V. IMF and World Bank Push Water Privatization

and Full Cost Recovery on Poor Countries

So, yes, the free basic water supply model will work… It was a considered response to the experience from the ground that the policy of seeking to cover operating costs from payments by users was excluding the poor from access in some communities.
—Mike Muller, Department of Water Affairs and Forestry, South Africa

Financing the full $23 billion a year need with water utility rate increases would result in a doubling of rates on average across the nation. If this were to happen, at least a third of the population of the U.S. would face economic hardship…
—U.S. Water Infrastructure Network (WIN) on the need for continued public subsidy

A random review of IMF loan policies in forty countries reveals that, during 2000, IMF loan agreements with 12 borrowing countries included conditions imposing water privatization or cost recovery requirements (see Box 9). In general, it is African countries and the smallest, poorest and most debt-ridden countries where loan documents reveal IMF conditions on water privatization and cost recovery. Cost recovery, from the perspective of the IMF and the World Bank, entails ending deficit-inducing state subsidies. User fees paid by water consumers must cover water system costs, which include the costs of operation, maintenance and capital expenditures. In contrast, wealthy countries such as the U.S., continue to provide a range of government subsidies for water and sanitation services in accordance with statutory requirements including the federal Clean Water Act and the Safe Drinking Water Act.

In the division of labor between the IMF and the World Bank, it is the World Bank that has primary responsibility for "structural" issues such as the privatization of state-owned companies. Therefore, it can be presumed that in countries where IMF loan conditions include water privatization or cost recovery requirements, there are corresponding World Bank loan conditions and water projects that are implementing the financial, managerial, and engineering details required for "restructuring" the water sector.

The IMF and the World Bank argue that many developing country governments are too poor to provide subsidies for water and sanitation services. Hence, full cost recovery from water consumers is necessary. The institutions also argue that privatization and cost recovery will provide the resources necessary to extend the coverage of water and sanitation services to those outside the system. However, there is little empirical evidence that this has happened.

The IMF's and World Bank's drive to privatize and extract full cost recovery from water systems is generating concerns worldwide about the potential for such policies to compromise public health and rob low-income communities (which make up the majority of developing country populations) of access to affordable water. The most immediate impact of reducing the access to safe and affordable water will fall on women and children. More than five million people, most of them children, die every year from illnesses caused from drinking unsafe water. As water becomes more costly and less accessible, women and children who bear most of the burden of daily household chores must travel farther and work harder to collect water – often resorting to water from polluted streams and rivers. Families are forced to make trade-offs between water, food, schooling, and health care.

Below, Box 9 identifies the 12 countries and paraphrases the specific IMF loan conditions relating to water privatization or increased cost recovery. Eight of the 12 countries identified below are in sub-Saharan Africa. Box 9 also identifies the category of the loan condition. The IMF has different categories of loan conditions with corresponding degrees of leveraging power. "Performance criteria" are the most influential IMF conditions in that non-compliance with these conditions can result in loan suspension or cancellation. The IMF water privatization conditions identified in the table below are primarily "structural benchmarks," although four are unidentified types of conditions. (In Tanzania, water privatization was a condition for IMF and World Bank debt relief.) Structural benchmarks influence the overall "grade" the IMF attaches to a county's performance, but they do not, in and of themselves, constitute a basis for suspending disbursement of a loan.

Who should decide? Citizen and community involvement in water management decisions is essential. But, in the below-listed countries crucial decisions about water privatization and cost recovery were made by IMF officials negotiating with key government leaders behind closed doors and without the knowledge or consent of citizens. Neither the IMF and the World Bank nor borrowing governments are obliged to publicly disclose information about loan negotiations.[20] Eager, and sometimes desperate, government leaders will often adopt IMF policy prescriptions in order to secure necessary resources. In some respects governments, especially highly indebted governments, can become more accountable to international lenders than to their own citizens.

As described in Part I, the IMF has announced that it will streamline its conditionality and withdraw from the area of public enterprise restructuring and privatization. In the future, water privatization will rest almost exclusively in the domain of the World Bank. Unfortunately, as noted previously, the World Bank does not publicly disclose its structural adjustment-related documents. This is a secret domain. Thus, unless the

Box 9

Countries with IMF loans containing
water privatization and cost recovery conditions

Country	IMF Program	Loan Condition	Summary of Policy
Angola	Staff-Monitored Program	Structural benchmark: Adjust electricity and water tariffs in accordance with formulas agreed with the World Bank. Reduce accounts receivables of the water and electricity companies to one month of sales revenue	Adjust water tariffs periodically to recover costs, including a reasonable return on capital.
Benin	Poverty Reduction and Growth Facility (PRGF)	Other measure: After the revision of regulatory framework, the government expects to complete the privatization before the end of the third quarter of 2001	Privatize the water and electric power distribution company (SBEE)

Guinea-Bissau	Emergency Post-Conflict Program	Structural benchmark: Transfer of electricity and water management to private company	Transfer electricity and water management to private company.
Honduras	Poverty Reduction and Growth Facility (PRGF)	Other measure: Approve framework law for the water and sewage sector by December 2000	Facilitate private concessions in the provision of water and sewage services; approve the framework law by December 2000.
Nicaragua	Poverty Reduction and Growth Facility (PRGF)	Structural benchmark: Continue adjusting water and sewage tariffs by 1.5% a month. Offer concession for private management of regional water and sewage subsystems in Leon, Chinandega, Matagalpa, and Jinotega.	Adjust water and sewage tariffs to achieve cost recovery and offer concession for private management in key regions.
Niger	Poverty Reduction and Growth Facility (PRGF)	Other measure: Divestment of key public enterprises, including the water company, SNE.	Privatize the four largest government enterprises (water, telecommunication, electricity and petroleum) -- as agreed with the World Bank -- with the proceeds going to service Niger's debt.
Panama	Stand-By Arrangement	Structural benchmark: Complete plan to overhaul IDAAN's (state-owned water company) billing and accounting systems, allow to contract with private sector operators, determine need for tariff increase and possible rate differentiation among clients.	Overhaul the water company's billing and accounting systems; allow the government to contract with private sector operators; and launch a review of the tariff structure.

Rwanda	Poverty Reduction and Growth Facility (PRGF)	Structural benchmark: Put the water and electricity company (Electrogaz) under private management by June 2001.	Arrange private management of the water and electricity company (Electrogaz) as a prelude to its privatization.
Sao Tome and Principe	Poverty Reduction and Growth Facility (PRGF)	Structural benchmark: The new adjustment mechanism for public water and electricity rates will be brought into operation by decree. The price structure will cover all production and distribution costs as well as the margin of the water and electricity company. The accounts will balance consumption and resources without recourse to government subsidies.	In May 2000, the government conducted a study of alternatives for the future of the water and electricity company (restructuring, leasing, concession or full privatization), with assistance from the World Bank. By December 2000, it will select an option, adopt a financial restructuring plan, and strengthen revenue collection procedures.
Senegal	Poverty Reduction and Growth Facility (PRGF)	Other measure: Regulatory agency for the urban water sector will be created by end-2000. Transfer the recurrent costs of water pumping and distribution equipment to the communities. Increase the involvement of private sector operators.	Encourage the involvement of private sector operators in the water sector. Assess the possibility of private sector operation and financing of the infrastructure required to meet Dakar's long-term water needs.
Tanzania	Poverty Reduction and Growth Facility (PRGF)	Condition for HIPC debt relief: Assign the assets of Dar es Salaam Water and Sewage Authority (DAWASA) to private management companies.	Assign the assets of Dar es Salaam Water and Sewage Authority (DAWASA) to private management companies.
Yemen	Poverty Reduction and Growth Facility (PRGF)	Structural benchmark: Implement adjustments in water, wastewater, and electricity tariffs to provide for full cost recovery.	Implement formulas for automatic adjustments in tariff rates to ensure full pass through of product prices and full cost recovery; establish regional water authorities with private sector participation and independence to set regional tariff structures.

Box 10

Water Privatization: Common Legal Arrangements

	Source of company income	Control over labor	Control over tariff structure	Responsible for infra-structure and expansion	Length of legal arrange-ment	Control over assets
Management Contract	Set fee for managem ent service	Remains with state	Remains with state	Remains with state	Varies. Most often shorter than lease or concessio n	Remains with state
Lease	Company derives revenue from customer fees	Passed to private company	Private company with state oversight	Varies	8-15 years	Remains with state
Concession	Company derives revenue from customer fees	Passed to private company	Private company with state oversight	Private company	25-30 years	Private company gains assets at end of contract

World Bank changes its information disclosure policy, the public will be deprived of knowledge about water privatization loan conditions associated with structural adjustment lending.

International concern about IMF and World Bank water privatization policies. There are four basic reasons why the role of the IMF and World Bank in promoting the privatization of water services is causing widespread concern:

1. **Water is a resource essential to human survival – some have argued that water is a human right.** Decisions regarding the allocation of water should not be driven primarily by economic considerations. Decisions related to water provision touch upon critical issues related to public health, social equity, the environmental, gender roles and responsibilities, and sustainable resource management.

2. **Water is often viewed as common property or a "commonpool" good rather than a market commodity.** The fact that many governments have failed to provide safe and affordable water to large segments of the population does not automatically justify initiatives to treat water as a commodity or a strictly commercial or economic good. Because the private corporation exists to generate profit for its shareholders, it may not be the appropriate institution to manage the myriad of interests related to the provision of an important public resource.

3. **Democratic and community involvement in water management decisions is essential.** The IMF and the World Bank should not be making decisions about water management in countries around the world. Governments should be accountable primarily to their

own citizens for such decisions, not to the international financial institutions.

4. Public sector ownership provides a legal and sometimes constitutional basis for accountability to the broader public interest. Private corporations are not legally or constitutionally bound to serve the public interest in the countries where they operate. Many corporations have minimal information disclosure requirements which makes it difficult for citizen's groups or even governments to provide oversight and encourage accountability. Corporate interests may exercise undue influence over a government, compromising its ability to govern based on the interests of the public.

What is privatization? There are many different types of privatization. The least controversial form of water privatization involves providing incentives for small, local businesses to subcontract with publicly-owned water facilities to perform specific water services such as drilling bore holes, digging wells, expanding or improving connections, etc. However, most of the IMF loan conditions cited in Box 9 are promoting a more controversial type of privatization that involves the transfer of significant rights and obligations from the public sector to private sector companies through management contracts, leases, or concessions. Usually, contracts, leases or concessions are granted to foreign multinationals or their subsidiaries. There are some important differences between the three common types of water privatization identified in Box 10. The most common legal arrangement is the concession.

Why do the IMF and World Bank promote water privatization and full cost recovery? The IMF and World Bank promote macroeconomic and fiscal stability for all borrowers, especially those which are debt and deficit-ridden. When state-owned water companies contribute to the overall government deficit, as often they do, the institutions will encourage an end to state subsidies, full cost recovery, and better management and administration of the accounting and fee collection procedures. The IMF and the World Bank, generally believe that abandoning state-owned enterprises for privately-owned and managed firms will improve the economic efficiency of water management with positive downstream benefits such as a reduced public debt and improved management of the national budget. In general, the two institutions believe that the private sector is more efficient and cost-effective as the provider of basic goods and services in many sectors, including water.

However, there is little evidence that privatization improves the access to, or affordability, of water – especially for the poorest sectors of the population. Too often water price hikes and water quality problems follow in the wake of privatization. Box 11 describes the process of water privatization in Ghana and the potential for tariff increases.

Governments may expect that privatization will reduce their debt. The willingness of private sector companies to invest will depend upon the profit stream the company can expect. This, in turn, will depend on the level of fees charged to water consumers and agreements between the government and the private company about how the costs of infrastructure maintenance and expansion should be borne and who owns the company assets. In the end, the reduction of developing country debt and a guaranteed profit stream to the new private company, will likely be borne by increased costs to water consumers. Should water consumers be saddled with the responsibility for ensuring debt reduction and corporate profitability? This seems inappropriate, especially in developing countries where the majority of water consumers are low income or poor. Consumers who are unable to afford safe water may be forced to use untreated and unsafe sources of water. Or, consumers may be faced with trade-offs between purchasing food, water, and essential medicine and paying school fees.

World Bank Policies on Subsidy and Cost Recovery in the Water Sector. While the World Bank encourages full cost recovery in the water sector, there appears to be some debate within the Bank about the exact definition of the term. The basic definition of full cost recovery implies that water consumers should cover the cost of operating, maintaining, and expanding the water utility as needed. There is some sensitivity on the question of whether full cost recovery should entail the provision of a "a reasonable rate of return on investment." However, in the case of a private company, full cost recovery includes a "reasonable" profit margin.

There is greater unanimity on the issue of government subsidies. In general, the World Bank will not finance water projects where a government has defaulted on subsidy payments. The general practice of the World Bank is to discourage debt and deficit-ridden governments from subsidizing water and to push for full cost recovery from water consumers. While government subsidies are discouraged, the World Bank does support cross-subsidies, wherein different classes of consumers — residential, industrial, and government — subsidize one another through differential rates. However, a tariff structure with differential rates among residential consumers is often discouraged. World Bank practices tend to encourage flat rates for residential tariffs with direct subsidies available for those who meet certain eligibility criteria. (Many critics have argued that this erects barriers and attaches a stigma to the subsidy.)

The IMF and World Bank position on subsidies and cost recovery should be viewed in the broader context of the financing practices for water and sanitation services in the G-7 countries. In the U.S., for example, there are substantial public subsidies of water and sanitation services. The federal Clean Water Act and the Safe Drinking Water Act, along with state and local resources, subsidize about ten (10) percent of U.S. water and sanitation needs. The American Water Works Association estimates that this public subsidy will need to increase by approximately $23 billion a year over the next 20 years due to the aging nature of the U.S. infrastructure. According to the April 2000 report, *"Financing the full $23 billion a year with utility rate increases would result in a doubling of rates, on average, across the nation. If this were to happen, at least a third of the U.S. population would face economic hardship…"*[21] Yet, the World Bank and the IMF insist that full cost recovery is appropriate public policy for the poorest countries in the world!

Box 11

Water Privatization in Ghana: The Poor to Pay More

The government of Ghana plans to lease the Ghana Water Company to two multinational water companies to provide major urban water service. The government's decision was influenced by pressure from the World Bank. The World Bank included water privatization as one of many conditions that determined the extent of Ghana's access to the portfolio of loans in the World Bank's Country Assistance Strategy (CAS) for Ghana. (See *World Bank Discipline of Ghana*, Part IIIC2.) Once the new private sector operators are chosen, the government will be eligible for an additional $285 million Water Sector Restructuring Project of which the World Bank will finance about $100 million.

What will water privatization mean to the urban population in the Accra-Tema metropolis? In this urban area much of the population does not have piped water in their homes. Many people buy their water from those who have piped connections or have access to tanker trucks. The poorest segment of the population cannot afford to buy piped water and is left to buy water from shallow hand-dug wells that is untreated and often unsafe. The average price for a bucket of potable water is 300 cedis. If a family uses 10 buckets of water a day (which is not too much water for a family of five), it pays 3,000 cedis a day. The current minimum wage is 2,700 cedis a day. Many people in Accra do not earn the minimum wage and a significant number have no regular employment. For the majority of the population in the Accra-Tema metropolis, access to clean, safe water is a difficult daily challenge.

Unfortunately, the decision to privatize the urban water supply will likely increase this daily challenge. The actual content of the leasing arrangement has yet to be decided. However, according to a report prepared for the government "the average tariff must rise considerably to enable the urban water sector to be financially viable." The report goes on to state that the tariff must be sufficient to enable the new private sector operators to cover their operating costs, capital expenditure costs, earn a reasonable rate of return and ensure that the Ghana Water Company can finance the investment necessary to improve the water supply system. The report concludes that a tariff increase of around 52% in real terms from the March 1998 tariff and 23% on from the average tariff in the June 1999 tariff schedule will be necessary.[23]

There has been little transparency around the bidding process. Unofficial sources have leaked a list of bidders. Regrettably, the list includes multinational water giants such as Suez Lyonnaise des Eaux and Biwater (that are embroiled in controversy regarding the lack of transparency and alleged public health hazards of water privatizations in South Africa) Saur and Halliburton Brown (a large U.S. defense contractor which touts the current U.S. Vice President Dick Cheney as its former CEO). Citizen's organizations in Ghana would like their government to consider a variety of water management options other than privatization.

Box 12

The General Agreement on Trade in Services (GATS): How GATS promotes and supports the privatization of water services

A whole new set of World Trade Organization (WTO) talks on global trade in services began in February 2000 with formal negotiations beginning in Geneva at the end of March 2001. The existing GATS regime, initially established in 1994, is already comprehensive and far-reaching. The current rules seek to phase out gradually all government "barriers" to international trade and commercial competition in the services sector. The GATS defines services very broadly, including publicly-provided services, and covers such areas as drinking water, health care, education, social security, transportation services, postal delivery, and services related to the environment, culture, and natural resources. Its constraints apply to virtually all government measures affecting trade in services from labor laws to consumer protection to subsidies, grants and licensing protections.

However, the gains from the current GATS agreement were not sufficient for corporate service providers vying in the fastest growing sector of the global economy and determined to expand their commercial reach. The new round of GATS negotiations taking place now in Geneva could facilitate greater corporate intrusion on public services by:

1. Imposing new constraints on the ability of governments to maintain or create environmental, health, consumer protection and other public interest standards through an expansion of GATS Article VI on Domestic Regulation. Governments would bear the burden of proof in demonstrating that any of their countries laws and regulations are "not more burdensome than necessary."
2. Restricting the use of government funds for public works, municipal services, and social programs. By imposing the WTO's National Treatment rules on both government procurement and subsidies, the new negotiations seek to require governments to make public funds allocated for public services available to foreign-based, private service corporations.
3. Forcing governments to provide unlimited market access to foreign service providers without regard to the environmental and social impacts of the quantity or size of service activities.
4. Accelerating the process of providing corporate service providers with guaranteed access to domestic markets in all sectors — including education, health, and water — by permitting them to establish their commercial presence in another country through new WTO rules designed to promote tax-free electronic commerce worldwide.

The World Bank's position on full cost recovery is often rationalized by thick studies undertaken by private consulting firms on the "willingness and ability to pay." The "ability to pay" for water is a rather straightforward figure based on the total amount which the average household spends on water. The World Bank's "rule of thumb," based on research done in the 1970s, suggests that a maximum of five percent of total household expenditure can be spent on water. Judgments about the "willingness to pay" are derived from surveys, focus groups, interviews and community meetings about how much improvements in water service are worth to different groups. Attempts to measure the population's "willingness to pay" more for water provides the rationale for increased cost recovery. Given the lack of other options, "willingness to pay" for something as essential to human life as water could be quite substantial. This could result in a serious discrepancy between "willingness" and "ability" to pay. This, in turn, raises questions about whether "willingness to pay" is an appropriate measure to determine future water fees. Confusion about the distinction between "willingness" and "ability" to pay are captured in a World Bank water project document that states: *It is assumed that the health benefits known to users are captured in their willingness to pay for good quality water.*[22] Such a statement demonstrates insensitivity to the daily obstacles poor people face in their ***ability*** to pay for basic necessities including water and the tragic trade-offs people may be forced to make between food, water, health and schooling.