



Public Private Partnerships and the poor in water supply projects

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*This factsheet examines some key issues and implications of involving the private sector in water supply and how this can impact on service delivery for the urban poor. It deals with those situations which involve relationships between organisations from the public and private sectors and identifies issues that are central to promoting the needs of the poor in Public Private Partnerships. The source for this summary is *Public-Private Partnerships (PPP) and the poor in water and sanitation*. (www.lboro/wedc/projects/PPPandthePoor); series editor M Sohail Khan.*

It is worth noting that whilst many documents exist which hypothesise about the effects of private sector involvement on the poor, many of which appear to strike up distinctly pro- or anti- positions on the wider and contentious issues around privatisation, there remains little direct evidence-based reporting on what does, and does not, work.

Water supply and the private sector

The involvement of the private sector in partnership with government has been advocated as a means of improving the development of sustainable water and sanitation systems. Public Private Partnership (PPP) is used as a general term to cover a wide range of agreements or partnerships made between private sector concerns, public sector utilities, government departments and civil society/consumer groups in relation to the delivery of water and sanitation services. Largely under donor pressure, governments are turning to PPP arrangements for the provision of services. The rationale includes a variety of factors, which may include:

- lack of capacity of government institutions to deliver a reasonable level of service or to improve service quality;
- financial weakness of public utilities;
- lack of public sector financing capability;
- inability of public institutions to respond to increasing growth in demand through, for example, rapid urbanisation; and
- problems related to the large numbers of employees in public sector providers and their productivity.

In addition, International Financing Institutions (IFIs) require that certain indebted countries reduce domestic spending as part of structural adjustment programmes; they promote the idea that the private sector is more efficient and effective, and delivers a better quality service.

Box 1. How do we define the private sector?

One of the problems in addressing private sector involvement in water and sanitation is the sheer diversity of the private sector. The headline news about the private sector tends to focus on the involvement of multinational companies; however, this is only part of the story.

We can identify formal private sector organisations ranging from multi-national companies with thousands of employees through to medium and small sized private enterprises with maybe less than one hundred employees, operating either at country level or sub nationally. In addition there is an informal private sector, including water vendors who retail water to citizens who do not have access to a formal supply - primarily the poor.

The contractual framework

The contractual framework is key to understanding the formation and development of PPP arrangements which involve the formal private sector. The process adopted prior to the award of contracts has an important influence on the way in which the operational details of service delivery are worked out. It is these operational details which subsequently impact either positively, negatively or neutrally, on the poor. There are four stages.

1. Preparing for PPP: strategy development by the public sector client to bring in the private sector
2. Selection of private sector operators and award of contracts through competitive bidding
3. Operation and regulation of service delivery within the terms and conditions of the contract
4. Completion and termination of the contract

Normally, a public sector institution is the client and they engage an operator from the private sector to be responsible for the operation of the water service. Exactly what the roles and responsibilities of the operator are depends on the type of contractual arrangement which is entered into - See Box 2.

Box 2. Type of contractual arrangements in PPPs

Contracting out: The client contracts out services to the private sector for a specific package of work (e.g. customer billing, specific maintenance tasks). Private sector role is limited to its tasks.

Management contract: Private sector takes over responsibility for part of the operations (e.g. all of operation and maintenance); client retains responsibility for system expansion and other capital works

Lease: The private sector organisation is responsible for providing agreed levels of service to customers and for providing working capital for repairs. The main tasks are operation and maintenance but with a greater degree of autonomy than for management contracts

Concession: The private sector organisation is responsible for financing the investment costs of the system including system expansion, as well as for all of the operation and maintenance, in order to achieve prescribed service delivery objectives.

Full divestiture: In addition to responsibilities for service delivery, ownership of existing assets (e.g. the physical infrastructure of the water system) is transferred from the public to the private sector. In the arrangements previously described, ownership of assets remain with the public sector.

It is the more complex contractual relationships, such as concessions, which provide most opportunity for the public sector to make use of the full resources of the private sector. This leads towards hitherto largely unexplored relationships between the formal private sector and groups of consumers who are very poor. Furthermore, relationships may need to be developed with the local informal private sector which may be involved in a secondary market for water and which provide the link to poor consumers.

Preparing for PPP

What happens during the process of preparing for PPPs prior to the award of contracts is crucial; the rules of the game are set. The key facts are as follows.

Policy: the poor do not get mentioned. At the outset, the client's objectives and terms of reference do not generally require the needs of the poor to be specifically addressed. Unless provision for poor groups is brought in at the start, it is unlikely to figure at the operational stage. The operator will follow the requirements of the contract; if this does not specifically require him to address the needs of the poor, then he will not do so.

Poor and vulnerable groups exert little pressure on the PPP development process, which focuses on the timely appointment of the operator. Information campaigns are sometimes requested but they are seldom expressly required to ensure access to disadvantaged groups. The poor particularly suffer from "information deficits", that is, the gap between what is known and what needs to be understood.

Core issues in PPPs are typically technical and financial and not those surrounding poverty. The quest for full cost recovery features prominently; attention is seldom drawn to the 'public goods' nature of a more efficient water sector. Wider social and public health objectives are not typically defined or included within contracts

Knowledge and understanding of advisers. Those who advise client governments are often distant from the client's organisation; their expertise will be determined by the requirement specified by

the client and normally focuses on the core specialities of technology and finance.

The time scale for the client's advisers to prepare the necessary bidding information is relatively short and they focus on the core technical and financial PPP issues. The complex and little understood issues around serving the poor (which are not likely to be part of the terms of reference) are unlikely to receive serious consideration at this stage

Bidding by the potential operators. The harsh commercial realities of competitive bidding often mean there is little material change in final service delivery when compared to that set out in the draft contract. Bidders rarely offer improvements over the minimum stipulated requirement and it is not realistic to anticipate that they will propose to extend service coverage into poor areas about which little is known.

Negotiations with successful bidder. In striving to strike the most favourable economic arrangements there is evidence of asymmetry of influence between clients and bidders. For complex, long term concessions the market is dominated by relatively few major international operators. In some cases government bargaining power is reduced.

Flexibility in the contract: PPP contracts in water supply often rely upon "command and control" contractual provisions that contrast with other services which appear to grow by adding economic value (and economic self-interest) into their business mentality.

Operational framework for PPPs

Once the contract has been awarded, an operator becomes responsible for some or all aspects of service provision in accordance with the terms and conditions of their contract. We have seen that the pre-award stages are crucial in determining the shape of things to come for what is potentially a very long time. We now look at how this works in practice regarding the services to which the poor have access. Based on the findings of a number of case studies of PPPs in Southern Africa and South Asia, this section lists the key issues and summarises their implications for service delivery to the poor.

Building relationships with low income consumers. Private companies have a lot to learn about operating in low-income areas, and consumers and civil society groups can play a key role in helping them, though they also have a lot to learn about private companies.

- A key lesson is the need to focus on understanding customer circumstances, offering appropriate service levels and focusing on customer outreach. The learning curve would seem to involve years rather than months. Much depends on continuing relationships between the operator, the public partner, civil society groups and the customers. In this context, it is important to note that the public utilities were never very responsive to low income communities, and hence are unable to transfer much knowledge on how to work in low income areas to private sector operators.
- There is little to suggest that the governance mechanisms arising through the formal contractual procedure are effective in terms of building relations with poor consumers. Partnering with either civil society groups (NGOs and CBOs) or small local entrepreneurs can, in the right circumstances, help companies along their learning curve while also increasing the capacities of these groups and consumers to engage with PPP arrangements.
- For poor consumers it can be hard to perceive any differences between the private utility and the pre-existing public utility. A sense of continuity is reinforced when, as in some cases, most of the utility staff is kept on. Consumer relations staff of the operators emphasise the

efforts made to inform local groups of the new arrangements and how the company intends to operate. However, given the large populations usually involved, such information spreads slowly.

- Where other than formal private sector companies are involved, we can see closer and more effective relationships developing both through local entrepreneurs, and NGOs and CBOs. Actual roles range from interlocutors to local service providers on behalf of the operator.
- Consumers are concerned with the quality of service at the point of delivery; they have little concern with improvements to physical infrastructure in their own right. Performance measures such as reduced leakage may lead to a more efficient system, but they have to translate into benefits which are tangible to the consumer groups in question
- Involvement in the processes leading up to change does appear to be critical. Whilst this does not guarantee success, cases in which stakeholder participation was absent or minimal were the least successful in terms of the perception of the poor.

Financial issues and tariffs. Household cash flow is critical for poor consumers and is highly sensitive to changes in the tariff structure; this can have a major impact on the poor.

- It is essential to understand and take account of typical household budgets when determining changes to both the tariff and the methods of payment.
- Tariff structure planning needs to identify and address impacts which might undermine the security of low-income households through increasing their vulnerability and exposure to risks.
- There is an opportunity to explore alternative financing mechanisms for poor households which minimise the need for large up-front payments. Reducing connection charges to a minimum and recovering them from the consumption tariff will make house connections a more feasible option for the poor, and for the market for the operator - to everyone's benefit.

Box 3. Tariff structures in South Africa

- Prior to 2001 in Cato Crest, Durban, a system of 'ground tanks' enabled the volume of water delivered to each household to be controlled by the local private entrepreneur. This was coupled with a flexible system of prepayment for water supplied; up-front payment could be made in full or in instalments. The system was self-regulating in terms of payment because people were required to pay in advance for the month, in order to receive an agreed volume of water. They knew what they were getting and could budget the cashflow accordingly.
- In Dolphin coast, a new tariff structure was introduced for the PPP; this created a tiered system of service levels and tariffs which includes a 'lifeline' tariff of 10 kiloliters. The problem is that for low volume users, which includes most poor consumers, the fixed charges for water and sewerage turn out to be much higher than the metered consumption (variable) charges. Consumers are not able to regulate their consumption to achieve lower bills. As a specific measure targeted at the poor, the lifeline block has had hardly any impact.

Technology and innovation. PPPs bring a new operational environment which offers scope for innovation in the use of different technological solutions. The private sector can resources and know-how to exploit such innovations to achieve improved service delivery:

- Firstly, introduction of differentiated levels of service to take account of users' ability and willingness to pay.

- Secondly, introduction of more flexibility in engineering standards to make them more locally appropriate

Information. There is a pressing need to develop a base of information about low income groups which is directly usable in the development of PPP arrangements.

- This requires a clearer understanding on the part of the designers of PPP arrangements, and also local institutions and organisations, about information needs.
- There is also a clear need to provide information for consumers particularly about proposed roles and responsibilities. Lack of understanding and consensus leads to operational problems and is ultimately disempowering.
- Communication is a vital component of PPPs; investment in it will pay dividends in operational terms. Lack of information does not mean that low-income communities will comply with the partnership; rather, it increases the risk of non-payment of bills.

Land tenure. Lack of formalised land tenure arrangements is normally a barrier to the extension of networked infrastructure. For example

- the regularisation and notification process undertaken by the public sector partner in the informal areas of Karachi (Pakistan) was a prerequisite to the successful partnership with a civil society group and the consumers.
- however, this is not always necessary. In Kibera, Nairobi (Kenya) when improvements to the water supply were delivered, it gave residents the hope that they would eventually be given title to the land.

Contractual. Operational performance with respect to poor consumers reflects the focus of the contract preparation process, which is usually based around the financial concerns of the client (e.g. local government or utility) municipality rather than a concern with the poor.

- Approaches where the concepts of the contract are translated clearly into agreed roles and responsibilities down to the household level have been successful.
- Non-payments are dealt with in a variety of ways which depend upon the contractual agreements. In one concession contract where non-payment is increasing, it is the public sector partner (municipality) that bears the risk of non-payment by households. The private sector operator is guaranteed payment based on metered supply regardless of household payment levels. The situation of non-payment did not arise in the case where pre-payment for a fixed volume of water was made.

Regulation, monitoring and complaints. There is lack of capacity on the client side, particularly with smaller municipalities, to monitor and regulate complex contracts.

- More attention needs to be paid to performance measures; where PPP objectives require service improvements for poor consumers, performance indicators need to reflect the quantitative and qualitative nature of the improvements. For example, the price charged for water by informal vendors is an indicator of water shortage in an urban area, and the operator of the water supply could be given a contractual incentive to reduce it.
- Care needs to be taken when making international comparisons on regulation. There are important distinctions between regulating a contract, which may be the responsibility of a municipality, and regulating a sector through a national body such as happens in the UK.

- Regulation is not a key issue for all poor households. The “unconnected poor” only become stakeholders in the event that rising tariff revenue leads to coverage being extended into their neighbourhood.

References and further reading

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Regional Annex: the Ghanaian experience

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This fact sheet highlights some key issues that have emanated from the Ghanaian experience with Public Private Partnerships (PPP) and how these efforts are impacting on supply of water to the poor. The information was gathered from the Author's experience in the Ghanaian Water Sector, and also from a number of publications relating to the sector reform in Ghana as well as on the outcomes of a recent study sponsored by NGO caucus of the Netherlands Water Partnership (NWP-NGO).

Context to the PPP Process in Ghana

Ghana water sector is segmented into two parts. The community water sector deals with over 16000 rural communities and some 287 small towns. Management of water supply is the responsibility of District Assemblies with facilitation and oversight role by the Community Water and Sanitation Agency (CWSA). The urban water sector comprises about 87 cities and towns where the state water utility- the Ghana Water Company Limited (GWCL) owns and manages water supply.

The term “public” as used within the sector in the Ghanaian context includes all government agencies (Ministries, Departments and Agencies), and local authorities (District, Municipal and Metropolitan Assemblies). The Ghana Water Company Limited (GWCL), the main utility in charge

of urban water supply, though registered currently as a limited liability, company still receives financial support from Government. It has no shareholders and does not pay dividends. Hence within the context of the current discussions, the GWCL is still considered as a public organization.

The term “private” refers to the private sector and is used in two different contexts. Firstly, to describe the formal private sector ranging from multi-national companies through to small/medium sized private enterprises and informal service providers who basically operate with a profit motive. In the second instance, the word private in the developmental context is used simply to contrast the public sector. Within this context NGOs, civil society groups, community-based organizations and other not-for-profit organizations can all be considered as part of the private sector although they do not meet the criteria of profit making and their status as economic agents is open to discussion.

The terms ‘public private partnership (PPP),’ ‘private sector participation (PSP),’ and ‘privatization’ are often used interchangeably. Generally the terms PSP and privatization refer to the involvement of the private sector in some form, at some stage in the delivery of water supply services. The involvement could range from PSP in management contracts to complete divestiture of public utilities. There are some examples of public-public and public-private partnerships in small towns – but most of the discussions on PPP within the urban sector in fact relate to PSP. In discussions on water supply to poor areas the term tripartite partnership (TPP) is an increasingly popular concept that is used to describe situations where NGOs work in tandem with the public and private sector.

Ghana’s Urban Sector-Recipe for Privatization?

Under the management of the public sector (through the GWCL), the urban water sector has experienced considerable deterioration. Coverage figures are given as 70% but it is estimated that only about 40% of the urban population have water flowing regularly through their taps. There has been no significant rehabilitation or extension over a long period and a lack of autonomy and weak management has resulted in poor operational efficiency and a very precarious financial situation. Since 2002, GWCL has more or less been bankrupt. Cost recovery barely keeps the company operational or meets the recurrent costs. Meanwhile the company is estimated to be indebted to the tune of US\$400 million. About 50% of all water production is unaccounted for. In 2003 alone, losses in operations were of the order of US\$34 million – almost 100% of total revenues. It is also estimated that the company actually needs about US1.8 billion to extend, rehabilitate and renew systems so that water can be extended to all the urban population over the next 20 year period. Since 1995 very little inflow of capital has occurred to meet this need. Generally water supply in urban poor areas is very poor and communities are forced to buy water from tankers – often at prices of up to 10 times the recommended tariffs.

Overview of PPP in Small Towns

Under the on-going decentralization process, management of small towns water supply is the mandate of the district assemblies with the support of the Community Water and Sanitation Agency (CWSA). Until the year 2000, PPP was virtually unknown in small towns. A pilot project sponsored by the World Bank’s “Public Private Infrastructure Advisory Facility (PPIAF)” initiated private sector involvement in decentralized water supply management in 4 small towns with populations between 5000-25,000. This process involved relatively small local water enterprises.

A feasibility study sponsored by the Netherlands Water Partnership in 2004 broadly reviewed PSP processes in small towns and peri-urban areas in cities. The review of the PPIAF Projects led to

some important conclusions. (i) The introduction of private operators allows some continuity in a regularly changing political stage where local level institutions (like the District Assembly, small towns Water Boards and Watsan Committees) regularly change composition due to elections or power play; (ii) Before PPP can be feasible and adequately pro-poor, fine-tuning of institutional frameworks and substantial capacity building is required for most stakeholders. Regulation of small towns water supply, in particular, needs clarity; (iii) There is strong evidence that NGOs in small towns often contribute in a creative and innovative way to support the roles of these small scale water operators and are effective in advocating for the needs of the poorest in the community. Tripartite partnership involving public, private and NGOs presents a feasible option for effectively dealing with the needs of the poor.

On-going PSP Effort in the Urban Sector and it's Implications for the Poor

Between 1995 and 2002 the urban water sector made significant advances in pursuing PSP as a feasible option for improving efficiency and attracting investments in the sector. Initial proposals for PSP involved 87 urban water systems packaged into two large concessions to be leased to two different foreign companies over a period of about 10 years. Like many business framework documents for PSP in the sector, the initial proposals laid emphasis on the legal, technical and financial issues. The initial proposals for the PSP were hotly debated. Key NGOs and civil society organizations (CSOs) formed a 'Coalition against the Privatisation of Water in Ghana (CAP)' to oppose the official plans. The key arguments of the CAP was that the proposals for the PSP were not pro-poor. The CAP also questioned the transparency of the process and the track record of many of the short-listed operators with regard to their performance in similar assignments in other countries. Following several months of social and political agitation, plans for implementing the PSP were finally suspended in 2002.

Following the unsuccessful initial attempt to introduce PSP in the urban sector, the original proposals have been revised. A new Project - "The Water Sector Restructuring Project" has instead been put together to advance the PSP agenda and a grant of about US\$105 million has been made available by the World Bank to start implementation. The key strategies of the new project involve:

- A 5-year management contract instead of a 10-year lease as originally proposed;
- Strengthened role of Government and the Regulator in the process;
- A limited supportive role of the private operator and less emphasis on capital mobilization and role of external donors;
- More clearly defined pro-poor interventions ; and
- Increased attention to stakeholder needs in terms of the social, political, cultural and legal environment of Ghana.

Generally debate in the sector on how to make the PSP process pro-poor has led to a convergence on a multi-pronged approach for raising the profile of service delivery to the poor:

Box 4. Some Options for making PPP more pro-poor

The current discussions are seeking to incorporate the following interventions:

- Increased investments to ensure network expansion to poor areas;
- Increased reliability of water to poor areas to reduce reliance on water vendors;
- Targeted subsidies involving the establishment of a lifeline tariff for low income houses;
- Establishment of a revolving connection fund to assist poor houses finance the costs of new connections;
- Establishment of a low-income unit within the Sector Ministry to strengthen advocacy on pro-poor issues, promote research and policy debates;
- Regulation of water tanker services to discourage excessive pricing for poor consumers.

Conclusions / lessons learned

Despite the lack of success in achieving the ultimate objectives of PSP in the urban sector so far, the experiences have provided many useful insights as follows.

Acceptability of the process. The Ghanaian experience clearly shows that the process towards the introduction of a PPP in urban areas and small towns is a complicated process with far reaching socio/political consequences. Political will for the PSP process is a key pre-requisite but not enough to guarantee a successful PPP process. The processes adopted prior to the award of contract – during the stage when the rules of the game are set - ultimately determine the acceptability of the PPP process and the level of success with regard to the ultimate quality of service delivery to the poor.

Stakeholder involvement. A key lesson is that stakeholder involvement is crucial in the process of setting out the framework for the PPP and all effort should be made to ensure dialogue between government agencies, donors, civil society, NGOs and private groups. Ignoring stakeholder concerns could result in a limited success or complete failure of the process. Successful engagement with NGOs and CSOs in this area requires a long time frame.

Pro-poor Measures. PSP efforts are unlikely to work without a commitment to protect low-income consumers. The Ghana experience has clearly shown that there is a dearth of knowledge on policies and strategies that make PPP efforts truly pro-poor. Key constraints to delivering services to the poor such as inequitable tariff structure and unaffordable connection fees are difficult to deal with at a sectoral level.

Other Alternative Approaches to PPP

For poor urban areas and small towns, options that involve NGOs and CBOs working in tandem with public and/or private bulk providers are feasible in ensuring improved sustainable service delivery to the poor. Recent discussions in the sector have led to agreement on the need to review current approaches to PPP which only emphasizes the involvement of large multi-nationals and places less emphasis on local small scale private entrepreneurs and the potential facilitative role of NGOs.

Leadership role of government. Government's ownership and technical leadership of the process is essential to ensure stakeholder acceptance. In Ghana the public perception of the process was negatively affected by: (i) an excessively strong influence by donors like the World Bank and (ii) a rather inexperienced team of Government advisors to provide management of the process. This led to a lingering perception among the public that the Government did not 'own' the process and the donors are driving the process to suit the foreign operators. These factors contributed to the mass resistance by civil society groups which led to the rejection of the initial proposals of the PSP process.

The myth of increased investments

The Ghanaian experience leads to the conclusion that PSP does not always lead to leveraging of financial resources (credit, capital and insurance markets) as the proponents of PPP often strongly argue. In developing countries like Ghana, the process of PSP does not imply financing problems can be overcome by mobilizing finances from the private sector. In the case of Ghana, only about 20% of the needed funds were secured or pledged from donors before the process was stalled in 2002.

Challenge of linking up with CSOs

The Ghanaian example clearly illustrates the immense influence that Civil Society Coalitions can wield in the PSP process. On one hand the CAP effectively advocated for the poor and helped highlight issues concerning the inadequacy of the PSP proposals. But the entrenched position of the CAP to discussions on the involvement of multinational companies and their failure to bring forward any viable alternatives led many stakeholders, including poor urban communities, to question the real intentions and commitment of CAP to improving the plight of the poor. The general lessons are that adequate government-driven public education, a greater transparency in the PSP process, and increased stakeholder involvement which provide for the voices of the poor to be heard is important in ensuring that the PPP process is not derailed by well-resourced civil society groups who have little to offer by way of alternative proposals for meeting the real needs of the poor.

Capacity building of sector institutions

Ongoing discussions in Ghana have clearly established the need to develop the capacity of the Regulating Body and to emphasize its independence in the process. From the Ghanaian context the Public Utilities Regulatory Commission (PURC) could have a crucial role in ensuring service delivery to the poor in two ways: (i) regulation of informal service providers (eg. tanker services) which serve about 40% of the populations in some cities, and (ii) defining a social tariff that is better structured to benefit low income households and by eliminating access to the lifeline tariff by middle and upper income customers.

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