	Manages activities related to water metering in industries, businesses and institutions and to the provincial program for reduction of drinking water use.
General Water Directorate	Monitors investment and financing plans. Supervises the Montréal 2011-2020 Water Strategy.

The Strategic Water Networks Management Directorate (SWNMD)
It is through the SWNMD that the MWD manages its relations with the 19 boroughs. The SWNMD manages a budget that it can allocate based on intervention plan priorities and yearly partnership agreements with boroughs. It appears however that a significant proportion of the budget is not used to initiate investment projects that were prioritized and included in the partnership agreements. (VGVM, 2013: 221) In a context where so much catching up is urgently needed, this is preoccupying.

The SWNMD is responsible for the establishment of a database on the state of the secondary network, which is still incomplete. Knowledge about the state of the network does not yet allow efficient prioritization and the intervention plan is not always a reliable tool for decision-making. (VGVM, 2013)

Finally, responsibility sharing between SWNMD and boroughs does not work towards achieving efficient integrated planning. The SWNMD is responsible for investments, and plans interventions such as rehabilitation and replacement. Meanwhile, boroughs independently determine operating expenses for maintenance and minor repairs. Boroughs are thus responsible for preventive maintenance, but the consequences of neglecting this maintenance are reflected in the SWNMD capital budget. (VGVM, 2013: 199-200)

There is clearly a lack of coordination between the boroughs, the MWD and other municipal services, like the Infrastructure Department (which often executes the City's construction works), to efficiently plan and execute operations on the secondary network.

4. Switching context for the Montréal Water Department

After a period of major investments in Québec and Montréal during the 1960s and 1970s (1966 subway construction, 1967 World Expo, 1976 Summer Olympic Games), the 1980s gave way to a fiscal crisis and a period of fiscal restraint. The local level is no exception and in 1979-1980 the

City of Montréal made a major reorganization focusing on the versatility of municipal employees. The aqueduct service was merged with the roads, parks and buildings services within the new Department of Public Works.

Montréal then reduced capital expenditures in underground infrastructures and neglected their systematic maintenance and renewal. These investments were not considered to be politically profitable. On the contrary, road works were a nuisance to traffic and businesses. Meanwhile, the water-dedicated staff decreased significantly. From the late 1980s and during the following decades, the effects of the expertise loss and lower maintenance levels became increasingly apparent. It was later revealed that some pipes put in place during the 1970s were badly-conceived: they did not prove resistant to corrosion from water infiltration charged with de-icing salts used abundantly on the streets in cold weather. By the 2000s, infrastructure degradation was confirmed by many expert reports, as well as spectacular water leaks. (Blais-Poulin, 2013; Canada NewsWire, 2013; Croteau, 2007)

The water services management organization in Montréal has evolved from the former Public Works Department created in 1979 to the current Montréal Water Department (MWD) created in 2010. The MWD brings together all water-related operations (drinking water and wastewater) into a municipal department distinct from the Public Works Department (now called the Infrastructure, Transport and Environment Department), for the first time since 1980.

Since 1990, reorganisation projects were discussed but never implemented. These initiatives were undertaken sometimes under the leadership of politicians and sometimes under that of the public servants (managers). Firstly, there was an unsuccessful delegation project (privatization). Secondly, Montréal water services managers proposed the creation of an autonomous local public company responsible for the management of all water-related activities on the territory of the island of Montréal. This project did not materialize. Thirdly, following the disamalgamation in 2006, the idea of creating an intermunicipal board is discussed. This section will analyse these various projects and the reasons for their failures.

4.1 The decade 1990-2000: privatisation projects and national water debate

The 1990s were the stage of privatization discussions, first within closed circles at the City of Montréal and then at large in Québec society. Primarily motivated by municipal financial constraints and strained relations with unions, this idea was also in the spirit of the times. Under the administration of Mayor Jean Doré at the beginning of the decade, serious discussions took place about "change options" for the City's water management. An internal city working group presented in 1991 a first report on *Water management in Montréal: some options for change*. This was followed by a second report in 1992, *Water management in Montréal: an option for change*. (Audette-Chapdelaine, 2008; Ville de Montréal, 1996) The same year, the Drinking Water Industrial Chair at the École Polytechnique de Montréal (engineering school) was inaugurated. The Chair included representatives from the City of Montréal, the City of Laval, Groupe John Meunier, the compagnie Générale des eaux, and the consulting firm Vallée Lefebvre et associés. This Chair played an important expertise-building role during the following decades and became a privileged source of information and advice for water-related decision-making in Québec. Also in 1992, the government announced its intention to update the drinking water quality regulation, which was still based on 1978 standards. This "would force many cities to update part of their drinking water treatment process."(Francoeur, 1992) In 1993 and 1994,

the City of Montréal's Executive Committee and the Public Works Department discussed modalities for setting up a water services mixed enterprise in Montréal. (Bibeault, 1997; Ville de Montréal, 1993, 1994) Discussions were underway with French water sector companies and the Union of Montréal blue-collar workers was invited to Europe by Bouygues in January 1994.

Until the election of a new mayor at the end of 1994, Pierre Bourque, these projects did not attract any public or media attention. (Audette-Chapdelaine, 2008) During 1995 and 1996, however, these initiatives gained more visibility. Both the City of Montréal and the Ministry of Municipal Affairs (MMA) continued to consider possible changes in water management, including the participation of private companies. The MMA commissioned a study on the state of water and sewer infrastructures in Montréal from the INRS-ETE, the CERIU and CNRC and established in February 1996 its *Proposal for a Québec water services privatization model*. (MAM, 1996) At the end of 1996, a bill on mixed enterprises was presented at the National Assembly. In Montréal, local elected officials prepared a *Green Paper on water management*. (Ville de Montréal, 1996)

Mayor Bourque's public announcement of his will to privatize municipal services raised a strong opposition from unions, which set in motion their resources and allied with artists and environmentalists to gain high media visibility. (Audette-Chapdelaine, 2008: 89; Le Devoir, 1997; St-Pierre, 2005) The year 1997 began with the creation of the *Coalition for a public debate on water in Montréal* and *Eau Secours! The Québec Coalition for responsible water management* which brought the debate to provincial scale. Public opinion pressure against all form of water services delegation forced the Québec government to impose a moratorium on all partnership projects, to exclude water services from the Act on mixed enterprises in the municipal sector, and finally, to announce a public consultation on water management at the end of 1997. Given the scale of the debate, which included not only municipal services options, but also underground water resources management and water exportations, the case was entrusted to the Office of Public Hearings on the Environment (BAPE) in autumn 1998. The provincial government thus temporarily replaced elected officials and local administrations at the helm of the debate. In May 2000, the BAPE submitted its final report which did not recommend privatization or mixed enterprise projects. (Bureau d'audiences publiques sur l'environnement (BAPE), 2000). This led to the Québec National Water Policy in 2002. (Gouvernement du Québec, 2002; St-Pierre, 2005)

During the 1990s, in parallel with political initiatives and union and popular mobilization, managers of the water service also began thinking about water management in Montréal. Prior to the amalgamation in 2000, the Montréal Urban Community (MUC), a supra-municipal authority, oversaw wastewater management across Montréal Island. It is in the MUC administration and more particularly in its wastewater treatment plant that a global vision for the management of all water-related activities on the island of Montréal was first considered. It is also MUC managers that first became aware of the large volume of water to be treated, and therefore the need to control usage and leaks upstream. This is important because after the BAPE report and the National Water Policy, elected officials (provincial and local) tended to stay away from the delicate question of water services organization in Montréal and it is the managers who took over the organizational change initiatives over the following decade.

4.2 The decade 2000-2013: Municipal reorganizations and projects towards an autonomous water organization

Just weeks after the filing of the public hearing report in May 2000, the "Walkerton tragedy" in the province of Ontario caused 7 fatalities and 2,300 sick people due to a drinking water network contamination[7]. The context was thus particularly favourable for the Québec Ministry of Environment to update the drinking water quality regulation in 2001, as announced ten years earlier, and for the adoption of the Québec National Water Policy, in 2002.

At the administrative level, the Québec Government carried a territorial reorganization in 2001 which had a great impact on local governance and services management. "The forced amalgamation of local municipalities imposed by the government was without a doubt the element of the reorganization that caused a strong sense of discontent among the population in some of the municipalities affected by these measures." (Rivard *et al.*, 2005: 6) The new City of Montréal, created by the amalgamation of all local municipalities on the Island of Montréal, was responsible for the management of the entire production, distribution, collection and treatment of water. (Fleury, 2003)

This amalgamation process brought together a dozen managers, some of whom were related to the ex-CUM and others to the public works departments of the various ex-local municipalities on the island. During the transition period, this more or less formal group of managers elaborated and proposed their vision *For an Integrated and autonomous water management in Montréal*, that is to say the creation of a water LPE. (GTIU, 2001) The Transition Committee integrated this idea in its final proposal to the newly elected local officials. However, the new mayor Gérald Tremblay did not take action in this way and water and wastewater management were instead entrusted to the Public Works, Transport and Environment Department (SITE) of the new amalgamated city.

Elected officials did however take note of the urgency of water infrastructure degradation and the "new City of Montréal" commissioned three studies (CFC, 2003; PriceWaterhouse Coopers, 2002; SNC-Lavalin et Dessau-Soprin, 2002) that confirmed the alarming state of the deteriorating infrastructure, as discussed in section 3 above. In 2003, an entity was created within the SITE: the *Group for the development of water management*, to manage the follow-up on these reports. The same year, the city created the Water Fund.

In 2005-2006, the Group for the development of water management was replaced by a new Water Directorate, still within the SITE, that was also entrusted with the administration of the Water Fund and what is called the Great water works, a 20-year program to upgrade the plants and the networks and to install water meters for commercial, industrial and institutional users. (Ville de Montréal, 2011: 6) Within the Water Directorate, the Strategic water networks management directorate (SWNMD) was responsible for planning and allocating funds for the secondary distribution network, in collaboration with the boroughs, as we discussed in section 3. (Ville de Montréal, 2011: 6)

[7] Montréal issued a preventive boil advisory to the population in 2013 because the water level in one of its main drinking-water reservoir went below its normal level, which resulted in out of norm turbidity. Although this caused disagreements to the population and businesses, the water was not contaminated. The reasons as to why the water-level dropped in the reservoir are still being studied.

The 2006 municipal "disamalgamation", following an electoral promise by the Liberal government during the 2003 campaign, led to the reconstitution of 15 out of 28 municipalities on the Island of Montréal and the establishment of the Montréal Agglomeration, with a new division of local responsibilities and increased organizational complexity. (Rivard *et al.*, 2005: 16) Water management responsibilities were shared as follows:

Responsibility sharing between the Montréal Agglomeration and its constituent municipalities	
Agglomeration	Equipment and infrastructure for water supply and wastewater treatment, except local water networks.
Local municipalities (City of Montréal and 15 related cities)	Local drinking water and sewer networks.
Responsibility sharing within the City of Montréal	
Central city	Plants, water mains and reservoirs
Boroughs	Secondary water mains

In the disamalgamation context, the idea of a water services autonomous entity resurfaced. The City of Montréal proposed the creation of an inter-municipal autonomous organization in a memoir submitted to the National Assembly's Land Use and Planning Commission during the hearings on Bill 22 (*Act amending various legislative provisions regarding Montréal*):

> "In 2001, the idea of creating an administrative body to manage water on the island was under discussion between the City and the Montréal Urban Community. With the new agglomeration, this issue has resurfaced. The City Council is willing to take the matter outside the City's current activities and entrust it to a specialized public organization governed by representatives appointed by the expanded city council and where reconstituted cities could play a significant role. We thus think it is possible to unite rather than divide all the island's related cities' assets' potential to provide the best possible service at the lowest possible cost. Discussions are ongoing on the subject and we are certain that we can put forward a proposition to the parties' satisfaction in order to manage this valuable resource in the most responsible way possible." (Ville de Montréal, 2007)

The provincial government also seemed favourable to the creation of an autonomous water management organization in Montréal, as was expressed in particular by the Minister of Municipal affairs in June 2008 during the study of the same bill: "(...) we will of course set up a working group with Montréal and the reconstituted cities for the possible creation of a water management paramunicipal organization. (...) We will work hard on building and developing a bill that will see the birth of a new paramunicipal company which will allow a thorough cleaning of Montréal agglomeration water management." (ANQ-CPAT, 2008)

However, these discussions did not lead to a change in the organizational form of water services management in Montréal. The political environment became increasingly difficult for the Liberal government, with numerous allegations of collusion and corruption that only worsened (Unité permanente anticollusion, 2011) until the establishment of the *Commission of Inquiry on Public Contract Attribution and Management in the Construction Industry* in November 2011.[8] Although the issue goes well beyond the water sector, it is in this corruption context that the

[8] https://www.ceic.gouv.qc.ca/accueil.html

City of Montréal Auditor General issued a report (VGVM, 2009) which cancelled, in 2009, a controversial contract (Champagne, 2007; Coalition québécoise pour une gestion responsable de l'eau - Eau Secours!, 2007; Corriveau, 2007; Descôteaux, 2007; Lévesque, 2007b, 2007a) which had been awarded to a consortium of contractors in the context of the 2007 great water works.

Following the "water-meters scandal", the Water Department received in 2010 a mandate to implement a follow-up to the Auditor General's report. (Ville de Montréal, 2011: 6) This episode served as a new catalyst for managers of the water service to once again advocate with elected officials for their vision of water management in Montréal and among other things, the need for a long-term financing plan. The managers were granted more time and a wider mandate and set up a *Monitoring Committee for the optimization of the drinking water network*. This committee wrote the *2011-2020 Water Strategy*. (Ville de Montréal, 2011) At the same period, in June 2010, the City transformed the Water Service Direction in a Water Department directly under the City's General Direction. (Ville de Montréal, 2011: 6)

Despite the turmoil following the disamalgamation and the complex distribution of water responsibilities and operations among local administrations, the water fund established in 2003 continued to provide income to the Water Department and led to the hiring of staff and slow rebuilding of its expertise and internal capacity. As we will see in the next section, internal expertise has been one of the main challenges for the MWD in the past decade.

5. Challenges for the Water Department

The Montréal Water Department (MWD) did not follow trends observed in Europe such as corporatization, organizational autonomy, or even marketization of water services management. Many factors explain this situation, despite the managers' desire for more autonomy and a depoliticized financing plan and decision-making process.

On the one hand, the importance of trade unions in Québec and the strong popular opposition to any form of delegation of services make it difficult to achieve organizational autonomy, even in a publicly managed form. On the other hand, abundance and quality of raw water resources and the high tenancy rate in Montréal do not favour the development of a "pay for use" system. The issue is more about infrastructure funding and efficient management than consumption decrease. Finally, political tensions among local municipalities within the Montréal Agglomeration make it difficult to establish an intermunicipal board.

As we will see now, the Montréal Water Department has progressed in recent years, but it still faces many challenges to fully catch up on its past decline, as we have outlined in section 3.

5.1 The City of Montréal's gradual loss of water expertise: still a challenge today

Before the 1980s, the City of Montréal[9] had good internal expertise with regard to infrastructure, in terms of blue collar workers as well as engineers and managers. During the

[9] This refers only to drinking water, as wastewater management then fell under the Montreal Urban Community jurisdiction and not the City of Montréal.

1970s, blue-collar workers were experts in inspection and repair and there was even a certain prestige associated with being part of the Aqueduct Department staff. Employees of the water network at the time were competent and knowledge was systematically collected in training manuals illustrated with Polaroid photographs and manuscripts describing tools and procedures.

The 1970s were also the heyday of Québec engineering, and the City of Montréal in the 1960s played a key role in the rise of the new class of French-speaking engineers (Gagnon et Ross, 1991) in Québec. This era remains the reference period for many, especially for engineers now retired who began their careers at the time.

The Aqueduct Department was integrated to the new Public Works Department between 1979 and 1981, along with the establishment of a new principle of versatile employees. This is one of the events that most influenced the development of water service management in Montréal in the following decades. Despite the goal of improving efficiency, of enriching job descriptions and of training competent managers (Ville de Montréal, 1981), it has led to what some now describe as the "disappearance of water-related skills (*métier*)" in Montréal (Audette-Chapdelaine, 2008).

Following this reform, the 1980s and 1990s were marked by staff attrition and internal expertise loss. Blue-collar workers, attracted by better conditions and an easier work on roads, have gradually migrated to other types of tasks. Also, since blue-collar workers were protected by an employment floor, the city has slowly streamlined its professionals, engineers and managers, who were not replaced upon retirement.

Despite the reaffirmation of a public form of water services management in Montréal following the privatization debate of the 1990s, the governance issue was not addressed and the City has remained highly dependent on external resources at all levels: research, design, implementation, and supervision.

Thus, when it set in motion the "Great water works" of the 2000s, the City of Montréal and its Public Works Department were not able to provide adequate contract management and project supervision, for lack of internal resources. (Bherer et Breux, 2011: 4) Since 2009 and the cancellation of the water meter contract, the Water Department has hired many people to rebuild its workforce, gain knowledge on the state of the network, improve its capacity to execute in-house and improve its ability to manage contracts. However, this new generation of employees still has to gain grounded experience: in the late 2000s, three staff levels combined just five years of experience while in the 1970s, a new employee's supervisor may have had 15 to 29 years of experience. Only time will recover some knowledge gaps.

5.2 Managerial autonomy, political control and intermunicipal coordination

The water sector requires a particular balance between managerial autonomy and political control. Management autonomy can allow decision-making processes and operations based on the technical criteria required by the industrial and material context of such services, including long-term investment planning. Political control, on the other hand, is necessary for social, environmental and health reasons. (Audette-Chapdelaine, Tremblay and Dupré, 2009)

As presented in section 3, local governance in the Montréal area is very complex, with a division of powers among many local decision-making bodies. An OECD report already stressed, before the disamalgamation, Montréal's « over-complicated institutional mosaic of the metropolitan area ». (OECD, 2004) For water management, the situation is further complicated by administrative boundaries that do not match network management reality and difficult coordination between administrative levels to set priorities and interventions. Autonomy is a recurring theme at several levels: local municipalities seek autonomy from the provincial government; boroughs seek autonomy from the City of Montréal; related cities seek autonomy from the agglomeration; and finally, managers seek autonomy from the political process.[10]

The creation of an autonomous water management entity, an option that was repeatedly discussed, does not solve in itself the Montréal water problem. One could argue that this would simply add an additional stakeholder, especially if this entity does not have jurisdiction over the entire agglomeration territory. Many issues must be addressed, including the limited capacity of subcontractors to respond to these great investment needs, the coordination with other types of public works and the availability and source of financial resources.

However, if political councils fail to set service levels and to give the MWD appropriate long-term means to meet them, and if a more efficient coordination between the MWD, boroughs and related cities is not achieved, the LPE option will remain a strong credible alternative for managers to hope for, along with more stringent provincial regulation. In light of the events of the past three decades and the state of the infrastructure today, the managers' desire for depoliticization of water management is understandable. For water services managers, the main advantage of such options would be the possibility to plan financing and investment strategies independently from local yearly budget priorities. In Ontario, the provincial legislation requires local municipalities to manage their critical infrastructure according to a long-term plan. Montréal managers have in the past given input to influence provincial regulations, forcing municipal councils to give them the means to comply.

On another note, Québec's municipal democracy faces the dominant vision of an apolitical municipal sphere. According to this view, municipal issues are more about effective management of technical services, for which values are not taken into consideration during decision-making. (Bherer et Breux, 2011: 4) "Municipal democracy in this context boils down to a question of local public services management, and is not the expression of a political agenda." (Collin, 2011: 343) Municipal reforms towards greater local action autonomy are essentially "administrative and managerial, are centered on the issue of local services provision efficiency, and have little interest in terms of new public policy formulation." (Collin, 2011: 344-345) According to the Union of Québec Municipalities, "... there is a continuing tension between the traditional perception of the municipality as an administration dispensing services and the more contemporary one of a largely autonomous government level. "(UMQ, 2013: 13) The fact that public services management is so central to the definition of Québec local municipalities might explain the difficulty for municipalities to dispose of such activities in favor of autonomous entities or other municipalities. It does not, however, explain why Montréal administrations have failed to address the water problem.

[10] We could extend this logic to the federal-provincial-municipal relations in the case of Québec. See: Collin, J.-P., H. Bérubé, A.-C. Labrecque et M. Audette-Chapdelaine. 2010. *Under Close Watch. Provincial mediation in Federal-Municipal Relations: The case of Québec.* Inédits / Working papers, no 2010-6. Montréal: Institut national de la recherche scientifique, Centre Urbanisation, Culture et Société, 35 p.

The current situation leads us to believe that the transition is not yet complete in Montréal in terms of water services organization. We assume that the coming years will see a simplification of intermunicipal relations and a centralization of the management of services of common interest in the metropolitan area. The MWD created in 2010, combined with resources provided by the Water Fund, is already a step towards a new balance between political control and managerial autonomy. As we have seen in section 3, the centralization of drinking water production plants management at agglomeration level proved more efficient. Some expertise and tasks now executed at borough level, such as leaks detection, could also be centralized at least at MWD level for more efficiency.

Finally, in order for managers to feel that they have enough leeway to do their job as well as to ensure that citizens are well served by these same public officials, the city will need to build on the expertise and experience of its staff and develop with them a trustful relationship. In the current organization framework, a competent and efficient organization is also something that citizens must require through the exercise of a healthy local democracy and that must be reflected in council priorities.

Annex I - The Québec local administration

<table>
<tr><th colspan="2">REGIONAL: Administrative Regions</th></tr>
<tr><td colspan="2">Québec is divided into 17 administrative regions of the state. There are four types of administrative regions: metropolitan areas, regions surrounding Montréal, intermediate regions, and resources or peripheral regions. These regions are "the framework for territorial organization of public services" (Observatoire de l’administration publique, 2012: 11) and "administrative extensions of the state in its various “subnational” territories." (Proulx, 2008: 12)

Since 2005, regional conferences of elected officials (CRE) have a role in coordination and planning, and serve as an interlocutor with the government in matters of regional development. CREs "are part of the emergence of a new regional level of political representation, in that members of these structures of representation and consultation of regional interests are now mostly local elected officials." (Observatoire de l’administration publique, 2012: 12) However, CREs have no taxation power and are funded by the government. The members of their Board of Directors are the CRE’s RCM prefects, municipal mayors and municipal councillors. Other members may also be appointed by the government. (MAMROT, 2013c: 17)</td></tr>
<tr><th colspan="2">SUPRALOCAL</th></tr>
<tr><th>Regional county Municipalities (RCM)</th><th>Metropolitain Communities</th></tr>
<tr><td>The RCMs are directed by a prefect elected by the municipal mayors of the RCM’s territory. These mayors and other municipal officials form the RCM council. RCMs have responsibilities in planning, economic development, waste management, establishment of local development centres (LDCs), etc. In Québec’s unorganized territories, RCMs are in charge of responsibilities normally attributed to local municipalities. Finally, 14 cities and towns, including the City of Montréal, are responsible for some RCM competencies. (MAMROT, 2013c: 13; Observatoire de l’administration publique, 2012; Proulx, 2008: 11)</td><td>The two metropolitan communities, created in 2001 and 2002 during Québec’s territorial reorganization, have responsibilities in planning, economic and cultural development, infrastructure and equipment, transportation, and waste management. The Québec Metropolitan Community (CMQ) has responsibilities in tourism development while the Montréal Metropolitan Community (MMC) is responsible for social housing and the environment.</td></tr>
<tr><th colspan="2">LOCAL</th></tr>
<tr><th>Local Municipalities</th><th>Agglomerations</th></tr>
<tr><td>In Québec, there are 1,111 local municipalities[11], of which 883 are governed by the Municipal Code and 228</td><td>Since the "disamalgamation" of some municipalities between 2004</td></tr>
</table>

[11] This does not include the Province’s unorganized territories (TNO) and First Nations’ territories, which are not considered local municipalities.

by the *Cities and Towns Act*. Ten cities[12] represent 47% of Québec's population and form a triangle near the St. Lawrence River. (MAMROT, 2013c: 4-10) Local municipalities are responsible for fire safety, drinking water, water purification, waste and transport. They also share some responsibility with the provincial government on housing, roads, police, leisure and culture, parks and green spaces, as well as land use and planning and economic development. (MAMROT, 2013c: 11) Municipal responsibilities were imposed over time by government interventions. (Proulx, 2008: 7) Control over municipalities is exercised mainly by the Ministry of Municipal Affairs (MMA).[13] (Collin *et al.*, 2010: 11) However, more than 100 national agencies can "intervene in typically local or supra-local fields. These interventions are carried out by the application of about 150 to 200 laws providing a framework for municipal operations. In short, the local appropriation of public responsibilities in Québec happens through a very strong State leadership, the government remaining not only the initiator (indications, incentives, coercion) but also strongly present throughout the territory." (Proulx, 2008: 7-8) The 1980 tax reform, whose main objective was "to strengthen local autonomy and the appreciation of the local authority" (UMQ, 2013: 13), provided municipalities with almost exclusive use of property taxes, while eliminating government transfers from the sales tax. In Québec, the municipal financial burden is mainly supported by land and real estate owners. This has created pressure for increasing land and real estate value to create additional municipal revenues. (Collin *et al.*, 2010: 2; UMQ, 2013: 13)	and 2006, 11 agglomerations comprising 41 municipalities were put in place "to exercise powers of common interest." (MAMROT, 2013c: 12) Agglomeration responsibilities vary across cases but may include, for example, police, security, municipal assessment, public transport, arterial network, water supply and wastewater treatment, and waste management.
INFRALOCAL: Boroughs	
Since the 2001 municipal amalgamation, eight local municipalities in Québec now have boroughs at an infralocal level. Boroughs are a representative, consultative and decision-making body with an elected borough council. Boroughs locally manage some proximity services. (MAMROT, 2013c: 11; Observatoire de l'administration publique, 2012)	

[12] Montréal, Québec, Laval, Gatineau, Longueuil, Sherbrooke, Saguenay, Lévis, Trois-Rivières and Terrebonne.

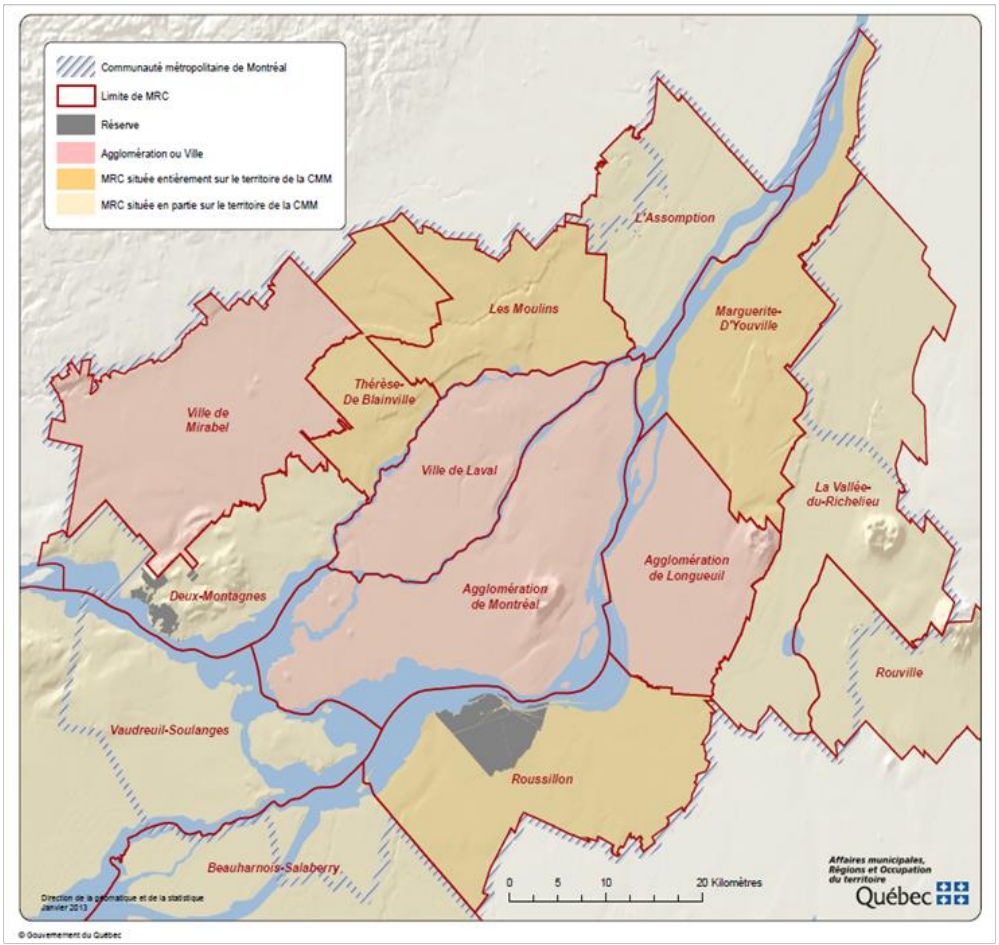
[13] Since 2008, it is the Ministry of Municipal Affairs, Regions and Land Occupancy ("MAMROT"). Previously, it was the Ministry of Municipal Affairs and Regions ("MAMR") and the Ministry of Municipal Affairs, Sports and Recreation ("MAMSL").

Annex II - The Montréal local administration

Supralocal administration: the Montréal Metropolitain Community (MMC)

The MMC extends on four administrative regions (the territory of the Montréal agglomeration corresponds to that of the Montréal administrative region). The MMC has four RCMs located wholly within its territory, six RCMs partially on its territory, two agglomerations (Montréal and Longueuil) and two cities (Laval and Mirabel), for a total of 82 local municipalities and a population of 3.78 million. Its board is composed of 28 representatives of member municipalities, presided by the mayor of Montréal. (MAMROT, 2013a, 2013c: 15; Observatoire de l'administration publique, 2012; Organisation de Coopération et de Développement Économiques, 2004; Rivard et al., 2005)

The Montréal Metropolitain Community
and its constituent agglomerations, cities and RCMs
(MAMROT, 2013a)



Montréal Agglomeration

The Montréal agglomeration brings together the 16 local municipalities of Montréal Island, that is to say, the City of Montréal and 15 "related cities" which have been de-almagamated and reconstituted in 2006. The Agglomeration Council is the democratic body responsible for common services provided to all citizens of the Agglomeration. It is composed of 31 elected officials: 16 of them are from City of Montréal, including the city mayor who chairs the

agglomeration council and appoints the other 15 representatives. The related municipalities are represented on the agglomeration council by 14 mayors, one of whom is appointed vice president. One of the related municipalities, particularly populous, appoints an additional representative. The City of Montréal accounts for approximately 87% of the Agglomeration population; related cities are proportionally over-represented on the Agglomeration Council.

City of Montréal boroughs

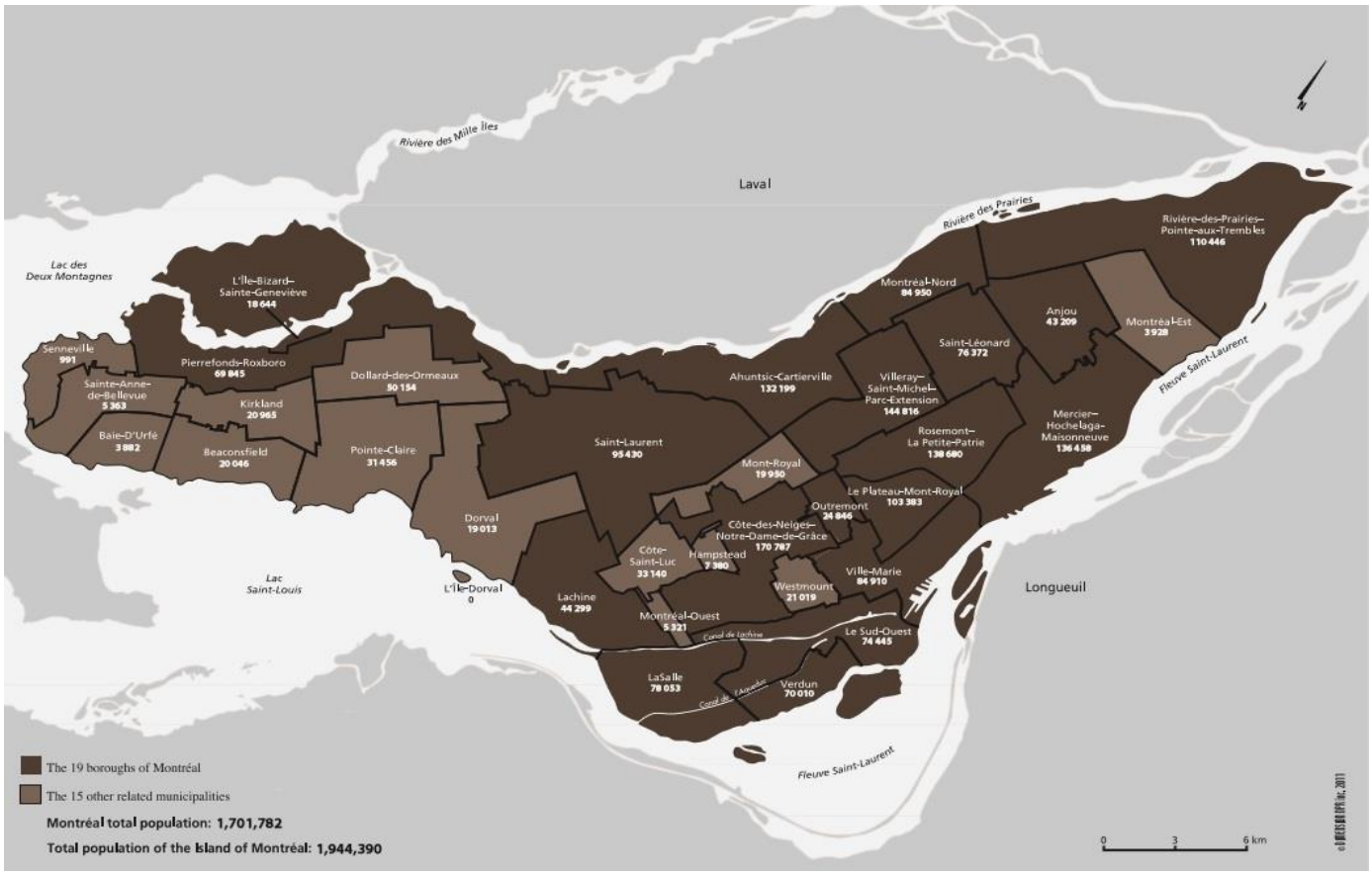
At the infralocal level, City of Montréal is divided into 19 boroughs. Decentralization of powers to the boroughs was meant to counter opposition to the 2001 municipal amalgamation. (Rivard *et al.*, 2005: 7) In accordance with the City of Montréal Charter, local responsibilities are shared between the city council and the borough councils:

> "City of Montréal's City Council is responsible for local competencies over Montréal's territory, including the 19 boroughs. Borough councils are responsible for providing local services on their respective territories. The municipal council consists of the Montréal mayor who is ex officio mayor of Ville-Marie borough, and 64 municipal councillors, 18 of which are borough mayors. A borough council has a minimum of five members, including the borough mayor, city councillors and, in some cases, borough-level councillors. In total, the 19 boroughs count 46 councillors sitting on the city council and an additional 38 borough-level councillors." (Ville de Montréal, 2012: appendix 2, p.2.3-2.4)

The following diagram shows the entire Montréal agglomeration, including the 15 related cities and the City of Montréal's 19 boroughs.

The Montréal agglomeration: City of Montréal boroughs and related municipalities

(Source: Montréal's 2012 financial report, p. VII)

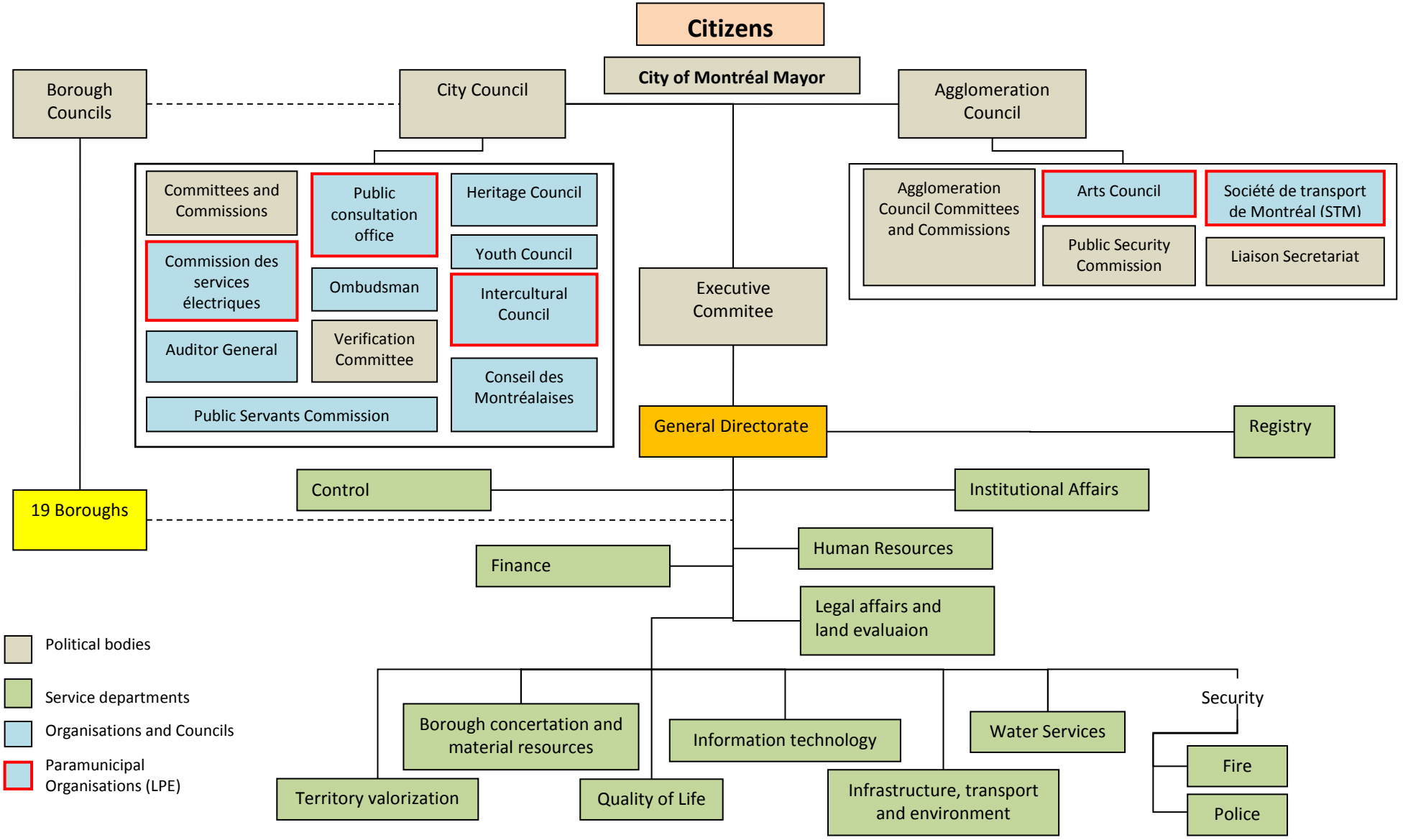


City of Montréal Organisation

The chart below shows the different political bodies of Montréal as well as related organisations and councils. The service departments are shown under the director general. The water service is one department among other municipal departments. We have outlined in red the organisations considered Montréal LPEs, although not all Montréal LPEs are included in the organisational chart (see section 1.2).

Simplified organizational chart

Source: Author, with data from City of Montréal 2013 Operating Budget



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Local public enterprises

German case study

Water provision in Stuttgart

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1. Executive Summary

Local public enterprises (LPEs) are a longstanding and integral feature of economic activity by local governments in Germany.

As a result of the federal system in Germany and the principle of municipal self-determination, the use of LPEs to pursue economic activities is codified in the country's constitution. The associated far reaching rights have led to LPEs being used in basically any part of German public service and goods provision, with water, sewage, housing, public transport, power, gas and waste disposal representing the most frequent activities. Over the last decade, the number and turnover of LPEs has increased rather than decreased, questioning the sometimes proclaimed demise of public enterprises.

The German water sector is characterized by provision at the local level whereas ex-ante rule setting (legislation) as well as ex-post control (supervision) are typically carried out on regional and national levels.

On the legislative side, regional governments regulate the organizational rules of provision while national and international institutions focus on basic water rights issues and environmental questions. The implementation of the service is on the local level where the local government chooses the governance structure to carry out the service, potentially a LPE. Ex-post price controls are carried out by courts and cartel authorities whereas water quality is assessed by independent public health agencies.

LPEs are virtually the only relevant institutional arrangement in German water provision.

Despite a trend towards more enterprises based on private law and an increase in private sector participation, LPEs remain the most important type of water provision. Distinguishing different types reveals that 26% are mixed public private firms (with a private minority shareholder), 20% are intermunicipal cooperations between municipalities, 38% are corporatized firms and 16% are directly managed LPEs which are legally a part of the local government.

The difficult climatic conditions with little precipitation have shaped water supply in Stuttgart.

As the state of Baden-Württemberg and therefore also the region around Stuttgart is comparatively dry with only 665,5 mm precipitation per year, the city is served by a long-distance water supply. The two sources are more than 100km distant and supply is carried out by two intermunicipal cooperations. As Stuttgart is the largest customer and shareholder in the cooperations, it has a great influence on strategic decisions of the organizations.

Within roughly 10 years Stuttgart's water provision went from public to private and back again.

After more than 60 years of water provision through a corporatized LPE (TWS AG), Stuttgart successively gave up control over its water provision. Just a few years after an intermediate step towards privatization by merging the local provider with another regional provider (NWS), the

city sold ownership share to the company EnBW. The concession contract with EnBW will, however, not be renewed in 2013 because public discontent forced the local government to re-municipalize water provision. As a directly managed LPE, which is legally not independent, the water provision will be even more integrated into the city administration than ever before. The privatization reversal proved, however, difficult as the city still required technical expertise and competence from EnBW and because the parties disagreed about the buyback price for the infrastructure.

The privatization of Stuttgart's water provision is closely related to the multi-utility nature of the TWS AG (water, energy, gas) and the liberalization of the energy sector.

An analysis of the drivers that led to the decision of the city of Stuttgart to privatize its water provision reveals that the relevant factors have little to do with the supply of water itself. Instead of a service specific explanation, the determinants of the switch are rather located at the meso and macro level, and are related to the multi-utility nature of the city provider. Specifically, in Stuttgart the TWS AG was historically always responsible to provide both water and energy/gas.

Given the liberalization induced by the European Union and the uncertain future of the energy sector, the city government decided to privatize its energy provider because it was expected that the value of the local energy provider would decrease. Hence, as a side product of the merger and privatization wave in the energy sector, Stuttgart's water provision was privatized because it was part of the multi-utility LPE.

Fiscal and tax incentives too, played an important role in the decision to privatize.

A proposal to spin-off the water provision from the TWS AG into an independent organization was dismissed by the city government as too complicated and unfavorable from tax perspectives. Tax incentives, to avoid a retention period of seven years before shareholdings could be sold tax free, were also detrimental for the city to change its original plan of keeping a 25% stake in the provider to selling the whole holding company.

Although after the privatization the city of Stuttgart was no longer directly involved in water provision, a number of relations and contractual agreements between the city and ENBW remained.

The city would receive 50 million Euros as a concession fee annually, thereof roughly 13 million for water provision. Moreover, despite selling its shares in the long-distance networks, the city agreed with EnBW that they would retain their seats in the distance-water supply associations.

Regarding price setting, the previously applied system of cost accounting to calculate prices would remain the basis for tariff decisions. The city would also have the right to review all relevant documents and accounting material if a price increase was envisaged.

Finally, city representatives became members of the advisory boards to the firm. In this consulting capacity the city was supposed to influence the organizational strategy and improve communication between the city and the firm.

Similar to the privatization, water service characteristics played only a minor role in the decision to re-municipalize.

Considering the development of some key service characteristics it appears unlikely that the drivers of the switch are connected to public discontent with the provided service characteristics: water losses and service disruptions decreased during the concession period and water prices increased slower than in the decade before.

A shift in public attitude against privatization and direct democratic participation are the key aspects to understand the re-municipalization.

Potentially the most important driver was a shift in public attitude against privatization which materialized in the public movement the 'Stuttgarter Wasserforum'. After some initially successful campaigns, e.g. against the use of cross-border-leasing, in 2009 the organization launched a petition for referendum with the goal to re-municipalize water provision.

Local elections in mid-2009 increased the momentum further as the topic became a major issue for the opposition parties to criticize the government. As a result, even before the end of the petition for referendum and just before the election, the governing party announced that it would support the re-municipalization. Moreover, the city government accepted the successful petition without putting it up to popular vote.

Despite initial plans to keep EnBW involved in the service provision, pressure by the public movement and opposition parties ensured a complete privatization reversal, buying back not only the infrastructure but also integrating the service into the municipal administration.

The envisaged re-municipalization proved to be more complicated than expected.

Two factors led to complications and slowed down the re-municipalization process. Firstly, the city was unable to take over the water provision immediately due to the lack of skilled personnel and expertise. Although EnBW was initially ready to assist during the transition period, it put the city government at a disadvantage in the negotiations.

Secondly, after it was clear that the concession contract would not be renewed, the city and EnBW were unable to reach an agreement about the buyback of the infrastructure. The different valuation methods led to a difference of several hundred millions of Euros. As a result, the city has taken legal action against EnBW to force a buyback.

Table of contents

Executive Summary 49

1. LPEs in Germany 53

2. Water provision in Germany and the Stuttgart Case Study 56
The German water sector 56
Water provision in Stuttgart 61

3. Governance of the water provision in Stuttgart 63
TWS AG 63
NWS AG 63
EnBW Regional AG 65
KWS 66

4. Switching context for Stuttgart's water provision 68
From TWS AG to NWS AG and to EnBW Regional AG: The dissolution of municipal control over water provision 68
Creation of KWS Stuttgart: Re-municipalization of water provision and its infrastructure 70
Preliminary appraisal on the pros and cons of the adopted governance structures 75

5. Challenges for a LPE governed water provision in Stuttgart 76

References 79

Appendix 82

2. LPEs in Germany

Local public enterprises (LPEs), constituting a particular type of municipal economic activity, have a long standing history in Germany that goes back to the 19th century. The main legal basis for economic activity by local governments is the constitution (Grundgesetz) which guarantees sub-national jurisdictions a self-governing status.[14] Such constitutional provisions are not surprising given the federal structure of Germany and highlight the distribution of competences among different levels of governments. It implies that municipalities have the right to engage in business activities, potentially through public enterprises, in order to administer local affairs and carry out their constitutional responsibilities.

While the limits of municipal economic activity vary somewhat depending on the respective state laws, an important constraint lies in the fact that activities should be limited to the local sphere (see Hornung (1998)). Although the local sphere definition still allows for intermunicipal cooperation beyond jurisdictional borders, it critically limits the municipal governments – therefore also LPEs – scope of action in terms of territory. In addition, economic activity by municipalities has to be justified by a public interest. As a result, purely profit oriented activities are prohibited.

Another feature of the federal structure of Germany and the concept of self-governance is the organizational freedom given to municipalities. German municipalities have few limitations regarding the choice of a legal structure for the LPE. While public law based LPEs that remained within the local administration ('Regiebetriebe' and 'Eigenbetriebe') dominated in the past, in recent decades more and more LPEs are organized using private law organizational types like joint-stock ('AG') and limited liability firms ('GmbH'). Regards LPEs based on private law (incorporated LPEs) there are no explicit requirements regarding capital structure of LPEs in Germany but usually the local government is the sole or at least majority owner of an LPE.[15]

Data from public accounts shows that municipalities operate more than 10,000 LPEs. Interestingly, both the number of firms as well as their turnover has significantly increased in the last decade (see Figure 1). Roughly two thirds of these LPEs are already organized under private law and almost 50% of municipal employees are employed by incorporated LPEs. Moreover, survey data from municipalities above 50,000 inhabitants also shows that larger cities have on average 90 LPEs, indicating a veritable difference between urban and rural regions.

[14] The relevant sections are in Art. 28 Abs. 2 S. 1 of the German Grundgesetz.

[15] Minority and non-controlling interest are not explicitly ruled out by law but are very rare in practice (see Grossi and Reichard (2008)). Also, firms where the public partner does not have a controlling influence are not considered as public enterprises, for instance for government accounts and statistical purposes.

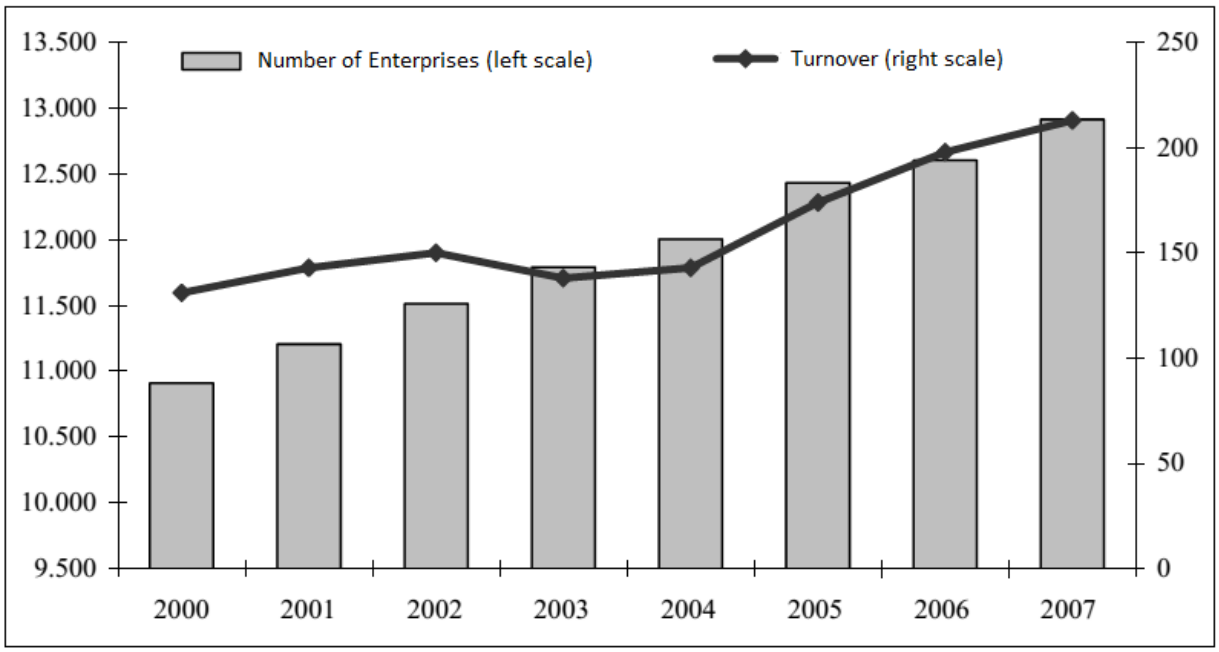

Figure 1: Evolution of LPEs in Germany (Bardt et al. (2010))

Both major trends, the increase in economic activity as well as the move towards legally independent organizational structures, can be explained by a changing attitude of municipalities regarding their role for providing public goods. Municipalities are engaging in new economic activities in order to ease the financial pressures from continuously increasing cost for health and social services. As shown in Bardt et al. (2010) this behavior is best illustrated in the energy sector, where the increasing profitability of decentralized production through renewable energy sources has led many municipalities to engage in the sector. A recent study by Deutsche Bank (2013) indicates that a large part of previous re-municipalizations but also planned re-municipalizations are related to the secular shift towards energy the associated new role for municipal provision.

This is part of a larger trend in which larger municipalities and cities increasingly see themselves as enterprises with a group structure (see Linhos (2006)). A typical reason why legally independent governance structures are chosen is for the sake of flexibility. For instance, corporatized LPEs and similar arrangements are less subject to typical public sector restrictions such as strict employment laws. Like holding companies many municipalities nowadays produce consolidated financial statements (see Table A1 in the appendix) and hire finance and accounting trained staff to optimize their holdings from tax perspectives. Overall, as argued by some researchers tax advantages for municipalities – regarding sales tax but also profit taxes – are an important factor why public enterprises are increasing their share in sectors where public and private firms compete with each other (see Bardt et al. (2010)).

As indicated by Grossi and Reichard (2008), LPEs in Germany are active in a wide range of sectors with water, sewage, housing, public transport, power, gas and waste disposal representing the most frequent activities. In addition, LPEs are occasionally used for health care, city marketing, economic promotion but also social, cultural, and recreational services such as theatres and museums. Figure 2 exhibits the sectorial distribution of LPEs.

It should be noted that the steering of these typically single function LPEs is in many cases effected through municipal holding companies.[16] The holding companies are therefore usually multi-sectoral/multi-utility LPEs, which leads to a multi-layered structure in which the local government groups its economic activities. Depending on the degree of integration, it is not uncommon that for the citizen the collection of public services like water and energy is available through the holding company, without the need to deal with the individual LPEs.

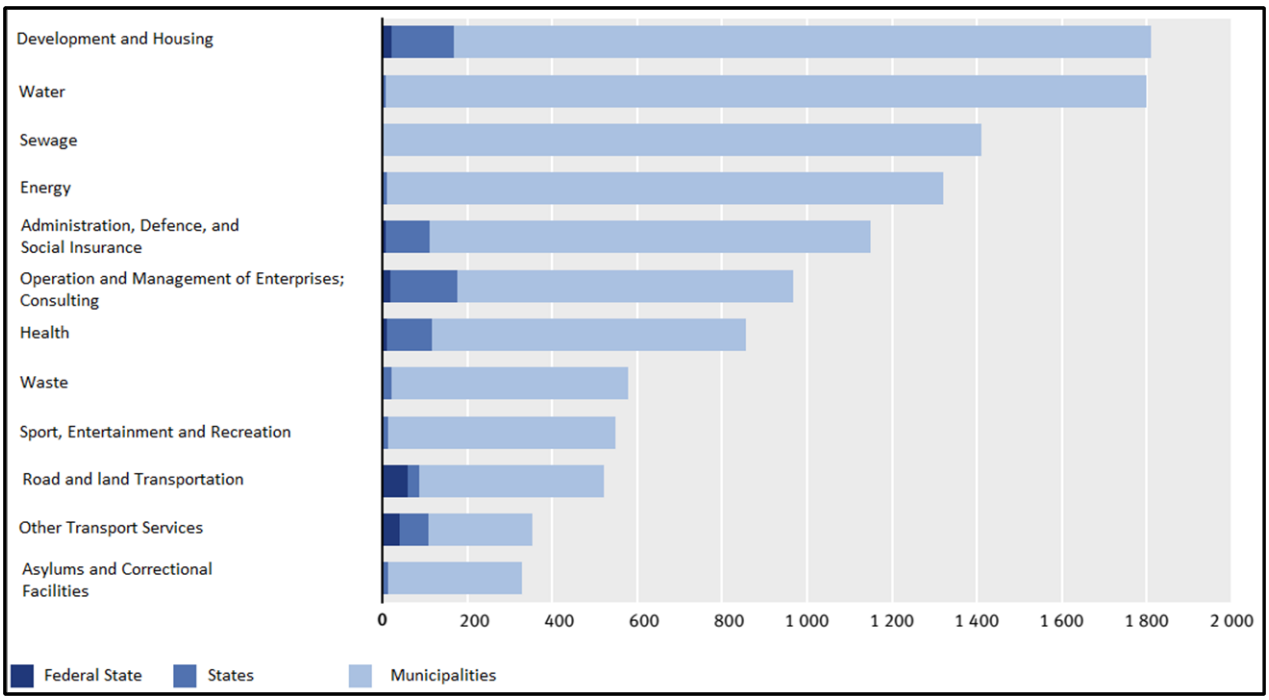

Figure 2: Sectorial distribution of LPEs (based on Schmidt (2011))

[16] Grossi and Reichard (2008) refer to these types of holding structures as municipal corporate groups.

3. Water provision in Germany and the Stuttgart Case Study

The German water sector

As this study focuses on a particular case in the water sector, this section presents an outline of the institutional environment for water provision in Germany. The relevant actors in the water sector and their relationships are displayed in Figure 3. For analytical purposes, 5 different groups of may be distinguished.

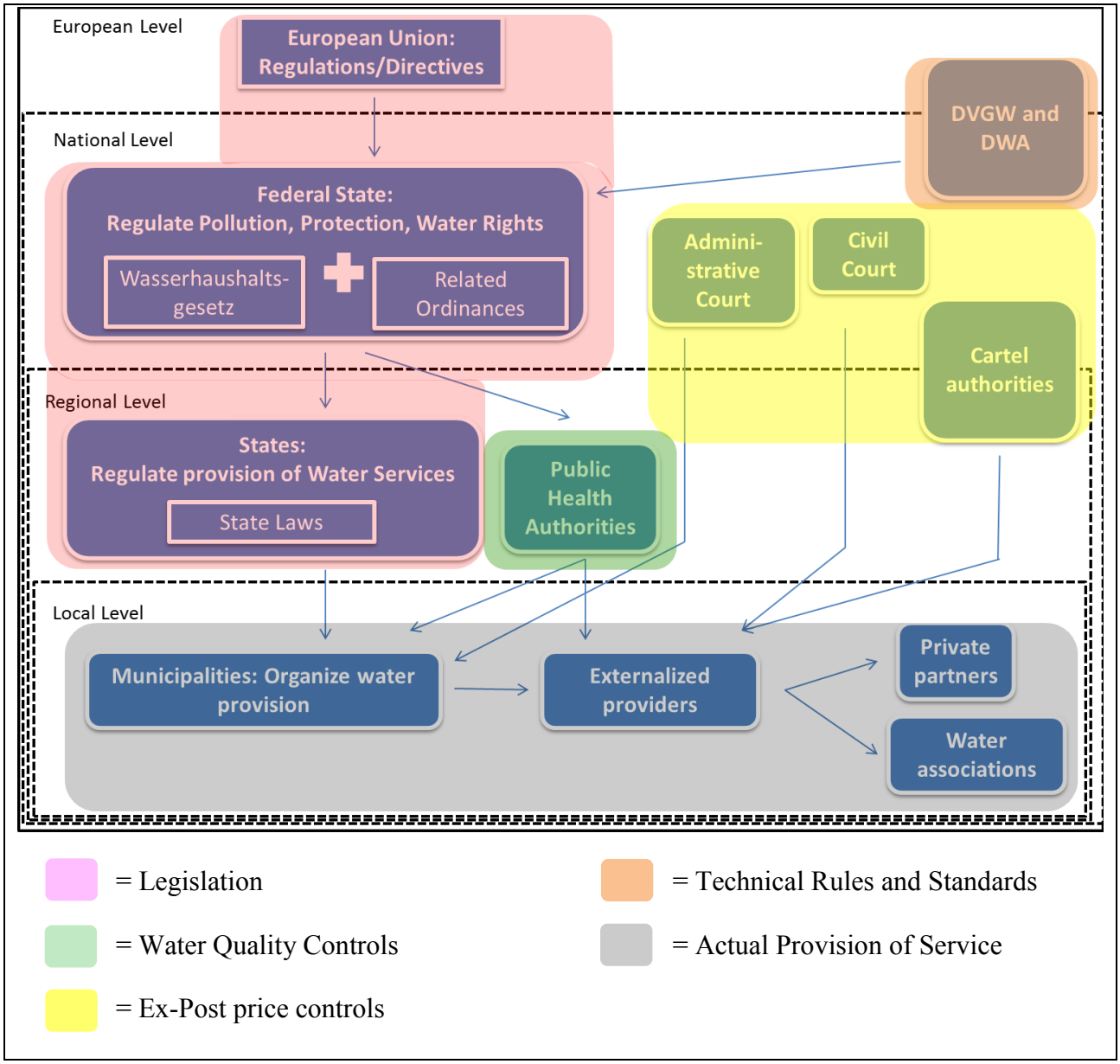

Figure 3: Institutional Framework of Water Provision in Germany

Before going into the details of the five distinguished groups, a quick outline of the subnational responsibilities for water provision is called for. In general, water provision is a municipal task and implemented on the local level. Even in the case of intermunicipal cooperation like water associations, the individual municipalities choose to enter and are typically represented according to their size. In contrast, the roles for federal and regional governments as well as other stakeholders are limited to setting the legislative framework and standards of operation.

Moreover, unlike other sectors like public transport, where the regional government and voluntary regional level associations play an important role in coordinating municipal and regional activities, the water sector is seldom on the agenda of regional planning activities.[17]

First, regarding the legislative side, actors from various levels are involved. On the European level, the European Union has a regulatory role through its directives. Particularly the Water Framework Directive (Directive 2000/60/EC) had an important regulatory impact and led to a significant change in the German 'Wasserhaushaltsgesetz' (WHG), the main legal basis for water issues on the national level. Main focus of the amendment was the introduction of regulations prohibiting any deterioration in the existing water quality status and improvements in the area of water management planning (see Block et al. (2001)). Apart from the WHG, on the national level there exist a number of related ordinances that regulate for instance emissions, sewage imissions, and pollution thresholds. Finally, on the regional level state laws regulate the operational details of water provision but have to be consistent with the legal framework designed by the federal state.

The second group of actors is responsible for developing and improving technical rules and standards in water provision. Instead of the legislator specifying technical standards, organizations consisting of honorary experts are responsible for the so-called technical self-administration of the sector (see ATT et al. (2011)). The 'Deutscher Verein des Gas- und Wasserfaches e.V' (DVGW) and the 'Deutsche Vereinigung für Wasserwirtschaft, Abwasser und Abfall e.V.' (DWA) gather technical and scientific expertise to elaborate technical rules and standards. On a European level the two organizations cooperate with other relevant standardization organizations. These organizations are therefore also relevant when legally defining environmental requirements conditional on technological standards.

Third, public health agencies on the regional level are responsible for monitoring drinking water quality. These independent public agencies evaluate water quality through chemical analysis in regular intervals. Cities with more inhabitants have more frequent and more diligent controls.

Fourth, the actual implementation and organization of water provision is effected by actors on the local level. Depending on the organizational design chosen by the municipality, the provision may be effected by an LPE that is legally part of the government or an externalized provider. In the latter case, when the LPE providing water services is legally independent from the municipality, three archetype organizational structures arise:[18]

- Corporatized LPEs where the firm is legally independent while the local government is the sole owner.
- (Water) Associations as a form of intermunicipal cooperation.
- Mixed Public-Private LPEs where a private partner holds a minority share in a corporatized LPE.

A further outline of the organizational types in the German water sector is given in Box 1.

The fifth and last group that plays a role in German water provision relates to the judicative side. The Administrative Court and the Civil Court as well as the federal and regional Cartel authorities are responsible for ex-post price controls. An important distinction arises here as to

[17] This is also the case for the Stuttgart, where the long-distance water supply for the region is organized and steered by the member municipalities.
[18] For a more detailed exposition of the these institutional arrangements and a taxonomy of LPE types see Klien and Saussier (2013).

what legal basis is chosen for the water providing LPE. In the case of public law based organizations the Administrative Court is legally responsible, whereas LPEs based on private law are monitored both by cartel authorities and the Civil Court is responsible for legal actions. While for the two courts to react it is necessary that citizens take legal action against a water provider, the cartel authorities are free to carry out inquiries and impose potential sanctions themselves.

The question of price supervision has received increasing attention in recent years, after a regional cartel authority forced a corporatized water provider to revoke an already implemented price increase. In the particular case, to circumvent price controls by cartel authorities, the municipality has chosen to re-municipalize its water provision.

Box 1: The distribution of organizational types of German water providers

According to statistics from the national federation of German water providers there are 6211 water suppliers and utilities in Germany (ATT et al. (2011)). However, roughly 5000 of these are very small scale municipal providers that despite their large number represent only 25% of water output.[19] It therefore suggests that the production structure is very small scale in Germany. As shown in Figure 4, over the last two decades there has been a shift from public to private law based LPEs, both with respect to number of suppliers as well as output.

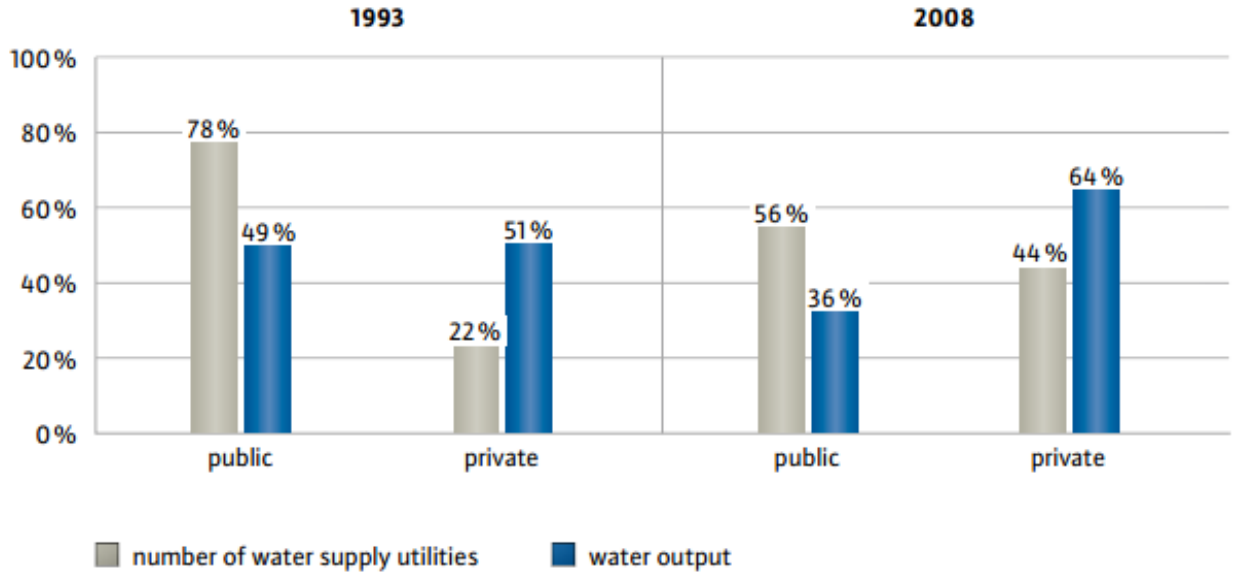

Figure 4: Development of LPE types in the German water sector (from ATT et al. (2011) based on 1,218 providers)

The classification as 'private' indicates only that the LPE has is based on private law and is uninformative about whether the municipality remains the sole owner of the water provider or if a private firm holds a minority share in a corporatized LPE.

When looking at the specific types of LPEs that exist in the German water provision, a wide variety of organizational types can be observed. Conceptually, the nine different types identified by the national federation of German water providers can be grouped according to the taxonomy in Klien and Saussier (2013), leaving four main governance structures. Figure 5 exhibits the shares of the respective types along with a classification.

[19] As a consequence, the following tables represent only the 1,218 larger providers and utilities.

Directly managed LPEs account for around 16% of water output in Germany. While actual Régies account for only 1% today, the most frequent organizational types are organizationally and budgetary more independent agencies. These agencies are, however, not legally independent and remain part of the government administration. Similarly, their staff consists of municipal employees and the water infrastructure is part of the municipal assets.

The largest group of governance structures in Germany are corporatized LPEs with 38% of output. Representing an institutionally separated and legally independent governance arrangement, the various types of corporatized LPEs vary by the specific legal structure as well as the degree to which their budget is still part of the municipal budget. Regardless of the specific design, municipalities have surrendered decision rights over business decisions in corporatized firms. Although the local government as sole owner can rather easily install or change executive managers, firm decisions are taken by the company management and not by the city council or the mayor.

Of great importance particularly in rural areas is intermunicipal cooperation to provide water services. Being either a water association or a special purpose association, which can pursue multi-sectorial activities, intermunicipal cooperation accounts for roughly 20% of water output. Apart from being legally separated from the individual municipality and representing an independent organization, this type of governance structure is characterized by a fragmentation of control rights. As a result of the shared ownership, each municipality has typically one vote in the association. Even in the situation where a large city is cooperating with a large number of small neighboring municipalities, this boils down to one organization having multiple principals.

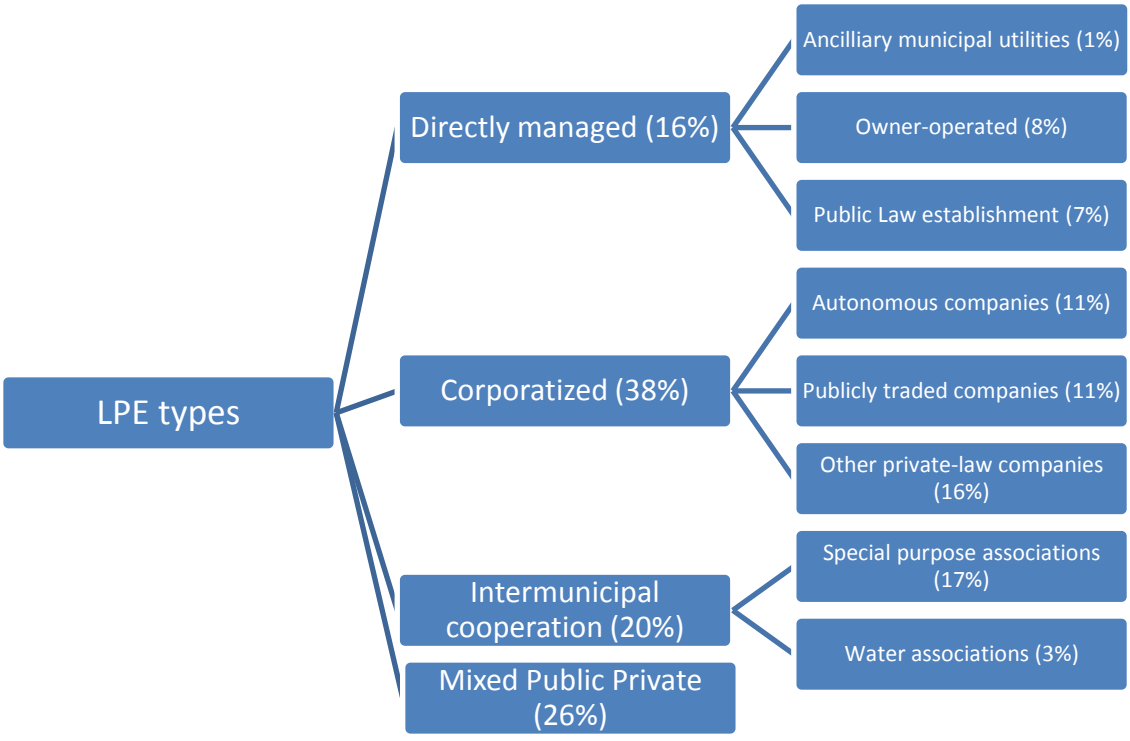

Figure 5: Organizational types in the German water sector (shares based on water output and based on 1,218 providers)

Finally, LPEs with a private partner amount to 26% of water output. The legal structure is usually very similar to corporatized firms, with the difference that ownership is shared with a private

firm. Under such arrangements, the private partner is often responsible for the operation of water provision whereas strategic decision and also pricing falls under the competence of the municipal representatives on the executive board.

Water provision in Stuttgart

Status	Capital city of the state Baden-Württemberg
Population	591,000 in the city (2.7 and 5.3 million in the region and the metropolitan area resp.)
Area	207 km^2
Climate	Dry with little precipitation (665,5 mm per year on average)
Political leadership and mayor	1974 to 1996: Manfred Rommel (CDU) 1997 to 2013: Wolfgang Schuster (CDU) Since 2013: Fritz Kuhn (Bündnis 90/Die Grünen)

Table 1: Factsheet Stuttgart

As a consequence of its topographic structure and a very unequal distribution of water resources, municipalities in the state of Baden-Württemberg started, with the help of the regional government, already at the end of the 19th century with long-distance water supply. This is also true for its capital city Stuttgart, whose water sources are more than 100km distant. The potential maximum demand of 400,000 cubic meters per day is supplied in equal parts by the 'Landeswasserversorgung' (LV) and the 'Bodenseewasserversorgung' (BWV). In the former case, the water is a mix of groundwater, spring water and river water whereas in the latter case all water is surface water extracted from the Lake of Constance (see Zweckverband Landeswasserversorgung (2009) and Zweckverband Bodensee-Wasserversorgung (2011)). Figure 6 show the water network of the metropolitan area of Stuttgart along with its connections to LV in the northeast and BWV in the southwest.

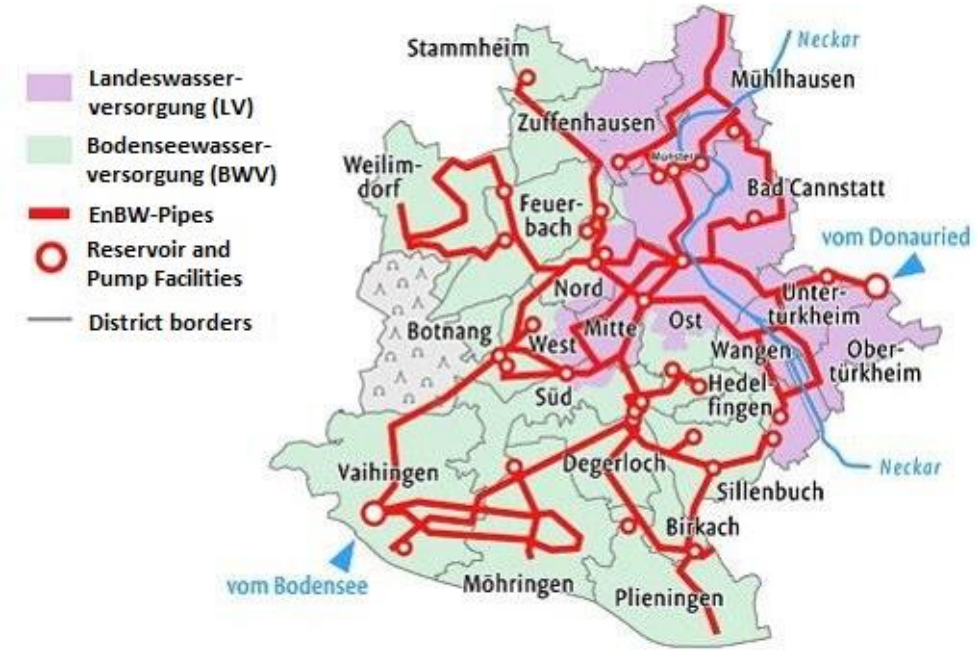

Figure 6: Water network of the Stuttgart metropolitan area

Both the LV and BWV are intermunicipal cooperations (special purpose associations) who manage water extraction at its source and long-distance water supply networks. Its members, typically municipalities but also private operators, share the cost of operation as well as financing and re-investment according to the amount of delivered water. Moreover, upon joining the

association an initial capital contribution relative to the expected water delivery is made, making the municipality a quasi-shareholder of the cooperation.

As Stuttgart was and is the largest consumer of drinking water from the associations, the water provider servicing Stuttgart, the city itself or the respective operator has a 33% stake in the associations. Traditionally, the role of Stuttgart was therefore particular which showed in its influence on the strategic decisions of the associations and also the number of representatives the city of Stuttgart had on the association boards.

Since the city of Stuttgart privatized its water provision in 2002, it is no longer a member of the associations and has transferred its capital share to 'Energie Baden-Württemberg Regional AG' (EnBW Regional AG). The privatization involved not only a concession contract until the end of 2013 but also the sale of the infrastructure and assets. It constitutes one of the very rare cases, where a German municipality not only delegated water provision but resorted to material privatization of its infrastructure.

At the time of writing this case study, water provision in Stuttgart was still operated by EnBW Regional AG but the re-municipalization was imminent, only stalled by unsuccessful negotiations about the buy-back conditions. The government's decision to initiate the re-municipalization process was strongly driven by a citizen's movement that used an instrument of direct democracy, the 'Bürgerbegehren' to mount pressure on politicians. As a consequence, roughly 10 years after the privatization, the city of Stuttgart would switch back to municipal service delivery in the form of a LPE.

At the latest from 01.01.2014 onwards, this date was specified as a deadline in the 'Bürgerbegehren', the municipality is expected to provide the service again itself. According to government documents this will be achieved by expanding the existing directly managed LPE, an owner operated Régie that is responsible for wastewater, to form a general provider for both water and sewage: The 'Kommunale Wasserwerke Stuttgart (KWS)'.

4. Governance of the water provision in Stuttgart

In order to understand the current situation and changes surrounding the water provision in Stuttgart, it is necessary to discuss the evolution process during the last two decades. For this reason Figure 7 depicts the organizational types that were present in the recent past along with the ownership of the city of Stuttgart in each of these institutional arrangements (see Horvath & Partner GmbH (2011) for details on the organizational changes).

TWS AG

As can be seen in the graph, for the most part of the past century, the water provision in Stuttgart was governed through the TWS AG ('Technische Werke der Stadt Stuttgart'), which dates back to 1933. The TWS AG was a typical multi-utility joint-stock company with the city owning 100% of the shares. It was not only responsible for water provision but also electricity and gas distribution. As outlined before, the city was/is supplied by two long-distance water networks and the TWS AG as the organizational vehicle for the city held the 33% shares in the two associations, LV and BWV, which supply the Stuttgart with drinking water. Moreover, as the largest city in the associations, Stuttgart was strongly involved in the strategic decision making. Apart from several city representatives on the board, Stuttgart's mayor was traditionally the chairman of both associations.

The TWS AG represented a classical corporatized LPE, where the organization is both legally as well as organizationally independent and the local government can influence the firm through its ownership rights. While professionals and engineers play an important role in firm management, representatives of the city have key positions on the firm's management board.

NWS AG

In 1997, the TWS AG merged with a regional electricity provider, the NW AG ('Neckarwerke AG Esslingen') and formed the NWS AG ('Neckarwerke Stuttgart AG'). Whether the NWS AG still constituted a corporatized LPE or an intermunicipal cooperation is ambiguous. On the one hand, the city of Stuttgart was the largest shareholder but still below 50%. On the other hand, the city still had a controlling influence on the firm and also the other shareholders were at least partially if not majority publicly owned.

As was typical for utility firms, the state government, large cities like Stuttgart but also associations of smaller municipalities were frequently engaged as minority shareholders in regional providers. At least in 1997, the two relevant shareholders in the NWS AG apart from the city of Stuttgart, the EnBW (Energie Baden-Württemberg) and NEV ('Neckarwerke Elektrizitätsverband') were both majority owned by different public entities. The former one, EnBW was forged through a consolidation of regional providers and was designated to become the regional champion in energy provision (see Box 2 for an outline of EnBW and its organizational evolution).

Consequently, the NWS AG may be interpreted as an intermunicipal or even intergovernmental LPE where several distinct government jurisdictions share ownership. As the focus of the NWS AG and the shareholders apart from the city of Stuttgart was on energy, the effects of the merger on water provision and its governance were very limited. The city of Stuttgart hence remained responsible for the operation of the services, which for water were limited to the Stuttgart area. For instance, a contractual arrangement between the city and the NWS AG ensured that Stuttgart kept its seats on the boards of the two long-distance water associations.

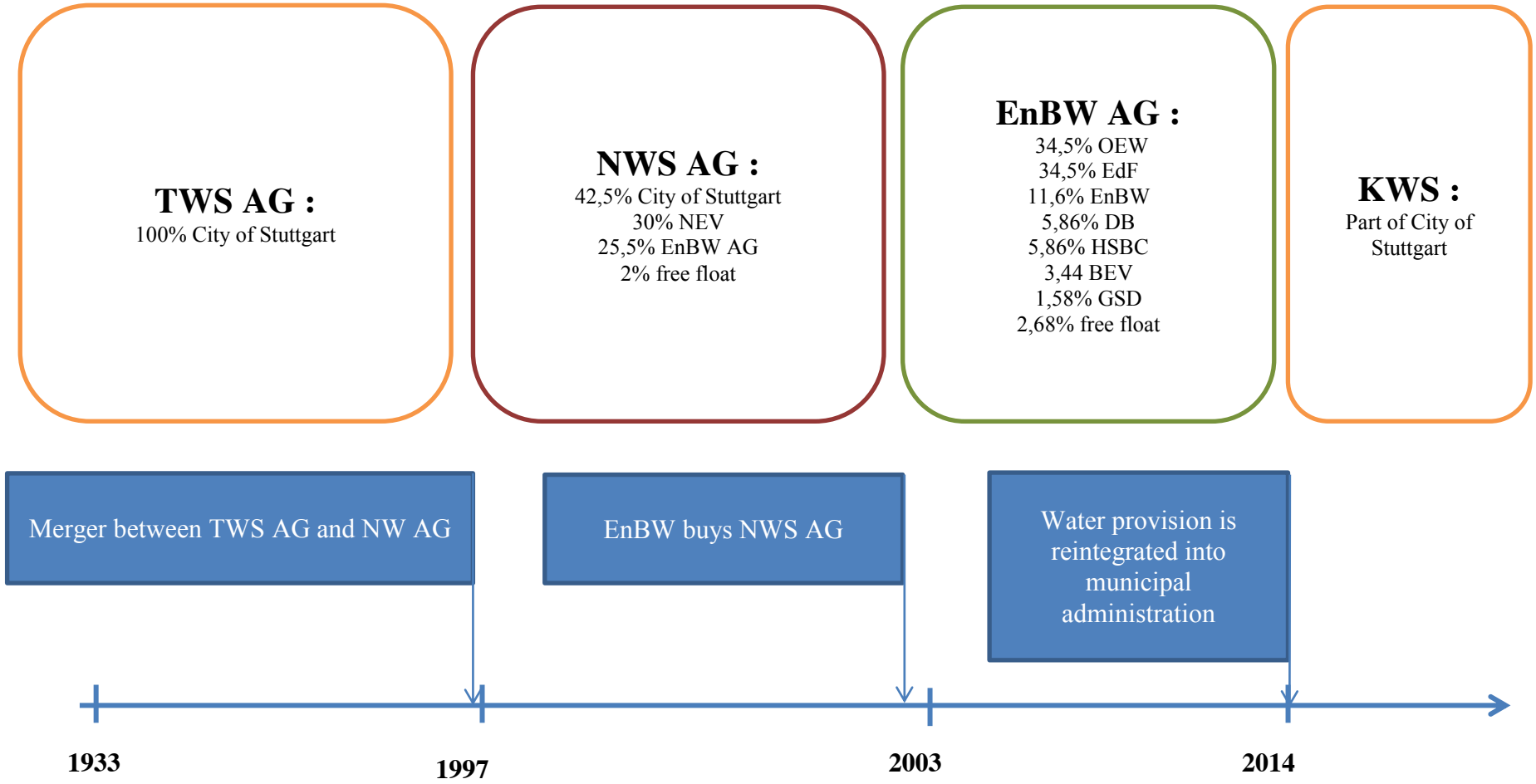

Figure 7: Evolution of the water provision in Stuttgart[20]

[20] The shareholder positions refer to 1997 for NWS AG and 2003 for EnBW AG.

Box 2: Focus on EnBW

Energie Baden-Württemberg was created in 1997 as a result of the merger between two publicly owned energy providers, Energieversorgungsunternehmen Badenwerk AG and Energie-Versorgung Schwaben AG (EVS). At that time its main shareholders were (see Horvath & Partner (2011) :

34.5%: OEW (=association)
9.0%: City of Stuttgart
11.8%: Landeselektrizitätsverband Württemberg (=association)
25.1%: State of Baden-Württemberg
19.6%: Other municipal associations

The creation of EnBW and the increased number of mergers and acquisitions at the end of the 90's was closely related to the structural changes in the legal framework of the energy sector in Germany and Europe at that time. To implement the European directives EG 96/92/EG the German electricity regulations were significantly changed in order to account for the required liberalization of the sector. As politicians and policy makers expected a more fierce competition due to the liberalization, a strategy of creating sufficiently large, sufficiently expanded operators, so-called national/regional champions was pursued.

To this end, the consolidation of smaller regional providers as well as the dissolution of the Stuttgart based water and energy provider NWS AG into EnBW was strongly supported by the state government. Despite selling the state share to EnBW and EdF, former governor Teufel was not only involved in arbitrating conflicts between unwilling merger partners but also heavily invested in choosing Electricité de France as a strategic foreign partner.

„Selling the state shares to EdF and the associated restructuring and reorientation of Baden-Württemberg's energy provider EnBW constitute the end of the central political undertaking of this legislative period […] Through the connection with a strong foreign partner the state government reacts to the Europeanization and globalization of energy markets." (translated from Strom-magazin (2000))

After this strategic reorientation, the shareholder structure of EnBW had already changed markedly (see Figure 7 for the situation in 2003) and EdF was not only contractually empowered to be the managing partner but acquired additional shares in the coming years. Somewhat surprisingly in December 2010, however, the state government announced that it would buy back the 45.01% stake of EdF.[21] As a result, at the time of writing this study EnBW is again under public control by the state of Baden-Württemberg and municipal associations (see E&E Consult Gbr (2011)).

EnBW Regional AG

In the first years of the new millennia, the state government and the city of Stuttgart both sold their minority shares in EnBW and both private national firms, e.g. Deutsche Bank AG, but also foreign firms acquired considerable stakes, Electricité de France or HSBC. Following the same trend, in 2002 Stuttgart sold its remaining share in NWS AG to EnBW.

[21] The buyback itself is not without controversy. A public inquiry by the state parliament is currently investigating whether the buyback price of 4,67 billion Euro was appropriate as well as whether keeping the contract secret and without parliamentary control was in line with the constitution.

Hence after 2002, the city of Stuttgart had no ownership any more in the city's water and energy provision. After a squeeze out of the remaining shareholders, EnBW becomes the sole owner of NWS AG in 2003 and integrated it completely into its firm structure through the subsidiary EnBW Regional AG.

Although the city of Stuttgart was no longer directly involved in water provision, for the governance of the water (but also energy) provision a number of relations and contractual agreements remained between the city and EnBW Regional AG (see Landeshauptstadt Stuttgart (2001b)).

Firstly, the city and EnBW concluded a concession agreement until the end of 2013. For this concession agreement the city would receive 50 million Euros annually, thereof roughly 13 million euros for the water provision.

Secondly, despite selling its stake in NWS AG along with the 33% share in the long-distance networks, the city agreed with EnBW that they would retain their seats in the distance-water supply associations. This meant that despite EnBW having acquired the 33% share in the associations, a contractual agreement ensured that Stuttgart would be able to nominate city representatives for the association board. Also these representatives would not be answering to EnBW but only to the city of Stuttgart itself (see Zweckverband Landeswasserversorgung (2012) and Zweckverband Bodensee-Wasserversorgung (2012)).

Thirdly, the two parties agreed that price setting would be based on the current system of cost accounting as applied by the NWS AG. In case of an intended increase in price the city would have the right to view the necessary documents to justify a potential change (see Landeshauptstadt Stuttgart (2001b)).

Finally, city representatives became members of the advisory boards ('Beiräte') of EnBW AG and EnBW Regional AG. The idea of these boards is to consult the firm about its strategy and to improve communication between the city and the firm.

- Stuttgart's mayor Wolfgang Schuster as one out of 38 at the advisory committee of the holding EnBW AG
- Five Members from different political parties represent the city in the 'Dachbeirat' of EnBW Regional AG
- And the 'Regionalbeirat Stuttgart' comprises 21 local politicians from the city.

KWS

After the end of the concession contract at the end of 2013, the city intends to re-municipalize water provision and potentially also energy. While this process is not yet finished and the details of the switch are discussed in the next section, the city intends the following structure: Water provision will join the existing LPE that manages sanitation and sewage under the new name 'Kommunale Wasserwerke Stuttgart' (KWS). This LPE is not legally independent but a part of the city administration, hence a directly managed LPE. In addition to the local water network, KWS is envisaged to represent the city directly on the boards of the long-distance water associations. For this purpose the city intends to buy back not only the city's infrastructure but also the 33% shares in the associations that were sold to EnBW in 2002.

As Stuttgart gave up a large part of its competences to manage water services in the process of the privatization, an immediate inhouse provision without EnBW capacities would be difficult if not impossible. For this reason, the details of the re-municipalization process were discussed

between the parties in terms of a comprehensive unbundling concept. After a first round of negotiations, the current demerger concept as shown in Figure 8 arose (see Landeshauptstadt Stuttgart (2012)):

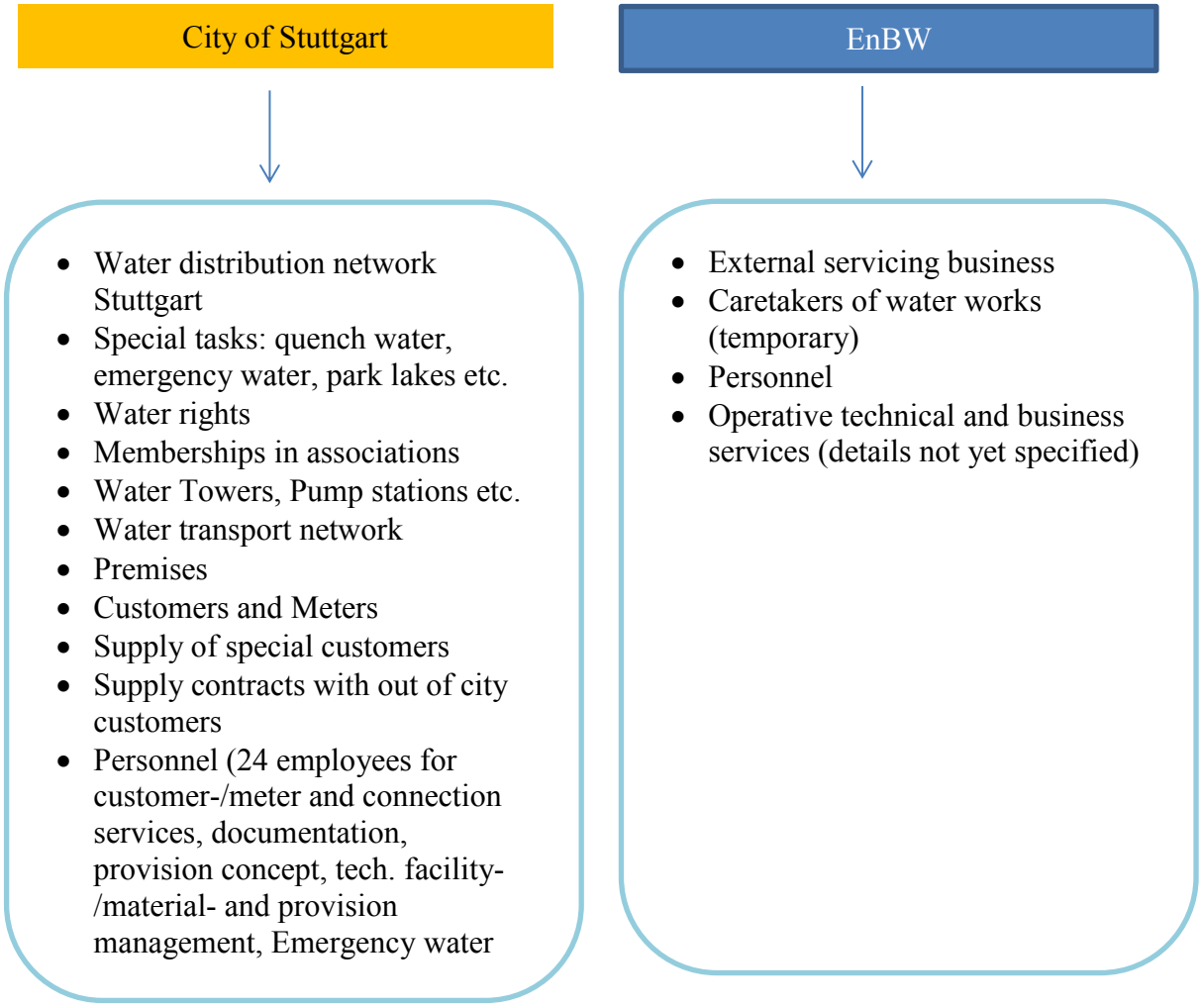

Figure 8: Competence sharing under the envisaged water provision arrangement (adapted from Landeshauptstadt Stuttgart (2012))

Particularly for the first three years, the parties agreed that for the transition period of at least three years EnBW would provide technical services for a full scale of operations, corresponding to the current quality and scope of the operations management. It was further agreed that for this services EnBW would receive 30.65 million Euro per year.

There was still some discussion, however, about a number of particular tasks which the city preferred to be taken over by its own LPE immediately:

- Business services like administrative and cost accounting as well as controlling
- Tariff related services including metering and bill settlement
- Drinking water laboratories and control stations

Finally, as a result of the conflicting assessments about the buy-back price, EnBW agreed only under a reservation clause that the parties successfully negotiate on a price, the schedule as well as the concrete process of the planned re-municipalization are questionable.

5. Switching context for Stuttgart's water provision

In this section, the switches from one institutional arrangement to another are examined in more detail. Although the four outlined organizations would lead to three switches, switch one (from TWS AG to NWS AG) and two (from NWS AG to EnBW Regional AG) are deeply linked and therefore treated as a succession of steps leading towards the privatization of the city's water provision.

From TWS AG to NWS AG and to EnBW Regional AG: The dissolution of municipal control over water provision

An analysis of the drivers that led to the decision of the city of Stuttgart to privatize its water provision reveals that the relevant factors have little to do with the supply of water itself. On the contrary, water provision does not appear to have been a very intensively discussed issue and no reports about particular experienced problems or the need for a reform of the service exist.

Instead of a service specific explanation, the main drivers of the switch are rather located at the meso and macro level, and have to do with the multi-utility character of the TWS AG (and later the NWS AG) coupled with the significant structural changes in the European and German energy sector. From today's perspective the privatization of the water provision can to some extent be interpreted as a byproduct of the evolution of the local energy provision, both of which were managed through the TWS AG.

As already mentioned, it was and still is typical for (larger) German municipalities to have one or even several multi-utility LPEs to provide public services. In Stuttgart, the TWS AG was historically always responsible for water and energy provision. Later on, the TWS AG was part of a nested holding structure through which the city controlled its various enterprises. As the annual investment reports of the previous decade reveal, the city of Stuttgart has been managing more than 10 mostly corporatized LPEs in various different service areas (see Landeshauptstadt Stuttgart (2001a) and Table A1 in the appendix for an outline of the 2001 consolidated financial statement).

While the strong reliance on multi-utility LPEs in Germany has a historical component, there are also clear financial and economic factors. Most importantly, in their corporatized form multi-utility LPEs can benefit from tax-deductible loss compensation. This system allows municipalities to balance profits and losses from different activities, resulting in a reduced tax burden. As can be seen in Table A2 in the appendix, this was also the case in Stuttgart where traditionally the deficits from public baths and other deficient activities were used as a tax shield and hence reduced the profits made through public services like water and energy.[22]

A strand of research on German cities and their entrepreneurial activity, see Edeling et al. (2004) and Reichard and Grossi (2008), also states that the corporate (holding) structure of these LPEs

[22] Some observers like Bardt et al. (2010) argue that the system of tax-deductible loss compensation along with other tax privileges lead to a substantial distortion of competition in the many sectors of public goods provision and put private firms at a considerable disadvantage.

also affects the role of the city and the firms, as well as their relationship. For Stuttgart, the council communications suggest that the city government and the whole political class considered the city's LPEs not only as a vehicle to provide public services but also as investment and financial wealth. In the council meeting discussing the sale of NWS AG to EnBW, which received overall support by virtually all political parties represented in the council, the realization of the firm value was considered an important result of the privatization:

"For the future it is unclear whether higher prices or value appreciations could have been achieved for these shares. It has always been important to us Freie Wähler [remark: a political party in the council], as well as for the other parliamentary groups that we conserve and add to the investments and values of our ancestors. This, we believe, we do with the envisaged package of measures. The value remains and is, as often named, the family silver for the future generations." (translated from Landeshauptstadt Stuttgart (2002))

The statement also shows that the uncertain future of the energy sector was a major driver in the privatization of TWS AG because it was expected by many that the value of the local energy provider would decrease as a result of the liberalization. Later on in a statement in 2007, Stuttgart's mayor Schuster explained that the city withdrew for strategic reasons from energy provision as increased competition was expected (see Landeshauptstadt Stuttgart (2007)).

From a larger perspective, the whole evolution TWS AG to NWS AG and further to EnBW was just the logical consequence of the state government's strategy to unify the regional energy providers under the control of a single enterprise: EnBW as a regional champion. To arrive at this goal, a step by step process was followed, initially leading to two simultaneous merges in 1997: TWS AG and NEV AG to NWS AG as well as Energieversorgungsunternehmen Badenwerk AG and Energie-Versorgung Schwaben AG to EnBW.

The next step in the plan of Baden-Wurttemberg's government was to deepen the cooperation between the two remaining firms. As explicitly stated by the state governor in March 1999, NWS AG was supposed to collaborate more closely with EnBW (see Handelsblatt (1999)). After some initial resistance by employees and also the firm management of NWS AG, who saw no need for a change in the existing structure und intensified cooperation, the two firms announced a close and sustainable cooperation in February 2000 (Stuttgarter Zeitung (2000)). The final takeover of NWS AG by EnBW occurred in 2003.

Hence, as a side product of the merger wave in the energy sector, Stuttgart's water provision was privatized because it was part of the multi-utility LPE. Although one opposition party suggested spinning-off the water provision into an independent organization, this was dismissed by the city government as too complicated and unfavorable from tax perspectives (see Landeshauptstadt Stuttgart (2002)). The tax incentives were also mentioned as the reason why the city changed its original plan of keeping a 25% stake in NWS AG to selling the whole holding company (SVV), entailing the sale of the whole 42.5% share in NWS AG as well as the 9% of EnBW shares that the city was holding until 2002.[23]

For its share package, the city received a compensation of 2,349,983,169.94 Euro. To ensure that EnBW would be the major owner of NWS AG, a part of the compensation would be paid only after other municipal shareholders sold their stakes and EnBW exceeded 75% of the shares. Apart

[23] At that time, a seven year retention period applied before acquired shareholdings could be sold tax free. Hence, to sell its NWS AG shares, which it received in 1997, tax free, the city would have had to wait until 2004. To circumvent this retention period, the city government suggested to sell of the whole holding company, which was all along city property.

from the initial payment, the city would further receive 50 million Euro per year as a concession fee. Further, an agreement with EnBW was reached to guarantee facility locations as well as employment protection.

Creation of KWS Stuttgart: Re-municipalization of water provision and its infrastructure

After the privatization at the end of 2002, water provision received little attention in the following years. Regarding the political discourse in the city council, the topic of privatization or its reversal were not discussed except for two motions by opposition parties in 2004 (see Landeshauptstadt Stuttgart (2004a) and Landeshauptstadt Stuttgart (2004b)). Considering the development of some key service characteristics it appears unlikely that the drivers of the switch are connected to public discontent with the provided service characteristics: water losses, which are a main indicator of network quality, maintenance and re-investment effort, decreased from 9% in 2001 to 7% in 2009. Similarly, during the same time service disruptions decreased from 1,100 to 700 per year.

Also with respect to tariff/price, a factor that is often politically delicate, the average annual increase since 2002 was 2.7% and therefore well below the 4.8% in the decade before the privatization. Given this, there is little doubt that similar to the previous switch towards privatization, factors other than the service characteristics were driving the re-municipalization (see Landeshauptstadt Stuttgart (2012)).

The long term evolution of water prices in Stuttgart is displayed in Figure 9 (see EnBW (2010)). In recent years, particularly the price increase in 2013, implemented in 2012, led to intense discussions. After allegations of unjustified price increases to manipulate the valuation of the network before the re-municipalization, the regional cartel authority is now concerned with the case and it is not impossible that it may force EnBW to undo the last price increase.

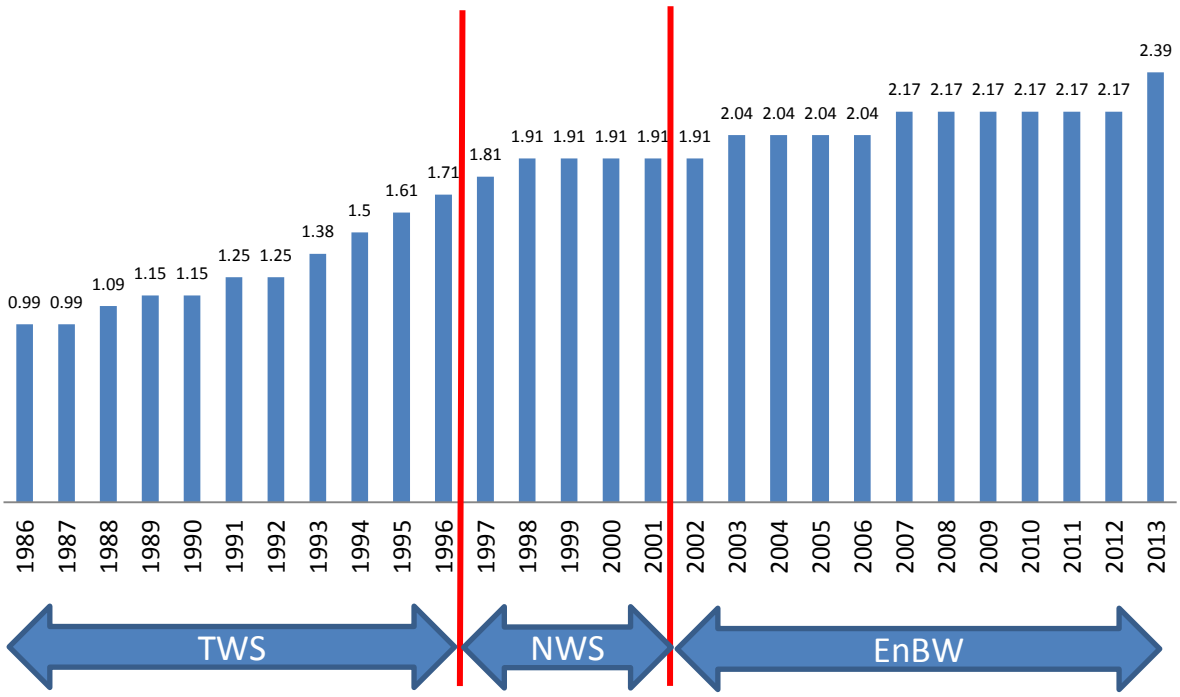

Figure 9: Evolution of water price in Euro per m^3 (net of taxes)

Among the alternative explanations, the single most important factor for the switch is the public movement called 'Stuttgarter Wasserforum', which is strongly related to the privatization reversal. While it is hard to discern if the Wasserforum was actually a causal force for the re-municipalization or itself rather a feature of a changing attitude in the public, it was certainly an important trigger.

The 'Stuttgarter Wasserforum' is a loosely organized public movement that formed after the privatization of Stuttgart's water provision in the end of 2002. Its main aim is to stop and reverse the sale of municipal providers and facilities for public services in general and the re-municipalization of the water and electricity provision in Stuttgart in particular.[24]

After a successful campaign against cross-border-leasing in 2003 – the deal envisaged by the city government was unable to reach a majority in the council – the Wasserforum launched a number of public relations activities for the re-municipalization of Stuttgart's water provision: Firstly, demonstrations/vigils after the re-election of the city council and mayor Schuster in 2004 as well as on the international water day 2005. Secondly, the distribution of information material and leaflets in Stuttgart, which intensified before the election. Thirdly, a number of seminars and podium discussions to water and public service related topics in Stuttgart but also in the region (see Stuttgarter Wasserforum).

Finally, in April 2009 Stuttgarter Wasserforum launched a petition for referendum with the goal to re-municipalize water provision. The petition was supported by a considerable number of (local) NGOs like 'attac Stuttgart' but also political parties from the city council like the Green party and the post-communists. As their declared goal, the city's water provision should be 100% re-municipalized. Cooperation for the provision with outside parties through a concession contract, particularly EnBW, was therefore opposed by the Wasserforum.

The most relevant events surrounding the petition are exhibited in Figure 10, which also reveals the close relationship between the petition and how city politics reacted to a mounting shift in public opinion. In spring 2009, just a few weeks before the start of the petition, the city and EnBW produced a declaration of intent, outlining the plans for the future water provision through a mixed public private LPE with 50% ownership for each partner (see Landeshauptstadt Stuttgart (2009)).

The launch of the petition for referendum made the organization of Stuttgart's water provision an important topic for the local elections. While there were only two related motions in 2004 and three motions in 2007, in total 19 motions regarding the design of water provision were discussed in the city council of Stuttgart in 2009, 18 thereof before the elections in June (see Landeshauptstadt Stuttgart (2013)). Interestingly, the preliminary decision to re-municipalize has likely already occurred two months after the start of the petition: Shortly before the election, the governing party itself filed a motion to completely transfer water provision to the municipality, thereby nullifying the previous accord with EnBW.

[24] In addition, the Wasserforum demanded that the practice of cross-border-leasing (CBS), where a US trust would obtain ownership of an asset and lease it back to the city, should be ceased. CBS were typically concluded between US Trusts and European cities and enabled the parties to benefit from national differences in tax laws. CBS were used until the end of 2004 when the US government changed the regulations and declared such operations as abusive.

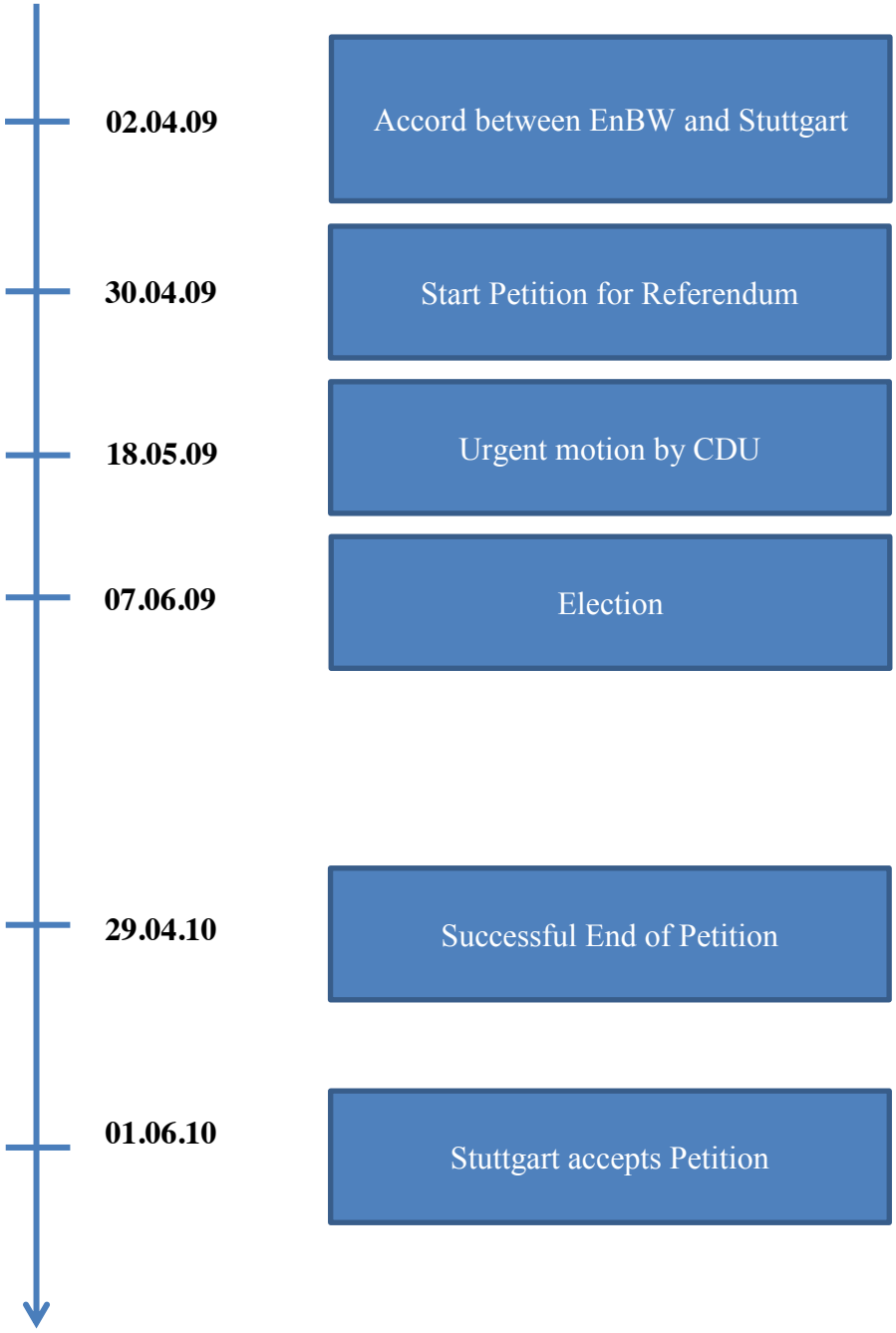

Figure 10: Relevant events before decision to re-municipalize water provision

Until spring 2010, the Wasserforum was able to collect 28,500 signatures by local supporters and the city government was now forced to decide whether to accept to demands of the petition directly or put it up for popular vote. Finally, in June 2010 Stuttgart's government accepted the petition proposal with a council resolution (see Stuttgarter Zeitung (2010) and Landeshauptstadt Stuttgart (2010)).

To the question, why the public movement 'Suttgarter Wasserforum' was so successful, it is important to understand the Wasserforum as linked to an increased citizen participation in Germany through public movements and tools of direct democracy. Particularly in the state Baden-Württemberg, public participation and public movements experienced an increased interest as a result of the Stuttgart 21 discussions and protests (see Box 3 for more on Stuttgart 21).

Box 3: Public participation, protests and Stuttgart 21:

Stuttgart 21 is a railway and urban development project in Stuttgart, Germany's sixth largest city and capital of the state Baden-Württemberg. The concept attempts to make Stuttgart part of the "Magistrale of Europe", a high-speed line connecting Paris to Bratislava as well as improving local infrastructure and substantially modernizing the current terminal station. Upon introduction of the project in 1994 cost were estimated at 2.46 billion Euros to be shared among the German railway company Deutsche Bahn AG, the Federal Republic of Germany, the state Baden-Württemberg, the city of Stuttgart, Stuttgart airport and the European Union. Construction works started in 2010 (see Deutsche Bahn AG (1994)).

Stuttgart 21 was a highly controversial project from the start with criticism centering on the destruction of natural habitat, the demolition of cultural heritage, an entanglement of politicians and commissioned construction companies as well as exploding costs (latest estimations of total costs amount to 6 billion Euros) (see Der Spiegel (2013)). Protests spiraled after a petition for referendum signed by 62.000 people asking to stop Stuttgart 21 was ignored by the city's then-mayor from the Christian Democratic Party. The Green Party who was the only major political party in opposition to Stuttgart 21 won elections of the city council in 2009 with a record high while the Christian Democrats lost 8.6% (see Stuttgarter Zeitung (2009)).

Following the start of construction works in 2010 protests peaked when tens of thousands took to the street on a weekly basis. The question of a referendum received nationwide media attention and was discussed by the federal government with Angela Merkel arguing against a popular vote (see Süddeutsche Zeitung (2010)). These debates are cited as one key factor driving the outcome of regional elections in 2011. While the Green Party reached an unprecedented 24.2% and ever since has headed the first and only government in a German state, the previously governing coalition of Christian Democrats and Liberals lost 10% in total (see Der Spiegel (2011)).

Relatedly, in the water sector a number of similar initiatives for the re-municipalization of water and public services had emerged in other large cities such as Berlin or Hamburg. As in the case of Berlin, the movements had successfully campaigned for the disclosure of previously confidential contracts between the city and the private water providers. As such, the Stuttgarter Wasserforum and its success may also be interpreted as a general trend in public participation instead of a singular case.

With respect to the re-municipalization process that started with the success of the petition, it has not yet been concluded. Although after the petition it was clear that the infrastructure and

therefore ownership would be transferred back to the city, the operational details as well as the buyback price presented two considerable obstacles.

Regarding the former, as the petition did not clearly specify the details of the re-municipalization, the question arose if to what extent the city should re-integrate water provision into the government administration. The city government decided to commission a consulter to compile and expertise report on this question, covering not only water but also energy and gas. As the concessions for both water and energy would cease in 2013, a general approach to the question of public services was intended (see Landeshauptstadt Stuttgart (2011)).

In this expertise, the consulting firm suggested to leave operation with EnBW (see Horvath & Partner GmbH (2011)). During the negotiations, however, the city government, potentially under pressure from the Wasserforum and the political opposition, did not follow the suggestions of the expertise and changed its stance. Eventually, after a transition period also the main operations should be transferred to the city and a very limited number of tasks remain with EnBW (see Figure 8 and Landeshauptstadt Stuttgart (2012)).

As it appeared clear that the scope for future cooperation became increasingly limited, the negotiations turned sour the focus shifted to the buy-back price of the infrastructure. The differences in valuation are substantial: Using different valuation methods the EnBW arrives at 600 – 750 million Euros compared to 160 – 180 million Euros as calculated by an expertise for the city. As no solution could be found during the negotiations, the city government has taken legal action for restitution of the water network (see Stuttgarter Nachrichten (2013)).

Preliminary appraisal on the pros and cons of the adopted governance structures

As shown in this section, despite the changes, the different governance types had little impact on the service provision, which is largely determined by the quasi-fixed structure of water supply in Stuttgart. In light of some recent evidence on the (unclear) efficiency differences between public and private provision of public services, this is not very surprising. For instance by reviewing the existing empirical evidence Bel and Warner (2008) and Bel et al. (2010) find that cost for providing public services (water and waste) do not statistically differ between public production and contracting-out (see Klien and Saussier (2013) for a revision of the evidence on LPE efficiency). Hence, it is not just the particularity of the chosen case study of water provision in Stuttgart, but appears to be a frequently observed phenomenon.

So the question arises if questions of governance are negligible and whether it does not matter which type of LPE is chosen by a local government to provide a service. This case study has shown that service characteristics like tariffs or quality are certainly not the only features that stakeholders take into account. Particularly on the side of civil society and the public movement 'Stuttgarter Wasserforum', more 'soft' issues like accountability, transparency and citizen involvement in decision making were perceived as important arguments for or against specific governance structures.

For instance, the secretive nature of the contracts with EnBW and the negotiations behind closed doors was highly criticized. As such, the need for a formal contractual relationship as the basis for service provision is a disadvantage in terms of transparency. This applies most strongly to contracted-out services but also mixed public-private or even corporatized LPEs. Not surprisingly, the initiators of the referendum demanded a directly managed LPE that is under total control of the municipality.

A closer integration into the local government is also often demanded in order to increase (political) accountability. Especially political scientists have long stressed this issue in the debate over limits to privatization and the demarcation between public and private sectors (see e.g. Moe (1987), Sullivan (1987) or Gilmour and Jensen (1998). In the case of Stuttgart, accountability issues were initially not taken seriously enough by the local government. Even as public discontent grew, the city tried to address the criticism by creating a mixed public private LPE together with EnBW. From the point of many stakeholders, this was not enough to ensure the effective control of the city over water provision. This case also shows that municipal ownership alone may not be enough to ensure (perceived) accountability and even corporatized LPEs may be questioned on grounds of accountability.

The important role of public opinion and the fact that discontent with policy choices has to be taken seriously, reveals some striking similarities with the privatization experiences in Latin America. As explained in more detail in Martimort and Straub (2009), in the wake of large scale privatizations of former state owned enterprises, public discontent with contracting-out in general had increased considerably. Despite likely increases in efficiency, the perceived and sometimes real increase in corruption had undermined public support for governance types involving private partners. In this sense, the rather intransparent situation surrounding the relationship between Stuttgart and EnBW may have further enforced problems of accountability.

Thus, in the case of Stuttgart, the questions of transparency, accountability and citizen participation appear to have played a more important role in favor of the re-municipalization and more integrated types of LPEs than factors like service characteristics.

6. Challenges for a LPE governed water provision in Stuttgart

In less than two decades, the institutional arrangement for water provision in Stuttgart has gone from a corporatized LPE to an intergovernmental cooperation and further to a complete privatization before returning back to a directly managed LPE. As argued above, these changes are very loosely related to the transaction characteristics of water provision, which experienced little change under either provision mode. In contrast, the drivers of the organizational changes highlight that contextual factors, the political and institutional environment as well as stakeholder participation often trump the logic of transaction cost economics: characteristics of the water service itself are unable to explain the switches in Stuttgart.

Regardless of this, the switches identify a number of critical capacity challenges for managing water provision through LPEs.

Co-ordination and administrative challenges
The state's strategy for energy proved to be a crucial factor for the development of the local provision structures in Stuttgart. Although water provision was not the target of the strategy to consolidate the regional energy providers, the typical multi-utility structure of the TWS AG and later on NWS AG had important ripple effects on the water provision in Stuttgart.

These cross-jurisdictional but also cross-sectorial linkages raise the question about the costs and benefits of multi-utility LPEs. Apart from tax incentives and the potential of profit shifting, the main argument for multi-utility LPE refers to economies of scope or more generally synergy effects. Moreover, if the services are somehow operationally related, multi-utility LPEs have an important role in ensuring a horizontal coordination between municipal services. This was typically considered to be the case for water and energy in Stuttgart, where for instance hydroelectric power stations were managed along with energy and water services.

The disadvantage of multi-sectorial LPEs is of course their decreased individual flexibility. The same governance structure is naturally not always a priori optimal for different services. In the end, multi utility LPEs have to be seen as a trade-off between potential synergies with easier coordination between services and a suboptimal one-size fits all structure. Importantly in the present case of Stuttgart, the trade-off appears to have changed significantly over time. In retrospect, while the structure of combining energy and water under a single organizational structure proved successful for a long time, the liberalization and the associated structural changes in the energy sector might have called for a more differential approach for the two public services. The separate tenders for the concessions after 2013 in water and energy/gas seem to point into this direction.

But again, although a separation of the two services was considered, ulterior motives like tax benefits appeared more important to the city government. Moreover, despite potential concerns, synergy effects between services still gain a lot of attention and are often put forward for using the same governance type for different services. This is confirmed by the arguments in the expertise by Horvath & Partners GmbH (2011) which proposes a bundling of the concession contracts.

Capacity challenges
A crucial role in the current re-municipalization has the question of capacity. Besides the buy-back of the infrastructure, the city also envisages to take over the operation of the water system itself. For this reason, a potential transfer of technical capacity, trained staff, time and knowledge

from EnBW to the new provider KWS is a central issue in the negotiations. Without this transfer, taking over the operations in 2014 will be very hard if not impossible for the city.

Even if the city manages to 'borrow' the necessary capacities from EnBW, a transition period of at least three years is expected before own skills and resources have been built up to replace external capacities (see Landeshauptstadt Stuttgart (2012)). While capacities for general administrative tasks like metering are considered manageable with existing resources, particularly the technical skills for operating a whole water network through specialized personnel (so-called 'caretakers of the network') are hard to obtain in the short term.

This fact also suggests a kind of lock-in effect through the outsourcing of the operation as part of the privatization. Although the city had sufficient managerial and contracting capacity to manage its relationship with EnBW for the duration of the concession, the reversal itself is hampered by a limited capacity to manage the water network. Hence, while the buyback of the infrastructure is mostly a question of financial resources, a re-municipalization that involves also a transfer of operations is more difficult in terms of the requirements for skills and operational capacity.

Finance and budgeting challenges

Financing water provision in Stuttgart has never been a problem in the sense that cost-recovery would not be achieved and additional support from the municipal budget would have been required. On the contrary, similar to the electricity operations, water appears to have been generating profits for the local government that were used to balance deficits from other services like public transport. Also for the last 10 years, the city budget profited directly from the annual concession fee of 50 million euro.

The financial challenge that arises then is how to organize water services as to optimize on taxes. Such tax considerations have been crucial for organizational decisions in the past and it is therefore open as to what extent the final governance structure after the re-municipalization will be affected. Integration into the public administration is favorable for both corporate and value added taxes, which do not apply to municipalities providing water services because it is mandated by the constitution.

In sum, it is a priori unclear if the re-municipalization will have positive or negative effect on the municipal budget. The tax advantages may prove favorable while the concession fees no longer apply.

Risks to integrity and accountability, the particular role of stakeholders

From the perspective of integrity and political accountability, the re-municipalized LPE will again more clearly under the responsibility of the city government. Not only control rights, which are acquired through the buyback of the infrastructure, but also decision rights will be under the control of the city council. Importantly, this means that pricing (and investment) decisions are directly taken by the election politicians. This has not even been the case during the decades of operation by the TWS AG.

As raised by the political opposition but also the citizen movement 'Wasserforum', a number of areas for improvement of accountability and stakeholder involvement remain. Firstly, the fact that the re-municipalization was initialized by the citizen movement did not change the classified and somewhat little transparent nature of the re-municipalization process. Meetings and details from agreements, also during the negotiation phase were kept as confidential.

While such secrecy may sometimes aid the negotiation process, it gave rise to speculations about the envisaged goal of the city council and the intended degree of re-municipalization. Secondly and related, the relationship between some major political actors and EnBW remained questionable in the eyes of many observers. As outlined before, a number of politicians from Stuttgart as city representatives became members of the advisory boards ('Beiräte') of EnBW AG and EnBW Regional AG. From a corporate governance point of view, this close connection between EnBW and key policy makers through financially rewarded positions on the advisory board did not live up to standards of transparency and measures to avoid conflict of interest. Potential lobbying efforts or even accusations of political capture (see Loewe (2010)) were the result of this close but informal relationship between the firm and the local political class.

Thirdly, that a citizen movement outside the political sphere, the 'Wasserforum' refuses any connection or support from political parties, could develop such pressure on the city government through means of an instrument of direct democracy is remarkably. It is also indicative that not only the former governing party but the whole party system was unable to integrate the concerns of a significant number of citizens.

In general, the case of Stuttgart shows clearly that cities and municipalities need to incorporate stakeholder participation more closely into their decision making, and if only for the sake of informing citizens. Failing to do so undermines political accountability and moves important debates outside the political channels. In Stuttgart this has led to a situation, where stakeholders and citizens now seek to influence city decision by means of petitions and referenda instead of through party politics. The organizers of the successful 'Wasserforum' have extended their demands for re-municipalization now to the energy and gas sector. A corresponding petition for referendum with enough (more than 20,000) signatures was rejected by the city council as invalid but debates are still on-going.

Summary

To summarize, the challenges for a successful re-municipalization of Stuttgart's water provision are manifold. Capacity challenges to integrate the actual operation of water supply but also accountability challenges in the question of how to deal with citizen movements and stakeholders appear most crucial. Other challenges like financing and co-ordination of services have been shown to be important but are well within the means of the existing capacities of the city.

Two important more general observations can be made from this case study. On the one hand, the actual provision of service seems to have little influence on the decision to change governance structures, at least in the present case. This was the case for both privatization as well as re-municipalization of the service. From a theoretical perspective a purely transaction cost economics approach falls therefore short of explaining the switches. Further research on explaining organizational switches should therefore consider more political economy related factors, as outlined in this study.

On the other hand, the experiences of the re-municipalization process also raise the question of reversibility of a material privatization. The complicated and until now unsuccessful negotiations with EnBW are suggestive of this problem. Although the city is expecting the courts to rule in its favor and force the firm to return the network at an 'acceptable' price, this study reveals the potential hold up problems in cases of material privatizations. Specifically the problem of asset valuation at the end of a concession contract, as predicted in Williamson (1976), proves to be a substantial complication for the re-municipalization.

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8. Appendix

	1999	**1998**	**1997**	**1996**
	TDM	TDM	TDM	TDM
· Versorgung und Verkehr (SVV, SSB, HSG)	36.581	157.220	242.205	-52.954
· Messe, Veranstaltungen, Marketing und Märkte (SMK, SM, VMS)*	-13.390	458	4.085	6.098
· Wohnbau und Immobilien (SWSG, BAG's)	-1.705	21.301	16.405	11.385
· Entsorgung (SES)	0	0	0	-1.356
· Kur- und Bäderbetriebe (KBB, KBB H+F)	112.046	- 28.881	- 29.330	-15.862
· Krankenhäuser (BH, KH, OH, Ca)	56	1.689	71	-8.750
· Übrige Bereiche	-3.685	- 4.259	- 11.418	-12.418
Flughafen	-361	-426	-782	-486
Wohnanlage Fasanenhof				
Konzernjahresergebnis	129.542	147.102	221.236	-74.343
* nachrichtlich:				
darin enthaltene Zuschüsse aus dem städtischen Haushalt an die SM und Kostenerstattungen an die SMK	11.745	10.530	12.496	12.956

Table A1: Consolidated financial statement of the city of Stuttgart 2001

Local Public Enterprise

French case study

Eau du Ponant

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October 2013

Executive summary

In France, three different types of LPEs can be distinguished: semi-public companies, local public enterprises for local development, local public companies. However all types of LPEs are defined as entities organized under private law and delivering services of general interest. Public authorities hold at least the majority of the capital in those companies.

Most of the French LPEs can be found in the sectors of urban planning, tourism and housing.
As of June 2013, there are 1,158 local public enterprises in France which represents 7.2% of the overall 16,000 LPEs identified in Europe. French LPEs employ 70,000 people and have an annual turnover of 11.93 billion euros. They represent an overall capitalization of 3.56 billion euros.

The local public company "Eau du Ponant" was created by four existing and distinct inter-municipal public authorities in charge of water service provision on their territories: Brest océane métropole, SIDEP, syndicat du Chenal du Four and syndicat de Kermorvan et Kersauzon. These four local public bodies decided to join through a LPE to manage their water services at a larger and more relevant scale. Three of the four inter-municipal public authorities share and use the same raw water resources within a common watershed. Hence the territorial and hydrographical context was part of the rationale for the LPE creation. Moreover, the concomitant ending of delegation contracts between Veolia and the four local authorities was the opportunity to trigger the SPL creation. These two contextual factors lead to the set up of "Eau du Ponant" SPL in June 2010, just a few days after the French Act on SPL came into force. The territory supplied by "Eau du Ponant" is both urban and rural and it is located in a coastal area in the western part of France.

"Eau du Ponant" is supplying water to 24 municipalities, 76 500 customers and 260 000 inhabitants through 2 700 linear Km of networks. It produces 14.31 million m^3 per year generating 40 million euros of turnover. It employs 136 people.

The SPL "Eau du Ponant" holds different missions on the territory of its four shareholders.

Competence and responsibilities of "Eau du Ponant" and its shareholders

<table>
<tr><th>Missions</th><th>BMO</th><th>SIDEP</th><th>Chenal du Four</th><th>SKK</th></tr>
<tr><td>Operation of water production and distribution</td><td rowspan="2">Eau du Ponant
(99 year contract)</td><td rowspan="2">Eau du Ponant
(12.5 year contract)</td><td>Eau du Ponant
(10 year contract)</td><td>Eau du Ponant
(10 year contract)</td></tr>
<tr><td>Investments – water service</td><td>Chenal du Four</td><td>SKK</td></tr>
<tr><td>Operation of wastewater collection and treatment</td><td rowspan="2">Eau du Ponant
(99 year contract)</td><td>Other inter-municipal authority</td><td>Other inter-municipal authority</td><td>Other inter-municipal authority</td></tr>
<tr><td>Investments – sanitation service</td><td>Other inter-municipal authority</td><td>Other inter-municipal authority</td><td>Other inter-municipal authority</td></tr>
</table>

(source: Eau du Ponant website, 2013)

In order to supply drinking water to its four shareholders, "Eau du Ponant" has passed contracts with Veolia to operate the six water treatment plants and associated reservoirs. It also signed contracts with Veolia to operate the six wastewater treatment plants. These contracts started on April 1st 2012 and should last 6 years. But they can be denounced after 3 years. The contracts amount to 1.3M€/year for water and to 2.3M€/year for sanitation. They comprise a profit sharing scheme to give an incentive to Veolia to manage efficiently energy and inputs.

The ownership of the SPL capital is entirely public as all four shareholders of "Eau du Ponant" are inter-municipal entities. The SPL was created with a capital of one million euros held for 90% by BMO, 4% by SIDEP, 4% by SKK and 2% by Chenal du Four. The ownership of the water and sanitation infrastructure remains in the hands of each of the four shareholders. The Board of directors (BoD) is composed of 9 representatives from BMO, 2 from SIDEP, 2 from SKK and 1 from Chenal du Four, 2 staff representatives and 3 censors, the five latter having a consultative voice. The BoD gathers at least three times a year and decisions are voted by a majority of the present representatives. During the yearly general assembly, each shareholder holds one vote, i.e. 25% of the voting rights.

The funding model of SPL "Eau du Ponant" relies on the collection of a fee paid by the service user. "Eau du Ponant" sends out the invoice to customers and collects their payments. Then it reallocates a share to each of the four inter-municipal local authorities, as agreed and stated in the delegation contracts signed between each inter-municipal authority and "Eau du Ponant".

The advantages of the EPL structure lie in the transparency of its management, the control capacity of its shareholders, the decision making processes which ensure the autonomy of tariff and investments policy for each contract and each water service and on the capacity to invest operational benefits in the service. On the drawback side, the fact that SPL did not have to face competition to be awarded the water services contracts has been questioned by some of the partners.

Each year, the SPL "Eau du Ponant" provides the four inter-municipal authorities with the technical data necessary to produce the regulatory annual report on the water service quality and price[25] which each and every French water service is bound to produce legally. In this report 14 performance indicators[26] have to be calculated by water services (15 for sanitation services). Such a report is a key element of the French sunshine regulation model as it provides information to assess the economic, technical, social and environmental performance of the services. Performance assessment of the four water services is done yearly using mainly the French regulatory set of performance indicators. However these statutory performance indicators have been complemented with specific indicators designed by the contractual partners. As of now, performance assessment is not used by the four local public authorities to reward or penalise their service provider "Eau du Ponant". It is used as a steering tool to manage efficiently the service rather than as a real target driven incentive scheme. However, in the upcoming years, it is planned to use performance assessment, reporting and monitoring in much more incentive perspective. Furthermore contractual partners have periodic renegotiation meetings (at least once

[25] Article 73 de la loi n°95-101 du 2 février 1995 relative au renforcement de la protection de l'environnement
[26] Arrêté du 2 mai 2007 relatif aux rapports annuels sur le prix et la qualité des services publics d'eau potable d'assainissement

every five years) where they can discuss elements of the contract. Three endorsements have already been signed since 2012.

When “Eau du Ponant” was created, 90% of Veolia staff was transferred to the new SPL. Very little competence and know-how were actually lost. However some specific competences were missing in the new structure. Employees had to be recruited for the call centre, for the invoice department and for the communication department.

One of the reasons for the SPL creation is that such a structure makes it possible for the four distinct inter-municipal bodies to share means and resources especially for support functions (such as procurement, customer relationship, contract supervision or human resources and finance).

Regarding customer dispute settlement, local public company “Eau du Ponant” joined the water Mediation on November 2012. The objective is to promote the amicable settlement of disputes that may arise between the water service and its users.

SPL budget is strictly distinct from municipal and inter-municipal budgets and it is funded directly by the customers water invoice. There is no contribution made by the municipal or inter-municipal budgets. The water price is revised yearly for each of the four water services according to a price revision formula embedded in the service provision contracts. SPL pays taxes and VAT as a private company. The budget of “Eau du Ponant” is discussed during in the commission of resources where representatives of the four shareholders sit. The accounting of the SPL is controlled by independent auditors as well as by the revenue Court.

Before and during the switching process, a specific communication campaign has been implemented to explain the rationale of the SPL creation. An information brochure was sent along with the customer invoice. Public notices were posted and press conferences were held.

A consultative water council has been set up. Once every three months, it gathers 12 local stakeholders such as consumers associations and environmental associations. It ensures public participation as it provides an opportunity for discussions on specific themes such as social tariffs or water supply security, for instance.

Table of Contents

EXECUTIVE SUMMARY 85

1 OVERVIEW ON LOCAL PUBLIC ENTERPRISES IN FRANCE 89

1.1 Semi-public companies (SEM—Société d'économie mixte) 89

1.2 Local public enterprises for local development (SPLA—Société publique locale d'aménagement) 90

1.3 Local public company (SPL—Société publique locale) 90

1.4 Key facts and figures about French LPEs 91

2 SETTING THE SCENE FOR THE CASE STUDY: FOCUS ON WATER 93

2.1 Institutional mapping of water services governance: allocation of roles and responsibilities among stakeholders 93

2.2 Overall presentation of SPL "Eau du Ponant" 95

3 GOVERNANCE OF SPL "EAU DU PONANT" 97

4 SWITCHING CONTEXT AND OUTCOMES OF THE SWITCH 100

5 CAPACITY CHALLENGES FOR SPL "EAU DU PONANT" 102

5.1 Co-ordination challenges and tools 102

5.1.1 Technical co-ordination and reporting with local public bodies 102

5.1.2 Local coordination across sectors with the consultative commission for local public services 103

5.2 Capacities of public officials and institutions 103

5.3 Finance and budgeting 104

5.4 Risk to integrity and accountability 104

5.5 Promoting results and learning 105

6 ANNEX 106

6.1 Generic characteristics of LPEs 106

Special thanks to Maxime PAUL, vice-president of Brest métropole océane in charge of water and wastewater affairs, and to Christian CLEMENT, director of Eau du Ponant.

1 Overview on Local Public Enterprises in France

In France, three different types of LPEs can be distinguished (table 1): semi-public companies, local public enterprises for local development, local public companies. However all types of LPEs are defined as entities organized under private law and delivering services of general interest. Public authorities hold at least the majority of the capital in those companies.

Table 1. *Different types of LPEs in France*

	Semi public company (SEM)	**Local public enterprise for local development (SPLA)**	**Local public company (SPL)**
Structure	mixed public private capital	100% public capital	
Shareholders and partners	Minimum of 7 shareholders with one private shareholder Capital: from 50% to 85% for local public authorities; from 15% to less than 50% to other shareholders Subsidiaries and participation in other companies allowed	At least two local authorities shareholders 100% of capital belong to local public authorities Can only operate for its shareholders Can not create subsidiaries nor take participation in other companies	
Territory	No territorial limit, except for SEM operating in energy sector and in funeral services	Missions limited to the territory of the local public shareholders	
Control by local public authorities	Local public shareholders have a certain control over the company through its representatives in the governing bodies	Local public shareholders have total control	
Contractual relationships with local public authorities	Competitive tendering	No competitive tendering	
Contractual relationships with private sector	Competitive tendering	Competitive tendering	

Source: LPE federation, *Les sociétés publiques locales: un an pares la loi, quel bilan?*, June 2011

A more comprehensive table can be found in annex of this document.

1.1 Semi-public companies (SEM—Société d'économie mixte)

Semi-public companies have been created in 1983[27]. It is traditionally the most significant type of local public enterprises in France. It requires at least seven shareholders, some of them being private organizations, such as banks, companies, or the chamber of commerce or industry. Between 50 to 85 percent of the capital share has to be held by public authorities, i.e. the State or local authorities. Such local public enterprises are not limited to the territory of the local authorities which are financing them. They can compete with private enterprises in other geographical areas. To do so, they have to go through the usual call for tender procedures. SEMs

[27] Loi n°83-597 du 7 juillet 1983 relative aux sociétés d'économie mixte locales codifiées au code général des collectivités territoriales le 7 avril 2000. Modifiée par la loi n°2002-1 du 2 janvier 2002 tendant à moderniser le statut des sociétés d'économie mixte locales.

are competent to carry out development and construction operations or to operate commercial or industrial public services or any other activity of general interest within the scope of responsibilities of the local authorities shareholders.

1.2 Local public enterprises for local development (SPLA—Société publique locale d'aménagement)

Local public enterprises for local development were created in 2006[28]. They require a minimum of two local authorities for setting up a local public enterprise, which is exclusively financed by public authorities. Such LPE is limited to regional and urban planning and cannot operate outside of the local authorities' territory. Considered as natural extensions of their local shareholders, SPLAs are being entrusted with tasks directly by them, without competition. This status appeals to local authorities wishing to remain in full control of their urban development and to rely on a single operator they completely control.

1.3 Local public company (SPL—Société publique locale)

Local public companies have been introduced in France by the Act[29] of May 28th 2010 (figure 1) after a reform initiated by 271 parliamentarians and adopted unanimously by the Parliament. They are limited companies established by local public authorities within the framework of their competence and mainly governed by the French Commercial Code. Their capital is 100% public and is held by at least two local public authorities. In SPLs, all members of the board of directors (or supervisory board in the case of dual structure) are local elected officials, representatives of local shareholders. Its activities go beyond regional and urban planning. It might be dedicated to construction or all kind of services of general interest. However its activities can only be exercised for its public shareholders within their territory. SPLs do not have to go through usual call for tender procedures.
SPLs are competent to carry out development and construction operations or to operate industrial or commercial utilities and other activities of general interest within the competence of local authorities (see annex 6.1 for generic characteristics of SPL).

Figure 1. *Article 1 of the Act of May 28th 2010 creating Local public companies (SPL)*

"Local authorities and groups of local authorities may create, within the framework of competences assigned to them by law, local public companies in which they hold the entire capital. These companies are competent to carry out development projects, construction or to operate industrial or commercial public services or any other activities of general interest. These companies operate exclusively on behalf and on the territory of their shareholders."
Act May 28th, 2010 - Article 1 (Article L1531-1)

[28] Loi n°2006-872 du 13 juillet 2006 portant engagement national pour le logement créant les sociétés publiques locales d'aménagement.
[29] Loi n°2010-559 du 28 mai 2010 pour le développement des sociétés publiques locales.

1.4 Key facts and figures about French LPEs

Several drivers can explain the development of LPEs in France. They are perceived by local public authorities as an attractive economic model positioned in between public and private sectors. From the private sector, they borrow a capacity of responsiveness and flexibility in business management. From the public, they borrow the duty to fulfill long term and general interest missions within a local anchorage. Drawing from private business mechanisms while relying on the fundamentals of public model, LPEs accompany local communities in virtually all their missions. Moreover, LPEs steer projects and produce appropriate responses to local challenges. They give priority to local resources and actors since their jobs and decision centers cannot be relocated. They favor general public interest compared to financial interests as they reinvest most of their profits in their territory to make it more attractive and competitive.

LPEs provide local public services in forty fields such as urban development, housing, transport, tourism, energy or waste (table 2).

Table 2. *LPEs' field of activities*

Regional & urban planning
Creation of public spaces
Urban renewal
Building of public equipments

Business development
Talent pool for companies
Airports, ports, multimodal platforms
Food industry, trading
Financial engineering (banks…)
Territorial promotion (development agencies…)

Environment – Networks
Water & wastewater
Waste
Communication & media
Energy (electricity, gas, renewable energies)

Public transport
Parking
Transport

Housing
Housing construction
Rental management
Commercial real estate

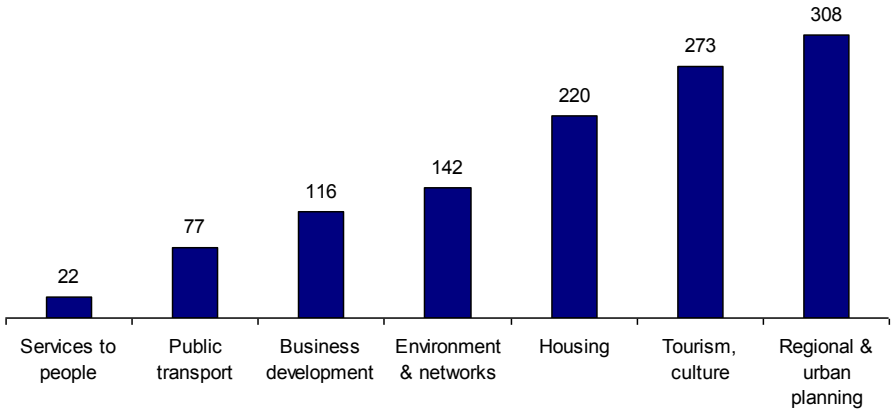
Tourism - Culture - Leisure
Marinas
Ski lift
Touristic accommodation
Sites & monuments
Museums
Theme parks
Theatres, cinemas
Leisure & nautical centres
Sports clubs
Hydrotherapy
Tourist information centres
Reservation centres
Congress halls
Exhibition parks
Events

Services to people
Funeral
Catering
Health and social institutions

(Source: French federation of local public enterprises – 2012)

Most of the French LPEs can be found in the sectors of urban planning, tourism and housing (figure 2).

Figure 2. *Number of French LPEs by sector*



(Source: French federation of local public enterprises – 2013)

As of June 2013, there are 1,158 local public enterprises in France (figure 3), including 62 created in 2012. Within the context of the economic crisis, the pace of creations has doubled in 2012 compared to the annual average rate of the past five years (figure 4). French LPEs represents 7.2% of the overall 16,000 LPEs identified in Europe.

Figure 3. *Number of French LPEs*

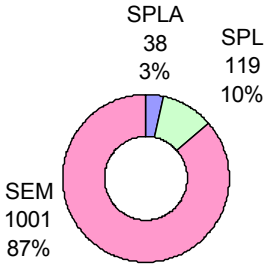
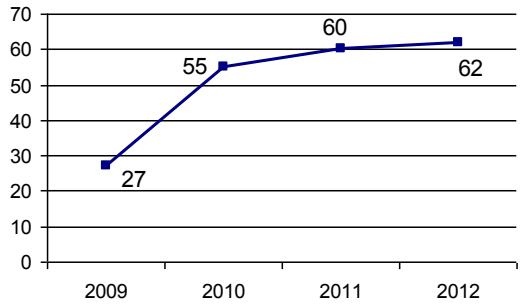


Figure 4. *Number of French LPEs created*



(Source: French federation of local public enterprises – 2013)

French LPEs employ 70,000 people and have an annual turnover of 11.93 billion euros (figure 5). They represent an overall capitalization of 3.56 billion euros (figure 6).

Figure 5. *Annual turnover of French LPEs*

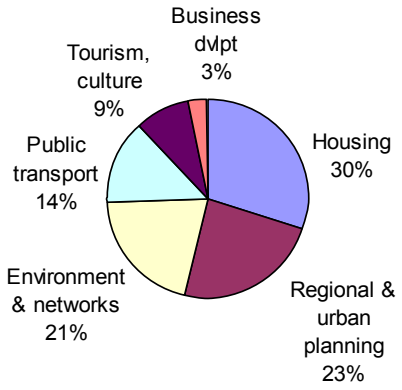
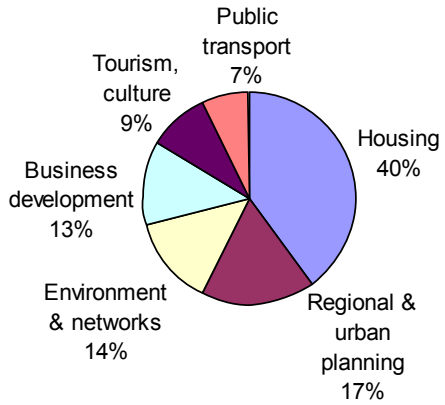


Figure 6. *Capitalization of French LPEs*



(Source: French federation of local public enterprises – 2013)

2 Setting the scene for the case study: focus on water

2.1 Institutional mapping of water services governance: allocation of roles and responsibilities among stakeholders

In France, all public water and sanitation services are public and fall within the responsibility of municipal authorities. These may, however, transfer their responsibility to inter-municipal cooperation bodies which then become in charge of providing the service to customers.

At watershed levels, some organisations (SAGE, CLE, Commission de rivière) gather water users and stakeholders for projects management and consultation purpose.

At River basin level, 6 water agencies collect taxes through the water bill in order to provide funding to water and sanitation service to invest in water resources preservation and pollution reduction actions. Water agencies are also in charge of implementing national water policy priorities on their territory.

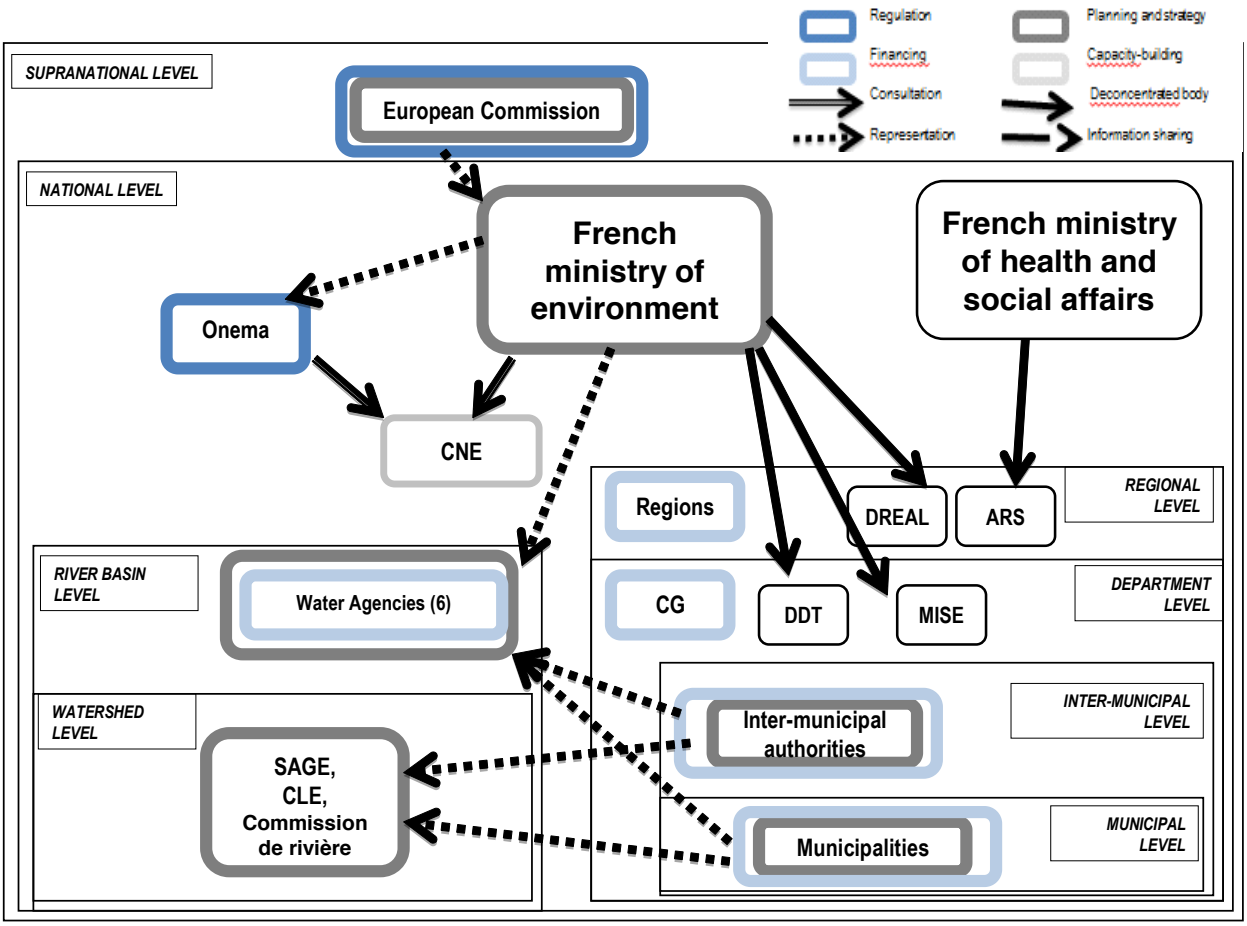
At regional and departmental levels, Regions, Departments and deconcentrated State services provide assistance and funding to water and wastewater services.

At national level, the French national water agency is acting as a sunshine regulator for the water sector. The French ministry for environment is in charge of overall planning and strategy for national water policy. The Comité national de l'eau is a consultative organisation giving its views on the national planning and strategy for water policy.

With the help of its regional agencies, the French ministry for health ensures that drinking water distributed to customers is safe and potable with regard to regulatory physicochemical and microbiological parameters.

The overall governance of water services gathers several stakeholders at very different scales (figure 7).

Figure 7. *Institutional mapping of water services governance in France (2013)*



ARS: regional agency for health
DDT: Departmental directorate of territories
DREAL: regional directorate for environment, planning and housing
CLE: local water commission
CG: Department council
CNE: national committee for water
MISE: interservices mission for water
Onema: French national agency for water
SAGE: water management and planning scheme

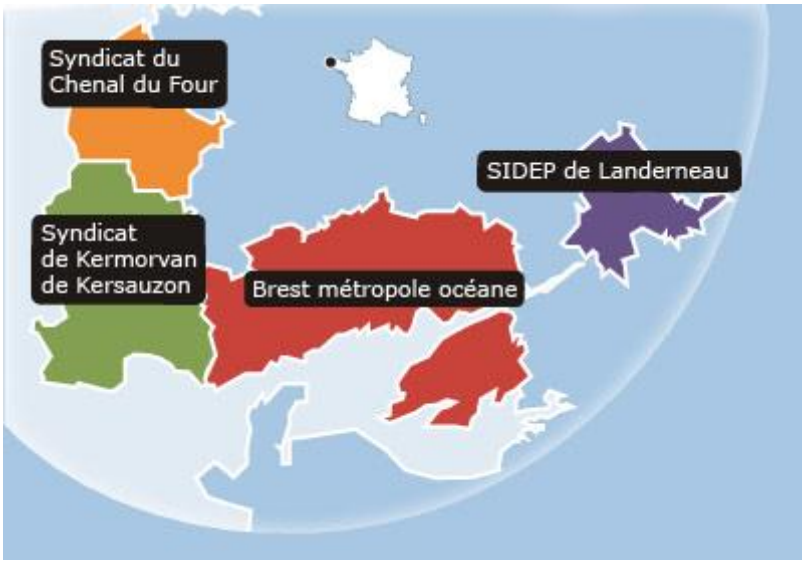
2.2 Overall presentation of SPL "Eau du Ponant"

The local public company "Eau du Ponant" was created by four existing and distinct inter-municipal public authorities in charge of water service provision on their territories. These four local public bodies decided to join through a LPE to manage their water services at a larger and more relevant scale. Three of the four inter-municipal public authorities share and use the same raw water resources within a common watershed. Hence the territorial and hydrographical context was part of the rationale for the LPE creation. Moreover, the concomitant ending of delegation contracts between Veolia and the four local authorities was the opportunity to trigger the SPL creation. These two contextual factors lead to the set up of "Eau du Ponant" SPL in June 2010, just a few days after the French Act on SPL came into force.

"Eau du Ponant" is driven by the four following public shareholders:

- **SIDEP**, an inter-municipal public authority gathering the municipalities of Landerneau, La Roche-Maurice, Plouédern and Trémaouézan
- **Syndicat du Chenal du Four**, an inter-municipal public authority gathering the municipalities of Breles, Landunvez, Lanildut, Plourin and Porspoder.
- **Syndicat de Kermorvan et Kersauzon**, an inter-municipal public authority gathering the municipalities of Lampaul-Plouarzel, Plouarzel, Ploumoguer, Trébabu, Le Conquet, Plougonvelin and Locmaria-Plouzané.
- **Brest métropole océane**, an inter-municipal public authority gathering the municipalities of Bohars, Brest, Gouesnou, Guilers, Guipavas, Le Relecq-Kerhuon, Plougastel-Daoulas and Plouzané.

Figure 8. *Territory supplied by "Eau du Ponant"*



(source: Eau du Ponant website, 2013)

"Eau du Ponant" is supplying water to 24 municipalities, 76 500 customers and 260 000 inhabitants through 2 700 linear Km of networks. It produces 14.31 million m^3 per year generating 40 million euros of turnover. It employs 136 people.

The SPL "Eau du Ponant" holds different missions on the territory of its four shareholders (table 3).

Table 3. *Competence and responsibilities of "Eau du Ponant" and its shareholders*

Missions	BMO	SIDEP	Chenal du Four	SKK
Operation of water production and distribution	Eau du Ponant (99 year contract)	Eau du Ponant (12.5 year contract)	Eau du Ponant (10 year contract)	Eau du Ponant (10 year contract)
Investments – water service			Chenal du Four	SKK
Operation of wastewater collection and treatment	Eau du Ponant (99 year contract)	Other inter-municipal authority	Other inter-municipal authority	Other inter-municipal authority
Investments – sanitation service		Other inter-municipal authority	Other inter-municipal authority	Other inter-municipal authority

(source: Eau du Ponant website, 2013)

Brest métropole océane and SPL "Eau du Ponant" signed a concession (build, operate, transfer, B.O.T.) contract starting on April 1st 2012. Since then, "Eau du Ponant" is in charge of the following missions on the territory of Brest métropole océane:
- drinking water production and distribution;
- wastewater collection and treatment before discharge;
- works on water and sanitation network;
- customer relationships (management of a local call centre, billing);
- fire safety.

SIDEP and SPL "Eau du Ponant" signed a concession (B.O.T) contract starting on July 1st 2012. Since then, "Eau du Ponant" is in charge of the following missions on the territory of SIDEP:
- drinking water production and distribution;
- works on the water network;
- customer relationships (management of a local call centre, billing);
- fire safety.

Chenal du Four and SPL "Eau du Ponant" signed a management contract starting on July 1st 2012. Since then, "Eau du Ponant" is in charge of the following missions on the territory of Chenal du Four:
- drinking water production and distribution;
- customer relationships (management of a local call centre, billing);
- fire safety.

SKK and SPL "Eau du Ponant" signed a management contract starting on January 1st 2013. Since then, "Eau du Ponant" is in charge of the following missions on the territory of SKK:
- drinking water production and distribution;
- customer relationships (management of a local call centre, billing);
- fire safety.

For BMO and SIDEP, which have signed concession contracts with "Eau du Ponant", a specific investment commission has been created. This allows BMO on the one hand and SIDEP on the other hand to discuss their investment policy with their service provider.

In order to supply drinking water to its four shareholders, "Eau du Ponant" has passed contracts with Veolia to operate the six water treatment plants and associated reservoirs. It also signed contracts with Veolia to operate the six wastewater treatment plants. These contracts started on April 1st 2012 and should last 6 years. But they can be denounced after 3 years. The contracts amount to 1.3M€/year for water and to 2.3M€/year for sanitation. They comprise a profit sharing scheme to give an incentive to Veolia to manage efficiently energy and inputs. The contracting procedure followed by "Eau du Ponant" derives from a French order[30] dated June 6th 2005 which is quite similar to the provisions of the French procurement code. Following the call for tenders, four offers were received among which only three were admissible. Veolia offer was then chosen as the best bid.

3 Governance of SPL "Eau du Ponant"

Referring to the taxonomy proposed in OECD report on Local Public Enterprise (2013), SPL "Eau du Ponant" can be described as an inter-municipal cooperation (table 4).

Table 4. *Taxonomy of LPEs*

	Decision rights	**Fragmentation of control**	**Property rights**
Directly managed LPE	Local government	Unique control	Public
Corporatized LPE	LPE management	Unique control	Public
Inter-municipal cooperation	LPE management	Joint control	Public
Mixed LPE	LPE management	Joint control	Public-Private

source: Local Public Enterprise report, OECD, February 2013, p.22

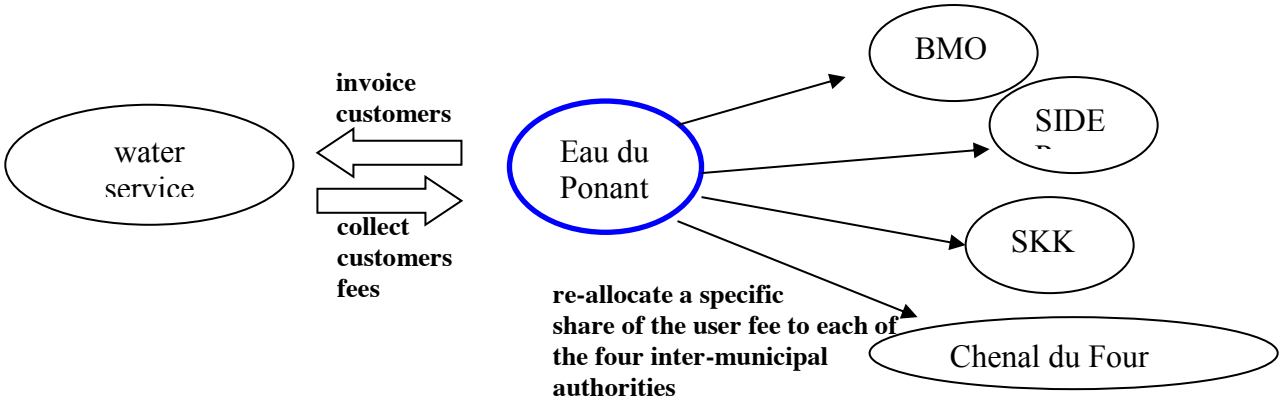
The ownership of the SPL capital is entirely public as all four shareholders of "Eau du Ponant" are inter-municipal entities (see description in the previous section). The SPL was created with a capital of one million euros held for 90% by BMO, 4% by SIDEP, 4% by SKK and 2% by Chenal du Four. The ownership of the water and sanitation infrastructure remains in the hands of each of the four shareholders. The Board of directors (BoD) is composed of 9 representatives from BMO, 2 from SIDEP, 2 from SKK and 1 from Chenal du Four, 2 staff representatives and 3

[30] Ordonnance n°2005-649 du 6 juin 2005 relative aux marchés passés par certaines personnes publiques ou privées non soumises au code des marchés publics.

censors[31]; the five latter having a consultative voice. The BoD gathers at least three times a year and decisions are voted by a majority of the present representatives. During the yearly general assembly, each shareholder holds one vote, i.e. 25% of the voting rights.

The funding model of SPL "Eau du Ponant" relies on the collection of a fee paid by the service user. "Eau du Ponant" sends out the invoice to customers and collects their payments. Then it reallocates a share to each of the four inter-municipal local authorities, as agreed and stated in the delegation contracts signed between each inter-municipal authority and "Eau du Ponant" (figure 9).
For SKK and Chenal du Four, the amount of money reallocated by "Eau du Ponant" is used to finance their water asset management policy and the associated investments.
For BMO and SIDEP, the amount of money reallocated by "Eau du Ponant" is used to cover water service staff expenses.

Figure 9. *Mapping of financial flows and funding model of SPL "Eau du Ponant"*



The advantages of the EPL structure lie in the transparency of its management, the control capacity of its shareholders, the decision making processes which ensure the autonomy of tariff and investments policy for each contract and each water service and on the capacity to invest operational benefits in the service. On the drawback side, the fact that SPL did not have to face competition to be awarded the water services contracts has been questioned by some of the partners.

[31] Censors: Brest métropole office HLM, association CLCV, association Eau et rivières de Bretagne.

Overall the water services operated by "Eau du Ponant" are being funded through the water tariffs. "Eau du Ponant" turnover is estimated to 40 million euros for approximately 14 million cubic meters distributed. No taxes are used to provide funding. Some transfers between domestic and industrial users may exist through the grants allocated by the Water agency.

The water tariff structure is the same in the four water services operated by "Eau du Ponant". It is composed of a fixed part and a variable part. However the water price is different in the four services as it is decided and voted by each of the four inter-municipal bodies (table 5).

Table 5. *Water tariff structure for the four water services operated by Eau du Ponant*

120m^3 consumption	BMO	SIDEP	Chenal du Four	SKK
Annual fixed part of tariff	12.02€	61.80€	102.00€	112.27€
Variable part of tariff	237.44€	216.10€	197.57€	219.31€
Share going to Eau du Ponant	*170.48€*	*121.79€*	*108.69€*	*82.56€*
Share re-allocated to inter-municipal authority	*20.26€*	*48.61€*	*44.45€*	*89.28€*
Water agency fees	*46.70€*	*45.70€*	*44.43€*	*47.47€*
TOTAL water	***249.46€***	***277.90€***	***299.57€***	***331.58€***

Figures April 2012

4 Switching context and outcomes of the switch

Prior to the switch and to the creation of SPL "Eau du Ponant", the water services of the four inter-municipal authorities were organised and managed as described in the table below (table 6).

Table 6. *Competence and responsibilities*

Missions	BMO	SIDEP	Chenal du Four	SKK
Operation of water production and distribution	Veolia (25 year contract)	Veolia (10 year contract)	Veolia (10 year contract)	Veolia (10 year contract)
Investments – water service	BMO	SIDEP	Chenal du Four	SKK
Operation of wastewater collection and treatment	Veolia (25 year contract)	Other inter-municipal authority	Other inter-municipal authority	Other inter-municipal authority
Investments – sanitation service	BMO	Other inter-municipal authority	Other inter-municipal authority	Other inter-municipal authority

BMO had signed a 25 year management contract with Veolia which started in 1987. During this period, Veolia was in charge of operating the service while BMO remained in charge of the asset management policy and the investments.

SIDEP had signed a 10 year management contract with Veolia which started in 2002. During this period, Veolia was in charge of operating the service while SIDEP remained in charge of the asset management policy and the investments.

Chenal du Four had signed a 10 year management contract with "Compagnie de l'eau et de l'ozone" which started in 2002. During this period, Veolia was in charge of operating the service while Chenal du Four remained in charge of the asset management policy and the investments.

SKK had signed a 10 year management contract with "Compagnie de l'eau et de l'ozone" which started in 2003. During this period, Veolia was in charge of operating the service while SKK remained in charge of the asset management policy and the investments.

In 2008, during the electoral municipal campaign, the mayor of Brest (centre city of BMO) expressed his strong will to switch to public management of the water and wastewater services if he was to be re-elected. The switch was to happen when the management contracts with Veolia would end in 2012. In such perspective, BMO asked the two surrounding water services (SIDEP and Chenal du Four) which all share the same water resources to join a common reflection on the future management and organisation of their water services. Using the same raw water implies a common interest to preserve it and manage it in a sustainable way.
Later this initiative was expanded to the inter-municipal water service of SKK which has its own water resources. This water service and the three others had signed management contracts with Veolia which were ending concomitantly in 2012.

In this context three different scenarios of switch were discussed.

1) the set up of a "régie" exclusively on the territory of BMO. This solution would not allow means and resources sharing. It would not allow either the management of the water service at a larger and more relevant scale. This scenario was not chosen.

2) the creation of a new inter-municipal water service which all four inter-municipal bodies would have joined. This solution would have added one more inter-municipal structure to the four existing ones. In a context of political reform for administrative structures simplification, this evolution was not favoured. Moreover this solution would have implied one single water price and one consistent asset management policy on the whole territory of the four water services. All four partners intended to retain their autonomy of decision in tariff policy and investment choices.

3) the creation of a semi-public company with an institutional bank as the private shareholder (Caisse des depots et consignation for instance). This solution was not chosen as it implied the implementation of call for tender procedures for all commercial relationships.

None of these three scenarios appeared as a satisfying solution to the four partners. On May 2010, the adoption of the new regulation on SPL came as a real opportunity. The four inter-municipal authorities agreed to use this new EPL format to switch to public management for their water services. This solution allowed the four partners to four sign separate contracts with the newly created SPL "Eau du Ponant" without having to go through the call for tender procedure.
Signing separate contracts provide an easier control over the SPL, more transparency, similar autonomy compared to the situation prior to the switch, management flexibility, means and resources sharing as well as more efficient cost control. Moreover, the creation of SPL "Eau du Ponant" reflects the willingness to work together on water policy at a more relevant spatial scale, corresponding to technical, contextual and economic realities. But it also reflects the strong will of each of the four partners to remain in control of their own water service and to take into account their own local specificities.

The functional division between what would be outsourced in the form of provision contracts and what the SPL would do in house had to be discussed. The implementation of a provision contract covering the drinking water plants and associated tanks operation was voted as well as a contract encompassing BMO wastewater treatment plants operation. This strategic and structuring choice is based on an overall risk analysis and business analysis. The four inter-municipal bodies wanted the SPL to be in charge of all aspects of the service related to the user. There were some discussions regarding networks and plants. On the business side, the plants (water and sanitation) correspond to an electromechanical and chemistry professional know-how whereas networks correspond more to public works. On the risk side, a broken pipe is not a rare event, but the issue can be tackled by a competent team able to solve the problem before it becomes dangerous. If drinking water is not potable (accidental pollution) or if it were to run out, serious issues would then have to be addressed. Hence it is an area of greater risk. Finally, the rationale for the switch to public management of BMO is to achieve better management of investments over time. The decision was not linked to any issue of poor quality of water supplied or processed. Networks represent 80% of the investment. Therefore it appeared logic to focus primarily on this issue. This

division of the scope of action of the SPL allows the local inter-municipal bodies to focus on what is the most important for them: the relationship with clients and investment management, while outsourcing clearly defined and controllable functions. SPL – "Eau du Ponant" aims to advance step by step, prioritizing areas of operations according to their highest value for the benefit of users.

The SPL creation also made it possible for the four distinct inter-municipal bodies to share means and resources especially for support functions. For instance, "Eau du Ponant" and its four shareholders have set up four specialised commissions:

- a commission for procurement
- a commission for customer relationship
- a commission for contract supervision
- a commission for human resources and finance.

Each of these commissions gathers a representative of "Eau du Ponant" and a representative from each shareholder. They gather four times a year before BoDs.

Without the creation of Eau du Ponant, SIDEP, Chenal du Four and SKK may not have been in capacity of setting up these specialised commissions. This is clearly an ex-post benefit of the switch for the service provision.

However as the switch is pretty recent, it is not yet possible to asses comprehensively the impact of the switch on the full service provision.

5 Capacity challenges for SPL "Eau du Ponant"

5.1 Co-ordination challenges and tools

5.1.1 Technical co-ordination and reporting with local public bodies

Each year, the SPL "Eau du Ponant" provides the four inter-municipal authorities with the technical data necessary to produce the regulatory annual report on the water service quality and price[32] which each and every French water service is bound to produce legally. In this report 14 performance indicators[33] have to be calculated by water services (15 for sanitation services). Such a report is a key element of the French sunshine regulation model as it provides information to assess the economic, technical, social and environmental performance of the services. It enriches the information available to consumers.

Local reporting is done through BoD and commissions (see 5.2) meetings, bearing in mind that the four shareholders of the SPL are also its four customers.

[32] Article 73 de la loi n°95-101 du 2 février 1995 relative au renforcement de la protection de l'environnement
[33] Arrêté du 2 mai 2007 relatif aux rapports annuels sur le prix et la qualité des services publics d'eau potable d'assainissement

5.1.2 Local coordination across sectors with the consultative commission for local public services

It is legally compulsory for municipalities with more than 10 000 inhabitants and for inter-municipal bodies comprising more than 50 000 inhabitants to set up a consultative commission for local public services (CCSPL[34]). This commission gathers local stakeholders involved in all local public services across sectors. It ensures public participation as the attendance to those commissions is totally open. CCSPL has to meet at least once a year to examine annual activity reports for all public services whether they are managed by a private or public operator.
Because it gathers more than 200 000 inhabitants, BMO has implemented such a commission. On the contrary, CCSPL has not been implemented by SIDEP, Chenal du Four or SKK as the population concerned is under the legal thresholds.

One of the censors sitting at the BoD is a representative from the HLM. This presence ensures a close coordination with the social housing sector.

No process and no mechanism to ensure national coordination across sectors have been clearly identified.

5.2 Capacities of public officials and institutions

When "Eau du Ponant" was created, 90% of Veolia staff was transferred to the new SPL. Very little competence and know-how were actually lost. However some specific competences were missing in the new structure. Employees had to be recruited for the call centre, for the invoice department and for the communication department. With the SPL, the four inter-municipal bodies manage their water services at an optimal and efficient scale. They become in capacity of hiring project ownership assistance and specialised consultancy whenever needed.

Regarding customer dispute settlement, local public company "Eau du Ponant" joined the water Mediation on November 2012. The objective is to promote the amicable settlement of disputes that may arise between the water service and its users. Mediation water was created in 2009 at the instigation of the Association of Mayors of France (AMF) and the Assembly of communities in France (ADCF) to prevent disputes between water and sanitation utilities and their customers to end up in court. Justice is long and expensive, while mediation is fast and free. The intervention of the mediator settles amicably 90% of cases on average. Mediation also has the advantage to suspend any enforcement action. Customers can ask for mediation by email, by postal letter or online by completing the form on www.mediation-eau.fr

[34] Article L1413-1 du Code général des collectivités territoriales

5.3 Finance and budgeting

SPL budget is strictly distinct from municipal and inter-municipal budgets. As described in part 3 of this report, SPL budget is funded directly by the customers water invoice. There is no contribution made by the municipal or inter-municipal budgets.
The water price is revised yearly for each of the four water services according to a price revision formula embedded in the service provision contracts. SPL pays taxes and VAT as a private company. The budget of "Eau du Ponant" is discussed during in the commission of resources where representatives of the four shareholders sit.
Furthermore, a share of the water invoice collected for each of the four water services managed by "Eau du Ponant" is re-allocated to the inter-municipal authority in charge of the water service (figure 9, part 3).
For Chenal du Four and SKK, this share is mainly used to fund water service asset policy and investments.
For BMO and SIDEP, this share is used to fund a few full time positions within the inter-municipal bodies. As these two inter-municipal public authorities have signed concession (B.O.T.) contracts with "Eau du Ponant", a specific investment commission has been created. This allows BMO on the one hand and SIDEP on the other hand to discuss periodically their investment policy with their service provider.

5.4 Risk to integrity and accountability

Before and during the switching process, a specific communication campaign has been implemented to explain the rationale of the SPL creation. An information brochure was sent along with the customer invoice. Public notices were posted and press conferences were held.

A consultative water council has been set up. It gathers 12 local stakeholders such as consumers associations and environmental associations. It ensures public participation as it provides an opportunity for discussions on specific themes such as social tariffs or water supply security, for instance. It gathers once every three months.

A report on the water service quality and price is produced each year. This document gathers information on the organisation, the management and the performance of the service. It is composed of an annual feedback on the SPL activity plus a specific chapter for each of the four water services. It has to be approved through a voting process by shareholders. It provides information to consumers.

The accounting of the SPL is controlled by independent auditors as well as by the revenue Court.

A website (https://www.eauduponant.fr/) and a call centre (☎ 02 29 00 78 78) are also available to answer customers enquiries and to provide generic information.

Furthermore, three censors sit at the BoD. These censors are representatives of the local social housing office, a local environmental non-profit organization ("Eau et rivière de Bretagne") and a local consumer non-profit organization ("CLCV").

5.5 Promoting results and learning

Performance assessment of the four water services is done yearly using mainly the French regulatory set of performance indicators (table 7). However these statutory performance indicators have been complemented with specific indicators designed by the contractual partners.

Table 7. *French regulatory performance indicators for water services*

Code	Indicator's name
P101.1	Microbiological compliance rate of samples on distributed water
P102.1	Physicochemical compliance rate of samples on distributed water
P103.2	Asset knowledge and management and knowledge index of drinking water networks
P104.3	Efficiency of the distribution network
P105.3	Linear index of unaccounted volumes
P106.3	Leakage index
P107.2	Average rate of drinking water network renewal
P108.3	Water resource protection improvement index
P109.0	Sum of debt waivers or payments to a solidarity fund
P151.1	Occurrence rate of unscheduled service interruptions
P152.1	Compliance rate of new customer maximum connection times
P153.2	Length of the local authority's debt extinguishment
P154.0	Rate of unpaid water bills the previous year
P155.1	Complaint rate

(source: arrêté du 2 mai 2007)

As of now, performance assessment is not used by the four local public authorities to reward or penalise their service provider “Eau du Ponant”. It is used as a steering tool to manage efficiently the service rather than as a real target driven incentive scheme. However, in the upcoming years, it is planned to use performance assessment, reporting and monitoring in much more incentive perspective. Furthermore contractual partners have periodic renegotiation meetings (at least once every five years) where they can discuss elements of the contract. Three endorsements have already been signed since 2012.

6 ANNEX

6.1 Generic characteristics of LPEs

	Semi public company (SEM)	Local public enterprise for local development (SPLA)	Local public company (SPL)
Structure	Company with mixed public private capital Creation upon local authorities voting decision	Company with 100% public capital Creation upon local authorities voting decision	
Corporate purpose	Development, housing, industrial or commercial public services or any other general interest activity Several activities possible if they are complementary	Development	Development, housing, industrial or commercial public services or any other general interest activity
Shareholders and partners	Minimum of 7 shareholders with one private shareholder Capital: from 50% to 85% for local public authorities; from 15% to less than 50% to other shareholders Subsidiaries and participation in other companies allowed	At least two local authorities shareholders 100% of capital belong to local public authorities Can only operate for its shareholders Can not create subsidiaries nor take participation in other companies	
Governing bodies	Board of Directors (BoD) or dual structure with Management board and Supervisory board Elected representatives hold more than half of the votes in governing bodies. President and CEO are appointed by the governing boards where elected representatives and private shareholders sit. Specific protection for elected representatives: ▪ local authority bears the civil liability not the elected representative ▪ elected representatives are not considered as municipal service entrepreneurs (no risk of ineligibility) ▪ protection against illegal interest taking Possible remuneration of administrators with tokens	Board of Directors (BoD) or dual structure with Management board and Supervisory board Elected representatives represent their local authority in the BoD. President and CEO are appointed by the governing boards where elected representatives sit. Specific protection for elected representatives: ▪ local authority bears the civil liability not the elected representative ▪ elected representatives are not considered as municipal service entrepreneurs (no risk of ineligibility) ▪ protection against illegal interest taking Possible remuneration of administrators with tokens	
Territory	No territorial limit except for SEM operating in energy sector and in funeral services	Missions limited to the territory of the local public shareholders	
Control by local public	Local public shareholders have a certain control over the company	Local public shareholders have total control.	

authorities	through its representatives in the governing bodies.	
Accounting	Private	Private
Staff	Staff under private law Possibly staff under public law within the framework of secondment	Staff under private law Possibly staff under public law within the framework of secondment
Contractual relationships with local public authorities	Competitive tendering	No competitive tendering
Contractual relationships with private sector	Competitive tendering	Competitive tendering
Corporate tax	Yes	Yes

Source: LPE federation, *Les sociétés publiques locales: un an pares la loi, quel bilan?*, June 2011