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**Explaining Partial Privatization:
The Emergence of Mixed Ownership Water Firms in Italy (1990's-2000's)**

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1. Introduction.

Within the field of study of privatization, quite a deal of attention has been placed on the creation, operation, and performance of mixed ownership forms of service delivery, i.e., of firms partially owned by both public authorities and private investors. The creation of mixed ownership firms has attracted the efforts of scholars that aimed to explain why such forms of service delivery emerge as an alternative to either full public or full private ownership firms. Some studies highlighted that, under certain assumptions (e.g., concerning governance and coordination costs and benefits arising from the internalization of resource provision), mixed ownership firms are selected because they are expected to outperform other forms of service delivery (Eckel and Vining, 1985; Boardman and Vining, 1989; Megginson and Netter, 2001; Chen, 2009). The emergence of mixed ownership firms as a way of providing public services, then, can be explained because policymakers appreciate that, by combining features of public service concern and private entrepreneurial spirit, mixed ownership firms result in better performance in such terms as service quality, cost efficiency, and return to investments. Accordingly, mixed ownership firms may be regarded as the corporate governance system that provides the possibility to attain public service goals while also subjecting the public service provider to the discipline of market pressure.

Yet, this explanation for the emergence of mixed ownership firms is not fully satisfactory. First, there is not any conclusive evidence that mixed ownership firms accomplish superior performance than other ownership forms, while some research has rather shown that the opposite may hold (Boardman and Vining, 1989). Second, the assumption that policymakers make design decisions in such a way as to accomplish superior performance in the delivery of public services may be open to question. A long established research tradition in political science has shown that policymakers make decisions through successive approximations to some desired objectives and that what is desired itself continues to change under reconsideration (Lindblom, 1959). Within the discipline of economics, various studies have highlighted that politicians are primarily interested to exert political pressures on public enterprises rather than in any efficiency or effectiveness concerns (Shleifer and Vishny, 1994;

Vernon and Aharoni, 1981; Donahue, 1989). Finally, if mixed ownership firms result in superior performance and policymakers care about it, then why aren't they more common than we actually observe?

An alternative line of explanation is that the decision to share ownership of public service providers between public authorities and private investors may be related to other factors, including features of the decision-makers, status quo conditions, and particular historical context circumstances. For example, conditions related to the stakes of public authorities in the public service firms, the menu of option choices for designing privatization schemes allowed by the legislation, and the structure of the industry to privatize may play an important role in shaping what public authorities aim to accomplish out of the privatization, what they are allowed to do, and what they are likely to attain. Accordingly, the emergence of mixed ownership firms may be explained by the process dynamics of making and implementing privatization within a changing institutional context. The selection of mixed ownership firms, therefore, may result from the occurrence of particular historical circumstances rather than from any specific traits of this particular form of public service delivery organization that make it generally win the favors of policymakers with respect to alternative arrangements for public service provision.

This paper presents an exploratory case study of the implementation phase of the policy cycle to privatize Italy's (drinking and waste) water sector in the 1990's and 2000's. The case provides the opportunity to investigate the implementation of a privatization policy that partially resulted in mixed ownership forms of public service delivery. Moving from status quo conditions that included diffuse public ownership of water firms and high fragmentation of the water industry, the implementation of the privatization of the water sector in Italy led to massive organizational restructuring of incumbent water firms and profound reconfiguration of ownership structures. At the end of the implementation episode, about two thirds of Italy's water sector was retained under full public ownership, about one fourth of water service providers were partially opened to private operators (especially, major French water multinationals) and investors (especially, in water firms whose shares had been floated in the stock exchange), while in a few cases only were water franchises awarded to fully privately owned companies.

The rest of the paper is organized as follows. Next section will briefly review the scholarly literature about the implementation of “pro-market” regulatory reforms, conceived

as a category of public policies that aim to radically reconfigure the regulation of entire sectors of the economy by exposing incumbent public sector operators to some kind of competitive pressures. Section three will present the research design of this study. The fourth section will narrate the implementation of the privatization of the water sector in Italy during the 1990's and 2000's. Section five will analyze and discuss the case and the research findings. Finally, the last section will draw the conclusions of this study.

2. The implementation of privatization policies.

Privatization is a kind of “transformative” regulatory reform that aims to radically reconfigure the regulation of entire sectors of the economy by broadly replacing a regime based on public ownership with one where economic activity is open to private operators and investors (Howlett and Ramesh, 1993; Bös, 1991; Vickers and Yarrow, 1988). What exactly privatization means and how it is carried out, however, does vary considerably across countries, epochs, and doctrinal orientations (Clifton et al., 2006; Savas, 2000, 1987; Feigenbaum et al., 1998; Wallin, 1997; Starr, 1988; Lundqvist, 1988; Kolderie, 1986). Generally, privatization entails that public authorities give up ownership and control of public service providers, that are opened up to the participation, in various forms, of private operators and investors. For example, privatization may take the form of making business companies carry out specific contracted-out tasks, or of awarding concessions to private operators for managing the provision of public service, or of letting companies or private investors acquire ownership and control of key assets (e.g., infrastructure) (Gómez Ibáñez, 2003).

Among the various forms of involvement of private operators and investors in public service provision, the creation of mixed ownership firms has attracted some attention especially from the side of scholars working within the disciplinary fields of both economics and political science. Some studies have been done, for example, on the political rationales and conditions that underpin mixed ownership firms (Heald, 1988), on the emergence and performance of mixed ownership firms in transition economies (Meyer, 2002; Jelic et al., 2003), and on the performance effect of mixed ownership firms (Boardman and Vining, 1989; Backx et al., 2002; Oum et al., 2006). The fundamental question as to why mixed ownership firms emerge while other options for organizing public service provision are available but discarded, however, has not been fully and satisfactorily researched so far.

Privatization is broadly conceived as a component part of policy reform efforts intended to improve the performance of selected sectors of the economy. In this respect, the implementation of privatization policies falls within a broader category of political processes related to so-called “pro-market” regulatory reforms, that is, transformative regulatory reforms that aim to radically reconfigure the regulation of entire sectors of the economy by exposing incumbent operators to competitive pressures, including opening up the possibility to acquire ownership and control of key assets (e.g., infrastructure) to companies or private investors. Of course, it is questionable whether the privatization of public sector providers into mixed ownership firms contributes to increasing competitive pressures, when the effect of privatization on the structure of the reformed sector is the one to replace a public monopoly with a mixed ownership one. For one thing, “pro-market” regulatory reforms should also contain policy initiatives that liberalize access to the market and provide measures against collusive agreements and the abuse of dominant positions. Privatization that results in the formation of mixed ownership firms, then, may not necessarily fulfill the policy objective of opening up the regulated sector of the economy to competition (or to more competition). Such privatization outcome may rather subvert “pro-market” reform efforts by relegating private operators and investors to an “ancillary role” as minority shareholders of privatized firms, rather than making them compete over the provision of public services.

Among the studies that focused on the making and implementation of “pro-market” regulatory reforms, the edited book of Landy et al.'s (2007), *Creating Competitive Markets: The Politics of Regulatory Reform*, is relevant here. Landy et al.'s (2007) edited book aimed to examine “what is now a thirty-year history of policy innovation dominated by a rhetoric of freeing up competitive forces and replacing flaccid and cumbersome government intervention with the flexibility and creativity that markets are supposed to stimulate” (Landy et al., 2007: 2). Drawing on various case studies, *Creating Competitive Markets* proposed generalizing arguments about the political economy of regulatory reform policy cycles. The cases related to regulatory reform policy episodes in such sectors as banking, social policy, freight railroad, electricity, pensions, education, and airlines, situated in the country cases of the US, the UK, and Canada. On the basis of the explanatory arguments about the path and outcome of the cases, the authors argued that “old-fashioned group-based politics never died away. Indeed, political interference of that nature – and policymakers' failure to anticipate it – is probably the strongest single reason that policy reform failed to promote competition” (Landy et al.,

2007: 9). Durable reforms, instead, were those which “do not merely destroy an existing policy subsystem, they generate a self-reinforcing process in which the identities and organizational affiliations of relevant interests change and key social actors adapt to the new regime” (Landy et al., 2007: 16).

The book resulted, in general, in the identification of factors associated with policy sustainability. Part of the book, however, also highlighted sources of resistance against the making of competitive markets, including forms of “governmental protectionism” when public service providers oppose the opening up of private sector participation to the delivery of public services. For example, Vogel (2007) noticed that often the strongest obstructionism to open up regulated industry to competition originates from the joint interests of businesses and governments. Hess (2007) showed that resistance to open up an industry to market forces may originate from the government, if the reform is intended to replace public provision of services with private ones. In the conclusions of the book, Bardach (2007) commented that the dynamics of governmental protectionism make take various forms, including buffering public sector providers against competitive losses and granting limited access to the industry to selected “entrepreneurial personalities”.

One limitation of Landy et al.'s (2007) study was their lack of attention to the role played by sub-national governments in the implementation of privatization policies. Features related to such role are remarkably different from those attached to the executive bureaucracy and to governmental agencies. They include, for example, such prerogatives as the exercise of veto powers provided by the constitution and/or relevant legislation, the right to appeal to supra-national, constitutional, and administrative courts, and exclusive competences on the regulation of local public services. More generally, sub-national governments play an active role in the making and implementation of public policies so that policy outcomes become especially sensitive to their “partisan mutual adjustment” (understood as “fragmented or greatly decentralized political decision making in which the various somewhat autonomous participants mutually affect one another”; Lindblom, 1979: 522). When privatization policies are made and implemented in the context of multi-level governance (Marks, 1993; Rhodes, 1996, 1997; Jordan, 2001), then, these features of sub-national governments' role have important effects on the political economy of privatization, including the possibility that “pro-market” regulatory reforms passed at the central government level are fundamentally diluted, if not even subverted, at the local level.

3. Research Method.

This paper aims to address the question of why, within the implementation part of the privatization policy cycle, mixed ownership firms emerge for the provision of public services. This question is tackled through an explorative case study of the implementation episode of the policy cycle to privatize Italy's (drinking and waste) water sector in the 1990's and 2000s. The selection of the case is justified by the distinguishing conditions of the case country context – particularly, Italy's multi-layered structure of governance. The selection of the case reflects, in other words, a variation-centered strategy for researching the process of privatizing large-scale infrastructure-based public services. The selection of the case study method (Ragin and Becker, 1992; Stake, 1995; Yin, 2003), additionally, is generally regarded as appropriate for filling the kind of knowledge gap which is addressed by this study, i.e., broadly conceived, understanding “how” the process of privatizing the delivery of public services unfolds.

Data were collected from primary, secondary, and tertiary sources. Primary sources included parliamentary minutes, official reports and other documents issued by the national water regulatory agency (*Comitato di Vigilanza per l'Uso delle Risorse Idriche* or Supervising Committee on the Use of Water Resources), and interviews. Secondary sources included reports issued by the water research centers Proaqua, Astrid, and Utilitatis, proceedings of the conferences “H2Obiettivo 2000” organized by the water firms' association Federgasacqua (renamed Federutility from 2005), and articles from the press *Il Sole 24 Ore* and *La Repubblica*. Tertiary sources included various scholarly works done on the water reform in Italy, such as Anwandter and Rubino (2006a, 2006b), Asquer (2011, 2010a), Bigatti et al., (1997), Carrozza (2008), Citroni and Lippi (2006), Citroni et al. (2007), Danesi et al. (2008), Fraquelli and Moiso (2004), Gilardoni and Marangoni (2004), Guffanti and Merelli (1997), Lippi et al. (2008), Massarutto (2005, 1993), Muraro (2003), and Riccaboni and Grossi (2000).

The analysis of the case was conducted by following a processual approach. A processual approach to the study of social phenomena builds on a long established tradition in the disciplines of sociology, organizational sociology, and political science (Pettigrew, 1997; Bennett and George, 1997; George and Bennett, 2005; Kingdon, 1984). Generally, works done along this approach aim to gain a causal understanding of social processes conceived as

interpretations based on supposed “concatenations of social mechanisms” (Gambetta, 1998; Merton, 1968; Hedström and Swedberg, 1998; McAdam et al., 2001; Mahoney, 2003) and interactions with context factors. Explanatory arguments developed from a processual perspective tend to highlight the role played by time, path dependency, and changing context conditions among the key explanatory resources (Mahoney, 2000; Pierson, 2000, 2004; Abbott, 2001). By following a processualist approach, theoretical arguments about the emergence of mixed ownership forms of service delivery are especially attentive to how policy content, policy process features, and historical context conditions affect the decision to establish joint public-private forms of public service provision.

This study follows, in particular, the so-called institutional processualist approach to the study of social phenomena. Originally developed within a research program about public management policy-making, institutional processualism has been widely applied and discussed in various scholarly works so far (Asquer, 2010b; Barzelay and Gallego, 2010a, 2010b, 2006; Corbett, 2010; Gallego and Barzelay, 2010; Mele, 2010; Barzelay, 2003; Barzelay and Fuechtner, 2003; Cejudo, 2003; Gaetani, 2003; Gallego, 2003; Malee, 2003; Moynihan, 2003). Explicitly drawing from Kingdon's work (1984), this analytical approach aims to attain a causal reconstruction (Mayntz, 2004) of episodes of public policy cycles by placing attention to the flows of situated interaction, to the interplay between belief and action as experience unfolds, and to the historical context (especially, the way causation arises from combinations of conditions, under the principle of “multiple conjunctural causation” as formulated in Ragin, 1989). Based on this approach, the result of the analysis takes the form of “historically-grounded analytic generalisations” (Barzelay and Gallego, 2006) about the process dynamics of the emergence of mixed ownership firms within the privatization of public services.

4. The privatization of the water sector in Italy (1990's-2000's).

4.1. The award of the first water franchise (1994-1999).

In late 1993, the Parliament of Italy passed a legislation containing the reform of the national water sector (Act 36/1994). The reform was mainly intended to improve water sector performance (in such terms as cost efficiency and service quality) by consolidating a quite fragmented industry (that counted about 23,500 operators in the country), eliciting competitive pressures for the award of water franchises, and attracting private operators and

investors. The water reform provided that the regions passed legislations that provided the definition of the boundaries of new water administrative jurisdictions (called *Ambiti Territoriali Ottimali* or Optimal Territorial Areas, henceforth OTAs) and the specification of various details of the new regulatory system. Additionally, local governments were required to establish local regulatory authorities (*Autorità d'Ambito* or OTA Authorities) that would draft water infrastructure development plans and award water franchises to either mixed ownership firms or to business companies selected through tender offer competitions.

Initial conditions within this episode included quite diverse kinds of water firms operating in the country. In the northern regions, water services were generally provided by local government departments within the administrative jurisdictions of the municipalities only. Especially in the central regions, local governments had often decentralized water services to local government-owned organizations (*municipalizzate*) or local government-owned consortia, according to a local service provision scheme that dated back to the early twentieth century (Act 103/1903). In the southern regions, instead, most of water industry segments (water collection, storage, and transport) were managed by central-government or regional-government owned water firms, while downstream activities (distribution, sewage, and wastewater treatment) were carried out by municipal departments. Relatedly, the water sector was especially fragmented in the northern and central regions, while in the southern part of the country water activities were partially performed by relatively large water firms.

The first instance of award of water franchise took place in the OTA named Alto Valdarno in Tuscany. On 3rd October 1998, local governments of Alto Valdarno published a call for tender offers for selecting the private partners of the water firm that they intended to form by merging their incumbent water operators. The tender offer competition led to the selection of a syndicate led by Suez-Lyonnaise des Eaux (which a share of 51%), which included the water firm owned by Genoa AMGA (35%), a local artisans association named Iride (10%), and the banks Banca Popolare dell'Etruria e del Lazio and Monte dei Paschi di Siena (2% each). On 21st May 1999, the OTA “Alto Valdarno” Authority awarded a 25-year water franchise to the mixed public-private ownership firm called Nuove Acque, owned by the local government (54%) and by the Suez-led consortium (46%).

The award of the water franchise in the OTA “Alto Valdarno” originated from earlier negotiations that local governments of that area had already conducted about the centralization of water services. In 1990, the gas firm Coingas, owned by the municipality of

Arezzo, had proposed to the mayor to let the firm develop into a multi-utility company operating in the gas and water industries (Lobina, 2005). Having gained the support of the centre-left parties which backed the city executive, in October 1992 Coingas submitted a plan which provided that the firm would be reincorporated as a business company and would be assigned the water franchise of Arezzo (which directly managed water services at that time) and of 24 other neighboring local governments. The Coingas plan was approved, first, by the Arezzo city council in December 1992 and, later, by all the other 24 local governments by October 1993.

In 1995, the support for the Coingas plan dissolved after the formation of a new centre-left coalition executive in Arezzo, chaired by the mayor Paolo Ricci. Following the political orientation of the time of the regional branch of the leftist *Democratici di Sinistra* party (DS), Ricci favored the formation of mixed public-private ownership companies for the management of local public services. The Coingas plan was overruled on the basis of the lack of transparency which could arise from cross-subsidization between gas and water activities, and of the firm's modest experience in managing water services. In February 1996, the city council of Arezzo approved Ricci's proposal to establish a local government majority-owned water company, that would be assigned the provision of local water services before opening up ownership to private operators and investors. After some legal issues were solved, and region Tuscany completed the transposition of the water reform, in July 1997 the OTA Authority "Alto Valdarno" decided to award the water franchise to a local government majority-owned company and that a minority share of this company would be tendered out to private operators.

Apart from the experience of Alto Valdarno, in the rest of the country the privatization of water services progressed quite slowly. Especially in the northern and southern regions, local governments were generally reluctant to privatize water services, because control of water service provision allowed local government politicians to exert influence on water-related jobs and public contracts. Within the context of local governments' political economy, this influence on the water industry helped local politicians in executive positions to cultivate supportive constituencies. Especially in the central regions, instead, the decentralization of water services to *municipalizzate* had resulted in the formation of a network of water policy professionals and experts that played a major role in advocating and diffusing the idea that mixed ownership firms could result in more efficiency and better service quality in the

provision of public services. Also the executives of *municipalizzate* came to share the view that transforming public water firms into mixed-ownership ones could result in improved performance, especially in conjunction with the merger of incumbent water firms into larger water service providers.

4.2. Awarding water franchises to mixed ownership firms (2001-2003).

In December 2001 the Parliament passed a reform of local public services (Act 448/2001), that provided the general rule that local public services should be contracted out to private operators through tender offer competitions. Special provisions, however, allowed to postpone tender offer competitions in the water sector for a period up to 9 years when water services were provided by firms that operated in local governments with up to 5,000 inhabitants only. Other provisions, moreover, allowed to postpone tender offer competitions in the water sector if water firms merged together to form larger operators. According to this scheme, within 18 months after the enactment of the reform (i.e., by 30th June 2003) the OTA authorities could directly award 5-year long water franchises to business companies fully owned by the local governments of the OTA, provided that local governments would later open up ownership of the water firm to private operators or investors within 2 years after receiving the franchise. If further particular conditions were met, the duration of the water franchises could be extended up to 10 years (Petretto, 2001).

As soon as the Parliament passed the 2001 local public services reform, some local governments urged the OTA authorities to speed up the procedure for awarding water franchises before the 2001 reform came into force. Within a few weeks in December 2001, four OTA authorities based in Tuscany awarded water franchises to local government-owned water firms, whose minority shares would be later tendered out to private operators and investors. In this way, those local governments could preserve the position of their merged water firms in the local water industries while bypassing the tender offer competition rule for awarding the water franchises and the other strict requirements set by the new legislation.

After the 2001 local public services reform came into force, several local governments sensed the opportunity to protect the incumbent position of their water firms in the local water industries by exploiting the reform provisions that allowed to avoid tender offer competitions. Accordingly, these local governments made their water firms quickly restructure in order to match the requirements set by the legislation, then made the OTA

authorities award the water franchises to the local government-owned merged firms, and then made the water firms partially open up their ownership to private operators or investors. By following this privatization scheme, local governments also realized that, far from completely giving up their influence on the water industry, they could anyway retain some sway by appointing the company management and keeping influencing organizational processes. An illustrative description of this view was provided, for example, by the mayor of Grosseto (a municipality located in Tuscany) and chairman on the Local Public Services Committee of ANCI (the national association of local governments), Alessandro Antichi, who, during a conference of Federgasacqua held in Trieste on 24-26 September 2003, said: “We know well, we mayors, that a tight control on third entities, like the companies which provide local public services, is actually more effective than the one we have on our own managers, that we find in a local authority because they won a public selection, they chair a division which is only respondent to them, and, as a matter of fact, for us it is much easier to manage through the companies than through the managers [of the local governments]”.

4.3. Awarding water franchises to full public ownership firms (2003-2009).

In September 2003, the central government passed another reform of local public services (Legislative Decree no. 269, later partially amended by Act 350/2003), that restated the general rule that local public services should be awarded through tender offer competitions. Additionally, the reform provided that all franchises which had been awarded without following this rule would automatically expire on 31st December 2006, apart from those that had been awarded before 1st October 2003 to firms whose shares had already been floated in the stock exchange. The reform also allowed, however, that franchises of local public services could be legitimately awarded either to mixed public-private firms, where the private partners were selected through tender offer competitions, or to firms fully owned by local governments, provided that these firms deliver most of their services to the same local governments, and that local governments exercise on these firms a control as tight as the one exerted on their own divisions (so-called “in house” arrangement).

After the 2003 reform came into force, several OTA authorities started awarding water franchises to “in house” firms, that, as a form of water service provision, secured local governments' close control on local water industries. The provision concerning “in house” firms (whose legitimacy as a way of managing local public services originated from a

decision of the European Court of Justice taken in 1999) had been introduced in the 2003 local public services reform as a way of providing legitimacy to franchises *already* awarded to fully local government-owned water firms. From December 2003 onwards, instead, the OTA authorities started to apply the “in house” provision to awarding *new* water franchises to fully local government-owned firms. The “in house” provision, in other terms, was exploited as a way to bypass the tender offer competition rule or the requirement to partially open the ownership of the water firms to private operators or investors.

On the whole, the implementation of the water reform led, by the late 2000's, to the set up of new regulatory institutions in most of the country and to some degree of reorganization of the water industry. A survey of the water sector in 2009 showed (Table 1) that water franchises had been awarded in about two thirds of the OTAs (67 out of 92), and that most of them had been granted to “in house” firms (i.e., without any tender offer competition). About one fourth of water franchises, however, had been awarded to water firms whose ownership had been opened up to private operators (in the form of minority share of mixed ownership firms) or investors (in the form of share ownership of companies floated in the stock exchange), especially in those central regions of the country where water firms *municipalizzate* had been operating in the past.

< insert Table 1 about here >

5. Explaining the emergence of mixed ownership firms in the water sector in Italy.

The path and outcome of the implementation of the privatization part of Italy's water reform presents various analytically relevant traits. The privatization episode included three sequential trajectories. During the first trajectory, which lasted from 1994 to 2001, implementation was hesitant and largely ineffectual: by 2001, it resulted in the award of one water franchise only, in the OTA “Alto Valdarno” in Tuscany. After December 2001, the implementation process swiftly accelerated, and resulted in the award of various water franchises to mixed-ownership firms especially in the central regions of the country. After September 2003, finally, an increasing number of water franchises were awarded, especially to “in house” firms. These stylized facts suggest the following questions: Why was the privatization process so obstructed during the first period while it accelerated from December 2001 onwards? Why was the privatization of water services in Alto Valdarno faster than

elsewhere in the country? Why were mixed ownership firms especially established in those water districts where municipal water firms operated?

In order to tackle these questions, first we discuss how the decision to privatize water service provision was made. An important condition, in this respect, is the governance system of the OTA authorities. The OTA authorities were established as organizations owned and controlled by local governments, rather than as independent agencies. Local governments, in other words, retained considerable influence on the decisions made by the OTA authorities, especially those related to the privatization of water service provision. These features of the governance system of the OTA authorities resulted from the decisions that local governments made in the establishment of the OTA authorities themselves. These decisions, in turn, were especially affected by features of the water reform statute (which did not provide that the OTA authorities ought to be established as independent regulators of local water industries) and of general legislation of local public services (which did not provide that local governments should give up their regulatory functions), in conjunction with local governments' interest to retain influence on the local water industries.

Another important condition within the privatization process relates to the characteristics of the water sector, especially local governments' stakes in the local water industries. Local governments' influence on the local water industries played an important role in local government politics, because politicians could acquire support of voters' clienteles by granting favors in the form of water-related jobs and public contracts. Local governments, then, were generally inclined to resist privatization schemes which implied any significant loss of control of water management functions, if not compensated by any commensurate benefit. The governance system of the OTA authorities allowed them to affect the selection of privatization schemes, provided that only the majority of local governments could make the OTA authorities adopt binding decisions. Local governments' stakes in local water industries, in this respect, were rather homogeneous within any given OTA, hence conflicts between local governments concerning the adoption of privatization schemes were unlikely to arise.

Why, then, did local governments not make the OTA authorities award the water franchises in the first part of the episode? In order to answer this question, we take into account the causal role played by design features of the water reform and features of the setting in which the implementation of the privatization process took place. Design features

of the water reform included the provisions that each OTA authority would award water franchises to one only water company (apart from exceptional circumstances where water franchises could be awarded to more than one water company in the same OTA if incumbent water firms satisfied criteria of economic self-sufficiency). In order to be eligible to receive water franchises, then, water firms should achieve at least the size required to service the OTA users' basins.

Features of the setting included sector characteristics and territorial organization of water service provision. Sector characteristics refer to the diffused local government ownership of the water industry. Given that the design features of the water reform required that water franchises should be awarded to mixed ownership firms or to business companies selected through tender offer competitions, then incumbent local government-owned firms did not match the requirements to be eligible for managing water service provision. Local governments, however, were generally inclined to resist sharing ownership of water firms with private partners, because this would significantly limit the discretion that they had traditionally exercised on the management of water firms. Typically, local governments were also very reluctant to contract out water service provision, because this would have spoiled them of their sway on water business.

Features of the territorial organization of water service provision included the fragmentation of the water industry into relatively small service areas. In general, water service areas corresponded to municipal jurisdictions or administrative territories of local governments' consortia, especially in the central and northern regions of the country. In the southern regions, instead, local governments especially retained control of downstream water services (water distribution, sewage, and wastewater treatment). This industry structure made local governments enjoy influence on water service provision operated in the respective municipal territories. Centralization of water management function into one only water firm within each OTA, instead, would significantly diminish local governments' influence, as they would share control of the merged firms with other municipalities.

Taking these conditions into account, local governments were not inclined to consider the privatization of water service provision in their agendas. Design features of the water reform implied that local governments should consolidate their incumbent water firms into larger providers and give up part (if not all) of their ownership. Given local governments' traditional role in the supply of local public services, the costs of pursuing privatization of

water service provision were apparent, in the form of loss of influence on water-related jobs and public contracts. No apparent benefits, instead, did local governments expect from the decision to privatize water service provision according to any of the schemes provided by the water reform.

Why, then, was privatization of water services accomplished in Alto Valdarno? Particular features of the setting of Alto Valdarno contribute accounting for the deviation of the trajectory of privatization of water services in this area from the general pattern in the country. Well before the enactment of the water reform in 1994, in this part of Tuscany the idea to consolidate and partially privatize incumbent municipal water service providers had gained serious consideration among local policy-makers. Negotiations conducted for the privatization of Coingas and other local utility firms, in particular, had contributed to the formation of a water policy community that had come to agree on the terms of the merger between incumbent water firms and the sale of minority shareholding to private operators and investors. Additionally, political actors of the dominant DS party had come to accept the ideological position that mixed-ownership firms combined the benefits of both public sector organizations (that were supposed to pursue public service goals) and privately owned companies (that were expected to enhance cost-efficiency and return to investments). Moreover, executives of municipal water firms could anticipate that larger mixed-ownership water firms could offer them better career and income prospects than incumbent water service providers.

The agreement between local governments of Alto Valdarno and between local government politicians and parts of the local water policy network (including water professionals, experts, and executives of municipal water firms) played an important causal role in the privatization of local water service providers. Once the OTA Alto Valdarno Authority was established, local governments required little further negotiation to come to agree to merge their water firms and make the OTA authority select the private partner. Indeed, the privatization of water service provision seems to have never been removed from local governments' agendas – at least, from the one of the leading municipality in the area, Arezzo. Additionally, the privatization scheme which had been considered for the centralization of water service provision – namely, the award of water franchise to a mixed ownership firm – corresponded to one of those allowed by the water reform design. These conditions, then, facilitated the privatization of water service provision in Alto Valdarno and

account for the deviation of this local trajectory of the privatization part of the water reform from the general pattern in the rest of the country.

Another analytic issue to address is why, after 2011, the privatization of water services accelerated, and resulted in the award of various water franchises to mixed-ownership firms especially in the central regions of the country. The 2001 reform of local public services brought about important changes of the design features of the water reform, especially concerning the privatization schemes allowed to OTA authorities. While the original water reform statute provided that water franchises should be awarded to either mixed ownership firms or to business companies selected through tender offer competitions, the provisions introduced by the 2001 local public services reform mandated to tender out water service provision, although it also allowed, provided that certain conditions were met, to bypass the tendering out rule by awarding the water franchises to mixed ownership firms within a set deadline. Local governments, then, faced the alternative between surrendering ownership of water firms by tendering out water franchises to business companies or opening up partial ownership of water firms to private operators and investors. The deadline set for selecting the option to make the OTA authorities award the water franchises to mixed ownership firms could contribute to raise the water privatization issue in local governments' agendas. Even if local governments generally preferred to retain the status quo, the requirement to tender out water service provision after the 30th June 2003 deadline made them seriously consider the merits of privatizing water services according to the mixed ownership scheme.

The social mechanism of attribution of opportunities and threats (McAdam et al., 2001) contributes explaining why local governments accelerated the privatization of water service provision after the 2001 legislation. Attribution of opportunities and threats is “an activating mechanism responsible in part for the mobilization of previously inert population” (McAdam et al., 2001: 45). At the core of the mechanism is an interpretation of the context which frames conditions as originating potentially beneficial or harmful outcomes. The 2001 reform, accordingly, could be perceived by local governments as a source of both opportunities and threats: on the one hand, the mandate to tender out water service provision evidently threatened local governments to lose their influence on local water industries, while, on the other one, the possibility to award water franchises to mixed ownership firms offered the opportunity to retain some ownership of the privatized water firms. The deadline set on 30th June 2003, moreover, could play the role of focusing event (Kingdon, 1984) which

catalyzed local governments' efforts to speed up the privatization of water service provision.

Particular conditions, especially related to features of local context, may also account for why the privatization to mixed ownership firms after 2001 did not take place all over the country. The fragmentation of local water industries into several small-scale water firms and the heterogeneity of ownership forms implied that local governments had to engage in relatively long periods for negotiating the terms of the privatization schemes. In the parts of the country where water services had been traditionally provided by municipal firms, local water policy networks could facilitate the formation of agreements about the merits of mixed ownership privatization. A mechanism of diffusion of ideas may contribute explaining how, on the basis of evidence provided by the forerunner case of Alto Valdarno, water policy networks oriented water professionals, experts, and municipal executives towards accepting mixed ownership as a viable and beneficial policy option. Instrumental rationality, moreover, may contribute explaining why municipal executives could be especially favorable to the privatization scheme, provided that the formation of larger and privatized water firms also related to better career and income prospects. In contrast, in those parts of the country where water service had been long provided by municipal departments, organizational conditions were not favorable to the raise of mixed ownership privatization into local governments' agendas. Such organizational conditions, in particular, lacked features such as integration with other water policy networks and executive positions that may account for the absence of consideration and efforts to implement the mixed ownership privatization scheme. As an effect of this variety of conditions, Italy was not uniform in the readiness of local governments towards the privatization of water services after the 2001 legislation. Only a part of the country, therefore, came to to privatize water service provisions by mid-2003.

Finally, another analytically relevant issue is the one related to why, from 2003 onwards, water franchises were generally awarded to fully local government-owned firms rather than mixed ownership ones. An important event which contributed to this part of the privatization process was the reform policy cycle which resulted in the 2003 reform of local public services, that granted legitimacy to the award of water service provisions to “in house” firms, although under exceptional circumstances. This change of conditions, in conjunction with steady conditions of sector characteristics and interests of local governments recalled above, was an important causal factor in enhancing local governments' efforts to privatize water service provision. In part, these conditions stimulated local governments to collaborate

to merge their water firms and reincorporate them as business companies. In part, they made local governments inclined to select the “in house” scheme for the award of water franchises.

The award of water franchises to “in house” firms clearly offered local governments the benefit of retaining shared influence of local water industries. Rather than giving up ownership of water firms, either completely (by tendering out water service provision) or partially (by opening ownership to private operators or investors), local governments could have the OTA authorities assign water franchises to water firms formed with neighboring municipalities within the OTAs. According to this scheme, local governments would not enjoy full control of water firms, nevertheless they would exercise influence on larger organizations together with other municipalities. Again, the social mechanism of attribution of opportunities and threats (McAdam et al., 2001) contributes explaining why local governments made the OTA authorities assign water franchises to “in house” firms after the 2003 legislation. Especially for those local governments that used to provide water services through municipal departments, the 2003 reform was perceived as a source of opportunity to retain greater influence on local water industries than other schemes allowed to. Such condition, therefore, allowed local governments to bypass the general requirement to open up ownership of water service firms to private operators and investors.

6. Conclusions.

As discussed in the literature review, studies on the privatization of public services placed relatively little attention on the emergence of mixed ownership forms of service delivery. Additionally, within the more general literature on the political economy of “pro-market” regulatory reforms there has been a lack of attention on the role played by sub-national governments in the implementation of privatization policies. Some works, like the edited book of Landy et al.'s (2007) *Creating Competitive Markets: The Politics of Regulatory Reform*, provide generalizing arguments about causal sources of outcomes of “pro-market” regulatory reforms, whether successful or not. Generally, however, we miss an explanation for why mixed ownership forms of public service delivery arise, especially when “governmental protectionism” tends to hamper the efforts to open up ownership of public service providers to private operators and investors.

The present case study suggests some ways to improve the existing theoretical arguments about the political economy of privatization policy reforms. In broad terms, the

analysis suggests that particular historical context circumstances play an important role in the way public service provision is opened to participation of private operators and investors. In the privatization of the water reform in Italy, an important causal role for explaining the acceleration of the privatization process is played by the combination of conditions which include (a) changes of substantive rules for conducting privatization (specifically contained in the 2001 local public services reform), (b) features of stakes of local governments in the reformed sector, and (c) features of the institutional arrangement of the reformed sector (specifically related to status quo conditions such as diffused public sector ownership of public service providers) and (d) of the territorial organization of the water services (especially related to the fragmentation of the water industry). These conditions also contribute explaining why the privatization process may follow different trajectories within the same country, provided some variation of local conditions that include (e) the kind of organizational form that provides water services (especially whether municipal firms provide water services rather than municipal departments), (f) the presence of past negotiated agreements about centralization and privatization of water services, at least in some part of the country, and (g) diffusion of ideas about the merits of mixed ownership firms channeled through water policy networks. The explanation for the emergence of mixed ownership firms in the water sector, then, is especially sensitive to the combination of particular conditions that originate in the temporal and institutional context.

Among the conditions identified in the present case study, those related to features of the multi-layered structure of the governance system and to diffused public provision of services are particularly important to explain how the emergence of mixed ownership firms took place. Within the multi-level governance context, local public authorities engage in “partisan mutual adjustments” between themselves and across levels of the governance system. Such adjustments include, in particular, those related to the negotiations between local governments that took place for the merging of local government-owned water firms, for the award of the water franchises, and for the design and implementation of partial privatization schemes. They also include those related to the negotiations between local governments that took place for making water franchises awarded to “in house” firms in accordance to the terms of the 2003 local public services reform. Also the conditions related to diffused public sector ownership of public service providers come to play in explaining how the privatization process takes place. In the privatization of the water services, local

governments' stakes in the provision of water services in the form of *municipalizzate* water firms affected, together with other causal conditions recalled in the explanatory argument, the award of water franchises to mixed ownership firms. In sum, this case study highlights that the embeddedness of the privatization process within the multi-layered governance system and status quo conditions including diffused public ownership of public service provision are important conditions for explaining the partial emergence of mixed ownership firms.

Finally, at least one limitation of this study should be duly acknowledged. If we consider that local governments had deep-seated stakes in local water industries, then we may find simplistic that they could change their attitude towards privatizing water provision in relation to exogenous changes of context conditions, namely the 2001 and 2003 local public services reforms. An alternative line of explanatory argument may be that local governments became inclined to privatize water provision because they took an active part within the process of Europeanization of public services which were traditionally owned and managed by public authorities. Following this perspective, the behavior of local governments could be also explained, in part, by taking into account their efforts to both “upload” policy issues and solutions at the EU level, and to “cherry-pick” and “download” selected policy issues and solutions from the EU-level to the domestic policy process. We certainly subscribe to the view that the case of the privatization of the water sector in Italy could be reframed within the conceptual scheme of Europeanization research. The lack of consideration of the Europeanization process in this study is merely due to different research interests than contributing to Europeanization literature's research agenda, rather than to any intent to oversimplify the analysis of the policy reform episode under consideration.

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| Regions | No. OTAs which have awarded concessions (No. OTAs established) | “in house” firms | Mixed public-private ownership firms | Firms traded in stock exchange or owned by financial institution | Safeguarded public sector firms | Private firms selected through tender offer competition | Private firms in negotiated transitory regime | Total |
|-------------------------------|--|------------------|--------------------------------------|--|---------------------------------|---|---|------------|
| Piemonte | 6 (6) | 17 | 3 | 4 | | | | 24 |
| Valle d'Aosta | 0 (1) | | | | | | | |
| Lombardy | 6 (12) | 8 | 1 | | 2 | | | 11 |
| Veneto | 7 (8) | 12 | | 1 | | | | 13 |
| Friuli Venezia Giulia | 1 (4) | 1 | | | | | | 1 |
| Liguria | 2 (4) | 4 | | 1 | | | | 5 |
| Total northern regions | 22 (35) | 42 (78%) | 4 (7%) | 6 (11%) | 2 (4%) | 0 (0%) | 0 (0%) | 54 |
| Emilia Romagna | 9 (9) | 1 | | 6 | 3 | | | 10 |
| Tuscany | 6 (6) | 1 | 5 | | | | | 6 |
| Umbria | 3 (3) | 1 | 2 | | | | | 3 |
| Marche | 4 (5) | 3 | | | 3 | | | 6 |
| Lazio | 4 (5) | 1 | 1 | 1 | | 1 | | 4 |
| Abruzzo | 6 (6) | 4 | | | 2 | | | 6 |
| Molise | 0 (1) | | | | | | | 0 |
| Total central regions | 32 (35) | 12 (33%) | 8 (22%) | 7 (19%) | 8 (22%) | 1 (3%) | 0 (0%) | 36 |
| Campania | 2 (4) | 1 | 1 | | | | | 2 |
| Puglia | 1 (1) | | | | 1 | | | 1 |
| Basilicata | 1 (1) | 1 | | | | | | 1 |
| Calabria | 3 (5) | 2 | | | | | 1 | 3 |
| Sicily | 5 (9) | | 1 | | | 4 | | 5 |
| Sardinia | 1 (1) | 1 | | | | | | 1 |
| Total southern regions | 13 (21) | 5 (38%) | 2 (15%) | 0 | 1 (8%) | 4 (31%) | 1 (8%) | 13 |
| Interregional OTAs | 0 (1) | | | | | | | |
| Total | 67 (92) | 58 | 14 | 13 | 11 | 5 | 1 | 102 |

Table 1. Distribution of the types of firms which were awarded water concessions, per region, 2009 (Source: Supervising Authority on Water Resources and Urban Waste, 2008; web sites of the OTAs, last access in December 2009).