



EAP Task Force

Document 7

Joint Meeting of the EU Water Initiative's EECCA Working Group and the EAP Task Force Environmental Finance and Water Networks

29 March –1 April 2005, Chisinau, Moldova

OUTLINE PAPER: PROGRESS ON IMPLEMENTING THE ALMATY GUIDING PRINCIPLES FOR THE REFORM OF THE URBAN WATER SUPPLY AND SANITATION SECTOR IN EECCA

Participants are invited to take note of the document and to provide their comments on its content. In particular delegates are invited to provide their views on the key messages contained in the document and highlight any country examples of institutional and legal reforms that they would wish the secretariat to include in the document when it will be developed into its full length.

***ACTION REQUIRED:** For information and discussion.*

1 Objective of discussion

At their meeting in Almaty in October 2000, EECCA Ministers of Economy, Finance and Environment adopted Guiding Principles for the reform of the water supply and sanitation sector. They asked the EAP Task Force to monitor the implementation of these Guiding Principles and to organize a follow-up conference to review progress in their implementation, no later than 2005. The report, of which a brief description is being presented in the following, aims at fulfilling this mandate. It would present an objective description of the situation of the water supply and sanitation sector in EECCA and its diversity across different countries, as well as identifying the key areas where progress in implementing the Guiding Principles has been achieved and where more efforts are still needed. This is a first draft to generate a debate in the Chisinau meeting, and the language that is being used may not be as polished as it would be in the final version. The full background paper would be prepared by the EAP Task Force secretariat and presented at the second preparatory meeting on 6 June in London. The full paper is intended to support the Ministers discussion on these issues at the Ministerial consultations of EECCA Ministers of Finance/Economy and Environment and their OECD partners on WSS sector reform in Moscow, in November 2005.

2 Key issues

The process of municipal water sector reform in the EECCA region started in the late 1990s. The first steps were the decentralization of the water sector and transformation of water utilities into communal enterprises. These actions were taken without appropriate tariff and institutional reforms in place. The old concept of water as a purely social service was abandoned, direct subsidies to water utilities were phased-out and utilities expected to function as self-financed companies. At the time of the Almaty Ministerial conference, this “shock-therapy” appeared to have largely failed, leaving the sector in poor condition. The Almaty Guiding Principles set-out recommendations for the reforms that would need to be undertaken in four key areas: establishing strategic objectives, reforming of institutions and clarifying their roles, establishing a framework for financial sustainability, and promoting efficiency and cost-effective use of resources.

The paper starts with a presentation of the main trends in water supply and sanitation sector performance that could be gathered from about 400 water utilities in the region. It then continues to describe some of the main institutional and legal reforms that have been undertaken in the region since the Almaty Guiding Principles were agreed in 2000. This involves a description of actual reforms as well as planned reforms. It finally identifies the key inputs that would be used to draft the paper, as well as some of the questions that Ministers could address during the Ministerial conference.

2.1 *Current state of the water supply and sanitation sector*

The work carried-out by the EAP Task Force to promote and implement water utility performance indicators to monitor and manage the sector reveals that this situation has not fundamentally changed so far. While connection rates to water supply and sanitation infrastructure remain at very high levels compared to countries with similar GDP per capita levels in other parts of the world, the quality of water services that are being provided has remained at very low levels, due to the continued deterioration of the infrastructure.

- Unaccounted-for water in many EECCA countries is close to or above 50%, significantly in excess of the typical figure in the OECD of about 20%.

- Continuity of services, that means the number of hours per day where water services are available, are stagnating at an average of less than 20 hours in most countries and can be as low as 7 hours on average in Armenia.
- Pipe breaks have been increasing significantly in some countries, indicating a continuing deterioration of water networks, and remain at stable but very high levels in all other countries when compared to the OECD figures. A similar situation can be observed in relation with sewerage clogs.
- Cost recovery levels (for operation and maintenance) have deteriorated in many cases and usually remain well below 100%

A consequence of this situation is that the quality of water that is being delivered to customers has been further decreasing, forcing many people to boil water for drinking or using other purification methods. WHO indicators on water related diseases corroborate these findings by showing persistently high levels compared to OECD figures, even though the trend in some of them is slightly positive. Anecdotal information about outbreaks of diseases in the population due to contaminated water is abundant.

At the same time there have been several more encouraging developments appearing in the utility performance data, mostly relating to efforts to improve the efficiency of water utilities:

- Water production and consumption has decreased significantly in many EECCA countries, even if average consumption levels per capita remain high compared to many OECD countries. The reason for this decline is a steep increase of metered water connections, which now cover close to or more than 50% of connections in 4 EECCA countries.
- The effectiveness with which bills are being collected (expressed as average collection period), has also been improved, converging towards OECD levels in at least 3 EECCA countries, while three others have a trend in this direction.

In the rural water supply and sanitation sector the situation appears to be even more preoccupying than in towns and cities. Even though there is hardly any systematic data available, anecdotal information seems to indicate that in many rural villages and settlements public water services have completely collapsed and the population is resorting to using water from unprotected, private sources, such as wells and rivers.

2.2 Legal and institutional reforms undertaken since the Almaty Conference

While the situation in the municipal water sector is still worrying, especially in terms of the social, health and environmental impacts that it generates, there are a number of legislative and institutional initiatives that have come into force or will shortly be implemented that could help to create a basis for an improvement of the situation further down the road. At the same time there are also a number of important legal and institutional reform areas that require significant additional efforts. The following presents some of the key reform areas set-out in the Guiding Principles and tries to summarise the situation and main conclusions across the region. While these are the main messages, the full report would contain various case examples to illustrate the points that are being made.

2.2.1 Establishing strategic objectives

In several EECCA countries water supply and sanitation sector reform is an integral part of broader reform packages for the housing and communal services sector. These reform packages are usually consistent with the recommendations set-out in the Almaty Guiding Principles, but their implementation, especially at the local level has usually been very slow.

Several EECCA governments and regions have been developing financing strategies for their water supply and sanitation sectors. This has helped to develop realistic infrastructure development targets, as well as

identifying the financial and social challenges that are associated to reaching these targets. The key challenge lies in translating these analyses into the national budget planning process, as well as into the process of strategic water resource planning, which is usually carried out at the level of river basins. Armenia, with the support of the UK government and the EAP Task Force is now going to implement the results of the financing strategy that they developed into their budget process.

2.2.2 Reforming of institutions and clarifying their roles

Little progress has so far been achieved in improving the managerial and financial autonomy of water utilities. The vast majority of water utilities in EECCA are still being managed as budget entities by the municipalities, and only very few of them have established a clear definition of respective roles and responsibilities, as well as performance objectives between themselves. In many cases there are no inventories of facilities and installations, and it is unclear who the owner of these is. As a result utilities have very little autonomy vis-à-vis the municipal administration and little scope to improve their operations.

The private sector still plays a very marginal role in most EECCA countries. There are a few countries, where this has recently changed, and namely in the Russian Federation where the domestic private sector has engaged into a string of short-term lease contracts, which allows it to cover 8% of the urban population in Russia. In nearly all cases municipalities remain the owners of the infrastructure and the private sector merely operates it. While it is too early to say whether these public-private partnerships will produce positive results for water users, it is already clear that the way these deals have been awarded and the contracts drafted does often not correspond to international best practice. Also, the current legal framework in the Russian Federation makes it difficult to conclude long-term agreements and thereby prevents any major private sector investment into the sector.

A number of countries have undertaken steps to transfer the burden of social protection measures from utilities to government, mainly through the monetization of benefits, i.e. the replacement of discounted or free of charge services by monetary transfers to beneficiaries' accounts. In some cases this has met with resistance from the population concerned and it is unclear whether these reforms will be seen through. More generally, the targeting and the level of social protection mechanisms are usually insufficient and would need to be revised.

2.2.3 Establishing a framework for financial sustainability

The financial situation of the water sector still remains weak, and this is witnessed by the low level of investment that the sector is receiving both from public budgets, IFIs and private investors. There are some exceptions to that rule though as shown by EBRD's recent progress in extending its lending portfolio to the Russian municipal services sector, where it is operating with local currency loans and sub-sovereign guarantees.

Legislation addressing water tariffs has been drafted and adopted at the national level in a number of EECCA countries. This legislation aims at the elimination of cross-subsidies and the development of a legal framework that furthers the financial sustainability of the water sector (i.e. through the inclusion of the principle of full-cost recovery). This has not yet led to the elimination of cross-subsidies, nor has it succeeded in effectively de-politicizing the tariff-setting process. As a consequence the financial situation of water utilities has not been improving so far.

Efforts to address the issue of water utilities' arrears are being developed and draft laws that would allow to restructure or eliminate these arrears have been prepared in some countries. While these efforts have

been successful in some countries (e.g., Armenia) they have failed to produce the hoped for results in others. More generally, however, the build-up of arrears appears to have slowed significantly in many countries, which is to some extent due to the fact that budget organizations have been paying-up debt, and subsidies meant for the compensation of social services provided by utilities (i.e. cheaper tariffs to certain groups of consumers) have effectively been disbursed.

Financial planning capacities in utilities and municipalities remain generally weak and constitute an important impediment to the sound planning of infrastructure and business development. This has also been identified as an important obstacle to utilities and municipalities raising investment funds on capital and financial markets. The EAP Task Force, the PPC, IFIs and donors have been working with several municipalities and utilities to improve their financial planning capacities

2.2.4 Promoting efficiency and the cost-effective use of resources

In a number of countries, policies that promote the widespread use of house and apartment meters have been put in place, sometimes resulting in significant reductions of water production and consumption. A positive side-effect of these policies has sometimes been to help improve the collection rate of bills.

An important area where reform efforts have been slow or absent is on water-related standards. These have been identified as an important obstacle to the cost-effective operation of utilities and to investment, due to the excessive financial burden that they create, or simply due to their technical unfeasibility. While reform efforts are under way in several countries it is still unclear whether they will effectively address these problems.

2.2.5 Sequencing reforms

Despite the sometimes significant progress in bringing about institutional and legal changes to the water sector, the quality of services that consumers are receiving does not seem to have improved. Several factors may help to explain this apparent contradiction:

- Due to the inter-dependencies between different types of reforms (i.e. at different levels of government) some reform efforts may have been neutralized due to in-action at another level.
- Many changes have only been put in place fairly recently, and there is an important time-lag between the moment where legislation or institutional change is enacted and the moment where it is fully implemented and starts to produce results.
- Some reforms may lead to the temporary deterioration of performance before the situation starts to improve.
- The performance indicators that have been monitored may not capture some of the changes that have already occurred.

3 Relevant Task Force and Project Preparation Committee products

The following Task Force and PPC inputs will be used to develop the report:

- Survey of water utility performance indicators in 9 EECCA countries (available from the EAP Task Force website)
- Survey of water sector institutional and legal reforms in 6 EECCA countries (internal working papers), based on legal texts available in these countries

- Overview of domestic and international private companies operating in the utilities sector in the Russian Federation;
- Proceedings from three private sector roundtables jointly organised by the World Bank and EAP Task Force
- Guidelines for Performance-based Contracts between Municipalities and Water Utilities in EECCA

4 Other relevant inputs

- WHO health indicators on water-borne diseases, from WHO Health for All Database, Regional Office for Europe

5 Possible issues for discussion and next steps

Ministers could be invited to discuss the following issues during their consultations:

- Where has progress been achieved and where are additional efforts needed?
- Where should reform efforts be deployed in priority and where would international assistance be most productive?
- Are the Almaty Guiding Principles still a valid framework for sector reform?