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Public–private partnership and corporate public sector organizations: Alternative ways to increase social performance in the Portuguese water sector?

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ABSTRACT

Using survey data from the Portuguese Water Sector Regulator, the following study explores the relationship between social performance and the sector providing water service. In that sense, lower user prices and higher quality goods and services are linked to superior social performance. Our empirical analysis demonstrates that user prices have a stronger relationship with *organizational costs* than with *property* or the adopted *management model* in the delivery of public services. In contrast, the quality of the goods and services possesses a stronger connection with *property* rather than with *organizational costs* or *management models*. Such results contradict the New Public Management ideas; mainly that private sector participation through public–private partnerships in the delivery of public services will inevitably lead to a better use of scarce resources, and consequentially to lower user prices and higher quality goods and services. In the Portuguese case, policy implications are that public–private partnerships ceased until lower organizational costs, higher quality services and lower user prices are secured.

1. Introduction

To what extent does a sector providing a given service shape social performance? Our research question arises from the recent discussion trends regarding the ways in which public services can be delivered. In the past decades, private sector participation (PSP) in public services delivery became an important part of public administration reform worldwide (Pollitt and Bouckaert, 2004). PSP involves the transfer of ownership or management of public sector organizations to private firms through the sale of public enterprises, the outsourcing of services to the private sector, or public–private partnerships (PPP) (Savas, 2000). PPPs are arrangements which require the co-operation between public and private parties, which have a common goal in the long term, and share equally the risks and responsibilities for providing public services (Ham and Koppenjan, 2001). These contractual relationships can adopt a diversity of figures, namely concession contracts, lease-develop-operate, built-operate-transfer, built-operate-own and franchise, among others (Navarro-Espigares and Martín-Segura, 2011). We will focus our analysis on the concession contracts, where private firms are responsible for new investments and running the existing assets (Khalifa and Essaouabi, 2003).

Theoretically, PSPs in public service delivery aim to augment the use of scarce resources (Value-for-money) in order to improve organizational performance. With higher efficiency levels, those organizations can reduce users' costs whilst increasing the quality of the good and/or service (Parker et al., 2005). This means that by improving economic performance, it is expected a progress in the social performance (Pollitt, 1990). Because the organizational costs are lower, user prices can also be more reduced, guaranteeing the quality of the outputs (Hodge, 2000). PSPs emerged as a possible solution to engage private actors and the associated market mechanisms to follow social goals (Feigenbaum et al., 1998).

In recent studies, however, different frameworks were developed about the ways in which public services can be delivered. Some of those surveys were directed towards understanding the reasons which led to the use of public–private firms (Bel and Fageda, 2010) or corporate public sector organizations for the purpose of public service delivery (Tavares and Camões, 2010) – for corporate public services organizations we also use the term municipal corporations because in the Portuguese case they were adopted by local governments. These institutional models were developed in order to privilege non-commercial aims, i.e. efficiency being pursued in the first place. After becoming more efficient, these organizations should be able to deliver high quality goods and

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services, with lower user prices. The social dimension is thus emphasized by this approach (Bel and Fageda, 2010).

Due to the recent discussion on how public services can be provided, it is possible to carry out a survey in order to understand the regularities between the sector providing the services and social performance. We chose the water sector due to the lack of systematic analysis and statistical evidence in the relationship between the sector providing the service, the quality of the good and/or service, and user prices (Tati, 2005; Wallsten and Kosec, 2008). Additionally, this study is an assessment of the results of PSP in public services delivery, as well as a contribution to the theoretical arguments that support recent public sector reform (especially when the main concern is social performance). As you will see, this paper is organized as follows: firstly, we cover the literature concerning the description of PSPs and their theoretical support; then, we describe the emergence of Portuguese municipal corporations in public services delivery. After the description of the theoretical influences of PPPs and the emergence of corporate public sector organizations, we detail our working hypotheses and variables. At last, we will present our research results and conclusions.

2. Public–private partnerships in water services delivery: theoretical influences and practice

PSP became a popular mechanism for the delivery of public goods and services in the early eighties under the paradigm of the New Public Management (NPM). Until the seventies, public administration was based on a professional ideal: public organization executives were mainly focused on managing their daily activities according to the statutes. At the time, the emphasis was placed on the accomplishments of what the law established as the best practice for public service delivery, as there was no separation between politics and administration. With such an involvement, the focus was placed on the organizational inputs rather than the outputs or outcomes. As a result, it was debated that decisional processes were not flexible and managerial accountability was not possible (Osborne, 2006). Lastly, there were no efforts to promote new ways of delivering public services in order to be more efficient and effective (Araújo, 2003). Due to these constraints, the new ways of delivering public services, – supported by the NPM – focused on PSP in public services delivery, especially in the introduction of internal markets, performance assessment and productivity incentives (Bovaird and Löffler, 2001).

The theoretical influences for PSP in public services delivery should be understood in a specific political, economic, social and technological framework. Such framework was the main reason for the new public management reform paradigm (*cf.* Osborne and Brown, 2005). The theoretical influences of PSPs are commonly associated with the political intention of decision-makers and privilege the following:

- Introduction of market-type mechanisms in the delivery of public services;
- Competition as a key element;
- Economic efficiency improvement;
- Professional management in public service delivery;
- Provision production split.

The introduction of market-type mechanisms in the delivery of public services relies on the belief that the performance of public organizations is lower than that of private organizations (Bennett, 2001). In property rights theory, it is claimed that, since private organizations seek profits, the management of scarce resources is a primary concern (*idem*). Being more efficient, private firms tend to focus on economic wealth growth and on preserving assets value (Heitger, 2004). And that is possible due to PSPs in public services delivery, which takes on a market-oriented management style in order to increase efficiency (Torres and Pina, 2001).

In the water sector industry, this is being accomplished through the sale of assets and PPP agreements. The United Kingdom (UK) government, after the *Financial Management Initiative*, undertook the sale of assets of publicly-owned water organizations to private firms. Since then, 10 organizations have been operating in the water and sewage sector and 21 solely in water delivery (Marques, 2005). The UK experience is somehow peculiar because the majority of the other countries is using partnerships – concession contracts – when they decide to allow PSP in the water delivery industry. In France, 75% of water services are supplied by private firms under a concession contract agreement (Fisch, 2005), and the same happens in Spain, with 55% of the service under private responsibility (Marques, 2005). In Portugal, though, as well as in Germany (Fisch, 2005), in the United States (Wallsten and Kosec, 2008), in Canada (Rasmussen, 2005), and in The Netherlands (Meer, 2005), the majority of water services delivery is still under public sector responsibility.

Associated to the introduction of market-type mechanisms in the delivery of public services, we find *competition as a key element*. According to Stiglitz (1999), market economies need to fulfil two premises in order to be efficient: the existence of private firms and competition amongst organizations. Without competition it is pointed out that there are no incentives for the firm to be efficient since it establishes the market rules. Attached to property rights, competition is thus a primary concern regarding efficiency increases (Hood, 1994). On the other hand, the use of PSPs in the delivery of public services is dependent of market characteristics. In some sectors, it is not easy to introduce competition in the delivery of public services because we are dealing with natural monopolies, such as water delivery organizations.

In those cases, however it is possible to introduce *market competition* when we promote a tender for PSP – *ex-ante competition* (Torres and Pina, 2001). For PPPs, this has been the most common approach, because public entities sponsor a dispute before the concession of the water delivery system management is awarded. As expected, the best proposal will guarantee the management of the services through a concession contract (Marques, 2005). This has been applied in Portugal, Spain, and France among other countries. Additionally, the *benchmark competition* is also possible after the concession contracts have been signed. Under those conditions, some indicators are presented, and stakeholders are able to compare the results of each operator and thereby compel them to improve (Wallsten and Kosec, 2008). Another option is to promote the *within the field competition* when the government decides to sell public assets. However, and again, the government creates a key-figure as a regulator of the privatized services. This was the approach adopted for water service delivery in the UK in order to promote competition (Secretary to the Treasury, 1999).

The introduction of market-type mechanisms in public services delivery has had an additional consequence: *economic efficiency*. For Friedman (1962), markets and the associated price mechanisms are a better option when we are dealing with scarce resources. This assumption is based on private firms' main objective, profit, which, in turn, will lead to larger production efficiency (Romano and Guerrini, 2011). In order to become competitive, firms must produce something with a price as low as possible and still guarantee the quality of goods and services. Their survival depends on it as a better relation between price and quality will determine the firms' turnover. If a firm does not offer a competitive price and quality its survival will be at risk.

Furthermore, one of the major political reasons for the introduction of PPPs in the delivery of public services, including the