For Mari
Acknowledgements

As Booker (2004:83) writes in his book ‘The Seven Basic Plots’ about storytelling, one plot is a journey as a ‘quest’ where the main character strives towards some distant, all-important goal. This journey takes place in stages, where first, the main character is in an intolerable state and receives a ‘call’ that makes him recognize that he can only rectify matters by embarking on a long and difficult journey. Then he meets companions with whom he sets out together across hostile terrain, encountering a series of life-threatening ordeals including ‘horrific monsters’ and ‘temptations’ to be resisted. These encounters alternate with periods of respite, where the main character receives help and advice, often from ‘wise old men’ or ‘beautiful young women’. Then he arrives within sight of his goal, but he must undergo his ‘final ordeals’ a last series of tests to prove that he is truly worthy of the prize. This culminates in a last great ‘battle’ and after a ‘thrilling escape’, the prize, often a life-transforming treasure, is finally won. Lucky me, on my quest the monsters were outnumbered by the wise and the beautiful. And the prize at the end – instead of ‘getting’ a PhD – was to ‘become’ one.

Reflecting on my quest, I consider myself privileged to have had so many supportive colleagues, friends and family. During my ‘calling’, Professor Ajeet Mathur was crucial because he asked me to start a PhD in the first place, while I was still figuring out what to do with my graduate degree. Soon thereafter, Professor Marja Eriksson and Adjunct Professor Tapio Katko became my supervisors and provided encouragement, guidance and excellent advice while also allowing me great freedom and to learn from my own mistakes. Without their guidance and support, there would not be a PhD. While I was trying to get myself acquainted with a new system, Kyösti Koskela and Marketta Saikku were important in their role as administrators and were looking out for me.

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One of the ‘final ordeals’ during my quest was to submit my thesis to the preliminary examiners just in time before going with my wife on our honeymoon. Another ordeal was to find energy for extensively revising my thesis when I received it from the reviewers. However, the excellent and focused comments from both of them, Professors Risto Tainio and Matthias Finger, allowed me to significantly improve my manuscript and I am honored to have had them as examiners. Further, I am honored to have another leading expert on the subject, Adjunct Professor Jarmo Hukka, as my opponent.

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Turku, September 2007
Richard Windischhofer
Executive Summary

During the past ten years, the Finnish state has been continuously decreasing financial support for municipalities while at the same time encouraging them to adopt private sector practices and to intensify inter-municipal cooperation. In this still ongoing reform process, the municipalities have significant freedom in how to implement reforms, which allows them to find their own ways of organizing. Municipalities have become more entrepreneurial by embracing private sector managerialism and by adopting a more active role in attracting national and global resource flows to their local areas. Since the state’s role as financier is decreasing, municipalities are increasingly turning to investment bankers and financial consultants for advice on how to secure financial resources for their budgets. Thinking mostly in financial terms, the financial actor’s advice has a reinforcing effect on municipalities’ inherent individualism and new entrepreneurialism. Municipalities are commercializing their public services operations and their self-reform is leaning towards short-term financially-oriented local solutions instead of engaging in structural change on the regional level where benefits are hard to calculate and to predict.

Because the Finnish water utilities are owned by the municipalities, they are exposed to this entrepreneurialization and find themselves exposed to its consequences. These consequences comprise of: the increasing commercialization of water services; slow regionalization of water utilities; and the formation of combined water and electricity utilities. The commercialization of water supply is driven by the municipal entrepreneurialism that transforms water utilities into public-owned yet highly commercially-oriented monopoly enterprises. The regionalization of water utilities is taking more time than expected because municipalities’ inherent individualistic logic is combined with their new entrepreneurial spirit and financial actors’ rationalistic advice. As a result, it is difficult for municipalities to agree on water utility mergers because their main focus is on numbers and short-term individual benefits instead of having vision and a common interest. Local solutions to municipalities’ financial problems have therefore emerged, resulting in combined water and electricity utilities.

Contradicting the common perception that private sector companies are the reason whenever commercialization is taking place, I found that municipalities themselves played the main role in promoting commercialization, although driven by the state to entrepreneurialize in the first place. I am questioning the state’s approach to promote local public services reform by cutting municipalities’ resources and encouraging them to adopt private sector managerialism and entrepreneurialism – not because knowledge transfer from private to public sector would be harmful to public organizations as such, but because it is a process of learning by imitation. Therefore, the public sector ends up with a rationalized version of private sector professionalism and partly uses convenient private sector myths to justify its existing way of thinking and managing. The resulting municipal entrepreneurialism is counter-productive to local government reform and regionalization and to the reform of water services.
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List of Acronyms

FIWA  Finnish Water and Waste Water Works Association (in Finnish: VVY)
JV    Joint-Venture
PPP   Public-Private Partnership
WSS   Water Supply and Sanitation
1 Introduction

1.1 Water Services Commercialization and Public Sector Reform

This is a study about the commercialization of local public water supplies in Finland. I am studying this subject at a time when countries across Europe as well as the Finnish state have undergone continuous reform since the 1990s to improve the efficiency and effectiveness of administration and public services to resolve the financial crisis in public sectors. In recent years, there has been significant discussion in Finland about the regionalization of local administration and services and appointing private sector companies as the producers of services that were previously run by public sector entities. Public health care has received extensive media coverage in this context, but water services have received less attention although they undergo similar development. Municipal water supply and sanitation, which is maintained in the public sector in Finland, is therefore also subject to public sector reform and the changing roles of the public and private sectors.

In Europe, civic and scientific concern related to changes in the role of private companies in the provision of water services has, for example, focused on cities that partly or fully privatize their water utilities by selling shares to mostly large, multi-national companies, such as Budapest (in 1997), Berlin (in 1999) and Tallinn (in 2001). Still, the majority of the European population is served by public water utilities1.

In Finland, the municipality-owned and -operated water utilities serve ninety percent of the population, whereas the rest is served by small-scale consumer-initiated cooperatives or private wells. The main reason for the local or national government ownership of water services in Finland and most other European member states is the fact that it was historically a strategic issue to keep cities clean and safe by providing functioning water supply and sanitation and it is inevitably linked to municipal services as well as it is considered a quasi-public good and a natural monopoly. Public ownership of water services, which are local monopolies, seems preferred to private ownership in most EU countries. As they are natural monopolies, their sale to private companies is considered a much more sensitive issue than selling municipal energy companies. Further, there are commercial reasons for the public sector to own and operate them since in Finland, the water utilities of larger cities are profitable businesses.

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1 In the majority of EU countries in 2001, between 90% and 100% of the population were supplied by public utilities, such as in Finland (90%), Italy (96%), Belgium (95%), Sweden (98%) and Luxembourg, Austria, Netherlands, Denmark, Greece, Ireland (100%). Within the EU, in 2001, privatization of water services was most advanced in the UK (88% of population supplied by private water utilities), France (75%), Spain (38%) and Germany (18%). (Hall, 2001)
In the member countries of the European Union, large scale privatization of water services has occurred only in the UK and Wales, where the sector was privatized in 1989 and in France, where the majority of water utilities are run by private sector companies, although they remain in public ownership. In the remaining EU countries, the water sector is predominantly owned and operated by either the national, regional, or local government bodies. In recent years, most countries have experienced moderate increases in the private ownership of water services, such as in Germany or the Eastern European EU member countries. In the European context, objections by the civic movement regarding the increasing role of private sector companies resemble those that have been made in developing countries. The fact that the UK’s and France’s model of water service provision has not found large scale adoption in other EU countries is an indication that the European public’s preference is for a public owned and managed water sector. Still, whether it is more effective to have private or public water utilities run the water services is an ongoing debate, where almost equal amounts of studies find in favor of the private or public sectors.

The European Union has promoted the liberalization of its markets, specifically public and water services. As a result, its member states protected their water service sectors from outside economic governance. In 2004, European Parliament Members voted against the EU Commission’s proposal of placing water services under EU authority. Instead, the principle of subsidiary still applies, which means that water services remain a matter of national authority. Also, the EU Service Directive issued in 2006 excluded water services from the list of services that are to be opened for transnational competition. In 2006, the Netherlands passed a law that banned private companies from owning water utilities. Sweden, Austria, and Denmark implemented legislation that confined water utilities to non-profit operations (Pietilä, 2006).

Large, private owned utility companies, often multi-utility companies that not only own or manage water and sewerage services, but also waste and energy operations have emerged, with the largest players being companies from France, the UK, the US, and Germany. The need for finance in the public domain has driven private sector participation and ownership of water utilities and their assets. However, expertise in management and technology has been provided by private water companies, which has improved water supply and sewerage services in many cases, for example in the UK, where the quality and standards of the water sector have improved since the sector’s privatization.

The discussion whether to have public or private water utilities is mainly political, where each side demonizes the other and discredits their legitimacy to operate water services. The private side argues that the public sector is inefficient and the public sector argues that private sector is immoral and takes advantage of its monopoly character. However, both sides ignore the fact that the role of the public sector has changed and previous assumptions about its motives and effectiveness have become outdated. The changing
role of the municipal sector has been ignored, as is demonstrated by passing legislation that confines the water sector to a non-profit policy or as in the Finnish case the law limits profitability of utilities to ‘reasonable’ levels.

Such measures of governing water services create the impression that municipalities would follow that legislation and they would not require any regulation except regulating themselves through local democratic governance system. In the case of the Finnish water sector, a study has shown that municipal owners are bypassing that law through the use of creative accounting methods that disguise the actual revenue they receive from their water utilities (Näsi and Windischhofer, 2005). Therefore, it is even more important to clarify the changing role of the public sector and assess its ability to own and operate monopolies in an economically self-regulated environment.

A recent survey (Vinnari, 2006) among managing directors of the largest Finnish water utilities found that more than half were in favor of establishing a regulatory agency to protect the utilities from their municipal owners that place profitability above infrastructure investments. Occasionally, failures in delivering water services, such as pipe breaks caused by extreme variations in temperature during winter or water shortages during summer are reported in the media and detail the general lack of investments in the water sector and its water networks (Helsingin Sanomat, 2006). In Finland, the debate about structural changes and reforms in water services is predominantly an issue of local public services reform, where cities and municipalities have been trying to implement structural changes by increasing regional cooperation and investigating whether to give private companies a more important role in the production of water services.

To solve local public water supply and sanitation problems, Juhola (1995 in Hukka and Katko, 2003a) recommended and predicted an increase in autonomy of water utilities for the Finnish water sector, their incorporation, and their regionalization by creating larger water utilities. Ten years have passed since these remarks were made by Juhola; instead of his predictions coming to fruition, there are indications for the decreasing autonomy of water utilities and the tendency to merge them with energy companies. Further, municipalities have not incorporated their water utilities on a large scale, as expected, and the planned regionalization process in terms of creating larger water works has not significantly progressed either, although bilateral agreements between municipalities did somewhat increase.

In this thesis I am proposing a theory of local public water service commercialization to explain the process that has lead to the events as described above. This theory shows that Finnish water utilities are commercializing despite the absence of privatization because they are exposed to the entrepreneurialization of local governments, which creates a more commercially-driven attitude for municipalities towards governing their water utilities. Therefore, the above described loss in water works’ autonomy after their incorporatization, underinvestment, and attempts to create multi-utilities need to be seen
as a result of an increasingly commercial governance of water utilities by their municipal owners. Hence, I propose that the present form of local governance of water utilities in Finland creates outcomes that are counterproductive to the long-term interests of citizens regarding their water services. The state may have to engage and implement large-scale water sector reform and put public-owned water utilities under the supervision of a regulatory agency that safeguards the functioning of water supply and sanitation in the presence of a commercially-oriented municipal owner.
1.2 Subject of the Study and Research Questions

Water services’ commercialization is extremely ideological. Researchers in this field are predominantly concerned with water privatization and focus on the malpractices of private corporations when they take over public water utilities. On the other hand, there is also extensive research published under the World Bank organization that sees privatization as an option to improve access to safe water and sanitation, especially in developing countries. Most studies about the commercialization of water services focus on the role of a few dominating, globally active private water- and multi-utility corporations such as the French Suez and Veolia, as well as on the role of international institutions such as the World Bank and the International Monetary Fund. For example, Finger and Allouche (2002) studied the role of these multinational corporations and World Bank in the privatization of water supply on a global level, concluding that they are part of a much wider change in public sector and infrastructure reform in finance, construction, and operation. As a result, they point to the risks of private monopolies and call for concentrating on establishing regulatory authorities in involved countries. Among others, Hukka and Katko (2003b) concluded that private water services are proliferating, despite doubts of their higher efficiency compared to public water services and the fact that they pose a threat to the interests of consumers, especially when unregulated.

Globalization and commercialization, as a result of privatization, is a fairly well-researched area, especially when it comes to water services and other infrastructure-related public services (see e.g. Weizsäcker, Young, and Finger, 2005; Hall and Lobina, 2006; Hukka and Katko, 2003a). However, studies investigating the globalization and commercialization of public services in the absence of privatization are indeed rare and it seems to me as if water works first need to become privatized before attracting the interests of scientists studying commercialization.

There is also an on-going discussion in water policy-making that relates to privatization and commercialization regarding whether water is a public good or a commodity and whether water services are a public service or a business. This discussion divides commercialization into two camps, where methodological individualists stand for business interests, liberalization, night-watch state, and individuals taking care of the collective; while methodological collectivists stand for the collective taking care of the individual, strong regulation and role of the state, and a larger public sector (Livingston, 1993).

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2 Finger and Allouche (2002) use the term transnational companies (TNCs); I use the term ‘multinational corporations’ for simplicity since extensive discussion exists in the field of international business on the terminology of companies that are active in more than one country. However, I would like to point out that what Harzing (2000) calls ‘multidomestic companies’ would probably be the most appropriate term, since local water suppliers that become owned or operated by a foreign company maintain a large part of their local independence based on the fact that water supply and sanitation is a highly locally dependent business.
Much of the research on water services seems to justify a local public water sector that regulates itself through the local democratic system; therefore, I consider these studies as part of the methodologically collectivistic paradigm. For the purpose of justifying the present system of public water supply, researchers in the field of water privatization have quoted Williamson (1987:33) who noted that “we can only choose between three evils: private unregulated monopoly; private monopoly regulated by the state; and public monopoly”. However, when Williamson made that statement, the entrepreneurialization of the public sector was in most countries just beginning. Currently, this begs the question of whether a fourth organizational archetype should be added to this statement that acknowledges the emergence of commercially driven public monopoly enterprises. After having conducted this study, it is my opinion that one of the main problems with water services management research is that it focuses on the commercialization process caused by privatization and hence on private companies. Since the majority of local water supply and sanitation in Europe is still public owned and managed, it is my view that the commercialization of local public water supply in absence of privatization is one of the most important and most overlooked questions in research on the management and governance of water services.

Therefore, the key objective in this study is to build an understanding of the commercialization process, which occurs in the absence of privatization by addressing the research question:

*What drives the strategic decisions concerning the local public water utilities in Finland?*

This question is important because the problems water utilities and other organizations encounter with public sector market-oriented reforms are ubiquitous, but poorly understood. Despite a significant amount of research on the subject of public sector reform, liberalization, privatization, and commercialization of water services and public services, our understanding of the driving forces, key actors, and their relational dynamics remains as ambiguous as does our understanding of the outcomes of this market-oriented turn. For example, the dichotomy described above of individualistic and collectivistic ideological preferences in water services management may be outdated, considering the changing role of public sector towards market-oriented reform. The main research question investigates the commercialization process of public-owned water utilities in the absence of privatization and investigates the role of a broad range of actors in that process, including private companies that may nevertheless have an important role. The following sub-questions were addressed:

- *Who are the relevant key actors for the strategic decisions concerning local public water utilities?*
- *What are their institutional logics and what are the main issues?*
- *How do these actor’s logics connect with each other; what is the mechanism?*
- *What are the outcomes of that mechanism?*
My approach to clarifying what drives strategic decisions concerning the water utilities in Finland is to study it from an institutionalist perspective by investigating the actors, their changing roles, and their ideas and beliefs within a longitudinal timeframe that allows capturing the processual nature of the commercialization phenomenon. I assume, therefore, that the way water services are organized and governed is based on decisions and these decisions are based to a large extent on institutional ideas and beliefs about ‘appropriate’ management and governance of water services, rather than being merely based on a ‘rational’ assessment of economic, social, and environmental conditions and demands.

In my view, another possibility to study this phenomenon could have been to use the institutionalist policy-making approach that also assumes ideas and beliefs to be the basis for policy-making. However, since my goal was to build a theory of commercialization, I found it only necessary to use institutionalism as a ‘lens’ through which I analyzed the roles, issues, and institutional logics of actors to build my commercialization theory. Overall, I would say that my approach could be called an ‘institutionalist theory of water services commercialization’ whereas the commercialization phenomena emerged during the research process rather than it being chosen from the beginning.

With this thesis, I hope to contribute to a more holistic understanding of the market-oriented turn of local public services and its outcomes by using examples from water supply and sanitation services. Another objective is therefore to develop a theory of local public services commercialization processes and explain their outcomes, as well as their effects primarily on local government and water services reform. Further, I aim to provide information to researchers and policy makers on what drives strategic decision-making related to public-owned water utilities and provide an assessment of the consequences for the long-term viability of water services.

Besides my goal to contribute to the research on water services management and privatization, I also aim to contribute to my own discipline of management and organization. It is my view that organization theorists need to be more interested in the public sector reform process. With the changing role of public sector organizations, the role of private sector organizations has changed as well. The private sector assumes a more important role in the provision of public services and in the context of this study certain private sector actors fulfill a small but rather important role in the transformation process.

Researchers in management studies that traditionally are more interested in private relative to the public sector should follow ‘their’ sector when it enters or tries to enter the public sector, especially during the mimetic processes where the public sector imitates private sector management principles and techniques. In my opinion, this mimetic process has counter-productive effects on public sector reform and should be of significant interest to management studies. If researchers of management studies would
engage more in this research area, they would likely reflect more on what they write because as knowledge rationalizers and organizational translators, they distribute not only knowledge about private sector management that is implemented by the public sector but also ‘myths’.

I have written this thesis with a certain audience in mind. This audience includes water sector managers that complained to me about the lack of transparency regarding the ‘fate’ of utilities they manage and the lack of predictability of their public owners. Further, I wrote this thesis for the municipal managers because they complained that despite the need for cooperation among municipalities, the implementation of such cooperation is a troublesome process. I hope that information in this study regarding the counter-productive effects of municipalities’ and their advisers’ logic helps municipal managers reflect on their actions and improve their ability to proceed with reforming local public services and administration. I also wrote this thesis for state governance actors and policy makers and I hope that by pointing to the municipalities’ and water utilities’ difficulties in creating sustainable water services, the policy makers would begin to discuss how to solve problems before they become acute. Last, I had my own discipline of management and organization studies in mind where studying institutional change is of great interest to many researchers but where the changing roles of public and private sector are usually studied separately. I hope that this study inspires more research that studies their roles in a combined and processual fashion to make the dynamics and outcomes of their interaction processes visible.

Based on my study, I am not going to position myself as a supporter of the individualistic or collectivistic ideological camp by arguing either for or against privatization of water services. Instead, I am arguing that this dichotomy is outdated because globalization, financialization, and the public sector reform process has helped to promote an entrepreneurial local public sector with such significant commercial orientation that the question of who owns and manages public water supply is in my opinion secondary to the question of how to effectively regulate the owners and operators of water supply and sanitation. Personally, I believe that in countries with functioning institutional and governance frameworks that have the capacity to effectively regulate water utilities, private ownership and/or operation of water services represents a viable arrangement, similar to the public model.
1.3 Composition of the Study

Chapter 1 introduces the study subject and my theoretical ‘lens,’ which uses institutionalism to study commercialization.

In chapter 2, I introduce and discuss the theoretical framework that relates to my contribution of building a theory of water services commercialization. These theories contribute to the link between commercialization and entrepreneurialization; these two concepts are driven by the larger processes of globalization and financialization, which also drives liberalization, privatization, and corporatization.

Chapter 3 reports on the methodology of my thesis and elaborates on the grounded theory approach I utilized. I do not engage in a discussion on scientific paradigms, but instead describe the ontological, epistemological, and axiological assumptions that guide me as researcher. Also, I provide a detailed account of my journey of ‘scientific discovery’.

Chapter 4 marks the beginning of the empirical part of my study by presenting a field analysis that introduces the relevant actors of this thesis, provides a basic knowledge of the water sector, and demonstrates the relevance of the financial actors in the commercialization process by providing an analysis of the changing roles of commercial actors. I conducted this analysis of the wider context of relevant actors for the water utilities by using a qualitative social network analysis (reported in the ‘Methods’ chapter), where I subsequently interviewed an emerging managerial elite. During these interviews and by conducting additional documentation analysis, the governance actors, municipalities, and financial actors emerged as the most relevant actors in understanding the institutional change process.

In chapters 5, 6, and 7, I am analyzing the institutional logics and changing roles of state governance, municipal, and financial actors. These chapters contain a variety of data sources such as longitudinal analyses of relevant legislative changes for state governance actors and longitudinal content analyses of professional journals and newspapers for municipal and financial actors. These data analyses are used to complement the qualitative interview data derived from these actors, which represents the main data source. For each actor, I extracted the key characteristics of their logics and analyzed them according to managing water services and public sector reform by using my theoretical ‘lens’ of institutional theory.
Chapter 8 represents the discussion chapter where I summarize the empirical results discuss them in the light of institutional theory and conceptualize them to create and propose a theory of how and why the local public services have commercialized over the past decade. I also propose a mechanism that explains the connection between the key actor’s different logics and actions. Finally, the implications of the commercialization process are discussed from the water sector’s perspective by drawing three different scenarios for structural change.

Chapter 9 comprises the conclusions, recommendations for practice and policy-making, study limitations and suggestions for further research.

The appendix includes parts of the data analysis for this study and comprises the longitudinal qualitative content analysis of the business newspaper Kauppalehti, and the aide memoir that guided me in my interviews. I do not include the list of interviewees’ names and dates because they were granted anonymity for this study. However, I provide some information about the interviewees’ number, status, and professions in the methodology chapter.
1.4 Studying Commercialization from Institutionalist Perspective

I am studying the commercialization process of water services and its outcomes by investigating the actors, the main issues, their logics and actions. Therefore, I am looking at the phenomenon of commercialization through another ‘lens,’ which originates from new institutionalism in organizational analysis. I then move on to discuss literature associated with entrepreneurialization and commercialization in a separate chapter, to which this study’s contributions are aimed.

1.4.1 Framework of Actors, Processes, and Theories of the Study

Figure 1-1 provides an overview of the framework for this study and emphasizes the central concepts of actors, processes, and outcomes by studying the actor’s institutional logics and actions. Here, I regard organizations as the actors involved in a process of entrepreneurialization and commercialization. The focus of the study is to clarify the relationship between entrepreneurialization and commercialization and the roles of different actors involved in these processes in order to propose a theory of the commercialization process and its outcomes.

The role of institutional theory in this study is not primary, but it is used to establish a theory that relates to commercialization. However, the key concepts I use as tools and that originate from new institutionalism are discussed in the paragraphs below. I begin by discussing how institutional change has been studied by others and explaining the tools I used to represent key concepts of institutionalism, which comprise actors, organizational fields, legitimacy, and mimeticism.
1.4.2 Discussing related Research in Institutional Theory

New institutionalism explains stability and change in organizational fields through adopting an ‘open systems’ perspective (Scott, 1987), in which organizations are affected by their environment and other organizations residing within this environment. The boundaries of this environment are porous and problematic in nature. Organizations are affected not only through competitive or efficiency-based forces, but also through cultural and cognitive forces such as norms, symbols, beliefs, and rituals. Powell and DiMaggio (1991:8) point out that ‘the new institutionalism in organization theory and sociology comprises a rejection of rational-actor models, an interest in institutions as independent variables, and a turn toward cognitive and cultural explanations.” Thus, the belief systems or institutional logics of organizational actors are important in studying organizations and organizational change (DiMaggio, 1988; Scott et al. 2000).

New institutionalism in organizational analysis focuses on power, informal structures, and institutional logics. Institutional change occurs over time as a process of “institutionalization and deinstitutionalization”, where new norms are introduced and become adopted by actors and may substitute old norms, values and beliefs that need to be altered, changed, ‘unlearned’ (Hedberg, 1981) or ‘forgotten’ (de Holan and Phillips, 2004). Changes rarely occur in a revolutionary fashion, but rather resemble more gradual and evolutionary developments (Tainio and Lilja, 2003). Therefore, institutional change is studied by adopting a long-term perspective, which often comprises several decades, such as DiMaggio’s (1991) study about the US museum sector, or Holm (1995) and his study about the evolution of the Norwegian Fisheries sector.


The data of these studies may comprise structural data of the changing amount of organizations, changes in legislation, or for example, changes in journals. Examples include Holm (1995) using structural data in his study of the Norwegian Fisheries, Hoffman (1999) tracking the main topics in journals for his study about the rise of the environmental approach in the North American chemical industry, or Cousens (2000) tracking legislative changes in her study about the North American sports leagues. A number of studies use a combination of qualitative and quantitative data, especially when connecting the structural and cognitive changes of a field, such as Cousens (2000) including interviews and quotes of key persons from newspapers. As Reay (2000) argues, most studies about institutional change in this tradition take a historical approach and focus on structural aspects rather than cognitive issues.
I am studying commercialization of the Finnish water supply and sanitation by adopting a similar approach and combining structural and cognitive data. My interests include explaining criteria that are the basis for strategic decision about water utilities. Therefore, my interests can also be interpreted as relating to the strategy process. As Pettigrew (1992a:9) suggests, research on the strategy process should be guided by the following five principles:

- Embeddedness, studying processes across a number of levels of analysis
- Temporal interconnectedness, studying processes in past, present, and future time
- A role of explanation for context in action
- A search for holistic rather than linear explanations of process
- A need to link process analysis to the location and explanation of outcomes

Further, Pettigrew (1992b:163) emphasizes that ‘the study of managerial elites is one of the most important, yet neglected areas of social science research’. Difficulties in access is one of the major constraints, which also explains the vast amount of speculative articles on the influence of ‘capitalist elites and companies’ and their supposed effects on changes in the environment, such as the liberalization of markets and privatization of water utilities. My approach was to collect primary empirical interview data from actors that are relevant to the process of strategic decision-making for water utilities and I chose to locate these relevant actors by conducting an elite study of qualitative social network analysis combined with interviews.

In this study, I aimed to longitudinally investigate institutional changes in the Finnish water sector based on new institutionalist concepts and according to Pettigrew’s’ (1992a; 1992b) recommendations. However, following Pettigrew and his recommendations on how to conduct research on the strategic process was not that planned as it may seem. As I used the grounded theory approach (Glaser and Strauss, 1967) from the beginning of this study, I started at the organizational level from where the managerial elite emerged by using qualitative social network analysis (explained in the methods chapter). To gain a holistic understanding of the key issues of my research area, I conducted a multi-level analysis and turned to the interconnectedness of key actors, their context of action and outcomes.

Therefore, I used all guiding principles that Pettigrew emphasized (1992a), although I was not aware of them until after the empirical analysis for this thesis was completed. I regard the similar outcomes of the Grounded Theory approaches’ as a testimony to its purposefulness for research on the strategy process because similar to Pettigrew’s (ibid.) recommendations, it encourages the researcher to gain a holistic understanding of what is studied. Scott et al. (2000) suggest in their study about institutional change of the medical field in the San Francisco Bay Area institutional logics are analyzed according their actor’s domain, definition of success, and principles of organizing. I found this distinction useful for my own study and therefore applied it to each actor’s analysis.
1.4.3 Actors, Action, and Agency

I am proposing a theory of local public services commercialization based on new institutional theory, which means that I regard actor’s institutional logics, structural positions, and roles as crucial for understanding the commercialization of local public services. As a result of this approach, the concepts of actors, action, and agency are basic elements of this study and are briefly explained below. In the following paragraphs, I seek to clarify that actors are individuals or organizations and their actions take place in awareness of their circumstances and thus, are ‘knowledgeable’, although constrained by subconscious dimensions of their actions and the boundedness of their knowledgeability due to unacknowledged conditions and unintended consequences. Actors have the ability to act (agency) but it is constrained by the boundedness of their own knowledgeability and by their institutions or ‘the established ways of doing things’ in their environment.

By ‘actor,’ I am referring to an individual or organization that is subject to social action (Scott, 1994). Actors can be individuals, organizations (such as companies, municipal administrative bodies, or government agencies), but also on a more aggregated level, I consider elites or nations as actors as long as they pursue a certain homogenous interest. The managerial elite that emerged during my analysis of the commercialization of water services does not fulfill the requirement of having a homogenous idea of itself, nor of what it does, or what it should be achieving. I do not consider the managerial elite an actor, but instead it consists of groups of actors that share certain institutional ideas and beliefs, although they may not necessarily engage in coordinated action. The actors I investigate in this thesis are organizations represented by human beings with ‘clout’. When I talk, for example, about municipalities as actors, I do it based on what I have found out about that actor from interview material with managers representing that particular actor and by using secondary data as well.

Following Giddens (1984) notion of ‘action,’ an actor is capable of cognitive action (or ‘knowledgeable’ action) and maintains a theoretical understanding. Sevón (1996:49) summarizes ‘action’ by saying that actors are able “to attend to the environment, to make comparisons and judgments, to reason about causality and to act according to desires. An actor is also able to conceive of itself as having identities.” However, the actor’s awareness of its actions is bounded by a number of limitations that prohibit the actor from fully reflecting on its own capability. Giddens (ibid.) points out actors are knowledgeable about their actions to the extent that when asked why they are doing things, they will be able to provide an explanation, although not entirely clear about conscious and subconscious dimensions of their actions and intentional or unintentional consequences of these actions. Actors cannot be fully aware of these issues because although they may be able to explain their intentions for their actions, they are guided by subconscious motivations. Further, even intended actions may have unintended consequences which feed back into the reproduction cycle of social structure and may become unacknowledged conditions of future acts. Subconscious cognition and motivation is distinguished from what Giddens (1995:27) calls ‘practical consciousness’
which means that actors are not fully aware of their actions but still ‘know how to go on’ and are ‘knowledgeable’ about what they do and why they do it. Action is highly routinized and this knowledgeability mostly refers to the daily activities of actors. Giddens and Pierson (1998) also point out that action mostly rests on monitoring one’s’ behavior in relation to others; whether on the individual or organizational level, this also takes place partly subconsciously and partly consciously.

By ‘agency,’ I mean the actor’s ability to act. Giddens (1984) describes agency as referring ‘not to the intentions people have in doing things but to their capability of doing those things in the first place’, which is why agency implies power. Having power means being able “to intervene in the world, or to refrain from such intervention, with the effect of influencing a specific process or state of affairs” (Giddens, 1984:14). Although institutionalists consider power to be a resource itself, technically, it is not a resource but draws on resources to become enacted. In order for actors to possess agency and enact power, they also require a subject position within their environment (Bourdieu, 1990) or in other words, they need to be part of the field and its processes to have a chance to affect their environment. For example, access to other key actors, forming alliances, or building constituencies may be helpful.

In institutional theory, the concepts of actor, action, and agency are largely based on Giddens’ (1984) structuration theory and these notions can be found for example in the works of DiMaggio and Powell (1983), Scott (1994), Sevón (1996), and Czarniawska (2002, 2004). For Giddens (1984), in his theory of structuration, human agency and social structure are intertwined in the sense that human action occurs as a continuous flow of conduct and repetition of acts, which reproduces social structure. Social structure is seen by Giddens as the ‘established way of doing things’ that are represented by traditions, institutions, or moral codes. This is also one of the major links to new institutional theory, where institutions are defined as ‘social structures’ that represent the ideas and beliefs of actors, whereas actors can be both human individuals and organizations. In both theories, the importance of time takes a central position because action takes place as continuous flow that produces and reproduces social structures. In new institutional theory, actors possess autonomy in their actions (agency) to the degree that it is bounded by isomorphic forces.

Scholars in new institutionalism directed their attention mostly towards studying processes of institutionalization and how the actors’ actions are constrained by isomorphic forces. In other words, they are mostly concerned with how the ‘ways of doing things’ are established and how they guide actor’s actions, for example through taken-for-granted assumptions and behavior (DiMaggio, 1988). New institutionalism is largely based on Giddens’s theory of structuration that views actors as being knowledgeable and able to reflect at least to the extent that they have a choice in their actions. However, new institutionalism mainly analyzed institutional change from the perspective of institutionalization (as opposed to de-institutionalization) and how actor’s
actions and their agency becomes more narrow over time as their ideas, beliefs, and practices become similar to others’ and thus, more limited.

I am studying the commercialization of local public water services by looking at the actors, their logics, and interactions over time, which is a rather established approach in institutional theory. My approach to new institutional theory and actors, action, and agency is to acknowledge that norms, values, beliefs are exposed to isomorphic forces and path dependency, but nevertheless, actors are ‘knowledgeable’ and they are able to reflect (to certain extent) on their actions. These assumptions have a number of implications for my study.

The actors that I studied are individuals presenting their organizations and their actions take place in awareness of their circumstances and thus, they are ‘knowledgeable’, although constrained by subconscious dimensions of their actions and by the boundedness of their knowledgeable due to unacknowledged conditions and unintended consequences that feed back into the reproduction cycle of the social practices, norms, values, and believes. Actors have the ability to act (agency) but it is constrained by the boundedness of their own knowledgeable and by their institutions or ‘the established ways of doing things’ in their environment.

From a methodological standpoint, this means actors are to some extent able to explain their intentions, to reflect on their actions, to monitor their own behavior and that of others, and that they perceive themselves as having a particular identity. Therefore, my role as researcher was to uncover the unacknowledged conditions and unintentional consequences of (relatively) intentional conduct (Giddens, 1984) to specify processes that produce outcomes and make actors aware of the unacknowledged, unintentional part of their conduct.
1.4.4 Organizational Fields

The commercialization of local public water supply and sanitation takes place in an environment that consists of different actors that interact with each other. In institutional theory, these environments are so-called ‘organizational fields’ and since I had to identify the relevant actors to explain the commercialization process, I had to have an appropriate concept of the field, which actors it contains, what roles they play. As Pettigrew (1992) suggests for studies of process research, it is crucial for the researcher to understand organizational dynamics in the context of larger organizational and institutional environments, in which they are embedded.

I performed a qualitative social network analysis in the beginning of my study and discovered that the organizational field in which the water utilities are embedded contained a variety of actors that do not fit the usual classification of sectors or fields being structured around markets or technologies, but forming around issues and activities. In this case, it was the activity of organizing water supply and sanitation. In order to describe this field, I am using Powell and DiMaggio’s (1983) concept of organizational fields but I am calling it ‘the field of managing the water sector’ rather than just the ‘field of the water sector’. Thus, I am emphasizing the importance of the processual nature of the field (Czarniawska, 2004), as it constantly evolves by actors entering, exiting, or changing their roles. I agree with Hoffman (1999), who argues that the notion of the ‘organizational field’ as defined by Powell and DiMaggio (1983) and extended by Scott (1994) focuses too much on spaces and positions of actors, making it necessary to draw field boundaries based on markets or technologies.

My notion of organizations being embedded in fields that are centered on issues and activities rather than just around markets or technologies, therefore includes a larger diversity of actors. However, a proper field analysis that identifies the relevant actors also reduces the number and variety of actors because it focuses only on those that affect the process under investigation. There can only be a few highly relevant actors because although I see actors as part of ‘the field of managing the water sector’ when they have an interest in it (which may relate to almost anything, including market, technology, society, or just ‘money’), but they need to acquire or maintain subject positions in the field which enable them to act or interact with others in the field.

The subject position is important because as Bourdieu (1990) suggests, each field only has a limited number of subject positions that provide actors with the necessary resources such as power or legitimacy to affect the process. For example, university research groups are part of the organizational field of managing water services in Finland and they are involved in the commercialization process by publishing their opinions in professional journals and business newspapers – but they do not have a subject position

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3 For more information, please refer to the methods chapter for a summary of the social network study.
in the field that enables them to actually affect the commercialization process in a manner similar to financial actors, who enjoy close ties with owners of the water utilities.

Having established that fields contain actors and fields evolve around issues and activities, it is also important to briefly explain the difference between an organization and an institution. The former are actors such as companies or ministries. The latter are meaning systems of ideas and beliefs. As depicted in Figure 1-2, organizations not only operate in structural environments or fields but also in institutional ones. Scott (2001: 49) provides a definition of institutions by saying “they are social structures that have attained a high degree of resilience transmitted by various types of carriers, including symbolic systems, relational systems, routines, and artifacts. Institution’s central ingredients are rules, norms, and cultural beliefs.” In this context, institutions refer to systems where norms, values, and beliefs are shared among a group of actors as institutional logics (Scott et al. 2000). These systems function as frameworks of orientation for actors regarding the type of what kind of behavior is appropriate within the group (Scott, 1987). North (1994) distinguishes between formal and informal institutions. Formal institutions are norms that were written down. They often establish legally binding property rights and specify how and by whom resources can be used. Informal institutions refer to social structures with a similar meaning as the formal institutions, but they are much harder to grasp because they are usually not officially documented.

Institutions arise from a process of interaction between social actors and hence, they are considered socially constructed systems. As such, they are able to decouple from the social actors and assume a relatively independent role, for example manifested in the institution’s ability to constrain actors’ actions through taken-for-grantedness and path dependency. Therefore, organizational fields have an organizational dimension such as the number of organizational actors operating in them and their roles, their characteristics, and tasks; and an institutional dimension represented by social structure of the norms, values, and beliefs these organizational actors hold and may share with

![Figure 1-2 Distinguishing between Institutions and Organizations](image-url)
each other. Institutional changes are inevitably linked to organizational ones, because structural changes are based on decisions made by managers and decision-makers, whose beliefs, values, and behavioral norms are part of a particular institutional system.

Therefore, I see decisions and policies as being based on institutional beliefs and by studying these beliefs, one can find out more about how and why these decisions are being made. During my analysis, two concepts of institutional change emerged as most crucial in explaining why the strategic decisions about water utilities are being made. Organizations that suffer from a lack of legitimacy may try to increase their legitimacy by mimicking practices of other organizations that are perceived as more successful. In the following paragraphs, I briefly review the concept of legitimacy as a resource for organizations and then explain mimeticism as part of isomorphic forces and its key characteristics.

### 1.4.5 Legitimacy

Institutions are social structures. They provide the organizational actors residing within their sphere with meaning about what kind of behavior is legitimate. Since these entities not only compete for traditional economic resources such as financial and human resources but also for social legitimacy (Meyer and Rowan, 1977), they adapt to legitimate behavior whether through coercive, normative, or mimetic forces. This makes legitimacy a resource on its own, as it provides the organization with reasons to exist that are not necessarily based on pure grounds of efficiency.

Suchman’s definition of legitimacy (1995:574) is that it ‘is a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions’. Therefore, an organization possesses legitimacy when it is accepted or supported by a social group and therefore, legitimacy is dependent on a collective audience. Yet, it is independent from the individual observer because an organization may deviate from the observer’s values but retain its legitimacy because the deviation draws no public disapproval (Suchman, 1995).

Kostova and Zaheer (1999) suggest that legitimacy is vital for the organizations’ survival and success and is acquired during a process where the environment builds its perceptions of the organization. In this process, the environment or key actors may accept or reject certain practices of the organization and thus decrease its legitimacy to exist or to perform the way it does. But this process is interactive and it needs to be stressed that the organizations’ perceptions of its environment are a key factor in the process of increasing its acceptance and legitimacy. Striving for legitimacy has the potential to make the organization adapt to structures or behavior that is based on its own, rationalized perception instead of the ‘original’. In this context, Meyer and Rowan (1977) speak of ‘rationalized myths’ that the organization adapts in the hope to increase its legitimacy. These myths are ‘rational’ because they are goal-oriented but ‘mythical’ because they are
less empirically grounded. To increase their legitimacy, organizations engage in imitative behavior occurring in a *mimetic process* where they imitate behavior and structures of others to improve their own performance but also, as I demonstrate in this study, to justify existing institutional beliefs and logics.

### 1.4.6 Institutional Isomorphism and Mimeticism

The fact that organizations become increasingly alike because they are mimicking and copying each other is studied by institutionalists as part of the larger framework of institutional isomorphism. ‘Institutional isomorphism’ emerged as a central concept of new institutional theory (Powell and DiMaggio, 1983; Scott, 1987) stating that organizations become increasingly alike because of coercive, normative, and mimetic forces.

**Coercive** forces refer to the regulatory dimension of an institution, where organizations become increasingly alike because they adopt structures or procedures that they are forced to adhere to because of laws and regulations. Here, the authority relations between organizations and especially the ability of public organizations rely on legitimate coercion, acknowledging the political dimension of institutions (Scott, 1987). For example, as most sectors are exposed to some form of governance by state or public institutions, the coercive force is crucial in explaining continuity and change of organizational fields. In this study, the state governance level for example exposes water works to coercive pressure by implementing stricter environmental legislation.

The **normative** force refers to the structures and procedures of an organization and how it accomplishes its tasks by conducting them in a certain manner (Scott, 1987). It is often defined through codes and norms of behavior that are developed and promoted by professional associations (Greenwood et al., 2002). This may entice the organization to adopt structures or procedures that are regarded by relevant actors as a legitimate standard but in fact their benefits may not even be empirically proven. For example, new management practices are promoted by the state and disseminated through professional associations in the public sector and become applied in public organizations, municipalities, and cities as the new way of ‘how things should be done from now on’.

There is a strong link between the process of adopting these new norms of behavior and the mimetic process of imitating behavior and norms of others. New norms rarely come out of a vacuum but they may exist in other organizations and merely are discovered and imitated.
Mimetic forces refer to the creation of shared conceptions among organizations in order to reduce uncertainty and increase their legitimacy (Scott, 1987). As a result, organizations mimic or imitate each other through making similar management decisions. Organizations and their managers engage in imitation because organizations must appear to be correctly managed and they do so by adapting management techniques that are collectively believed to be effective and rational (Meyer and Rowan, 1977). If they fail to do so, they may lose stakeholder support (Abrahamson, 1996). Often, new norms of behavior are created by adopting what is ‘currently fashionable’ (Abrahamson, 1996) to obtain legitimacy. For example, Lacity and Hirschheim (1993) documented how Kodak’s success with outsourcing its IT management triggered large scale imitation of the company’s outsourcing practices by other companies that continues presently, although there is lacking evidence that outsourcing leads to greater effectiveness and its performance improving effects are exaggerated. Where practices and behavior are imitated that lack empirical evidence of being performance improving, Meyer and Rowan (1977) speak of ‘rationalized myths’ because they are goal-oriented but ‘mythical’ because they lack empirical evidence.

Imitation may fail because it is a process of translation (Sevón, 1996) and thus, the outcome of imitation never fully resembles the practice, behavior, or object that has been the subject of imitation. Instead, the outcome represents a mere version of what has been imitated. Processes of imitating are at the same time processes of rationalizing (Sevón, 1996) because what spreads are not practices per se but edited versions of what happened (Sahlin-Andersson, 1996:83). Distributed by ‘editors’ such as consultants, researchers, the media, or simply by managers who are eager to learn and keep their eyes open, success stories are encountered and they turn into ‘recipes’ by being made ‘logical’ and they are often promoted by those who were not even present when ‘it’ happened (Sahlin-Andersson, 1996). As a result, the imitated private sector style of ‘managing’ is a rationalized version of what is in fact taking place in the private sector and hence, I consider it to a significant extent as being a ‘myth’.

Imitators usually lack first-hand knowledge of what they imitate (Sahlin-Andersson, 1996:80) and therefore it is understandable that public sector managers lack sufficient knowledge of the necessary ingredients that contributed to the successful private sector management practice. Successful imitation also requires innovation (Sevón, 1996) and if those who aim to improve by imitation would have sufficient innovative capacity to make the imitation a success, they would probably not have to imitate in the first place, but instead be imitated by others. Abrahamson (1996) points out the imitation of others and creation of myths may also happen because of a collective frustration that renders managers vulnerable to unrealistic hopes and makes them look for magical solutions that will relieve their source of frustration.
Mimetic isomorphism and imitation is not only used to improve effectiveness but to acquire stakeholder support by using rhetoric that are full of ‘fashionable’ phrases originating from the organizations that are perceived as more successful, in order to justify existing management behavior. For such cases, I have distinguished between the ‘altruistic’ form of imitation where public sector managers faithfully imitate in order to improve their organizations’ effectiveness and ‘egoistic’ imitation, where managers use the discourse of private sector management thinking to justify their existing management beliefs and decisions. I must also add that organizations sometimes only borrow or imitate from other organizations what is convenient and not the whole pattern that would be necessary for the imitation to work in its new context (Sevón, 1996).
2 Theoretical Foundations of the Study

I am primarily aiming in this study to increase the insights into the commercialization of water services. Therefore, this chapter represents a review of the current state of commercialization theories by proposing a theoretical framework within which the commercialization of local public (water) services can be studied. This framework is comprised of globalization and financialization theory; liberalization, privatization, and corporatization theory; theories of urban entrepreneurialism; and of commercialization (in public sector and public water services).

My approach is to study the different actors, their main issues and logics, and the interactional processes between these actors in order to explain the commercialization process and its outcomes. As this is the approach I take in the empirical analysis later on in the thesis, I am following a similar approach in discussing the theoretical foundations of this study in the present chapter by including a review of the actors, main issues, and processes that have been studied by others. Before I introduce the relevant theories in more detail, I present the theoretical framework that shall link the entire chapter together.

2.1 Introducing a Theoretical Framework for WSS Commercialization

In this subchapter, I propose a theoretical framework that describes how and where the commercialization of water supply and sanitation (WSS) has been studied so far, and which theories need to be combined in order to gain new insights on the phenomena of local public WSS commercialization. Figure 2-1 provides an overview of the theoretical framework of the study, comprising the different fields of theory that deal with commercialization of water services and public services in one way or the other. First, although they are separate theoretical fields and neither the main focus of this study, I combine globalization and financialization theories in order to represent my wider context.

The main emphasis in my theoretical discussion is contingent upon privatization, in order to show where the commercialization of water services has mostly been discussed and on urban entrepreneurialism, which I see as a major driver for water services commercialization. By presenting my theoretical framework I propose that globalization and financialization affect and create the process of urban entrepreneurialization, as well as the processes of privatization and corporatization. I regard commercialization as the outcome of these different processes. In this context, liberalization would also need to be discussed rather extensively, as it represents in many cases a prerequisite to privatization. Still, I will refer to it only briefly because liberalization did not occur in the Finnish water sector, where (at least in theory) private ownership of water utilities is and has been a possibility.
Referring to Figure 2-1, the theoretical fields are depicted within the boxes, and the text next to the arrows describes what each theoretical field has to say about the main actors (in italics), main issues, and how they are affecting other processes. Figure 2-1 is supposed to guide the reader through the entire theory chapter, as it also identifies the theoretical gaps (in grey boxes) that will be discussed at the end of the chapter.

In the subchapter below (2.2), I first shortly explain and define commercialization and commodification in order to provide the reader with a picture of the study’s theoretical focus (which is to build a theory of commercialization) while discussing the related theories. In subchapter 2.3, I briefly discuss globalization and financialization as it represents the ‘big picture’ of the study, in which the entrepreneurialization, privatization, and corporatization processes take place. Although privatization is not a focus of this study per se, it is discussed because much of commercialization literature (especially related to water services) is written in that field. The major part of the theoretical discussion is therefore dedicated to privatization, corporatization, and urban entrepreneurialization. I conclude the theory chapter with a paragraph on identifying the gaps in these theories, at which this study’s contributions aim.
2.2 Commercialization and Commodification Defined

Although often used as interchangeable terms, commercialization and privatization are two distinct concepts. I see commercialization as a process of increasing commercial interests and priorities in the operation of an economic activity, such as in the provision and production of water services or health care. Privatization, on the other hand, merely refers to a change in ownership structure. Thus, commercialization is an independent process although often linked to and caused by privatization. This distinction is important because this study investigates commercialization in absence of privatization and specifically argues that commercial priorities and interests are by no means restricted to private owners; public owners may hold them as well and operate their public services activities accordingly.

Having briefly distinguished between privatization (which is discussed in more detail below) and commercialization, I define commercialization as the process of introducing market mechanisms and market practices to markets, products, or services by subjecting them to commercial principles. Profitability or profit maximization may be part of commercialization, but it is not a condition. Non-profit organizations and public sector organizations, for example, may also be guided by commercial principles without having the goal of making profit but rather of recovering the full costs of their service. Commercial principles include financial accountability, risk management, contract-based management, performance measurement and benchmarking, and the principle of return on investment (or profitability). McDonald (2005) also mentions, as commercial principles in the context of water services commercialization, cost recovery and demand-driven investments and puts them in opposition to more traditional public sector operating principles, including (cross) subsidization (water services being subsidized via municipal tax) and supply-driven decision-making. However, I argue in this thesis that the need for cross-subsidization is, in fact, one of the drivers for local governments to commercialize their operations in order to finance the municipal services whose costs cannot be fully covered by tax increases. Therefore, commercialization in the context of water services includes a reversed notion of cross-subsidization, which means not only to stop subsidizing the service and operate based on full cost recovery, but, further, to operate it as a profitable service whose profits can be used to cross subsidize other municipal services.

When talking about commercialization, commodification needs to be mentioned as well. When a service that has not previously been associated with commercial use is subjected to it, one may speak of commodification. For the purpose of this study, I distinguish between commercialization and commodification by arguing that commercialization is a broader concept in which a set of commercial principles are applied to a product or service, with profitability a possible part. In commodification, on the other hand, products and services are subjected to the principle of profitability as the guiding principle. Studies on commodification span across all aspects of life, from the commodification of sports (Phillips and Hutchins, 2003), body parts in medicine (Seale, Cavers, and Dixon-Woods,
Studies on commercialization similarly include a wide spectrum of topics, such as the commercialization of academic research (Stein, 2004) or the water sector (Seppälä et al. 2001a). These studies have in common that they identify some aspect of globalization, financialization, privatization, or corporatization as drivers. Entrepreneurialization has been studied especially regarding universities adopting a more entrepreneurial thinking that leads to their commercialization (Ovetz, 1996; Vaira, 2004). Yet in the field of urban entrepreneurialism the effects on the commercialization of local public services still need more clarification, as will be explained in this chapter.

### 2.3 Globalization and Financialization

The discussion about public sector reform and the ever increasing role of the private sector in public service production has been going on since the 1980s, and scholars of different disciplines—including sociology, political science, urban studies, administrative sciences, and management sciences—have been writing about the effect of globalization on a variety of issues that relate to the changing role of governments and corporations. Writings include the privatization of water services (e.g. Weizsäcker, Young, and Finger, 2005; Hall and Lobina, 2006; Hukka and Katko, 2003a), the rise of professionalism (e.g. McDonald, 2005; Greenwood and Hinings, 1996), the rise of managerialism in public services (e.g. Pollitt, 1993), globalization in public administration (e.g. Farazmand, 1999), entrepreneurialism in the public sector (e.g. Harvey, 1989), glocalization of city management (Czarniawska, 2002a; 2002b), the rise of the global city (e.g. Castells, 1989; Sassen, 2005) and the financialization of corporations (Tainio, 2003).

These writings have in common that they describe sub-processes of the globalization process and deal with outcomes created by policies associated with neoliberalism (Fourcade-Gourinchas and Babb, 2002). In this context, I understand neoliberalism as a set of economic and political principles that aims at reducing or keeping the state’s role to a minimum, promoting free market methods instead of state intervention, and opening overseas markets to global trade. Globalization is therefore to large extent a result of neoliberal policies and it can be defined as a process of continuing capital accumulation in modern capitalism. Besides neoliberal policies, globalization has intensified due to the collapse of the Soviet Union, the diminishing borders of capital transfer, the availability of modern technology (Farazmand, 1999; Giddens, 2000; Castells, 2000) and the opening of China starting in the 1980s (Harvey, 2005). Production and finance have become flexible and global, which makes the economy seem increasingly exogenous and uncontrollable (Piore and Sabel, 1984; Castells, 2000; Fourcade-Gourinchas and Babb, 2002). In an economy that is perceived as uncontrollable, capitalists are part of a reciprocal process where they are dominated by their environment but also shape it (Harvey, 1989).
These macro-economic processes of globalization also spill over into the local governance level, where they become relevant for the provision of local services and create the ‘global village’ (Garcia-Zamor and Khator, 1994) through the process of ‘glocalization’ and entrepreneurialization (Harvey, 1989). That process had been observed, for example, by Finger and Allouche (2002) in their analysis of the role of multinational companies and the World Bank in the privatization of water services across the globe. Lending policies by international institutions such as the World Bank are decided on the macro-level but translate into the local level as they become adopted by local actors. For example, Morgan (2006) argues that the present ‘water welfarism’ (where private investments are mixed with public aid that is connected to loan-conditions) leads to commercialization, driven by the few large multinational water companies and international lending institutions such as the IMF (International Monetary Fund) and the World Bank. These public-private partnerships are mainly focused on developing countries and they have been increasing from almost zero in 1990 to close to 400 in 2000 (Finger and Allouche, 2002).

With the increasing flow of goods and capital across market economies, companies are competing on a global scale for the investor’s attention and capital. Capital has turned global, disconnecting it from territorial finance (Farazmand, 1999; Scholte, 1997). With this new wave of globalization, the 1990s were characterized by a ‘financialization’, i.e. shareholder activism and the rising significance of shareholder value that forced managers to restructure their companies and put more (or primarily) emphasis on the return of investment (Tainio, 2003; Williams, 2000). A similar process took place in the public sector, where the state and its entities (such as municipalities) are increasingly required to exercise budgetary discipline and implement more effective systems for cost and resource control. In Finland, as in other member countries of the European Union, this process has been accelerated by the stability pact criteria upon the introduction of the EURO as common currency and by a general need for consolidating public sector finances. As a result, maintaining the financial balance of the public sector and its entities has become a priority for many governments, including Finland. As I will demonstrate during my analysis of the managerial logics of local government, maintaining the overall balance of the budget forces municipalities to put more emphasis on the return of investment of their own operations as well as on restructuring the municipal organizations in ways that create financial and structural benefits from a budgetary point of view.

Globalization and financialization has been facilitated by key events such as the collapse of the Soviet Union, or certain key innovations such as the Internet; but as a process, it requires and contains actors that try to affect their environment and the process according to their interests. Most research has focused on ‘the usual suspects,’ such as multinational corporations, international financial institutions (such as the World Bank or the IMF), and some key nations, including the US, France, and Great Britain. Some scholars argue that global corporations and investors represent an elite, powerful enough to cause the
collapse of economic regions, stock indices, and currencies—and that they have proliferated and became influential forces on a global scale in affecting their environment (Dicken, 2003; Harvey, 2005). As an example of investor power and global trading and investment activity, the volume of financial transactions in international markets increased from $840 billion in 1983 to $40 trillion in 2001, although $800 billion would be sufficient to sustain international trade and productive investment flows (Dicken, 2003).

Financialization is relevant for water services and public services in general as the financial community increasingly targets water services as appropriate investments, and for which the exposure to global capitalism is only a recent experience. For example, the stock price of the five publicly traded water companies in the UK had approximately tripled during the years 1999 to 2001 before it returned to its previous level. The news agency Reuters reported on 18 September 2006, that “in the absence of a futures market in water, speculators have bought shares in utilities and water-related companies such as Waste Management, ITT Corp., American States Water and Suez, expecting them to profit from intensified efforts to tackle water scarcity.” Several stock exchanges have water investment indices by now and for example over the past ten years, the Media General water utilities index has outperformed the Dow Jones Utilities Index by double. Investments have been placed directly into privately and publicly held water companies all over the world and become managed in investment funds that focus on the water industry and bet on the rising value of water as water shortages occur more often and infrastructure becomes outdated. In the UK where most water utilities are privatized, the financialization of water services is also demonstrated by the increasing number of investment bankers on the executive boards of UK water companies (Näsi and Windischhofer, 2005).

In particular, accounts like the abovementioned—about the interest of global capitalists in local water services—create serious concern and resistance among citizens and consumer interest groups, and often are in the focus of civic movements and corporate-watch sites against privatization and commercialization. Because of citizens’ concern about globalization and its outcomes, organized civic activism has been proliferating. Here, the Internet especially has enabled interest groups all over the world to connect and share their concerns, as, for example, expressed in the research and opinions published by organizations such as Globalalternative.org, Corpwatch.org, Alliance for Democracy.org, Citizen.org, or The Democracy Center. However, I would like to point out that these organizations direct their attention mostly towards the private sector and international organizations that are associated with promoting neoliberal policies, such as the World Bank, the World Trade Organization, or the International Monetary Fund, while my investigation into the commercialization of water services in absence of ‘the usual suspects’ will demonstrate that the local government and its increasingly commercially-oriented conduct deserves a watchful eye as well.
As discussed above and as shown in Figure 2-1 at the beginning of this chapter, globalization and financialization contribute to the commercialization and commodification of goods and services that were previously mainly social or public goods and services (such as water supply and sanitation) via entrepreneurialization and privatization/corporatization. Therefore, the following sub-chapter will review privatization and corporatization before turning to entrepreneurialization.

### 2.4 Liberalization, Privatization, and Corporatization

Before privatization and corporatization are discussed, a brief basic definition on the two concepts as well as on liberalization will be provided. I will mention liberalization only in a short paragraph because it is not subject to this study. This is because in Finland any kind of ownership and management option regarding water services has been available in theory (although in practice, there is no private corporate ownership of water works).

#### 2.4.1 Basic Characteristics and Distinctions

Liberalization is usually a prerequisite for privatization, and it can be defined as the introduction of competition to sectors which previously were characterized through operators with exclusive or special rights and where it is possible not only in theory but also in practice to have various forms of different ownership. In this context, unbundling is the activity to separate true monopoly activities from such activities for which competition can be generated. For example, the network of a water utility represents a monopoly function because it is almost impossible for different producers to lead their water into the water network due to water quality concerns and negative consequences on the infrastructure itself. However, the construction of networks and pipelines can be put under competition as well as laboratory services, meter reading, or even the operation and maintenance of water and wastewater treatment plants.

Before entering a more detailed discussion about privatization and corporatization, I would like to distinguish between these two concepts. Corporatization is defined by Carew (1996) as changing the structure of a public entity so that it operates on business lines, with a mandate to trade profitably and an obligation to be accountable to the government for its financial performance. When the public-owned service producer transforms into a commercially-oriented enterprise (without changing ownership or management), the citizens become subjected to commercialization although the service producer is still owned and operated by the public entity. As a result, commercialization can take place disregarding whether privatization takes place or not.

Privatization, on the other hand, can be defined as transfer of ownership and assets from a public-owned entity to a private entity or individual, who may not necessarily pursue commercial interests with the asset that has been acquired. Suppose an unprofitable railway connection is sold by the public railway company to a private club of railway enthusiasts which maintains and operates the necessary infrastructure, locomotives, and
wagons. The new operators may not necessarily (and probably rarely do) operate the railway connection under principles of commercial viability. On the other hand, a public-owned enterprise such as a Finnish municipal water works may be operated under strict commercial criteria and with profitability levels well beyond the rate of return generated by private operators of water utilities in England and Wales (Näsi and Windischhofer, 2005). Hence, commercialization may take place without privatizing assets from a public into private ownership, and privatization does not lead to commercialization per se, either.

2.4.2 Privatization

Privatization literature is discussed here because it is where commercialization of public services is usually studied. The subchapter is divided into the main issues in privatization literature that explains its different forms, regulatory, and efficiency issues, and the subsequent part describes the main actors, processes, and outcomes that are studied in this body of literature.

2.4.2.1 Main Issues in Privatization and its Literature on Water Services

Most of the previous studies about the commercialization of water services have focused on the role of the few dominating, globally active private water and multi-utility corporations such as the French Suez and Veolia, as well as the role of international institutions such as the World Bank and the International Monetary Fund. For example, Finger and Allouche (2002) studied the role of these multinational corporations and the World Bank in the privatization of water supply on a global level, concluding that they are part of a much wider change in public sector and infrastructure reform in finance, construction, and operation. There exists a significant amount of commercialization literature that regards commercialization as the outcome of privatization, while commercialization in absence of privatization has received fairly little attention.

Privatization as a concept can be distinguished into three different types (Vickers and Yarrow, 1991:112), which comprise 1) the privatization of competitive firms, i.e. firms that operate in markets free from substantial market failures; 2) privatization of monopolies, i.e. transfer of state-owned enterprises with substantial market power; and 3) outsourcing of services contracts, i.e. where long-term contracts are established instead of selling assets, and where the rights to profits are transferred to the private operator. Concerning type three, Vickers and Yarrow (ibid.) consider outsourcing a quasi-privatization because they regard the rights to residual earnings as central to what is meant by ‘ownership’. However, for type three there are still more issues to consider; for example, regarding investment decisions, where the private contractor may have the right to residual earnings but the public entity that owns the assets still makes the investment decisions and is responsible for financing them.
Probably the two most frequently asked questions in privatization literature are whether privatization has performance-improving effects on the organization, and how to effectively regulate privatized organizations that operate in monopoly markets, such as energy and water utilities. Vickers and Yarrow (1991) suggest that private ownership has efficiency advantages under competitive conditions but not necessarily under monopoly conditions, and that under competitive conditions, government ownership is not inherently less efficient than private ownership. Parker (2003) provided an extensive review on studies that investigated whether privatization can improve performance without coming to a clear conclusion whether it does or does not. Based on the choice of measures and timeframe, studies may reach rather different conclusions about the same industry. For example, Shaoul (1997) argues that based on main performance measures, greater efficiency gains occurred in the water industry in England and Wales prior to privatization, while Saal and Parker (2000; 2001) concluded that efficiency gains in the water industry in England and Wales were greater after privatization, but as mainly linked to regulatory tightening in 1995 after lax regulation since the privatization of the sector in 1989.

Parker (1999, 2003) also provides an extensive overview of regulative problems connected to the control of private monopolies and the high transaction costs that incur due to conflicting interests between the private water utility owner and its customers. While the water utility’s main objective is to create profits for shareholders, the society’s interest is to have high standards of service delivery. In competitive markets the behavior of the service provider is regulated through the consumer’s option to switch providers and therefore punish the non-performing provider. In a private monopolistic market, the public regulator has to take over this control function. However, these oversight functions bear significant principal-agent conflicts due to the information asymmetries borne by the management’s insider knowledge of operations and the regulator’s dependence on full disclosure. As a result, several authors argue for a careful approach to privatizing water services. Finger and Allouche (2002) point to the risks of private monopolies and call for concentrating on establishing effective regulatory authorities in the countries concerned. Hukka and Katko (2003b) came to the conclusion that private water services are proliferating despite doubts of their higher efficiency compared to public water services, and that they pose a threat to the interests of consumers, especially when not sufficiently regulated.

Establishing a regulatory agency that supervises the economic business conduct in water utilities has also been regarded as a prerequisite to privatization. Private ownership and capitalism need a strong state and a stable environment to prosper (Weber, 1947; Farazmand, 1999), which can be facilitated by coordinated state action and the establishment of a regulatory agency. The modern state has the role of safeguarding the efficiency of the market through protecting the system from collapse and providing safety nets for promoting capitalist development (Lindblom, 1990; Farazmand, 1999) and the lack of such order represents an obstacle to private sector capitalists. In an unregulated
monopoly market, governance is exercised through ownership and supervision, connected by having public-owned water utilities that are governed by public institutions and the democratic system. It would be rather difficult to have private water utilities in Finland as long as an effective regulatory agency is not in place.

In the context of privatizing public monopolies, Williamson (1987:33) noted that “we can only choose between three evils: private unregulated monopoly; private monopoly regulated by the state; and public monopoly”. This taxonomy indicates that previous research mainly focused on the commercialization process that is caused by privatization and it attributes commercialization to privatization while commercialization through the public owner remains unacknowledged. However, since Williamson’s statement was published in 1987 the public sector has become more entrepreneurial (as the paragraphs below will discuss), and I argue that Williamson’s taxonomy needs to be updated and acknowledge the rise of the commercial, public-owned monopoly. It is not sufficient for this new organizational archetype to be supervised and regulated through the democratic system; instead, a more formal regulation as it is usually applied to monopolies under private ownership is required.

Besides the risks of privatization, there is agreement among scholars that the private sector has an important role in the production of water services and that this role needs to increase. In this context, it is usually suggested to involve the private sector through outsourcing of public services and by initiating public-private partnerships (PPPs) (e.g. Katko, 1991; Hukka, 2003; Seppälä, 2001). In this case, public management concepts, coming from the private sector, are deployed, and it is assumed that outsourcing and PPP are viable solutions for increasing public sector efficiency and quality of service delivery.

2.4.2.2 Privatization as Process of Actors, Issues, and Outcomes

Although the literature on privatization is vast, the role of local actors in the privatization process has received fairly little attention and most studies focus on macro-level analysis and ‘the usual suspects’ such as the World Bank, the International Monetary Fund, single private corporations, and government policies (see e.g. Finger and Allouche, 2002; Katko and Hukka, 2003b). Besides numerous journalistic reports on the lobbying efforts of multinational corporations, international organizations (e.g. the World Bank and International Monetary Fund), or national governments (such as France, the US, and the UK), there is little empirical research about the dynamics of the privatization process on the local level.

Duncan and Bollard (1992), in their book about corporatization and privatization, assume that the process is planned and policy-driven and takes place in progressive stages, such as government departments first being corporatized before they are finally privatized. This description gives the impression as if privatization (and corporatization) were a planned transition. There is, of course, this possibility of a managed transition, such as in the water sector reform taking place in Australia in the 1990s that was a transition from a
municipality-owned, locally managed, fragmented water sector to a state-owned and managed, regionalized water sector (Martin, 2004). However, even the privatization of the water industry in the UK in the late 1980s has been argued to have been an ‘accident’ that was facilitated by a favorable constellation of actors at the time, rather than a carefully planned and managed transformation (Maloney and Richardson, 1994).

Where state coordination is lacking, as I will argue to be the case in the Finnish context, corporatization takes place in a particularly unplanned manner and with unintended consequences. As an example of how chaotic a transition can be, Carty (2003) provided an interesting journalistic account of a privatization process in the City of Hamilton, Canada. The city and its water utility started out with plans to become a public-owned, international player in water supply and sanitation and ended up as private-owned company, by changing ownership five times in eight years and with numerous accounting scandals during the process. Another example where a water utility finally ended up unintended in private ownership is reported from Sweden (Gustaffson, 2001), where the city of Norrköping corporatized and merged its water utility with its energy utility in 1997 and subsequently sold a 49 percent minority stake to Sydkraft, a majority-controlled subsidiary of the German energy company EON. A few years later, the municipal council decided to sell all its shares to the company in the year 2000, although local citizens protested against the privatization and sell-off of their energy (and also water operations) to a private company.

As can be seen from these examples, privatization can be, and often is, the last step in a process from public utility department to corporatized utility enterprise to, finally, a privatized utility. Therefore, corporatization and privatization are linked processes and the following subchapter will discuss corporatization in more detail.

2.4.3 Corporatization as Process of Actors, Issues, and Outcomes

Duncan and Bollard (1992) described the corporatization process as a step towards more independence of the enterprise from public decision-making and more private sector style professionalism. In their argument, corporatization is also considered a transitional stage in the transformation process from public ownership to private ownership. Whether the independence of a public-owned entity increases with its corporatization, however, cannot be taken as a given, and neither can the argument that corporatization is followed by privatization per se. Also Smith (2004) argues that corporatization is not necessarily a precursor to privatization because cost recovery methods, more professional management and higher operational efficiency employed by the corporatized entity may be sufficient to achieve increased efficiencies.

Globalization and commercialization as a result of privatization is a fairly well-researched area, especially when it comes to water services and other infrastructure-related public services (see e.g. Weizsäcker, Young, and Finger, 2005; Hall and Lobina, 2006; Hukka and Katko, 2003a). Studies that investigate the globalization and
commercialization of public services in the absence of privatization are rare; in particular, accounts about specific actors and their roles in these transformation processes are missing. However, Smith (2004) investigated the corporatization process of water utilities owned by their local government in low-income communities of South Africa. By reviewing how the process of corporatization has transformed public sector management, she argues that this process emerged from a second wave of neoliberalism, but she remains unclear about the specific actors that were involved in the process. She further argues this corporatization to threaten to undermine the democratic accountability of local authorities due to a higher independence by the utility engineers, who can use the rigid cost control mechanism to shield themselves off from political interference. Smith’s conclusions and the ones that I will draw in my thesis contradict each other in the sense that she attributes the loss of accountability to the utility management while I instead identify the municipalities’ management to have a similar role. But I see this contradiction as most likely caused by a difference in the empirical context and the fact that providing safe access to water and sanitation is in Cape Town still a greater priority than in Finnish cities, and the engineers may have greater influence on operations while they need to be rapidly extended. In the Finnish case, the number of connections to water and wastewater are fairly saturated and concerns for operational efficiency have been dominating for the past decade, which puts more emphasis on cost control, efficiency, and profitability.

Further, Finnish municipalities are increasing their influence over their utilities as a result of their entrepreneurialization, and in Smith’s case, it is possible that these low-income communities around Cape Town are not yet entrepreneurialized (although the City of Cape Town may well be) to the same extent as the larger Finnish cities. Smith (ibid) also argues that local government is a suitable regulator for local services, which I can only agree with when speaking of a phase of service production where the social aspects of the service are still the major concern (for example, when a large share of the population is still without safe access to the service) and the commercial interests of local government have not become a priority yet. But once that changes—and increasing the access to water supply and sanitation is not a priority anymore—commercial interests may become strong enough to dominate social concerns. Thus, a third party as regulatory agency may be required.

Another study about corporatizing water services is provided by Martin (2004) about corporatization as a means to improve water quality in Victoria, Australia. In this study it is argued that a ‘professional and forward-looking water industry’ was the outcome of a coordinated government effort. The government of Victoria undertook the reform of local water services in the 1990s due to a high fragmentation of the industry, poor accountability, declining infrastructure, the lack of a strategic approach to infrastructure development, and the lack of water quality (Martin, ibid.). Martin describes how local government was disentangled from local water services management and the utilities were merged and expected to have a clear commercial focus, with the only shareholder
being the Government of Victoria. The Victoria case study provides several parallels to the Finnish context in terms of the state of water services and increasing risks of service failures, underinvested infrastructure, and lack of strategic approach. However, the difference is that this corporatization in Victoria represents a coordinated transition with the state as the key actor while in Finland the state has taken a passive role in terms of large scales reform efforts and leaves the reform up to local government. Further, Martin’s account leaves out a more detailed description of which actors initiated the transition or participated in it.

Corporatization puts ‘bureaucrats into business’ (Shirley, 1999) and according to public choice theory, it may ‘allow public managers, bureaucrats and politicians to use their control over public-owned enterprises to further their own interests rather than the state firm’s efficiency’ (Shirley, 1999:117). The previous discussion may give the impression that my study supports the argument of public choice theorists such as Niskanen (1971), who argues that the self-interested behavior of public officials harms the citizens’ interests. As a result, neoliberals use public choice theory to argue that private firms could do the job at least as good as the public sector. However, I would like to note that I regard the arguments of public choice theory as seductive but too simplistic to apply to this study. Regarding the self-interested behavior of public officials and public managers, I found quite the opposite to be the case, because the entrepreneurialization of local government and the commercialization it causes are not the result of public sector managers and officials acting in self-interested behavior per se but they believe to act in the interest of their organization and constituencies, which are their local citizens. Second, as Vickers and Yarrow (1991) have stated, it is the question of market imperfections (such lack of competition) that determines the efficiency and effectiveness of organizations. Since the public sector is in charge of most tasks that have no ‘market’ or for political, economical, societal or ethical reasons should only be exposed to competitive forces as little as possible (such as high school education, hospitals, and national defense), it gives the impression that public sector organizations are less effective than private ones.

This is also a crucial question to consider when privatizing water services, which are natural monopolies. As a monopoly, the possibility to gain efficiency by privatizing well-managed public sector water works may be rather insignificant. The keyword here is ‘well-managed,’ which is one of the major reasons for public sector organizations to establish their business units as enterprises by corporatizing them and adapt private sector management principles, tools, and ideologies that should lead to more effective management. Higher flexibility in operational activities, more accountability for management regarding quality and financial benchmarks, and professional conduct of business and procedures are the ends which the public sector desires and for the past two decades, corporatization was seen as the means to achieve them. But as the following paragraphs about the entrepreneurialization of government and especially local government will show, a “second wave of neoliberalism” (Smith, 2004) has emerged
where the public sector tries to achieve these aforementioned ‘ends’ in operations across its organization – also in its administration and in those units that do not belong to its business operations. The entire local government organization is supposed to think and act increasingly in a more entrepreneurial fashion, as I explain in the paragraphs below by reviewing the literature on urban entrepreneurialism and theories of local government entrepreneurialization.

2.5 **Urban Entrepreneurialization**

In principle, entrepreneurialization refers to a change in the thinking of public sector managers towards a more pro-active, empowered, and entrepreneurial attitude towards management. Urban entrepreneurialism studies the entrepreneurialization of cities and local government in general. Therefore, most writings on the subject can be found across the disciplines of urban geography, regional studies, and administrative sciences. The following paragraphs will discuss the contents of urban entrepreneurialization as a concept.

2.5.1 **Basic Characteristics of Urban Entrepreneurialism**

One of the most influential books on the transformation of management thinking in the public sector, written with the objective to infuse a ‘new entrepreneurial spirit’ into the public sector, was Osborne and Gaebler’s (1992) book, ‘Reinventing government – How the entrepreneurial spirit is transforming the public sector’. As the authors argued, the US public sector on all levels is moving towards competition; measurement; outcome, market, and customer orientedness; empowerment of its units and employees; and is using the private sector for public service delivery. Here, the entrepreneur is understood as someone who ‘uses resources in new ways to maximize productivity and effectiveness’ (Osborne and Gaebler, 1992: xix), and the entrepreneurial organization is habitually trying to maximize the effectiveness of its resources. Osborne and Gaebler (ibid.) argue that many of the private sector principles and management techniques are transferable to the public sector and would enhance its effectiveness. While their book deals with the positive effects that entrepreneurial and empowered thinking and acting can have on all levels of government and all kinds of public sector organizational archetypes, there has also been extensive criticism of the entrepreneurial turn of government, especially local government.

Harvey (1989) has been one of the most prominent critics and argues that the local government’s entrepreneurial turn serves the interests of private sector capitalists and contributes to a commercialization of the public realm. Harvey (ibid.) calls the local governments’ entrepreneurial-turn municipal entrepreneurialism and identifies globalization as the root cause of it, where capitalist elites are looking for new investment opportunities by promoting privatization and commercialization. Harvey’s notion, that the commercialization of local governance is a result of the larger globalization process is very much in line with Castell’s (1989; 1996) argument that globalization is affecting
local governments, as they are trying to attract and direct global resource flows (especially those of capital and investments) to their local territories. As a result of globalization, the phenomenon of local governance entrepreneurialization appears in municipalities around the world, although in locally-flavored, ‘glocalized’ variations (Czarniawska, 2002a). With the adoption of private sector management principles and the financial pressures local government is facing, municipalities are trying to ‘save money’, to ‘make money’, and to achieve ‘customer satisfaction’. Hence, local governments have started to apply commercial principles in evaluating the outcome and effectiveness of their work. Also in Finland, the public sector’s turn towards market-oriented reform that has been a rather ongoing process since the early 1990s has been noticed for example by Filander (2003) who points out that the municipalities have been introducing a more ‘effective’, entrepreneurial, and private sector oriented way of managing their affairs that also meant for public servants to transform their identities.

Harvey’s writings on the role of urbanization and urban change in the transformation of advanced capitalist societies have provided the foundation for what could be called the subject of urban entrepreneurialization (Wood, 1998) and for a theory of what Harvey himself calls ‘a theory of uneven geographic development’ (Harvey, 2006). Urban entrepreneurialism describes the reorientation of urban governance from a predominant managerial approach in the 1960s (especially in the US although emerging later also in other advanced capitalist societies) to a more initiatory and entrepreneurial form of action in the 1970s and 1980s (Harvey, 1989).

As Harvey (1989:1) has pointed out, ‘urban governance has become increasingly preoccupied with the exploration of new ways in which to foster and encourage local development and employment growth and ‘such an entrepreneurial stance contrasts with the managerial practices of earlier decades which primarily focused on the local provision of services, facilities and benefits to urban populations’ (Harvey, ibid:1). For Harvey (ibid.), municipal entrepreneurialism is an attitude to management with a focus on growth and ‘boosterism’ that may require a visionary figure to take the lead (e.g. a major or a private sector entrepreneur). This municipal entrepreneurialism focuses on public-private partnership where the local public side absorbs risks while the private side absorbs the benefits, a relationship that describes private sector’s risk adversity. Urban entrepreneurialism as a concept also refers to cities’ and local governments’ supply-side oriented strategy that prioritizes business investment, cost competition, and fiscal conservatism through centralizing financial controls and benchmarking its own departments to the private sector and to departments of ‘competing’ cities. Demand-side strategies that could aim at improving competitiveness through investments in education, training, and social infrastructure are under-emphasized (Kipfer and Keil, 2002).
I agree with Harvey (1989; 2006) that the entrepreneurialization of local government has increased and that urban entrepreneurialism is the extended version of urban managerialism. ‘Managerialism’ refers to the adaptation and use of private sector management principles in public sector contexts, possibly in an excessive manner and by lacking the necessary understanding these principle’s usefulness and appropriateness. As an extended version, urban entrepreneurialism is managerialism ‘plus’ the ideas and language of the entrepreneur’s empowerment, can-do attitude, vision, and initiative. In this context, Filander (2003) points to the shifting identities of public servants as a result of the change process, where they perform a balancing act between adopting new, managerial behavior while at the same time trying to preserve who they were before the time of ‘market-oriented individualism’. However, my closer inspection of the notion of ‘market-oriented individualistic’ municipal reform in the following paragraph provides a more differentiated picture on market-oriented reform and its individualistic or collectivistic aspects in order to better understand the logics and actions of municipalities.

2.5.2 Municipal Individualism and Market-Oriented Individualism

Reviewing these writings, one may get the impression that the transformation process in local government was a transition from earlier, more citizen-oriented and collectivistic times to market-oriented individualistic times (see for example Filander, 2003). But while I agree with contrasting market-oriented and citizen-oriented municipal strategy and thinking, I am challenging the notion of contrasting individualistic with collectivistic in this transition, especially relating to the transformation and reform of local government.

I am arguing that the municipalities’ turn towards market-oriented individualism needs to be seen in context of the inherent individualism of local government. I argue that one of the major reasons for local government being inherently individualistic (expressed in local government’s lack of cooperation among each other) is that historically, local government boundaries did coincide more with the zones of urban labor and commodity markets or infrastructural formation during the agricultural and industrial age than since the emergence of a knowledge society during the 1980s and 1990s. The state also promoted that individualistic logic by transferring funds to individual municipalities, which were then able to organize local public services to a large extent individually instead of cooperating more extensively.

Thus, when ‘market-oriented individualism’ is put in context with the change process of local government and its entrepreneurialization, the novelty in this phenomena is rather its ‘market-orientedness’ than its ‘individualism’. Local government is characterized by an inherent individualism and new, entrepreneurial discourses are rather used to justify that particular individualism (and may also have a reinforcing effect on it) – but market-oriented reforms to not produce individualism per se. In fact, cooperation among local governments is a key element of market-oriented reforms that emphasize the regionalization of local government and public services. Relating to the intensified emphasis on cooperation, Brenner (2003; 2004) provided an account of the changes in
urban governance and metropolitan institutional reform in Europe that specifically refers to urban regional governance and how it has changed since the 1960s. By reviewing cases of large-scale urban agglomerations in Europe (such as London, Hamburg, or the Ruhrgebiet) he argues that since the early 1990s a competitive regionalism has emerged where cooperation among local governments of a region has been promoted by the state in order to enhance regional economic development.

Van Gramberg and Teicher (2000:476) explain that in urban entrepreneurialism, ‘public servants have their roles transformed to managers and the public to customers,’ but this new empowered managerial style may also contain a paradox, as the empowered, new public manager faces intensified government interventionism that, for example, tries to initiate more regional cooperation among municipalities. The rationale behind this regionalization trend can be found in Harvey’s (1989b: 1953) writings, who argues that “local government boundaries do not necessarily coincide with the fluid zones of urban labor and commodity markets or infrastructural formation. […] Local jurisdictions frequently divide rather than unify the urban region, thus emphasizing the segmentations (such as between city and suburb) rather than the tendency toward structural coherence and class-alliance formation”. Krätke (1999:696) connects regionalization with urban entrepreneurialism and explains that “the political-administrative authorities of the region are no longer content to offer business activities a suitable spatial framework containing good infrastructure equipment. They also seek to initiate entrepreneurial activities themselves.”

Cooperation is needed in these reforms in order to achieve efficiency gains in local services production and therefore I argue in this thesis that market oriented reform is characterized by collectivistic ideas to improve the sustainability of the region instead of a single municipalities. In Finland, the emphasis on extensive cooperation among local government has emerged during the time of market-oriented reforms of the 1990s and has intensified during the 2000s, and although the state’s policy is to promote cooperation among municipalities and inspire a kind of ‘market-oriented collectivism,’ I am going to demonstrate in this thesis that the outcome of the municipalities’ entrepreneurialization process is market-oriented, but also still individualistic.

2.5.3 Urban Entrepreneurialism as Process of Actors, Issues, and Outcomes

As Harvey (1989) points out, entrepreneurialization is a process where municipalities became more initiatory and entrepreneurial first in the UK and US, in the 1970s and 1980s due to reforms that redistributed tax and reduced the flow of federal or state income to local government. With less income, local governments become more active in attracting tax revenue themselves through a combination of raising taxes and attracting new tax payers, foremost businesses and entrepreneurs, to their area. Cities are competing with each other for the attractiveness as locations for tax payers. Thus, their ability to raise taxes is limited as it may decrease the competitiveness of the city through falling back in benchmark rankings that compare tax rates and costs of other municipal services
such as energy or water. Stimulating the city’s income through increasing the tax base is chosen over increasing the tax rate, as much as feasible. As a result, even without government interventions in the form of large-scale legislative changes, the decrease of state grants to local governments and inter-urban competition are sufficient to become external coercive forces over individual cities that bring them closer into line with the discipline and logic of capitalist development (Harvey, 1989; Wood, 1998). As Harvey (1989; 4-5) says further, ‘this consensus seems to hold across national boundaries and even across political parties and ideologies’.

Urban entrepreneurialism can also be regarded as a process of actors, such as investors and businesses that are seen as ‘transnational migrants’ and become forces in urban politics and the municipal arena (Sassen, 1998). These often nationally or even globally migrating actors are attracted by the city and participate in round-table discussions and interactions with municipal key persons that are responsive to their ideas in the hope of increasing the competitiveness of the city (Harvey, 2006). Through these processes, transnational migrants contribute to the glocalization process of the city. Harvey (1989:11) points out that ‘the task of urban governance is, in short, to lure highly mobile and flexible production, financial, and consumption flows into its space.’ This argument is in line with Castells (1989; 1996) who says that the modern network society is not constructed of spaces anymore, but rather of flows between spaces, such as information flows, capital flows, flows of symbols, or flows of sound. These flows are purposeful, repetitive, and programmable exchange relationships between spatially disjointed actors. The competitiveness of a city in the global age depends on its ability to attract the flows of capital, meaning, and symbols that are important to it and it increasingly engages in attracting these flows based on its own initiative.

Attracting new business and investments brings up the question of the role of these transnational and national migrants, and how they become relevant for the local level and decision-making. In this context, the role of actors as elites and their power to change the system and promote commercialization through privatization has been discussed by Harvey (2005). He assigns significant power to actors such as companies, organizations, and private individuals. Harvey (2005; 2006) argues that the main motivation for the financialization through opening of world markets and public sector reform was the top one percent income earner’s need for new income growth. This need for income growth, according to Harvey, could only be achieved through opening new markets and privatizing large portions of the public sector. Thus, Harvey explains the ‘neoliberal turn’ with the elites’ desire to restore its class power. He also asserts a key role to in the collapse of economies to hedge funds, which again, are often managed by individuals (Harvey, 2005).
Regarding the local level, Harvey could not offer more specific arguments and proof how relevant these global ‘capitalist’ migrants are for the local level. But the lack of evidence in this matter is especially a shortcoming for Harvey’s arguments regarding the entrepreneurialization of local government and its exposure to private sector ‘capitalists’, since most of his arguments about the influence of private actors are derived from a macro level analysis and empirical evidence from the local level is insufficient. This is understandable, considering that in scientific research it is difficult to get access to the elite circles that would be able to clarify the circumstances.

Contrary to Harvey, Stiglitz (2002) has more trust in the functioning of governance frameworks and rejects the idea of small elites of private sector actors are powerful enough to cause change that would primarily serve their own interests. He argues that a broad consent in the financial community as to what constitutes appropriate rates of return and economic activity are the drivers for capitalism, neoliberalism, and privatization. According to Stiglitz (ibid.) the United Nations affiliated agencies such as the International Monetary Fund (IMF) merely reflect the interests and ideology of the Western financial community. Harvey and Stiglitz regard the spread of neoliberalism and capitalism as a manifestation of the increasing power of capital over labor and assign a key role to institutional actors whose goal is to support the world’s hegemonic power, the US. Contradictory to that argument, those who work to promote the set of neoliberal policies (e.g. reliance on market forces, privatization, opening markets, diminishing boundaries for trade and capital) argue that these neoliberal policies simply work better than other policies (Fourcade-Gourinchas and Babb, 2002).

Useem (1984) conducted a study on the power of private sector elites that provides a perspective that stands somewhere between Harvey’s and Stiglitz’ approaches. Based on extensive empirical research, Useem argues that business elites are drivers of free-market policies and liberalization but that they do not merely act based on their individual self-interest. Instead, they represent class-wide business interests. These class-wide interests are ‘involving considerations that lead to company decisions beneficial to all large companies even if there is no discernible, direct gain for the individual firm’ and for most part they have evolved without conscious design (Useem, 1984:5). This means that the influence of elites exists but it develops in a more unplanned manner and outcomes are difficult to be directly associated with certain actors but they are rather a result of class-wide action based on values and beliefs that develop over time.

To summarize these arguments of Harvey, Stiglitz, and Useem, the role of actors in the commercialization of the public realm has mostly been investigated from a macro-economic perspective and lack empirical data collected at the local level. Therefore, it is hard to say whether private sector ‘capitalists’ are acting consciously, self-interested, and are successful with it (as Harvey argues); whether it is the broad consent of the financial community that drives the commercialization (as Stiglitz explains); or whether private sector elites are in fact powerful enough to affect the system but they do it because of
class-wide interests that evolve over time without conscious design and rather unplanned action (as Useem argues). In any of these cases, the role of private sector actors in the commercialization of the public realm has been the main focus, while the role of government as actor has been somewhat neglected. Regarding the levels of analysis, there is more information relating to the global and national governance frameworks and how private sector actors interact with them, while the local level has not received sufficient attention.

To conclude my discussion about urban entrepreneurialism, I would like to discuss some gaps in that theory based on my own arguments and on those of others. In his review and assessment of urban entrepreneurialism, Wood (1998), for example, pointed to a number of theoretical and empirical gaps in Harvey’s theory of urban entrepreneurialism, and Hall and Hubbard (1996) also called for more theoretical and empirical work on the subject. These scholars’ arguments include references to the lack of research on the implications of urban entrepreneurialism for the broader process of economic and political transformation, and to the lack of evidence as to how changes of urban governance actually facilitate that processes. It has also been argued (see in Wood, 1991) that Harvey underplays the active role of local government in driving urban entrepreneurialism while overstating the capacity of private interests to engender change (Wood, 1991:122). It needs to be noted that, for example, Castells (1989; 1996) describes the role of the local governance level in its own commercialization as more pro-active than Harvey, who regards the public sector as a more or less willing accomplice of the pro-active capitalist elite. Furthermore, Castells and Harvey agree that with less income, local governments become more active in attracting tax revenue themselves through a combination of raising taxes and attracting businesses and entrepreneurs as new tax payers to their area.

In addition to the criticism by other scholars, I would like to point out that Harvey’s arguments on the influence of private sector actors as drivers of urban entrepreneurialism and privatization lacks support from empirically grounded data. In addition, although the transformation process of local government towards a more entrepreneurial attitude is fairly well-documented, its implications for local public services and water services in particular are unclear. The commercialization of local water services has mostly been studied from the perspective of privatization and the role of private companies and because of that, we know fairly little about the commercialization of local public water services in the absence of privatization and in the presence of urban entrepreneurialization. These are the gaps in theory to which my study aims to contribute to by developing a theory of local public water services commercialization. The nature of these questions also demands an appropriate methodological approach that is able to identify the relevant actors over time, their roles, logics, interactions, and the outcomes of the commercialization process. In the following chapter I will explain my methodological approach in detail.
3 Methods

In the following text I will lay out the methodological approach that I used to gather my data and build my theory and explain the most important steps in my research process. I will start by explaining why I applied the grounded theory approach, where I position myself and grounded theory, and finally, I will describe my research process in a rather practical way that will allow the reader to not only follow the steps that I have taken but also to imagine what it was like to apply grounded theory and to ‘trust in emergence’. Therefore, I follow Silverman’s (2000; 233-38) recommendation that researchers should rather write a chapter of their ‘natural research history’ where they describe in their own words the history of their research instead of quoting extensively from the discussion in the philosophy of sciences.

I study water services commercialization from an institutional change perspective by investigating the interactions between actors and their connections via their logics and beliefs. As a result, I am using data and methods that are frequently applied in studies of institutional change, such as longitudinal analyses of structural data (for example the number of organizations and their incomes) combined with analyzing the development of values and beliefs by tracking themes in professional journals, newspapers, and interviews. Therefore, the methods that I use are rather usual in terms of studying institutional change as such, but they are more unusual for studying commercialization and especially the commercialization of water services. In the field of studying water services, economic analysis is frequently used but there also exists an extensive number of longitudinal and historical case studies of water privatization that also provide insights into changing institutional logics although they are usually of a more descriptive than interpretative nature. To my knowledge, there are only a few studies that use qualitative interview data. I have not found any study that investigates the roles of local actors and their logics, especially by drawing on such a wide variety of data as is the case in this study, and in particular, uses primary interview data from a social network of decision-making elite. Therefore, I hope to contribute to how water commercialization is studied, focusing on the importance of the local level, its actors, and their logics.

When ideas and beliefs are studied, a large variety of different kinds of data can be used to track them over a period of time including interviews, court decisions, investments, newspaper articles, and even parliamentary minutes. Here I could explain now how well thought out and planned my research process was, but in order to provide a more realistic account of it, I try to resist post-rationalizing the process of scientific discovery and merely write out ‘how it happened’. This means to ‘admit’ that I started out by trying to find an explanation for something I did not even know yet and thus, people who asked me in the beginning what I was going to contribute received a vague answer, at best. I only had a ‘hunch’ that ‘something interesting’ may take place in the strategy process that determines the fate of water utilities. I cannot even claim that I intentionally ‘chose’ grounded theory as an approach right from the beginning. Instead, my methodological
approach became clear while I took the first steps in my research project and thus, the decision to use grounded theory followed somewhat ‘naturally’ from my lack of knowledge of ‘exactly what’ I am studying and the lack of knowledge of what the answers could be. The only thing that I was certain of was that I was going to study the actors, their logics, and their interactions and how they relate to strategic decisions about water utilities. However, I did not know in the beginning that I would end up with a theory of water services commercialization. But what I also knew was that I had the desire to explain ‘why’ things are the way they are and what I found out is not only my interpretation of things but it is also ‘real’.

These issues of an ideological and philosophical nature have implications for epistemology and ontology and for what guided me in my role as analyst, which I briefly explain and relate to the grounded theory approach in the subchapter below.

### 3.1 Epistemology, Ontology, Axiology, and Notions of Causality

Before I describe the research history of this project as suggested by Silverman (2000), I clarify my role and identity as a researcher along four interrelated domains: ontology (what I think is ‘real’), epistemology (how can it be known), axiology (how ‘objective’ I can be or want to be), and notions of causality (the degree of explanatory power I want to achieve and answer ‘how’ or also ‘why’).

Ontologically, I assume that things exist independent from our awareness and despite whether we know their nature. As a result, a phenomenon can exist as real even if we do not know its nature or do not agree on its nature. However, I agree with post-positivists that it is not possible to perfectly know the nature of a phenomenon but that it is desirable to get as close to its true existence as possible (Cook and Campbell, 1979).

Epistemologically, I accept that a phenomenon exists independently from my cognition as researcher and analyst but that it is only accessible through my subjective cognition and interpretation. Also here I agree with post-positivists or critical realists that the world exists independently of human cognition but that it ‘is cognizable and accessible only and ultimately through human cognition’ (Halme, 1994:67).

Axiologically, by applying a number of scientific methods (triangulation) I can achieve sufficient scientific rigor that allows me as analyst and researcher to claim the findings as objective although never completely value-free and should allow the replication of these findings by others.
In terms of causality, my aim is not merely to describe the nature of a phenomenon and ‘how’ things are interrelated or ‘how’ they function but to explain the relationships of phenomena and build a theory that also explains ‘why’ a phenomenon is taking place. Therefore, causality is expressed in my thesis in a rather strong manner as I propose a theory that explains ‘why’ water services commercialize.

The grounded theory approach of Glaser and Strauss (1967) that I am applying in this study was originally developed to create a method that allows for qualitative material to be gathered and analyzed in a systematic manner so that findings would be better replicable and more reliable and thus claim scientific validity, as was mostly attributed to quantitative methods in the US at the time (Strauss and Corbin, 1998). The ontological, epistemological, axiological principles of grounded theory fulfill the characteristics that I described above and therefore, I see my study in accordance with the grounded theory approach. Also grounded theory determines to create theory and thus emphasize the importance of causality; this is one of my objectives in this study.

As Strauss and Corbin (1990:24) point out, ‘the grounded theory approach is a qualitative research method that uses a systematic set of procedures to develop an inductively derived [empirically] grounded theory about a phenomenon’. Although grounded theory is primarily used as a qualitative research method, it can also be used to generate and analyze quantitative data. Grounded theory emphasizes the systematic characteristics of its approach that are supposed to create scientific rigor in order to produce scientific knowledge that is theory-loaded, generalizable (as the theory it creates should be applicable to a general context) and reproducible from qualitative and quantitative data (although it is mostly used for the former than the latter). As there are differences in how grounded theory has developed, I follow Glaser’s (1998) notion that ‘all is data’ and researchers may draw on any kind of data source as long as it is helpful to gain insights into the phenomena at hand, which means to accept a large variety of data sources from both qualitative or quantitative data.

Although I use the grounded theory approach, adhering rather closely to its original ontological, epistemological, and axiological ideas, it needs to be pointed out that since Glaser and Strauss (1967) proposed the grounded theory approach, a variety of approaches have developed, and as Locke (2001) has pointed out in her review of grounded theory in business studies, it has been applied across scientific paradigms.
3.2 Research Approach, Design and Process

Silverman (2001) suggested that researchers should provide their readers with the story of their scientific discoveries. Also, Strauss and Corbin (1998) point out that the process of scientific discovery is crucial in evaluating the study in general. Hence, the following paragraphs give a processual account of data collection, data analysis and theorizing. As this description will show, theory and data collection went hand-in-hand and as the ideas about the theory emerged I collected new data in a flexible manner to support or reject certain points that I thought are emerging as a theory.

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<td><strong>Micro Level</strong>&lt;br&gt;Top Managers (Elite) representing their Organizations</td>
<td>Exploratory Interviews with 8 people of the Managerial Elite</td>
<td>Interviews with 8 more people of the Managerial Elite</td>
<td>Interviews with 26 more people the Managerial Elite and Experts related to the Field (including people having weak ties to the elite)</td>
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<td>Analysis of the first 15 interviewees’ social networks to identify key persons and to interview them</td>
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<td>Analysis of a Discussion on WSS Commercialization in a Business Newspaper</td>
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Figure 3-1 Overview of Data Collection and Levels of Analysis

The study uses a multi-level and longitudinal approach by comparing the institutional logics of actors, legislative changes, and additional quantitative data between the time periods of 1995 to 2006 (as depicted in Figure 3-1). Because in some cases, key events took place outside the time frame (for example, a key legislative change may have
occurred in 1994), there are exceptions where data has been included also from shortly before or shortly after the chosen time period, as long as it was necessary for explaining the phenomenon at hand. I use Glaser and Strauss’ (1967; Glaser, 1978; Glaser, 1998) grounded theory not only as a method but also as an approach to scientific discovery. Grounded theory was guiding me from the start of the discovery process instead of merely being utilized for analyzing data that had been collected. As a result of this approach, I had to acknowledge the emergent nature of the study and phenomena at hand as well as maintain an open mind regarding theoretical and methodological questions. Flexibility and creativity was necessary in applying the appropriate methods that would extract and validate the emerging phenomena.

3.2.1 Starting Out with Social Networks

The data for this study have been collected in the following manner. I started by conducting interviews with the managing director of a large water utility; the chairman of its supervisory board; and the responsible executive manager in the cities’ administration. In these interviews, I was guided by a list of topics relating to strategic management of water services which the interviewees could freely address, so that I could find out what the key issues in water sector management were from their perspective. In addition, I asked each of these people to draw their social networks (exemplified in Figure 3-2) regarding restructuring and managing water issues. Each map contained 15 to 30 contact persons and indicated the interviewee’s strength of ties to most of them (indicated in the figure below as numbers written on the tie, whereas 1 was for strong, 2 for medium, 3 for weak strength of tie).

Figure 3-2 Example of an Interviewee’s Social Network (anonymized)
I applied to these social networks the snowball technique and identified other relevant key people that I was going to ask for an interview. As a result of this process, a network of managerial elites emerged. By elite, I mean people “who occupy defined positions of authority, those at the head of, or, who could be said to be in strategic positions in private and public organizations of various sizes” (Pettigrew, 1992b:163). I collected the social networks from the first 15 interviewees, with 15 to 30 names in each social network and comprising people from a variety of backgrounds and organizations. According to Granovetter’s (1985) argument that ‘weak’ ties or seemingly peripheral people are also relevant for understanding social networks, I also interviewed less-connected people to compare the data with the views of the elite that emerged. Further, Pettigrew (1992b) points out about research on elites that researchers also need to include a wider variety of members of stakeholders than just the business or political institutions under focus.

As a result, these maps were also helpful in identifying the most relevant organizations that were involved in the commercialization process. The interviewees were also asked about the past and present most relevant actors and organizations for the water sector. The network maps were drawn between 2003 and 2004, but they also included information about which actors would have been and would not have been on the map in 1995. The network maps are used in this study as the basis for comparison of organizational field structure between 1995 and 2005, but otherwise the content of these maps (i.e. people’s names) was intended as confidential and not further used for this study except for identifying potential interviewees.

I started the first interviews in autumn of 2003, and problems in strategic decision-making about water services and the commercialization emerged after five or six interviews as the dominant issues. Hence, the interviews with all further participants of the study were adapted to these issues that had emerged. In order to get appointments with all those that I identified according to the social network analysis as important to interview, I had to be patient, but at the end of 2004, I had completed 39 interviews and had reached the stage of saturation (at which interview content started to repeat itself) a while before that. The relatively long time it took to conduct these interviews resulted from the fact that it was necessary to interview specific key people belonging to an elite, who had to be approached with consideration, and gaining access to them had been difficult at times. However, it happened only twice that I was declined an interview, but in both cases, the person referred me to a colleague, whom I then interviewed. I can only speculate about the reasons for gaining access to almost all interviewees. On one hand, once I had access to one of the members of the elite, I asked them for permission to use their name when contacting their most important contacts, which certainly helped in getting the necessary appointments. On the other hand, there is a possibility that it is easier to get access to top-level managers in Finland than elsewhere, and there is also the possibility that access is somewhat field-specific.
3.2.2 Characteristics of Interviewees and Interview Data

The 40 interviews that I included in this study comprised 11 top level water utility managers (including 1 manager from the Finnish Water and Waste Water Works Association); 11 top level municipal managers (including the Association of Finnish Local Authorities, a public-owned municipal consulting firm, and 1 municipal council member); 5 top level ministry public servants (including the Finnish Environment Centre); 3 investment bankers and 1 financial consultant; 3 scientists and 3 water sector consultants; 3 top level private sector enterprise managers; and one labor union expert. The data set comprises municipalities and cities from West, Central, East, and South Finland4.

The interviews were on average 1 hour 40 minutes long, conducted according to an aide memoir (semi-structured interview guide) and tape-recorded. Interviewees were assured that what they say will not be quoted in any publication by connecting it to their names. However, I told interviewees that it may be possible for ‘those in the know’ to correctly guess who is behind a certain quote. All interviews were conducted with Finnish nationals but in English language. All interviews were transcribed, which resulted in 950 pages of text that were analyzed by using NVIVO software for analyzing qualitative data according to grounded theory.

After a first screening of the data by using the NVIVO software program, the main themes (e.g. managerialization, calculating, compromising) had already emerged but they were rather unstructured and it was difficult to interpret their meaning and how they are linked with each other. At this stage I decided to complement the interview data with alternative sources that would help clarifying the interview data. Hence, a longitudinal analysis of relevant legislative changes was conducted, and in addition, the main topics in three sector-related publications were tracked over the years 1995 to 2005 (and in some cases until their last issue in 2006).

3.2.3 Tracking Legislative Changes

In order to understand the wider governance framework of the water sector, I tracked the legislative changes made by the national and EU governance actors, from 1980 until the present, whereas the most relevant ones started in the 1990s. The time frame for legislative changes comprised a somewhat longer period than for other data sources because it was necessary in order to provide a full picture of the process and certain key decisions, which had happened already years or decades ago. The analysis of legislative changes was mainly based on secondary data (a number of publications and summaries of a variety of authors, to which the empirical analysis refers in its text directly) rather than reviewing the different legislation directly.

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4 A detailed list of interviewees is not provided in this thesis because it was agreed their names remain anonymous.
3.2.4 Content Analysis of the Journal ‘Kuntatekniikka’

In order to compare what I had gathered in qualitative material to an alternative source, I performed a longitudinal analysis of the technical sector’s focus by reviewing the articles in the magazine Kuntatekniikka, one of the municipal technical sector’s key print media, published by the Finnish Municipal Technical Association SKTY and Municipal Construction Association RTS.

From January 1998 through June 2006, 644 articles were published. The publishers’ English translations of these articles’ titles and short abstracts, which were already available in the journal’s web pages, were used for the content analysis. The articles published during the time from 1998 to 2005 (N=644) were categorized according to whether they contained mainly technical, managerial, or citizen aspects. It was possible for abstracts to contain more than one aspect at a time; for example, when the content was about citizen’s involvement in constructing a new housing project. The typical title of a technical article would be: “Constructing street pavements from natural stone” while a typical managerial title would be: “Contracting out technical services”. The disciplines included in the magazine comprise construction, townscaping, urban planning, streets and traffic, municipal management, environmental management, waste management, and water and sanitation. Although this content analysis was only based on the publisher’s English translations of abstracts and titles and thus, not on an analysis of the entire article content I regard titles and abstracts as representative for the entire article due to the long time frame and large amount of articles reviewed.

3.2.5 Commercialization Discussion in Kauppalehti Business News

I decided to track the discussion about the commercialization of water services in the business journal ‘Kauppalehti’ and analyzed it from 1995 to the first half of 2006. I chose Kauppalehti business paper because it has been following the developments of different actors in the Finnish water sector rather well, while other, similar publications such as the second largest business news ‘Talouselämä’ that I also screened have not been following water-related issues that much. I accessed the Internet archive of Kauppalehti News and searched for water sector related articles during the time period. The search resulted in 45 articles that were analyzed according to their content with the help of a certified translator for Finnish – English language.

Kauppalehti is the largest daily business newspaper in Finland, with approximately 80,000 copies distributed daily (five times a week) in 2005. Kauppalehti newspaper is part of Kauppalehti Group, a business and financial news division of Alma Media, which is Finland’s largest media corporation and focuses on publishing and distributing print media, financial information, online services, and television broadcasting.
Media and especially mass media, such as the Kauppalehti News (80,000 copies), is a powerful actor as it may affect public opinion. Therefore, it is different from professional journals that usually reach only a small circle of experts and professionals working in a sector (e.g. 5,000 copies). Thus, Kauppalehti News is not only a daily business newspaper, but because of its potential to decide what to cover and to affect public opinion, it could also be considered an actor in its own right. However, while it is important to acknowledge the power of such mass media, the focus of the analysis at hand is not to investigate the role of Kauppalehti News in the commercialization as such, but merely to use it as a forum where the discussion about the Finnish water sector has been documented.
3.3 Data Analysis as Process

The qualitative data derived from interviews were transferred to the NVIVO software program for managing qualitative data. The interviews were first categorized according to actor groups, resulting in seven different groups. These groups were created by using the social network maps collected from the first 15 interviewees, where the social network of the water sector and its organizational field had emerged. The groups of actors are based on the similarity of interviewees’ and their organizations’ roles, tasks, and interests. The groups comprised: Water Utility Actors; Municipal Actors; Ministry Actors; Financial Actors (Investment bankers and financial consultants); Private Sector Actors (Industrial Companies and related Consultants); Scientists; and Labor Union Actors.

According to the grounded theory method, rounds of data coding were executed as many times as necessary to start seeing the categories and their linkages clearly. In this case, four rounds were required. Data coding meant reading through all interview data and categorizing what interviewees had said according to key words and key concepts. Each time something appeared in the interview text that seemed significant and theoretically loaded, I assigned to the quotation a name that symbolizes the data. For example, an interviewee would say about merging neighboring water utilities with each other: ‘The most important thing is to calculate how much we would get from merging our water works with the neighbor municipality before saying yes to such a deal’. Figure 3-3 shows I would have categorized such a statement as ‘municipal actor’ saying something about ‘decision-making’ that relates to ‘first calculating then deciding’.

<table>
<thead>
<tr>
<th>Actor Group</th>
<th>1st Level Category</th>
<th>2nd Level Category</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Municipal Actors</td>
<td>(1.1) Decision-Making</td>
<td>(1.1.1) first calculating then deciding</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.2) first deciding then calculating</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.3) involving others in d-m process</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.4) resistance and avoiding it</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.5) calculations not enough</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.6) keeping it simple, smaller steps</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.7) timing</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.8) making compromises or be against</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.9) visions and/or calculations</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.10) calculations difficult</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.11) financial motives for actions</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.12) financial calculations main point</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.13) argue over finance gets u stuck</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.14) different needs of towns</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.15) many options &amp; hard to decide</td>
</tr>
<tr>
<td></td>
<td></td>
<td>(1.1.16) role of champion</td>
</tr>
</tbody>
</table>

Municipal Manager says: ‘The most important thing is to calculate how much we would get from merging our water works with the neighbor municipality before saying yes to such a deal’.

Figure 3-3 Grounded Theory Categories after first Round of Coding with NVIVO
After going through a thousand pages of text, more than 400 (substantive) categories had emerged. And while talking with different groups of actors about the same issues – for each group emerged a slightly different set of categories that showed each groups’ different perspective on the same issue. In this case, the water utility managers had categories for decision-making like ‘stressing long-term benefits’, ‘visionary’, and ‘making compromises’. On the other hand, the municipal managers had decision-making categories such as ‘collaborating’, ‘calculating’, ‘individual interests’, and ‘compromising as last resort’.

Below I provide an example of what these categories looked like in NVIVO in practice (Table 3-1). In the table, I categorized interview text according to ‘collaboration’ and for example I found an interviewee talking about working together by saying: “we had to collaborate with the neighbors because we do not have any groundwater ourselves” which I then coded and categorized as collaborating ‘based on constraints’.

Table 3-1 Practical Example of NVIVO Tree Nodes

<table>
<thead>
<tr>
<th>Node Explorer</th>
<th>Node Set Tools View</th>
</tr>
</thead>
<tbody>
<tr>
<td>Browse</td>
<td>Properties Attributes DocLinks NodeLinks</td>
</tr>
</tbody>
</table>

- calculations difficult
- financial motives for actions
- financial calculations main point
- arguing over finance gets you stuck
- different needs of towns add to diff
- many options & hard to decide
- champion
- decision-making as game
- collaboration
- based on constraints
- safety & risk constraints
- economic constraints—advantages
- based on free will
- collaboration and independence
- technical and political levels of co
- history of collaboration
- collaboration with private sector
- collaboration is hard & slow
- financial logic behind collaboration
- financial incentives for collaborati
- collaboration among public sector
- trust
- regulation of water sector

After the first round of coding (open coding), the processual aspect of the data was extracted by categorizing what the interviewees said about the past, present, and future. From this data, it emerged that a managerialization is taking place but in order to verify this data, I used the content analysis of the three journals I reported in the previous text. My ‘hunch’ was that if the interview data showed that management issues became more
important over the past decade, this would also be visible in the articles published during that time. Hence, I undertook the content analysis of the key publications of each sector.

Each journal was analyzed according to the main focus of its articles it had published during a certain period of years. The data included the two periodicals Kuntatekniikka (1998 – 2006) and Kauppalehti Newspaper (1995 – 2006). The content analysis for these publications was performed by using Microsoft Excel although NVIVO could have been used for that analysis as well. For Kauppalehti, all articles related to water services from 1995 to present were screened according to their full text. For Kuntatekniikka, first and second level coding according to the titles and abstracts already available English language summary available for each issue from 1998 to present, from the publisher’s web site.

The categories emerging from the coding related to the focus of the article, which were technical, managerial, citizen, society, customer, regulation, policy, and general (see Table 3-2). After that round of coding, I decided to present the technical, managerial, and customer categories in a longitudinal chart that is presented in the chapter about municipal actors. I focused on these three categories because they had verified the impression that I had from the interview data, that technical issues had become less important over time, and that managerial and customer issues became more important. This was the moment when I first had the idea that there was something like a rising municipal entrepreneurialism.

Table 3-2 Example of First-Level Content Analysis of Kuntatekniikka Journal

<table>
<thead>
<tr>
<th>Kuntatekniikka Issue of 06/2005</th>
<th>Technology</th>
<th>Managerial</th>
<th>Citizen</th>
<th>Society</th>
<th>Customer</th>
<th>Regulation</th>
<th>Policy</th>
<th>General</th>
</tr>
</thead>
<tbody>
<tr>
<td>Environmental art project with company</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Lightning facilitates safety</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>3D scanning advantages</td>
<td>1</td>
<td></td>
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<td>Infraguide</td>
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<tr>
<td>Canadian forum for municipal technology</td>
<td>1</td>
<td></td>
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<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>New law on railroads</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Changes in law on maintenance</td>
<td>1</td>
<td>1</td>
<td></td>
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<td></td>
<td>1</td>
</tr>
<tr>
<td>GPS technology and virtual networks</td>
<td>1</td>
<td></td>
<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Data management systems</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Precipitation reservoirs</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New techniques for WSS rehabilitation</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Everyday life at Vihti water works</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Traffic patterns and mobility management</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increased car ownership as challenge</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Road as bottleneck</td>
<td>1</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

I found MS Excel more helpful for drawing tables and charts because I have been fairly familiar with it already, and it was possible to perform the coding also with that particular program although it probably required more time.
As a result of these journals’ longitudinal content analysis, I turned once more to my qualitative data and conducted a round of coding, where ‘water commercialization’ emerged from the previous categories as the main category. Since it appeared as the main category and the most interesting category, I selected it as the main category. The following stage meant to apply the selective coding technique (integrating and refining the theory) that helps to identity those categories, which have a relationship with the main category, making them sub-categories. At the stage of selective coding theoretical saturation is reached, which is the point in category development at which no new properties, dimensions, or relationships emerge during analysis (Strauss and Corbin, 1998).

Based on Glaser’s (1998) distinction between substantive and theoretical codes, more than 400 categories emerged that represented substantive codes (any empirically emerging phenomena that is interesting to the researcher and that is categorized) but during the stage of selective coding, theoretical coding had to be used to drop those categories that were not theoretically and conceptually relevant to explain the mechanisms of the main category of commercialization. Theoretical coding means to sensitively go through the categories and detect those which contain theoretical concepts and families of concepts, such as decision-making, that included ‘rationality’, ‘collectivism’, or ‘individualism’. As Glaser (1998) writes, the grounded theorist needs to be aware of theoretical families of codes because they make the researcher aware of their occurrence. However, they cannot be forced into the theory but rather have to emerge from the data.

After dropping most of the categories and only keeping those emerged as being connected to the phenomena of commercialization, the kept categories were analyzed once more and a model was built that explained the mechanisms. The theoretical categories that had emerged from the data, such as ‘rationality’ or ‘individualism’ were used to create the processual model of commercialization mechanisms. The categories that were finally left over from the originally more than 400 categories represent the headlines in the empirical chapter that explain the institutional logic grouped into actor’s domain, its principles of organizing, and its criteria for effectiveness especially related to its own organization and to water services.
Table 3-3 How Grounded Theory Categories transformed into Chapters

<table>
<thead>
<tr>
<th>6</th>
<th>Municipal Actors</th>
</tr>
</thead>
<tbody>
<tr>
<td>6.1</td>
<td>Domain and Principles of Organizing</td>
</tr>
<tr>
<td>6.1.1</td>
<td>The Municipal Domain and its Purpose</td>
</tr>
<tr>
<td>6.1.2</td>
<td>Collectivism and Individualism</td>
</tr>
<tr>
<td>6.1.2.1</td>
<td>Internal Collectivism</td>
</tr>
<tr>
<td>6.1.2.2</td>
<td>External Individualism</td>
</tr>
<tr>
<td>6.1.3</td>
<td>Rationality</td>
</tr>
<tr>
<td>6.2</td>
<td>The Emergence of Municipal Entrepreneurialism</td>
</tr>
<tr>
<td>6.3</td>
<td>The Municipalities’ Perspective on Water Services</td>
</tr>
<tr>
<td>6.3.1</td>
<td>Water Quality and Service Quality</td>
</tr>
<tr>
<td>6.3.2</td>
<td>Workforce and Retirement</td>
</tr>
<tr>
<td>6.3.3</td>
<td>Facing Resistance to Changes</td>
</tr>
<tr>
<td>6.3.4</td>
<td>Infrastructure and Investments</td>
</tr>
<tr>
<td>6.3.5</td>
<td>Profitability and Economic Regulation of Water Utilities</td>
</tr>
<tr>
<td>6.3.6</td>
<td>Water and Energy</td>
</tr>
<tr>
<td>6.4</td>
<td>Summary of Municipalities’ Logic of ‘Rational Entrepreneurialism’</td>
</tr>
</tbody>
</table>

In each chapter that analyses the logics of a particular actor group, it was reported on ‘how the water sector should be organized’ and the nature of decision-making from this actor’s point of view. The table above depicts the municipal actor’s logics, which comprise thinking collectivistic towards the inside of the organization (‘internal collectivism’) while individualistic towards the organizations’ environment (‘external individualism’) and applying managerial concepts grounded in ‘rationality’ to its decision-making.

**3.4 From Substantive to Formal Theory**

The aim of grounded theory is not only to generate theory that applies to a specific context (substantive theory), such as explaining why and how water services are increasingly becoming a commercial operation, but to derive from that substantive theory a theory that is more widely applicable, a so-called formal theory (Glaser and Strauss, 1967). Because generating first substantive and subsequently formal theory is the main objective of this research approach, I am briefly explaining the steps that I followed in order to create, what I call ‘a theory of public water services commercialization’ (substantive theory) and which can be generalized towards a formal theory of ‘local public services commercialization’. However, I consider the outcome of this thesis to be somewhere in the middle of substantive and formal theory since there would be more research necessary to establish a fully formal theory of ‘local public services commercialization’, resting on empirical data collected from other local public services as well.
Coming back to creating the substantive theory, my was 'hunch' that the answer for the lack of transparency in strategic decision-making about water utilities lies in the interactions between different powerful actors and their different logics and priorities on how to organize water services. I systematically conducted a social network analysis to derive the involved actor groups. I chose among these different groups of actors that emerged from the analysis (e.g. municipal managers, water utility managers, financial actors, scientists, ministry officials) those groups which were most powerful and most relevant for making the strategic decision in water utilities. These groups need to be considered my ‘comparative cases’, which comprised municipal managers, financial actors, water utility managers, and ministry officials. Following the steps in the analysis (as described in the paragraphs above), I derived the relevant categories for explaining the phenomena of commercialization from the interview material and described their properties. In practice, the relevant categories were sets of ‘principles of organizing water services’, with their properties being specified along three different main principles, comprising ‘rationally calculating’, ‘collectivism, and ‘individualism’. Then I used the longitudinal content analysis of newspapers and journals to verify whether the impression I got from the interview data about the actor’s opinions on the past and present.

Once I had described the properties of the different comparative cases’ relevant categories, I focused on how the actors’ interactions with each other had evolved along the longitudinal time period of the past ten years. This allowed me to build a substantive theory of how the priorities in strategic decision-making about water utilities had changed over the years, and under which conditions they had changed. The result was a context-specific theory of ‘water services commercialization in Finland’ that was the basis for moving to a higher conceptual level in order to build a formal theory of ‘local public services commercialization’.

In order to achieve that conceptualization, I had to recognize that the actor’s previously derived ‘principles of organizing water services’ are part of these actor’s general institutional logic they apply not only to the water sector, but also to other areas they participate in organizing. Glaser and Strauss (1967) argue about creating formal theory; it requires more than rewriting substantive theory by omitting context-specific words, and in most cases, more comparative research is necessary to validate that a theory created also has explanatory power in another context. Since the empirical material of this study was derived from different actors across sectors and governance levels and even when focused on ‘organizing water services’, it contained in the very most cases also the actor’s views of organizing ‘in general’. Therefore, I was able to apply my substantive theory of ‘water services commercialization’ to a broader context of ‘local public services commercialization’ or more specifically, to ‘profitable local public services’.

However, extending my theory of water commercialization to such an argument would require more research and a more thorough demonstration of linkages between my data and such a statement than I was able to provide in this study. If such a multi-area formal
theory would be established it could probably also be linked to a formal theory of the ‘commercialization of the public realm’. However, this study and the theories derived from it end with a well-grounded substantive theory of ‘water commercialization’, which points into the direction of a multi-area formal theory (Glaser and Strauss, 1967) of ‘local public services commercialization’, rather than walking this road to the end and effectively proving it. Because the theoretical argument made in this thesis is mostly of substantive nature, only with adding future research it could be achieved what Glaser and Strauss (ibid.) had in mind when they argued that generating formal theory is the ultimate goal of grounded theory.

3.5 Generalizability, Validity and Reliability

As Glaser and Strauss (1967) point out, the goal of grounded theory is to generate theory rather than verify existing theory. Also for this reason, Strauss and Corbin (1998) say that generalizability is not the main concern of grounded theory studies, which has important implications on the choice of methods as qualitative methods that give rich descriptions with explanatory power are preferred to quantitative ones (although the latter may be used for grounded theory studies as well).

Verification and generalizability do not necessarily matter for grounded theory. However, validity and hence, reliability does matter, since one of Glaser and Strauss’ main objectives in designing the grounded theory approach was to find a more systematic approach to analyze qualitative data and generate theory and hypotheses. Validity can be distinguished into instrumental validity and construct validity (Kirk and Miller, 1986). I see the purpose of instrumental validity to achieve theoretical validity or so-called construct validity. Instrumental validity is achieved by using data from different sources and deploying different methods for analysis (so-called triangulation) since the qualitative observations could have been affected by inaccuracies in measurement, the researcher’s own perceptions, or the nature of the research setting. Therefore, I triangulated my interview data of the managerial elite by interviewing persons outside that ‘inner circle’ as well, and by comparing the interview data with a longitudinal content analysis of three different journals relevant to my research topic. Further, the validity of the interview data was verified by directing similar questions to the data in the journals that I longitudinally analyzed. I acknowledge that the questions and findings from each data analysis that I performed were exposed to my subjective cognition and interpretation but by applying triangulation I was able to achieve sufficient scientific rigor that allows me to claim the findings as reliable, valid, and to some extent replicable by others.

I worked toward construct validity by following the grounded theory approach that requires phenomena to emerge from data that originates from comparative cases (the discovery of different actor groups and comparing their logics). I chose these comparative cases based on my findings from a qualitative social network analysis that
used a snowball technique. I did so because of my vague hypothesis (or ‘hunch’) in the beginning of this study, that the unpredictability of strategic decisions about water services (of which water utility managers were complaining) is a result of hidden interactions and interests inside a managerial elite coming from different organizations and sectors that makes the strategic decisions about these water utilities. Thus, before I could even build a theory of which interests drive strategic decisions in the water sector, I had to systematically search for comparative cases (identifying the relevant actor groups) by conducting an exploratory social network study.

As emphasized by Glaser and Strauss (1967: 169), ‘the discovery of useful comparison groups is essential to the generation of theory’ and although grounded theory requires the researcher to have control over the choice of comparative cases, there are situations when the ‘trust in emergence’ inherent in the grounded theory approach needs to be extended to the discovery of comparative cases as well, in order to ‘maximize potentially relevant comparisons’ (ibid.). I am therefore introducing the use of snowball technique in this particular case as a novel way of finding comparative cases for situations when research is of such exploratory nature that the relevant comparative cases are not even known yet to the researcher, but all he or she has is a vague hypothesis about where to look for them.

After I had my comparative cases and had collected the data, I worked towards construct validity by organizing the data in categories (the actors’ different institutional logics about how to organize water services), determining the categories’ properties and conditions and showing similarities and differences in these categories (actors’ different logics). Finally, I demonstrated the relationships between categories (showing differences and similarities in logics and how they connect in a processual manner) in order to discover their dynamics and consequences. Demonstrating the relationships between categories was accomplished through adopting a processual perspective on the research subject by investigating a period of ten years, and using data from various sources that has complemented each other. Keeping an open mind during the process of data analysis and theory generation has been important. Building theory grounded in data requires going back and forth between data and theory. When necessary, I had to find new data sources to support or reject my theory or to simply change my theory.

Finally, I would like to point out that besides using triangulation and striving for validity, I see this study and its findings as ‘objective’ in the awareness that this objectivity can only be an imperfect one. In fact, the aim of my methodological approach was to limit subjectivity rather than achieving objectivity.
4 Development of the Water Sector and Key Actors

I am pursuing two objectives in this chapter. First, I establish a basic understanding of the key characteristics of the Finnish water sector and how the utility managers I interviewed frame the challenges for the sector and how they believe water services should be managed in order to solve these challenges. This is an empirically grounded account of challenges and solutions in order to present the views of a particular managerial elite. Therefore, I do not take the views outside this elite into account. In fact, one may find rather different or opposing views held by people outside of this elite, such as by researchers and managers of smaller and geographically remote water works who may for example oppose plans to establish regional water utilities. Although these different views certainly exist, the reason for presenting the logic of a particular network and elite of key persons was to make their dominant views on managing water services explicit to outsiders.

Second, I present a field analysis of the commercial actors that shows how over the past ten years, the financial actors have become the most relevant actors for strategic decision-making regarding Finnish water utilities. Because to my knowledge, this phenomenon has not yet been investigated in scientific literature, I am providing a field analysis to demonstrate to the reader that the role of financial actors is more important in the Finnish context than the role of other private companies and other commercial actors and therefore is one of the main elements in the theory of local public water services commercialization that I propose in this thesis.

Before going into detail about the basic characteristics of the Finnish water sector and the emergence of financial actors among commercial actors, I present a brief overview of the different actors that are part of the organizational field. This overview of the different field actors should put them in context with each other and with the water sector. The four most relevant actors are then analyzed in chapters 4 (water and commercial actors), 5 (state governance actors), 6 (municipal actors), and 7 (financial actors). The distinction of the different actor groups is based on their domains and roles derived from interview data that was analyzed by using the grounded theory method.
4.1 Overview of the Field of Actors

The ‘field of managing water services’ is separated into four different levels of organizations (as depicted in Figure 4-1). The supra-national, national, and regional level are foremost governance levels. On the top level, the European Union actively governs the water sector in environmental and health issues, although it is almost inactive in economic issues, which are under national authority of the EU member states. The EU has been a relevant governance actor already before Finland’s accession because national governance actors had to include EU legislation in foresight of the possibility of joining the Union. On the national level, the most important ministries in terms of water governance are the Ministry of Forest and Agriculture, focusing on water supply and sanitation, while the Ministry of the Environment’s focuses on environmental issues, and the Ministry of Health and Social Affairs on health-related issues of water supply and sanitation.

Figure 4-1 Actors in the ‘Field of Managing the Water Sector’
Referring to Figure 4-1, adjacent to these ministries are the Regional Environment Centres—regional coordinators of the guidelines and legislations’ execution that give recommendations to municipalities and water utilities, as well as provide feedback and expertise to the ministries. However, these Environment Centres focus on environmental and health-related issues of water supply and sanitation, and do not exercise authority over economic practices in the water sector in terms of regulating and supervising profitability or investment policies of water utilities. (Still, in principle, they could and they are involved, especially in rural areas, in drawing up investment plans and representing the intermediary between ministry financial support and rural water and wastewater development projects.) Regional municipal committees do exist but mainly focus on the regionalization of social and health services. These regional committees have not been included in the figure because their role in the field of ‘managing the water sector’ is rather insignificant, concluding from the social networks of the managerial elite that was interviewed for this study. Also, Pietilä et al. (2005) arrive at a similar conclusion and argue that Finland’s lack of regional councils, whose role would be to enhance regional (and other) cooperation between municipalities in water services development and operation (as they exist in Sweden) is one of the reasons why the regional level administration has no stronger role in the provision of water services.

Finland is a unitary state, and administration is centred on the local and national level. Regional cooperation on issues that are not compulsory for municipalities to cooperate in is encouraged by the state level—for example, through providing financial incentives. For example, the Ministry of Forest and Agriculture grants through the Regional Environment Centres financial aid as incentives to municipalities that decide to engage in deeper cooperation with each other concerning water resources management, wastewater treatment or water and sewerage networks.

As depicted in Figure 4-1 above, the local level of actors includes five different groups, comprising the municipalities, water works, private sector actors, financial actors, and intermediary actors. Resulting from the social network comparison, I found two things especially striking. First, the social networks of actors belonging to the municipal and to the water utility elite had almost no overlap, with only one to three persons in common (out of 20 persons on average).

Second, the municipal elite were having contacts to the financial actors but those were rather isolated from the rest of the actor groups. As shown in the figure, these financial actors became active in the field of managing water services during the end of the 1990s. Around the same time, private sector actors who have been established field participants for several decades (comprised of suppliers, construction companies, and consulting firms) have also been trying to change their role by becoming operators of water supply and sanitation infrastructure.
As part of the intermediaries, especially the Association of Local and Regional Authorities and the Finnish Water and Wastewater Works Association are important in the field. The former represents the interest organization of the municipalities and promotes municipal reform, while the latter is the interest organization of Finnish water works, active in lobbying for water sector reform and governance.

4.2 Water Utility Actors

In the following subchapter I briefly introduce the basic characteristics of water supply and sanitation, the development of market structure and investments, as well as the challenges for Finnish water works.

4.2.1 Basic Characteristics of Water Supply and Sanitation

Water services represent a natural monopoly (Parker, 1999; 2003; Katko, 1991a; 1991b; Vickers and Yarrow, 1993) because the high infrastructure costs make it unreasonable to build water networks that would compete with each other for the same customers—for example, within a certain geographical area. Further, the characteristics of water as a resource are rather fragile and cause the water quality to decrease with increasing length in transport. Introducing the common-carriage principle, which allows competitors to use the same network and therefore leads to the introduction of competition in water services, has been argued as a risk to water quality (Katko, 2001) which serves as another limitation to breaking up the monopoly character of water services. However, England and Wales are introducing the common carriage system to certain areas in water wholesale, which is promoted by the government (Seppälä et al. 2001b). Another aspect of the difficulties with marketing water from the consumer’s perspective is the lack of consumer’s ability to verify the quality of the service, except in dramatic failure of service delivery.

The basic cycle of water services has remained relatively unchanged since the times of ancient high cultures, where the key principles of water supply and sanitation were a fixed part of the prerequisites for settlements, agriculture, and economic activity in general.

Figure 4-2 (see next page) provides the basic process of water supply and sanitation, based on water cycles presented by Hukka and Seppälä (2004). In principle, the cycle contains the stages of abstracting and distributing water to users and collecting water thereafter in order to treat it and discharge it to the environment. Abstraction, distribution, and treatment may be taken care of by separate organizations, but in Finland these are done by the same entity, which is the municipal water utility. In the beginning there is a water source—for example a lake, river, or ground water. The water is led through a pipe to a water basin. In some cases the basin is located at a sufficient altitude in order to receive enough pressure to lead the water from the basin through a pipe distribution network to the consumer households. In regions lacking such differences in altitude,
water pumps are used to transfer the water—for example, either straight to the network or also up to a water tower. After the water is used in the household or business, it is discharged into the sewage network, which consists of pipes leading from the real estate to the sewerage system, and subsequently into the sewerage treatment plant. In the treatment plant, the sewerage undergoes a combination of mechanical, chemical, and biological treatment processes. The treatment process removes some of the most environmentally harmful substances, such as nitrogen, phosphorus, or heavy metals.

After the treatment process is completed, the mostly dry component that remains is the sludge, which may be composted, incinerated, permanently deposited in landfills, or used as fertilizer for agriculture, although the latter option is becoming increasingly unpopular because of stricter environmental standards and concerns about harmful substances in the sludge (Hukka and Seppälä, 2004). The remaining cleaned wastewater is discharged into appropriate water bodies.

Large industrial complexes, such as pulp and paper factories, textile factories, dairy producers, or slaughterhouses may have their own water storage and treatment facilities because of the large quantities of water used during their manufacturing processes or their wastewater is forwarded to municipal systems after pre-treatment.

Figure 4-2 A Simplified Cycle of Water and Sewerage Services
4.2.2 Market Structure of the Finnish Water Sector

Finland has a population of 5.2 million, of which 4.7 million are connected to water supply and 4.2 million to sewerage systems. The systems which serve the population appear in different organizational forms. The urban population is usually served through a local water utility. Arrangements between municipal water utilities are quite frequent. For example, piped drinking water may be provided by one utility to the other if water resources are limited. Also, taking care of the neighboring utilities’ wastewater is practiced, especially when large wastewater treatment plants are built that can serve a number of municipalities.

In Finland, water bills are sent to the real estate holders who have water meters and therefore not always to the end-consumer. Families in detached houses are the direct consumers of a water utility while citizens living in an apartment building often forward their water charge to the real estate holder as part of the rent or monthly coverage, as, for example, in a housing company. The water charge is determined in many cases through water meters installed at the real estate.

Water supply is provided in Finland through 460 water utilities, 1000 cooperatives, 420 partnerships, and 160 shareholding companies. Rural areas may be served through local cooperatives and partnerships if their territory is outside of designated municipal areas and too sparsely populated. Small communities in such areas may jointly own water cooperatives for organizing water supply, whereas the wastewater is often taken care of individually or led to treatment plants that belong to municipal water works. There are
almost 1000 such cooperatives in Finland. In addition, the smallest form of organized water services is water partnerships, of which there are 420. They may be formal or informal agreements between two parties to exchange and help each other regarding the service (e.g. in Muukkonen et al., 2003).

These small cooperatives and partnerships usually provide drinking water services while wastewater services are mainly taken care of by municipal utilities. In addition, there are 160 shareholding companies, usually owned either by individual municipalities or by a number of municipalities together. The majority of them are bulk water suppliers. Figure 4-3 (previous page) shows that the smaller the communities are, the more likely it is that they are served through small arrangements. Starting with a population size of roughly one thousand in habitants, municipal water works become the dominant form of water services producer, with a total number of 460 water works. The size of water utilities varies significantly, with the smallest water utilities serving only a few thousand citizens and the largest ones serving more than 100,000 citizens. Many large municipalities established their municipal water works in the 1990s as municipal enterprises and therefore formally separated them from the remaining municipal technical division.

Table 4-1 Distribution of Water Utilities by Turnover and Population Served

<table>
<thead>
<tr>
<th>Size Cohort</th>
<th>Combined Turnover</th>
<th>Turnover in Mio €</th>
<th>Population Served</th>
</tr>
</thead>
<tbody>
<tr>
<td>Five Largest</td>
<td>25%</td>
<td>30 – 86</td>
<td>165.000 – 550.000</td>
</tr>
<tr>
<td>Next approx. 20</td>
<td>25%</td>
<td>5 – 20</td>
<td>35.000 – 117.000</td>
</tr>
<tr>
<td>Next approx. 200</td>
<td>25%</td>
<td>0.5 – 5</td>
<td>3.500 – 31.000</td>
</tr>
<tr>
<td>Next approx. 1000</td>
<td>25%</td>
<td>0.01 – 0.5</td>
<td>50 – 3500</td>
</tr>
</tbody>
</table>


Table 4-1 provides the distribution of water works according to their turnover and the amount of inhabitants served. Each category represents roughly one-fourth of the water sector. The largest water utilities measured by turnover (in year 2005) were Helsinki, Espoo, Tampere, Vantaa, and Turku. The turnover of the five largest utilities represents 25 percent of the entire water sector’s turnover. The next 20 water utilities, with a turnover between € 5 to 20 million represent another 25 percent of the market followed by approximately 1000 small scale water works. The concentration ratio (CR) of the water sector for the top five utilities is a rather low 25 percent. The total turnover of the water sector is estimated at € 1 billion. The Finnish Water and Waste Water Association suggests that the value of assets is usually three times the turnover of a water utility, resulting in a total asset value for the Finnish Water Sector of € 3 billion.
As depicted in Table 4-2, the combined estimated asset value of the five largest water utilities is roughly half of a billion Euros (€ 462 million). As the table above shows, the Cities of Vantaa and Turku are rather similar in terms of inhabitants served, amount of water distributed, and turnover. However, they significantly differ in their estimated asset value, which is € 71 million in the case for Vantaa and in Turku € 110 million. Determining the asset value of Finnish water utilities is a complex endeavor because a common standard for evaluating the utilities’ assets exists only tentatively (Näsi and Windischhofer, 2005). More explicit guidelines are under development—for example, with the help of a project in which the water utilities of Tampere, Turku, Lahti, and Espoo participate.
4.2.3 Structural, Technological, and Investment Development

4.2.3.1 Structural Development from 1995 to 2005

The long-term development of water utilities has been rather stable over the past decade (Figure 4-4). The coverage for water and wastewater services increased from 86 percent for water and 56 percent for wastewater in 1995 to roughly 90 percent and 82 percent in 2005, with most of the increase happening in the time period from 1995 to 2000. After that, the coverage of the water and sewerage systems increased only slightly. While the early 1990s have seen an increase in water undertakings from 1,067 in 1995 to 1,360 in 2005, mainly small cooperatives were established in order to cope better with increasing demand and stricter requirements for WSS also in the countryside.

Figure 4-4 Development of Water Sector Structural Key Data from 1995-2005
Source: Adapted from Finnish Environment Institute (2002a; 2002b)

Figure 4-4 shows water consumption has been also stable over the past decade with approximately 240 to 250 liters per person per day—after a sharp decline in the 1970s and 1980s—as more efficient technology was introduced in households and industry. Groundwater has become the preferred source for water supply because its quality is perceived higher than surface water. During the 1980s the use of groundwater outperformed the use of surface water and since then, the use of groundwater increased from 56% in 1995 to 61% in 2001 and it is estimated now at 63% as water utilities continue to invest in it.
4.2.3.2  Technological Development from 1985 to 2005

The technological development in the past decade has been most significant in automatization and remote supervision and control of water infrastructure such as pumping stations and treatment facilities, and in the technologies of wastewater treatment. Biological combined with chemical treatment has been applied in most wastewater treatment plants since the late 1970s. In 1985 additional nitrogen removal was introduced in some treatment plants. Since 1995 the additional removal of nitrogen has been increasing from 10 percent to 40 percent and almost 100 percent of population is connected to treatment facilities that use the biological-chemical method. Therefore, the limits set by the EU Wastewater Directive of 1991 of 100 percent biologically-chemically treated and 40 percent nitrogen removal are going to be fulfilled in that matter (Finnish Environment Institute, 2006).

4.2.3.3  Investment Development from 1970 to 2005

Figure 4-5 provides an overview of investment activities from 1970 to 2000. Taking a closer look on investments in water networks, sewerage networks, and wastewater treatment plants, the 1970s were the most active period and all three infrastructure components increased by around 100 percent. The rise in investments in the 1970s was caused through a wave of legislation in the 1960s and 1970s. During the 1980s investments in wastewater treatment were rising as new environmental legislation was introduced and network length doubled once more.

![Figure 4-5 Total Investments in Public Water Services, 1970-2000](image)

Source: Finnish Environment Centre (2002a)
At the turn of the decade from the 1980s to 1990s, the water sector was investing, as stricter standards developed by the European Union (and subsequently adopted by Finland) were foreseeable and obligations had to be met. For investments in wastewater networks and their treatment plants, the situation saturated as a satisfactory level of service had then been achieved for most areas. Investments in water supply continued to grow until the 2000s when access to piped water supply had reached more than 90 percent of the population.

After 1995, the investments especially in larger utilities are mostly driven by the need to create access to new urban housing projects, and to gradually rehabilitate networks and treatment plants. Further, smaller utilities and more densely populated areas were still catching up with stricter legislation and therefore had to invest specifically for that reason. But as Figure 4-5 (previous page) shows, investments became rather stable after 1995 and are nowadays limited to the usual construction of new infrastructure in growth areas, and smaller infrastructure rehabilitations of networks and treatment plants. As depicted in that figure, the longitudinal development of investments in water sector infrastructure shows the 1970s as the peak, with almost € 500 million invested in the peak year. Since the middle of the 1990s investments amounted around € 250 million annually, which means approximately one quarter of the € 1 billion turnover of water utilities is re-invested into the renovation and construction of water and sewerage networks. Approximately 70 percent of the networks have been constructed within the past 30 years, of which roughly one-third is younger than 15 years. Between 70 and 80 percent of all investments undertaken in the water sector are directed to the networks, which represent 80 percent of a water utilities’ asset value.

Much of the water and sewerage networks built before the 1960s are located in large cities and date back to the 1940s (or even earlier), while smaller towns and rural areas received piped water supply and sewerage in the 1960s and 1970s. Therefore, the large towns sometimes deal with severe problems such as loss of water caused by old infrastructure in their city centres and the need to rehabilitate their networks. A study by the Finnish Ministry of the Environment (the YVES-Project) concluded that smaller and rural areas have younger networks, but large parts of these networks also reach the end of their lifecycle between the years 2000 and 2010. It was estimated that 1.4% of water and sewerage networks are in very poor condition and 7.6% in poor condition. The estimated restoration needs until the end of the year 2000 were thus around 9% of the networks or 5400 kilometers. At that time, average yearly restoration was estimated to be 300-700 kilometers (Finnish Ministry of the Environment, 1992).

Network rehabilitation has increased since then and the present average of annual network rehabilitation is estimated at 1000 km; but in order to cope with the increasingly outdated infrastructure, the Finnish water sector would have to rehabilitate as much as 3000 km annually, which represents a threefold increase of the present investment activity. Although restoration is necessary for the pipes manufactured out of grey cast
iron in use before the 1960s, also networks built in the 1970s are partly in need of restoration. One of the reasons for that being, that in the 1970s water consumption was expected to rise and thus, required pipes with large diameter. But when water consumption in fact dropped, the flow velocity in the pipe network became too low, which resulted in problems in the functioning as well as corrosion (Finnish Ministry of the Environment, 1992). Further, challenging soil conditions and temperature changes (freezing and unfreezing of soil) may even cause fairly new network infrastructure to break.

The need for renovation of the networks and other infrastructure, such as water and wastewater treatment plants, is therefore significant in the coming years. Rehabilitation not only includes the infrastructure that is beyond its life cycle (for networks between 40 and 60 years and treatment plants 40 years), but also infrastructure that has become unsuitable due to migration. Also the Finnish climate that causes the ground to freeze in winter and unfreeze in spring puts stress to the networks as this process creates movements in the ground.

4.2.4 Framing the Main Challenges and Solutions for the Water Sector

The following paragraphs describe the main challenges for the Finnish water sector from the perspective of the water sector experts that I interviewed for this study. I decided to present this empirically grounded account of challenges and solutions because although there is agreement on these challenges in literature and among water sector experts, I could not take for granted that there would be widely shared agreement concerning the solutions to these challenges. It is important to note that the ideas and beliefs about how to solve a problem are based on the actors’ experiences and interpretative frames that come partly as the result of their experiences. Because I interviewed water experts who manage large- and medium- sized water utilities, their views may be different from those who manage water operations in very remote, rural areas of Finland. In fact, there has been criticism towards the regionalization and centralization efforts (which are predominantly the views of the managerial elite) by Mattila (2005), who argues that especially rural areas may require more locally-based solutions that are based on decentralization rather than centralization of water services.

There are three challenges utility directors have foremost on their mind. Probably equally important are the challenges of deteriorating state of infrastructure and the coming large scale retirement. Another challenge concerns the smaller, rural water works than large, urban utilities, which is the implementation of legislative changes to improve water treatment standards. The issue of adapting to stricter standards is perceived as part of the natural evolution of water treatment and because the Finnish water sector operates on fairly high standard already. These legislative changes are expected to be more of a problem for the smaller, rural water works, which often lack the necessary expertise and resources to improve their systems.
Figure 4-6 Utility Managers frame Water Sector Challenges and their Solutions

Figure 4-6 provides an overview of the challenges, and how they should be solved. The water experts would like to see more independence from the municipal owner in order to manage the utilities and plan investments primarily based on the needs of water supply and sanitation than based on the municipalities’ economic policies. Further, by merging water works with each other, larger economies of scale would allow to pool financial resources in order to prioritize investments. Larger organization sizes should provide better prospects for employees and allow hiring a workforce with more diverse skills, such as legal, management, and financial personnel.

4.2.4.1 Lack of Financial and Managerial Autonomy

If the current quality of water services shall be maintained, more investments in infrastructure will have to occur. The question for utility managers, however, is how to finance these investments. In particular, larger water utilities have been able over the past years to create savings for infrastructure rehabilitation, but they are not sufficient for the amount of networks that will have to be renovated in the future. In addition, in many cases these savings are used by the municipal owner as non-liquid assets that are for keeping the municipal budget in balance. The water experts are criticizing the municipalities’ expectations of running the utilities more as businesses and expecting financial profits for the municipal budget. Some utility managers express their concerns with the loss of the water sector’s identity as a public service and becoming a business.

“Water started out as basic service but it has become a business…nowadays some politicians think that there is a possibility to solve the city’s problems with the water utilities. The politicians should decide if it is a basic service or a business, and if it is a basic service, they should not use the water utility to solve the problems of the cities…these politicians don’t think in the long term.” (Water Utility Manager)
“Although we are very profitable and have some savings for investments, we cannot use them without permission by the city. They may invest them and we get the interest…we may even be forced to show a deficit in our annual report.” (Water Utility Manager)

Although water works have been established in larger cities as municipal enterprises, many important decisions are still political. Investment strategies and the level of the water and wastewater service fees are proposed by the municipal board to the municipal council where they are voted upon. The municipal council is the key decision-making body, which mostly acts on proposals from the municipal government and approves water and sewerage charges; the strategic objectives of the water utility; and the nominations of members of the board of directors of the water utility.

“The bigger towns are used to the water works profits but we have lots of networks that need big investments…even though we are a municipal business department and have separate book keeping, they calculate and decide our investments. Even when we need more investments it is not possible to make them if the economic situation of the city is bad and it needs our money to balance its budget. It is a problem.” (Water Utility Manager).

Water utility directors have been expressing concern about a lack of autonomy from the municipal owner. It is regarded as not necessarily a bad thing that the water utility shares certain public sector employment policies such as keeping staff employed, although the utility could operate more efficiently with fewer staff. But it gets tight for utilities when they have to fulfill such public sector policies and at the same time increase their profitability. In such cases, the municipalities’ policies affect and constrain managerial action and decision-making at the water utility level.

“Our costs for wastewater and ground water will go up significantly which makes it hard to decrease our overall costs, because we don’t have the permission to let go of any employees and at the same time we should be more profitable” (Water Utility Manager).

On one hand, the city or municipality expects increasing efficiency and higher profits from the water utility but on the other hand, the water utility may have to buy services from the municipal organization although they could be obtained from the private sector at a lower price. Here, the municipal overall policy is to make effective use of its other technical departments such as the construction department or vehicles department.

“The municipality made a decision that we have to buy all kinds of services from the city even though they are more expensive. The cars we use are leased from the city, which increased our costs on that item by almost half…earlier, when we had cars ourselves, we usually kept them ten years though they have a depreciation time of five years and now we have to change them every five years and make every time expensive changes on the cars…it is just lost money.” (Water Utility Manager)
“The city gets several millions a year in profits, which are not dependent on our change in net sales. The amount is reasonable, but in addition they force us to buy uneconomical products or services from the city where the price may be thirty percent higher than on the free market…we should have more autonomy so that I could manage this like a real company.” (Water Utility Manager)

If the water utility would be allowed to make entrepreneurial decisions, as is argued by water utility managers, its effectiveness and efficiency could be increased to a level that provides the municipality with a satisfying profit ratio. However, the question in operational management is how to bridge the gap between acting entrepreneurial and becoming more efficient while at the same time fulfilling municipal policies that keep the cost of water and sewerage operations higher as they need to be.

The strategic and operational planning and decision-making levels are rather clearly separated in the case where water utilities are governed as municipal enterprises. In such cases, the utility makes operational decisions and the municipality is in charge of strategic ones. In a few cases, the water utility has been transformed into a limited company, which according to the Limited Company Act should allow the utility more autonomy and flexibility but in practice the utilities’ board consists of representatives of the municipal owner. In such cases, it is hard to draw the line between operational autonomy and strategic dependency because the owners’ methods of governing the utility are more subtle. Thus, it is often up to the owner to decide which issues are considered as strategic (and thus to be decided by the owner or at least by the management consulting with the owner), and which issues are operational and clearly a matter of the utility management’s decision-making authority.

“The role of the board is clearly stated in the Finnish legislation for limited companies. It controls the work of the managing director and makes the long-term decisions. But in practice the role between me and the board is maybe a more flexible thing. We have a practice of what I can make, and what we discuss together in the board. And the board meetings take place nine times a year where all big decision, agreements, tariff decisions, strategic decisions, and such things are made. But, I take care of course of the everyday decision-making.” (Water Utility Manager)

Where the municipal owner corporatized its water utility from a municipal enterprise to a limited company, it has been reported that the municipal owner has regrets about that transformation because their possibilities to influence the management decisions of the utility became too restricted by the Limited Company Act.

“The managing director of a limited liability company doesn’t have to take orders…in the legal meaning, so, if the town wants to give orders, the managing director should be on the payroll of the town. We discussed it and that is what they want and I also think that the cooperation between utility and town is easier.” (Water Utility Manager)
“The people who make the ownership policies in the city said they regret having created these limited companies…because they are hard to control.” (Water Utility Manager)

A recent study (Vinnari, 2006) showed that 80% of the 17 largest Finnish water utilities’ managing directors would like to see some form of economic regulation. This demand, however, must be considered in context of the present lack of autonomy from municipal influence. When I asked water utility directors in my own study whether they believe a regulatory agency is necessary if their autonomy would increase, they declined. Utility directors see the advantage of regulation in protecting their investment plans from the municipalities’ demands to prioritize profitability over investments and therefore infrastructure rehabilitation. Utility managers emphasize that until recently the benefits of a regulatory agency would have been consumed by the bureaucracy it would create, but as the condition of networks continues to deteriorate and utilities have problems to convince their owners to invest, maybe such an agency would be able to protect the utilities from their profit maximizing owners.

“A regulative authority would be good because there should be an authority that monitors how much profit is taken and how much is invested into infrastructure. The owner can take now much more than the reasonable profit.” (Water Utility Manager)

“We wouldn’t need an economic regulator if the municipalities would give us more freedom…the system would work pretty well if our owners would just let us do our jobs more independently. They would still get plenty of money and we would be able to keep the whole system in good conditions…” (Water Utility Manager)
4.2.4.2 Lack of Economies of Scale

Increasing the economies of scale is clearly considered by the water sector actors as the best choice for the highly fragmented water sector to increase its viability and sustainability. While these interviewees' opinions of the optimum number of water utilities differ from 10, 20 to 100 or even more, the idea of merging water services as such is clearly dominant. Large, regional water utilities, preferably Limited Companies, would be able to solve the challenges the water sector is facing.

“Just now we are planning this regional cooperation with seven municipalities and I think this is the future and then we will be a limited company.” (Water Utility Manager)

“I think what should happen and what will happen is that we have bigger unit operations.” (Water Utility Manager)

“Our future strategy is to promote cooperation between municipalities and join water utilities together...then they are outside the municipal organization, they are limited firms, owned by municipality and they are more independent to make decisions than as a part of the municipality...for the small organizations it is important to be part of a bigger organization to have a better future...I think we need structural changes.” (Water Actor)

First, water sector actors argue that all water works, whether small or large, will feel the effects of the retirement boom; it is easier for larger utilities to rearrange parts of their staff and hire new ones than it is for smaller water works, where even up to 75% of workers may retire within five years. In extreme cases of the smallest units, often only three to ten workers take care of the service and they may all be between 58 to 63 years of age, and therefore a 100 percent would retire within five years, which leaves the municipality only the option of contracting out the water and sanitation services to a company or a neighboring municipality.

The future larger units are also regarded as more attractive for skilled people to work in because they offer a wider range of activities and career possibilities, which is an important argument when competing for skilled labor in the future. Further, with increasing scale increases the availability of resources for more professional management, such as calculating investments and water tariffs that would in fact recover the full costs of the service as opposed to the present practice in many small units, where the exact cost of the service may not even be known or is foremost a subject to municipal policy.

Some municipalities are facing problems with water supply because groundwater or surface water that is used for drinking water is not as easily available on their territory. Larger, regional utilities would have better options for acquiring drinking water than small autonomous water works because of a larger territory and because individual
contracts between municipalities for the purpose of transferring drinking water would be unnecessary. This is a challenge that concerns small municipalities but also large cities. For example, the municipality of Pirkkala, with 15,000 inhabitants, does not have its own groundwater resources and uses water from the neighboring city of Tampere, with 200,000 inhabitants. The City of Hämeenlinna with 47,000 inhabitants also needed better drinking water resources until recently, when a joint water company was established with its neighboring municipalities which improved the possibilities for the city to acquire drinking water.

“From the strategic viewpoint of the small municipalities, the water utilities need to merge because of lack of water resources and the difficulties to maintain adequate level of water supply. Especially in the future when regulations are becoming stricter the lack of competence can be noticed…also the water tariffs have to be calculated more professionally, based on the real costs instead of being only political decisions.” (Water Utility Manager)

“The large municipality needed the ground water resources in neighboring municipalities for the future. Now it is much easier to exploit new fields.” (Water Utility Manager)

In addition, because small water works lack professionalism, they often lack professional records about their infrastructure which means that employees may be the only ones who know the state of certain infrastructure; once they retire it is hard to create an accurate knowledge base for future employees and the work that needs to be done to keep networks and infrastructure functional. A larger unit that has more resources at its disposal would be better organized and hence able to create records of all infrastructures and safeguard the functioning of water services. It would also be better able to plan investments because as it deals with a wider territory once an inventory of the assets and their condition is created, the utility is able to prioritize the most urgent projects by concentrating resources on them. Further, the effects of increasingly stricter standards and regulations, which are especially challenging for smaller utilities, could be better managed through prioritizing investments.

“I think challenges for the water sector are how to operate these small utilities in the future, their problems with operation, water quality and distribution disturbances…the risks are getting higher all the time. Their workforce decreases while standards increase…” (Water Utility Manager).

“When we merged with those small water works we saw how bad the situation was in some cases. Some did not have adequate records of their networks, another lost more water than was consumed. But we could prioritize our investments and resolve those problems.”(Water Utility Manager)
Utility managers argue that a large utility is better able to acquire capital for its investments from the outside markets as it has more administrative and financial experts who are able to plan investments and forward their proposals to lending institutions, such as the state, the municipalities, or large, international development banks, such as the European Investment Bank. Larger utilities would therefore also allow employing a variety of experts from fields that are non-engineering related but nevertheless are important for managing a modern water utility, such as people with traditional business and legal expertise.

Merging water works with each other demands that the various parties involved in the process agree on the appropriate setup for the future company. This includes issues such as whether employees will be able to keep their workplaces or whether they will have to be released and whether the nature of the employees’ work may significantly change, possibly against their will. The decision-making power among the shareholders has to be decided by assigning the seats of the company’s board to individual municipalities in a manner that not only takes their shareholdings into account but also the power imbalances that will result from it. For example, if the largest utility represents more than all other joining utilities combined, it may be decided to grant the smaller utilities extra powers and seats on the board in order to decrease their feeling of being ‘bear hugged’. The asset value and sales price, as well as the tariffs, profits, and future investments are crucial issues as well.

Among the water experts that I interviewed, I found a widely shared agreement when it comes to merging water utilities with each other. Their jobs are safe even if efficiency would drastically increase because a large part of the workforce will leave the company for retirement. In fact, the utilities may suffer from a shortage of labor in the near future. The loss of the community’s water works’ local character is seen in connection to an improvement of the services and safeguarding its sustainability. To agree on decision-making powers and financing issues is not the water professionals’ task but the one of politicians’, and that is perceived by water utility managers as the biggest obstacle in merging the water utilities.

If large, regional water utilities would be created to secure the functioning of water and sanitation services of a wider territory, the interests of individual municipalities would have to decrease. Also, the legal title of the company would change from a municipal enterprise to a limited company. However, good cooperation between the water utility and the local municipality is necessary because water sector investments are closely linked to municipal strategies and investments. The water utility would have to be more flexible than it is at present, where its strategy is often compromised by the municipalities’ overall strategy, especially in terms of infrastructure rehabilitation as it requires investments that decrease the short-term profitability to the municipal owner. Further, water utilities need to make their operational decisions more independently and need to have the possibility for choosing contractors from the private sector whenever it
is necessary—as opposed to the present situation, where the utility is often required to purchase the service from the municipal organization, which is more expensive. In this context, changing the legal title of the organization from a municipal enterprise to a limited company is regarded as a useful tool to gain more autonomy.

“The limited company is in practice quite a flexible organization, which is another reason for establishing it. We should say who we hire, how much we pay.” (Water Utility Manager)

“We own the vehicle park ourselves. Earlier, they belonged to the city, but we paid too much and they were in very bad condition. When the water company was established, we took all the vehicles, and now we have good vehicles, they are in good condition, and all are very satisfied.” (Water Utility Manager)

Another key strategy is to increase the role of private sector companies in order to cope with the future labor shortage, but also to benefit from the private sector companies in cases where they are able to provide a service to a more competitive price and quality than the water works can. A clear distinction is made between hiring private sector companies to do contracting work in construction or maintenance and granting long-term contracts (for example, for operating entire water works or treatment facilities). Here, all long-term operation and management especially of water and wastewater treatment plants is regarded a core competence of the water utility that should not be contracted out to the private sector. But this is seen in a pragmatic manner rather than a decision per se. If it should become necessary to contract out also the operation of such treatment facilities for example because of labor shortages, it may be done.

“Just like other [private] companies, we also concentrate on some key areas to develop in our own organizations, and outsource some activities. But we must also in the future be the owners of the system and take care that the operation and maintenance will be done accurately. We should take care of operation and most of the maintenance of our water and wastewater treatment plants, our pipelines, but maybe not constructing the new ones and rehabilitating, but we may just follow up and control that the quality is good enough.” (Water Utility Manager)

“Also the administrative services, such as billing and accounting could be outsourced...that is a problem because most of the Finnish water utilities have lot of difficulties with their billing programs because these programs are not ready when they are introduced in operation...we worked two years to get it working. [...] There is no sense in it when hundreds of water companies are dealing with these problems in IT on their own.” (Water Utility Manager)
One may ask where the private sector should get sufficient labor in order to provide its services to the water utilities when the retirement of the post-war generation will create a general shortage of labor in the market. Here, the private sector companies are regarded as more successful and more attractive workplaces for young skilled labor. But increasing the water utilities’ size and flexibility should make the water utility as much of an attractive employer as private companies are perceived to be. At the moment, the time is not right for outsourcing operations that are considered core business. But it is a matter of definition what core business means. For most water utility directors it includes water and sewerage treatment plants, but not for all. Timing is very important in these matters and therefore even if outsourcing the operations of treatment plants is desired, it may have to wait until more staff has retired, the utility is more independent from the municipal owner, or it has been restructured.

“In the future, there could be only a small team of people who manage all the outsourced tasks, maybe one sixth of what we have now. But that would mean to outsource everything we can, such as the wastewater treatment process, water purification processes, network production which means repairing and maintenance, and all kinds of planning services.” (Water Utility Manager)

“We have to open the water sector to private companies and we should […] concentrate on the management of it, which is the core, we should go to the management.” (Water Utility Manager)

“There is a plan to build a big wastewater treatment plant in ten years from now, it will be very large and should compensate for all plants of the greater area. By then, it would be possible to be a private project but right now, it would be a public one.” (Water Utility Manager)

4.2.4.3 Human Resources Challenge

The age structure of employees working in the water sector is a problematic one in terms of large-scale retirements and knowledge transfer to younger employee generations. According to a survey conducted by the Finnish Water and Waste Water Works Association in 2001 (FIWA, 2003), approximately 35 percent of the 5,000 water sector employees were born in the 1940s or earlier and nearly 40 percent in the 1950s. This means that by 2010 to 2015, nearly half of the workforce employed in the water sector is about to retire (ibid.). This fact alone drives several other developments and changes that are about to come. Knowledge transfer is affected by the retirement wave since many water works have not hired sufficient new employees in the past years. This is emphasized by the fact that only about 17 percent of persons employed in the sector are born in the 1960s and eight percent in the 1970s or after (ibid.).
The difference between small and large water works is not significant in terms of age structure, but for very small water works where, for example, only a group of three to ten employees may be employed, the retirement may cause a reduction of staff from as low as 25 percent to as much as 100 percent. Small water works lack the practices which are common in larger water works—for example, keeping explicit records of their operations and infrastructure (records which only exist in the employees’ memory). Therefore, this information may leave with the employees once they retire and thus, the retirement boom’s impact is greater on smaller utilities than on larger ones. In large utilities, directors feel that their organization could be more effective with fewer employees. Utility directors argue that the water works do not require that many workers anymore as were hired between the 1950s and 1970s when the system expanded, but they are not able to decrease the amount of their workforce because of public sector and municipal employment politics.

“From those who retire we lose a lot of tacit knowledge, especially in smaller utilities where they didn’t hire anybody new to transfer it. In some places only the employees know the condition of the networks…there may be some service disturbances in the future.” (Water Utility Manager)

“We in the bigger cities all have too much personnel and we have a strategy to start buying services from private markets little by little…but there is so many people that we have to do it slow. And opposition from employees and their labor unions would be quite intense.” (Water Utility Manager)

Water utility directors also expect that once the large scale retirement sets in, it will be the biggest facilitator for structural changes, which are overdue but could not be executed yet because of difficulties with upset employees and the labor unions. Once labor shortage sets in, it will create conditions that only allow for a narrow set of options where pragmatism will have to prevail over ideological or self-interested behavior of employees, unions, or municipalities. Also a cultural change is expected towards a new, more entrepreneurial and business-like attitude by hiring younger, new employees to the water utility or through contracting out more tasks to the private sector than before.

However, the competition for new employees is expected to increase, as labor shortage is expected for many sectors, especially in those, which are perceived by the public as less attractive to work in. As a result, some utility managers have voiced their concerns that the competition for new employees will lead to more outsourcing to private sector firms. Here, the private sector is perceived as more dynamic, competitive, and as more desirable workplace than the public owned water utilities. Especially under present circumstances where the utilities’ autonomy is still rather limited and the organization is perceived as too static, it is not attractive enough to young job seekers who may want to work in a more dynamic environment.
“The bigger water works have quite good employment and career possibilities but I think the young people want to work in the private sector. That’s a problem if we think ahead a couple of years...we are not so attractive the way we are at the moment.” (Water Utility Manager)

4.2.4.4 Summarizing the Challenges and Solutions for Water Services

The main challenges and their solutions have been presented by using qualitative material derived from interviews with the managers of water utilities that belong to the elite that emerged during my analysis of relevant actors for the strategic decision-making about water services in Finland.

The main challenges comprise deteriorating infrastructure, large scale retirements, and stricter legislation and the tools required to solve these challenges comprise greater managerial flexibility, more financial flexibility, and a higher level of professional skills and diversity of skills. The managers I interviewed proposed certain organizational changes to supposedly bring them these tools, including increasing the size of utilities by regional mergers (regionalization) and increasing the autonomy from municipalities either by stricter separation from their decision-making or by establishing economic regulation.

These challenges were presented to establish a clear picture of the managing directors’ views that is empirically grounded rather than adopted from literature for three reasons. First, the solutions for challenges in water services require knowledge of their contexts in order to avoid the mimicking solutions that have been adopted in other countries or regions. Second, it gives the reader a chance to gain an insight into one particular view of how water services in Finland should be managed and compare these views with their own or those of water utility managers in completely different areas of Finland (such as remote, sparsely populated rural areas), if such information would be made available through scientific study. Third, differences among geographic territories in the Finnish water sector are rather significant and although remote, rural areas of the North for example may face similar challenges than larger growth centres in Finland’s South in terms of investments or human resources, it may require different, context-specific solutions and organizational changes for each case.
4.3 Commercial Actors and the Emergence of Financial Actors

The following sub-chapter provides a part of my field analysis where I demonstrate that among private sector actors, it is the financial actors that have become most relevant for the strategic decision-making about water utilities in the past ten years. In order to do that, I am explaining how commercial actors have been trying to affect the water sector and why financial actors emerged as the most relevant actor group. I am using the term ‘commercial actors’ to include all relevant organizations with commercial interests in water supply and sanitation. This comprises organizations and companies which are purely private owned such as investment banks, international water corporations, or industrial services companies, but also municipality-owned enterprises, such as municipal energy companies (Table 4-3).

Table 4-3 Changing Roles of Commercial Actors in the Finnish Water Sector

<table>
<thead>
<tr>
<th>Actors</th>
<th>Actor’s Goals and Actions</th>
<th>1995</th>
<th>2000</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Multinational Water Services Companies</td>
<td>Offers/investigations for partial or full privatization by French Multinational</td>
<td>Offer by Thames Water to buy Kemwater Services</td>
<td>Monitoring the sector</td>
<td></td>
</tr>
<tr>
<td>Jaakko Pöyry &amp; JP-Skansa (Infrastructure &amp; Services)</td>
<td>JV JP-Skansa company established for owning and/or operating WSS</td>
<td>Divestment but ready for comeback</td>
<td>Focus on industrial clients</td>
<td></td>
</tr>
<tr>
<td>Kemira &amp; Kemwater Services (Chemicals &amp; Services)</td>
<td>Strategy to become WSS operator but difficulties to grow in Finland - seeking growth outside Finland</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>YIT (Construction &amp; Services)</td>
<td>JV with Kemwater Services. YIT owns &amp; Kemwater operates sewerage treatment plant</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Helsinki Water (Water Utility of City of Helsinki)</td>
<td>Co-founder of Kemwater Services in 1999 and holds 49% until selling to Kemira end of 2002</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>PWC Finance (Financial Consulting)</td>
<td>Consulting in regionalization projects of the water sector</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>PCA Finance (Investment Banking)</td>
<td>Privatizing WSS</td>
<td>Sale-lease-back for Energy &amp; Water Utility</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Icecapital (Investment Banking)</td>
<td>Privatizing energy</td>
<td>Privatizing water</td>
<td>Merging water utilities with energy utilities</td>
<td></td>
</tr>
<tr>
<td>Jyväskylä Energia (Energy Company)</td>
<td>City merges Water &amp; Energy Utility</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Suur Savon Sähkö (Regional Municipal Energy Company)</td>
<td>Diversification into WSS</td>
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<td></td>
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<tr>
<td>Savon Voima (Regional Municipal Energy Company)</td>
<td>Diversification into WSS</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kauppalehti Newspaper</td>
<td>Coverage of water services as development assistance domestic and abroad</td>
<td>Coverage of water services as next sector to be privatized and restructured</td>
<td>Coverage of water services as in need of investments, discussion of different options, merging water and energy together</td>
<td></td>
</tr>
</tbody>
</table>
To this analysis, I also include a longitudinal content analysis of the largest Finnish business newspaper Kauppalehti, which I see here as commercial actor but also as a way to track the commercialization of water services in media. I am providing this analysis of the commercial actor’s activities and interests in the water sector because it allows demonstrating their relevance to the changes that appear in the sector, as well as their tactics. As a result of this overview and analysis (as presented in Table 4-3 on the previous page), I show that the financial actors are the most influential among private sector actors in affecting the water sector and thus, their role is more important in understanding the structural and institutional changes in the Finnish water sector than the role of industrial services companies and multinational water corporations.

4.3.1 Commercial Actors and the Commercialization Process

Referring to Table 4-3 (previous page), during the time period of 1995 to 2006 approximately one dozen commercial actors could be identified that have been trying to affect the Finnish water sector either by promoting privatization; by trying to acquire the partial share of a utility; by receiving concession and outsourcing contracts; or by promoting structural change that would benefit them in some other, mainly financial form. Based on these actors’ principal domain and ownership structure, I distinguished them into: multinational water corporations; domestic industrial suppliers and services companies; domestic private investment banks; and fully or majority municipality-owned energy companies. Further, I included in my analysis the coverage of WSS a business newspaper, which can also be regarded as an actor since it not only provides a forum for different stakeholders to discuss their opinions, publicly, but also because as a newspaper targeting the business community, it pursues commercially-oriented interests.

4.3.1.1 Multinational Corporations in Water Supply and Sanitation

At least one of the two largest French multinational water services companies has been trying to enter the Finnish water sector from the mid-1990s. The company tried to offer capital directly to municipalities for their entire water utility, but after being declined, its tactics changed to offering to become a partial owner. After the company’s plans did not materialize, it switched from this proactive approach to a more observing one and keeps monitoring the market. It continues contacting Finnish water sector and municipal actors about the prospects of cooperation and privatization.

“I had a representative of a big French water company here in my office with a suitcase full of cash [figuratively speaking]…they offered us a huge sum for a part of our utility but we didn’t take it…we didn’t need it” (City Manager)

“I have contact with these multinational companies once in a while, maybe every two years or so, and they check what is going on, but they probably have closer contact with the cities themselves, but I don’t really know.” (Water Sector Manager)
Finnish municipalities declined their offer because the larger water utilities, which are the most interesting ones for a private corporation to run since they offer the highest scale effects, are relatively well-managed. These utilities do not require such urgent and large investments that the municipalities would have to obtain capital from third parties, such as by taking a private owner on board. Further, before the Finnish municipalities would have to prevent their own bankruptcy by partly or fully selling their water utilities they have another alternative. At present, the water utilities’ assets are valued at historic costs (the costs incurred at the time of construction) and by incorporating the utilities as limited companies, their asset valuation could be changed to present cost (the value of assets if they were constructed today and by using present technologies), which approximately triples to quadruples their asset value. This would allow using the increase in value as collateral to borrow from banks in order to finance investments or balance the municipal budget.

“After we sold our energy utility we have to be very careful about what we do next…our employees and the labor unions are very sensitive about selling anything else…and some think we sold the energy company too cheap, some say we should not have done it at all…there has been a study that in those municipalities that sold their energy utilities, the prices went up, and I guess that makes people more careful now about the water utilities as well” (City Manager)

“The cities are not selling their water utilities right now because they can release their capital in other ways, by changing the accounting method and increasing the book value of their assets…but maybe after they have done that and used that money they will start selling…maybe first partly…their water utilities, in maybe 10 years or so” (Financial Consultant)

Another multinational water corporation, from the UK, had been trying to gain access to the market by offering to buy (either partially or fully) a subsidiary of a Finnish industrial company, called Kemwater Services (Corporate Parent: Kemira) that focuses on providing wastewater services to industrial and municipal clients in Northern Europe and was also trying to increase its market share in Finland. By gaining control of a domestic company, the British company had hoped to get a foothold in the Scandinavian markets, but its offer was declined since Kemira was confident that it would achieve its goals without taking the company on board. Selling Kemwater Services at that time was out of the question since it was hoped that the company would substantially grow over the coming years and become a major contributor for the parent’s company’s overall results in the future.

“A [large English private water company] made an offer to our parent company to purchase us…because they want a foot in our market, but we didn’t sell…we don’t need them and our strategy is quite clear…we want to grow our water business in Finland and internationally, and for municipalities and industrial clients. ” (Private Sector Manager)
All three transnational companies have in common their main focus on structural change by offering to acquire (either fully or partly) an organization that operates within the market, and gaining at least a first foothold in the market. The fact that these actors have been monitoring the Finnish water sector and periodically make contact with key actors shows that their strategy is to wait for the right time. These corporations chose to interact with the owners of the water utilities rather than with the utilities themselves, acknowledging that the power to make strategic decisions lies with the owner and, hence, the municipality or city. In the case of the French corporations, it has been doubted by a number of interviewees whether the Finnish water sector is interesting for the French companies at all, since they usually operate urban water works that take care of several hundreds of thousands of citizens and only a handful of Finnish cities’ utilities would fall into that category. Nevertheless, these transnational corporations are monitoring the Finnish market, which is a sign of their interest; the fact that relatively small utilities in Finland are also rather profitable organizations may be one reason for it.

4.3.1.2 Finnish Industrial Services Firms

The analysis produced three Finnish industrial services companies that have tried to enter the market for water supply and wastewater treatment in Finland. Additionally, this includes the water works of the capital, Helsinki, which shortly pursued such plans by cooperating with one of these industrial companies.

The globally operative Finnish private sector engineering consulting and industrial services company *Pöyry Plc* has tried to start a water services business in Finland. Pöyry set up a 50-50 joint company with Skanska Group in early 2000, called JP-Skanska Water OY in order to provide municipalities and industrial companies with wastewater treatment and environmental services. However, operations were discontinued within a year because the market for municipal and industrial water (and in particular wastewater treatment) had not developed as expected. An agreement between the pulp and paper industry and its labor unions to refrain from outsourcing made JP6-Skanska’s business targets impossible to reach. Municipalities and their water utilities still preferred to arrange treatment activities in-house. But Pöyry remains ready for entering the market again, once the timing is better. In the meantime the company continues to build expertise from its water operations in foreign countries and is monitoring the situation in Finland.

“We tried to get a business started, but it didn’t fly. We had a joint company with Skanska, and the idea was that the outsourcing of the operation of wastewater treatment for pulp and paper industry would show the way so to say, and three months after we had established this company, there was a trade union contract in pulp and paper industry that they will outsource nothing. The problem started with an effort to outsource cleaning services in these mills, and there was a huge threat of strikes and the outcome was the

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6 JP are the initials of 'Jaakko Pöyry Group', which was Pöyry PLC’s official company name before it was re-branded in 2006.
agreement that made our business target impossible. Also the municipalities did not outsource as we expected...everybody thought that now will be the time...but it didn’t happen, and those who say now, that ‘now is the time’ are probably wrong as well...but in case something really starts changing, we will start a business there...it does not take that long to build our expertise in that area because we have our overseas operations in Asia and also do some work in France, and we can utilize that expertise then.” (Private Sector Manager)

“Lobbying for a European water privatization just does not make any sense because the decision-making is so decentralized in that question and we do not have the resources to spend time and money on that issue, constantly...we will just wait and see what happens” (Private Sector Manager)

The construction company *YIT Corporation* formed a consortium with Kemira Chemicals Corporation and its subsidiary Kemwater Services, which signed a contract with the municipality of Haapavesi and the dairy company Valio OY in 2002 for the purpose of building, owning, and operating the first privately owned and operated wastewater treatment plant in Finland that takes care of the combined wastewaters of the large dairy company and the municipality. YIT constructed and owns the facility, while Kemwater Services is responsible for its operations. The consortium won a tender competition including the renovation and operation for 12 years that was organized by the municipality and Valio, and it was the first case in Finland of outsourcing construction (by YIT), financing (by OKO Bank), and operations (Kemwater) to a private company or consortium (Haapavesi Wastewater Treatment Plant OY). YIT also has the possibilities to enter the water market in the near future through its extensive expertise in maintenance services. The company has been targeting the highway and street sector as well and expects in the long-term to increase its activities as a domestic operations and maintenance services provider for the public sector.

*Kemira Chemicals*, a Finnish-Swedish owned chemicals and industrial services company, established a daughter company called Kemwater Services as a joint venture between Kemira and Helsinki Water in 1999 (a share owner was the City of Helsinki). Kemwater Services is based in Finland and has been trying to receive management contracts for operating water and wastewater treatment facilities in Finland. Due to the lack of business opportunities in Finland, for similar reasons as in the case of Pöyry Corporation, the company became more active in growing its operations in neighboring countries and its management plans to focus on the foreign markets until business opportunities in Finland have improved. In the beginning of 2003, Kemira acquired all shares previously held by Helsinki Water and became the sole owner and still hoped for significant growth of its operations in Finland and abroad in the near future. However, the companies’ expectations were not met and Kemwater Services was re-integrated into Kemira in 2006.
“There are now some private companies that think that municipalities are going to give them outsourcing contracts, soon, any time...any day...but I remember that we thought the same thing in ten years ago [in the mid 1990s] and it didn’t happen...and I don’t think it is going to happen now, either”

(Manager of an Engineering Consulting Company)

In connection with Kemira Corporation, Helsinki Water (the water utility of the City of Helsinki) had been trying to expand its operations. The company started a joint venture with Kemira Corporation by founding Kemwater Services and owning a 49% minority stake. The goal was to receive management and operation contracts from water works across Finland but business started too slowly and Helsinki Water divested from this venture by selling its shares back to Kemira.

In both cases, of Pöyry Corporation and Kemira Corporation, it was expected that municipalities as well as large industrial companies (especially the pulp and paper companies) would soon start outsourcing the wastewater treatment, although both companies’ attempts are five years apart from each other. Pöyry tried it in the late 1990s and established a company for that purpose in 2000, while Kemira did so in the early- and mid- 2000s. Actors in the water sector in general had at both times the expectation that things would soon turn in favor of outsourcing providers, but they were disappointed. However, it needs to be mentioned that in 2006, a small municipality named Askola outsourced its technical services operations (including water services) to the Swedish-based company Coor Services Management and thus, small, recent developments in the market are noticeable.

4.3.1.3 Financial Actors

Two private investment banks and one financial consulting firm emerged during the analysis as relevant actors for the water sector.

PWC Finance is the financial consulting division of Price Waterhouse Coopers Finland, and it became active in consulting municipalities on regionalization projects in water services in the beginning of the 2000s after a manager joined the firm who previously tried to promote water services privatization by selling private capital to municipalities. PWC Finance has been working with a number of municipal regions on developing solutions for the financial aspects of establishing regional water utilities, such as the distribution of investments and profits among municipal prospective partners. The firm is advising municipalities on creating regional, municipality-owned water utilities rather than trying to promote the privatization of utilities. This represents a learning process where the consultant accepted the momentary market conditions by adapting to them and providing the municipalities with the kind of concepts and solutions that they ask for. Hence, the firm focuses now on the financial side of regionalization projects of water services by finding arrangements to distribute financial benefits and risks among municipalities in such a way that they would be acceptable for all parties.
“I have been trying for three years to sell private money as a representative of the private sector to the municipalities but they are not very keen because they can release the capital in other ways and they are not planning to sell the water works…and because they don’t want to privatize, so we made a concept that they are regional water companies under a limited company…fully owned by the municipalities.” (Financial Consultant)

*PCA Corporate Finance* (later acquired by HSH Gudme Corporate Finance) is a company that also offers investment banking services for utilities and the public sector, including energy, where it had a strong expertise due to senior staff coming to the company from the energy sector. After trying to promote privatization of water services for a relatively short time around the year 2000, PCA Finance had adapted to the ownership policies of the municipalities and developed a sale-lease-back concept for public utilities that was supposed to be applied to the City of Lahti, for the water utility and the energy utility. As a sale-lease-back project, it was supposed to be a compromise for releasing capital without letting completely go of the control over assets. The project did not succeed as it faced resistance from the city council.

“We [the investment bank] took the initiative…there was a new major…and I knew him very well, and we discussed already before…about this concept… I didn’t recommend anything, I just said which options he has…both the major and the financial director…felt this is from the owner policy view much easier politically to sell in the city than selling the whole utilities. [Our] point was that we have to create a concept which actually is...somewhere in the middle…not to keep it all as it is today, but also not to sell it all away… if we can’t create new concepts like this, nothing happens in the market. And if you create this type of new businesses, those parts of these businesses where competition is possible may be sold later, and we will be there doing it.” (Investment Banker)

The investment bank *Icecapital* has been rather active in assisting the privatization of municipality-owned electricity companies after the liberalization of the electricity market in 1995 - 1998, and subsequently targeted the water sector as being the next sector that could become privatized. However, after a few years the company adapted, in the early 2000s, to the logic of the municipalities, and instead of promoting the straightforward privatization of water utilities, it started promoting the sale of water utilities to energy utilities, creating multi-utilities.

“Water utilities as enterprises are still very close to the municipal administration and…the municipality has very heavy decision-making power in the investments, the strategy, and the direction for the water company. The owner thinks more about profitability and about keeping the investments at a minimum…there has to be found a solution that satisfies the owner’s profit needs and the investment need of the utility…for example by raising the tariffs, and…more productive ways to provide the services.” (Financial Consultant)
“From this concept’s point of view, it is the same whether it is the water or electricity or whatever that is integrated. It does not make any difference. And the value of these networks is huge in Finland…we are talking about millions.” (Investment Banker)

Icecapital’s expertise in energy-related questions is especially solid, which is a characteristic that also applies to PCA Finance. The financial actor’s strong competence in energy-related issues is a result of the former liberalization of the Finnish electricity sector where sector-wide restructuring took place and several Finnish municipalities partly or fully sold their electricity utilities to the private sector. The liberalization of the electricity sector and the following organizational and financial restructuring of utilities required the expertise of a relatively new set of actors, namely, the financial actors or investment bankers. The demand for this kind of expertise attracted persons from the energy sector to switch to the financial and investment banking sector, where they started to provide expertise especially on financial aspects of restructuring municipal energy utilities, including their sale or partial sale to private companies. This line of business has provided investment bankers with sufficient work during the late 1990s but their services have also become useful to municipalities in restructuring other municipal assets and utilities, such as water utilities. The contacts which financial actors have been forming with municipalities during the liberalization of the electricity sector and are also beneficial when it comes to creating new business for financial actors concerning the water sector.

Icecapital advised the city of Jyväskylä on its asset restructuring and merger of its water utility with its energy utility in 2004. The case of Jyväskylä represented the first time of a larger multi utility company in Finland owning and managing water and energy within one company. Further, Icecapital has been the most visible private sector actor in a discussion about the future of the Finnish water sector in the Finnish business newspaper, called Kauppalehti, where the firm had been clearly favoring and predicting the privatization of water services around the year 2000, but thereafter lowered its expectations in this regard and promoted merging water and energy utilities (refer to the analysis of Kauppalehti below).

4.3.1.4 Municipality-owned Energy Companies

The city of Jyväskylä merged its water utility with its energy utility in 2004 with the help of Icecapital. The case of Jyväskylä represented the first case of a larger multi utility company in Finland that owns and manages water and energy within one company. Since then, the energy sector’s interest in the water sector has been on the rise. For example, two municipality-owned (or majority-owned) energy companies, namely, Savon Voima OYJ and Suur Savon Sähkö OY, have been voicing their interest in diversifying into water services.
The development of creating multi-utility companies that manage energy, as well as for water services, is partly driven by investment bankers. Their extensive experience with energy utilities comes from previous employment at such companies or years of consulting in the energy sector. That has provided investment banks with relationships to the energy sector and the municipal sector as well, because the sector has been fully municipality or public-owned prior to its liberalization, and many energy utilities are still municipal-owned today.

In the case of Savon Voima OY and Suur Savon Sähkö OY, the plan is to merge several smaller water works under the roof of the energy company and to manage them as a daughter company. Hence, a regionalization of water services would take place in this case, although the new water company would not be independent but inside the energy company. Regionalization of water services would therefore be taking a ‘detour’ by first merging with an energy company. This route, however, bares implications on the private ownership of water supply and sanitation because full or partial private ownership of energy utilities. When the ownership of an energy company that also owns water services operations changes from public into private hands, it automatically moves the water services activities into private hands as well. While energy-related activities are under regulatory supervision that supervises economic issues such as pricing, quality, and investment policies, the water-related activities are only regulated according to environmental and health issues. This would allow a commercially-oriented energy and water company and thus, a multi-utility company, to operate its water activities as unregulated monopoly. If shares of such a company would be sold to private investors, it would result in a full or partial private ownership of water services and hence, private ownership of a natural, unregulated monopoly. For example, according to the annual report 2005 of Suur Savon Sähkö OY, the ownership structure of this municipality-owned energy company already includes ‘other organizations and companies’ holding 30.6% and private shareholders owning 7% of the company.

4.3.1.5 Kauppalehti as Actor and Forum for Water Commercialization

The following longitudinal content analysis of Kauppalehti newspaper should be seen as to complement the interview data and support the argument that the commercial and business interests of actors have increased over the past decade. Among daily newspapers and magazines, the business newspaper Kauppalehti had been covering water services most extensively and at least since 1995, which represents the starting date for the analysis at hand. Media and especially mass media, such as the Kauppalehti newspaper, can be a powerful actor as it may affect public opinion and therefore, it is different from professional journals that usually reach only a small circle of experts and professionals working in a sector (e.g. 5,000 copies) although these small journals may also be important because they may be read by policy makers. Therefore, Kauppalehti News is not only a daily business newspaper but because of its potential to decide what to cover it may affect public opinion and needs to be considered also an actor in its own right.
In order to provide a longitudinal description of how water supply and sanitation was covered in the magazine and how that has changed over the years, I chose the time period of January 1995 (beginning of energy market liberalization) to March 2006 (latest data available when the empirical analysis for this study ended). On basis of my analysis, three periods of different thematic coverage emerged. I named the first period ‘the phase of development assistance’ which lasted from 1995 to 1998, followed by the second period of ‘privatization interests’ from 1999 to 2002, and the third period, named as ‘the phase of restructuring and commercial interests’ from 2003 to 2006. The following paragraphs briefly summarize the characteristics of these phases by referring to Figure 4-7 (a more detailed account of the analysis is to be found in the appendix).

As depicted in Figure 4-7, the newspapers’ coverage of the water sector in the middle of the 1990s was mainly focused on business activities of Finnish firms abroad that were constructing water supply and sanitation in developing countries. Also, development aid that was granted by the European Union to Finland in order to rehabilitate water and wastewater infrastructure, especially in rural areas, was reported. However, the commercial focus in Kauppalehti changed in 1999 by providing a forum to investment bankers that argued for a privatization of Finnish water services while also publishing articles that report on the poor condition of water and wastewater infrastructure in Finland and thus, on the investment needs.
But the articles that seemed to promote or at least suggest privatization as an option for the Finnish water sector to acquire new capital stopped in 2002 and it became rather quiet in 2003. However, while 2003 was a quiet year for articles in Kauppalehti about water services, it becomes clear in the articles of 2004 that actors had still been rather busy in the previous years. This was noticeable by the unsuccessful attempts to privatize water services that were admitted by investment bankers; they changed their proposals for restructuring the water services by promoting mergers between water and energy companies.

In 2006, the discussion had clearly shifted into the direction of creating energy and water multi-utilities as also municipality-owned energy companies pronounced their interest in Kauppalehti. From this perspective, the issues in the water sector have been changing from commercial interest of in fact privatizing the water sector (during 1999 to 2002) to merely restructuring it and finding new organizational forms, including creating water and energy multi-utilities (in the years 2003 to 2006).

Almost all articles published from the year 2000 onwards discuss the renewal of the domestic WSS in some way, even though from rather different angles. Those who would like to see the water utilities merged with electricity utilities have some kind of change and renewal in mind, as do the water professionals who argue for a water sector independent from the electricity sector. Therefore, both parties argue for change but in different ways. An increasing business interest in the Finnish water sector is noticeable in these last two periods. The development started with information about the serious and worrying condition in which the Finnish water and sanitation sector, especially in rural areas, seems to be, followed by a report on the problems with financing necessary infrastructure rehabilitation. Subsequently, privatization is suggested by the investment bankers as a means to inject new capital into the sector and finance infrastructure rehabilitation. After that, interest by the electricity sector (especially the municipality-owned electricity utilities) starts to surface. As a result, the discussion between water, electricity, and investment banking professionals gains momentum. During the last two periods, water professionals (mostly academic experts but not water utility directors) ‘defend’ the water utilities in Kauppalehti News and argue against merging water and energy. They try to maintain the water sector’s professional boundaries by openly arguing for more independence from the municipal owners and restructuring inside the water sector.

Therefore, the business newspaper Kauppalehti allows to trace the commercial interest in the water sector as it changes from foreign and domestic development – related infrastructure construction to ownership and operational changes by proposing privatization and last, to giving up privatization and acknowledging the municipalities’ determination to hold on to their utilities but also to propose and promote the merging of water and energy companies. This development shows that the initial intention of financial actors to promote the privatization of water utilities did not succeed and after a
period of learning they adapted to the municipalities’ needs for capital and restructuring without privatizing their water utilities. Therefore, the content analysis of Kauppalehti also provided insights into how financial actors adapted to the circumstances in their environment.

Instead of attributing significant power to their ability to influence other actors and create change, the investment bankers’ success needs to be seen in terms of staying in the game by adapting to the powerful actors’ logics and requirements, which in this case are the municipalities. Nevertheless, the emergence of the multi-utility concept that seeks to combine municipal water and energy utilities is driven by the municipalities’ need for capital and willingly facilitated as well as promoted by investment bankers.
4.3.1.6 Financial Benefit for Restructuring Municipal Water Utilities

The articles in Kauppalehti News describe the rise of the water and energy multi-utility concept that developed within a few years to an organizational and economic model, which now seriously competes with the water sector’s own model of creating regional water companies. When financial actors recognized that their attempts to promote privatization in the Finnish water sector are for the moment in vain, they changed their strategies and concepts by proposing alternatives that would also lead to transactions and allow municipalities to release capital and the investment banks themselves to earn fees. The following paragraphs represent a brief analysis of the financial rationale behind the financial actors’ ability to stay in the game and become relevant actors for the municipalities by helping them to find and create money for their municipal budgets. Figure 4-8 depicts the trends of regionalizing water utilities and merging them with municipal energy companies to multi-utilities (based on interviews and information collected from FIWA and Kuntaliitto).

<table>
<thead>
<tr>
<th>Project Objectives</th>
<th>2000</th>
<th>TIME</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Projects to create Regional Water Utilities by merging Water &amp; Water</td>
<td>Hämeenlinna (completed)</td>
<td>2000</td>
<td>2006</td>
</tr>
<tr>
<td></td>
<td>Kouvolan Voima</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Lahti</td>
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<td></td>
<td>Lohja</td>
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</tr>
<tr>
<td></td>
<td>Loviisa</td>
<td></td>
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<tr>
<td></td>
<td>Rauma</td>
<td></td>
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</tr>
<tr>
<td></td>
<td>Salo</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>South-Pirkanmaa</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Kotka (completed)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Kuopio</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Projects to create Multi-Utilities by merging Water &amp; Energy</td>
<td>Jyväskylä (completed)</td>
<td>2000</td>
<td>2006</td>
</tr>
<tr>
<td></td>
<td>Nurmi</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Joutsa (completed)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Kuusamo (completed)</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>Kuopio Region</td>
<td></td>
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<tr>
<td></td>
<td>Mikkeli Region</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td>Vaasa</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Valkeakoski</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Figure 4-8 Restructuring Projects related to WSS from 2000-2006

Figure 4-8 shows multi-utility projects start being planned somewhat later than pure water regionalization projects but quickly pick up pace and even outnumber water utility regionalization in terms of completed multi-utility projects. From the water sector actor’s perspective, the multi-utility concept is against their idea of a municipality-owned, but from electricity independent, regionalized water sector. Nevertheless, the multi-utility trend is emerging because of the municipalities’ need for finances whereas the investment bankers assist them and promote this option.
Financial actors could stay in the game and are still relevant actors in the decision-making about Finnish water utilities, while other private corporations have mostly withdrawn after their unsuccessful attempts to promote change. In order to understand why this has happened, it is necessary to analyze the financial benefit of restructuring the water sector, as most managers across different actor groups that were interviewed have argued that the attempts to change the water sector are predominantly about one thing – ‘money’.

One of the major points about the restructuring of water utilities and making them limited companies or merging them with energy companies is that the water utilities’ assets are re-evaluated in such cases, which leads to a higher asset value. The gains in higher asset value are one of the major motivations for municipalities to restructure their utilities, and they allow the municipalities to release capital that otherwise could only be released through selling the utilities – partly or fully – to private investors. A brief analysis of the water utilities’ finances explains in a more practical manner what the benefits of reorganizing the water sector could be for the owner and the water utilities.

In the following paragraphs I present a comparison of the nine largest water and sewerage utilities in Finland, which are all owned by their municipalities and governed as municipal enterprises and hence, not as limited companies. Two of the largest water utilities are therefore excluded, Lahti Water and Hämeenlinna Seudun Water, because although they are municipality-owned, they are limited liability companies. I have excluded them from the analysis because the re-evaluation of assets is a result of changing the legal title of the organization from municipal enterprise to a limited company. The comparison and calculations need to be seen as estimates because the analysis of a water utility’s assets and infrastructure and its value is a rather complex undertaking, and only parts of the necessary data can be retrieved from the water utilities’ annual reports. For example, one of the problems is that the return on the basic capital (in Finnish: Pääoma) does not only come through the annual returns the utility pays to the municipality. In most cases, charging higher interest rates than the usual market rates for loans given by the owner to the water utility allow the owner to receive an additional return from the water utility. This interest-borne return, however, is not included in this calculation because most water utilities do not report on it sufficiently in their annual reports, and neither do the municipal owners (Näsi and Windischhofer, 2005).
Table 4-4 Comparing Historic and Present Asset Valuation

<table>
<thead>
<tr>
<th>Water Utility</th>
<th>Asset Value Based on Historic Costs (Method currently in use)</th>
<th>Asset Value Based on Present Costs (Method promoted by Financial Actors and used in the Energy Sector)</th>
<th>Changes in Assets and Returns</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Basic Capital (based on historic cost system) M EUR</td>
<td>Annual Return to Owner %</td>
<td>Annual Return to Owner MEUR</td>
</tr>
<tr>
<td>Espoo</td>
<td>67,4</td>
<td>10,0</td>
<td>6,7</td>
</tr>
<tr>
<td>Helsinki</td>
<td>144,3</td>
<td>9,0</td>
<td>13,0</td>
</tr>
<tr>
<td>Jyväskylä</td>
<td>25,2</td>
<td>12,7</td>
<td>3,2</td>
</tr>
<tr>
<td>Kuopio</td>
<td>21,6</td>
<td>5,4</td>
<td>1,2</td>
</tr>
<tr>
<td>Oulu</td>
<td>18,5</td>
<td>18,4</td>
<td>3,4</td>
</tr>
<tr>
<td>Pori</td>
<td>42,1</td>
<td>14,0</td>
<td>1,7</td>
</tr>
<tr>
<td>Tampere</td>
<td>70,3</td>
<td>14,2</td>
<td>10,0</td>
</tr>
<tr>
<td>Turku</td>
<td>109,4</td>
<td>5,5</td>
<td>6,2</td>
</tr>
<tr>
<td>Vaasa</td>
<td>23,9</td>
<td>8,8</td>
<td>2,1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>522,7</strong></td>
<td><strong>9,8</strong></td>
<td><strong>47,5</strong></td>
</tr>
</tbody>
</table>

As depicted in Table 4-4, the nine largest water and sewerage utilities that are governed as municipal business departments have a combined asset value of EUR 522.7 million, according to their annual reports of 2004. This figure is based on the value of their assets measured according to historic cost, meaning, according to the expense that occurred at the time of constructing the assets. For water service infrastructure, the infrastructure life cycle often goes over decades, or even a century, as some parts of the networks have been constructed a hundred years ago and may still remain intact.

The present cost value, however, means valuating these assets according to the expense that would occur if one had to construct this infrastructure today and with present technology and according to present standards in quality and safety. According to financial actors and engineering consulting firms, the present cost value of a Finnish water utility represents on average the threefold to fourfold of the historic cost value. This results in an increase of asset value from EUR 522.7 million to EUR 1.57 billion in case of a threefold increase or to EUR 2.1 billion in case of a fourfold increase.

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7 These calculations are based on information received during interviews and conversations with several experts from the water, finance, and municipal sector on the methodology of these calculations and by using financial data from the water utilities’ annual reports.
In order to maintain a conservative estimate of the potential transaction volume for the selected water utilities, I decided to use a threefold increase of asset value, which results in EUR 1,568.1 million (Table 4-4 on previous page).

“Our logic is based on the regulatory side, which is applied in the energy market and which the energy market authority applies, so we applied the same principle to the water sector. The energy market authority uses the replacement value as the basis of where the return should be calculated because it cannot be calculated on the basis for how much you would buy that water utility, for example including the goodwill, or that much, it can’t be the book value because you have assets of varying ages, you can have new assets, you can have old assets, you always have a mixture of those.” (Investment Banker)

“The financial statements of these companies do not have a relation to the reality of what the real value of the assets is. The real value of the assets is three or four times bigger than the book values.” (Investment Banker)

Because the municipal owner can borrow against the assets of the water utility at the financial markets and the value of assets increases three times, the municipalities of these nine cities would be able to take loans for approximately EUR 1 billion, which represents the lump sum payment, as financial consultants often call it. In other terms, the increase in water utilities’ assets is used by the municipal owner as collateral against which capital can be borrowed from financial markets.

In addition to this lump sum, the continuous revenue flow would increase if the same methodology as in the energy sector is applied to the water sector (the financial actors assume that it would be the case). For the energy sector and electricity utilities in particular, the return of investment is connected to the present cost value of the transmission network, which is on average six percent as permitted by the regulative authority for the energy sector.

Concerning the profitability and annual return on basic capital the return for the water utilities in the larger Finnish cities has often been higher than the six percent in the energy sector. This has been the case for examples in cities such as Oulu, Tampere and Helsinki. Based on the historic value of their utilities’ assets, the return on capital for the year 2004 was within a range of 4 to 18.4 percent, with an average of 9.8 percent. However, the present return on capital in relation to the present value of assets is significantly lower than 6 percent. In fact, on average, the return on capital invested based on a conservative threefold increase in asset value ranges between 1.4 and 6.1 percent, on average 3.2 percent. Switching to a similar methodology of regulating the return on capital as it exists for the Finnish electricity utilities, the owners of these nine Finnish water utilities could increase their returns from 3.2 to 6 percent, a growth by 47 percent.
Under such a new regime, with re-evaluated assets and a regulation allowing 6 percent return on these assets would allow the nine owners to increase their combined annual revenue flow from their water and sewerage utilities from EUR 47.5 million by fifty percent to EUR 94.1 million, if the conservative threefold asset value increase is applied.

From the investment banker’s perspective, the fees that could be earned from the transactions in this sector are rather substantial as the approximate total asset value of only these nine utilities is EUR 1.5 billion (if considering a threefold increase in assets). Basically, transactions of any kind provide the financial actors with income and in this case without even privatizing any of the public assets but just transferring them within the public organization.

The impact of these changes in valuation of assets and return on capital on water tariffs—and therefore on the consumers—is not included in this analysis. However, a rise in prices for consumers seems inevitable in my opinion if the water sector is to renovate its infrastructure according to sufficient quality standards. This rise in water tariffs may be even greater when municipalities continue receiving profits from the water utilities at current levels or try to increase them.

4.3.2 Summary - The Emergence of Financial Actors

In the previous paragraphs, I have analyzed the different commercial actors that have been trying to affect the water sector and split them into three different groups according to the nature of their interests and their roles for the water sector and their success in creating structural or institutional change.

To the first group, which is the less successful one, belong the traditional industrial companies and transnational water companies. Companies within this group had been trying to get a foot in the Finnish market for owning or at least operating water services but could not succeed. While their expectations were rather positive at the end of the 1990s and beginning of 2000s to go into business with the municipalities and their water utilities, these companies had resigned from their efforts to by the mid 2000s.

The second group, which was partly successful, consists of small investment banks, or so-called financial actors. These firms were until the beginning of the 2000s counting on the privatization of the water sector, just as it had previously happened with the energy sector. However, by the beginning of the 2000s they had realized that their efforts to make municipalities sell their water works are in vain. But instead of abandoning the water sector, the financial actors adapted their concepts and efforts to promote structural change and could at least partly enjoy some success by advising municipalities on the restructuring of their assets and consulting them on organizational changes.
Further, I consider the business newspaper Kauppalehti as part of this group of actors because it promoted commercial interests by providing a forum to those interested in structural and institutional change in the Finnish water sector, especially to financial actors. As such, the newspaper needs to be considered an ally of those actors with commercial interests in the water sector, which is demonstrated by the newspaper’s shift of coverage from foreign and domestic-related assistance and construction projects to actually changing the structure of the Finnish water sector by privatizing or combining with the energy utilities.

Compared to the first group that merely focused on structural change of the sector, the second group of actors also made efforts towards altering the institutional logics of the sector by infusing their own arguments for change and creating discussion via mass media. I have also shown that one of the main reasons why financial actors were able to keep participating in the development of the water sector was the municipalities’ need for finance and the financial actors’ ability to adapt to the municipalities’ needs by suggesting concepts that acquire finance that fit to these needs.

The third group of commercial actors that emerged during the analysis consists of the relatively new entrants, the municipality-owned energy companies that are diversifying into water supply and sanitation. I see this development as result of the financial actor’s and municipalities’ logics and activities. Municipality-owned energy companies therefore are affected by the emerging municipal entrepreneurialism and the interactions between municipal and financial actors by being encouraged to diversify their operations into water services. I see their prospects of becoming more important in the future as promising if the entrepreneurialization of municipalities continues and no large-scale reform of the water sector is undertaken because their diversification into water services is supported by municipalities and financial actors.
5 Governance Actors

In this chapter I analyze the different types of governance actors, with a particular focus on the European Union and state governance actors. The local governance level is represented by the municipalities, analyzed in a separate chapter. A longitudinal analysis of the major legislative changes provides insights into the pressures from governance actors towards the water sector. Further, an analysis of state governance actors and how water services should be managed, as well as the nature of that governing process, is provided. These analyses provide the basis for my argument with which I conclude this chapter, that there exists rather strict and transparent governance for water utilities in terms of health and environmental governance, although in terms of economic governance, the water utilities are subjected to rather non-transparent governance.

The state exercises what I call ‘interventionist’ governance by having strict health and environmental governance in a direct negotiation process with the water sector, while its economic interventions are directed towards the municipalities. For economic governance of water services, the state therefore applies a ‘laissez-faire’ governance style that gives freedom to municipalities in managing their water utilities, which exposes the utilities in terms of economic issues to the municipalities and their demands.

5.1 Governance Framework and Different Types of Actors

The Finnish water sector is embedded in a governance framework that comprises supra-national, national, regional and local authorities (see Figure 5-1).
As depicted in Figure 5-1, the supra-national level is represented through the European Union and its Directorates General, which create Directives in cooperation with the national level of EU member countries. Directives enacted by the European Union are usually (within a few years) also passed by the Finnish Parliament and therefore become binding for the national context and its organizations, such as those active in the water sector. Organizations that assist the Ministries in supervising and executing legislation and regulations, as well as in proposing new governance measures, belong to the regional governance level.

Referring to the local level as depicted in Figure 5-1 (previous page), the municipalities and cities are the governance actor which has the authority to grant certain permits to organizations and to supervise environmental and health related regulations. Although the water utilities are not a governance actor, they participate in creating new legislation and regulation, either based on their own initiative or on the governance actor’s invitation.

### 5.1.1 EU Governance Actors

The European Union and several of its General Directorates, which are headed by the commissioners, represents an important governance actor for the Finnish water sector. Because water services do not have their own directorate (in contrast to energy), water services are covered in a wide range of EU directorates, such as the Directorate General for Agriculture and Rural Development, the Environment, and Health and Consumer Protection. Also, because of recent plans to liberalize and increase competition in public services, the directorates for Internal Markets and Services, and Competition have become relevant actors. The EU and its institutions are important to the Finnish context because EU Directives are adopted in Finnish national legislation and are thus binding to the organizations acting in Finland, including the water utilities. Although there have been discussions about liberalizing EU member countries’ water sectors, the EU parliament voted against the Commission’s plans to gain authority over how the member states are managing their water sectors. As a result, water supply and sanitation remain subject to the principle of subsidiarity, which means that they are under the authority of member countries.

### 5.1.2 National and Regional Governance Actors

On the national level, the Ministry of Forest and Agriculture is the party mainly responsible for the management of water services, cooperating with the Ministry of Environment, which is mainly responsible for water resources management. In addition, the Ministry of Social Affairs and Health is in charge of setting requirement standards for drinking water, which usually follows the requirements set by the European Union. In terms of drafting legislation and policies, these three ministries interact and cooperate with each other rather frequently. As a fourth ministry, the Ministry of Trade and Industry is considered responsible for watching over the water sector by way of the Finnish Competition Authority, which regulates economic activities and competition in
the water sector. However, the Ministry for Trade and Industry is not as regular a part of the network formed by the other three ministries.

The linkage between the national and regional level is provided through the Finnish Environment Institute, which works in close cooperation with the Ministry of the Environment but also has ties to the Ministry of Forest and Agriculture—for example, in distributing the funds that are provided by the Ministry. Through the Finnish Environment Centre, the Ministry of the Environment is represented on the regional level, in the form of 13 Regional Environment Centres that assist and supervise practices in the water and sewerage sector. These practices are mostly related to water resources management and issues in water and sewerage management, such as the development and implementation of water resources management plans, and enhancing regional municipal cooperation for improving the general condition of foremost rural water and wastewater services.

Another crucial role of the Regional Environment Centres is to distribute funding for projects in the name of the Ministry of the Environment and the Ministry of Forest and Agriculture (especially to smaller municipalities). However, the Regional Environment Centres are not responsible for the management, excluding particularly economic practices such as investment or profitability levels as related to the water sector or water utilities.

5.1.3 Local Governance Actors
The local level of authorities is represented through the municipalities, which have responsibilities and powers in regulating environmental issues—for example, by granting permits and supervising local health issues through controlling practices and collecting data about quality standards of drinking water. The municipalities or cities, however, are the local authorities and the owners of the water utility, which is the entity they are supposed to regulate. This is not a matter of legislative force, but it is the municipalities’ choice to be the owner and manager of the water services. Legislation would only require municipalities to organize for the provision of the water services—for example, by appointing the task to a private, jointly public-private-owned company or by granting concession contracts to private operators. Because the water utilities are owned by the cities and municipalities, legislative changes in municipal laws are also relevant to the water sector. The most significant law in this context—and one of the most important laws for the Finnish Water Sector in general—is the Local Government Act of 1995.
5.2 Key Legislation

The Finnish Water Sector is affected by a broad range of national legislation, from construction codes to procurement legislation to water sector-specific legislation. Therefore, the body of legislation passed relevant to the water sector within the past 15 years is rather extensive, although only half of it targets the water sector explicitly. In addition, the role of the national legislator has somewhat decreased due to much of national legislation being preceded by European Union directives; this needs to be mentioned explicitly in order to show the connection between European Union and Finnish legislative mechanisms.

The list below provides an overview of the legislation passed from 1991 to 2005, choosing a slightly wider timeframe than the regular 1995-2005 period, in order to include the beginnings of a wave of new legislation that had mainly been driven through European Union directives. Even though Finland was not yet an EU member in 1991, much of the Finnish legislation has been developed while considering EU directives. In fact, Finland’s accession to the European Union in 1995 has also been perceived by lawmaking institutions as an advantage to the previous situation. Earlier, laws had to be adapted in accordance with the EU because as a non-member it could not affect the legislative process—its role was confined to observing the process. This changed after the country joined the EU.

The Finnish state adopts the Directives into Finnish national legislation, and as a result, EU legislation becomes binding for Finnish water utilities. This has taken place with EU Directives such as:

- The EU Urban Wastewater Treatment Directive (1998)
- The EU Directives on Public Procurement (1992; 1993)

These Directives have been included in the Finnish national legislation in the years 2000 to 2003, with amendments to existing legislation and by creating new legislation, such as:

- The Government Decree on Treating Domestic Wastewater in Areas outside Sewer Networks (2003)
- The Amendment of Land Use and Building Act (2001)
- The Amendment of Health Protection Act (2001)
- The Amendment of Water Act (2001)
- The Water Services Act (2001)
- The Decree on Water Intended for Human Consumption (2000)
- The Environmental Protection Act (2000)
In addition to the list above, one of the most significant laws during the time period was the Finnish Local Government Act of 1995, as it required municipalities to separate the accounts of water works from the municipal organization and established larger water works as municipal enterprises.

<table>
<thead>
<tr>
<th>Legislation</th>
<th>91</th>
<th>92</th>
<th>93</th>
<th>94</th>
<th>95</th>
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<th>97</th>
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**Figure 5-2 Legislation Relevant to Finnish WSS from 1991-2005**

Figure 5-2 provides a longitudinal picture of water sector-related EU and Finnish legislation. As depicted in the figure and shown in the analysis of interview material with Finnish ministry officials in the following paragraphs, Finnish legislation is driven by EU Directives, as national legislative activity rises after EU legislative activity has occurred.

Based on data I collected from the interviews with water sector professionals, the figure provides a weighted timeline of legislation, emphasizing the fact that although in some years several laws relevant for the water sector have been amended or passed, their combined significance may be lower than that of single laws in other years. This is an important factor in assessing the intensity of legislative activity and the pressures and changes on the water sector that may result from it. In this context, the years 1995 and 2001 were especially important for the Finnish Water Sector; in 1995 the Finnish Local Government Act was passed, and in 2001 the Water Services Act was passed.
However, it needs to be considered that EU Directives are created during a process of negotiation among EU institutions, as well as EU member states. Therefore, the outcome of Finnish national governance is not merely a result of EU Directives; rather, EU Directives are the outcome of a negotiation process between all member states, which are subsequently passed by the national parliaments to become national laws.

The most significant events in terms of legislation relevant to Finnish WSS occurred in the years 1995 and 2000-2001. In these years, the Local Government Act (1995) was amended in order to allow municipalities to establish their water utilities as municipal enterprises. It represents the most significant change in legislation besides the Water Services Act (2001), according to the directors of urban water utilities. Because of their significance, the content of legislation of 1995 and 2000-2001 is briefly explained.

5.2.1 The Water Services Act

The Water Services Act (2001) was developed parallel to the EU Water Framework Directive before it was submitted to Parliament in 2000 and came into force in March 2001. The law supersedes previous laws such as the Act on Public Water and Sewerage Systems and the Act on Wastewater Rates (Pietilä et al., 2005).

The Water Services Act represents a key law because of its integrated perspective on the responsibilities of the municipality as the organizer of water services, the system of charging for water, to clarify and improve the rights of the consumer and the transparency of the water utilities, to unify the contractual conditions and charges of water services, and to harmonize the charges so that they all are based on the civil law (Pietilä et al., ibid.).

The Act stipulates the municipality to have the obligation to organize the provision of the service on its territory, based on charges that cover all investment and operating costs, though allowing for subsidies by the municipality, the state or the European Union. Two issues related to water pricing are important. First, the connection fee of a water utility may differ for the different areas it serves, but the water price itself needs to be equal in all areas. Second, the rate of return is not set on a fixed level; instead, it stipulates rather tentatively that water utilities are allowed to make “reasonable” profit.

Both tariff issues have important implications in practice. The emphasis on serving all areas with equal water charges raises the problem that when water utilities are merged with each other, those operating in more densely populated areas have lower costs and end up subsidizing the water tariff of those utilities situated in more sparsely populated areas. Considering the cost structure of a water utility, 90 percent are fixed costs, and therefore based on the connection fee, and ten percent depend on consumption. Thus, it is understandable that water utilities have been trying to change their tariff model in recent years and adopt a model that resembles their cost structure. At the moment, consumers are billed to the contrary logic, with the smaller share of their water bill coming from
connection fees and the majority depending on water consumption, in order to provide an incentive to saving water.

Further, the definition of rate of return leaves much room for interpretation as the legislator, owner, consumer, and operator may have different opinions on what constitutes a “reasonable” rate of return. The water prices are fairly equal in Finland and therefore benefit those with the highest advantages in economies of scale—hence, earning the highest rate of return. This issue is taken up in the discussion of economic regulation, which is described in the paragraphs about economic regulation of water services.

5.2.2 The Local Government Act

One of the most significant changes in legislation in the past decade has been the introduction of the Municipal Company Act in 1994, which required municipalities to separate the business accounting of business units from the municipal organization and allowed municipalities to establish their business units as municipal enterprises. These municipal enterprises are component units of the municipality. They are included in the municipal budgets and financial accounts, even though they are separated in accounting books and have their own balance sheet, assets, liabilities and income measurement procedures (Näsi and Windischhofer, 2005).

According to the Local Government Act, the municipalities cannot be given new duties, nor be deprived of granted authority, as long as legislation does not say otherwise. Hence, the decision of whether to own or sell the water utilities belongs to the municipality. The Act explicitly allows municipalities to choose freely either to provide the services required (by itself), or to contract them out to other service producers (from the private sector). This also applies to water utilities, which are increasingly outsourcing activities to the private sector and the municipal organization.

The Local Government Act is considered by water utility managing directors as one of the most important laws, as it meant an organizational change which separated the utilities from the municipal organization to a certain extent. In this context, organizational changes are regarded as more important than technological changes because the latter are part of everyday life of a water utility while the former only occur occasionally, and refer to changing structures and administrative processes.

“The most important law was the one for our separation from the municipal technical department […] those technical changes are part of our evolution, but these organizational changes are always the more difficult ones and have the most impact.” (Water Utility Manager)
Governing and legislating for the EU and Finnish state actors means coordinating their actions with water sector actors in a negotiation process rather than imposing legislation in a top-down manner. Acknowledging this aspect is necessary as the hierarchical distinction into supra-national, national, regional, and local governance structures may give the misleading impression that legislation and governance is a strictly hierarchical process.

5.3 **Governing the Water Sector**

The following paragraphs represent the analysis of governance actors’ main issues in terms of governing water services and the process in which this governance takes place. The main objective is to show how the governance process works and why the state governance actors are not executing economic governance for water services, choosing to instead focus on health and environmental governance. Finally, I show that this kind of governance creates non-transparent economic governance for the water sector.

5.3.1 **Main Issues for State Actors in Governing Water Services**

The main issues in water sector governance can be distinguished into health, environmental, and economic governance. While there is rather extensive governance for health and environmental issues, as shown in the previous sub-chapter about the most important water sector legislation, economic governance is not yet a priority for state governance actors.

In terms of *health-related governance*, state governance had to deal with a number of unexpected problems discovered during the past centuries which represented a health risk to citizens, such as in the 1990s when some ground water was found to contain arsenic. A more recent health risk was when the magnitude of uranium in ground water became known. The uranium problem is a country-specific one, and thus, the Finnish water sector not only deals with actions that are taken based on common developments in the European Union but also based on the characteristics of its own territory, geography, and climate. There is a false impression, as argued by health officials, that because water in Finland is to be found almost everywhere and most of it is of reasonable quality for human consumption, it is safe. Because of easily available, reasonably safe water (compared to other areas in Europe where water is more polluted), water is treated less in Finland before distribution to households, and thus more vulnerable in cases of service failures.

“Nobody can know what will happen in the future. For example, during my working period, several unexpected problems appeared […] we just found out in the 1990s about the arsenic problem in our boreholes and about uranium only in the last years. Arsenic and uranium are not problems of public water supplies but private drinking water wells, and so they would benefit from being part of the public water supply.” (Ministry Official)
“Since the quality of raw water is so bad in densely populated countries, the treatment of the water must be very effective. But in Finland, our reliance on the excellence of our ground and even surface water is so deep that usually we do not treat it enough, and we still have one or more waterborne epidemic outbreaks in Finland every year.” (Health Official)

As a result of these problems, the health governance actor argues for a regionalization of water supply and sanitation in order to bundle resources and thus to have more sophisticated equipment for water and wastewater treatment compared to small local water works. Further, it is criticized that municipalities, and especially smaller ones, are too concerned about the costs of infrastructure solutions and prefer to believe in the safety of their water rather than acknowledging that it is a vulnerable resource requiring investments in order to be safe.

“Usually the municipalities decide how much to invest in infrastructure and what to build, and they usually want the cheapest solution even though I told them of certain risks connected to it. […] those bigger treatment plants could use more expensive and advanced treatment processes that are impossible for small units because the price per cubic meter would be really high. In such a way, the risk of epidemic outbreaks, usually connected with small water supplies, could be avoided.” (Health Official)

Environmental governance is mainly concerned with rural areas, where especially the wastewater treatment needs to be brought up to the new environmental legislation. The Finnish regional environment centres are the main actors in this context as they distribute funding for water supply and sanitation development and coordinate projects for the improvement of the services, especially via increasing the cooperation among municipal water works. In this context, the state may grant funding for projects but may also use funding to initiate development projects based on the state governance actors’ initiative with the purpose of providing an incentive for municipalities to cooperate and take part—for example, in creating regional water management plans. Hence, cooperation between environmental governance actors’ and the municipalities is crucial to the sustainability of water supply and sanitation; this needs to be increased. The financial incentives the state offers shows both that there exists need for such finance, especially in rural areas, but also that municipalities and their water works may require a financial incentive in order to cooperate among each other, which points to the fact that cooperation among these parties requires at least informal coercion in order to take place.

“The legal basis concerning wastewaters has been changed and now we have ten years time to improve treatment for the wastewaters also in the rural areas […] most of the time the cooperation projects we have [with rural municipal water supply and sanitation] work pretty well, because usually we give assistance or financial support […] for example in this regional development plan all the municipalities have their representatives in the working groups […] and there is lots of cooperation. We are negotiating all the time to find
the best solutions and the best cooperative settings to manage the water services.” (Environmental Governance Manager)

But the Regional Environment Centres in charge of implementing environmental policies developed by the ministries have also become interested in the economic issues of water governance, although they are not yet active in that area. They are aware of the underinvestment, taking place in terms of infrastructure and profit levels in some cases, which is against the common interpretation of the law.

“We know that there are some municipalities that make too large profits and do not pay attention to their infrastructure, and we have been thinking about what to do in this context, but there is no mandate for us yet to become active. Maybe we should.” (Environmental Governance Manager)

Regarding economic governance, the state governance actors are aware of the shortcomings. In particular, there are municipal owners who do not allow their utilities to invest sufficiently in infrastructure because profitability is more important to them. This is against the governance actor’s common interpretation of the Finnish Water Services Act that says profitability must be ‘reasonable’, whereas they regard any number ‘around ten percent’ of return on investment as acceptable. The fact that these violations are taking place is tolerated because, as one governance actor put it, “It only concerns a few cities.” Therefore, the phenomenon is not significant enough to justify introducing economic regulation which would increase the bureaucratic burden for water utilities and the state.

“There are about 20 utilities which are bigger and which I would say the turnover is so big that you can actually get some profit; and the rest is so small that even if they make a high percentage of profit, the money they get is quite low. So, there is about ten or fifteen utilities where we can say that the profit they take out is too big. But anyways, it is a very small amount of utilities it concerns.” (Governance Level Manager)

“Some of the cities make too much profit with their water utilities. They raise the water tariffs even more in order to keep their municipal tax rate as low as possible. But it is only a few cities, and it gives them an unfair advantage over most other municipalities, especially smaller ones.” (Ministry Official)

“We are a very small country and you have to be careful with introducing new bureaucracy to the system. That can get very expensive […] and there is only a few water works that act against the present standard of profit making.” (Ministry Official)

In the economic context, the governance actor’s concerns for water utilities are mostly focused on the question of how regulation and restricting the profitability of utilities would affect ownership. Leaving freedom to the municipal owners is regarded as a suitable option for economically governing the water utilities and continuing public
ownership. This ‘laissez-faire’ attitude of the governance system, regarding economic regulation and organizational reform, means to leave the economic policies and reforms such as the regionalization of water utilities up to the municipalities. Therefore, laissez-faire is a governance ethic that results in a lack of legislation and regulation—not only in order to give municipalities the possibility to act and decide more or less on their own, but also to keep private sector firms from acting. State governance actors regard effective regulation by a new regulatory agency as a prerequisite for the privatization of water utilities. Therefore, this laissez-faire style is the opposite of market-oriented or private-sector-friendly governance and represents instead a protectionist tactic; as Weber (1947) noted, the private sector and capitalist institutions in fact require a strong state to establish the rules of the game.

“Maybe, the investment bankers are just waiting for us to establish a regulatory agency so that the local government would not be needed to supervise anymore.” (Ministry Official)

“What we want the state to do is to create a regulator […] because then control would happen disregarding the ownership, and we could have private water utilities as well” (Investment Banker)

Therefore, the national governance structure is promoting an unregulated context for the water sector concerning economic issues, although it notices that municipalities need to improve in managing their water works, criticizing its current practices of predominantly focusing on the financial benefits extracted from the utilities and not taking enough care of investments and the quality of the service. Nevertheless, state governance allows the municipal owner to find solutions to their problems individually, with occasional incentives and informal pressure from the national governance side, such as through subsidies for municipalities that merge their water services, or initiatives and guidelines for municipalities to regionalize water services.

“The municipalities still don’t see their roles well enough and are mainly concerned with money, loans, investments, and how they can use the utilities to balance the municipalities’ total economy. They don’t see well enough, that their task as owners is also to take care that the services are functioning, that they cooperate, have agreements, and develop the services. They are not concerned enough about the service levels, yet.” (Governance Level Manager)

“There will be a need to do with less people the same work and better services and that may as well result in new kinds of organizations. There should be more regionalized and independent but municipality-owned water utilities.” (Ministry Official)
These occasional incentives and cooperation initiatives are the governance actor’s tools of informal coercion rather than formal regulation and law-making processes. But their effectiveness must be questioned, as they have not produced the governance actor’s desired outcome, which was to encourage utilities and municipalities to act more moderately on their profitability policies and to merge with neighboring water utilities.

5.3.2 Governance as Process

In 1980, the European Union passed the first significant directive on water services, the Drinking Water Directive. Because Finland had not joined the EU yet, its ability to participate in the process of drawing up the Directive was very limited. If Finland would ever join the EU, it would have to adapt to its Directives beforehand in order to avoid a shock to the system. But because Finland did not have sufficient possibilities to participate in the legislative process, its country-specific conditions for the water sector could not be considered—instead, the Directive was based on the conditions for water supply and sanitation in Central Europe. When Finland and Sweden joined the EU in 1995, they were able to affect EU legislation to consider their sparsely-populated territory, cold climatic conditions, and cultural preferences of water supply (which affect the practices and outcomes of water supply and sanitation).

According to Hukka and Seppälä (2004), there exist cultural differences and preferences in European water supply. France and the UK consider drinking water a product that is treated before its consumption, while in German-speaking countries and in Scandinavia it is preferred in its natural form, if possible. Also, lower water temperature, especially during the spring when the snowmelt sets in, creates different conditions for treating drinking water and wastewater.

Table 5-1 Development of the Urban Waste-Water Treatment Directive

<table>
<thead>
<tr>
<th>Date</th>
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<tbody>
<tr>
<td>27/28 June 1988</td>
<td>European Environmental Ministers Seminar in Frankfurt a. M.</td>
</tr>
<tr>
<td>13 November 1989</td>
<td>First proposal for the Directive by European Commission</td>
</tr>
<tr>
<td>25 April 1990</td>
<td>Opinion of the Economic and Social Committee</td>
</tr>
<tr>
<td>13 September 1990</td>
<td>Opinion of the European Parliament</td>
</tr>
<tr>
<td>25 October 1990</td>
<td>Amended proposal by European Commission</td>
</tr>
<tr>
<td>21 May 1991</td>
<td>Notification</td>
</tr>
<tr>
<td>30 May 1991</td>
<td>Published</td>
</tr>
<tr>
<td>27 February 1998</td>
<td>Amendment by Directive 98/15/EC</td>
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</table>


As Hansen and Kraemer (2002) point out in Table 5-1 above, the process of creating the Urban Wastewater Treatment Directive of 1998 took one decade; starting with a seminar for European Environmental Ministers, input from Economic and Social Committees, the European Parliament, until the final amendment of the Directive in 1998. The new EU member countries that joined in 1995—namely, Austria, Finland, and Sweden—were also able to participate in the process, although their input in the beginning was of course rather limited. Hansen and Kraemer’s (ibid.) table, however, does not account for the role
the national water sectors play in the legislative process. As an example, the legislative process is described by a member of the Ministry of Health and Social Affairs in the following manner.

“When we [the Ministry] develop new drinking water standards, we do it together in a commission with other representatives of EU countries…but we always go back and forth between the demands by the European Union and what our [domestic] water sector is saying. We have to find the middle ground between having safer and higher standards but also not to inflict too much cost on our systems.” (Ministry Official)

The interaction between the water sector and the legislative bodies has also intensified during the last two decades. The role of National and European Associations for the sector, such as the Finnish Water and Waste Water Works Association (FIWA), as well as the European Union of National Associations of Water Suppliers and Waste Water Services (EUREAU), has increased. Initially, they were focused on the technical issues and progress of water and sanitation services, but they have become increasingly involved in the lawmaking process.

In the Finnish context, for example, the Ministry of Forest and Agriculture, which was responsible for drawing up the Water Services Act of 2001, the FIWA, as well as some directors of water utilities, were involved in the process and could give their opinion on the possible impact of new legislation on the quality, the cost, and organizational issues of the service. Also, for the new EU Directive for Drinking Water of 1998, the Finnish Ministry of Health and Social Affairs, which was the responsible party, took the opinions of the FIWA and water utility directors into consideration before voicing its position on new drinking water standards in the European Union working group.

Taking the opinion of the national water sectors into account includes several factors that benefit both sides – the water sector as well as the national government – as stricter standards incur large capital investments that may result in higher water price for consumers and even privatization of water utilities, as capital may have to be acquired from the private sector. For example, the EU Directives on Drinking Water of 1980 created rather high standards and allowed only a relatively short time frame for the national water sectors to fulfill the new requirements. If all the requirements had been fulfilled in time, tremendous capital investments would have been necessary and, therefore, deadlines and standards were renegotiated to a certain extent with national governments. For example, the parameters for water quality were reduced from 66 in the Drinking Water Directive of 1980 to 48 in the Drinking Water Directive of 1998 and deadlines for compliance were extended. Renegotiating these requirements was also possible because a large number of parameters applied to aesthetic product features, such as to odor, taste, and color, and therefore did not affect product safety as such.
Because the functioning of water services is also to a large extent a question of investments that have been made in treatment plants but foremost in network infrastructure, countries with old and under-invested networks may be forced to acquire capital and skill from the private sector. This has happened in the UK where stricter EU standards are said to have played a role in the privatization of the Water Sector in 1989, and in France, where the majority of water works are operated by private firms through long-term concession contracts. One of the most significant new requirements in the Directive was the aim to abolish lead pipes in order to reduce the amount of lead in drinking water, as it is a harmful chemical substance. The abolishment of lead pipes would incur approximately EUR 70 billion on the EU-15, whereas one-third of these costs concerns France alone, where lead pipes are widely in use (CEC, 1995).

The cooperation between the Finnish Ministries and the Water Sector serves both parties because neither wishes to trigger liberalization or even privatization of the sector, at least not based on the pace imposed by parties other than themselves. In order to avoid forced liberalization of the sector by the EU, Finland supports the group of countries that are in favor of keeping the water sector under the principle of subsidiarity (matter of national authority), which has been successful so far. Privatization, on the other hand, is avoided through reaching compromises for EU Directives, which are non-subsidiary, as the health-related Directive on Drinking Water, because these Directives also have the potential to trigger privatization through incurring investments so large that the private sector would be needed.

As depicted in Figure 5-3 (opposite page), health and environmental legislation is developed in an interactive process directly between the water sector and the state governance actors. What the lawmakers propose and decide does usually not come as a surprise to the water sector. Instead, the development of the sector could be described as a continuous process of adopting higher quality standards. National governments and water sector interest organizations have succeeded in finding a compromise between increasing the standards while considering the impact on costs. This is also demonstrated through a water professional’s opinion that “nothing revolutionary, really” is happening anymore, since the main technologies for the water and wastewater treatment and purification process have not significantly changed, and water utilities in Finland manage adapting to the evolutionary increase of standards rather well.
Referring to Figure 5-3, while the state governance in terms of health and environmental issues is rather transparent and, thus, predictable for water sector actors, economic governance is less transparent for the water sector because it is taking place via the municipalities who are the owners of the water utilities. The state’s pressures directed towards the local government and municipal organizations are affecting the water utilities in their economic governance. This economic governance process is more unpredictable for water utilities since they are not directly involved in the local government reform process that is going on between the state and the municipalities.

### 5.4 Summary of State’s Logic of ‘Laissez-Faire Interventionism’

In order to summarize the logics of state governance actors that are relevant to the water sector, it is necessary to consider governance actions targeted towards the water sector itself but also towards the local government level.

Regarding the water sector, state governance needs to be distinguished into different governance areas for environmental, health, and economical issues. Regarding the municipal sector, especially economic governance, in terms of local public services governance, is relevant. Further, informal governance actions are important that are not expressed by the state in laws but which are rather represented by the states’ continuous encouragement and coercion towards the local government level to increase its effectiveness, by adopting private sector managerialism and increasing cooperation among municipalities. I argue that the state governance actions towards the local government level are important drivers for the commercialization of the water sector because they create certain behavior in municipalities.
I observed during the period since the beginning of the 1990s two different governance strategies that occur simultaneously. These governance styles can be categorized as laissez-faire and interventionist governance styles. I argue that this mix of interventionist and laissez-faire governance by the state creates circumstances that lead to outcomes that are unplanned and unintended by the state.

5.4.1 Interventionist Governance

Over the past ten years, with regard to formal state intervention via laws, governance of health and environmental issues has been characterized by interventionism on behalf of the EU and the Finnish national level. The EU level has been an especially important driver for legislation, as it has authority over member-states in environmental and health issues. On the European Union level, five key laws were passed and adopted by Finnish lawmakers in seven national laws, mostly referring to some environmental or health aspect of water services. Thus, new standards and practices based on the demands by the national and EU governance actors were implemented by the water sector. For economic issues, however, the EU level has no authority over water sectors. On the Finnish national level, laws that concern the reform of local government were passed in the mid-1990s that demonstrated a renewed effort by state government for local government reform.

Besides this type of rather obvious legal intervention (by changing the laws that govern the municipal and water sector), a more subtle intervention is taking place with the intention of coercing the municipalities to increase their effectiveness. This more subtle or informal state intervention is represented by the state’s decreasing transfer of funds to the local level, which represents an action to coerce municipalities to become more self-reliant and entrepreneurial (which I discuss in more detail in the following chapter about municipal actors). Further, different government initiatives and incentives that are offered to municipalities as a ‘reward’ when they implement organizational changes, such as merging local governments together or forming cooperation, also need to be considered as a type of intervention because it decreases the legitimacy for things staying organized as before.

But at the same time, as the state tries to coerce municipalities towards more self-reliance and effectiveness by formal and informal types of intervention, it grants rather significant leeway to them by allowing municipalities to find individual answers to their problems, which I call a ‘laissez-faire’ governance style.
5.4.2 Laissez-Faire Governance

On the Finnish national governance level, for the past ten years the state has exercised informal intervention by reducing its role as financer in Finnish local government and promoting reform with informal tools of intervention such as by providing financial incentives to projects that follow the ministries’ recommendations. Here, the state is acting in a laissez-faire or free market manner by allowing the municipalities a significant amount of freedom in finding solutions to their finance- and services-related problems, even if that means that municipalities may act against the common interpretation of the law. For example, the Water Services Act says that the profits from water should be ‘reasonable,’ which is generally understood by governance actors as approximately a ten percent return on investment. But larger cities overcharge their citizens for use of the water supply and sanitation in order to subsidize other municipal services. Because tighter legislation would decrease the municipalities’ interest in operating water services, the state refrains from introducing tighter legislation because it prefers water utilities to be public-owned. Therefore, laissez-faire is a governance tactic that results in a lack of legislation and regulation—not only in order to give municipalities the possibility to act, but also to keep private sector firms from acting, as effective regulation by a new regulatory agency is seen by the state governance actors as a prerequisite for the privatization of water utilities, which would be an unintended consequence.

Interventionist governance reduces state funding for municipalities, encourages inter-municipal cooperation, and promotes the adoption of private sector managerialism. The laissez-faire governance style in economic issues—and the lack of a strategy for the water sector—allow, on the other hand, the municipalities to find their own solutions, which may clash with the lawmaker’s intentions. For example, merging water utilities with energy utilities is a solution that the municipal and financial markets have found to solve the financial problems of some individual municipalities, but it compromises the state governance actor’s intention that water utilities should merge with each other. As a result, the combination of interventionist and laissez-faire governance makes outcomes of the local reform process in terms of water services management hard to predict for the state governance actors.
6 Municipal Actors

The following chapter analyses the institutional logics of the municipal sector. First, I provide an analysis of the municipal domain and its purpose in order to introduce the municipalities’ roles, tasks, and how managers see themselves performing.

Second, I present an analysis of the municipalities’ principles of organizing that describes the municipalities’ collectivistic and individualistic characteristics that are important to understand their logics about reform and restructuring. Within this subchapter, I further provide an analysis of the municipal actors’ idea about ‘appropriate management’ and professionalism by discussing their means to achieve effectiveness, which are predominantly concerned with being ‘rational’.

The third subchapter contains a longitudinal analysis of the emergence of municipal entrepreneurialism by combining interview data with a content analysis of one of the sector’s periodicals and data about the income of municipalities and the state’s contributions.

Fourth, the qualitative data from municipal managers are analyzed according to their institutional logics about how to manage municipal water services.

In subchapter five I extract and summarize the institutional logic of municipal actors from the data and call it municipal ‘rational entrepreneurialism’.

6.1 Domain and Purpose of Municipalities

The analysis of the domain and purpose of municipalities is divided into briefly describing the ‘tasks’ of municipalities; and municipal managers seeing themselves as ‘service providers’ as well as ‘business owners’.

6.1.1 Tasks of Municipalities

Municipalities provide roughly two-thirds of public services; the state, one-third. The municipalities are required by law to be responsible for organizing different tasks or so-called basic services, as depicted in Table 6-1 (next page). Of these, the most important basic services are education, health care, and child day care, which is in Finland a constitutional right of the citizens. In addition, planning and housing are part of the municipal domain, as well as technical services that include energy and water services. The amount of regional cooperation in health care and municipal planning has been constantly increasing, partly due to the compulsory regional authority committees for these sectors. The local, rather independent municipalities are obliged by state law to provide for certain services, such as child day care, health care, education, or water services, but they are free to choose the method of service production in many cases.
Therefore, the municipality has the duty to make sure that within its defined territory—for example, of a city—every citizen has access to drinking water and sanitation. While the municipalities are required to organize these services, they have a certain degree of freedom in how to do so. That means that in practice, it is up to the municipality to organize the local health care through contracting the private sector or by doing it itself. Water and sanitation services fall in that category as well. Private sector participation in service delivery has also been increasing—for example, in delivering health care and technical services such as energy, water, waste, maintenance, and construction services.

<table>
<thead>
<tr>
<th>Mostly in-house, some utilization of private producers</th>
<th>In-house or joint-municipal authority/other co-operative solution</th>
<th>Mostly joint municipal authority</th>
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<tbody>
<tr>
<td>Primary Schools</td>
<td>Secondary Schools</td>
<td>Specialized Health Care</td>
</tr>
<tr>
<td>Day Care for Children</td>
<td>Primary Health Care</td>
<td>Vocational Education</td>
</tr>
<tr>
<td>Care of the Elderly</td>
<td>Environmental Protection</td>
<td>Regional Planning</td>
</tr>
<tr>
<td>Libraries, Culture</td>
<td>Industrial Policy</td>
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<td>Technical Services</td>
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<td>Local Zoning</td>
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</tr>
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</table>

Table 6-1 Patterns of Service Production in Finnish Municipalities

The municipality is predominantly regarded by the municipal technical managers as a service provider, and it is clearly distinguished between the so-called core services and non-core services. Within the core service domain, the usual view is that child day care, educational, health, and social affairs are parts of it, as well as the management of major infrastructure. Major infrastructure includes roads, bridges, certain buildings but also recreational infrastructure of strategic importance, such as a city’s amusement parks. Wastewater networks are usually rather the affair of the municipality than of the water utility because sewer canals are underneath the municipal streets. They are also often counted as major infrastructure and therefore as the municipalities’ core activities. Especially because the municipality has invested significant sums in network infrastructure of all kinds, including district heating, roads, electricity, water, or sewerage, they are often considered as part of the strategic core because of their high asset value.
6.1.2 Being a Service Provider

Especially in areas where the operation of services or infrastructure faces missing or imperfect markets (monopolies or quasi-monopolies), the law states that municipalities are responsible for organizing them. For educational services, municipal technical managers clearly emphasize that the municipality and therefore the public sector should remain as the owner and operator. But there are other areas where they make a clear distinction between owner and operator, in overseeing and controlling key decisions—for example, regarding service levels and service quality.

“We have four areas of core services, and they are health, social, schooling and major infrastructure, such as roads, bridges, and the sewerage system.”
(Municipal Manager)

“Our task is to produce educational services, health care, street maintenance, child day care. But I think for example managing real estate is not so important and we could outsource it or sell them.” (Municipal Manager)

Municipal managers feel many of the activities the municipality performs as burdensome due to the difficult budget situation. But they also emphasize that it is not enough to be a mere provider of services, which the municipality is obliged to provide by law. Voluntary or value-added services are regarded as significant contributors to municipalities’ inhabitants’ quality of life and, therefore, as important factors for image.

“We must think about our image and that it is not enough to have services based on law but we also need cultural services, sports, environmental services, recreational services, and all kinds of services, and not only based on what we are required to do by law.” (Municipal Manager)

Therefore, not only are core services valuable to the municipality; a wider range of activities needs to be provided for, whether by the municipality or by a chosen contractor. Slimming down the municipalities’ operations is of great concern and therefore is linked to business divestment as well.

The question of whether to divest from certain business activities requires municipal managers to determine a service unit’s ownership value, meaning that owning a certain service entity brings value to the municipality. That value can take on several forms. Many municipal services and infrastructure is operated by the municipality because they are facing missing or imperfect markets. Opera houses, conference centres, or amusement parks are important organizations for urban life and achieving profitability is difficult. Nevertheless, these units create some form of value for the municipality, remaining the owner and controlling entity. In the example of a local amusement park, the value might not be in the form of financial profits to the owner, but it has strategic importance as attraction for the municipality as a whole, creating spillover effects for other local businesses and enhancing the quality of life for inhabitants—and therefore contributing to the overall competitiveness of the municipality.
“We have companies that have very big strategic meaning for the city, such as the amusement part, or the conference hall. It is not so important how profitable they are. The strategic meaning is ownership value. That is the most important thing.” (Municipal Manager)

Concerning the municipal organizations related to technical services, a distinction can be made between operations which are unlikely to be profitable, such as operating a conference centre and operations that can be profitable, such as the water utilities or energy utilities, which could be even more profitable if management and cost structure, would change, although the current situation often does not allow it. In the first case, it seems evident to the managers that it is only the public sector or the municipality for that matter who takes care of such services. However, in the second case, profitability is a possibility, and therefore it indicates that a market exists and private sector organizations would be interested to perform the task instead of the municipality.

6.1.3 Being a Business Owner

Where profitability of a service is realistic and privatization would be a theoretical option, municipal managers legitimate municipal ownership and management control through the strategic importance of the particular unit or through unique market characteristics, such as the natural monopoly character of water services. These units are organized as municipal technical services and infrastructure, managed either as departments of the municipality, as more independent municipal enterprises, or even established as limited liability companies.

In cases where there exists a functioning market in the sense that private sector companies are readily available to perform the same tasks as the organizations controlled by the municipality (for example in the case of operating bus lines) municipal managers can imagine that either the municipality divests from these activities or that it remains in the market. The fact that the municipality should maintain ownership and the operation of certain service units (despite the possibility of allowing a third party organizes these activities) is justified through the municipality’s need to protect itself from private sector cartels. But having one of its own organizations participating in the market also enables it to execute municipal policies.

“When we are talking about the housing system, the reason why we own the companies is how to handle the housing policy of the city. You can’t handle it if you are not in it. Of course, the most of them are working in the open market, but we need to be in there to use our housing policy, because the housing policy comes from the law. So, that is only the tool to make the policy.” (Municipal Manager)

“Our logistics transport centre takes care of all the transport, so when units order transport services, we have that kind of services because there is not enough competition. The price level is so high that it is good to have your own organization to affect the price level.” (Municipal Manager)
Regarding water services, another reason for it to be a municipality-owned service business is that its domain is a natural monopoly. Competition in natural monopolies can only be created through competitive tendering for long-term service contracts of service infrastructure, but not in a sense that the end customer can choose between several service producers—to, say, switch water service producers, as it is possible for electricity services.

Municipal managers believe that it is better to have the public sector operating a local natural monopoly rather than the private sector because, after all, citizens are able to execute some sort of monopoly supervision through the local democratic municipal government system. If the water utility were owned by a private company, it could not be effectively supervised and regulated because the utilities’ economic decisions would be made by an owner who is independent and mainly guided by profit motives.

Here, a lack of trust towards the private sector is visible because in case of a monopoly market, the lack of competition would create a lack of incentives for the private company to put the customer’s interests before economic interests. The municipality is seen as the more suitable owner and provider because the democratic system assures that the inhabitants’ interests come before economic interests, or are at least considered as important. And even if the municipality is as profit-seeking as a private enterprise—as municipal managers argue—its profits benefit the citizens because the income is used to finance services the municipality could otherwise not afford to provide, such as leisure and cultural activities.

“We are in very big financial difficulties and know that we need to do something but many of us have not concluded yet, if it is more reasonable to privatize because it mostly does not get cheaper but the citizens have to pay more.” (Municipal Manager)

“It is in the interest of this city and us, the people, not to destroy the nature which affects the water quality and availability. But if there would be a private firm, I believe they would not think so much about that.” (Municipal Manager)

“What are the benefits to change from public monopoly to private monopoly? It makes no sense.” (Municipal Manager)
6.2 Principles of Organizing

The following subchapter discusses the municipalities’ principles of organizing as they emerged during the analysis in the form of collectivistic and individualistic ideas as well as rational ones.

6.2.1 Internal Collectivism

The municipal technical service companies are especially important when they are profitable, because the financial resources the municipality acquires through these companies are used for financing other municipal services. Therefore, the role of municipal service businesses is to contribute to the balance of the city budget by allowing the municipality to support services that otherwise would have to be financed through increasing the municipal tax level and using financial resources meant for law-based or so-called basic services. Discontinuing a particular service is rather difficult and not desirable because most services fulfill a certain need, such as the recreational and sport activities. Discontinuing the service would reflect poorly on the image of the municipality. The profitable service units such as water and energy utilities are of strategic importance not only because they allow the municipality to be an active participant in the particular sector, but also because they provide income to the municipality, which can be used to support other service areas.

“You cannot put more taxes to the inhabitants. That is not the way to finance services. If you have a high tax rate, it is not good for your city image.” (Municipal Manager)

“When we need to create balance in the whole city, the income of the water utility is one part of the balance. Theoretically, we cannot do it, but in reality, we do it.” (Municipal Manager)

“We want to own these companies; we don’t want to sell them to the private sector. They are municipal companies.” (Municipal Manager)

The principle domain of the municipality is providing and producing services, which it is obliged to by law. But the purpose of the municipality is wider than that. Value-added services, which contribute to the overall well-being of the inhabitants, need to be provided as well. Therefore, safeguarding the viability of the overall service portfolio, from child day care services to recreational facilities and services, is regarded as the main purpose of the municipality as an organization and as its appropriate domain. In the eyes of municipal managers, ensuring the overall balance of the municipal budget justifies to own and manage service business units and use their profits for cross-subsidizing other municipal services.
The service domain is about to change, especially with pressures from financial and human resources side (decreasing state funds and retirements). For the future, municipal managers expect the municipality to focus more on being a service provider than a service producer. The actual production of the service might switch to a third party, in most cases a private sector company. Redefining the core leads to an increase in service provision through contractual arrangements rather than self-owned and self-managed service organizations. However, municipal managers seem convinced that the municipal sector is catching up with the private sector in terms of professionalism and effectiveness. Municipal actors think that it is nowadays mainly their structural disadvantages that make municipal services perform at a lower level than private sector services, rather than the difference in management skills. An ownership and management style is emerging that imitates the private sector in its practices. However, the municipalities’ entrepreneurial logic does not automatically assume that privatization is the only answer to increasing the effectiveness of the municipality. Instead, it regards itself as an eager learner of private sector practices and, hence, as capable of successfully managing public enterprises, which also shows a rising self-confidence of municipal actors as being successful economic actors and entrepreneurs.

From a conceptual standpoint, the previous analysis demonstrated that local government level consists of organizations that are internally collectivistic. Resources of individual units are shifted within the organization to create balance, in order to secure the overall survival of the organization. However, the following paragraphs turn to the local municipalities’ relationship with its environment, calling for a distinction between internally collectivistic and externally individualistic institutional logics.

6.2.2 External Individualism

As previously demonstrated, the local government level is characterized by collectivistic principles when it comes to managing the municipal organization internally. It is crucial for the municipality’s viability to shift resources from profit-making units to loss-making ones, in order to sustain current service levels. In this paragraph, however, I am turning to the municipalities’ principles in relation to its external environment and especially to other neighboring municipalities. As this analysis will show, local government is characterized by an individualistic notion in dealing with its neighbors, and I am arguing that this notion is not a result of entrepreneurialization, but has already existed prior to it. As a result, local government can be described as an internal collectivistic, but externally individualistic, actor. This distinction is important for understanding the difficulties municipalities have in merging their services operations and assets together, and how comparatively easy it is to execute structural changes within one single municipality.
Table 6-2 Size Distribution of Municipalities in 2002

<table>
<thead>
<tr>
<th>Inhabitants</th>
<th>Municipalities</th>
<th>Municipalities, %</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; 2 000</td>
<td>88</td>
<td>19.7%</td>
</tr>
<tr>
<td>2 001-5 999</td>
<td>180</td>
<td>40.4%</td>
</tr>
<tr>
<td>6 000-9 999</td>
<td>76</td>
<td>17.0%</td>
</tr>
<tr>
<td>10 000-19 999</td>
<td>50</td>
<td>11.2%</td>
</tr>
<tr>
<td>20 000-39 999</td>
<td>34</td>
<td>7.6%</td>
</tr>
<tr>
<td>40 000-99 999</td>
<td>12</td>
<td>2.7%</td>
</tr>
<tr>
<td>100 000 &lt;</td>
<td>6</td>
<td>1.3%</td>
</tr>
<tr>
<td>N=</td>
<td>446</td>
<td>100%</td>
</tr>
</tbody>
</table>


The Finnish local government level is rather fragmented, with 432 local municipalities. The municipalities are comprised of 114 cities and 318 other municipalities as of 2005. Table 6-2 shows a similar size distribution of municipalities as the water sector does, and which can be explained through the fact that water supply and sanitation have been a local municipal affair for decades. Municipalities smaller than 10,000 in particular (but also larger municipalities) have been the target of efforts to merge them together entirely or by just creating regional services units. But despite the efforts by the national governance level to promote this process, the number of municipalities has been only slightly decreasing over the past years—for example, from 446 in 2002 to 432 in 2005. As a study by the Association of Finnish Local Authorities conducted in the year 2000 found, the support for merging municipalities in general was especially low among citizens of municipalities up to the size of 10,000 inhabitants, although they were slightly more in favor of it than their candidates in the municipal elections (Sandberg, 2005). These results are partly explained by the strong tradition local self-governance has in Finland and by the fact that if municipalities were merged together, the candidates’ chances to get elected to the municipal council would decrease, especially for those candidates from previously smaller units.

Sandberg (2005) points out efforts to restructure the Finnish municipalities by increasing their administrative size date, at least, back to the 1960s, when the state tried to implement a local government reform that would have reduced the number of municipalities to almost half. However, the state faced resistance from the municipalities and finally it was agreed that the state would resign from its right to merge municipalities. Nevertheless, the number of municipalities decreased from 1965 to 1980 by about 100 (Sandberg, ibid.).

The regionalization process of local administration and local services, therefore, has a history of at least four decades. The municipalities’ resistance against the state’s efforts to restructure the local level, then, can be taken as an indication for the municipalities’ will to remain independent and locally rooted, while the state has been trying to achieve a more regionalized structure of local government.
Local services are deeply rooted in local communities and, hence, may be individualistic by default. And as water services are local services, it is rather natural for municipalities and citizens to think about them individualistically and reject merging them with neighboring units, as it would decrease their independence and de-root them from the local community.

"Why should we have a bigger size for everything...the local services are very important for our local democratic system...our inhabitants have a feeling that they can affect them, but when everything becomes bigger, it disconnects the local people...it is important for our identity...but maybe it is not the modern way to do it anymore" (Municipal Manager)

The 1990s had seen an increase in autonomy for municipalities. According to the Local Government Act of 1995 the state could not transfer new tasks to the municipalities without their agreement. At the same time, municipalities have been confronted with decreasing state funds for municipal service production. The grand strategy of the state’s governance reform had been to decentralize administration and give more powers to the local level and new efforts to reduce the number of municipalities were made based on the municipalities’ voluntary action and incentives offered by the state. But only about ten such mergers were accomplished during the 1990s and ten to twenty more were planned; as Sandberg (ibid.) writes, these mergers mostly concerned larger cities and were rather ineffective in reducing the number of small municipalities.

As a result of the unsuccessful efforts to reduce the number of municipalities, the state has been emphasizing since the 2000s the implementation of national standards and regional cooperation among municipalities, in order to achieve the regionalization, at least in service production, instead of merging entire municipalities (Sandberg, ibid.). Not only would the state governance actors like municipalities to merge; managers of the Association of Finnish Local Governments recommend a minimum population size of 10,000 inhabitants as they pointed out in their interviews. Further, the PARAS project by the Ministry of the Interior to investigate the restructuring of municipalities and their services concluded that for example for health service a population base of at least 20,000 inhabitants is required; one of the project outcomes was a government proposal to the parliament that would provide an incentive for municipalities to merge (Ministry of the Interior, 2007).

Besides the municipalities’ resistance in regionalizing municipal administration and services, I found a widely shared agreement among municipal, state governance, and water sector actors that cooperation and regionalization of services is the solution to many problems the municipalities face today. However, municipalities do not eagerly cooperate with each other, according to municipal managers. The Association of Finnish Local Authorities, which also focuses on enhancing the effectiveness of local government, has been trying to increase municipal cooperation; their managers admit that this is tough. As municipal managers admit, much cooperation in water services has been
established because of some constraint (and not voluntarily). For example, the lack of groundwater in a municipality or water safety concerns are often reasons why municipalities cooperate in water supply. The nearing retirement of the post-war generation represents another reason why municipalities may have to deepen their cooperation, as especially the smaller ones run out of employees. But what has started as compulsory cooperation may also mark the beginning of deeper cooperation in other areas.

“They only cooperate if they really have to. If they can afford to do things independently by themselves, they will do it, and only cooperate if they are obliged.” (Municipal Actor)

“Our lack of groundwater was a big problem and that is why we had to cooperate with the neighbor cities. In the beginning it was very hard, fifteen years ago, but now things are going well. It was hard because the city majors did not get along very well […] they also take care of our customer billing now although we had difficulties, of course, in the beginning. But now it goes well. We might have a limited company for water services together in the near future, and [we] must be in that company, because we don’t have groundwater.” (Municipal Manager)

One crucial explanation why regionalization fails is the municipalities’ individualistic thinking and, subsequently, its inability to make compromises. By definition, to compromise means “to come to an agreement by the partial surrender of position or principles” (Oxford English Dictionary). Restructuring and improving the effectiveness of water services is linked to creating larger service units, and therefore merging service operations and/or assets of several neighboring municipal water utilities. The differences in opinions about the distribution of benefits and costs occur among the negotiating parties. At the end of such a negotiating process and the merging of several water utilities usually stands a compromise of financial or political nature, meaning that somebody needs to give up some of their money or power. Whether that party is receiving something in exchange is often a matter of perspective. From a local point of view, the municipality may think to have gained nothing and lost significant resources and power, but from a regional perspective, the municipality may think that the regional water company will strengthen the long-term viability of the service and also bring additional benefits to citizens and employees by being a more professional organization.

Such compromises are often perceived by municipal manager as a weakness and exemplary of unprofessional behavior. Municipal managers identify themselves with an idea of professionalism as they imagine it to be in the private sector. The notion is that private sector companies do not ‘subsidize others’ because they are efficient and competitive. This idea is imitated in the public domain, where compromising the distribution of profits and investments is seen as a weakness and lack of professionalism. To justify one’s own individualistic thinking, it is explained that no municipality would agree to finance or subsidize others, either.
“If we establish a private company, like a business company that is owned by the municipalities, it is a limited company, and that is very different. You cannot make a deal like that then…it is different and all these municipalities think the same way. If they have a company, they would not want to subsidize somebody else either, they would have deals like in the private sector.” (Municipal Manager)

Agreeing on the distribution of financial resources is one thing, but giving up decision-making power is another. In most cases of regionalizing municipal water services, a larger core municipality merges its water services with its surrounding, smaller municipal neighbors. Usually, the size of the assets of the larger core municipality might exceed even the combined assets of the remaining negotiating municipalities. This means that if the share of assets determines the share of seats in the supervisory board of the new combined water utility, a power imbalance arises that leaves the smaller municipalities vulnerable to the largest one, which then would have the power to decide against the will of the others. To avoid such a situation, smaller municipalities may leverage their power by striking deals where the large municipality gives up a share of its seats on the board, and as a result, its share of decision-making power in the new water utility is smaller than the share of the assets it brought into the new entity. That kind of compromise is seen as a strategy of last resort.

“We gave up the majority stake in the company even though we had the most assets in it. We needed the company so badly that we needed to give up.” (Municipal Manager)

“Most pipe nets and treatment plants of the new water utility are inside our municipality…when politicians discussed how to make the executive board of the company, though we must have a majority in the board because we own the majority of the shares, but the other municipalities said that they want to have the majority together, so that if they all think in a different way than us, we cannot do anything on our own against the will of all others. Our politicians decided to give up the majority. There are now altogether nine board members and four of them are from us and five are from the surrounding municipalities.” (Municipal Manager)

What is described by the municipal manager in the statement above is an example of a municipality willing to compromise and to create a regional water utility (Hämeenlinnan Seudun Vesi OY). In return for its compromise to give up the majority of the seats on the new executive board, it gets easier access to drinking water resources it needed through the new company’s larger territory. Therefore, in this case a significant constraint (lack of water resources in the largest municipality) was a major driving force for creating the new company and for agreeing on the compromise to give more decision-making power to the smaller owners. The smaller municipalities received a good deal because their water and sanitation services were improved through investments and better management. The water and sewerage tariff in all these municipalities is the same although the largest municipality has scale advantages compared to the small, more rural
municipalities. All municipalities gain from a more flexible investment planning schedule where urgent investments can be prioritized.

Municipal entrepreneurialism is an institutional logic that was shaped through increasing the municipalities’ legitimacy by adapting private sector practices and principles. The private sector is used as a standard of comparison for different reasons. First, it is framed as a desirable model when justifying public sector reform and managerial action. Second, it is framed as an undesirable model when it is perceived as competition, especially when the municipality tries to keep certain activities in-house that theoretically could also be performed by the private sector.

“I think if the utilities are profitable, the business world is interested. But if they are interested, you should keep it yourself, because you get money every year from it. If it is not profitable, than no one wants it, and then you have to keep it anyways […] we, the city, also think of society.” (Municipal Manager)

“The prices for water are on a quite high level, and annual profits from water and energy especially are used for financing other sectors, so-called soft sectors that would be hard to support otherwise, such as cultural and leisure services.” (Municipal Manager)

In both cases, however, the framing of the private sector and entrepreneurship contradicts what private companies and entrepreneurs actually do by over-emphasizing their rational aspect. Entrepreneurs calculate and plan carefully, based on loads of information. They do not compromise their goals. They have to maximize their profits—or benefits in general—in order to survive. However, there is plenty of evidence in literature on entrepreneurship and business management explaining that entrepreneurship is rather the opposite and comprises vision, dealing with ambiguity, listening to one’s own gut feeling, making compromises, building constituencies, and forging cooperation.

Thus, municipal actors have to some extent a mythical understanding of the private sector. The eager adaptation of private sector practices and principles shows that municipal actors are serious about absorbing private sector characteristics. However, the private sector discourse may sometimes also serve as a rather convenient, rhetorical excuse for justifying managerial actions and decisions.
6.2.3 Rationality as Means to Achieve Effectiveness

In the municipal organization, professionalism is a dominating principle in the sense of making decisions based on rational calculation of potential risks and benefits. Municipal managers emphasize the increasing importance of planning and financially calculating the impact of decisions on the service organizations and the municipal budget. This development of becoming more rationally calculating is perceived by most managers as positive, often justified with the argument that it is a successful management principle in the private sector and one of the sources of effectiveness. Importing these principles to the public sector therefore means to increase the professionalism of the public sector organization and thus, its effectiveness.

“We are nowadays more careful in calculating our decisions and it is becoming more all the time. When we realized for example the ownership aspect and these kinds of things, we have learned business thinking.”
(Municipal Manager)

Applying financial logic to the water utilities of the larger cities is based on three incentives. First, operating water services is rather profitable and, therefore, the water utilities deliver significant sums to the budget of the city. Increasing these profits is possible by increasing water tariffs and through increasing the effectiveness of the water utility. Therefore, the municipality and the water utility are striving for improving the cost structure and efficiency of the water utility.

Second, restructuring the water utility and changing its legal form from the municipal business department to a limited company allows re-evaluation of the company’s assets. The water utilities’ assets are usually valued at the historic cost level, meaning that their values reflect the cost incurred at the time when the asset was constructed. However, when changing into a limited company, these assets will be valued by using the present net value, reflecting the cost that would incur if the asset were constructed at present-time and according to present technology standards. This re-evaluation increases the fixed asset base of the water utility approximately three- to fourfold. This allows the owner, which is the municipality, to borrow against that increase in value, using it as collateral.

Third, the water utilities were earlier a part of the municipality in the legal form of a municipal business department, which allowed profits to be transferred without paying tax. When water utilities are transformed into limited liability companies, the municipality would benefit from the re-evaluation of assets but profits transferred from the limited company to the owner are subject to taxation. Hence, the municipality reduces its taxable profits, by trying to find arrangements that allow the water utility to remain a limited company, but that would also minimize the tax to be paid on profits from the water services. Also when water utilities are run as municipal enterprises the municipal owner has an incentive to disguise the total amount of profits because they may be regarded by the law as unreasonably high. Whatever option municipal managers
consider, the financial benefits and risks of restructuring and reforming water utilities often seem to be the main concern.

“We thought about how we could get some advantage in both of these areas, the service and the finance, and lower the costs but keep up the good service, still. There is approximate potential for cost savings of ten percent and then there are also investments.” (Municipal Manager)

“If the assets would be re-evaluated, the asset base would be twenty million Euros higher. That was one of the things that lead us to think about this cooperation through a limited company that would be owned by the municipal neighbors.” (Municipal Manager)

“The major wants a certain annual sum from that utility. And it is true, the energy utility is making good profit but now this profit stays somehow with the company because it is a limited company, and the city has difficulties to get that money without paying too much tax. If we merge it with the water utility, the tax could be reduced.” (Municipal Manager)

However, in those cases where the motivation for restructuring the water utility—for example, through integrating it with smaller water utilities from surrounding municipalities—is mainly financial, the solutions tend to be rather complex constructs of legal entities, financial transfers, and legal stipulations. In such cases, the discussion about the restructuring revolves around the numbers and whether the new arrangement can show that it will deliver the financial benefits that it promises. But this is difficult, as the trust in numbers and calculations is not particularly strong, especially among municipal decision-makers and politicians of different opinion who start doubting each others’ calculations. The task suddenly becomes not only to prove that calculations are correct, but to explain rather complex models to a variety of persons and stakeholders in the decision-making process.

“Until now, nobody was able to really show how to get more money out of that restructuring.” (Municipal manager)

“I believe our financial director, he and the major are in favor of the change, but he has not been able to show the financial benefit yet.” (Municipal Manager)

When it becomes a discussion about numbers, they are disputed along the process for various reasons; additional calculations are demanded. Additional calculations are often based on the disagreement of distributing the future benefits and costs. Especially concerning restructuring projects where several neighboring water utilities should be merged, a negotiation process on the municipal political level takes place, where it is demanded to take each municipalities’ own characteristics into account.
However, in most cases the municipalities (even though being neighbors) exist under rather different conditions. For example, municipalities might have different growth or decline rates in population or economically, which means that investments in water networks are different. The age of their networks and the conditions can be different, resulting in more investment need in the renovation of networks in one municipality than in the other. Or, their city centres and municipal areas in general can be populated more or less densely, where more water connections per square kilometer result in higher efficiency, as it is the case with city centres compared to rural areas. In addition, even though it might make sense geographically and economically to merge certain municipal water utilities and water networks with each other by following topographical conditions, the inhabitants of these municipalities might feel much closer to neighboring municipalities in the opposite direction—for example, because many inhabitants are commuting for work over there.

These circumstances make the financial calculation of distributing future profits and investments rather difficult. They involve not only numbers but often also feelings about each other and relationships with others. The long-term nature of investments in the water sector and therefore the lack of predictability add to this complexity.

“We tried to calculate and the financial consultants tried too, to calculate and then to take this future growth into account in the distribution of shares, with the company structure, but it seems to be too difficult for this area at least. It mainly concerns the problem how each partner thinks the future investments should be divided, because there are differences in the growth of these municipalities.” (Municipal Manager)

“I think it is a financial problem. The pipe network in our municipality is in a bad shape and the other municipality is afraid of subsidizing the renovation of our water network if we join together.” (Municipal Council Member)

“There are differences between our two municipalities because almost half of the people who live in the other one commute for work to the Helsinki area, and that is one reason why they also want to cooperate with the Helsinki area and not only with us.” (Municipal Manager)

A distinction needs to be made between those decisions that require the cooperation of several parties—whether they are municipalities or water utilities—and those decisions that can be made by one municipality alone. Even though a municipality has a variety of service units, political groups, levels, and stakeholders, it represents a network of actors that make decisions that concern one municipality alone. Therefore, these decisions are relatively easy when compared to those decisions where several municipalities need to agree.
Therefore, applying the rational, financial logic to decision-making dealing within a single municipality might in fact facilitate faster decision-making. For example, the decision of a municipality to merge its water utility with its energy utility can be a rather fast process, compared to merging several neighboring water utilities owned by different municipalities. As described by some municipal managers, decision-making within the municipality seems to become easier because even though differences in political opinions might exist among decision-makers in the municipality, the tight municipal budget limits the options of decision-makers and forces them to agree based on ‘the bottom line’ and ‘put ideology beside’.

“But it [decision-making] becomes easier and easier because money talks.
(Municipal Manager)

However, applying the financial logic to a setting where municipalities need to find a common agreement when merging, for example, their water utilities, may in fact complicate the issue. The power in such a network of municipalities is dispersed equally, because even though one might deal with municipalities of different size and economic strength, the value of the agreement is determined by the number of participants, which makes also smaller municipalities powerful. Under such circumstances, resorting to a logic that favors the rational, financial calculation of distributing present and future benefits and costs starts a game of calculating; where each party can demand that its individual characteristics need to be taken into account and aim at gaining individual benefits. But demanding calculations can also be a tactic to delay decisions or make them obsolete. Here ‘the reality of the bottom line’ is interpreted by each party in a different manner and thus it does not facilitate swift decision-making but even has the potential of slowing it down.

“It can also be a tactic for those who don’t like some new solutions, they can demand all kinds of new calculations […] there can be some delegates, which can demand all the time new calculations if they don’t like the decision.” (Municipal Manager)

“I get worried when I read in the news that it becomes very thorough and they make more calculations and more calculations, and they decided to include the future investments in the calculations, which describe the portions of different municipalities of the ownership of the company. It seems to get so complicated now that they never get the results, or the decisions made.” (Municipal Actor)

Criticism of the financial logic comes from the few actors that have managed to restructure their water utility successfully, telling about the importance of focusing not on quantitative aspects but on qualitative ones. They emphasize that numbers and calculations should be used, but that they cannot be the starting point and, neither the main focus, during the project. After all, numbers can be rejected, disputed, and doubted, leading to various re-calculation. They stress that the main focus in this context needs to
be a common interest, such as the long-term viability of the municipalities as a community of municipalities—as a region. Water safety and water quality aspects have been emphasized as the leading rationale for the regionalization project, while efficiency gains in the operations and staff reduction were intentionally downplayed since staff reduction would be achieved through natural retirements and in order not to upset the work force and the labor unions.

“I think the other municipalities that try to regionalize look at the wrong things. Large gains in efficiency are not the main purpose. If we think about that, we always must show everything with calculations and all calculations are just calculations. If you don’t believe calculations, you will say that this is nonsense. It is not possible to say what the future, especially in numbers is […] and if we say that efficiency is the main purpose to create one single company for providing the services, our workers will ask whether this is done by increasing their workload, and by firing a part of them. When they are discussing about that with politicians, because they also have connections to politicians, then it is not easy anymore to tell about other benefits for the municipality.” (Municipal Manager)

“If the decisions are purely based on numbers and calculations, and without reasonable trust, they don’t work. Those plans will be rejected at some stage, anyways.” (Municipal Manager)

So, it all comes to money, but you should find something else, something more beautiful you can hold onto, to help you see beyond.” (Municipal Council Member)

I see the rational, financial logic on the local level as the substitute for the lack of a defined, common interest on the regional level; lack of the ability to think collectivistic in terms of one’s environment; and a lack of making compromises. Without such a higher interest it is hard to make decisions especially in cases where the power is dispersed among actors. Nevertheless, the municipalities’ domain and principles of organizing are also developing into a more professional organization that is confident of being able to ‘manage’. On the following paragraphs, I will explain how and why this rational-financial logic entered the municipal thinking, creating ‘municipal entrepreneurialism’.
6.3 The Emergence of Municipal Entrepreneurialism

In the following sub-chapter I will provide a longitudinal analysis of how the municipalities’ managerialism and entrepreneurialism increased over the past ten years. For this purpose, I first present an overview of how municipal income has developed since the 1980s in terms of the state’s contribution to municipal budgets. Then I present my own empirical data from interviews with a longitudinal content analysis of a professional journal from the municipal technical sector. By combining these three analyses, I show how income development and entrepreneurialism are linked with each other.

![Figure 6-1 Municipal Income and the Share of State Funds from 1980-2007](image)

*Source: Turkkila, Association of Finnish Local Authorities, 2006*

Figure 6-1 provides an overview of municipal income from local tax and state funds since the 1980s. While income from both sources was rising until the end of the 1980s, the following recession caused a state and municipal income crisis with the consequence of large scale reforms and changes in financing the local system. As depicted in Figure 6-1, from the early 1990s onwards state funding continuously decreased in absolute terms and started rising again in the 2000s in absolute terms but the share of state funds as part of municipal income nevertheless remained on a low level. Sandberg (2005) points out, that state grants were almost equally important as local taxes in the beginning of the 1990s and represented 45% of municipal income (from local tax and state grants combined). This percentage decreased significantly and state transfers represented in the beginning of the 2000s only 25% of municipal income (from local tax and state grants combined). One way to compensate for the loss of income was for municipalities to increase municipal tax, which represents nowadays roughly a third of citizens’ tax burden. It ranges between 16-21% at the moment, and the average tax rate continuously increased from 17.31 percent in 1990 to 18.87 percent in 2006 (Sandberg, 2005; Turkkila, 2006).
As the municipal managers pointed out to me in their interviews, they also benchmark their municipalities’ local tax rate and ‘compete’ with other municipalities of comparable size. Keeping the tax as low as possible while state funds decrease creates an income gap that can only be filled either by savings achieved through structural changes, generating additional sources of income, or by restructuring municipal assets. Municipal managers perceive the municipal utility businesses such as water and energy as rather suitable targets for generating additional income and restructuring municipal assets. Municipalities need to become all the time more self-sufficient which means that they need to think how to create income for their budgets by being innovative and creative. As a result, municipal ‘tax planning’ has become an important part of municipalities’ strategy to ‘optimize’ the use of their assets.

“Nowadays we always look who has the lower tax rate […] the tax rate is important for our businesses and citizens, and we cannot just increase it. We need to become more and more efficient […] and we can use the income from our businesses to support other services we have.” (Municipal Manager)

“We are nowadays very busy with tax planning […] it is an important element in our strategy and it means we have to optimize how we use our assets […] nobody wants to pay too much tax to the state, nor the citizens and neither do we.” (Municipal Manager)

With the decrease in state funds and the state’s pressure on municipalities to improve their management practices, the municipal sector turned to the private sector. Figure 6-2 (next page) provides a longitudinal analysis of the technical sector’s focus by reviewing the publications of the magazine Kuntatekniikka, one of the municipal technical sector’s key print media.

Referring to Figure 6-2, from 1998 to 2005, the managerial perspective on municipal technology has been increasing from roughly 30 percent in 1998 to almost 70 percent in 2005, causing a drop in attention given to predominantly technical articles that decreased from almost 70 percent to 40 percent. Therefore, the focus of the technical sector has been shifting from a purely technical oriented one to improving management practices. Private sector management concepts are increasingly used and a serious effort is made to improve the effectiveness of the municipal technical organizations. Arranging tenders, contracting out, and increasing the cooperation in procurement are just a few of the management topics that have increased over the time period in the journal.
Also an entrepreneurial attitude towards managing the scarcity of resources is expressed through articles appearing at the end of the period about ‘where to acquire resources from’—for example, about ‘how to engage the private sector in partly financing cultural and leisure projects’. Further, attention increased towards developing the city by using prestigious housing construction projects such as on river- and lakefronts and finding new forms of organizing such as for projects about reorganizing municipal services. This shows that the focus shifted from merely improving the effectiveness of technical services to introducing private sector managerialism to improve municipal technical services and, finally, to a wider range of topics where new forms of organizing and attracting resources (such as business but also mere attention) are important and information technology is used not only to reorganize technical departments but also administration and local public services.

### 6.4 The Municipalities’ Perspective on Water Services

Managers in the municipal services domain do have an opinion about how water services should be organized and managed. That opinion, however, is rather different from those of water sector professionals. The municipal service domain needs to secure the functioning of a service portfolio consisting of basic services (such as education and health care) and value-added services (such as culture and leisure). Therefore, its business enterprises, such as water and energy companies, need to be effective and profitable organizations which allow the municipality to subsidize its basic and value-added services. I found that the municipal managers I interviewed widely agreed on the problems and challenges for their water utilities. The municipal managers’ ideas of how water services should be organized are not predominantly concerned with water services per se, but always include the interests of other municipal sectors as well.
6.4.1 Water Quality and Service Quality

From a water quality perspective, municipal managers are satisfied with the current quality and service levels, but emphasize that measures have to be taken to safeguard the current situation. Keeping up the good standard is regarded as very important, but there are problems especially in smaller municipalities.

“We had always very good water quality. The city has very good laboratories and the health inspector controls the quality thoroughly.” (Municipal Manager)

“After the [other municipality] joined our water utility, I noticed their problems. They had bacteria in the drinking water, so we were told by the health inspecting authorities. I asked the authorities why they haven’t done anything before, and they replied ‘because the municipality wasn’t able to do anything’. […] In those small municipalities, most politicians do not understand how bad the situation is and the main reason for their problems was that they did not have enough professional skills to run the water supplies.” (Municipal Manager)

“We must take care that they remain on that standard and make them more effective. The environmental standards will be very strict in the future in Europe and that means we must have the money to keep the system on that standard level.” (Municipal Manager)

6.4.2 Workforce and Retirement

Some municipal managers see a problem in this situation because the retiring generation and the new generation are usually not working in the utility at the same time because the municipality or the water utility do not have the necessary financial resources to pay for additional jobs, which means that transferring tacit knowledge to the younger generation is difficult. From a technical perspective, problems with the management of water services infrastructure might occur in the beginning, until the new generation has learned its ways.

“In a few years we will have 20 percent of personnel retired, which is a big change. And they will retire before we can hire new ones, because we don’t have the money to pay salaries to both. That means that we must move the knowledge to the new people so rapidly, which means a very big change.” (Municipal Manager)

From a cultural perspective, some municipal managers perceive the generation change as rather positive because they expect the water utility to think and act more like a business organization, and the new generation of employees is expected to bring a certain amount of business thinking and business culture into the water utilities. In this context, a certain amount of frustration with the water sector’s independence and strong culture can be noticed, and municipal technical managers try to emphasize that times for the municipalities are changing and the values, beliefs and the thinking in the water utilities
must change as well. The need for more business oriented thinking is strongly emphasized, also recognizing that previously the water sector was mostly about engineering and technologies, and that in the future more economic thinking and education is needed.

“The retirement is not going to be a problem at all, because the business unit of water supply is overstaffed now. When those workers are going away […] we are hiring people in and we get more of business culture because those old workers are going out, and they have no business culture.” (Municipal Manager)

“[The water sector people] are too proud in their minds and think they know everything but if we think about their education, they are not economical people, they are engineers mainly. I don’t have all the knowledge for this sector but I believe we should start thinking in different ways but perhaps it is normal resistance in their thinking and that belongs to these changes. And because they are owned by the municipalities and the municipalities’ thinking has changed, or was forced to change, and therefore all the sectors that belong to the municipalities need to change their thinking as well, like the water sector.” (Municipal Manager)

6.4.3 Facing Resistance to Changes

Involving employees from the start is seen as the absolute necessity if changes are supposed to succeed. However, this notion also collides with a frustration over the power of the unions and employees over the management and the owner, where a more autocratic leadership style sometimes is desired, but municipal managers quickly remind that in a democratic system there is no way to make decisions alone. Here, the municipal democratic system represents a network in which the power is dispersed among a large number of network participants, such as the management of the service unit, the management of the owner, the municipal council, and the employees.

The employees do have power through being often represented in the municipal council as council members, and in cases where a municipal service unit might be outsourced to the private sector, the labor union, the employees, and the municipal council are perceived by the municipal managers to build an alliance that can resist the proposed changes in the management of the service unit. Especially the labor union’s ability to carry conflicts from the original source to other service units seems to make municipal technical managers careful about proposing changes that would be too dramatic or too fast.

“[… we have 60 persons cleaning personnel and it was very interesting to make a competitive tender and get to know what it would cost for a big school, but it has been very difficult here to change that. The labor union is interested in salaries and keeping the own personnel in their jobs. They can go straight to the city government because many of the employees are sitting in the city government and they are like bosses to us.” (Municipal Manager)
6.4.4 Infrastructure and Investments

A large part of Finnish water services infrastructure, such as water pipelines and wastewater treatment plants, have been constructed in the 1960s and are close to needing renovation, which, of course, requires financial resources. Municipal managers recognize the gap between the need for rehabilitating water services infrastructure and the financial resources that can be made available. While some managers acknowledge this bottleneck, they also emphasize that the profits the municipal owner is taking from the water utility are needed somewhere else in the municipality and making funds available for water infrastructure rehabilitation is not regarded as the highest priority at the moment.

“The renovation of networks is a problem, yes...and also the construction of new networks, because actually, it is a matter of the costs, and it is going to be a problem.” (Municipal Manager)

“The water utility has enough savings, yes, but they cannot use it without our permission, and the city does not give the permission because it is a matter of the balance of the city economy. The whole monetary system is the bank loan and a customer paid system. So, they don't really have savings, but I think there is enough, if we let them use those savings.” (Municipal)

6.4.5 Profitability and Economic Regulation of Water Utilities

In cases where profit can be made from the water services, they are used for subsidizing other municipal services and that justifies taking rather high profits, especially in municipalities with scale advantages, where the income from the water utility to the city budget can be rather significant. Some water utilities in Finland deliver to their municipal owner profits that are clearly beyond the “reasonable” limit as it is written in the law. However, establishing a regulative authority that would control the economic activities of water utilities and their profits, investments, and price politics is regarded as unnecessary and potentially harmful. Regulation is regarded unnecessary because the water utilities are owned by their municipalities, and therefore they can be controlled through democratic means directly through the inhabitants. Municipal managers are satisfied with this system of control and do not regard any further means as necessary, also with the argument that any supervision would increase the bureaucracy in the system, and ‘in a small country like Finland’ the benefits of such regulation might be outweighed by the costs it incurs through making management processes more complex and bureaucratic.

“I think the control is at the moment strong enough. And [...] when people elect council members they elect then the board, and the board elects then the members for the companies [...] people have a straight connection to these representatives that have been elected to the council and that is quite a hard pressure and control system.” (Municipal Manager)
“There are a certain contradicting interests among those people, who are sitting in those political places in the boards [city boards]. They are representatives of the customers or local citizens and the owners of the utilities but as long as the prices are on an affordable level, it should be okay.” (Municipal Manager)

“Establishing a regulator for water services is a bad thing [...] I have always tried to point out that instead of obligatory regulation, the sector itself should open their practices and activities, sort of benchmarking or that kind of evaluation, so that they can really compare themselves among other utilities and how they can improve and cut the costs.” (Municipal Manager)

However, in the case water utilities become privatized in Finland, the utilities would have private owners, and because in such case no democratic supervision is possible, a regulative authority would definitely be needed. For some managers, establishing a regulative authority in the present situation could even accelerate privatization because the question of economic regulation would be disconnected from democratic supervision. It would become possible to have private owners because they could be supervised as well. Therefore, having no regulative authority is regarded as an advantage because it represents an obstacle for having private ownership of water utilities in the market, since there is no supervision possible for them. In addition, having a regulative authority would mean that municipalities would lose their autonomy in managing the profitability of water utilities, and lowering the profit margins could decrease the incentive for municipalities to own the water utilities. In this question, municipal managers put the economic motives for owning the water utilities before societal motives through assuming that ownership of the water utilities could switch to the private side if the profitability for the municipality would not be high enough anymore.

“Regulation would be needed especially if the municipalities would sell their water supply systems totally to the outside, to private companies. Although they are companies, the municipalities elect members into the board and that is a very strong way to control these companies.” (Municipal Manager)

“Now, when it’s in public hands and the money goes to the public good in a way, the people don’t care so much, but if it goes to the private pocket, it becomes a bad thing that should be regulated.” (Municipal Actor)

“If we have such an authority, it could mean that the selling out of the utilities would accelerate because the municipalities might think the price would be regulated by the authority if we sell. But if we don’t have an authority, then they don’t sell because they can regulate the prices themselves.” (Municipal Actor)
6.4.6 Water and Energy

Water services essentially belong to the group of network businesses, such as the energy business, including electricity and district heating services. Most municipalities own the energy and water companies which serve their inhabitants. However, the market liberalization of the electricity sector in 1990s led to the sale of a number of Finnish municipal electricity utilities to private sector utility companies. The electricity market is nowadays liberalized, and competition among electricity companies for household and corporate customers is possible.

When talking with municipal managers, the relevance of the energy and especially electricity sector for how they believe the water sector should be managed becomes apparent. Whether the municipality still owns its energy utility or whether it has been sold to the private sector, the energy sector always comes up when talking about water services. After all, water and energy are the two domains in the municipal business that can make the most profit, and electricity used to be a monopoly business while water continues to be one. Because the municipality is managing its technical service units as part of a portfolio of municipal tasks, the water and energy services belong to the municipal thinking of creating balance in the municipal economy and budget.

The years when some of the municipalities were selling their energy utilities to private companies are remembered by municipal technical managers as desperate, where the recession hit the municipal budgets hard and choices about selling the utilities were made too quickly. Studies that say those municipalities which held on to their electricity utility have lower prices than those which sold them to the private sector are also mentioned rather frequently by managers. Therefore, selling to the private sector is interpreted as negative and something that is very likely to increase the prices without increasing the benefits for the consumers. This thinking is also applied to justify municipal ownership in the water sector by using the energy sector as a show case.

“In 1995 or 1996 when I first came to the city they had just sold their electricity utility and got some [millions Euros] but everything has gone with the wind by now […] there was a study that claimed that in these municipalities which sold their own electricity company, the price is much higher than in the other municipalities. So, it has been a very expensive project for the consumer of electricity.” (Municipal Council Member)

“The privatization of our municipal electricity works certainly affected the water utility because our water services employees were much more aware and they were afraid that we were creating a regional water company just to sell it out.” (Municipal Manager).

In those municipalities where the energy utility is still owned by the municipality, it is significant for restructuring the water sector because municipalities are thinking about creating multi-utility organizations, where water and electricity are merged into one company. Such ambitions have been started in Finland already, and most of them seem
driven by financial motives, as municipal managers argue that through such a merger, the municipality would save on paying taxes and increase its borrowing from financial markets but also gain efficiency. The main commonality between the water and energy utilities is that they are network businesses, and in many cases this is enough for municipal managers to justify that they can be integrated into one single company. After all, from the municipality’s perspective, the business service units are still owned by the municipality and changes within the portfolio would not have much effect on the overall balance of the municipal activities and also would not create too much opposition from labor unions, employees and council members. However, some managing directors of municipal energy companies have opposed to merge with the water utilities although in the past three years municipal energy companies’ interests in integrating municipal water operations have increased.

“There are certain similarities [between water and electricity services]. They both need networks to be distributed, large capital investments, and they are connected to a network, they are always regional monopolies, and the costs should be covered by the price of the products. So, they can be done as a business activity.” (Municipal Manager).

“They are completely different. Actually, when the business manager of our electrical company and our water supply companies…they don't want to get the multi-utility system.” (Municipal Manager)

While in Central Europe, many multi-utility companies exist that serve consumers with energy, water, and even waste services, there has been only a few attempts to form such utilities in Finland. However, one large city has merged its energy utility with the water utility, and in this case, the similarities between the two services are emphasized stronger in order to justify the merge through creating synergy effects between the two utilities. But in any case, through merging the water and energy utility a larger organization would be established with more financial resources at its disposal for investments, and the owner would be able to save tax on profits through more effective tax planning.

“You can combine all the administration and networks, so that you have a bigger network company […] it will be easier to plan investments and financing because it is a bigger company and it is easier to work when you plan all investments and re-investments in the same company.” (Municipal Manager)

“One reason for merging the network businesses is tax planning. Our energy company makes profit and it is no use to pay taxes and this is an easier way to accomplish it when we have this combined water and energy company and have debt.” (Municipal Manager)
“Another reason is that you can have all customer relationships managed from one office that is one point, to handle marketing, it is easier then to invoice customers and for all kinds of systems it is easier then.” (Municipal Manager)

“Our energy company is making good profit but now this profit stays somehow with the energy company and the city has difficulties to get that money without paying too much tax.” (Municipal Manager)

6.5 Summary of Municipalities’ Logic of ‘Rational Entrepreneurialism’

Over the past decade, municipalities were continuously subjected to cuts in state funding and an increasing amount of tasks, which significantly contributed to a scarcity of their financial resources. The public debate about decreasing the size of the public sector and redefining its purpose and core activities has led to a lack of legitimacy. The pressure the state puts on the local government to become more competitive and implement private sector management practices is significant. Municipalities are also eagerly trying to learn from private sector based on their own motivations of enhancing organizational effectiveness – but also to justify existing beliefs with the new, seemingly more legitimate rhetoric of private sector managerialism.

At the end of the 1990s, it was considered sufficient to improve the effectiveness of the municipal organization through implementing private sector management principles for example by using competitive tendering and benchmarking. However, at the beginning of the 2000s, municipal actors emphasized becoming more entrepreneurial, which means to be more active in acquiring resources, more passionate about one’s own business, more professional in arriving at decisions by calculating more extensively, and more determined to achieve results by maximizing the organizations’ own benefits. In other words, municipalities were striving to become more ‘professional’ by grounding their decisions on ‘facts and calculations’ that should justify decisions that are ‘dictated’ by an ongoing municipal budgetary crisis.

The pressure on municipalities to regionalize their services and to merge together to form larger administrative units has been increasing, especially over the past five years. This pressure is manifest in the public discourse of public services reform and the issue’s ubiquity in the media, as well as in the data I collected from journals, newspapers and interviews. The ministry officials have voiced their frustration with the municipal regionalization process and their decreasing confidence that the municipalities will be able to achieve structural reforms without the intervention of the national governance level. On the other hand, municipal managers are showing commitment to structural reforms and are well aware of the regional cooperation they are required to improve, but they perceive this process as difficult because they have their own individual
municipalities’ interests in mind and want to ‘protect’ them, ‘just as any other private company or municipality would do it’.

The pressures coming from the state governance level are a combination of decreasing financial support and encouragement to adapt new management practices, as well as cooperation. But these pressures are designed to force municipalities to change on their own, with significant freedom in finding individual solutions to their problems. Through the new entrepreneurial spirit, the municipalities have started to deal with their problems by themselves and find new solutions to the financial crisis. The answer is often sought after in the financial restructuring of municipal assets such as their water utilities, which is executed in close cooperation with financial actors. Although municipal actors emphasize the importance of inter-municipal cooperation in order to create synergies through large, structural change, inter-municipal asset transactions are preferred because they don’t require other municipalities to agree to the deal.

The restructuring of municipal assets, such as merging the energy utility with the water utility, or transforming the energy utility into an independent limited company are financially-motivated transactions for the benefit of releasing capital that is used for balancing the municipal budget. As it is easier for the municipality to restructure internally than doing it regionally, together with other municipalities, it is more likely that water and energy companies of one municipality merge together than merging creating regional water-only companies.

When it comes to a municipalities’ individual affairs, municipal actors apply a collectivistic idea by shifting resources within the services portfolio, in order to create a balance of the entire municipality. Thus, a collectivist attitude oriented towards municipal internal affairs is applied, which requires profitable units to finance unprofitable ones. When it comes to dealing with the external environment, such as regionalizing services in cooperation with other municipalities, an individualistic logic is applied. The regionalization process for water services and other municipal services is often criticized as being too slow. Municipal actors perceive it as a difficult process because an agreement with other municipalities needs to be reached. In this context, the problem is the strong emphasis on calculating the risks and benefits based on self-interest and benefit maximization of such regionalization projects. The entrepreneurial logic lacks an emphasis on the ability to make compromises based on a common, shared interest or vision. Thus, it misinterprets some of the most vital characteristics of entrepreneurship, which is to have vision and to build constituencies. In order to survive, the entrepreneur needs to command more resources than he owns himself and, thus, needs the constituency of networks—or, in this context, requires the constituency of other municipalities.
Therefore, I define municipal entrepreneurialism as a set of principles originating from the private sector that is applied to municipal decision-making. These principles comprise: 1) significant inherent individualism when dealing with third party outsiders that is expressed by the attempt to maximize individual benefits; 2) the need to be ‘entrepreneurial’ to acquire resources and the confidence in being entrepreneurs and business owners; and 3) the idea that effectiveness is achieved through professionalism, where rationality and extensive calculations are the basis of ‘sound’ decisions.

However, I would like to stress once more that although municipal entrepreneurialism is a set of principles that originate from the private sector it does not necessarily mean that the principles of this entrepreneurialism exist in the private sector per se. Instead, as I will show in the discussion part of this thesis, the principles of municipal entrepreneurialism are myths created during an imitation process that are combined with the municipalities’ inherent individualism.
7 Financial Actors

The following chapter represents an analysis of the group of financial actors, comprising investment banks and financial consulting firms, which are providing their services to municipalities. The group of financial actors comprises a financial consultant as part of management consulting firm, and three investment bankers from two investment banks. These investment banks should not be confused with investment banking institutions, for instance, belonging to the European Union, such as the European Investment Bank (EIB), which is active in the water sector through participating in the financing of construction projects in Finland and other European countries.

The process before the actual transaction takes place (for example the sale of a water utility to an energy utility) is especially of interest to me, because it allows looking at the concepts and solutions that are proposed by financial actors to their clients (the municipalities). The advice of financial actors to their clients is significantly shaped by their own institutional logics, as to what they think their business is about, and how things should be organized. This means that advice is an interactive process. The client’s (municipality’s) needs are respected by the service business (financial consultants) but the service businesses’ own interests and principles affect the advice the client receives.

I divide this chapter into three subchapters whereas in subchapter one I analyze the domain, purpose, and principles of organizing of financial actors.

In subchapter two, their perspective on how to manage water services is presented.

Third, I provide a summary of the institutional logics of financial actors. This chapter can also be seen as a continuation of chapter four where I demonstrated how the financial actors emerged over time as the most relevant actors among the group of private sector actors.
7.1 Domain and Principles of Organizing

The following paragraphs represent an analysis of the domain and purpose of financial actors. Further, their key logics are analyzed by emphasizing their rationalistic and individualistic key characteristics.

7.1.1 The Financial Domain and its Purpose

Investment banks usually have a portfolio of activities they take care of on behalf of their clients. These activities may include advisory services for specific mergers and acquisitions; assisting and executing capital market transactions such as privatizations; and more general advisory services for structuring a client’s finances, including the optimizing of asset, investment, and tax strategies. In principle, the goal is to enhance the value of a company in terms of shareholder value.

Besides investment bankers, financial consultants within the management consulting domain also offer their services, which comprise strategic advice for enhancing investment and shareholder value strategies, but also more operational activities, such as optimizing the distribution of financial benefits and risks among contracting parties, as is the case in mergers of neighboring water utilities.

A major difference between the financial consultants and investment bankers is that the advice from the former is a combination of management and finance advice and is remunerated through a consulting fee, while the latter hopes to close a deal at some point, which will lead to receiving a percentage of the transaction volume as remuneration. The advice from a financial and management consultant also differs in that the client receives financial advice that is ‘flavored’ with management advice, while the investment banker is more focused on optimizing the client’s capital and finances and to prepare, assist, and execute financial transactions.

“Water utilities as enterprises are still very close to the municipal administration and…the municipality has very heavy decision-making power in the investments, the strategy, and the direction for the water company. The owner thinks more about profitability and about keeping the investments at a minimum…there has to be found a solution that satisfies the owner’s profit needs and the investment need of the utility…for example by raising the tariffs, and…more productive ways to provide the services.” (Financial Consultant)

“From this concept’s point of view, it is the same whether it is the water or electricity or whatever that is integrated. It does not make any difference. And the value of these networks is huge in Finland…we are talking about millions.” (Investment Banker)
In the case of investment bankers, financial advice represents a step into the direction of assisting or executing a financial or capital transaction, of making a deal so to speak. When that is happening, a sometimes year-long effort pays off, through earning a percentage of the transaction volume as a fee for the investment bank. In some cases, the client approaches the investment bank on the basis of a concrete need to receive advice in the restructuring of an asset. As in a concrete case in a Finnish town, the discussion with the investment banker shows that the city expected to solve its financial problems by restructuring some of its assets with the help of the investment bank. The investment bank has been advising this municipality also in previous matters concerning the restructuring of their energy utility.

“The original idea came for the city, because they need money…and want to avoid paying corporate taxes on the energy company…we recommended doing that transaction….there are several benefits concerning that transaction. The most obvious is that they pay less company taxes through that transaction…the value of assets of the water utility increases fourfold through using their present cost value instead of historic cost value…and there are also some synergies they can get through that transaction.” (Investment Banker)

The financial actor’s clients’ or municipalities’ policies and requirements represent important guidelines for the financial consultant. In most of the larger Finnish municipalities, ownership policies have already been developed, or their development is in progress. Ownership policies are sometimes developed independently, by the municipality and its politicians or officials, but it is common to use private sector consultants and financial institutions that assist in the process as well.

“Regarding energy and water sector the primary issues we have seen in [municipal] ownership policies are risk appetite, quality of service and price of service in the city, competitiveness, decision-making, employment issues, capital injections, value of the assets and the development of the value, and these fiscal issues like tax effectiveness…it is difficult to find real differences in them.” (Investment Banker)

The restructuring of municipal assets, such as water utilities, can be a lengthy and time consuming process because this field is politically charged, and the power is dispersed among numerous actors in the field. This also means that the investment banker has to carry the risk of the deal not going through, for example when the municipal council rejects the plan to restructure the energy and water utility.

Especially at times when private ownership is rejected in a sector, such as it is the case with the Finnish water and sewerage sector, the work of an investment bank takes on an additional meaning and purpose. Here, the investment bank is not merely a service organization that is hired once it is needed to execute a financial transaction. Instead, it is a rather proactive player that is involved in an organizational field through constant
interaction with some of the actors, which is a role that makes the investment bank an important actor itself. In organizational fields where the power is dispersed among actors, it is a time and resource consuming negotiation process in which the investment banks and financial consultants keep generating new solutions and concepts that could be accepted by the relevant parties, to finally come to the decision to approve a deal. That means to constantly develop new concepts and to test and suggest them to those actors which have been identified as the most powerful ones. It also means to adapt to the logic of these actors and to the circumstances, for example when noticing that the municipalities do not plan to sell their utilities, a different concept needs to be suggested to stay in the game.

“I have been trying for three years to sell private money as a representative of the private sector to the municipalities but they are not very keen because they can release the capital in other ways and they are not planning to sell the water works…and because they don’t want to privatize, so we made a concept that they are regional water companies under a limited company…fully owned by the municipalities.” (Financial Consultant)

“We took the initiative…there was a new major…and I knew him very well, and we discussed already before…about this concept…I didn’t recommend anything, I just said which options he has…both the major and the financial director…felt this is from the owner policy view much easier politically to sell in the city than selling the whole utilities. [Our] point was that we have to create a concept which actually is...somewhere in the middle…not to keep it all as it is today, but also not to sell it all away… if we can’t create new concepts like this, nothing happens in the market. And if you create this type of new businesses, those parts of these businesses where competition is possible may be sold later, and we will be there doing it.” (Investment Banker)

Those strategic questions of restructuring municipal water utilities clearly start out on the owner level and not on the water utility level. In some cases, the utilities oppose the strategic changes proposed by the municipal owner.

“Actually, I had approached the energy and the water company already earlier…and now they [water utility] signed an agreement to pursue this change but they were not willing to do that actually, they were very reluctant and they almost had to be forced to do it.” (Investment Banker)

What the municipalities’ and financial actors’ plans for restructuring the water utilities have in common is that the main concern is of a financial nature, whether from the municipalities’ perspective or from the financial actors’ perspective. However, while the municipalities’ criteria for effectiveness as a service provider comprises also a large variety of non-financial measures, the financial actors’ criteria for effectiveness speaks a clear financial language that is a result of the client’s objectives and the investment bank’s own perception of effectiveness, as is shown in the paragraphs below.
From a financial actor’s point of view, the major criteria for effectiveness are how effective an organization is managed and how effectively it uses its resources, which of course also affects profitability. In terms of resources, the fixed assets of a water utility represent the major share of capital investment and therefore the effectiveness with which these infrastructure assets are used is of major importance to the financial actor. Here, the water utilities are criticized for ‘wasting their resources’ for example through constructing pipelines whose diameters are larger than needed.

“They have forgotten the financial side totally, when they are constructing the pipelines, if there is no financial aspect, the pipelines are twice as big as they should be.” (Investment Banker)

Such seemingly inherent lack of effectiveness is explained with the culture of the water sector and its professionals, who have been ‘too independent in the past’ and were able to design and execute projects that were mainly focused on technical aspects, but left economic aspects underemphasized. Here, the water sector professionals are regarded as professionals when it comes to technical aspects, but they lack financial thinking and the ability to perceive their water utility as a business organization. Increasing the private sector participation, for example through selling a part of the water utilities’ shares to a private company (which would mean to get managers from the private sector onto the management board as well), is regarded as a possibility for improving the economic effectiveness of these water utilities.

“I think that the financial thinking is missing [in the water sector] and if the private sector is involved, the financial thinking is immediately in the business, and that is the benefit.” (Investment Banker)

“I think the lack of financial thinking in the water utilities is the major difference [between them and the energy sector]. If you think about business, the most important thing is the capital employed but now the key driver is the technical aspect, not the financial aspect. If they would have also thought about the financial aspect, I think the capital employed would be only half of what it actually is now.” (Investment Banker)

The private sector is regarded as more effective than the public sector water utilities not merely for economic effectiveness but also regarding management skills. Comparing the public sector to the private sector, the former is lacking the accountability for delivering economically viable results because its organizations do not cease to exist once they became unprofitable, while a private company needs to be efficient in order to stay in the game and maintain stakeholder and shareholder support. Here, a reason for being ineffective is one of ownership, public or private, and not whether markets, such as monopoly markets or competitive markets, are affecting the behavior of the organization through creating incentives and disincentives for economic effectiveness. Effectiveness, therefore, is mainly seen as a function of ownership rather than as a function of market conditions.
“The private sector, the way I see it, in terms of management skills and in terms of financial or economic sense or understanding, is more sophisticated. Efficiency of operations is also better, because in public organizations you always have slack, because there are always guys who are, you know, lean against the wall, and in the private sector you can’t afford that because you are accountable on what you make on the bottom line. So, you have to make it more efficient by default.” (Investment Banker)

When the municipality is the consultant’s client, the municipal owner clearly states that a certain return on the capital invested in the water utility is expected and that it should preferably rise in the future while at the same time, other challenges need to be mastered as well. Those challenges include reacting to the legislative pressures coming from the European Union, such as stricter health and environmental standards for water and sewerage, the increasing shortfall of labor through large scale retirement in the coming years, and the increasing need to invest in the construction and rehabilitation of water and sewerage networks and infrastructure. These challenges affect each other as they also affect the profitability of the water utility in times where higher returns on the capital invested in the water utility is expected by its owner, the municipality.

“The water utilities do not have enough money to make the investments they need…the municipalities cannot raise the tariff too much because they compare it to other cities [and] in the next five years, [water sector] investment needs will grow and if regulation comes…quality factors will be supervised and investment…which will help the utilities. The municipalities want to increase the profits and it means for the water companies to produce more…but also from the ownership side it is not wise when these assets are in bad condition and there will be some problems with quality, which can affect the profit to the company as well.” (Financial Consultant)

“The water companies are producing money for the municipal budget, and the total costs for the municipalities will increase in the future and one part of how to finance these costs is to take the revenues of the municipal enterprises, such as waste management, water, energy, and some other services. This part is 25% of all municipal income and…this is a very difficult situation for the water utilities [in the face of] personnel, investment, and legislative challenges.” (Financial Consultant)

The fact that municipal budgets become tighter does not necessarily mean that the municipalities are willing to sell off their water utilities. The continuous revenue flow from the utility to the municipal budget helps to finance other municipal services. In addition, if the water utility switches its legal form from a municipal business enterprise to a limited liability company, its assets become re-evaluated. This can increase their value fourfold just through switching from valuing them at historic cost to present cost. Therefore, the municipal owner is able to receive a lump sum payment as well. The municipalities’ option to release capital by re-evaluating the assets of their water utilities
is a major reason why financial actors started to believe that it is not yet time for privatizing the municipal water works.

7.1.2 Rationality

Financial aspects have been the major principle of organizing for financial actors. Finance needs to take a bigger role in the management of the public sector and the water utilities. The effects liberalization had on the electricity sector are interpreted as mainly positive and similar effects are expected for the water sector. Private sector management professionalism and financial thinking that makes the water utilities more effective organizations are stressed as the tools needed to create a sustainable water sector. Here, the private sector organization is regarded as a rational business organization, which is a more effective owner than the public sector.

“The water utilities need to think more financially, more rationally…if the private sector would be involved, they would become more rational.”
(Investment Banker)

The changes financial actors propose to the municipalities, as well as the strategic changes municipalities have in mind predominantly deal with improving the financial situation for the owner, the municipality. Therefore, most restructuring plans for the water utilities are driven by financial motivation, and designed or executed by the municipality and with the help of financial actors.

“The directors of the municipalities are responsible for financing of all services the municipality provides, and […] it is the remarkable results for the municipal finance when you establish such a company with re-evaluated assets. So, that will be one interesting thing for the ownership side.”
(Financial Consultant)

“I explain it [to the politicians] just to give them a taste of the real things that can be done and what could be the end result of this restructuring…they get a lot of capital for the development of the city, they still manage the monopolies completely, and they have managed to sell or outsource these activities with the result that they have lower tariffs and costs there, and the value of these assets has grown, and that gets them more capital again. That is the total picture of what can be done.”
(Investment Banker)

However, the re-evaluation of assets of single water and sewerage utilities solves the short-term financial problems only of the owning municipality, if no other surrounding municipality joins with its own water utility. Therefore, the preferred solution for the Finnish water sector is to gain economies of scale by putting smaller, neighboring water utilities together and creating larger units that allow more professional management of the water services. Also financial actors understand that regionalization and creating larger economies of scale for water works would enhance their sustainability although they emphasize that the process of getting municipalities to agree with each other is rather difficult.
“They [the municipalities] understand that one possibility is to put together all assets of the units to one single company and producing the service based on shared ownership and not just shared operation...but it is very difficult for them to agree”. (Financial Consultant)

Different methods of calculating the distribution of future investments and profits are used by financial consultants that take into account the different needs and characteristics of municipalities. But even though the models for calculations are often adjusted to the individual needs of the parties, it remains difficult to arrive at a common agreement on how to distribute investments, profit, and ownership.

“In the projects where we are involved, about ten regionalization projects, the main issues are how to distribute the ownership and what will be the investment in each municipal area. We have a good system to analyze it so that it will be the same for each municipality that is involved…and it is open to all, so they understand what the future will be. But still it is difficult.” (Financial Consultant)

A financial actor’s major principle of organizing is to calculate and to approach management problems predominantly from the financial aspect. In this case, being concerned about the finances of organizational and economic life, the financial actors share important characteristics with the municipal actors for whom calculating and financial aspects represent a major principle of organizing as well. The analysis of the second key principle of organizing, the ability to compromise in the following paragraphs also shows that financial actors and municipal actors share a preference for individualism as well.

7.1.3 Individualism
Regional cooperation among municipalities for service provision and production represents the main task for securing the viability of many of Finland’s municipalities for the next years. For water and sewerage services, this cooperation is regarded as a solution to current and future challenges for the water sector. However, either creating larger water utilities through merging assets of water utilities, or just cooperating based on service production has been a rather troublesome and slow process.

Regarding the analysis of the interview data from financial actors, when it comes to initiating restructuring and making the creation of larger entities happen, the interesting things in the data are a combination of what has been said and what has not been said. The need to financially and rationally calculate and restructure the water sector is emphasized rather strongly by financial actors. However, problems in this process are dealt with by complaining about the political process in municipalities rather than by aiming to achieve a deeper insight into what it takes to create successful change and cooperation among municipalities.
A successful regionalization project of Finnish water services, the water utility of Hämeenlinna region, which merged with eight of its surrounding municipalities’ water utilities, is criticized by the financial actors for giving up some of its power and financial benefits it would be entitled to according to its relative size compared to the other company members. Further they point out that the previous water utility of Hämeenlinna had better economies of scale that allow a lower water tariff in its larger urban territory as in the surrounding, less densely populated neighboring municipalities with whom it merged together. Here, compromising is interpreted as a weakness and as an action against the principles of financial rationality.

Financial actors think structural change is less complex where a water utility is sold to an energy utility, both belonging to the same municipality, because one has to deal only with one municipality in which all decisions are taking place, opposed to the case of merging entities that belong to a number of municipalities with each other. But financial actors also recognize that out of the necessity to merge water services there may be no other option than giving in to the demands of others.

“In this case [where the water utility was sold to the energy utility, both belonging to the same municipality] there was only one decision-maker and they can do what they want…but in the case of Hämeenlinna region, it is different because the decision-making is dispersed...you have to do it differently there. Establishing the company in Hämeenlinna was...a regional necessity...to pool the resources.” (Investment Banker)

“But I think that if you forget the financial side, the parties make some mistakes. For example in Hämeenlinna I am sure that some municipalities have made some mistakes, and that Hämeenlinna is the city that has made the worst decision because they have the same transmission tariff in Hämeenlinna than in the neighboring municipalities, even though they have larger scale effects [in Hämeenlinna]. From a financial side, the tariff should be much lower in Hämeenlinna than in the outside area. This is only one example for their mistakes because they forgot the financial aspects. The water customers of Hämeenlinna are subsidizing now the rural areas.” (Investment Banker)

“I think gifts to individual municipalities should not be made because it would affect the balance of the company, and its future.” (Financial Consultant)

Financial actors have been trying to facilitate these restructuring processes, for example by talking to the municipal leadership, to politicians, to managing directors of water and energy utilities, and to the media. However, they have been facing opposition, and financial actors are mainly blaming the municipal decision-making system for the slow progress in these projects and the fact that power is dispersed among so many different actors, especially when more than one municipality is required to agree to a restructuring plan. Here, the municipalities’ lack of willingness to think about the bigger picture and to
make compromises is criticized by financial actors, even though according to the financial logic earlier, making compromises would be against their own logic. For example, financial actors do not like the idea of agreeing to the same water price in all participating municipalities if that means that the largest municipalities would end up subsidizing the water rates of others.

“Now we are establishing these regional companies and maybe they will be established within one or two years but I cannot say exactly because these projects are very slow. So, maybe the horizon will be about five years…” (Financial Consultant)

“The problem with regional cooperation or merging of business activities is that you have so many different decision-makers. In each municipality there are authorities, politicians, the board, the council, and then a second municipality and a third. Everybody has his own agenda and is trying to remain independent and still get the most profit out of it.” (Investment Banker)

One way for financial actors to try and make progress despite complications in the municipal decision-making process especially in situations where several municipalities need to agree is to propose financial and organizational solutions that favor the municipalities’ individualistic interests. For example in the question of not having any municipality subsidize the others’ water tariff because of the different economies of scale advantages and disadvantages, one of the investment banks also proposed a model according to which every municipality would be allowed to have its own tariff and investment policy.

In this case, however, the structure of the proposed organizational model would create a separate entity for the assets of all utilities; merge the service operations, and have, for each municipality, its own entity that manages its individual tariffs and investments, under the guidance of its direct municipal owner. Such a model creates not one single water utility as a result of the merger of several existing ones, but instead a service organization is created, an asset organization, and for each municipality a management organization. The result is a rather complex organizational arrangement, which represents in itself a challenge to municipal decision-makers because of its complexity.

“[In our concept] every municipality is able to have their own tariffs and own investment policy. If you have a tightly build city and rural area around, you can differentiate the investments and have different types of connection fees. But still, you can merge the operational parts of the water sector and that makes it a useful tool for local and regional cooperation of municipalities. The municipalities are most happy about that…this is a big advantage of this concept.” (Investment Banker)

“I have discussed with several towns about owner policies and how they should treat these [utilities] as owners and […] I have been meeting the
politicians of the city, different political parties, explaining them very practically what are the real issues, political issues, and how the decision-maker should treat these issues… they should not for example try to understand the complicated financial issues…but they should focus on different issues, and leave these more complicated issues to experts.” (Investment Banker)

In a situation like that, where the municipalities as owners of the utilities are struggling to agree on merging their water works in order to create larger, more resource effective units, financial actors are hoping for and welcoming pressures or incentives from the state level that would facilitate the necessary progress.

“There are 444 municipalities and it is very difficult to merge them, which is why the state administration has given out some rules now to push the regionalization of the services, which is also difficult but it is still easier than merging municipalities as a whole.” (Financial Consultant)

“The state or somebody should decide, who are outside; or offer large enough incentives, because the decision-makers of these municipalities are not the right persons to make the decision because they would be cutting their own jobs.” (Investment Banker)

Financial actors are predominantly concerned with the financial aspect of organizations, and their ideas shape their approaches to strategic change in the Finnish water sector, through continuously proposing financially innovative solutions to their municipal clients. However, these solutions are serving both the financial actor as well as the client although implicitly, the financial actors are working towards more private ownership in the water and sewerage sector.

From a financial actor’s perspective, and especially from an investment banker’s point of view, the current restructuring that would be possible through changing the municipally-owned water utilities from municipal business departments into limited companies is a beneficial business where large fees are to be expected. Because municipalities are able to release their capital through such an arrangement, they are rather passive about accepting private capital, for example through partly or fully selling their water utilities. Therefore, privatization as such is not expected to happen, neither by the municipalities nor by the financial actors, who had to learn about the limited possibilities of privatization and adapt their concepts to alternate solutions. These solutions either deal with the question of how to create larger units of water utilities or whether to merge them with energy companies. But despite the benefits the financial actor’s concepts offer the municipal owner, problems especially with the integration and regionalization process still exist. The answer to these problems lies in municipalities’ and financial actors’ focus on rationally calculating the risks and benefits. Financial actors are trying to optimize the risks and benefits according to the needs and demands of individual project participants although making compromises would promise more success.
7.2 The Financial Actor’s Perspective on Water Services

In this subchapter the analysis of financial actors’ logics is divided into their perspectives on how the culture of WSS should change; that regulation for WSS is needed; that the role of the private sector in WSS should increase; and how relevant the electricity sector is for the water sector.

7.2.1 Changing the Culture of WSS

From a financial actor’s perspective, one of the most important issues that need to be taken care of is putting the water utilities on a more solid financial basis, by putting their capital and its valuation on the basis of private sector principles and guidelines that have also been adopted by the electricity sector. In fact, the present system of dealing with the accounting and economics of water and sewerage utilities is perceived as rather unprofessional from a financial perspective since it does not represent the ‘correct value of the business’, meaning the value as it would be seen if the utility were to operate under private sector principles. This criticism of lacking economic and financial thinking also applies to how water tariffs are constructed because the current tariffs do not reflect the real cost of the service.

“The only way to calculate the value of the utility and evaluate it would be through a standard for all, to calculate the present replacement value of the transmission network. The return of that in the water sector in the big cities is about four percent. It is much lower than on the electricity sector or the district heating sector. […] That affects the tariff policy, and I think that those who made these tariffs are not aware of that.” (Investment Banker)

“They don’t calculate it from top to bottom by saying, okay, this is the capital employed in the business, and there is a certain minimum return that I have to make, and…okay, this is the tariff.” (Investment Banker)

Water utilities are regarded as rather traditional organizations compared to, for example, those sectors which have been liberalized and are now functioning under competitive markets or at least under quasi competition facilitated by a regulative authority, such as the energy sector in Finland, or the energy and water sector in the UK. Especially the fact that previous decades in the water sector have been dominated by technological issues and later also environmental issues, the water utilities were allowed much independence because their dealings were hard to understand to outsiders. However, because nowadays the main focus is on financial concerns, the water utilities are more transparent to outsiders, because finance is a somewhat universal language and can be spoken with any organization; that is a fact which the water utilities have to get used to.
“The water sector is still much more conservative than the energy sector. It is really extremely conservative compared to energy, especially now, when the energy market has changed…A few years after the liberalization of the energy sector, they really discussed about mobility issues and finance for example, finance was a word they never used in the companies in the beginning. They were completely unfamiliar issues, ‘profit’ for example.” (Investment Banker)

“The water utilities have been extremely independent…it has been so technically special what they manage there, but now the issues are not technical issues but more financial and owner policy type of issues. But [the utilities] got used to the idea to manage the company as they wish.” (Investment Banker)

“20 years ago it was mainly technical and quality issues…now it is more a business and management and financial issues, which are much more important. Before, the water works were only one part of the technical services and after that they are more like businesses and they have income statements, balance sheets…now they care more about the opinion of the water customer, and private services are purchased more.” (Financial Consultant)

“Effectively, in a public utility you don’t have strong management. You have a pool of engineers or civil engineers, who are in the business of transmitting water from A to B or making water and wastewater treatment plant activities but they don’t have any other activities.” (Investment Banker)

7.2.2 Regulation and Ownership of a Monopoly Business

Whether the Finnish water and sewerage utilities should be owned by the private sector rather than by the public sector is an issue financial actors approach from the question of regulation in the hope of maintaining a more neutral position on the issue of privatization of water services.

Regulation is regarded as the key issue in developing the Finnish water sector into a more competitive and sustainable business sector. First of all, the common notion among financial actors is that a regulatory authority establishes a certain set of rules and regulations by which the entire sector has to operate. This is perceived as rather fair to all organizations and not at all as disadvantageous to the owners, utilities, and neither to the consumers. Financial actors are also in favor of a regulatory agency because in such a case, it would become more likely to adopt similar methodologies for regulating the economics of water utilities as in the electricity sector. It is likely that such a regulator would allow the owners to make higher profits, while at the same time the regulator would demand the owners sufficiently invest in the water and sewerage infrastructure. Such measures would secure the quality and safety of water and sewerage services for consumers.
A higher price for consumers is accepted in this case, especially since with or without regulation and switching to a similar methodology as in the electricity sector, the rise of water tariffs in the future is inevitable, both because the owners demand more profits and because extensive parts of the infrastructure need to be renovated. The regulative authority is expected to protect the consumer from the municipal owners’ interest of trying to maximize profits from the water utilities for the purpose of compensating for lower municipal tax and on the expense of the future viability of the water utilities.

“[The municipalities] claim that this is the service to their inhabitants, their customers, and that they do it for free.” (Investment Banker)

“If the municipalities instead of increasing the tax…increase the water tariff...it can be considered as tax substitute or hidden tax.” (Investment Banker)

In addition to the fact that a regulator would be fair to all, financial actors also emphasize the risks involved in switching from a publicly owned monopoly to a privately owned one. If there is going to be any privately owned water utility, strong regulation needs to be in place. Here, the monopoly character of the water sector is stressed and the risks for the private monopoly taking advantage of its position are regarded as being greater than under a public monopoly, because the financial actors are well aware that the private company is mainly driven by profitability.

“… when you talk about monopolies, it is very questionable whether you should privatize or convert the public monopoly to private monopoly.” (Investment Banker)

“One crucial requirement for introducing the private sector into the public water sector is a…a strong regulator that has influence over the pricing and the tariffs …nobody wants to move from public monopoly without supervision to private monopoly and prices quadruple.” (Investment Banker)

### 7.2.3 Increasing the Role of the Private Sector as Owner or Operator

Regulation is also seen as a tool to increase the chances for private sector participation in the form of partial or full private ownership of water utilities. A regulative authority for the water sector is also seen as the precondition for privatizing any of the water and sewerage utilities because once the supervision of the monopoly business is safeguarded, the question of who owns the regulated business becomes a political and economic choice rather than a necessity of being owned by the municipalities and therefore under regulatory control of the local democratic government. Once the monopoly is regulated by a separate authority it almost becomes a business like any other, which would allow the private sector as owners of such a business as well.
“Once you start a water regulator… it is only a question who owns regulated business, who is the most natural owner of regulated businesses… I’m not trying to commit myself actually into who should own it.” (Investment Banker)

“It is easy to say that the municipalities should own them. I don’t think that this is what they should want… this type of thinking “we ought to keep it to ourselves” is not good.” (Investment Banker)

In case the municipality remains the owning entity of the water and sewerage utility, at least it could manage itself and its assets through increasing private sector participation by outsourcing certain activities, such as the management and operation of water and sewerage treatment plants, network maintenance, and even finance. Principally, the financial actors see the end of outsourcing the municipalities’ activities to the private sector where its decision-making function begins, but everything else does not necessarily need to be managed by the municipality or the water utility. This idea is also regarded as the end stage of a process the public sector and municipalities are undergoing at this time already.

“I can easily see the trend is that the municipalities only manage it all and they buy the services from different parties. Even finance can be kind of outsourced. Actually, what we are doing is kind of capital outsourcing.” (Investment Banker)

“Of course the municipalities can have their own people for managing the outsourced service units…but in the extreme case, even they can be outsourced to consultants. And you can change those consultants if you are not happy with them. You just keep the decisions like a real owner. As an extreme, even the management of the municipalities’ own things was outsourced… that’s the general trend what is taking place.” (Investment Banker)

7.2.4 Relevance of the Energy Sector for Financial Actors and WSS

For the financial actors, the energy and especially the electricity sector serves as an important source for ideas how to manage the water and sewerage sector in Finland. To a large extent, this phenomenon can be explained through the fact that most of the investment bankers started their professional careers in energy companies where most of them experienced the liberalization of their sector not only in Finland but also in other European countries, and later moved over to the financial domain.

“Most of my expertise absolutely comes from the energy sector; I have been there for a long time. Actually, this [other investment bank] is full of my old friends… we used to work at [the energy company] before and then also together [abroad]… now we are competitor… both investment banks in the same business area and even the same type of companies.” (Investment Banker)
For financial actors, the difference between water and electricity services is not as clear and distinct as it is for water sector professionals, for example. If the water sector would become liberalized, similar developments as in the electricity sector are expected in terms of competition, professionalism, and management, which are perceived as more advanced in the energy sector than in the water sector.

“The difference between the water and electricity is that the market of the water is limited to the region. You need to have different tools to have competition in that region…I think it is not so easy.” (Investment Banker)

“I think that energy and water sector is not much different from any other private business sector except that they are monopolies. I believe there is a lot of cost savings but the effectiveness would be much better if many things are privatized. But it’s not only to save costs…it’s about widening the operating area and providing better opportunities for employees.” (Investment Banker)

“If I look at the businesses, the transmission of electricity or drinking water or wastewater, I don’t see any big differences. One difference is that we have a regulator concerning the transmission of electricity and gas but otherwise I think they are quite similar.” (Investment Banker)

The water sector can learn plenty from the electricity sector and could increase its effectiveness on a whole, for the benefit of the owners, the water utilities and their employees, and consumers. Through merging water and electricity and therefore forming a so-called multi-utility, it is suggested that more professional and effective management could be introduced to the water utilities. After all, liberalization and privatization increased competition in the electricity sector, and if the water sector would be liberalized, its effectiveness would increase as well.

“If you think about energy companies who are limited liability companies, they are much more efficient than the water utilities and for the municipality it is a very effective way to put the water sector in good shape, if they put these activities into the same unit…it could also be one way to introduce business thinking to the water sector.” (Investment Banker)

“If you look at the energy business before and after the privatization, it is much more efficient at the moment and the costs are much lower...if the water sector would be privatized, the same effect could be seen in the water sector as well.” (Investment Banker)

The direction the water sector is heading seems to be rather clear for financial actors, except that the time frame is subject to different estimates. The water sector follows the developments in the energy sector, which means that enabling private ownership by establishing a regulatory agency will take place at some point in the next few years. A regulative authority which could adopt similar methodologies to regulating the water sector as in the electricity sector will be established in order to create the conditions for a
fully liberalized market. Because regulation is seen as the first step to full liberalization as opposed to the current ‘quasi’ liberalization where private ownership is possible in theory but not in practice, financial actors are hoping for such a regulative authority to be created soon.

“On the energy side there is a regulator in Finland, but in the water sector the regulation will come a little bit later [and when it comes] water will be closer to the energy side and the rules will be the same, the methodology I mean.” (Financial Consultant)

“In the energy sector, this evaluation of assets has come because of the regulation, and now they have to know the value of the company since the regulator is continuously comparing the results. But in the water sector the directors just don’t know the regulator system, the methodology, they are out of that but they will come to that.” (Financial Consultant)

“The change of the water sector follows the energy sector…we even discuss about those at the same time when we talked in that one city about our model to finance the network businesses.” (Investment Banker)

Even though financial actors expect the full liberalization of the water sector to follow the pattern of the similar process in the electricity sector, it is recognized that fundamental differences between water and electricity services exist that prohibit a similar type of competition for water services as compared to electricity. After all, water production depends on locality while electricity production is not as constrained by geographic conditions. In addition, it is possible to transfer electricity through a nationwide or even transnational electricity transmission network, while the distribution of water is limited as its quality decreases with the distance it is transported, and leakage and pipe pressure issues are critical.

“Liberalization of the energy sector is different from the water sector, because… there is competition for the sales of energy. But in the water business, there is only one water utility that produces water, locally. There are no possibilities to add another supply system or another producer, which means there will not be this kind of liberalization.” (Financial Consultant)

Besides the electricity sector being a driver for the change in the water sector, issues from the liberalization of the electricity sector a decade ago also have the potential to complicate matters for those whose aim is to fully liberalize the water sector. Financial actors have the impression that the municipal sector regrets having sold some of the electricity utilities to the private sector. At that time when the sell-out happened, in the beginning of the 1990s, municipalities were in a financial crisis due to the great depression which started in the late 1980s. Since then, political opposition to the idea of selling more municipal assets has increased and the municipality has been more careful with its assets, partly because of criticism concerning the way prices and electricity service quality have been developing after the liberalization. Even though the current
financial crisis could be a motivating factor for the municipalities to sell their water utilities or energy utilities, the past experiences with the liberalization of the electricity sector have made them more cautious.

“When [the municipalities] didn’t understand that energy is a business, they sold the companies too cheap… and they have already lost the money that they got. I think that the owners are much more careful when they are now selling the water companies.” (Investment Banker)

“[The liberalization of the energy sector] is not a clear issue at all. Some cities and rural municipalities sold energy companies, electricity companies especially…they got huge amounts of cash, because when the market opened, all these power companies were really eager to buy, and to pay almost whatever they asked for. There was not… there was only a rule of thumb about the price of a utility. So, the prices were really high, so I would have sold as well, I believe.” (Investment Banker)

“Then after this phase from 1995 to 2000 or something…there was some anger about the tariffs because they rose somehow, and there were payments to customers who need to have reserved a lot of capacity use only little electricity.” (Investment Banker)

Financial actors’ notions about effectiveness revolve mainly around financial concerns, and their ideas about how the water sector should be organized are affected by the insights they have in the electricity sector. Regulation, therefore, is regarded as a key to promoting privatization in the Finnish water sector.
7.3 Summary of Financial Actor’s Logic of ‘Flexible Financialism’

In order to summarize the financial actor’s logics I will first briefly review why financial actors were able to become relevant to the development of the Finnish water sector (thus referring to the analysis in chapter four about the emergence of financial actors) and then summarize the key characteristics of their institutional logic.

Table 7-1 shows that when the financial actors entered the field of ‘managing water services’ around 1999 and 2000, they expected to assist in the privatization of municipal water utilities, as had happened a few years earlier with municipal energy utilities. However, within a few years, it became clear that municipalities are holding on to their utilities and that they require a different sort of advice from financial actors with regard to the financial restructuring of municipal assets. The financial actors were able to adapt their solutions to the municipalities’ problems and provide their expertise. Therefore, the financial actors stayed in the game, while other private sector companies, such as industrial services companies that also tried to promote privatization or at least the outsourcing of municipal water and wastewater operations to private contractors, had to withdraw from their plans of taking on a more influential role in the change process of the water sector.

Table 7-1 Financial Actors’ Strategies and Tactics Affecting the Water Sector

<table>
<thead>
<tr>
<th></th>
<th>1995</th>
<th>2000</th>
<th>2005</th>
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<tbody>
<tr>
<td></td>
<td>Tactics: Talking to media about privatization of water sector. Approaching water utilities and municipalities.</td>
<td>Tactics: Focusing on Municipalities as most powerful actor. Adapting the concepts to this actor’s needs and logics. Solving the client’s problems allows staying in the game, waiting for opportunities. Leveraging the municipalities’ logic to promote own goals.</td>
<td></td>
</tr>
<tr>
<td>PWC Finance (Financial Consulting)</td>
<td></td>
<td>Consulting in Regionalization Projects of Water Supply and Sanitation</td>
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<tr>
<td>PCA Finance (Investment Banking)</td>
<td>Privatizing Water</td>
<td>Sale-Lease-Back for Energy &amp;/or Water</td>
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<tr>
<td>Icecapital (Investment Banking)</td>
<td>Privatizing Electricity</td>
<td>Privatizing Water</td>
<td>Merging Water Utilities with Energy Utilities</td>
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Financial actors were able to maintain their relevance for the water sector because they possess a certain conceptual flexibility. Those actors who are in the business of pure intangibles – such as the financial consultants – are in the business of knowledge and especially knowledge about finance. As I pointed out in the analysis of municipal logics, finance becomes even more important for municipalities that have budgetary problems. They are trying to solve their financial problems by exploring their options and the financial actors with their intangible services have an advantage compared to companies who provide a tangible services offering, as industrial companies mostly do. If a company is in the business of operating wastewater treatment plants, it becomes difficult to stay in the game as long as municipalities are unwilling to outsource the operation of their wastewater treatment plants. However, if a company is in the business of providing management and financial consulting, it can stay in the game regardless of whether the municipalities are selling their assets to the private sector or whether they just shift assets internally. It is the nature of their service offering, combined with strategies of how to access the networks of decision-making and to build constituencies for their goals that allows financial actors to be involved in a large variety of contexts.

The institutional logics of financial actors can be summarized as flexible and financial. Their logics contain rather strong belief in the possibility to maximize individual benefits by calculating and thus convincing decision-makers through the ‘rational facts’ of the numbers. The financial actors inherently prefer and advocate market liberalization and privatization, but they equally have the ability to change their views according to their clients’ needs and promote concepts that may even contradict their inherent ‘free market’ principles. Thus, although these actors’ belief in the effectiveness of ‘the market’ and private firms, which is a neoliberal mindset, they are flexible, perceptive, and adaptive in what they do and propose to their clients. Besides the free-market agenda financial actors may have, their primary goal still is to make money and that is achieved by serving their clients.

Financial actors also possess vision that is more according to their own inherent ideas and beliefs about how water services and the economy in general should be managed. The vision of financial actors is to increase the private sector share in the economy because they believe in its managerial supremacy. But while they regard the private sector as managerially superior compared to the public sector, they acknowledge its ‘moral inferiority’ when it comes to taking advantage of monopoly positions. Therefore, financial actors acknowledge the necessity of having regulation in place and would not accept a non-supervised private monopoly. But there is another reason why these actors call for regulation, which is the fact that they regard it is a prerequisite to privatization. Here, the demand that the state should take action and lay out the ground rules for private sector activity is clearly visible. Financial actors regard it as a problem that the state has no plans at the moment to establish these rules of the game, most likely, also because state actors are aware that they would establish the very conditions which would promote private players in the market. But once more, financial actors’ views on why a water
sector reform and more participation of private sector companies (either as owners and operators or merely as operators) is important does not exclusively relate to their individual self-interests. Instead, these actors are also convinced that the Finnish water sector’s sustainability is threatened and a large-scale reform with more private sector participation serves the long-term interests of the economy, citizens, and the water sector.

The financial actors’ involvement in the restructuring process of municipal water works and municipal reform provides more solid knowledge about finance and asset restructuring to their municipal clients but it also has negative consequences on the development of the water services themselves. Regionalization projects that have the goal to merge smaller water utilities together are hampered by the involvement of financial actors because their emphasis on rationally calculating the risks and benefits of municipal reform and restructuring somewhat ignores the ambiguity that arises from such projects. These projects are of long-term nature and contain a number of different known and unknown factors that come into play along the process, and a number of different parties need to agree by negotiating. Especially, the financial actors’ notion that making compromises is like distributing ‘free lunches’ in a world where no such thing exists, ignores what can be gained by giving something up. Financial actors try to convince of their solutions through the rationality of numbers and the financial benefits of a project in order to justify structural changes in municipalities. Hence, financial actors assume that decisions on local government level, although perceiving them as being ‘not rational’, are based on numbers and that financial aspects are the most important aspects. This is a logic that makes negotiations in regionalization processes difficult as every party wants to calculate and maximize its benefits.

However, in the cases where this logic is applied to the intra-municipal change such as when the local water utility is merged with the local energy utility, it is more successful because financial benefits are redistributed within one municipality. In such cases, whenever one side is losing, another is gaining and since the municipality thinks of itself as managing a portfolio of activities that requires overall balance, it matters less in which areas something is gained, and where something is lost, as long as the organization is balanced overall. Therefore, although a merger between the local municipally-owned water and energy utility may face resistance from the utility side, the municipal council may still agree on the restructuring because it delivers capital that is used to balance other activities of the municipality that may operate on a loss, such as health and cultural services.
8 Discussion

In the following chapter I discuss the empirical analysis and its findings. The chapter is divided into four parts.

In the first part, I reflect on the logic of municipalities by discussing its grounded characteristics of rationality, individualism, and collectivism. I am using my theoretical ‘lens’ of new institutional theory for that purpose, and I will demonstrate how the logics especially of financial actors fit together with municipal entrepreneurialism and what role state governance actors have in the process.

In the second part of this chapter, I propose a theory of local public (water) services commercialization (Figure 8-1) and propose a mechanism with certain outcomes (Figure 8-2) that shows how the governance level is responsible for municipal entrepreneurialism and much of its key characteristics; that the financial actors facilitate municipal entrepreneurialism but do not drive it because their logics merely fit conveniently to the municipalities’ logics; and that the outcome of municipal entrepreneurialism promotes the merging of water and energy utilities instead of the regionalization of water utilities as such.

In the third part, I will explain how the theory I propose contributes to existing theories by using the theoretical framework (Figure 8-3) that I first presented in the theory chapter.

In the fourth part, I discuss the implications of the commercialization process for the reform of public water supply and sanitation in Finland more in detail.
8.1 Underlying Causes for the Nature of Municipal Entrepreneurialism

In this subchapter, I clarify the underlying reasons for municipal entrepreneurialism resulting from rationalistic and individualistic logics and how that links the different actors’ actions together. I am discussing this issue because it is the basis for proposing my theory of local public service commercialization, and it represents a step towards understanding the mechanism of commercialization and its outcomes because it shows how actors’ actions are linked to each other by their logics.

I will first reflect on the logic of municipal entrepreneurialism that contains strong rationalistic-individualistic notions and discuss its linkages with the national governance actors’ logic of interventionalism and laissez-faire, and the financial actors’ rational-calculating logic. I will do so by using new institutional theory and reflect on the grounded categories of municipal entrepreneurial logic, which are rationality, individualism, and collectivism.

8.1.1 Rationality as Outcome of a Mimetic Process

The municipalities have been increasingly exposed to normative pressures from the national governance level to improve their management practices and their ‘professionalism’. This learning process, however, is mainly about adopting private sector management principles and techniques (such as the balanced scorecard) in order to improve the effectiveness of administration and local public service provision. Therefore, the normative forces (such as ‘becoming professional’ as the private sector) and mimetic forces (such as ‘imitating’ from the private sector) forces are both pointing the municipalities toward the private sector, which is perceived as more effective and successful in managing and hence, its practices are regarded as more legitimate and more worth imitating. I found it particularly interesting that municipal managers perceive the private sector as more effective and that they also believed that the ‘public’ does so. Municipal managers increasingly feel that they ‘must have a reason’ why the municipality is in charge of certain activities instead of letting a private company take care of it. As a result, municipal managers not only lack financial resources but also legitimacy as a resource. Embracing more private sector oriented ways of managing and being more flexible, passionate, customer- and outcome-oriented are believed to improve the organizations’ effectiveness and thus, provide legitimacy for the public sector to ‘exist’ and to ‘manage’. However, the private sector is also a useful resource for public sector managers from which they borrow phrases that help justify existing management thinking in the public sector. Especially the notion of ‘professional management is rational management’ is rather a myth than a reality and no one can actually expect that management in the private sector would be rational per se. Therefore, I will explain in the following paragraphs why municipal entrepreneurialism has adopted a private sector ‘rationality’ way of thinking by describing the imitation process as a process of rationalization.
As presented during my empirical analysis, municipal administration imitates private sector management practices and it mainly does so because of two kinds of motives. One motive is the genuine desire to achieve performance improving effects and to find solutions to problems, which I call ‘altruistic’ imitation; while the other motive relates to merely acquiring legitimacy for the organization and to justify existing beliefs of management, which I call ‘egoistic’ imitation. In both cases the benefit for the organization is not only to enjoy improved management and effectiveness but to obtain legitimacy for its ‘reason to exist’. Legitimacy that is gained through imitation therefore also needs to be seen as the organizations attempt to acquire a resource that will support their actions and their ‘reason to exist’ – not only based on mere grounds of efficiency and effectiveness.

8.1.1.1 Rationality as a Product of an ‘Altruistic’ Imitation Process

In cases where managers faithfully believe that the imitation of private sector and entrepreneurial management thinking and acting improves the performance of their own organization, I developed the category of ‘altruistic imitation’, which is one source for the rationality of municipal managers and urban entrepreneurialism. In this case, the practices that are imitated are perceived as successful and managers dedicate resources to implement the new practices and ways of thinking. This adoption of private sector principles may be a rational decision but in some cases, it is merely collective frustration that renders managers vulnerable to unrealistic hopes and makes them look for magical solutions that will relieve their source of frustration (Abrahamson, 1996; Klapp, 1969).

The managers look for these magical recipes in the private sector because they believe it to be more successful than the public sector, especially in entrepreneurial behavior and the positive outcomes that are associated with it, such as professionalism, self-confidence, success, risk-taking, and competitiveness. But while this makes public sector managers look like they are blindly following the private sector, I also saw a significant amount of doubt in public sector managers that the private sector would be more successful per se. Interestingly, even in these cases, they seemed forced to use entrepreneurial jargon, to imitate the private sector, and to benchmark themselves with the private sector in order to secure legitimacy for the public sector organization by securing stakeholder support.

Public managers engage in this kind of imitation because organizations must appear to be correctly managed, and they do so by adapting management techniques that are collectively believed to be effective and rational (Meyer and Rowan, 1977). If they fail to do so, they may lose stakeholder support (Abrahamson, 1996). Because the municipality is conducting its business in the ‘the right way’, or in what could be described as ‘in the current management fashion’ (Abrahamson, 1996), it obtains legitimacy.
The rigid application of outsourcing of local public services activities or the implementation of the ‘balanced scorecard’ are examples of the public organization following a management ‘fashion’ since their performance improving effects are promoted by business consultants despite their performance improving effects often being exaggerated.

Imitation is a process of translation (Sevón, 1996) and thus, the outcome of imitation never fully resembles the practice, behavior, or object that has been the subject of the imitation. Instead, the outcome represents a mere variation on what has been imitated. Such imitation also bears risks. As I showed in my analysis, in the case where local water services require structural reform and a regionalization would be called for, the public sector manager’s rigid application of ‘rational management as it is done in the private sector’ in fact leads to counter-productive outcomes in local public services reform. Local public services and water services reform requires different negotiating parties to concede some of their demands but instead of doing that, municipalities emphasizes the short-term individualistic benefit maximization of municipalities and thus, it hampers the negotiating municipalities’ abilities to form agreements with each other, for example, about regionalizing water services.

However, the counter-productive effect private sector imitation has on the local public sector cannot be blamed on the predominant logics of the private sector itself, for example by arguing that they would foster the municipalities’ individualism. This is mainly because of two reasons. First, processes of imitating are at the same time processes of rationalizing (Sevón, 1996) because what spreads are not practices per se but edited versions of what happened (Sahlin-Andersson, 1996:83). As a result, the imitated private sector style of ‘managing’ is a rationalized version of what is in fact taking place in the private sector and hence, it can be considered a ‘myth’ (Meyer and Rowan, 1977). Second, imitators usually lack first-hand knowledge of what they imitate (Sahlin-Andersson, 1996:80) and therefore it is understandable that public sector managers lack sufficient knowledge of the necessary ingredients that contributed to the successful private sector management practice. Third, successful imitation requires innovation (Sevón, 1996), which is a resource-intensive activity that requires time, capital, commitment by management, and in the case of local government, also significant amount of political will.

But in situations where the private sector management style is rather used to justify existing management thinking in the public sector organization than to actually change the thinking, the necessary innovativeness and commitment that are a prerequisite for the

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8 For example, outsourcing has been described as management fashion and its performance improving effects in the private sector are doubted by a number of authors and traced back to mimetic behavior among private sector firms (e.g. Lacity and Hirschheim, 1993), and a large number of outsourcing failures lead to another, more recent trend of ‘insourcing’ (Lacity and Hirschheim, 1995).
imitation to be successful are missing. For such cases, I have distinguished between the ‘altruistic’ form of imitation where public sector managers faithfully imitate in order to improve their organizations’ effectiveness and ‘egoistic’ imitation, where managers use the discourse of private sector management thinking to justify their existing management believes and decisions.

8.1.1.2 Rationality as a Product of an ‘Egoistic Imitation’ Process

Extensively calculating and making rational decisions is regarded by municipalities as a ‘better’ and ‘more professional’ way of managing but it also serves an important role as a discourse to justify existing beliefs and behaviors of management.

The application of practices and especially private sector ‘thinking’ allows management to justify its decisions and behavior (Sahlin-Andersson, 1996) by arguing that ‘those’ which are perceived as more successful and ‘efficient’ (usually represented by private sector companies) ‘do it the same way’. Cutting the budget, maximizing the benefits of one’s own municipality, or lacking the ability of compromising is often justified with the argument that ‘no private company would do it either’ although this perception needs to be considered a ‘myth’ of how the private sector conducts its business since there is ample evidence on cooperation and compromising in the private sector.

Private sector companies cannot be blamed for their practices to spread as ‘myths’ but neither can the municipalities be blamed for adopting these entrepreneurial ‘myths’ of the private sector. Sahlin-Andersson (1996:75) argues, as “public agencies are increasingly compared with private companies, and private companies are generally perceived to be more successful, then the ways in which the public agencies differ from the private companies increasingly constitute the definition of what their problems are”. She further refers to Sevón (1996) and says that during uncertainty, actors are on the search for more reliable experiences and models to imitate in order to find a new identity.

Distributed by ‘editors’ such as consultants, researchers, the media, or simply by managers who are eager to learn and keep their eyes open, success stories are encountered and they turn into ‘recipes’ by being made ‘logical’ and they are often promoted by those who were not even present when ‘it’ happened (Sahlin-Andersson, 1996). In this context, I would like to question the effectiveness of management consulting in the entrepreneurialization of municipalities that actively promotes the adoption of private sector management tools and practices. The entrepreneurialization of local government needs to be seen as the attempt to construct a new, more legitimate identity. Because the main components of this new entrepreneurial identity are imported by imitation, they are edited and rationalized versions (often through consultants and academics) of what had really happened. Thus, the municipality with an entrepreneurial identity is benchmarking itself with a type of rational and entrepreneurial private sector organization that only exists as a myth.
Further, public sector organizations sometimes only borrow or imitate from the private sector what is convenient and not the whole pattern that would be necessary for the imitation to work in its new context (Sevón, 1996). Therefore, I see the matching individualistic and profit-maximizing logics of municipal managers and financial actors as an example of the powerful municipal actors finding other actors that provide them with solutions to their problems that are ‘convenient’. Continuing this argument a bit further, it means that financial actors have no significant role in increasing the municipalities’ entrepreneurialism per se but the solutions they provide are based on financial-rational thinking that conveniently fits to the entrepreneurialized municipalities’ individualistic-rational logic. Hence, I argue that the entrepreneurialization of local government is based on coercive pressures by the state governance level and that the financial actors are merely used by municipalities to solve the problems that occur in this entrepreneurialization process – because their solutions are based on a logic of ‘rationalism, calculation, and benefit-maximization’ that fits the thinking of municipalities.

8.1.2 Individualism as Independent from Private Sector Imitation

The municipalities’ lack of vision and cooperation combined with an emphasis on rational calculation has been counter-productive to water sector and municipal reforms. This individualistic mindset, however, is not a new phenomenon although municipalities justify it by arguing that private sector companies would also not hand out ‘free lunches’ but first look after their own interests. This thinking has negative consequences for the municipalities’ ability to make compromises, which is required in regionalizing local public water services and public services in general. Also in this context, the argument in literature seems to be that ‘market-oriented’ reforms create individualistic thinking in the public sector although I question this idea and argue, based on my analysis, that individualistic and self-interested thinking is a separate process and is neither created nor promoted by market-oriented reforms.

In order to support my argument, I am drawing again on the characteristics of the imitation process. As I explained in the previous paragraphs on imitation, the public sector manager’s argument that the private sector also prioritizes self-interest over the interest of a community is supposed to justify the managerial beliefs that already exist in the local government. Self-interested behavior and individualism is even regarded by public sector managers as one of the private sector’s sources of competitiveness and success although literature on entrepreneurialism has provided ample evidence and arguments that cooperation is an essential element in the entrepreneur’s success because entrepreneurs rarely control all resources they need to be successful (Schumpeter, 1950; Johannisson, 1995). Therefore, municipal managers are legitimizing local government’s self-interested behavior by deploying the mythical discourse of self-interested behavior being a source for effectiveness and competitiveness of the private sector.
Instead of locating the source of municipal individualism in its adoption of market oriented reform and private sector managerial behavior, I would like to point to the municipalities’ inherent individualism that I regard as the source of its present self-interested behavior. I argue that the municipalities’ thinking is inherently individualistic because I could not find any indication in the data that municipalities would have been less individualistic in the past than they are at present. Instead, there is evidence provided through research for example by Sandberg (2005) and Helander et al. (2003) about decades of municipal resistance to cooperate and merge their administration and services, which is in accordance with my own analysis of municipal managers’ logics, who argue that inter-municipal cooperation is something rather new for them. In the past, cooperation between municipalities has often been the result of constraints. For example, when a municipality did not have own groundwater resources, it would cooperate with its neighbors. As a result, I conclude that municipal individualism is a phenomenon that has existed already decades ago and is an inherent characteristic of local government and I reject the notion that globalization and entrepreneurialization are the processes that create ‘market-oriented individualism’ in local government. Based on my analysis I argue that what has changed due to globalization and entrepreneurialization is that local governments’ individualism is nowadays more visible than in the past, because the state’s higher financial support in the 1980s and early 1990s covered up the municipalities’ individualism since it did not require them to cooperate with each other as much as they do today.

However, local government is not individualistic per se. In questions related to its individual survival it practices collectivism by shifting resources within the organization and demands its internal units to ‘think as a whole’. Therefore, I make a distinction between municipalities’ internal collectivism and external individualism because internally, compromises are achieved, and resources are shifted from one department to the other in order to keep the overall balance of the organization in order. If that thinking would be applied to the governance and management of administrative regions and not only to administrative localities as it seems to be the case at present, municipalities could be considered to think also externally in a collectivistic way.

Also in this context I would like to emphasize that the financial actors’ logic of calculating, benefit-maximizing, and rationality should not be considered a driver for municipal individualism per se. Instead, I found it to be more a facilitator because the fact that municipalities deploy financial actor’s advice shows that municipalities are thinking in individualistic and financial terms and the financial actor’s advice allows them to act accordingly. The discourse of ‘rationality’ and calculating in ‘due diligence’ is used by municipalities to give legitimacy to their decisions, since these terms are associated with professional management and decision-making, and to justify the inherent individualism of municipalities and other existing believes of its management.
8.2 Towards a Theory of Local Public Services Commercialization

In the following subchapter I am proposing my process-based theory of local public water services commercialization and extend it to a more general (or ‘formal’) theory of local public services commercialization because I argue that my theory on water services commercialization may also be applied to other local public services, especially when they have the potential to be profitable to the municipality. However, I would like to emphasize that this general theory of local public services commercialization would require more research and that I see my theoretical arguments more like the steps toward a more generally applicable theory of local public services commercialization.

I will first propose the theory followed by proposing a processual mechanism of commercialization and its outcomes. Subsequently, I will discuss my theories’ contributions to the theoretical framework of existing theories on the subject.

8.2.1 A Processual Theory of Local Public Services Commercialization

Over the past ten years, the large municipalities have increasingly regarded the water utilities as a source of financial resources. This commercialization has happened through a changing attitude in the municipalities towards managing their own affairs in a more entrepreneurial manner that allows them to actively substitute decreasing state funding with alternative sources of income. The water utilities represent one of these alternative sources of income that are used to help balancing the municipal budget. The most important driver for this process has been the state government’s coercive pressure on the municipalities. The state decreased its funding of municipal affairs and encouraged municipalities to become more effective, and as a result, municipalities were coerced into becoming more entrepreneurial.

As depicted in Figure 8-1 (opposite page), the state has been pressuring municipalities towards higher self-sufficiency from state grants, and imitation of private sector managerialism. The state is withdrawing from the scene as a financier and is implementing stricter standards on services provision, such as for water supply and sanitation, while the economic side of regulating municipal services and enterprises does not receive sufficient attention. In other words, municipalities face pressures from decreasing income and higher service standards, and as they are being told to become more entrepreneurial, the relaxed economic regulation allows them to conduct their business in a rather unregulated, flexible manner. The space (or subject position), which becomes available through the lack of state finance and regulation is filled by financial actors. Therefore, I find that contrary to the notion of the municipalities handing over their activities to the private sector, they substantially turn to financial actors. The reason is that increasing municipal entrepreneurialism has given municipalities the confidence and motivation to own and operate profitable businesses themselves. I see this trend as contrary to the initial response to crisis and reform, which the public sector showed in the early 1990s when it seemed to divest its operations by selling to the private sector rather
swiftly, such as during the liberalization and privatization in the electricity sector. Further, because of the experience with the energy sector liberalization, learning occurred in the meantime in municipalities since these decisions and the benefits that were hoped for have been questioned by a variety of municipal stakeholders and the municipalities themselves.

As shown in Figure 8-1, the role of the state becomes less important (especially in terms of financing the municipalities) and as a result, the municipalities are becoming more proactive and entrepreneurial and turn to financial actors to help them find new resources that can substitute (at least partially) for the decrease in state funding. Therefore, when the state actor withdraws from the scene, a subject position opens up, where other actors can enter. These actors, need a suitable value offering for municipalities (as financial actors do by providing valuable advice on financial restructuring) but also the right timing is important, and knowing who to talk to and how to get access to municipalities. Therefore, this space is filled by financial actors instead of other private companies because the municipality, emerging as self-confident owner, requires advice on restructuring its assets rather than selling them to the private sector.

Financial actors are filling these open spaces (referring to Figure 8-1) over time by adapting their proposals for municipal restructuring to fit the municipalities’ own logics and needs. Financial actors require but also possess the conceptual flexibility to adapt their solutions to the municipalities’ needs because their business is one of changing and
transferring assets, but whether they earn their commissions from transactions within the municipality or by privatizing municipal assets is only of secondary concern.

Change is the main issue financial actors really profit from. When municipalities increasingly cooperate with financial actors in restructuring municipal assets, any attempt to understand the process and its outcomes needs to consider the logic behind the financial actors’ advice and how it combines with the municipalities’ own thinking. The financial actors’ institutional logic is best described by summarizing it as ‘flexible financialism’. Although these actors have a rather strong set of normative assumptions that assumes, for example, private firms are more effective in managing and that the public sector is too large and lacks professionalism, they are highly flexible in their conceptual thinking. They can change their perspective and concepts according to their clients in order to stay in the game. Financial actors also argue that markets need regulation because on one hand, they believe that private firms would take advantage of their monopoly and go too far in trying to maximize their profits. On the other hand, regulation would serve their interests of bringing private companies into the market, which could only happen when a regulatory agency exists. Therefore, they regard regulation as a prerequisite to privatization.

The financial actors’ attempt to promote privatization by interacting with the media and decreasing the municipalities’ legitimacy to own or operate the water works (by criticizing their effectiveness and investment policies) did not produce any significant success. Instead, they adapted by analyzing the institutional logics and pressures residing in the water sector, identifying the most important actors (the municipalities), and using them in order to leverage their own goals. Three characteristics of financial actors enable them to stay in the game regarding the nature of change. First, they sell intangibles (knowledge about finance) and hence, are able to adapt their solutions to the clients’ problems – irrespective of what solution (privatization or some other form of restructuring) is required. Second, their service is highly flexible as financial expertise can be adapted to different sectors – making them a part of almost any organizational field today that deals with restructuring of some kind. Third, financial actors apply tactics in a comprising fashion: identifying the key actors in the game; adapting to their logics; and using coercive forces such as promoting regulation and undermining certain actor’s legitimacy to leverage own goals.

However, despite the important role financial actors play in municipal asset restructuring I do not see them as the drivers of the commercialization of water services or other local public services but instead, they are (often willfully) merely facilitators of the commercialization process. This commercialization process is caused by the entrepreneurialization of local government that is coerced into it by the market-oriented reform at the national governance level. A crucial feature of municipal entrepreneurialization is the increasing self-confidence municipalities have in their management abilities combined with their need to hold on to profitable service
operations, such as water services and commercialize them to such extent that operational and strategic decisions concerning these operations are made under significant commercial pressure in order to create substantial income for the municipal budget. This creates the situation where I see it less likely that municipalities are selling out their profitable operations and assets to the private sector but instead, aim to hold on to these operations and use them for subsidizing other, non-profitable local public services.

Therefore, I am proposing the following processual theory of local public water services commercialization:

- Local public services commercialization is the result of the entrepreneurialization of local government.
- As the state adapts a laissez-faire stance and withdraws from the local government level as financier, its subject position is open for another actor that can assist the municipalities in their finances.
- As municipalities become more entrepreneurial (due to isomorphic forces), they recognize their ability to be entrepreneurs and want to hold on to those operations which can be profitable and commercialize them.
- Because for municipalities it is primarily a question of their own commercialization rather than privatization, they turn to financial actors before turning to private companies to sell their operations and assets to them.
- Therefore, municipalities turn to financial actors who can help them commercialize their operations and the subject position that opened when the state withdrew is taken by financial actors.
- As a result, the more municipalities entrepreneurialize, the higher their level of commercialization, meaning that enterprises owned by the local government turn into publicly-owned, commercially-oriented enterprises.
- Further, the higher the municipalities’ entrepreneurialization, the less likely that they will privatize service entities that are profitable.

I see this theory as applicable to enterprises that are owned and managed as public service (especially public-owned water and wastewater works), and where it is possible in theory and practice to operate them as profitable business.
8.2.2 The Mechanism of Commercialization and its Outcomes

In the following paragraphs I am presenting a framework of the mechanism that binds the logics and interactions of three groups of actors (municipalities, state governance, and financial actors) together. The mechanism I present has the purpose to demonstrate that the commercialization process that takes place in the Finnish water sector needs to be seen as being driven by the municipal entrepreneurialization process that is created by the interactions between national governance actors, municipal actors, and financial actors. However, I will also argue that although financial actors do have an important role in municipal restructuring and reform, they are not the reason for municipalities becoming more entrepreneurial, and instead, I will identify the state actor as having that effect on municipalities. I will conclude this sub-chapter with proposing a theory that explains the outcomes of the water services commercialization process in context of local public water services reform.

Figure 8-2 The Mechanism and Outcomes of a Commercialization Process
As depicted in Figure 8-2 (opposite page), there are mainly three groups of actors involved in the commercialization process of Finnish public water supply, namely, national governance actors, financial actors, and at the center of all, the municipal actors. All three groups hold specific belief systems and pursue certain goals, giving them distinct logics. These logics contained for each actor distinct ideas, beliefs, and principles of organizing, whereas for national governance actors’ these principles were a combination of interventionalism and laissez-faire; financial actors’ logic combined flexibility and financialism; and local government actors’ beliefs combined rationalism and entrepreneurialism. As a result, I assigned to each group of actors a name according to the main characteristics of their logics where ‘laissez-faire interventionalism’ refers to the state governance actors; ‘flexible financialism’ refers to financial actors; and ‘municipal entrepreneurialism’ to municipal actors. Referring to Figure 8-2, the interactions between these actors (grey squares) take place in processes (white arrows) where their distinct logics create actions and lead to certain outcomes (white ovals), which I discuss in the following paragraphs.

As shown in Figure 8-2, the water sector itself has to deal with state level interventionalism in environmental and health affairs. In economic issues however, a laissez-faire governance style prevails. Although the Finnish water sector is liberalized and private ownership of water utilities is possible at least in theory, the lack of economic regulation created a ‘coercive vacuum’ where the common ground rules for private firms to operate the water service monopolies prevents privatization and restricts ownership of water utilities to the municipalities. However, this situation nevertheless allows financial actors to enter the scene and promote a combination of commercial interests together with the municipalities that I would describe as predominantly commercially-oriented. With the state’s lack of economic governance (and thus, laissez-faire) for water utilities while at the same time intervening and putting municipalities under financial distress and encouraging them to embrace managerialism and self-reliance, the municipalities find their own solutions through a new entrepreneurial spirit. Hence, municipal entrepreneurialism is emerging because the state encourages local government to embrace market-oriented reforms and, foremost, because the state withdraws from the scene as financier. The state’s withdrawal as financier, however, does not mean that it withdraws as an actor completely because its lack of action in terms of financing the municipalities is an action in itself that promotes entrepreneurialism in the municipalities.

When municipalities started becoming entrepreneurial and developing their own solutions to their financial problems, they started using those water utilities that are profitable in order to finance their budgets. Further, municipalities find new ways to organize water services by merging them with their local energy utilities, which creates another windfall profit for their budgets.
However, these entrepreneurial actions lead to outcomes that may be in contradiction to the state governance actors’ intentions. For example, the merging of water utilities with energy utilities is a solution that the municipal and financial markets have found to solve the financial problems of some individual municipalities – but it compromises the state governance actors’ idea that water utilities should merge with each other and become more regionalized, in order to create an overall sustainable water sector.

The municipalities’ entrepreneurialism is characterized by lack of financial resources that creates short-term thinking as municipalities look for financial income in order to solve their most pressing budgetary problems. Regarding the local public water services of larger cities, the municipalities’ prospect to receive profits from their utilities creates a lack of local government vision and decreases the municipal ability to cooperate with others because the financial benefits from the utilities are used to support the individual survival of the municipality. In cases where municipalities and water utilities have tried to form regional water utilities, it has been a struggle because of the municipalities’ emphasis on rational calculation, which has therefore been counter-productive to water sector and municipal reforms. However, municipalities have vision and practice collectivism concerning their internal affairs by shifting resources within the municipal organization to create overall balance – but it is rather difficult for them to see themselves embedded in the greater region, and to think of the ‘self’ as an individual habituating in a collective.

As a result, the structural reform for local public water services is hampered and regionalization efforts regarding water services may not go far enough or may happen too late; they may have to take a detour by first creating larger municipalities; or by merging water operations with regional municipal energy utilities. In this process, financial actors play a key role. In their efforts to restructure and create income, municipalities turn to financial actors because the municipalities themselves do not possess the necessary expertise to secure a quality decision. Hence, they are required to look for knowledge and expertise outside their formal hierarchy or authority. However, it also needs to be acknowledged that the municipalities are looking for answers to their problems that are convenient to their existing logics and thus, I consider their interactions with financial actors not a cause for entrepreneurialization but more of a symptom of it. Those financial consultants who advise municipalities on the regionalization of water utilities do not promote the entrepreneurialization of municipalities per se, but they facilitate the process indirectly by trying to justify the reform projects by using calculations – a rational and self-interest benefit-maximizing approach that conveniently fits the municipalities’ institutional logics.

The rational-individualist institutional logic of financial actors has important negative implications for water services and municipal reform by promoting the already quite individualistic attitude of municipalities. Some financial actors recognize that the individualistic thinking of them and the municipalities creates problems for reaching
agreements in networks where the power is dispersed among a set of actors – such as when a handful of municipalities negotiates about merging their water works. Hence, financial actors have been promoting in a number of municipalities the option to merge their water utilities with their energy utilities, as it only requires an agreement within a single municipality, or merging their water works with an energy company they already jointly own. Further, the options that include energy utilities are promoted by the financial actors who consult the municipalities because most financial actors are more familiar with the energy sector than with water services.

But financial actors also tried to solve the deadlocks in decision-making that some municipalities faced during their efforts to create regional water utilities. Financial actors were, for example, trying to persuade the municipalities with visionary approaches that included plans for how to use the capital that would be gained from the restructuring – but the tools to create that vision were based on convincing mainly by showing the financial benefits and proving them with calculations. Calculations and ‘facts’ are an ambiguous matter since each municipality has its own interpretations of them based on its individual circumstances. In regional strategic decisions about water services, for example, decisions require a perspective of 20 to 30 years and the involved parties deal with a process of unknown variables and uncertain consequences; each municipality has different circumstances. In such cases, trying to build a vision based on shared interests by convincing with rational, calculable facts is rather difficult. As March and Sevón (1988:432) point out, decisions are based to a significant part on gossip or ‘idle talk’, and “are often made in situations that are quite distant from the situations implicit in ideas of ‘rational choice’. Neither the decisions, the alternatives, the objectives, or causal structures are clear”. Thus, the idea shared by municipal managers and financial actors to make decisions in the spirit of an entrepreneurial organization by forwarding rationally calculated proposals to the municipal council may be ineffective because decisions are less based on calculations than these actors assume, even when municipal managers might believe that the economic situation dictates the decision-makers (municipal councils) to agree to their proposals for reform and restructuring.

In this context I would also like to point to the imitation process and its rationalizing effects on decision-making and management. Altruistic imitation or the well-intended application of private sector professionalism to decision-making by carefully calculating is one outcome of the urban entrepreneurialization that aspires to adapt professional management as it is done in the private sector. However, in these decisions egoistic imitation also becomes relevant because municipalities are applying rational, careful calculations and self-interested benefit maximization with the excuse that it is an attribute of private sector professionalism and success while it in fact serves their need for financial survival based on their inherent individualism. Calculations are important, in my opinion, but they cannot substitute for the lack of commitment to a shared vision, which is an important aspect of professional management in the private sector although not mentioned by municipal managers as worth imitating.
As the analysis has shown, calculations that support individual financial interests are an important part of the new, municipal entrepreneurial logic and they have become so important for municipal actors that visions (such as creating regional water utilities) seem to fail before their implementation. In the context of this study, the municipalities turn to financial actors for advice on improving the effectiveness of the municipal organization and on restructuring its assets. However, by doing so, they may be able to raise the effectiveness of a few individual municipalities but miss the opportunity to improve the sustainability of their larger region.

Therefore, I propose the following outcomes of commercialization for the regionalization process of local administration local public water services:

- As municipalities become more entrepreneurial and discover the commercial value of profitable service operations, their entrepreneurial spirit is combined with local government’s inherent individualism.
- As a result, municipalities behave more individualistically where profitable operations need to be regionalized, as they are required to secure the balance of the municipalities’ individual organization.
- Further, as municipalities behave more individualistically to the outside, they become more collectivistic to the inside, and increasingly shift resources within their organization in order to achieve overall balance, which also facilitates the creation of combined municipal water and energy utilities instead of creating large, regional water utilities.
- As a result, the regionalization process of local public services becomes more difficult the higher the commercial value of the units that are to be combined, which compromises their long-term sustainability in terms of putting profitability before investments and by failing to make more far reaching organizational changes.

I regard this theory as not only applicable to local public water services but also to other local public services, especially where differences in economies of scale and profitability among municipalities exist.

In the following sub-chapter I will explain how the theory and mechanism I proposed are linked to existing theories and what kinds of theoretical contributions can be drawn from it before I turn to a discussion about the implications of that commercialization process for the water sector in Finland.
8.2.3 Contributions to Existing Theories

In the following paragraphs I will link my theory of local public water services commercialization and (profitable) local public services commercialization to the theoretical framework that I introduced in chapter 2. I will present this framework again below although in a slightly altered version by filling in the theoretical gaps that I identified in chapter 2. Based on Figure 8-3 that presents the theoretical framework, I am going to discuss my contributions to existing theories of globalization and financialization, corporatization and privatization, urban entrepreneurialization, and commercialization.

**Figure 8-3 Contributions to the Overall Theoretical Framework**

Figure 8-3 shows that globalization and financialization are interlinked processes that are co-created by nations, international organizations, investors, and lenders that cause private companies, nation-states, public sector organizations, and also themselves to compete for resources, including capital and legitimacy. Liberalization and privatization are regarded by the public sector as a means to create more effective services and industries; and corporatization is seen as a way to improve the professionalism of public services enterprises. The private sector is perceived as more successful and thus becomes...
imitated by the public sector, in a global trend (at least in the western world) that lead to corporatization of state enterprises and to privatization of former public services, such as in the telecommunications and energy sectors.

Globalization means that production and finance have become flexible and global which makes the economy seem increasingly exogenous and uncontrollable (Castells, 2000; Fourcade-Gourinchas and Babb, 2002). In an economy that is perceived as uncontrollable, capitalists have been attributed to be important actors in a reciprocal process where they are dominated by their environment but they also shape it (Harvey, 1989). Globalization and financialization coerce states to reform their administrations and coerce local government to become more self-sufficient in terms of state grants by adopting a more ‘entrepreneurial’ attitude. Cities are trying to attract global resource flows of capital; symbols; and workplaces to their areas and to do what the state has asked of them by regarding themselves as entrepreneurs and trying to learn especially from the sector that is perceived as more successful, which is the private sector.

Looking at the process of how this entrepreneurialization of the public sector took place, Harvey (2005) argues in his theory of ‘uneven geographical development’ that cities and therefore urban governance is exposed to similar competition for investors and businesses as states or regions are. Therefore, cities are made in a social process of transformation that is affected by capitalism. As Castells (1989; 1996) points out, the competitiveness of a city in the global age depends on its ability to attract flows of capital, meaning symbols that are important to it; and the cities increasingly engage in attracting these flows based on their own initiative because the state is withdrawing from the local scene. With less income, local governments become more active in attracting tax revenue themselves through a combination of raising taxes and attracting new taxpayers, foremost businesses and entrepreneurs, to their area. Therefore, the city itself created its own brand of entrepreneurship that actively seeks to attract and create new industry and commercial activity by improving the local business climate (Harvey, 1989; Boddy, 1984; Rees and Lambert, 1985). In this process of urban entrepreneurialism, investors and businesses are transnational migrants that become forces in urban politics and the municipal arena (Sassen, 1998) as they are attracted by the city and participate in round-table discussions and interactions with municipal key persons that are responsive to their ideas in the hope of increasing the competitiveness of the city (Harvey, 2006).

However, I would argue that these actors not only raise the competitiveness of the city by bringing new business, but they also have another important role, which is the restructuring of the city itself. While the city is attracting these global resource flows and is approached by global or transnational private sector actors, such as investment banks or private industrial companies, it has recognized that it owns enterprises which it wants to keep. Therefore, the city may reject private companies as buyers but instead have important linkages to private sector actors which can help the city to sustain itself on its own, such as financial actors and management consultants. Here, also a financialization
of the local government and public services needs to be pointed out. I am arguing that the
capitalization of the local public sector has progressed especially in the late 1990s and
2000s following the private sector, where the capitalization has taken place already
during the 1990s. As Tainio (2003) points out, shareholder activism and the rising
significance of shareholder value forced managers to restructure their companies and put
more emphasis on the return of investment and I argue that the same applies to local
government enterprises.

As capitalism needs a strong state and a stable environment to prosper (Weber, 1947;
Farazmand, 1999), it was not surprising that financial actors were in favor of establishing
a regulatory authority for the water sector, which they see as a prerequisite for private
sector ownership. The modern state has the role of safeguarding the efficiency of the
market through protecting the system from collapse and providing safety nets for
promoting capitalist development (Lindblom, 1990; Farazmand, 1999) and the lack of
such order represents an obstacle to private sector capitalists. But as I am arguing, the
lack of state intervention in terms of economic governance also promotes the
development of public capitalists. The state has also contributed to the commercialization
of local government by withdrawing from the scene as financer and promoting the
imitation of the global phenomenon of private sector managerialism, as well as through
legislative inaction giving space to financialism that entered the local level through
financial actors.

Another issue that comes up in commercialization and globalization theories is the role of
actors and elites, and their power to change the system and promote commercialization
through privatization. Some theories (e.g. Harvey, 2005) assign significant power to
actors such as companies, organizations, and private individuals but these theories seem
rather conspiratory to me as long as not supported by primary empirical data although I
do acknowledge that scientific research has it difficult to get access to the elite circles
that would be able to clarify the picture. Harvey (ibid.; 2006) argues that the main
motivation for the financialization through opening of world markets and public sector
 reform was the top one percent income earner’s need for new income growth which could
only be achieved through opening new markets and privatizing large portions of the
public sector. Thus, Harvey explains the ‘neoliberal turn’ with the elites’ desire to restore
its class power and also asserts a key role in the collapse of economies to hedge funds,
which again, are often managed by individuals (Harvey, 2005).

Contrary to Harvey (1989; 2006) I could not find ‘capitalist’ actors to import the
globalization and financialization to the local level but instead I argue that it is the
entrepreneurial municipality that promotes these processes. ‘Capitalist’ actors mostly take
part in these processes because they are ‘invited’ by the local public sector. The local
public sector’s entrepreneurialization (which causes the commercialization of local public
services) has been indeed created by the globalization and financialization but what has
happened since then cannot be explained without acknowledging that the local public
sector is not a ‘victim’ of these processes anymore but instead is a proactive player. To keep insisting on the ‘capitalist’ actors to be the driving force behind globalization, financialization, and commercialization would release the public sector and national, (regional), and local government levels from their roles and responsibilities in these processes and for these processes. Acknowledging local government as a proactive actor in these processes is also required to understand why even in the absence of privatization, more attention needs to be directed towards the regulation and supervision of public services enterprises, because they are about to become ‘capitalist-like’ actors themselves who have learned practicing ‘public sector shareholder activism’.

My approach to the commercialization of a sector was by interviewing elite managers within the context of a country with fairly well-functioning institutional frameworks and low public sector corruption. In this very context, I could not find enough evidence that change is the result of an influential, small elite and although I cannot generalize this result to a national or global level, I suspect that the power of elites may be overestimated, at least in cases where a functioning institutional framework is in place, especially because the commercial actors’ timing, tactics, and propositions need to be suitable to the context, in order for actors to utilize them and their environment for their personal agenda. The importance of these factors leads me to conclude that an actor’s success depends more on external factors (such as the local government having specific demands for restructuring) than on the actor’s actions themselves, especially when we deal with actors that have limited resources and neither have the time nor the money to keep trying to promote change for a number of years without success.

Turning now to the literature on commercialization, it has mostly been concerned with focusing on cases where private corporations take over former publicly owned and operated services; and in the cases where the public sector has corporatized its services into a publicly owned enterprise, it is mostly reported from the perspective of increasing the professionalism of the new organization in order to become more effective and able to compete with the private sector.

As a result of the significant number of studies in these areas, there exists a rather thorough understanding of how globalization and financialization drive, on one hand, the liberalization, privatization, and corporatization process while on the other hand, they drive the urban entrepreneurialization process. The outcome of these two processes is commercialization, which is extensively researched when it comes to liberalization and privatization, while on the urban entrepreneurialization side research on this issue hardly exists. In this context, I would like to especially point to the research on the performance of privatized water utilities. The only study I could find that investigates the changing role of the municipalities in fact argued that the corporatization of water utilities compromised the sustainability of water services and local society because ‘the engineers’ were allowed to be more independent from the local government than previously (see Smith, 2004). I could not find any study that pursues the question of what
happens to local public water services when municipalities entrepreneurialize. Most studies about the privatization of local public water services conclude that they are being commercialized as a result of the takeover, which idealizes the former public owner as less commercially interested than private corporations and more focused on non-commercial or civic interests.

I have taken a bottom-up approach and started at the local government level and identified the relevant actors for the commercialization, with the result that the interplay of municipalities and financial actors is more relevant in the Finnish context than any other combination of actors. Therefore, I am turning the attention from the global to the national and especially local level and to an area of water services commercialization that is usually overlooked by researchers, which is the role of the local government as driver behind commercialization. On the local level, I observed that private sector actors and financial actors have tried to change their environment according to their own agenda but with very limited success, as the nature of their business, timing, and tactics are crucial and could not persuade the municipalities to privatize their utilities as long as they still can explore other options in order to release capital.

My study of changes in local public water supply in the absence of privatization represents so far a mostly overlooked linkage between urban entrepreneurialism and commercialization, where I argue that the former is causing the latter without significant involvement of the private sector. Municipalities and financial actors together find new forms to organize water services driven by desire to maintain control over the organization in order to control and receive residual earnings and other financial benefits such as those created by restructuring the water utilities. I see the municipalities as the main actors in commercialization, together with financial actors, although they do not cause the commercialization per se but rather facilitate it. Municipalities embrace commercial principles and have increasing confidence in owning and managing profitable services. Profitability has become more important to municipalities in order to balance overall budget than securing the long-term viability of water services, as can be noticed by their lack of investments and regional strategies. Municipalities have developed ownership policies based on commercial aspects and they are willing to exercise them even by reducing independence that was once given to corporatized water utilities. Therefore, the water utilities’ notion that their independence increases when they become corporatized may also be a misinterpretation of municipal restructuring, management, and ownership policies.

As Harvey (1989:1) has pointed out, ‘urban governance has become increasingly preoccupied with the exploration of new ways in which to foster and encourage local development and employment growth. Urban entrepreneurialism refers to a supply-side oriented strategy that prioritizes business investment, cost competition, and fiscal conservatism through centralizing financial controls, benchmarking departments to private sector and other ‘competitors’. Demand-side strategies that aim at improving
competitiveness through investments in education, training, and social infrastructure are under-emphasized (Kipfer and Keil, 2002). ‘Public servants have their roles transformed to managers and the public to customers’ (Van Gramberg and Teicher, 2000: 476) and ‘such an entrepreneurial stance contrasts with the managerial practices of earlier decades which primarily focused on the local provision of services, facilities and benefits to urban populations’ (Harvey, 1989:1).

I agree with Harvey in terms of the local governments’ preoccupation with entrepreneurialism but I would like to emphasize that in the era before, in which municipalities focused on the provision of local services and benefits to their citizens, they took care of their affairs probably just as individualistically as today. Harvey’s contrasting of old and new municipal management does not say much about cooperation among municipalities, although his statement that in the pre-entrepreneurial era, local government was focusing ‘primarily on local provision of services’ implies, in my opinion, that their affairs were managed more autonomously from each other than they do today, especially when the state government is coercing them to do so. Also from my own data analysis, I can conclude that municipal managers are stressing that intra-municipal cooperation and regionalization are one of their major concerns, whereas in the past, they were not required to cooperate significantly and did not cooperate as extensively as today.

Also, economic flows of labor and consumption today coincide less with the municipal administrative boundaries than they did before (see e.g. Harvey, 1989). The state coerces municipalities to be more entrepreneurial in terms of self-sufficiency from state funding and also to compete with each other for example by benchmarking service tariffs and tax levels. However, the state’s idea is to achieve increased municipal independence from state funding via municipal cooperation. Because of these reasons, I argue that the states’ pressure for regional cooperation and market oriented reform that increased over the past ten years requires municipalities to cooperate to an unprecedented extent and as a result, it made the inherent individualism of local government more visible – but it did not create it.

Before I explain why municipal entrepreneurialism is the way it is and what outcomes it creates, I would like to make a remark on Osborne and Gaebler’s (1992) influential book that advertised a more entrepreneurial management of public sector activities. Their work relates to theories of urban entrepreneurialization as it argues that the effectiveness of the public sector could be improved by changing the institutional beliefs of municipal managers by adopting ‘entrepreneurial attitudes’ – with serious implications as I will argue.
Osborne and Gaebler (1992) write in their influential book *Reinventing government – How the entrepreneurial spirit is transforming the public sector* that the US public sector on all levels is moving towards competition; measurement; outcome, market, and customer orientedness; empowerment of its units and employees; and using the private sector for public service delivery. Here, the entrepreneur is understood as someone who ‘uses resources in new ways to maximize productivity and effectiveness’ (Osborne and Gaebler, 1992: xix) and the entrepreneurial organization is habitually trying to maximize the effectiveness of its resources. Osborne and Gaebler (ibid.) argue that many of the private sector principles and management techniques are transferable to the public sector and would enhance its effectiveness. However, I would like to point out that a distinction between mimicking private sector management for operational- and for strategic management of public sector organizations is required. Osborne and Gaebler refer mostly to private sector management practices that are applied to the operational level, which indeed may enhance the performance of public sector organizations.

However, I would like to question whether the public sector has learned the right things from the private sector in terms of strategic management. I found that strategic decisions that involve complexity in terms of the number of involved parties, time frames, and uncertainty of outcomes, that the municipal entrepreneurialism is counter-productive to decision-making and local public services reform. Municipal managers pride themselves with using ‘rational management’ that is combined with the municipalities’ inherent individualism and the financialism and rationalistic calculatory advice from financial actors. This combination of public-private management thinking is in fact counter-productive to the local public services and administrative reform process and hence, it is diminishes its effectiveness instead of enhancing it. Therefore, I see Osborne and Gaebler’s notions about the positive aspects of entrepreneurialism for the public sector confined to *operational* management and decision-making.
8.3 Implications of Commercialization for the Finnish Water Sector

In the following subchapter I discuss the major implications for Finnish water utilities that result from the municipal entrepreneurialization process and the commercialization of water services. Subsequently, I propose three different scenarios for structural change in the Finnish water sector that especially refer to the regionalization of water services. I would like to point out these three scenarios are developed on the basis of the dominant logics of an elite of persons involved in managing the water sector and therefore I do not consider these scenarios to represent the entire spectrum of options that would be available to policy makers and I will deal with the shortcomings of the elite’s dominant logics in a separate paragraph about ‘recommendations for practice’ at the end of this study.

8.3.1 Implications for the Water Sector

In order to assess the implications of the municipalities’ entrepreneurialization and the commercialization of water services that it causes, I would like to explain three major implications for the sustainability of water supply in Finland more detailed as depicted in Figure 8-4. First, pressure is going to increase on the profitability of water utilities in those cases where profit is feasible (which refers mostly to larger water utilities). Second, the autonomy of water utilities in terms of strategic and operational decision-making is likely to decrease because they become even more important for the municipal economy. These two implications are interlinked, and they affect the third implication, which refers to structural changes in the water sector. Specifically, these structural changes are going to be motivated mainly by financial concerns which does not prohibit regionalization per se, but makes it less likely to happen by creating large, independent, regional water utilities as the water utility managers I interviewed would like it to take place.

Referring to Figure 8-4, the first implication of municipal entrepreneurialization and the commercialization of water services is, that pressures on water utilities to maintain or increase their profitability can be expected to increase because municipalities need these
profits to help balancing their budgets. The entrepreneurialization of municipalities contributes to this development because their financial shortage is combined with business thinking and the confidence of being able to professionally operate and govern local public services as commercial and profitable enterprises.

Second, it can be expected that the strategic and operational independence of water utilities is going to decrease. Water utilities become strategically more important because their significance as providers of income to the municipal budget increases which affects the investment policies that are decided by the municipal owners. Because the municipality requires more profits from the water utilities it has an incentive to put profitability before making the necessary investments in water services that would secure the long-term viability of the service. The operational autonomy of water utilities is also affected because the municipal owner directs the utility to buy services from the municipal organization in order to use the resources of other municipal departments more effectively.

These two processes of increasing financial pressures and decreasing autonomy have important implications on the structural development of the water sector. They mean that structural changes are mainly motivated by financial considerations instead of improving the sustainability of water services per se. The entire municipal sector, including its local government and administrative structures and boundaries and the local public services are undergoing a reform process with the aim of finding new ways of organizing local government and public services and raising effectiveness. This affects also the structural change of local public water supply, which I will explain in more detail below by contrasting the water utility managers’ plan or scenario with two alternative scenarios of structural change that are derived from the implications that the urban entrepreneurialism and commercialization have for water services.

The water utility managers (and even municipal technical managers and state governance actors) that I interviewed for this study basically all agreed that the regionalization of the local public water supply is required to increase the sustainability of water services. Especially among the water utility managers, the view was widely shared that it is in every utility’s best interest to increase the size of its organization by merging with surrounding water works. This is seen as a viable option for smaller water works as well as for larger water utilities in order to gain economies of scale, to increase professionalism of human resources, and to optimize investment planning. Thus, the grand, long-term strategy for the water sector is more or less agreed upon by these water sector managers and only differs in the degree to which the water sector should concentrate (whether there should be ten water utilities left or one hundred). Based on the interview data, it is my impression that if it would be only the water utilities’ decision, the concentration process would have progressed significantly further, as there is rather much agreement among water professionals on what to do.
However, these decisions are made by the local political level because the water works are owned by the municipalities and they make the strategic decisions while the water utility keeps to operational decisions. In that setup, the utility may propose to the owner to merge together with other water works, but the final agreement is up to the municipal managers who negotiate the deal and prepare a concept the municipal council will vote on. Therefore, the plan of the water managers I interviewed to create regional, rather independent, water utilities may be ineffective as long as they cannot convince the political decision-making level and as long as their owners apply a different, and more individualistic and financial logic to such regionalization projects and municipal restructuring in general.

To follow this plan of creating large, regional water utilities that are fairly independent from the municipal level although being owned by the municipalities they serve is difficult to execute. There is only one case so far where this kind of regionalization took place, which is the case of Hämeenlinna City and its surrounding municipalities that merged together in 2001. Similar regionalization projects were initiated in several other regions but with little success because the negotiations and decisions take place on the local government level. Municipalities are inherently individualistic actors and are struggling for resources; they lack a common goal that would be required for an agreement among them. I also see their lacking ability to make compromises as an obstacle to reaching agreements within networks where the power is dispersed among actors (such as in projects where local public services are regionalized and several municipalities need to agree). Some project partners need to give in more than others and may contribute their resources without benefiting from the regionalization immediately. This is for example the case when water works with scale advantages merge with rural areas that have poor infrastructure. In the long run it should be possible for all parties to gain, but that does not help municipalities in solving their financial problems they have at present.
8.3.2 Scenarios for Structural Change and Regionalization

The following scenarios that I will propose should not be seen as a sophisticated conceptualization of water *scenarios* as it has been done for example under Finger’s leadership in the Euromarket Project for the European Commission from 2003-2005 that developed different scenarios for the water and sanitation sector in Europe (Finger et al. 2007). Instead, I merely aim to explain the implications of the commercialization of local public water services by combining the logics of actors with their various efforts to create structural changes in the sector. Based on emerging trends, I propose three different scenarios for the processual structural change in the Finnish water sector.

All three scenarios (Table 8-1) that I propose deal with regionalization and thus, concentration of resources and comprise: 1) a water sector driven regionalization process with the outcome of a highly regionalized (concentrated water sector) with relatively independent public-owned water utilities; 2) municipality and financial actor driven process based on merging water and energy utilities together where the outcome is a low to medium regionalized water sector with public-private water works that highly depend on the energy company’s owners; and 3) a municipality-driven regionalization process based on merging entire municipalities together where the outcome is medium regionalization and public-owned water works highly depending on municipal owners.

### Table 8-1 Three Scenarios of Structural Change Processes in WSS

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Main Actors</th>
<th>Initiative in Process</th>
<th>Main Issues</th>
<th>Degree of Regionalization</th>
</tr>
</thead>
<tbody>
<tr>
<td>1) Regional Water and Wastewater Utilities (utility result of a merger of several separate municipalities’ water works)</td>
<td>Water Actors and Municipal Actors</td>
<td>Based on the Water Actors’ Initiative</td>
<td>Improving WSS sustainability and maintaining water sector’s professional autonomy</td>
<td>High (reducing the number of water works down to 10-100)</td>
</tr>
<tr>
<td>2) Water and Energy Multi-Utilities (intra-municipal merger of W&amp;E or merger of units belonging to several separate municipalities)</td>
<td>Municipal Actors, Financial Actors, and (Municipal) Energy Actors</td>
<td>Municipalities, Financial Actors, Energy Actors (recently)</td>
<td>Financial motives main issues; water attractive business; sustainability of water services</td>
<td>Low to Medium (no state-wide regionalization but only in some areas of Finland)</td>
</tr>
<tr>
<td>3) Municipal Water and Wastewater Utilities (owned by one large, ‘regionalized’ municipality that has been the result of a merger between several separate municipalities)</td>
<td>Municipal Actors</td>
<td>Municipal Actors</td>
<td>Regional water utility a side product of extensive municipal reform and restructuring</td>
<td>Low to Medium (depends on the degree to which municipalities merge together)</td>
</tr>
</tbody>
</table>

Scenarios 2 and 3 are especially interesting from this study’s point of view because they contrast the dominant logic of the water actor elite and their plans (represented by scenario 1 with a trend that I clearly see as the result of municipal entrepreneurialism and commercialization, since the motives for creating water and energy multi-utilities are
mainly of financial nature and the financial actors, which so far have not received much attention in literature, play a key role in that process. The trend of merging water with energy that is based on the municipalities’ and financial actor’s initiative has only started in 2002 and 2003 but since then has had more concrete outcomes than the process of creating regional water utilities that is mainly based on the water actor’s initiative and that had been started in several regions in 1999 and 2000.

The first scenario, as depicted in Table 8-1 (previous page), is the option that water actors see as the most appropriate action to safeguard the water sector’s sustainability. The water managers I interviewed proposed that basically all water works in Finland should be merged to the extent that approximately 100 to even as few as 10 large, regional water utilities would remain and take care of water and wastewater operations in Finland. These water utilities should be municipality-owned enterprises with relatively large autonomy in terms of decision-making that would allow the water utilities to take care of water services based on its professional knowledge. This option also represents the water managers’ intention to stay independent from other sectors and become even more independent from their municipal owners. The most important issue for water sector managers, however, was the concern for the long-term viability of water services and their answer to this concern is this particular form of creating regional, fairly independent water utilities that would increase the utilities’ ability to deal with their challenges, including the lack of financial and managerial autonomy; the human resources; and the economies of scale.

The second scenario (see Table 8-1 on previous page) concerns the emergence of water and energy multi-utilities. Because creating regional water utilities is a slow process and has so far only succeeded in less than a handful of areas, another trend is emerging where municipalities try to merge water utilities with energy utilities. In these cases, the progress seemed to have gained momentum since the past three years and already outpaced the number of regionalized water utilities. Such a merger has taken place for example in the City of Jyväskylä in 2004, allowing the owner to re-evaluate the asset value of the water utility by changing its assets valuation from historic to present costs, which usually leads to a threefold to fourfold increase in asset value (according to my interviews, the asset value of the water utility in this case increased from approximately EUR 40 million to EUR 160 million).

Besides this financial incentive, it is easier for municipalities to agree within their own organization to these changes because they do not involve other municipalities. However, there are also other cases where municipal energy utilities have been trying to acquire municipal water operations of several municipalities, which are facilitated by the fact that municipalities can regionalize their water operations based on the already existing regional structure of their energy operations. One crucial element in this scenario is the role of financial actors, which favor this scenario because the energy sector is more familiar to them from their previous work than the water sector, and because they regard
this option as less difficult than regionalizing water services based as independent utilities.

Last, as depicted in Table 8-1 (page 197) the third scenario for structural reform is to regionalize water utilities as a result of merging municipal administrations and local governments. This process has been extensively promoted by the state governance level and several regions have been working on it but only a handful of mergers have yet succeeded. Therefore, this process has been rather slow and troublesome for municipalities in the past but it is progressing nevertheless and it represents an option for creating larger units of local public water utilities. In these cases, also the separate municipal budgets merge and therefore the question of how to maximize the individual financial benefits and risks that would arise from establishing a joint regional water utility becomes obsolete. This regionalization process is mainly a process of far reaching municipal reform where local governments are merged and synergies in administration, governance, and local public services are investigated. Therefore, the regionalization of water services is in such a case merely a byproduct of the municipal reform and restructuring process.

Particularly reflecting on scenario 2 and 3, I would like to point out that regionalization of water services would take place in both cases but by taking a detour via merging with energy utilities or via merging first entire municipalities and then their water operations. In both of these cases, the size of the water services operations increases and thus it is in my opinion a right step towards achieving larger unit size – but that structural change may not go far enough. At the end of that process there may be a significant number of local public water services left whose size is still insufficient to master the challenges. In these two last scenarios, local public water supply becomes an instrument that is used by municipal and financial actors to achieve their primary goals (which are financial) rather than to focus on solving the challenges of local public water supply as such.

Especially the emerging trend of combining local public water utilities with municipal energy companies may represent a privatization of water services through the backdoor. Some municipalities’ energy companies do have private shareholders already and there is also a possibility that municipalities may sell their energy utilities during a financial crisis, which would then have the effect that the water services operations as part of the energy company change owners as well, as it happened for example in Norrköping, Sweden (Gustaffson, 2001). However, disregarding whether there is private ownership of water utilities or purely municipal ownership, in all three scenarios the water utilities will be increasingly exposed to a commercially-oriented owner. Thus, water utilities may require protection from a regulatory agency that would have to be established for example to ensure that the sustainability of water utilities and their infrastructure is not compromised by the owner’s demands for profitability.
9 Concluding Remarks

In the following chapter I provide a conclusion of my thesis and some recommendations for practice and policy-making. Further, I will reflect on the limitations of my study and use these limitations as starting points for future research.

9.1 Conclusion

During the past ten years, the state increasingly withdrew as a financier from the local government scene and pressured municipalities towards market-oriented reform by encouraging them to adopt practices that are perceived as successful in the private sector and to intensify the cooperation among municipalities in administration and local public services. The state is granting to the municipal level significant freedom in how to implement these reforms and thus it allows municipalities to find their own solutions to their problems. Under this combination of financial pressure and freedom to find new ways of organizing, municipalities have become more entrepreneurial and started embracing their active role in attracting national and global resource flows to their local areas. With increasing professionalism and by learning from the private sector, municipalities have gained self-confidence in being business owners and ‘entrepreneurs’.

Based on the municipalities’ new entrepreneurial confidence, they are developing new ideas to create income by using the help of financial actors rather than continuing the privatization trend that took place during the 1990s. Here, the financial actors fill the space that was created through the state’s withdrawal as financier. Today, they assist municipalities in their asset restructuring by providing solutions that conveniently fit the logic of municipal reform that resides in municipalities. The financial actors provide advice based on their own financially-oriented mindset but it is the municipalities that are more powerful and determine what happens. This is demonstrated by the financial actors’ efforts to adapt their strategies to the municipalities’ needs in order to stay in business with them. Municipalities and financial actors together are restructuring the local level in the search for financial resources, which affects the public water utilities.

Because the Finnish water utilities are owned by the municipalities, they are in the middle of this advent of entrepreneurial activities and find themselves exposed to the consequences. These consequences mainly relate to the increasing commercialization of water services and to the hampered regionalization of water utilities. Especially water utilities in larger cities are regarded by their municipal owners as an important source of income that can be used to subsidize other local public services and thus, they try to maximize the profits and tend to neglect investments. Utilities of smaller municipalities may not be the target of profit-maximization as such, but they suffer from the consequences of municipal entrepreneurialism because they require more cooperative arrangements among municipal water works such as being merged into larger utilities,
but it is difficult for municipalities to agree on how investments, costs, and profits are distributed among them in such regionalization projects. It is also difficult for municipalities to agree on regionalization because, foremost, these local reforms require cooperation. However, the municipalities do not, as hoped by the state, focus on cooperation but instead, approach cooperation and regionalization individualistically and with too much deliberation and rationality.

Municipalities become more innovative in their solutions to their financial problems and apply private sector management techniques to increase their effectiveness, but to a large degree do not succeed because what they mimic is only an imitation of private sector practices and success recipes. As a result of an imitation process, private sector management techniques are only a rationalized version of what was being imitated, for example, demonstrated by the municipalities’ belief in ‘rational’ entrepreneurship. On the other hand, they use private sector managerial philosophy as a convenient excuse to justify their inherent logic, especially their individualistic thinking and lack of cooperative spirit. Hence, one of the reasons for entrepreneurialism being so embraced by municipal managers is the fact that it combines well with the inherent individualistic logic of local government that was already in practice before the market-oriented reform process started.

On the water utility level as well as the state governance level, the need for cooperation and regionalization is well understood and intended to proceed in order to solve the sector’s problems. But as only operational decisions are made at the water sector level, while strategic ones are made by municipal owners, regionalization is a political game. In the absence of effective state governance for the sector, the responsibility for the progress of water-sector and municipal reforms lies with the municipalities themselves. However, the municipalities’ individualistic logic combined with its new entrepreneurial spirit, and the financial actors’ financial and rationalistic advice gives rise to the financialization and commercialization of local government and local public services. This logic is a combination of the belief in rationality, extensive calculations, financialism, benefit-maximization, and being ‘professional’ as the private sector. This set of ideas and beliefs is counter-productive to the sustainability of water services because it over-emphasizes their profitability and neglects investments. Further, it is counter-productive to regionalization because it is used to justify the inherent individualism in municipalities.

I argue that this new municipal entrepreneurialism is counter-productive to the local public sector reform process and that it is the cause of the commercialization of the Finnish water sector. The local government cannot be expected to effectively operate its water services when municipalities become commercially-driven actors because of a conflict of interests as operator and regulator of the local water services monopoly. It is my conclusion that this form of municipal entrepreneurialism gives rise to a new organizational archetype, which I describe as public-owned, highly commercially-oriented, local monopoly enterprise in the water sector that is at the moment unregulated.
Water utilities are either regarded by their municipalities as a valuable financial asset that delivers continuous income to the municipal budget which can be restructured to release capital that is used to balance the cities’ budgets; or they are perceived as liability in cases where water works suffer from underinvestment and low economies of scale, which can also be interpreted as sign that water services are foremost a business and only second they are a public service.

Private sector actors, such as multinational water companies that are usually regarded as drivers in promoting the privatization and commercialization of water services, play only a minor role in this case. The same holds true for private sector industrial companies. However, financial actors, such as investment banks and financial consultants are important actors in this change process because they provide expertise to the municipalities. Because of the intangible and flexible nature of their services, financial actors can be part of any sector at almost any time, providing that there is reasonably foreseeable structural change. They can adapt to almost any circumstance by changing their solutions according to the client’s needs, and they are not required to execute their inherently free-market agenda in order to stay in business. However, in the Finnish case, their power to change structures and institutions was rather limited and it depended on whether key actors, municipalities in this case, are willing and listening to their advice and making use of it.

Therefore, contradicting the common perception that the public sector is a ‘victim’ in commercializing the water services and public realm in general, I found that the municipalities themselves played the main role in promoting the commercialization of the water services sector, although driven by the state to entrepreneurialize in the first place. If it was the state’s intention to promote local public service reform and regionalization by cutting resources and encouraging entrepreneurial thinking in the municipalities, I am questioning the success of these plans and instead, based on the evidence in my study, I argue that this entrepreneurialization has counter-productive effects on the reform of local public services and water services.

Public sector reform occurs throughout the world in slightly different and context-specific forms. However, clusters of similar development occur because of cultural, geographic, economic, and institutional characteristics; as a result, my findings surrounding commercialization of the Finnish local public water supply may also help to better understand the development of water services, at least in other European Union member states. I suggest that citizens, pro-democracy and anti-globalization activists, scientists, and politicians recognize and acknowledge that the public sector actors carry major responsibility for the commercialization of water services and the commercialization of the public realm in general – rather than assigning the major responsibility to the private sector.
9.2 Recommendations for Practice and Policy-Making

I propose that the present municipal and local government logic is unfit for executing the local reform process when it concerns the regionalization of local public water services. For the water sector, regionalization has been especially troublesome, as some municipalities derive profits from their utilities or have systems that are in rather good shape, which makes them especially reluctant to merge with other less profitable and less developed water works. However, the regionalization in water supply and sanitation will be necessary in order to secure the interests of the collective society. The state is, in my opinion, the only actor that has the potential to act collectively in this reform process. If policy makers decide that regionalization is the key to a sustainable water sector, the state may have to intervene and implement a large scale reform of the water sector.

The commercialization of municipalities and local government calls for establishing a regulatory agency that will supervise the economic practices of water utilities. The common assumption that commercial interests in the water sector can be restrained through confining the sector to quasi non-profit policy and public ownership bears significant risk because the local government and municipalities are commercializing themselves. The rise of the public-owned commercial enterprise in the case of water services represents a ‘capitalistic-thinking’ monopoly operator, which leaves citizens vulnerable to service and investment levels that threaten the sustainability of water services. This finding implies that the water supply and sanitation sector would be well advised to lobby for a regulatory agency that supervises the economic practices of the public owner. I am proposing a regulatory agency because I do not consider the local democratic system strong enough to supervise a municipally owned but capitalistic company. The common practice that municipalities are sacrificing investments for the sake of profits demonstrates they are compromising their water operations in the long term and the local democratic system is unable to regulate its own water utility. The state should recognize this need for regulation disregarding whether it may facilitate private companies to enter the water sector or not. Regulation is needed in any case, whether there is private ownership of water utilities, or whether the sector is fully public-owned.

I would like to emphasize that municipal entrepreneurialism also has rather positive characteristics as it strives to increase its effectiveness and develop. However, I argue for more caution regarding the choice of role models for the public sector and for awareness that the imitation of managerial success recipes contains risks, as it promotes managerial myths. Municipalities need to be aware that the current rational and financial entrepreneurialism is counterproductive, especially when being applied to complex decisions that require long-term vision and the ability to take other parties, especially municipalities, on board as well. I therefore suggest that local governments engage in visionary thinking that is based on values rather than on numbers, and that identifies a common, shared interest with its municipal partners. Besides these shortcomings in the ‘entrepreneurial turn’ of municipalities, I also believe that the municipalities’ commitment to own and operate local services is a reasonable decision, as long as they
can do it effectively. Once the cost structure of municipalities changes due to the large scale retirement and a more entrepreneurial and flexible culture has been created, the municipal organization may be as effective in delivering services as private ones. In addition, local government should maintain a key role in local public services and water services to be less vulnerable to the lack of competition that exists in a number of private sectors that cater their services to the public sector.

9.3 Limitations to the Study

This study did not include structural change by increasing inter-municipal cooperation regarding the provision of water services. These cooperation agreements may have provisions that smaller water works especially are contracting out administrative and operational work to larger water utilities or forming regional service organizations that take care of operations and maintenance. Ryynänen (2005) provided a comprehensive list of approximately 160 water works that are part of some form of inter-municipal cooperation in water services, including regionalized utilities, organizations for water intake and treatment, for wastewater treatment, and for planning and construction. These cooperation agreements are important for improving the viability of water services in Finland and they are growing in number but they were not emphasized by the elite that I interviewed as being sufficient for solving the challenges ahead of the Finnish water sector.

It may be argued that this thesis concentrates too much on solving the challenges for the water sector by regionalizing it and creating larger units. Some researchers in the field have suggested that the answer to the problems in rural water supply do not lie in regionalization but in improving ties with the local community. This suggestion needs to be recognized as it also refers to an urgently needed change from modern to postmodern thinking, where the answers to structural problems are not automatically sought in the increase of economies of scale and ‘making it better by making it bigger’. Creating larger water utilities without reflecting on its effects on local civic lives and the involvement in decision-making of service provision may have negative consequences for the dynamics in rural areas. Decentralization may in fact be a viable solution, for example, for areas that require water supply and sanitation but are so remote that it is uneconomic to connect them to the network. I tried not to automatically assume that the only answer to the water sector’s problems lies in increasing its economies of scale but instead, that the regionalization process of water utilities emerged as one of the most important issues and challenges for the water sector. The fact that the sector requires a significant increase in regionalization and cooperation cannot be disputed – but it is subject to discussion whether there should only be ten water utilities left standing, or one hundred.
During the final stage of the study, some new developments in the sector could be observed, as one municipality had contracted out its technical services (including water services) to a private-sector services management company. Another municipality was in the process of concluding a similar agreement at the end of 2006. One suspects that a few years into the future there will be a significant amount of such outsourcing contracts as especially smaller municipalities struggle with keeping up service quality, for example for water and technical services. Even though these developments were not included in this study, however, they only support the findings of the present research because once again, the individual contracting out of water services to private services management companies is according to the municipal entrepreneurial logic that seeks individualistic solutions rather than regional ones.

Regarding methods, one of the limitations of these studies is that the qualitative longitudinal data derived from interviewees was conducted recently (between 2003 and 2005) and hence, their memories about ‘the past’ do not provide as reliable information as if interviews would have been conducted at the beginning of the period (1995) and at the end (2005). However, this bias was triangulated by investigating the longitudinal development of managerial themes in different sector-related journals.

One limitation may have been that the study was conducted by a foreigner with only limited language skills in the local language and therefore, much of the discourse about water services and municipal reform (the latter is discussed in almost any media arena on weekly basis) could be missed. Also, interviewing in the English language and not in the interviewees’ native language may have distorted some of the information retrieved. However, being an outsider to the field can also be seen as an advantage. Much of the taken-for-grantedness did not exist in this case, which meant that I did not have a discourse of my own about municipal reform or water services management, as I was also new to the field of local public services and water services. When it came to the interviews that were conducted in English, it could have also been an advantage to be perceived by the interviewees as an outsider, as they might have felt freer to explain their ideas, rather than talking to somebody who already had ‘a reputation’ or knew about the main issues. Further, my wife, a professional interpreter and translator for the Finnish and English languages, has helped me with many of the texts and statistics by translating them for me and proofreading my own translations.

In addition, although information about municipal and water sector restructuring projects was collected from interviewees – the Association of Finnish Local Authorities, and the Finnish Water and Waste Water Works Association – it is likely that not all projects there were captured. However, as those projects which are successfully concluded receive significant publicity and certainly come to the attention of the sources that were used to screen the sector for projects, it is unlikely that any successful projects were missed. (This could have contradicted the finding that regionalization and water sector reform is difficult.)
Last, a limitation is the sheer diversity of scientific disciplines that meet in such a research project. This study was located at the linkage of organization studies, administrative science, water services management, urban geography, regional studies, and political science. Due to the workload such interdisciplinary research creates, a team of researchers from different fields would actually be required to achieve higher theoretical sophistication of this study and to combine more of the work that has already been produced in each field about this subject. In fact, the field of organization and management sciences is the discipline with the least experience in dealing with questions of commercialization and new roles of public and private sector. This study is hopefully the beginning of more research about the linkages between public and private sector that originate in the management and organization studies.

### 9.4 Suggestions for Future Research

The first suggestion for future research that comes into my mind concerns the research area of water privatization. While research and knowledge about the privatization of public water services and corporate practices is continuously growing, the management of public water supply in absence of privatization or outsourcing does not receive sufficient attention. It is almost as if researchers in that area believe that as long as water services are publicly owned and managed, there are no reasons for concern and no need to study their governance and management practices. These researchers neglect to consider that the majority of European water supply is publicly owned, managed, and operated and that the entrepreneurialization at the local level, and probably also on the national levels is continuing, and they become more commercially driven. Hence, one needs to investigate how that affects the sustainability of water supply.

Second, I have proposed a substantive theory of local public water service commercialization and attempted to formulate also a formal theory that is more widely applicable, especially where local public services and local government are to be regionalized. The substantive theory should now be tested or applied to other countries, and in order to build a more solid and empirically proven formal theory, it would be a start to test it in the Finnish municipal sector and also in other countries with comparable local and state government authority systems that are going through a reform process.

Third, I propose that researchers study the ideas and beliefs of managers and decision-makers regarding the modernist ‘bigger-better’ thinking, the consequences of it, and the alternatives to it. I presume that there is need for a more reflective thinking that is based on a post-modern notion that considers the context and individual characteristics before proposing a solution. Researchers should bring alternatives to the ‘bigger-better’ logic to the attention of citizens, policy makers, managers, and fellow scientists where ‘smarter’ does not automatically mean ‘putting more technology into a device’ or making it ‘better’ does not necessarily mean having to make it ‘bigger’. I think there is need for a large scale reform of public water supply in Finland that increases the size of utilities but
within these new regional utilities there would have to be solutions for areas that are better served by adopting small and local solutions for water supply and sanitation.

Connected to this proposition is my suggestion to initiate research about the Finnish water sector that investigates whether state reform of the water sector is needed and if it is, what kinds of new ways to organize local water supply are required. This means to pay attention to concentration or regionalization in densely populated areas and whether decentralization could be a solution for sparsely populated areas. Personally, I think there could be linkages between water and energy especially in sparsely populated areas in the future because renewable energy production also means decentralized and more local production. These units could also be ‘hubs’ for expert services to local households that have decentralized solutions for their water and sanitation systems. Combining centralization and decentralization by finding new ways to organize may be the most appropriate way to provide any kind of service, whether water, energy, or other municipal services and one should also remain open about how these different services could be combined into one organization, for example in the case of water and energy.
References


Toronto: Earthscan Canada.


Appendix

A. Analysis of Kauppalehti Newspaper from 1995-2006

This content analysis was the background for Figure 4-7 and it separated the period under investigation into three distinct phases as shown below.

i. 1995 – 1998 Commercial Interest in Development Assistance

First, WSS is covered by reporting on Finnish development aid provided to countries such as Kenya or Vietnam. In addition, the role of the EU in financing WSS infrastructure in Eastern European countries is reported. In both cases, the angle on the issue is one of commercial interest. Domestic, Finnish companies are awarded contracts for constructing infrastructure in the target countries and provide consulting services. Therefore, development assistance given to foreign countries is also beneficial to domestic enterprises. One case that has received special attention is the improvement of conditions for wastewater operations in St. Petersburg because of negative effects to the Baltic Sea, which extends well beyond the coastal area of Helsinki.

In addition to these issues, Finland’s domestic water sector is only covered by reports illustrating problems with WSS in rural, sparsely populated areas, which have been granted funds from the European Union as well. Therefore, the time period from 1995 to 1998 can be generally characterized as the period of “Water Supply and Sanitation (WSS) Development Assistance”.

ii. 1999 – 2002 Privatization Interests

Articles about assisting foreign countries (either through development aid or in a sense that Finnish companies receive construction and management contracts), ends with the years 1999 and 2000. The years 1999 and 2000 represent a new period where Kauppalehti starts to cover both, assistance-related topics and restructuring and renewal related ones. From 1999 onwards interest in the privatization of Finnish water utilities starts.

While during the assistance period, the focus was on smaller, rural areas and their need for support from the state and the EU, the attention turned now to the Finnish WSS as a whole. The article that starts this trend is a piece on the critical condition of Finnish water networks and the problem of how to finance their rehabilitation considering the tight budgets of municipalities. As the article concludes, the current progress in network rehabilitation is insufficient and a three to five-fold increase in rehabilitation activity is required to satisfy only the most urgent rehabilitation needs of only 15 percent of the water network in the coming decade.

One possible solution to the increased need of capital in the WSS comes from the private sector, the private investment bank Icecapital entering the discussion. The managing
director, Ari Lahti, is quoted in an article that in his opinion, the water sector will follow privatization in a similar manner as it took place in the Finnish electricity sector between 1994 and 1997.

Kauppalehti follows this article by publishing two articles by a professor of water and environmental engineering, Heikki Kiuru, who criticizes the investment bank and points out that water is, contrary to the business of electricity, a natural monopoly and unsuitable for pure commercial interests. In regards to the need for capital for WSS to be able to rehabilitate the network, the professor points out that in a number of municipalities, the required capital for the investments would be available if the municipal owner would allow it to be used. But because the municipality is using too much of the profits to subsidize other municipal services, there is no sufficient capital savings or investment plans on behalf of the water utility.

In 2001, an extensive portrait of Ari Lahti, Managing Director of Icecapital includes his potential business for the energy sector and the water sector, arguing that the water sector will also require private capital and privatization. At the end of 2001, an article reports on RWE, a German multi-utility company that has previously mainly been associated with the energy business. As reported, RWE’s water activities account for 4 percent of its turnover but constitute 23 percent of operational profits. Readers of Kauppalehti can now see that water is a profitable business, which is becoming a global business and millions of inhabitants, especially in France, Great Britain, the US, and soon Germany will be served by private operators. The benefit for the consumer is argued to be between 10 to 15 percent lower water tariffs. In all these articles, the privatization of water services is a dominating theme and it is argued that water utilities will follow energy utilities in terms of privatization. I would like to point out to the reader that RWE divested in 2006 from all its water operations outside its home market in Germany, according to the new company strategy of focusing on energy.

The fact that the Finnish electricity market had just been liberalized in 1994 to 1997 and the privatization business for investment banks in the electricity industry was slowing down again freed up their resources for new business opportunities, such as the water sector. But in my opinion, this period of ‘privatization interests’ also needs to be seen in context of the general economic and the stock market hype during the time period, where revolutionary changes were expected to take place in many different industries and countries by applying new business models.

iii. 2003 – 2006 Restructuring and Commercial Interests

The years 2002 and 2003 are rather quiet, with no significant publication on the water sector regarding the previous discussion of privatizing and commercializing it. But as the articles from 2004 onwards show, the scene had been rather active during the previous two years. The water sector and municipal sector have been active in trying to achieve progress in regionalizing water services and creating larger units that would benefit from
increased economies of scale. In 2001, without catching too much attention, the first regional water company was formed in the region of Hämeenlinna, jointly owned by the City of Hämeenlinna and eight neighboring municipalities.

The topic of water privatization gains momentum once again in 2004 and shows that even though the previous two years were quiet in terms of media coverage, different investment banks had been actively working in the field to achieve some business transactions. In 2004, the water sector itself became active in the media in defending itself against what it perceived as commercialization. The Hämeenlinna example for successful regionalization and restructuring of the water sector is used by professor Kiuru in an article in 2004 to argue that the water sector can achieve improvements on its own and that privatization or restructuring the assets of municipal water companies in other ways is not necessary. The article argues in particular against a model proposed for restructuring the water utility in the City of Lahti, which is a project that includes a sale-lease-back arrangement, and has been developed by another investment bank, PCA Corporate Finance OY. Also, the concept creator’s competitor, Icecapital, argues in Kauppalehti against the proposal for the city of Lahti by saying that that the sale-lease-back concept is too bureaucratic and complex. In the same magazine issue, the finance manager of Lahti explains this concept, its benefits, and the reasons for considering it as a solution to the water services in the region and the financial difficulties of the city.

Three more articles about WSS are published in 2004, of which one is about a labor union organization asking the Finnish state to stay firm against attempts by the European Union to liberalize the WSS. The other article reports on the difference in municipal water tariffs, bringing up once more the subject of hidden taxation, the profitability of water services, and concludes that water tariffs largely depend on a municipalities’ tariff policy. The last article that year mentioning water services argues for a more decisive approach in changing Finland’s public services in order to increase the competitiveness of the nation, including increasing the role of the private sector in producing water services.

In 2005, although a quiet year for discussion in the newspaper about developing the Finnish WSS, a significant article appears outlining the plans of Suur Savon Sähkö OY (Great Savo Electricity Company), a company majority-owned by the public sector and approximately a third owned by the private sector. As the company announces in the article, it plans to purchase 24 water and sewerage utilities in East and Central Finland, most of which belong to municipalities which already have a stake in the electricity company. Also, the city of Jyväskylä is mentioned in that context, which merged its water utility with its energy utility in 2004. The article further points to the potential benefits of merging water and energy utilities together. Through this kind of transaction it is possible to release capital in order to assist the municipalities in their difficulties with keeping up the necessary investments in these utilities while facing budget problems.
Further, it is possible to create synergistic effects from merging a water company with an energy company, as both deal with networks and have similar clients.

In 2006, the increasing interest by the electricity sector in the water sector put more pressure on the water sector to create more effective units, as is shown in the first article of that year that provides an account by an employee of Kiuru & Rautiainen, a consulting firm in the water sector that is partly owned by professor Kiuru. In this article, progress in plans and negotiations to regionalize water services are reported from a handful of regions in Finland. In the same issue, another article provides a more critical picture of the regionalization process of municipal water works. The chairman of the Association of Finnish Water and Wastewater Works, Rauno Piippo, favors a path for the water sector that is independent from the energy sector and questions the motives of electricity companies by drawing suspicion to the commercialization of water services and a rise in prices, since most smaller water works are not profitable but in fact have to be subsidized by their owner. However, the same article also reports that progress in merging water with electricity utilities has been made already in the region of Savo, where the municipality-owned energy company Savon Voima established Savon Voima Vesi OY, a company for transferring the municipalities’ water utilities into a joint company that is a subsidiary of the electricity company. In addition, the Great Savo Electricity Company has established a daughter company called Järvi Suomen Vesi OY, for the same purposes.

As a reply, Dr. Jarmo Hukka, water professional and scientist, had his own opinion published in Kauppalehti, defending once more the perspective that the water sector should remain independent. According to his opinion, it could remain independent and viable, if water utilities would be allowed to use more of their capital for investments instead of delivering it as a profit to the municipality. Furthermore, he argues that merging water utilities with electricity utilities would bring an increased commercialization to the sector, which would be against the nature of water services since they are a basic service and a natural monopoly.
B. Aide Memoir for Interviews

Please note that this aide memoir slightly changed during the course of the study and does not represent the complete set of questions interviewees were asked. Its purpose was to provide a guideline during the interviews that could be followed, but at the same time, also allowed for sufficient flexibility when other topics of interest to the interviewee or interviewer came up.

- Please introduce yourself and your career background.
- What is your work like in relation to the water sector?
- Can you tell me about a recent project you had, what challenges you faced there, and how you solved these challenges, or what should be done to solve them?
- What means success in your business? (Own business point of view)
- What means success for water services? (Water sector point of view)
- What does a successful water sector look like? And how different is that picture from the reality of the Finnish water sector?
- What is wrong with the water sector at the moment?
- What is right with the water sector at the moment?
- What are the challenges ahead of the water sector?
- What can be done to solve these challenges?
- Who are the most important actors in the water sector?
- How do you see the role of the EU, the ministries, the municipalities, the environment centres, the water utilities, Kuntaliitto, FIWA, the private contractors, and other organizations?
- What is your role in the water sector?
- Who are your most reliable partners?
- Do you feel pressure from some other part of the field?
- In what direction should the water sector move?
- What should be done to move the sector in that direction?
- From where or whom do you learn?
- What role do international developments in water services management play for you?
- How did the water sector develop over the past decades? What were the main issues ten years ago and what are the main issues now?