

Two for the Road

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control of New Orleans' water*

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An update on the companies vying for control of New Orleans' water

Just days before the Sewerage and Water Board is scheduled to decide whether to hand the city's combined water and wastewater system over to private hands, former board member Katherine Maraldo is scheduled to be sentenced for bribery-related charges.¹ Maraldo's conviction, along with that of former privatizer Michael Stump and the guilty plea from the company that once ran the local sewer system, should remind the Sewerage and Water Board of the corrupting influence of those who think water is a growth industry.²

Just days after the board makes its decision on privatization, leaders of one of the foreign-owned corporations vying to control the city's water will be meeting in Paris to talk about how their floundering, debt-choked company can survive.³ The firm's dance with default, along with its profound identity crisis and recent class action litigation filed by shareholders, should remind the Sewerage and Water Board of the dangers of handing a vital public service over to corporate entities under immense pressure to deliver—not water, but profit.

And all the while, the other international conglomerate hoping to profit from providing water to New Orleans citizens is scrambling to convince Atlanta officials that it shouldn't be fired—despite failing to perform maintenance, billing the city for work it didn't do and otherwise bungling the administration and delivery of Atlanta's water service.⁴ The company's dismal track record there should warn the Sewerage and Water Board that New Orleans doesn't need the same mess.

When New Orleans began its adventurous consideration of privatizing a combined water and wastewater system, several national and international companies spotted what they saw as a clean shot to profit from delivering tap water to New Orleans citizens, and began circling the city like buzzards. About this time last year, Public Citizen's "Big Greedy" report chronicled some of the corruption, environmental harm

and profiteering that those companies tried to inflict on the communities where they had managed to seize control of a vital public resource.⁵

The field has since been narrowed to subsidiaries of two foreign conglomerates, the undisputed global heavyweights in the push to turn the world's water into a commodity: Vivendi, a debt-smothered giant desperately trying to stave off financial ruin and clueless about what it wants to be when it grows up; and Suez, which never misses an opportunity to slash a workforce, break a promise and show that it cares more about getting money from you than getting water to you. Vivendi's subsidiary claims it can reduce operating costs by 9 percent. United Water's subsidiary claims it won't reduce operating costs at all. The bid that would save the most—13 percent—comes not from a private corporation, but from the public employees who already operate the water system.

But even that bid doesn't match the savings that have been realized in other cities through focused reengineering programs. Through measures such as cross-training employees, cutting staff responsibly through attrition, revising procurement practices, and overcoming the "we've always done it that way" mindset, Houston, Colorado Springs, San Diego and other cities have achieved operation savings of 20 percent or more.⁶

Like the bids from the private companies, the public employees' bid was submitted under a flawed process that fails to account for the total future responsibilities and expenses of operating the system safely and efficiently. Instead of a de facto, inadequate restructuring of the water and sewer system's administration as would happen if the public employees' bid is accepted, the employees in the public system should be allowed to continue to identify opportunities for efficiencies, and implement those opportunities through a comprehensive reengineering program.

Meantime, with the Sewerage and Water Board's decision imminent, Public Citizen has taken a fresh look at the two private sector finalists in New Orleans' water privatization and profitization sweepstakes. Both companies have been up to quite a bit over the last year—more than enough, in fact, to persuade the Sewerage and Water Board to tell both water profiteers to hit the road.

USFilter

Hopelessly entangled with a European Enron

From bribery convictions in France to bungling incompetence in Puerto Rico, the dismal record of USFilter and its corporate parents as outlined in Big Greedy still stand, and are reason enough for New Orleans to run the company out of town. But in the last year, the risk of hooking up with USFilter has become more profound, as financial shenanigans place even further doubt on the company's ability to run a water and sewer system safely, effectively and in the public interest.

USFilter is a subsidiary of Vivendi Environnement, which in turn is a subsidiary of Vivendi Universal. Jean-Marie Messier, the former chairman of Vivendi Universal, took the corporation on an extravagant spending spree—publishing, cable TV, telecommunications, the Internet, a Hollywood movie studio—as far as Messier was concerned, it was all good.

If not for Enron, WorldCom and Martha Stewart, Vivendi's subsequent financial collapse would be dominating headlines. It's lumbering under \$16.7 billion in long-term debt, with \$5.5 billion due at the end of the year. The company's stock price has tumbled nearly 80 percent since January, and its credit rating is solidly mired in the junk range.⁷ Securities fraud litigation has been filed against the company on behalf of shareholders contending that Vivendi Universal repeatedly and deliberately overstated the company's financial health while falsely understating the severity of the company's debt obligations.⁸

Little wonder then, that USFilter is trying to give the impression that it is separate from and unaffected by the floundering, overextended, underfinanced corporate parent. USFilter CEO Andrew Seidel claims that Vivendi Universal's flirtation with disaster will have no effect on Vivendi Environnement.⁹ And USFilter Vice President David Smith

has tried to assure New Orleans citizens specifically that his company's bid to operate service in New Orleans "will not be affected" by Vivendi Universal's struggles.¹⁰

USFilter officials argue that since Vivendi Universal sold down its ownership in Vivendi Environnement, from 63 percent to roughly 40 percent, in June, Vivendi Environnement and USFilter are insulated from the corporate parent's woes.¹¹

That's not exactly the way Vivendi Universal sees it. In a letter to shareholders and employees in August, new CEO Jean-Rene Fourtou suggested that one of the corporation's going-forward strategies could include regaining majority ownership of Vivendi Environnement.¹² Debt-rating firm Standard & Poor's was not amused. Reacting to Fourtou's letter, S&P noted that Vivendi Environnement's credit rating has been hovering at "stable," but "any change in VU's ownership to regain majority control over VE—a potential strategy hinted at yesterday by VU's CEO, Jean-René Fourtou—would, however, result in VE being placed on CreditWatch with negative implications."¹³

Vivendi's board of directors, meanwhile, is fighting with itself, and there are news reports nearly every day about a division being bought or another division being sold, in what can only be described as a haphazard scramble that casts dramatic uncertainty on just what Vivendi Universal will be next year, next month, or next week. For instance, Vivendi was considering selling its stake in a French telecom, while at the very same time considering increasing its ownership share of the very same company. "I think they're just making lots of propositions, asking people 'What would you want and at what price,'" said Jean-Francois Legoux, a Paris-based UBS Warburg fund manager that holds a small stake in Vivendi, in an interview with *Forbes*.¹⁴

A corporation so confused about its own mission and motives can't be taken too seriously when it makes pronouncements about what it's going to be when it grows up. But it's worth noting that Vivendi Universal, seeking "to put an end to market rumors," issued a statement asserting that it is committed to retaining a heavy interest in Vivendi Environnement, and absolutely will not allow its ownership to fall below its current 40.8 percent.¹⁵

Vivendi started out as a water company, and throughout the parent corporation's ill-fated quest to become a global media giant, Vivendi Universal used water operations as a "cash cow," loading debt to on to Vivendi Environnement.¹⁶ As the parent corporation struggles to emerge from the dizzying uncertainties it's mired in, every deal does indeed appear to be on the table, thus extending chaos and uncertainty to Vivendi Environnement and USFilter.

If the New Orleans Sewerage and Water Board makes a deal with USFilter, board members could wake up days later holding an agreement with a very different entity, depending on decisions made by Vivendi Universal's board. More alarming, USFilter could find itself cannibalized, squeezed and drained as the corporate parent tries to eke every last drop out of the "cash cow" to bankroll whatever whimsical strategy Vivendi Universal finally lands on. The losers would be the citizens of New Orleans when the company that's supposed to be running their water and sewer system doesn't have the resources to fulfill its obligations. In any case, there is far, far too much uncertainty surrounding USFilter, Vivendi Environnement and Vivendi Universal. It's a foreign entanglement that the Sewerage and Water Board should definitely avoid.

United Water

Sewage in your river is money in their pocket

United Water, the U.S. subsidiary of French water giant Suez, was already failing dismally to meet the terms of its much-touted contract with Atlanta when Big Greedy took a look at the company last year. A year later, things have gotten decidedly worse.

As has been widely reported, Atlanta Mayor Shirley Franklin put United Water on 90-day notice August 12, telling the company to clean up its act or it would be fired.

Franklin's action came on the heels of a city report that found dramatic staff reductions and "a readily ascertainable correlation between the decline in United Water

staff and the continuing and unacceptable increase in backlogged facility maintenance items, as well as delays in distribution system repairs." Inadequate staffing was also linked to United Water's response times that "are consistently and habitually inadequate and potentially hazardous conditions are not remedied in a timely manner." Among the report's many other complaints is that United Water hasn't flushed the system regularly, putting water quality at risk.

The report also charges that United Water has improperly billed the city—for instance, performing routine maintenance yet billing the city for "capital repairs"—and billing the city for work that wasn't actually done.

And the city claims United Water personnel, on Atlanta's dime, are tasked with working on projects United Water is working on elsewhere—even working on contracts United Water is trying to win in other towns. Throughout, United Water's operation has been characterized by a failure to adequately provide information that the city has requested.¹⁷

The city has so little trust in United Water, it is proposing to spend \$1 million to hire inspectors to double-check the firm's work.¹⁸ The \$21 million per year, 20-year contract was intended to save the city money, not cost it more.

United Water's contract in Atlanta was touted by United Water and the rest of the private water industry as the wave of the future. The company's debacle in Atlanta has instead become a powerful warning for New Orleans and other communities across the nation of just how empty privateers' promises can be.

Generating front page coverage in national newsmagazines, the Atlanta debacle has become the poster-child for why a city shouldn't privatize.¹⁹ Somewhat lost in the shuffle is yet another United Water story of failure, in Milwaukee.

United Water was hired in 1998 to operate the Milwaukee Metropolitan Sewerage District's system of tunnels and treatment plants, with the customary promises of million of dollars saved and full compliance with environmental and regulatory standards.

What United Water didn't promise was to cut corners, save money and let raw sewage into area waterways, but that's what happened.

Wastewater flows into the MMSD's system of collector sewers before it is treated or temporarily stored in 19 miles of tunnels at depths of up to 325 feet, part of a comprehensive, multi-year, \$2.3 billion sewer improvement program that the District began in 1986 to comply with federal water quality standards by reducing the amount of untreated sewage discharged into local waterways.²⁰

The tunnel system was expected to entirely eliminate discharge of untreated sewer, but has failed to do so for a number of reasons, according to an audit of the system's performance conducted by the Wisconsin Legislative Audit Bureau. Insufficient capacity, sediment deposits in the tunnels and other unanticipated problems have hindered the system's performance, and the MMSD attributes the discharges to other unavoidable problems such as severe storms.²¹

But the audit also lays blame squarely on the shoulders of United Water's quest to cut costs as well:

"We estimate that 107 million gallons of untreated wastewater was discharged into waterways from June 1999 through June 2001 because United Water Services had temporarily turned off Deep Tunnel pumps while switching to a lower-cost source of electricity. The contractor saved approximately \$515,000 by switching power sources during that period."²²

The Deep Tunnel system has not been as successful as Milwaukee officials and residents might have hoped. Of the system's shortcomings identified in the audit, some do indeed appear to be unanticipated, the result of underestimating system growth or

other errant assumptions when the system was built. But as Milwaukee officials and citizens struggle to address those problems, the last they need is the added complication of a company willing to cut corners to save a few bucks, even if it means dumping raw sewage into area waterways.

Milwaukee's experience with United Water is yet another example of how private water and wastewater companies are primarily concerned with making money, not providing public service. And raw sewage dumped in Wisconsin rivers is yet another reason why New Orleans should reject United Water's bid to run the sewer and water system, and instead send the company packing.

Houston provides yet another example. Amid privatization talks several years ago, Houston instead determined that it could save more money and retain control of a public resource by reengineering the public system operated by Houston Public Utilities.²³

But Houston also decided to partially privatize its system, and hired United Water to operate the city's Southeast Water Purification Plant in 1996 under a five-year contract. When the contract expired in 2001, the city gave another company the bid.

In an effort to get one more bite at the public funding apple on its way out of town, United Water sued the city in November 2001 seeking \$900,000 for services. The city countersued for \$2 million, claiming United Water failed to maintain the plant, and necessary repairs will cost \$2 million.²⁴ Doing business with United Water is also costing the city an additional \$370,000—the amount the city has approved to pay for legal support in the case.²⁵

Houston's reengineering program has reduced some costs, and may provide valuable lessons for New Orleans if it wisely rejects the bids currently being considered and opts instead to reengineer the public system. But Houston also provides valuable

lessons about mistakes that New Orleans should seek to avoid—mistakes like getting into business with a litigious company.

Fortunately for Houston, that city's contract with United Water was limited to five years, and the city was able to switch operators when it became clear that United Water's operation wasn't competitive. New Orleans, by contrast, is considering entering into contracts that could last as long as 20 years. Judging from United Water's attempt to bleed public money from Houston even after the contract has expired, New Orleans might find it very difficult—and very costly—to extract itself from a long-term contract with United Water, even if the company failed to meet its obligations.

Notes

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² “Water Company Ordered to Pay \$3 Million Fine for Bribing New Orleans Water Authority Member,” Department of Justice release, Dec. 14, 2001.

³ “Vivendi Nears Tech Sale as Grand Plan Shapes Up,” Reuters Market News, Sept. 11, 2002.

⁴ “City Blasts United Water,” *Atlanta Business Chronicle*, Aug. 9, 2002.

⁵ “The Big Greedy: A Background Check on the Corporations Vying to Take Over New Orleans’ Water System,” Public Citizen, September 2001.

⁶ “Privatization of Water and Wastewater Systems in New Orleans,” Bureau of Government Research, June 15, 2001.

⁷ “Vivendi Goes to Pieces,” *Forbes*, August 20, 2002.

⁸ Class action complaint filed by Bernstein Liebhard & Lifshitz, LLP, in U.S. District Court, Southern District of New York, July 22, 2002.

⁹ “Vivendi Up-Ended; VE/US Filter Afloat,” *Public Works Financing*, June 2002.

¹⁰ “No S&WB bids stand out yet near deadline,” *New Orleans CityBusiness*, Aug. 26, 2002.

¹¹ “Vivendi Up-Ended; VE/US Filter Afloat,” *Public Works Financing*, June 2002.

¹² Letter from JR Fourtoun to Vivendi Universal’s Shareholders and Employees, Aug. 19, 2002.

¹³ “Bondholder Vote to Remove Cross Default Clauses Leaves Vivendi Environment Rtgs Unchanged,” Standard & Poors Ratings Services statement, Aug. 20, 2002.

¹⁴ “Vivendi Goes to Pieces,” *Forbes*, August 20, 2002

¹⁵ Vivendi Universal “Statement on Vivendi Environnement,” July 25, 2002.

¹⁶ “Vivendi Universal Corporate Profile,” Polaris Institute, January 2002.

¹⁷ “City blasts United Water,” *Atlanta Business Chronicle*, Aug. 9, 2002.

¹⁸ “Mayor wants outside check on water firm,” *Atlanta Journal Constitution*, Sept. 12, 2002.

¹⁹ “The Coming Water Crisis,” *U.S. News & World Report*, Aug. 12, 2002.

²⁰ “An Evaluation: Milwaukee Metropolitan Sewerage District,” Wisconsin Legislative Audit Bureau, July 2002.

²¹ “Sewage dumping policies faulted,” Milwaukee Journal Sentinel, July 30, 2002.

²² “An Evaluation: Milwaukee Metropolitan Sewerage District,” Wisconsin Legislative Audit Bureau, July 2002.

²³ “Thinking, Getting and Staying Competitive: A Public Sector Handbook,” Association of Metropolitan Sewer Agencies, 1998.

²⁴ “Legal deluge inundates first city water plant privatization project,” *Houston Business Journal*, Aug. 19, 2002.

²⁵ Ibid.