

## Conference Report

### **International Workshop on Water Pricing and Roles of Public and Private Sectors in Efficient Urban Water Management, Granada, Spain, 9–11 May 2011**

During the past two decades, the issues of both water pricing and the roles that public and private sectors have played, and could play in the future, in urban water management have generated heated debates among policy makers, public- and private-sector representatives, academics, researchers, non-governmental organizations and the media. In the area of water pricing, the debates have been often acrimonious between those who consider that the era of free or highly subsidized water is long over and thus water must be appropriately priced, and those who believe that water is a human right and thus should be provided free to all human beings. Similarly, the discussions on the roles of the public and private sectors have been equally heated. Some claim that private-sector involvement would make urban water supply more efficient and also bring in significant new investment funds and management expertise. Others argue that the private sector is only profit-oriented and should not be allowed to profit from a basic resource essential for human survival. They claim that the involvement of the private sector will ensure that the poor will not have access to reliable and safe water services, since they cannot afford to pay.

The national and global debates on water pricing and public-private partnership are evolving continuously. There is no single optimal solution that is universally valid or appropriate over different time-spans. Furthermore, there are continual changes in societal expectations and aspirations, socio-economic conditions, political processes, institutional and legislative arrangements, and water planning and management techniques. Consequently, in a rapidly changing world, it is important that there should be continuous assessments of issues associated with water pricing and public-private partnerships in order that urban water management practices and processes could be regularly improved.

In order to conduct an objective and fact-based assessment on these two complex issues, some 30 experts from different parts of the world were specially invited by the University of Granada, Third World Centre for Water Management, International Water Resources Association and Global Water Intelligence to a specially convened workshop in Granada. Participation was by invitation only, and the number was deliberately kept low in order to ensure free and candid discussions. It included leading academics and researchers from several universities, heads of public utilities and private sector organizations who had concessions to run utilities, and representatives of national and international organizations like the Organisation of Economic Development and Cooperation (OECD) and the International Water Management Institute (IWMI). The facilities of the Euro-Arab Foundation in the historic city of Granada provided an excellent backdrop to conduct the discussions.

The participants were welcomed by Rector Francisco González-Lodeiro of the University of Granada. He noted the importance of good urban water management for the continued growth and development of an arid city like Granada for the past several centuries. The University has been giving increasing emphasis to efficient water management in recent years to ensure that the needs of the region are met in a timely and efficient manner. Prof. Asit K. Biswas, President of the Third World Centre for Water Management, noted in his opening address the seemingly endless growth of the urban areas of the developing world, near-total poor urban water management in such regions, and the escalating coping, health and environmental costs of poor water management. He pointed out that urban water management is not rocket science. Solutions are well known, technology has been available, and investment funds are not a constraint for well-planned sustainable business models. There is no good economic or technical reason why people living in the urban centres of the world should not have access to good, safe and reliable water services.

There is no question that proper urban water and wastewater management will require significant investment funds. In developed countries, this will mean updating and rehabilitating the networks, some of which were laid more than 100 years ago. In fact, some of the networks in the United States date back to the time of the Civil War of the 1860s! In developing countries, substantial funds will be needed to construct water infrastructure. As Celine Kauffmann of OECD noted, these investment funds can come only from tariffs, taxes or transfers. The participants were unanimous in their view that water demands for the future have to be managed, and one of the most efficient tools for such management has to be water pricing, irrespective of whether the public or private sector provides that service.

Dennis Wichelns of IWMI argued that water professionals, public and private officials and academics often promote water pricing as an important policy tool which contributes to its efficient use in domestic, industrial and agricultural sectors. A good pricing structure would communicate to the users scarcity conditions and encourage conservation measures. However, all the goals that are expected to be achieved through pricing could be beyond the scope of any one single policy measure. For example, pricing may communicate water scarcity conditions, encourage wise use, generate revenue to cover operational and maintenance costs, and contribute to equitable distribution, but simultaneously ensure that no undue hardships are imposed on household or farm incomes. Under such conditions, more than one policy tool would be necessary to achieve these objectives. They may need a combination of fixed fee and volumetric water pricing (perhaps with an increasing block-rate structure), strategies for water allocation, cost-sharing programmes that encourage investments in water-saving technology, and incentives for measuring and reporting actual individual water use.

The design of water pricing structures and efficient collection of revenues to pay for the full costs of water development and services has to be improved in most parts of the world. Considerable knowledge exists at present to design a good pricing system which could contribute to financially sustainable water services and delivery programmes. Unfortunately, in most municipalities of the world and for agricultural uses, water is delivered to consumers at prices that do not often reflect its development and delivery costs. Consequently, water is used at levels that exceed socially efficient rates, and many urban residents and farmers do not have access to a reliable and adequate supply of necessary quality water. In most cases, the potential social gains from wiser policy choices

and improved and enforceable regulations for water pricing would most likely far outweigh the social costs.

Case studies of various water utilities in terms of pricing from Spain, Portugal, Chile, England, Wales, Bolivia and Venezuela were discussed, as well as experiences of public-private partnerships from different parts of the world. In this connection, David Lloyd Owen presented an interesting case study of the not-for-profit model used by Glas Cymru, which is a single-purpose company formed to own, finance and manage Welsh Water. It has no shareholders, and thus financial surpluses are retained for the benefit of its customers. The business model aims to reduce its asset financing costs, which is often the single biggest cost of any water utility. Since 2001, savings have been used to provide 'customer dividends', cutting its bills below that agreed with the regulator, for discretionary spending on environmental and service quality and to build up reserves to improve its credit quality. Customers bills have risen at a materially lower rate compared to its peers in England and Wales. This business model has been demonstrated to be viable and could be replicated elsewhere under appropriate regulatory, political and management frameworks. This innovative model, unfortunately, has not received the attention it deserves in other parts of the world.

Over the past two decades there has been considerable interest in using the private sector to provide water services under a good regulatory framework which often is considered to be a surrogate for competition. The conventional wisdom at present is that the private sector, working under a good regulatory system, would provide sound and effective water services. The important question that has to be answered is whether the current wisdom is correct. There is considerable evidence which indicates that it may not be, or, at least not as effectively as it is perceived at present. In several cases, the results have left much to be desired. There have been successes but there appears to be a reluctance to acknowledge that all is not well.

A fundamental problem stems from the fact that the regulators of water companies do not have appropriate experience and knowledge to carry out the tasks entrusted to them. Many times regulators appear to have little or no experience of the sector. Often they consist of people who mostly have theoretical or superficial experience, and may appear to think they do not need to know how the industry actually works and operates. This has proved to be a major problem.

Ofwat, the regulator of England and Wales, has a very high standing in the world, and many countries are trying to replicate somewhat similar regulatory regimes. Ofwat has some important shortcomings. Currently a major review is under way which is expected to recommend major changes. When Ofwat was established, it was expected to encourage much-needed capital expenditure. Unfortunately, it has now been reduced to a system where company profits benefit from capital expenditure to the detriment of good operation and maintenance, to the extent that the fabric of many works has deteriorated and the skill base has declined. In addition, the five-year programme has contributed to uneven spread of expenditures, with very little money spent during the first half of the period followed by an overburden of work during the remaining period. This cycle has had a major impact on the suppliers of goods and services to the industry, which, combined with severely reduced profit margins, has reduced competition in the supply chain, while trying to introduce unrealistic competition in the supply of water.

In many places, regulatory systems have become complex and difficult to manage properly, and have introduced asymmetries of power. In countries with new regulators,

there is often an asymmetry in favour of the water companies, especially if they have significant international experience. In England and Wales, at least two power asymmetries can be observed, first between Ofwat and the water companies in favour of Ofwat, and second between the companies and the supply chain to the detriment of the latter. The high profile and the interventionist style of regulation used by Ofwat may not be appropriate elsewhere due to the high cost of providing this service and the potential to distort the procurement cycles if price reviews are carried out on a periodic basis.

Great care is needed when decisions are made as how to measure the performance of private-sector utilities, since indicators may become an end by themselves to the network operators so that they can “keep the regulator happy” rather than focusing on the overall management of the service and the water cycle and a good service delivery.

While the concept of regulators has been widely accepted and used, there have been very limited objective and reliable studies on the effectiveness of the current regulatory processes, and even less on how these could be improved significantly. A good process which would enable regulators and consumers to interact appropriately is still missing. Good training courses for regulators are conspicuous by their absence. Also, *quis custodiet ipsos custodes?* (Who will guard the guards themselves?)

Among the many interesting conclusions of the workshop were the following.

- There appear to be differences in perspectives between engineers, environmentalists, and economists. For example, engineers often define efficiency in terms of distribution losses and unaccounted-for water, rather than service delivery and delivering an appropriate service at the lowest cost. Common definitions of outputs such as levels of service delivery, tariffs, affordability and sustainability are needed so that genuinely comparative analyses of different utilities can be made.
- While the private sector can play useful roles in providing water supply and wastewater services, in much of the world these will remain with the public sector in the foreseeable future. While the public sector contains some of the world’s best-run water utilities (e.g. Singapore and Tokyo), they also harbour very many bad utilities, especially in the developing world, because of poor management and governance practices. The possibilities of such utilities attracting sufficient private (or even public) funds are remote. Thus, the heated debate of the past between proponents and opponents of private-sector involvement has distracted attention away from some of the more important issues, such as how can the performance of the public utilities be defined, measured and significantly improved.
- Collection, treatment and disposal of wastewater in developing countries has become a serious issue. The Third World Centre for Water Management has estimated that only about 10% of point sources of Latin America now are properly treated. There are many serious financial and institutional problems that have to be overcome, and also some technical problems. These problems will only be addressed when there is sufficient political will, which will probably come only after the citizens actively demand such services. For example, in Kenya, only 1% of the population have access to good wastewater services but 16% have mobile

phones. Unless there is a strong societal demand, political will is unlikely to emerge.

Selected papers and case studies from the Granada workshop will be published in a forthcoming special issue of the *International Journal of Water Resources Development* in 2012.

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