Essential Services and Natural Resources at Risk

Selected Cases of Water Privatization in Asia

Bangladesh
Indonesia
Malaysia
Nepal
Pakistan
Philippines

Jubilee South Asia Pacific Movement on Debt and Development

JUNE 2012
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The Fourth Dhaka Water Supply project follows from three other supply World Bank-financed projects focused largely on deep tube well construction. The Dhaka Water and Sanitation Authority (DWASA) led implementation, in line with its mandate to provide tap water, sewerage and storm water drainage in Dhaka.

In the 90s, it was observed that these earlier infrastructure projects were causing the lowering of ground water table by at least one meter.

**Sectors privatized**
Revenue billing, collection, metering, meter repair, and system loss reduction-related activities

**Name of the project(s)**
Fourth Dhaka Water Supply Project

**Privatization type**
Partial privatization via management contract

**MOVES TOWARDS PRIVATIZED WATER**

The Fourth Dhaka Water Supply project follows from three other supply World Bank-financed projects focused largely on deep tube well construction. The Dhaka Water and Sanitation Authority (DWASA) led implementation, in line with its mandate to provide tap water, sewerage and storm water drainage in Dhaka.

In the 90s, it was observed that these earlier infrastructure projects were causing the lowering of ground water table by at least one meter.
annually (Hoque, 2003). Other water sector problems included aging infrastructure, high levels of unaccounted water (up to 55 percent), and financial and operational inefficiencies.

The response to this situation was the Fourth Dhaka Water Supply Project, funded through a US$ 80.3 million loan from the WB (IDA) approved in December 1996. The stated objectives of the project were: a) to commence a program of institutional reforms that would lead to efficient operation of the water and sanitation sector in Dhaka on a commercial basis and prepare a strategy to enhance private operations and mobilize private finance; b) to increase the life of existing assets and reduce water losses through a water loss reduction and rehabilitation program; c) to strengthen water resources management for the greater Dhaka area, by optimizing use of available water resources in the most economic and environmentally acceptable way; and d) to increase potable water supply in the Dhaka area by effectively utilizing available surface and groundwater resources to expand water supply in the Dhaka metropolitan area (World Bank, 2002).

Hence, in addition to the traditional infrastructure component, the project proposed an experiment of privatization involving the following services: revenue billing, collection, metering, meter repair, system loss reduction and other associated activities (Hoque, 2003).

The plan met strong opposition from employees, however, and as a result, the WB withdrew from the project, cancelling portions of the loan half a year before the scheduled closing date (World Bank, 2002). DWASA in turn did not renew the contract with EPC Ltd. and turned over its operations in Zone 4 to the EC (Hoque, 2003).

In November 10, 2007, a Partnership Framework was signed between the Government of Bangladesh and the ADB, WB, DANIDA, and the governments of Japan and Korea to scale up financing for and implement a long-term support program for the urban water supply sector in Dhaka and Chittagong. The Framework intends to “improve business strategy and financial management capacities” of the respective water authorities in these two major cities.

The following month, the ADB approved the Dhaka Water Supply Sector Development Program (DWSSDP), the first phase of the Roadmap that is part of the Partnership Framework. The ADB granted a US$ 50 million loan for urban water supply sector reform and a US$ 150 million for the rehabilitation and strengthening of the water supply system in Dhaka. The government is extending counterpart financing of US$ 62.7 million. These efforts aim for water sector-wide reforms and continue where the thwarted privatization of water services in Dhaka left off.

In December 2008, the World Bank approved a US$149 million loan for the Dhaka Water Supply and Sanitation Project. The WB called this a “reengagement” with Bangladesh, following the failed attempt to privatize DWASA. The remaining balance for the US$165.7 million, project was to be provided by the Pakistani government as its counterpart (The Bangladesh Today, 2011).

The following year in August 2009, the Parliamentary Committee of the State Owned Enterprises privatized the state-owned water bottling agency (Ahmed M. I., not dated).

GOVERNMENT AND LAWS

Mohiuddin Ahmad, in his paper Aspects of Water Privatization in Bangladesh, enumerated some of the roles of government agencies that contribute to greater private sector presence in the water sector and to implementation of full cost recovery, for example these are:

• Public water institutions will, to the extent feasible, use private providers of specific water resources services in carrying out their mandates, giving preference to beneficiary groups and organizations.

• Public water schemes, barring municipal schemes, with command area of over 5000 ha will be gradually placed under private management, through leasing, concession, or management contract under open competitive bidding procedures, or jointly managed by the project implementing agency along with local government and community organizations.
Changes in Laws and Policies

The Fourth Dhaka Water Supply Project required the enactment of the 1996 WASA Act that, among other changes, gave more autonomy to the DWASA Board, including the removal of the need for a Government’s approval in undertaking projects and securing financing (Hoque, 2003).

The National Policy for Safe Water Supply and Sanitation, adopted in 1998 became the “parent policy” that laid the ground for private sector participation. PSP-related objects of the Policy are:

- To accelerate the development of sustainable public and private water delivery systems with appropriate legal and financial measures and incentives, including delineation of water rights and water pricing.
- To bring institutional changes that will help decentralize the management of water resources and enhance the role of women in water management.
- To develop a legal and regulatory environment that will help the process of decentralization, and environmental management, and will create investment climate for the private sector in water development and management (Ahmad, 2003).

The 1998 National Policy for Safe Water Supply and Sanitation encourages direct investments and attracting private participation in the implementation of water sector agencies’ mandates. Under the section on “Policy Principles”, the role of the private sector is explained thus: “Many functions of the water supply and sanitation sector can be undertaken by private organizations. This will promote increased service coverage and thereby lessen the burden on the government. It is necessary to strengthen an administratively and financially enabling environment for the private sector to participate and contribute to sector development. Involvement of the private sector is essential to establish a closer relationship between the quality of services of the sector and its financial viability.”

As water is increasingly considered to be an economic good as well as a social good, water supply services shall be provided based on user demand and cost-sharing. In the near future concerned communities shall share at least the following portions of costs: (a) 50 percent for hand tube wells in shallow water table areas, (b) 25 percent for hand tube wells in low water table areas, (c) 20 percent for deep hand tube wells and other technologies for difficult areas.

User communities shall be responsible for operation and maintenance of water supply facilities and shall bear its total costs.

As for urban water supply, the national policy provides for private sector participation through the promotion of BOO/BOT (build, own and
operate / build operate and transfer). It adds that “[f]or this purpose, opportunities will be created for involving the private sector in billing and collection. The Government will prepare a guideline on private sector participation in the sector (Ahmad, 2003).”


INTERNATIONAL FINANCIAL INSTITUTIONS

Since 1963 World Bank has committed about US$ 1 billion to the water sector. Its four water supply and sewerage projects in Dhaka (1963, 1979, 1986, and 1996) amounted to US$ 145.5 million. ADB has provided nearly US$ 700 million since 1975. Other multilateral sources of financing include IFAD, the European Union, and the UNDP. The Government of Netherlands has been a major bilateral donor contributing more than $200 million.

Aside from financing, the WB was instrumental in crafting and enacting the WASA Act of 1996 and the National Water Policy in 1998. The ADB, as well has been involved in the sector development program of the country’s water supply and sanitation.

CORPORATIONS

A local corporation, the Engineering Planning Services Ltd. (EPC Ltd.) took part in the 1997 privatization experiment of the Government and World Bank.

Degremont (a subsidiary of Suez Lyonnaise) was involved in building, designing and operating a drinking water facility in Bangladesh.

IMPACTS

During the one year privatization trial period, the Zone managed by EPC Ltd, which is an engineering consulting firm, suffered heavily from poor service while DWASA had to bear with non-compliance with several items in the contract (i.e. it did not maintain manual consumer ledgers and files, as well as the Registers for detection of unauthorized activities, meter chamber construction, and meters withdrawn/replaced /infringed/repaired) (Hoque, 2003). Regardless of the failed outcome, the Government still had to pay for the WB loan associated with the project.

CAMPAIGNS

The proposal for the Fourth Dhaka Water Supply Project was met with heavy resistance by the unions. Through several negotiations, a compromise agreement was achieved: the DWASA Employees’ Cooperative would be assigned to Revenue Zone 5 (Tejgaon to Uttara) while Revenue Zone 4 (Mirpur) would be offered to the private sector. The Engineering Planning Services Ltd. (EPC Ltd.) won the bid to service Zone 4. The trial period is one year (1997-1998).

Performance data showed that the Employees’ Cooperative clearly outperformed the private player. The EC managed to bring down system loss to 31.88 percent from 68.32 percent while the private contractor managed to bring it down to just 46 percent from 62 percent. Billing and collection data also highlight the EC’s much better performance in revenue generation. As part of its strategy, the EC doubled the salaries paid by DWASA to amplify employees’ esteem and integrity and at the same time took advantage of the workers’ knowledge and experience through participative decision-making (Hall, Corral, Lobina, & dela Motte, 2004). The EC even extended its services to slum dwellers that were not covered by DWASA because they do not have land titles. They collected normal household
rates, which in turn augmented their revenues while effectively increasing access of water by the poor (Hoque, 2003).

Faced by the threat of losing their jobs, the DWASA employees organized and led resistance to the project. After several confrontations, the unions were able to make the Government and the WB agree to their counterproposal of allowing the Employees’ Cooperative and a private player to each operate a revenue zone of DWASA for a year, the result of which would be the basis for the further implementation of the privatization plan. In the March 2003 International Seminar on Advancing Alternatives to Water Privatization in Kyoto’s Seika University, Zaharil Hoque of Dhaka WASA presented the results of their operations:

“We started operations in 1997, by now the revenue from billing has increased three times, collection increased three times from the base either of the private operator or of the Dhaka Water Supply and Sewerage Authority in the public sector. Consumers’ satisfaction: they are happier because they get the right bill at the end of the month. Complaints attendance is much better. System loss reduction which was in the vicinity of 70% has now come down to 30 to 35% in two zones. In Dhaka, one percent system loss yearly amounts to 20 million Bangladesh Taka (Hoque, 2003).”
REFERENCES


INDONESIA

<table>
<thead>
<tr>
<th>Sectors privatized</th>
<th>Water supply</th>
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</thead>
<tbody>
<tr>
<td>Name of the project(s)</td>
<td>Private Infrastructure Development Operation: Build-Operate-Transfer and Build-Transfer-Operate</td>
</tr>
</tbody>
</table>

PRIVATIZATION MEASURES

Like many other developing countries in Asia, Indonesia inherited the system of drinking water provision (particularly in urban areas) from the colonial era. Santono cites the establishment of the public water provision bodies (Perusahaan Daerah Air Minum or PDAM) in the cities of Jakarta (1843), Semarang (1911) and Solo. From these limited services areas, the coverage of the PDAMs expanded from 1945 onwards, in the early years of independence, as part of the Public Works Department. By the 60s, the PDAMs became known as municipal water companies or enterprises (Santono, 2007).

The entry of the private sector involvement in the provision of drinking water service in Indonesia began in the 90s when the central government, burdened by an economic crisis, faced budgetary constraints. The first project was in North Serang in 1993 under a Build-Operate-Operate (BOO) scheme, followed by a concession contract in Batam Island by PT Aditia Tirta Batam (ABT) in 1996. In 1998, a similar scheme was implemented in Jakarta, with its signing of a 25-year concession.
agreement through the direct appointment of two private foreign firms, namely PT Palyja of France and PT Aetra formerly PT TPJ of UK.

There are now four concession projects in Indonesia, each respectively managed by the following firms: PT Palyja, PT Aetra, PT Adhya Tirta Batam and PT Aetra Air Tangerang. PT Aetra Air Tangerang obtained the concession contract for serving the five kecamatans not serviced yet by the PDAM PDAM Kabupaten Tangerang only in end 2008.¹

The table below provides a summary of the four concession contracts in Indonesia.

<table>
<thead>
<tr>
<th>Description</th>
<th>PT Palyja</th>
<th>PT Aetra Jakarta</th>
<th>PT ATB</th>
<th>PT Aetra Tangerang</th>
</tr>
</thead>
<tbody>
<tr>
<td>Owner</td>
<td>Suez Environment (51%) Astratel (30%) Citigroup (19%)</td>
<td>Acuatico (95%) Alberta (5%)</td>
<td>Casal BV (50%) Bangun Cipta Kontraktor (50%)</td>
<td>Acuatico Capital Inc</td>
</tr>
<tr>
<td>Population</td>
<td>4,414,993</td>
<td>4,352.566</td>
<td>850.000</td>
<td>5 kecamatan</td>
</tr>
<tr>
<td>Customers</td>
<td>371,987</td>
<td>395,253</td>
<td>136,065</td>
<td>72,000</td>
</tr>
<tr>
<td>Service Coverage</td>
<td>59%</td>
<td>66%</td>
<td>86%</td>
<td>Not yet in operation</td>
</tr>
<tr>
<td>NRW</td>
<td>47%</td>
<td>53%</td>
<td>26%</td>
<td>Not yet in operation</td>
</tr>
<tr>
<td>Investment</td>
<td>1 T (-2006)</td>
<td>1 T (-2006)</td>
<td>270 M (-2007)</td>
<td>520 M (target)</td>
</tr>
<tr>
<td>IRR</td>
<td>22%</td>
<td>22%</td>
<td>26.5%</td>
<td>16%</td>
</tr>
<tr>
<td>Average Tariff (2007)</td>
<td>7.100</td>
<td>6.400</td>
<td>4.431</td>
<td>3.500 (initial)</td>
</tr>
<tr>
<td>Regulator</td>
<td>Regulatory Body</td>
<td>Regulatory Body</td>
<td>Batam Authority</td>
<td>--</td>
</tr>
</tbody>
</table>


Since the Jakarta privatization in the late 90s, Indonesian consumers have had to suffer 10 rate hikes that now make Indonesia’s water tariffs the highest in Southeast Asia. Consumers have also reported poor water quality and unreliable service. The financial difficulties posed by these conditions for PAM Jaya, in addition to persistent reports of PT Palyja’s poor performance in terms of water quality and unreliable service, provide more than enough reason to renegotiate the contract, but as of early 2012, negotiations have not progressed significantly. PT Palyja reportedly wants tariffs tied to yearly inflation, which would mean an increase in water tariffs by about eight percent each year. It has also proposed a state-supported “investment program” and “the debt-payout of IDR 1,01 trillion (USD 113 million) by PAM Jaya or the provincial government of Jakarta”. PAM Jaya has not agreed to these proposals, recognizing the financial strain that this will bring over the life of the contract (Zamzami, 2012).

Other quarters suggest a simpler solution – termination of the contract between PAM Jaya and PT Palyja. “It is true that the cooperation agreement means PAM Jaya will have to pay penalties if the contract is terminated before the agreed due time. However, the potential loss will be much greater if the current cooperation agreement continues”. PT Palya has also been the subject of a probe by Jakarta lawyers for the alleged transfer of PAM Jaya’s assets estimated at IDR 3 billion (USD 326,000) (Zamzami, 2012).

¹ This section is lifted from History of Private Sector Involvement in Drinking Water Provision, provided by Muhammad Reza of Indonesia People’s Coalition on the Right to Water (KRuHA).

(To illustrate the process and dynamics of water privatization in Indonesia, see the briefer on page 10.)
Jakarta Water Concession

The public-private partnership scheme in Jakarta was introduced in 1994 through a World Bank loan tied with the medium term investment plan for the improvement of clean water service in Jakarta. The consultants who conducted the study was later assigned to assist the PDAM DKI Jakarta in the negotiation with two water companies, Lyonnaise des Eaux (France) and Thames Water International (United Kingdom) that have expressed their interest in Jakarta's water business. The two companies later joined to establish a joint venture with two local firms. After a protracted debate and process, the cooperation agreement was signed in June 1997 between PDAM DKI Jakarta (as First Party) and its two private partners (as Second Party). The agreement was made effective in February 1998 and later was amended in 2001 because of economic crisis that affected the foreign exchange rate.

The western zone of the concession is held by PT Palyja with 51 percent shares owned by Suez Environnement. PT Astratel Nusantara owns 30 percent while Citigroup Financial Products Inc. has a 19-percent share. For the concession in Eastern Jakarta, PT Aetra Air Jakarta is 95 percent owned by Acuatico Pte. Ltd. (registered in Singapore) and the remaining 5 percent by PT Alberta Utilities.

The Jakarta privatization project has proven to be a profitable enterprise for the concessionaires. PT Palyja’s net revenues, for instance, during the period 2004 – 2008, continually increased from Rp 560 billion in 2004 to Rp 920 billion in 2008. The net profit also showed a similar trend. Net profit of Rp 114 billion in 2004 rose to Rp 138 billion in 2008. Significantly, this increase was also accompanied by the escalation of water tariffs. From Rp 4,450 in 2004, water charges hiked up to Rp 7,020 in 2008 (PT PAM Lyonnaise Jaya, 2004-2008). The concession contract also gives the right to the holder to receive an internal rate of return (IRR) of 22 percent along with the power to collect several types of fees like the fee for using the expertise in human resource development, finance, legal, technical and management. Another example is the “know how license agreement” by Suez that gives it the right to collect a fee (4 percent of revenue up to 2004, 2.5 percent for the period 2004-2012) for the utilization of “technical expertise.” PT Palyja pays this fee to Suez.

According to the Regulatory Body, the Jakarta water tariff is one of the highest in Southeast Asia outside Singapore and Hong Kong. Since 2004 an Automatic Tariff Adjustment has been applied every six months. Using this mechanism, the private operator can propose tariff increase once every six months to the Regulatory Body for submission and approval by the Governor. Nine tariff hikes had already been applied as of December 2008. Perhaps wary of public opposition to tariff hikes, the water operators unilaterally implemented customer category adjustments which had the same effect of hiking up water bills.

The high tariffs pass on to customers, pressure on the part of the concessionaires to pay the interests on their various loans. PT Aetra Air Jakarta has loans from a number of banks and debt obligations totaling Rp 601 billion, which it used to repay its loan to Citibank (AS$ 69.5 million). Interest payments on this Citibank loan must be made by the company until 2015 (PT. Aetra Air Jakarta, 2008-2007).

PT Palyja also has debt obligations that must be repaid by 2012. Like PT Aetra, PT Palyja also took out loans to repay its loan to European Investment Bank and Calyon Merchant Bank Asia. On March 18, 2008, the company again received a loan from the Asian Development Bank worth Rp 45 billion (PT Palyja, 2007-2008).

The terms of CA agreement itself have not been met. These include targets for reducting unaccounted-for-water or Non-Revenue Water. PT TPJ/Aetra reached its NRW target briefly from 2003-4 but again fell behind its commitments in succeeding periods. On service coverage, PT Palyja managed to achieve the target in 2003 but not for subsequent years. Meanwhile, PT TPJ/Aetra achieved service coverage targets only in 2003 and 2004.
Prior to the overall revamp of the water sector of Indonesia, management of Indonesia’s water resources was governed by Law No. 11/1974 on Irrigation. In 1998, the WB extended a program loan to Indonesia for the restructuring of the water sector. Under the auspices of the National Development Agency (Bappenas) and the Ministry of Settlements and Regional Infrastructure, the Task Force for Reform of Water Resources Sector Policy or WATSAL Task Force was formed on November 2, 1998 with the WB staff.

In March 1999, the WATSAL Task Force submitted to the WB the Letter of Sector Policy, which included the WATSAL policy matrix and implementation plan. With the completion of these requirements, a US$ 300 million Water Resources Sector Structural Adjustment (WATSAL) loan from the World Bank was approved within the year.

Changes in Laws and Policies

Although the legal basis of private sector cooperation had been in place since the 90s, the legal framework to regulate private sector involvement in clean water supply provision was viewed as inadequate. At that time, the existing law to regulate private sector participation was only the Law on Foreign Investment (Law No. 1/1967 jo. Law No. 11/1970); it held that economic activities affecting the life of the majority of people, including the provision of drinking water, should not be under the operations or management of the private sector, including foreign investors.

Because of the pressing need for fresh capital and to promote favorable investment climate, in 2000 a more clearer regulation on private sector participation to addressing clean water supply provision was issued through Presidential Decree (Keppres) No. 96 Year 2000 on Closed Business and Open Business Fields. The Decree stipulates that foreign investors could own up to 95 percent of the share of the company engaged in sector development. In its development, the decree was later revised into Keppres No. 116 Year 2000.

This presidential decree, and an earlier issuance (Government Regulation or PP No. 20/1994 on the Ownership of Share in a Company for Foreign Investment) allowed foreign investors to own as much as 95 percent shares of companies doing business in fields deemed crucial to the nation’s well being, such as drinking water provision. In effect, these measures provided the legal basis to skirt the 1967 law on foreign investments that protected such critical sectors as water from private business encroachments.

To date, policy reforms adopted/implemented resulting from WATSAL are the following:

1. Water Law No. 7/ 2004 - legalization of privatization of water resources where water is considered as a tradable good with economic value; unbundling of drinking water provision industry allowing private sectors to invest in all aspects of the clean water supply and service. This law upheld the driving role of the private sector in the development of the water sector.
3. Policy and institutional reforms related to Water User Farmers Associations (WUA) - transfer of responsibilities to WUAs on irrigation operation and management financing, including divestment of public rights to collect irrigation levies in all irrigation areas.
   - Government Regulation No.77/2001 on Irrigation
   - Home Ministry Decree No.50/2001 on Water User Farmer Association Empowerment Guidelines Ministry of Settlements
   - Regional Infrastructure Decree No. 529 / 2001 on Irrigation Management Authority Transfer Guidelines to WUA
4. Policy on the provision clean water service
   - Government Regulation No.16 / 2005 on Drinking Water Provision System – removed the restriction prohibiting foreign investment in drinking water delivery and precluded private sector involvement in community drinking water supply
   - Public Work Ministerial Regulation/Public Work Ministerial Regulation No.294/PRT/M2005 on Supporting Board for Drinking Water Provision System
   - Unbundling of drinking water provision industry

5. Regionalization of PDAM - one of the objectives of PDAM regionalization is to make PDAM operate more efficiently, making it attractive and viable for business ventures

The central government role was very dominant in that it provided equity through the construction of treatment plants and distribution network and management assistance to the municipalities. For a small city with population of less than 50,000 people, the management and operation of the water supply system were to be carried out by interim water works body called BPAM (Badan Pengelola Air Minum). After the BPAM reaches cost recovery level, its status could be elevated into PDAM (Water Works Enterprise or Company, owned by the local government). All PDAMs then could have the capacity to borrow money from the bank or central government in the form of two-step loan as the water works enterprises is viewed to be bankable.

**INTERNATIONAL FINANCIAL INSTITUTIONS**

The role of IFIs in the water sector is not only evident in their respective loan portfolios but also in the development of water-related policies that were attached as conditionalities to the loans they extended. The following describes their respective interventions in the country's water sector:

**World Bank**

World Bank first made its water sector loan to Indonesia in 1968, in the amount of US$5 million for the Irrigation and Rehabilitation Project. Since then, it has funded at least 23 irrigation projects in the country. Among the largest packages released in October 1987 was a loan of US$ 234 million for the Irrigation Subsector Loan Project.

In urban water, its role became even more significant with the Urban Development Project and Five Cities Water Supply Project approved in September and October 1974, respectively. In over three decades, the World Bank has funded not less than 29 water supply projects in Indonesian cities, support for and direct participation by WB team in the preparation of the Indonesia Urban Water Supply Sector Strategy.

The concept of cost recovery was explicitly stated in the Second Water Supply Project, the main component of which was the construction of water supply facilities in several cities in Indonesia. This project was approved in 1979 and finished in 1986, and soon the concept of cost recovery was also used by other financial institutions.

In 1991, the World Bank offered a $92 million loan to PAM Jaya for the improvement of infrastructure. At the same time that this loan was approved, a Japanese OECF loan for the construction of a water purification plant in East
Jakarta also came in. These loans paved the way for the privatization of PAM Jaya.

The 1997 Asian financial crisis brought even greater difficulties to the Indonesian economy. The World Bank immediately released two loans – the Policy Reform Support Loan (PRSL) of US$1 billion in June 1998 and PRSL II of US$500 million to pursue institutional and policy reforms in the country. The PRSL II called for the restoration of Indonesian water resources management as stated in the Matrix of Policy Actions of PRSL II. This supported the 1997 recommendation for the urgent need for water sector restructuring.

Earlier that same year, the Indonesian government was offered a US$300 million program loan for the restructuring of the water sector (WATSAL) but the slow progress in meeting the above conditionalities resulted in delayed disbursement of the last US $150-million tranche.

In February 2004, the new water law was finally passed, a complete embodiment of WB’s concepts of PSP, PPP and water as an economic good. Santono and Goeltom wrote of this measure: “Law No.7 on Water Resources,...was more market friendly than Law No.11 of 1974. The new law was imposed at the request of the World Bank through the Sector Adjustment Loan for Water Resources of 1999, amounting to $300 million USD. One of the requirements of the third loan disbursement was the replacement of water resources law with a water resources policy and implementation plan in accordance with the World Bank, and based on the principle of Dublin (World Bank, 1993), which states that water has an economic value in all its competing uses and should be recognized as an economic good (World Bank, 1999) (KRuHA People’s Coalition on the Right to Water, 2012).”

The Bank’s corporate entities, the International Finance Corporation and Multilateral Investment Guarantee (MIGA), also facilitated water privatization in the country through their respective roles of providing loans and guarantees to private investors as well as providing policy advices.

**International Monetary Fund**

Deep in crisis, the Indonesian Government was compelled to enter into an agreement with the IMF for a set of macroeconomic reforms to be instituted in the country, as detailed in the Memorandum of Economic and Financial Policies within the Letter of Intent (LoI) signed in October 31, 1997. Among the reforms included in the package was the restructuring of the water sector.

**Asian Development Bank**

ADB has been working directly with several regional water municipal companies in Indonesia and is preparing a policy framework through many projects like the Reform of Water Enterprises, the Water Supply and Sanitation and the Regulatory Framework for Private and Public Water Supply and Wastewater Enterprises. The ADB extended financing through technical assistance for these efforts, amounting to US $600,000 and US $790,000 respectively.

**CORPORATIONS**

Private sector involvement in water sector in Indonesia has not been limited to local investors. There are at least four multinational corporations operating in the country either through local subsidiaries or a consortium with local investors. Below is a list of the major private players with a brief description of their involvement.

Suez (Lyonnaise de Eaux) is a French company and the largest of the major multinational water companies in the world. Its operations in Indonesia include:
1. Concession on water distribution in west zone of Jakarta through its subsidiary Palya, 1997
2. BOT bulk water in Medan through a subsidiary Tirta Lyonnaise, 2000. This arrangement is subject to take-or-pay agreement with the City Water Board.
3. BOT bulk water in Tengarang, 2001
4. BOT water service in Serang through Ondeo
5. Concession contract for water distribution through TCP
Thames Water International was UK’s largest water company, and was taken over by the German-based energy group RWE in September 2000. It holds the concession contract for the east zone of Jakarta after having colluded with Soeharto’s son, Sigit Harjojudanto.

Cascal/Biwater is an international water company which is 50-50 owned by Biwater, a private British company, and Nuon, a Dutch municipal company. It holds a concession contract for the water distribution in Batam through its subsidiary Bangun Cipta Sarana.

The operations in Batam also involve Halcrow, a UK-based private sector infrastructure specialist. Its water-related contracts include “World Bank Toolkits For Private Participation in Water And Sanitation” and “DFID Public / Private”. Halcrow’s CEO Tony Allum, is the Chair of British Water, known as the leading trade association representing the interests of the water and wastewater industry in the UK and overseas.

United Water/Vivendi was awarded a 25-year bulk water BOT contract in Sidoarjo, Indonesia.

Other Local Investors. Below is a list of local investors involved in PSP water projects.

<table>
<thead>
<tr>
<th>Investors</th>
<th>Operations</th>
</tr>
</thead>
<tbody>
<tr>
<td>PT. Noviantama</td>
<td>BOT Jambi</td>
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<td>PT. Bangun Cipta Sarana</td>
<td>BOT Palembang</td>
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<td>PT. Sauh Bahtera Samudra</td>
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<td>PT WATTS</td>
<td>BOT Cikampek &amp; BOT Samarinda</td>
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<td>PT.Kemang Pratama</td>
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<td>PT. Tirta Artha Buana</td>
<td>BOT Badung &amp; Denpasar</td>
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Source: (Santono, Guaranteeing the People’s Right to Water: A Criticism on the Clean Water Supply Policy in Indonesia, not dated)

By ADB’s own account in 2003, “the private operator concessions in Jakarta have not been too successful in investments and efficiency improvements.” To illustrate:

- Suez investment remains below target, at a $200 million shortfall in 2003.
- Suez claimed it had increased connections to 50 percent but fell short of the 70 percent target.
- In 1997, at the onset of privatization, PAM Jaya’s unaccounted-for water was at 45 percent. In March 2006, this increased further, at 53 percent for PALYJA and 55 percent for RWE-Thames.
- Water services in Jakarta’s rich middle-class and industrial areas improved but not for poor communities who have not been able to afford connection charges and remain without piped water. Under full cost recovery principles, poor communities are not prioritized for expansion because the informal tenure arrangements pose high business risks for private investors.

**On Consumers**

Various groups report that around 40 percent of Jakarta households still do not have access to piped water. The poor also pay heavy burdens of having to buy water priced between Rp 37,000 and Rp 85,000 per square cubic meter (Sihite, 2012).

Water service and quality in Jakarta also remain major concerns under the privatized set-up. In many cases, consumers still boil their water while frequent water interruptions continue to occur leaving them without water for days. Nevertheless, companies have already raised water tariffs six times, starting in February 1998. Currently, the two companies are no longer required to conduct consultations with the Parliament or the governor as they have been given authority for automatic tariff increase every six months.
On Labor

New problems were also created, such as the labor dispute concerning the welfare of water workers who were transferred or seconded to the private concessionaires. These workers received discriminatory treatment due to unclear employment status. The attendant issues resulting from this unclear arrangement include: (1) seconded workers received significantly lower salaries (about 2.5 – 5 times) compared to the workers of PDAM; (2) meal and transportation allowances did not increase since privatization and were deemed no longer responsive to current prices; (3) failure of companies to remit retirement allowances to the appointed retirement fund.

The dispute led to various protest actions and workers’ strikes, and hundreds were fired. Those who were allowed to return to work were no longer allowed to go on field since it was feared that they would influence other workers to fight for their welfare.

Debt Situation of Water Utilities

PAM Jaya’s debt situation continues to worsen. The devaluation of the rupiah resulting from the 1997 Asian Financial Crisis spelled great losses for PAM Jaya as payments for the two concessionaires were dollar-denominated. At the same time, the concessionaires’ debts are increasing and may lead to additional burdens on the part of consumers in the form of higher tariffs. “[S]ince signing the 25-year contracts with the two private companies in 1997, PAM Jaya has suffered from debts of up to Rp 1.3 trillion ($142 million). Its assets dropped from Rp 1.49 trillion to Rp 204.46 billion a 2007 audit showed (Sihite, 2012).”

CAMPAIGNS

The resistance to water privatization that began in the late 90s with the Jakarta concession agreement widened with government’s adoption of the new water law, in compliance with IFI conditionalities. KRuHA recount:

The launch of the new Law on Water Resources also gave rise to the civil society movement in the water sector, which became possible after the fall of former Indonesian President Suharto. Since 2000, discussions, seminars, demonstrations, and public debate on the law echoed in public spaces. In 2004 and 2005 three NGOs: the Indonesian Forum for the Environment (WALHI), the People’s Coalition for the Right to Water (KRuHA), and the Jakarta Water Consumers Community led the call for a judicial review of the Law No.7 of 2004 in the Constitutional Court of Indonesia.

Civil society organizations and thousands of individuals argued the Water Law contradicted the 1945 Constitution; would turn water into a profit-oriented business, and possibly threaten people’s access to water. On July 19, 2005, the Indonesia Constitutional Court upheld the constitutionality of the new water law, which provides for the decentralization of control over Indonesia’s water resources to regional entities and water-user associations, and contains provisions allowing for private sectors involvement (2011).

Muhammad Reza of People’s Coalition Against Water Privatization (KRuHA)
Photo by KRuHA
Several groups have pursued advocacy and campaigning against water privatization and defending people’s rights to essential services and natural resources. These include International NGOs for Indonesian development (INFID), Indonesian People’s Coalition for the Right to Water (KRuHA), the Municipal Water Supply Workers Union of DKI Jakarta (SP PDAM Jakatra), and the Jakarta Legal Aid Institute. Some of the initiatives of these groups are as follows:

The results of the Constitutional Court’s judicial review of Law No.7/2004 gave for the first time in its history a detailed interpretation of the law and affirming water as a public good.

The decisions of the Constitutional Court are conditionally constitutional, meaning that the implementing regulations of the law should be based on the court’s interpretation and if the implementing regulations of the law are against the Constitutional Court interpretation, people can demand another judicial review. (KRuHA (People’s Coalition on the Right to Water), 2012).

On the conflicting interpretation regarding the status of water as an economic good or a public good, the court affirmed that water is a public good with social and economic functions.

‘Considering whereas water is res commune, and therefore that has to be subject to the provision of Article 33 Paragraph 3 of the 1945 Constitution, so that the management of water has to be included in the public legal system which cannot be made as the object of ownership in the concept of civil law (Constitutional Court interpretation on Water Law No.7) (KRuHA (People’s Coalition on the Right to Water), 2012).’

Developing Alternatives to Water Privatization

INFID and KRuHA have been engaging government officials, the Parliament, multinational corporations and the IFIs on the water privatization issue. Currently, efforts are being focused on developing viable alternatives to water privatization.

Workers Campaign to Bring Back Water to Public Hands

The SP PDAM Jakarta have been actively engaging government officials and parliamentarians for a renegotiation or contract termination of Suez and Thames in Jakarta’s water, with the end of bringing back the water management of PAM Jaya to public hands. Their work includes several research studies (The Impact of Privatization on Workers’ Condition and The Impact of Privatization on the Public’s Water Service Provision), media and public information, and labor organizing.
REFERENCES


### Sectors privatized

Water treatment and distribution

### Name of the project(s)

Selangor, the Federal Territory and Putrajaya: Privatization under a Concession Agreement (PCCA)

### Privatization type

Build-Operate-Transfer (BOT) and Build-Operate (BO)

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**MEASURES TOWARDS PRIVATIZATION**

The state water works department of Selangor -- Jabatan Bekalan Air Selangor (JBAS) -- was a highly profitable public company when it was privatized in the early 90s, reportedly for purposes of efficiency. Its unbundling led to the entry of three major companies: Puncak Niaga (M) Sdn Bhd (PNSB), Syarikat Pengeluar Air Sungai Selangor Sdn Bhd (SPLASH) and Konsortium ABASS Sdn Bhd through 25-30 year concession agreements.

The state government, through its corporatized Perbadanan Urus Air Selangor Bhd. (PUAS), absorbed the loss-making distribution sector. Along with this development, new water sources were also developed -- the Selangor River Water Supply Scheme Phases 2 and 3 on on a 'build-operate-transfer' basis (Subramaniam, 2004).
Taking over JBAS in 2002 was Perbadanan Urus Air Selangor Bhd. (PUAS), the corporatized Selangor Water Management Company under the state government. PUAS assumed the functions and duties of JBAS to manage the distribution of potable water to five million consumers including industrial and commercial customers in Selangor and the Federal Territories of Kuala Lumpur and Putrajaya. As a corporatized company, PUAS purchases treated water in bulk from the concession companies and distributes this to consumers served by the water grid (Subramaniam, 2004).

These concessionaires -- Puncak Niaga (M) Sdn Bhd, Syarikat Pengeluar Air Sungai Selangor Sdn Bhd and Konsortium ABASS Sdn Bhd -- hold the responsibility for water production while PUAS takes charge of water distribution. A Regulatory Office under the State Government supervises the state water industry (Subramaniam, 2004).

PNSB in particular won the 30-year concession the Sungai Selangor Water Supply scheme. Starting in 1994, the BOT concession allowed PNSB to take over, operate, maintain, manage, rehabilitate and refurbish 27 existing water treatment plants (WTPs) formerly under the management of the Selangor Waterworks Department (JBAS). The concession expires on 31 December 2020.

In 2004, SYABAS was granted a concession for 30 years starting January 1, 2005, after which it assumed all duties and functions of PUAS. Syabas or the Syarikat Bekalan Air Selangor is a subsidiary of PNSB (News Bits, 2010).

In another state, Syarikat Air Johor Holdings Sdn. Bhd. (SAJH), a wholly owned subsidiary of Ranhill UTILITIES won a 30-year concession in 2002 to operate the waterworks of Johor, which includes sourcing, treating and supplying water. Ranhill UTILITIES is Malaysia's first fully private water company to undertake an entire water privatization exercise, handling water from source to tap. The A wholly privatized set-up, Johor's water utility differs from the case of Selangor whose corporatized water utilities remain under majority public ownership but have private investors participating.

Water treatment and distribution has been fully privatized for the states of Johor and Selangor, the Federal Territory of Kuala Lumpur and Putrajaya.

Under the concession agreement between the Federal and state government of Selangor with Syabas, the water concessionaire for Selangor, Kuala Lumpur and Putrajaya, the following conditions will be complied with by the government until 2029.

- A tariff formulae which protects its downside risk;
- Cash compensation if the Government disallows it to raise the water tariffs;
- Financial support of RM2.9 billion from the government;
- Starting with a clean slate, no assumption of liabilities and unpaid receivables prior to 31 Dec 2004.
- Financial assistance [to concessionaire] by the Federal Government (Total RM2.9 billion)
- Repayment of receivables owed to water treatment concessionaires to be paid in 5 equal installments over 4 years –RM1335 million (RM1.3billion)
- Grant for non-revenue water works RM250
- Financing to Syabas for capital works (via preference shares) RM655 million
- Loans by Bank Pembangunan to Syabas RM410 million
- Loans by Bank Pembangunan to Syabas for NRW works RM250 million (MTCU and CAWP 2006)

In December 2008, the Selangor government reportedly wrote to the Ministry of Energy, Water and Communications to seek the termination of Syabas’ Concession. This move came after the National Audit Department got unsatisfactory results from two national audits into the concession’s performance. One of the issues raised was that "Syabas had spent RM1.8 billion more than the approved allocation to expand its capacity apart from the RM80 million it had
already spent on refurbishing the offices and for purchase of vehicles (Santiago, 2009).” The decision to buy back the Syabas water utility concession, not to mention five water treatment projects, proceeded from government’s conclusion that the concession contracts “[made] water supply in the state too expensive and unsustainable (The World Bank Group, 2009).”

GOVERNMENT AND LAWS

The government pursued the water privatization in Selangor without benefit of public consultations. As feared by civil society groups, water tariffs began to increase. In October 2006, Syabas raised water rates by 15 percent saying that it had decreased non-revenue water (NRW), by five percent. The Malaysian Trades Union Congress (MTUC) and 13 others asked to be furnished copies of the CA and audit report from the energy, water and communications minister but this was turned down by Minister Tun Dr Lim Keng Yaik, who invoked their confidentiality.

In a statement released by the MTUC and the Coalition Against Water Privatisation (CAWP) at the Parliamentary Select-Committee Hearings on Integrity in February 2006, they pressed for disclosure and pointed out:

On the 15th of December 2005, the Federal government of Malaysia, represented by the Economic Planning Unit, the implementing agency, the Ministry of Energy, Water and Communications (KTAK) and the Selangor state government signed a Concession Agreement that involves the taking over of PUAS by SYABAS in the distribution and supply of treated water to all consumers covering Selangor, Kuala Lumpur, and Putrajaya.

However, the Concession Agreement between the Federal government, the Selangor state government and Syabas (70% owned Puncak Niaga Sdn. Berhad) was done in secret although it involved a very important resource – water, as the public did not have any knowledge of it. In fact, the Minister, YB Lim Keng Yaik [then Minister of Energy, Water and Communications] had earlier promised that there would be no privatization (emphasis supplied) (Malaysian Trade Union Congress (MTUC) and Coalition Against Water Privatization (CAWP) Statement at the Parliamentary Select-Committee Hearings on Integrity Held at the MPPJ on 20th February 2006.

The Malaysian High Court ruled that the documents must be made public. According to Judicial Commissioner Hadhariah Syed Ismail, “In this area, where transparency, accountability and priority are given to the needs of the rakyat, it is only fair that the concession agreement be made public. I am of the view that courts should lean in favour of aggrieved parties in matters involving public interest (Hadhariah as cited in Jo-Ann, 2011).”

However, the federal government filed an appeal and the earlier decision of the High Court was overturned on the basis of lack of standing of MTUC and 13 other applicants, or that they could not establish a right to to the documents. “Dissenting Court of Appeal judge Datuk Mohd Hishamudin Mohd Yunus had a different take on the issue from his two colleagues. He said that because water was a basic necessity of life, any increase in tariffs would have an important impact on lives. As such, the process of determining water tariffs had to be transparent and the public had a
legitimate expectation to know the process involved in setting tariffs (Jo-Ann, 2011)."

Changes in Laws and Policies

The Government underwent a restructuring of Malaysia’s water sector. In March 2004, water, together with other public utilities, was placed under the purview of the Ministry of Energy, Water and Communications. The restructuring was also supported by the Government’s Ninth Plan covering the period 2006-2010.

As a result, two laws were enacted in 2006: the Water Service Industry Bill 2006 and National Water Services Commission Bill 2006. These laws provided for the regulation of the water supply industry. They transfer control of water from the various states to a federal-level regulatory authority.

Moreover, a new national water assets management company Pengurusan Aset Air Berhad (PAAB) was set up to buy up all existing water infrastructure.

Among the major effects of the restructuring were the transfer of control over and regulation from the states to the Federal government of water supply and sewerage services. Likewise, water supply and sewerage services would now be jointly regulated.

The National Water Services Commission Bill established the commission Suruhanjaya Perkhidmatan Air Negara (SPAN) which would supervise and regulate the water supply services and sewerage services and enforce the water supply and sewerage services laws.

SPAN is tasked to oversee, regulate, monitor and maintain uniformity in the country’s water sector, addressing issues such as poor water quality, no supply, a loss in earnings due to non-revenue water via leaks, water thefts and unpaid bills and the disparity in tariffs among states and poor enforcement.

This Water Services Industry Bill, on the other hand would establish a licensing and regulatory framework for regulatory intervention to promote the national policy objectives for the water supply services and sewerage services industry.

INTERNATIONAL FINANCIAL INSTITUTIONS

March 2005, Malaysian government signed a loan accord (soft/low interest loan) for RM2.41bil with JBIC for the Pahang-Selangor Raw Water Transfer Project. The Government can only activate the loan after completing the pre-qualification and tender process. The project has been delayed for more than a year due to various setbacks but a lot of progress has been made of late. The Pahang-Selangor Raw Water Transfer project involves developing water resources in Pahang and constructing a 45km tunnel to transport water to Selangor. The loan would then be used to build the water transfer tunnel, dam, and related works and for consulting services, including detailed design and implementation supervision.

CORPORATIONS

Selangor, the Federal Territory of Kuala Lumpur and Putrajaya: The water treatment business was handed over to PNHB (Puncak Niaga Holdings Bhd) in 1996 and later to SPLASH (Syarikat Pengeluar Air Sungai Selangor Sdn. Bhd.), and KASB (Konsortium Aliran Bekalan Air Selangor Selatan Sdn. Bhd) while the water distribution aspect was given to SYABAS (Sdn. Berhad Syarikat Bekalan Air Selangor Sdn Bhd) in 2004, which is 70% owned by Puncak Niaga Sdn. Bhd. (PNSB) and 30 percent owned by Kumpulan Darul Ehsan Bhd. (KDEB), a Selangor state government subsidiary.

Johor, in 2000, the treatment and distribution of water was fully privatized under Air Johor Holdings Sdn. Bhd. (SAJH), a wholly owned subsidiary of Ranhill Utilities.

A major private player in the corporatization of the public utility in Selangor is PNSB. Selangor's water management facility, Syabas, is reportedly “70 per cent owned by Puncak Niaga Holdings Bhd, which is in turn 41 per cent controlled by
Puncak Niaga executive chairman Rozali Ismail”. Puncak Niaga’s Annual Report for 2008 also reports that, “directors’ earnings for the Puncak Niaga group totalled RM11.6 million for the year with the highest paid director earning more than RM5.7 million (Netto, 2010).”

IMPACTS

Since Malaysia suffered a water crisis in 1998, there has been an increasing number of complaints (mostly related to water distribution) received by PUAS from its customers. Averaging 7,500-8000 per month, these complaints include “frequent water disruptions, low pressures and also unsatisfactory water quality”. More homes are also installing water filters, indicating the dissatisfaction with the water quality. Other issues pertain to “uneven distribution, high non-revenue water losses, customer service and financial and manpower problems (Subramaniam, 2004).”

In terms of finances, Subramaniam (2004) writes that PUAS Bhd “...is presently facing a huge financial deficit in excess of RM400 million a year. This is mainly because of the high cost of purchasing water from the water producers, and the revenue from the sale of water is barely sufficient to pay for the purchase of treated water. Hence, it is very difficult to meet other operating, administration and maintenance expenses, let alone financing development projects, asset replacement or system improvement and development works.”

In 2010, Syabas demanded RM339 million from the Selangor government after it refused to increase water tariffs the previous year. Government stood its ground, pointing to violations of the CA (Netto, 2010). These included:
- Awarding 72 percent of contracts worth RM600 million [US$180m.] without open tender;
- A discrepancy of RM325 million [US$97.5m.] between the summary of contracts awarded in 2005, 2006 and 2007 and Syabas’ review document;
- Spending RM51.2 million [US$15m.] to renovate Syabas headquarters, despite Selangor Water Regulatory Department (JKAS) approving only RM23.3 million for the exercise
- Syabas’ decision to source RM325 [US$97.5m.] worth of pipes from Indonesia instead of locally in 2005, in breach of finance ministry instructions.
- RM5.1 million [US$1.5m.] paid in allowances to its chairman Rozali Ismail (the 32nd richest man in Malaysia)
- Syabas has a management fee agreement with its parent company Puncak Niaga. Syabas has to pay Puncak management fees, amounting to RM8.4 [US$million annually and RM32 million [US$9.6m.] since 2005
- Tariffs charged by Syabas are RM0.77 per cubic meter, more than double the amount of RM0.37 charged by the public sector water operator in Penang State (Hall, Lobina, & Corral, 2010)

Impacts on Consumers

Water consumers suffered these impacts of privatized water:
- Increase in water tariffs by 15 percent - RM100mil in pre-tax profits and delayed announcement resulted in a RM125mil penalty
- Increase in water disconnections - breakdown of suspended accounts after privatization: 257,436 are home consumers, 106,100 industrial consumers and 664 miscellaneous consumers out of 1.5mil consumers (24% of total number of consumers in Selangor and the two Federal Territories). Total amount of disconnections after privatization: 364,200 consumers. Total number of disconnections in 2006: 178,000 compared to 79,574 in 2005. Syabas makes a profit of RM18.2mil in reconnecting water supply.

CAMPAIGNS

The Coalition Against Water Privatisation (CAWP), or Pakatan Membantah Penswastaan Air is a movement of 127 different NGOs, environmental
groups, trade and labour unions, consumer associations, religious bodies, residents associations, and human rights defenders working on campaigning against the privatization of water in Malaysia (Monitoring Sustainability of Globalization, not dated).

In 2005, CAWP presented a Memorandum to the Government and urged it to adopt a public-public partnership model, similar to the case of the state of Penang (PBA). This was supported by a protest outside of Parliament to voice concerns over the privatization of the country's water supply.

The following year, the Prime Minister, through a Memorandum was asked to intervene in matters concerning the country's management and distribution of water and to investigate SYABAS' claims to a tariff increase. In particular, CAWP was lobbying to exclude concession agreements from the Official Secrets Act and thus be made public, as it “does not contain any information to national security or any sensitive issue relating to race or religion (Coalition Against Water Privatization, 2006).”

CAWP also demanded transparency about the audit report on NRW and whether the 15 percent tariff increase awarded to SYABAS after having reduced NRW by just 5 percent was justified. It also went to court after filing a Judicial Review against the Selangor State Government and the Federal Government, requesting the details of the Auditor-General’s report on NRW and the concession agreement be made public. The High Court eventually granted leave to seek judicial review.

The Coalition is also involved in conducting seminars, workshops, dialogue sessions, consultations, awareness programs, capacity building to empower groups opposing water privatization. It is also currently developing a training manual on the Human Right to Water. In 2007, a high level discussion on the “United for Water: Religious Perspectives on the Rights to Water” was held, in conjunction with the country's 50th year of independence celebrations.

In March 2009, MTUC and CAWP expressed its full support to the Selangor state government in its persistent attempts to bring back privatized water services to public hands.
REFERENCES


The Melamchi Water Supply Project (MWSP), a major inter-basin river project approved in December 2000 projected solving the water shortage in Kathmandu by diverting 170 million liters of water per day (MLD) from the Melamchi River to Kathmandu through a 26.5 kilometer tunnel for treatment and distribution in Kathmandu Valley. In addition, it claimed that it would benefit the health and well-being of about 2 million inhabitants in the capital (NGO Forum on the ADB, 2008).

The initial total project cost was estimated at USD464 million, but the approved financing plan reached more than US$534 million. (See table on next page)

However, due to various reasons that included the political instability of the country at the time, the World Bank, SIDA, NORAD and ADB withdrew

### PRIVATIZATION MEASURES

<table>
<thead>
<tr>
<th>Sectors privatized</th>
<th>Water supply and wastewater services</th>
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<tbody>
<tr>
<td>Name of the project(s)</td>
<td>Melamchi Water Supply Project (MWSP)</td>
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<tr>
<td></td>
<td>Kathmandu Valley Water Services Sector Development Program (SDP)</td>
</tr>
<tr>
<td>Privatization type</td>
<td>Management Contract (Performance-based)</td>
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</table>
Essential Services and Natural Resources at Risk: Selected Case

from the project in 2002 (NGO Forum on the ADB, 2008). These turn of events resulted in a financing gap of US$133 million, which prompted the ADB to come up with a revised financing plan and split the project into two, the Melamchi River Water Diversion Project and the Kathmandu Valley Water Supply and Sanitation Project. Under the adjusted financing plan, ADB provided US$137 million, JBIC, US$47.5 million, NDF, US$10.5 million, OFIC, US$13.7 million and JICA, US$18 million.

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<thead>
<tr>
<th>Melamchi Water Supply Project</th>
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<tbody>
<tr>
<td>ADB</td>
<td>US$120 million</td>
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<tr>
<td>World Bank</td>
<td>US$80 million</td>
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<tr>
<td>JBIC</td>
<td>US$52 million</td>
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<tr>
<td>JICA</td>
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<tr>
<td>NORAD</td>
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<tr>
<td>SIDA</td>
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<tr>
<td>NDF</td>
<td>US$9 million</td>
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<tr>
<td>OFID</td>
<td>US$14 million</td>
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<td>Government of Nepal</td>
<td>US$188</td>
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Another big project, the Kathmandu Valley Water Services Sector Development Program was designed as a follow-on program to institute reforms and introduce private sector participation through a performance-based management contract in water supply and wastewater service delivery in Kathmandu Valley. ADB financed this program with a US$15 million loan.

Reforms included restructuring of the Nepal Water Supply Corporation (NWSC), a government corporation responsible for water supply and sewerage for Greater Kathmandu and 11 other towns. ADB boasted that these institutional reforms were unprecedented in the entire South Asia region (Asian Development Bank, 2008). Also, new organizational substructures for the operations of the Kathmandu Valley operations were created:

- the Kathmandu Valley Water Supply Management Board (KVWSMB), asset owner of water and wastewater systems within Kathmandu;
- the Water Supply Tariff Fixation Commission, responsible for the economic regulation of the sector; and,
- the Kathmandu Upatyaka Khanepani Limited (KUKL), in charge of operating the assets under lease and license from KVWSMB

**GOVERNMENT LAWS**

**Changes in laws/ policies**

The 2002-2007 Poverty Reduction Strategy Paper of Nepal has as one of its targets “[making] basic drinking water services available to 85 percent (from 72 percent) of the population”. Several of the implementing strategies given “policy emphasis” clearly support water privatization, such as “cost recovery in the operation of drinking water supply (DWS) projects,...and involvement of private sector in the development and management of water supply system in urban areas (Nepal National Planning Commission, 2005).” These policy directions evidently underpin the changes in legislation related to the water sector.

In December 3, 2006, the Parliament passed a resolution to amend the Water Act, paving the way for the privatization of the NWSC. Then in January 2007, the House of Representatives passed the Nepal Water Supply Corporation (third amendment) Bill 2006. Amending the Nepal Water Supply Corporation Act of 1989, this measure reportedly “[changed] the present structure of the Nepal Water Supply Corporation (NWSC) by handing over the entire management that supplies drinking water in the Kathmandu Valley to private sector based on compulsory condition put forward by the major donor agency of Melamchi Water Supply Project, Asian Development Bank (ADB)”. Arrived at through a political agreement among the parties in Parliament, the bill passed into law. Minister Gopal Man Shrestha was reported as “[ruling] out any possibility of amending the Nepal Water Supply Corporation (Third Amendment) Act passed by the recently dissolved parliament”. Within the same month, the government handed to a British firm, the Severn Trent Water International, the management of
drinking water in Kathmandu for a period of six years (NGO Forum for Urban Water and Sanitation, not dated).

**INTERNATIONAL FINANCIAL INSTITUTIONS**

The World Bank and the ADB have significant presence in the water sector of Nepal.

For example, the International Development Association (IDA) of the WB group extended loans for the following projects which enable private sector development:


With the WB’s withdrawal from the Kathmandu Valley Water Services Sector Development Program, the ADB stepped in to help prepare a five-year management contract. It subsequently approved US$137 million (revised in 2005) for MWSP and US$15 million for the Kathmandu Valley Water Services Sector Development Project. ADB further mobilized considerable amounts of co-financing from other institutions for the costly MWSP. (See preceding section).

The ADB has continued to pour in money in technical assistance grants to support capacity-building of the newly created institutions. Consistent with its water policy strategy, the ADB TAs contribute to promoting private sector participation. Among these are:

- Enabling the Private Sector to Undertake Poverty-Focused Water Distribution and Strengthening of Institutional Reforms in Kathmandu Valley - US$150,000 (2006)
- Preparing the Improved Water Quality, Sanitation, and Service Delivery in Emerging Towns Sector Development Program - US$720,000 (2007)

When the contract award to a private company, UK’s Severn Trent Water International (STWI) was not immediately granted in 2007, due to the withdrawal of other bidders wary of Nepal’s political crisis during that time, the ADB successfully pressured the Nepal government thus:

Immediately, the ADB issued an ultimatum of terminating their loan agreement in the event of government’s non-appointment of STWI by May 15. It blackmailed the government saying that “without appointment of a private management contractor, there will be no ground to persuade extension of the funding commitment.” However, Yami [Minister for Physical Planning and Construction
Hisila Yami found support in a number of mass movements in Nepal who endorsed her decisions on the grounds that water was too precious and too basic a human right to be placed at the mercy of multinational companies whose primary goal is to maximise profits at the expense of the deprived and downtrodden. They also felt that water needs to be protected from predatory capitalist promoters, like the ADB, who forces privatization as a pre-condition for loans to developing countries. Inevitably, water then becomes more expensive and the quality drops contrary to higher quality claims by the so-called experts and promoters. It's the common people, especially the poor who then suffer as the soaring water price makes it impossible for them to afford the otherwise widely and easily available natural resource.

On May 22, 2007 the ADB finally washed its hands from the project and finally said that it was impossible to take the $500 million project to its logical conclusion because the government has not given the contract to manage water supply to the STWI as suggested by the bank (Dhar, 2007).

ADB later on lent Nepal $77 Million USD for improvement of Kathmandu Valley's water supply. Reported as the “main goal” of the project was to complement government efforts at ensuring adequate and reliable water supply to Kathmandu consumers. The loan supports continued work on the Melamchi Water Supply Project (Osaka News, 2011).

CORPORATIONS

Several big corporations are involved in the privatization of water services in Nepal. One of the most hotly contested was the granting of the management of Kathmandu’s drinking water supply to STWI, the sole bidder in this undertaking. The withdrawal of three other bidders in the management of the Kathmandu Valley’s drinking water, left Severn Trent Water International (STWI) as the sole bidder and eventually the recipient of the US$8.5 million contract to manage Kathmandu’s water supply for six years. This raised opposition, with questions raised on “the legality of selecting a single bidder and the lack of competition”. Government’s response was to “[insist] on STWI’s ‘foreign expertise’ over the local capacity of ameliorating public water supply. However, STWI record elsewhere in the world had not been as authentic as portrayed by government. In February 2007, the government of Guyana cancelled a five-year water management contract with them citing the company’s failure to meet the principal objectives in the contract (Dhar, 2007).”

This appointment of STWI was opposed in May 2007 by Minister for Physical Planning and Construction Hisila Yami who then postponed awarding the contract, saying that the matter needed to be reviewed in order that alternatives can be discussed. ADB quickly responded, warning government of a possible cancellation of its loan for the MWSP. (See preceding section).

Another private firm that has failed to live up to its commitments is the Kathmandu Upatyaka Khanepani Limited (KUKL), which is the “private-partnership company” created in February 2008 “to replace the Nepal Water Supply Corporation as a pre-condition to get funding from the Asian Development Bank (ADB), the major donor for the Melamchi Water Supply Project”. In 2009, it figured in several reports of irregularities:

First, Kathmandu Upatyaka Khanepani Limited (KUKL) was not able to spend its allocated annual budget of Rs. 48 million meant for improving water supply infrastructure, and is now asking the government to reallocate the remaining budget in other areas such as voluntary retirement schemes. Earlier, Kathmandu Metropolitan City (KMC), which holds 30 per cent shares in KUKL, had raised questions about the utility’s extravagance on monthly “meeting allowances” and failure in delivery.

Second, local residents in Kaldhara found out that KUKL staff had organised an
unscheduled water delivery one day at midnight while only informing their relatives about it. Kaldhara residents get water only once every 5 days.

Third, former project staff and other government officials, including Former Prime Minister Girija Prasad Koirala, have been accused of unauthorised use of eleven expensive vehicles belonging to the Melamchi Water Supply Project. In some cases government registration plates have been replaced by private ones. Meanwhile the project is spending Rs. 0.3 million a month on hired vehicles for its consultants (WASH News Asia and Pacific, 2009).

**IMPACTS**

**Melamchi Water Supply Project**

Hundreds of indigenous fishermen, traditional water mill owners, and small farmers rely on the water of Melamchi River for their survival. Once water gets diverted to the Kathmandu Valley, these groups will be displaced and lose their source of livelihood.

Residents also complained that they were not given the approved compensation rate of 1,200 Nepalese rupees (Rs) for each fruit plant and Rs 600 for every regular plant damaged during project implementation. Instead they only received a flat rate of Rs 600 regardless of plant type. Further, there was a lack of appropriate resettlement and compensation package and benefit-sharing provisions for affected farmers.

As for water consumers, it is they face potential tariff increases of five to ten times more than the old price once the Melamchi water reaches Kathmandu Valley. One study cites estimates of consultants of “a thirteen-fold increase of the water tariff between 1999 and 2009...to meet the operation cost of the water network and achieve financial equilibrium (Domenech, March, & Sauri, not dated. Citing Jeffrey, 2000 quoted in Etherington et al, 2003).

The environmental impacts of the project were also of significant magnitude. These ranged from irreparable damage to the ecology and increased soil erosion to irrigation problems in the Melamchi Valley. Domènech et al. (not dated) wrote also reported these impacts:

- The construction of access roads, the diversion tunnel and other infrastructures associated with the project have directly affected 2,935 private land parcels (MWSP, 2009). Futhermore, the supplementary Environmental Impact Assessment (EIA) report of the Melamchi Diversion Scheme (MWSD, 2001: ES 5) states regarding the diversion of a maximum of 1.97 m$^3$/s that “without any mitigation measures, the Upper Melamchi will experience a significantly reduced flow throughout the year and a severely reduced flow in the dry season”. The environmental flow of the river has been estimated at 0.4 m$^3$/s but this flow seems insufficient to guarantee water related activities such as irrigation, fishing and the operation of water mills (CPAD and IWMI, 2006)

- Initially only 14 Village Development Committees (VDCs) with around 40,000 people from Sindhupalchok District were declared affected areas. In 2007-08, after two years of protests, 5 VDCs more from Kavre district succeeded in their claims and were also declared affected areas. In total, 19 VDCs
are considered project affected areas (Domènech, March & Sauri, not dated).

**CAMPAIGNS**

Many groups resisted water privatization in Nepal and continue to do so against increasing private sector participation in other water projects, such as hydropower. These include:

- Consumers Interest Protection Forum
- Melamchi Local Concern Group (MLCG) – composed of Melamchi’s local citizens
- National Concerns Society
- Nepal Drinking Water Corporation (NDWC) / Nepal Water Supply Corporation
- Nepal Federation of Drinking Water Supply & Sanitation
- NGO Federation of Nepal
- The NGO Forum for Urban Water and Sanitation - a federation of NGOs in Nepal that conducts research on water-related issues, people’s participation in the control and management of water services and possible alternatives to the privatization scheme.
- Rural Reconstruction Nepal (RRN)
- The Water and Energy Users’ Federation-Nepal (WAFED) - filed a case in the Supreme Court to challenge the Nepalese government’s decision to privatize water

Water rights activists and affected community groups filed a complaint on ADB’s accountability mechanism in May 2004, citing noncompliance by the bank of its own policies in the Melamchi project implementation. The complaint invoked provisions on access to information; Environmental Impact Assessment; land acquisition, compensation and resettlement; Indigenous Peoples; Social Uplift Program; Agriculture; and Forestry. In July 2005, Norway pulled out of the project, citing developments after the February 1 Royal takeover as “a serious setback to multiparty democracy, constitutional monarchy and human rights” (“Nepal: Norway cuts bilateral aid (IRIN Humanitarian News and Analysis, 2005).”

Nepali locals and Kathmandu-based NGOs filed a case of corruption against the project officials at CIAA. In July 2005, Nepal’s former Prime Minister, another minister and Melamchi project officials were convicted of corruption and received a two-year jail sentence. The Swedish International Development Agency formally terminated its commitment in 2006.

In March 2007, a Joint Review Mission of project donors agreed to scale down the costs for the Melamchi Water Supply Project from US$464 million to $350 million, raising serious concerns about the original estimates. Earlier scheduled to be completed by 2006, the project will go beyond 2011. Although the delay in project implementation can be considered a short-term success for the water justice advocates, some argue that this is favorable to the government in terms of seeking possible increase in funding.

As for the privatization of the NWSC, the combined efforts of the activists and workers union successfully launched a campaign and booted Severn Trent out of the bidding process in May 2007. One tactic used was to expose the company’s dismal performance in other countries, such as in Guyana where it failed to meet five out of the seven objectives of its five-year water management contract. The said deal was cancelled by the government of Guyana in February 2007. Also, in 2008, the campaign was able to make ADB remove the requirement to award a private sector management contract to support the new utility as a precondition for awarding the tunnel civil works contract.

Workers also demanded from the Nepalese government that the participation of NWSC employees and consumers in management decisions be ensured, particularly on structural changes of the corporation. Workers are essential partners in the improvement and delivery of quality public water services.

Water justice advocates and even scholars outside the network of activists have put forward several alternatives to Nepal’s water problem. According to these groups, the failures of state-run models cannot necessarily be corrected through private
sector participation. Governments entertaining private sector participation in their water sector—a scheme largely pushed by international financial institutions—should look into other alternatives especially people-owned models. The role of Kathmandu Valley’s five municipalities and community based enterprises in water supply should also be strengthened.

In her paper, “Nepal Water Privatization: Role of ADB and PSI’s Call for Quality Water Services and Public Water Management”, author Violeta Corral stated:

“Public water management is still the solution, with reforms put in place to support the autonomy and efficiency of public water operators. NWSC has been saying that it had not been given any chance for reform, or to perform autonomously. … What Kathmandu needs is public investment in its water supply and management - to cut the leakage rate and upgrade the water supply network served by many small local rivers and springs and ponds. Nepali water experts argue that just upgrading the ageing water mains and cutting back on leakage would augment supply by anywhere between 40 to 70 percent. International donors had been quick to dismiss other cheaper and more appropriate options such as proper groundwater re-charging and collection; rainwater harvesting; constructing shallow tube well; rehabilitating hand dug well and traditional stone spouts; improving billing collection efficiency and cross checking for proper metering. Construction of reservoirs on the Kathmandu Valley rim to store monsoon runoff is much less expensive than drilling a long tunnel. Finally, the collaboration of NWSC and Kathmandu Valley’s municipalities in ‘public-public partnership’ (PUP) schemes should also be explored, where the provisioning of water remains a social good and controlled by a transparent, accountable and participatory public rather than viewed as a source of profit (Corral, 2007).”
REFERENCES:


One of the earliest signals of water privatization in Karachi was the establishment in 1981 of the Karachi Water Management Board (KWMB). It was “assigned responsibility for water distribution throughout the metropolitan area and was given enhanced powers of cost recovery”. This was followed in January 1983 by the Sindh Government’s enactment of the Sindh Local Government (Amendment) Ordinance of January 1983, creating within the Karachi Metropolitan Corporation (the distribution and retailing facility), the Karachi Water and Sewerage Board (KW&SB). The KW&SB was thereafter placed in charge of the water supply and sanitation services in Karachi (WB December 2010).

Water privatization in Pakistan began to intensify starting with the setting up, upon the World Bank’s advice, of the Privatisation Commission in 1991. Two World Bank missions in 1994 and 1995 presented the Sindh government a blueprint for

### Moves to Privatize Water

<table>
<thead>
<tr>
<th>Sectors privatized</th>
<th>Water supply and sanitation services</th>
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| Name of the project(s)              | Karachi Water Supply Project (1983 and 1993)  
| Privatization type                  | Restructuring the Karachi Water and Sewerage Board |
the privatization of the Karachi Water and Sewerage Board (KWSB). Further, WB assigned Banque Paribas as head consultant and submitted its report to the Sindh Government (Hasan 2001).

KWSB’s responsibilities included bulk water supply arrangements from the source; provision of retail water supply connections to consumers; undertake operation, maintenance and construction of water and sewerage works; collect water and sewerage charges from the consumers; undertake forward planning for emerging needs and requirements; impose penalties on defaulters; maintain accounts and records of the Board and prepare tariff proposals to Karachi Metropolitan Corporation (KMC).

By the mid-90s, KWSB was suffering from huge debts, a net loss of 35 percent, and collection rate of only 7 percent. Noting these problems, the World Bank advised the Government to initiate a private sector participation strategy (PSP) in 1994-95. Soon a World Bank mission on water and sanitation visited Karachi to hold discussions with the Chief Minister of the Sindh government and offered support to the provincial government for exploring the possibility of a PSP solution to Karachi’s water problems.

In January 1995, the World Bank presented a blueprint for radical reform of Karachi’s water and sanitation sector with PSP as the focal theme. The WB suggested a shortlist of eight leading international organizations possessing vast experience in water sector privatization for consideration of the Sindh government. The WB also brought the Chief Minister, senior officials of the government and the KWSB to a PSP seminar in Paris in June 1995. For 1995-1996, PSP in water sector was made a top priority.

The resulting privatization strategy of the KWSB was formulated by consultants from the Paribas-Halcrow consortium (NGO Forum on the ADB, 1998). Its recommendations include handing over all assets of KWSB to the private sector free-of-charge as a “concession” for at least 20 years. Some of the major issues surrounding the plan were:

- the absence of an oversight body except the Sindh legislature by default and a provincial regulatory authority.
- no specific targets for improvements in water delivery before privatization, increase of 30 per cent in tariffs and planned annual increases by 20 percent (or a cumulative increase of 300 percent by the fifth year of privatization for all consumers, rich or poor, domestic or commercial.
- layoffs of water utility staff -- 1,500 before privatization and another 4,000 after.
- less than 10 percent in private equity finance for rehabilitation and expansion. The bulk of investments were to be financed by additional international agency loans and rapidly increased revenues through a 3000 percent real increase in tariffs and doubling of collections.
- renegotiation of commitments after five years
- no imposition penalties for failure to meet targets
- self-assessment by the operator to measure service levels (NGO Forum on the ADB 1998).

Hasan writes: “All the suggestions made by the World Bank were based on the conclusions from the Paribas consultancy report (Paribas, 1997). These were approved by the Government of Sindh with only minor modifications, despite the fact that the terms of privatisation, as stated by the consultants and accepted as the basis on which privatisation was to take place, were blatantly to the benefit of the private operator. Moreover, they provided no guarantee or targets for the provision of water and sanitation services to the Government of Sindh or to the people of Karachi. The Paribas consultancy report nevertheless became the handbook for the privatisation of KWSB and it is in line with its conclusions that the conditions for the denationalisation of Karachi water and sewerage services were submitted to the Government of Sindh.”

Quoting the Paribas consultancy report, Hasan notes these “Requirements for Implementation:“

1. The Government of Sindh must agree to fully transfer management responsibilities to the
private operator and to set up an independent regulatory system. Based on such an agreement, the Consultants will assist on drafting the appropriate legislative changes.

2. The Government of Sindh must make a decision on the tariff increase to be implemented mid 1997. The 1997 increase should not be less than 30% in real terms and a 20% annual increase in real terms are required in the first five years of PSP.

3. The concept of making available to the operator a revenue subsidy, aimed at providing him with a minimum return on investment in the short term must be agreed.

4. The Government of Sindh must agree not to transfer the outstanding liabilities of KWSB to the private operator.

5. The Government of Sindh must agree to grant a corporate tax exemption to the concession company. (Paribas, 1997, p. 64)

Civil society groups, workers, and activists strongly vigorously opposed the proposal, causing the Sindh High Court (SHC) to rule that “such a vital and sensitive institution cannot be placed in private hands (Shah, 2004).” In 1999, the SHC ordered the process suspended and formed a committee to look into the matter. The body found “No firm guarantees for identified improved services...no clear legal guarantee of minimum quality standards” on the part of the operator, despite the Government of Sindh’s financial guarantees; “very little of emphasis on improvement of the sewerage system, perhaps because it does not yell [sic] substantial profits.” The lack of attention towards the fate of the Katchi Abadis and the unrealistic price hike. It also underlined the problem of KWSB debt servicing, in view of the proposed five years no concession fee status granted to the operator. The commission also reported that, owing to the change of mood in Karachi, i.e: the rising opposition against the projected denationalisation of KWSB, the World Bank itself did not any longer consider private sector participation as a viable option (Hasan citing DCET, 1999, p.11).

Though KWSB’s privatization was halted, other steps towards privatizing the water sector were undertaken. In July 2001, the ADB funded a Water Resources Strategy study that eventually produced Pakistan’s national water strategy, the roadmap for the development of the country’s water sector. The consultants involved in this undertaking belonged to the consortium led by Halcrow Group Ltd. of UK, together with ARCADIS Euroconsult (AEC) of the Netherlands, Halcrow Pakistan (PVT) Ltd., Euroconsult Pakistan (PVT) Ltd., and Asianics, Pakistan. In 2003, a leaked memo by a visiting ADB mission revealed that water privatization was being sought as a condition for extending financial assistance in general (Siregar, 2003).

Thereafter, KWSB’s banner has been “institutional reforms” as an alternative to privatization. This began after the enactment of Local Government Ordinance 2001, which devolved the service delivery function of municipal services to local government.

Assisting KWSB from 2005-06 in conceptualizing this process was the Water and Sanitation Program (WSP) of the World Bank. According to its report: “One of the key conclusions was that the reform of the utility was dependent on the overall reform of the political and administrative sector in which it operates. While the KW&SB—as the single-largest public service agency in the water and sanitation sector in Karachi—demands specific attention in any reform process, it was considered that the technical, financial, and organizational reform of the utility has to occur within a wider framework of governance reform. To tackle such serious and deep-rooted
institutional weaknesses, mobilization and support for change was desirable not only within the institutions itself but amongst the widest possible range of stakeholders. The KW&SB's recovery needed to be located within wider sector reform and a communitywide effort (World Bank, December 2010).

This effort is suspect however, because the institutions helping KWSB develop these “institutional reforms” are the ADB and JICA (Haider, 2007).

In 2008, the KWSB announced that the ADB and the World Bank would be financing the installation of water meters to all domestic, commercial, and industrial consumers (The Daily Times, 2008).

GOVERNMENT AND LAWS

Pakistan’s National Water Strategy shows government's bias for and direction towards privatization, and reflects how sector-wide reform will turn out.

In 2001, it undertook the Water Resources Strategy Study, through technical assistance from the ADB. This undertaking produced five volumes, collectively referred to as the National Water Sector Strategy. These flesh out directions for the water sector set by the government of Pakistan in its Ten Year Perspective Plan (Planning Commission, 2001), Vision 2025 (Water and Power Development Authority, 2001) and the National Water Policy (Ministry of Water and Power, Draft, 2002).

Vision 2025 states: “By 2025, Pakistan should have adequate water available, through proper conservation and development. Water supplies should be of good quality, equitably distributed and meet the needs of all users through an efficient management, institutional and legal system that would ensure the sustainable utilization of the water resources and support economic and social development with due consideration to the environment, quality of life, economic value of resources, ability to pay and participation of all stakeholders.”

The Water Sector Strategy covers a period up to 2025, in line with Vision 2025 and the Global Water Partnership Pakistan Framework for Action. Its key aspects are: (i) institutional aspects of water resources management and water service delivery including their capacity for planning, implementation and management; (ii) proposals for institutional strengthening and capacitybuilding programs and modalities; and (iii) efficiency improvements in service delivery; (iv) the future role of private sector financing and private-public sector financing partnerships; (v) improvement in information and data systems; (vi) stakeholder participation in project planning and implementation; (vii) recommendations on criteria for screening and prioritizing proposed water development projects.

INTERNATIONAL FINANCIAL INSTITUTIONS

The World Bank including ADB and some other financial institutions have been involved in the water sector in Pakistan since the early 1960s. Since the mid-90s these institutions have tried a number of times to introduce concession-type contracts to manage the country’s water sector, with the WB generally involved in water supply and the ADB in sewerage subsector. JICA is also involved in preparing the Water Supply and Sewage Master Plan.

World Bank financed loans on Karachi’s water supply:

ADB-financed projects:
- Water Resources Strategy Study (1998) – US$650,000 technical assistance

**Technical Advise**

The ADB-financed Water Resource Strategy Study and the Government’s Medium Term Investment Plan (MTIP) prioritize equity in water allocation, improving and maintaining the quality of water, the conservation of the country’s water resources and the need for efficiency and financial sustainability in water service delivery. These recommendations mean privatization and full cost recovery of water utilities and water resources.

Other Technical Assistance Programs extended to Pakistan include the following:
- World Bank/ ADB Public-Private Infrastructure Project
- JBIC’s Rehabilitation of Hub and Pipri Treatment Works
- JICAs Water Supply and Sewage Master Plan Preparation
- WB’s “Turn Around Programme” in support of operation and maintenance of Water and Sewage System

**CAMPAIGNS**

Trade unions, ex-officers of KWSB and civil society organizations like Citizens’ Alliance in Reforms for Efficient and Equitable Development (CREED) staged massive public protests to oppose the privatization of Karachi’s water supply. These succeeded in blocking the privatization of KWSB in the late 90s (see preceding sections).

The World Bank’s own Water and Sanitation Program found through one of its mechanisms for public participation, a Citizens’ Score Card) that “[a]lmost 49 percent of respondents were against the notion of private sector involvement in public service delivery” (World Bank 2010).
REFERENCES


In 1997, the Metropolitan Waterworks and Sewerage System (MWSS) was privatized through a concession agreement. Under this type of privatization, the ownership of utility assets remain with the state or local government, but the management and operations of the distribution system is contracted out to a privately-owned operator for a specified period. The same scheme was applied in the LGU-Urban Water and Sanitation Project wherein applicant municipalities such as the Municipality of Magdalena opened the operation of their water systems to private bidders.

**Other Privatization Mechanisms**

**Sale of Assets.** Signed into law by then President Corazon Aquino, Proclamation No. 50 or Philippine Privatization Program laid the policy basis and procedural framework for the
“divestment, disposition, and liquidation of non-relevant and non-performing government assets and corporations.” It formally signaled the development of an enabling environment for private sector participation in key public services, including water.

**Concession Contracts.** In 1997, the government awarded two 25-year concession contracts for the operations and management of the MWSS to two private corporations—Manila Water Co. and Maynilad Water Services, Inc. -- each a joint venture between an international water company and a firm owned by a local business elite clan. This move was deemed the answer to MWSS’ US$800 million debt to international financial institutions. At the same time, it was projected to address increasingly difficult water access in Metro Manila and neighboring provinces Rizal and Cavite. On average, daily water supply ran for only 16 percent and covered only 67 percent of the 12 million. Further, MWSS perennially failed to reach projected revenues because of unaccounted-for water that reached as much as lost two-thirds of its total water supply.

Water privatization was pushed on grounds that it would lead to:

- Lowering of water rates
- Uninterrupted water supply to connected consumers at no less than 16 pounds per square inch (psi) by year 2000
- Compliance with World Health Organization water and effluents standards by year 2000
- Virtually universal water supply by 2006
- 100 percent water service coverage within 10 years
- Reduction of Non-revenue water (NRW) from 56 percent to 32 percent in the first 10 years
- Investments of US$7.5 billion in new infrastructure
- Income tax revenues of US$4 billion over the 25-year life of the concession agreement
- Waste water program reaching 60 percent coverage in 15 years

The world’s biggest water privatization undertaking, as World Bank and the Asian Development Bank later hailed the MWSS private sector participation scheme, resulted in the immediate lowering of water tariffs by 73.6 percent in the East Zone (Manila Water’s service area) and 43.5 percent in the West Zone (Maynilad’s). However, this turned out to be an offshoot of extremely low winning bid rates (dive bids) of Php 2.32 per cubic meter (m$) for the East Zone and Php 4.96/m$ for the West Zone, as compared to the prevailing tariff of Php 8.78/m$ at the time.

In the course of its operations, Maynilad incurred foreign exchange losses that reached Php3 billion by year 2000. It proposed several tariff-adjustment mechanisms, which necessitated amending some provisions of the Concession Agreements. The government entered into these bail-out schemes when Maynilad, citing financial difficulties, threatened to periodically cut off water supply (a water “blackout”). So-called Amendment 1 engineered by Maynilad and MWSS resulted in several mechanisms disadvantageous to consumers:

- **Accelerated Extra-ordinary Price Adjustment (AEPA)** of Php4.21/m$ – for the recovery of Maynilad’s past foreign exchange losses incurred from August 1, 1997 to December 31, 2000, during the period October 15, 2001 to December 31, 2002 (instead of the remaining life of the contract-22 years);
- **Foreign Currency Differential Adjustment (FCDA)** of Php4.07/m$ – for the recovery of accrued foreign exchange losses or gains starting January 1, 2002, subject to quarterly review of the MWSS Regulatory Office, arising from the servicing of foreign-denominated MWSS debts (shouldered by concession fees) and concessionaire loans;
- **Special Transitory Mechanism** for the recovery of other foreign exchange losses incurred from January 1 to December 31, 2001 not covered by the AEPA and FCDA;

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1Corazon C. Aquino. Presidential Proclamation No. 50, Proclaiming and Launching a Program for the Expeditious Disposition and Privatization of Certain Government Corporations and/or the Assets Thereof, and Creating the Committee on Privatization and Asset Privatization Trust.

2Originally, Maynilad was pushing for an Automatic Currency Exchange Rate Adjustment (Auto-CERA), a mechanism that would provide for automatic price adjustments based on foreign exchange losses to be implemented without prior approval from the MWSS Board.
• A mandatory rate rebasing in 2002, which, among others, sought to correct flawed business assumptions of the concessionaires.

Expectedly, Manila Water also implemented and benefited from the above amendments, even as its contractual commitment for the payment of MWSS’ dollar-denominated loans was nine times less than Maynilad’s. It had also pressed as early as 1998 for the upward adjustment of its Appropriate Discount Rate (ADR)\(^{iv}\) from 5.2 percent when it made its bid in 1997. Adjusting the ADR upward meant tampering with the original bid of the concessionaire, making it actually higher than the original winning bid. MWSS lost the case before the International Arbitration Panel (IAP) and the ADR adjustment of 9.3 percent was granted. These events further cast doubt on the integrity of the bidding process.

In 2003, the Freedom from Debt Coalition (FDC) learned that Maynilad continued to implement the AEPA even beyond the 15-month authorized period. Overcharges arising from this anomaly reached a whopping Php 10 billion in the first quarter of 2004. An arbitration settled this issue in the consumers’ favor but was overtaken by negotiations for Maynilad’s corporate rehabilitation.

**Maynilad’s Corporate Rehabilitation**

The corporate rehabilitation controversy arose from Maynilad’s attempt in December 2002 to end its contract early. Maynilad, failing to get a tariff hike through the rate-rebasing process, filed a notice for termination. It blamed the failure to recoup US$303 million worth of investments on government’s “lack of support”. Government, to its credit, filed a countermotion stating the concessionaire’s failure to comply with the provisions of the Concession Agreement when it refused to pay concession fees and meet its service obligations. Concession fees are MWSS’ only source of income to pay its huge debts and fund its operations as asset owner (Corporate Office), a regulatory body (Regulatory Office) and

Maynilad and Manila Water’s supplier of raw water.

The IAP ruled against the early contract termination and ordered Maynilad to immediately settle its unpaid concession fees then amounting to Php7 billion. Shortly after, the company petitioned the Quezon City Regional Trial Court (QC-RTC) for corporate rehabilitation, gaining time to delay payment of its dues to the MWSS and other debts it owed to contractors and suppliers.

Maynilad’s non-remittance of concession fees as stipulated in the Concession Agreement forced the government to borrow from bridge lenders, thereby incurring more debts. It borrowed:
- US$21 million in 2001 from the Philippine National Bank and Banco de Oro;
- US$260 million in 2003 from Keppel, Deutsche, First Metro Investment Corp., Rizal Commercial and Banking Corp., etc.;
- US$150 million in 2004 from BNP Paribas; and
- P780 million in 2004 MWSS bonds.

Eventually, it came to the attention of the public that while Maynilad’s petition was being heard, MWSS and Maynilad crafted a compromise debt-to-equity scheme (Second Contract Amendment) that would be implemented as part of the company’s corporate rehabilitation plan. Accordingly, Php5 billion of the concessionaire’s then Php8 billion outstanding concession fees would be converted into MWSS’ shares of ownership in the bankrupt corporation. The remaining Php3 billion would be drawn against Maynilad’s US$120 million performance bond, a guarantee in the form of a

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\(^{iv}\) ADR is defined as the real (i.e., not inflation adjusted) weighted average cost of capital after taxes, payable by the concession business.
Standby Letter of Credit. Also, the company’s service targets would be reduced and it would be ensured of profit through a higher water tariff of PhP26.34/m³. Further, Maynilad need not refund billions of consumer’s money from its over-collections through AEPA and FCDA.

Controversy and public protest greeted Amendment 2, compelling MWSS and Maynilad to revise their compromise agreement. The new version basically revived the debt-to-equity, with additional provisions. The revised rehabilitation plan provided for the conversion of about US$22 million worth of concession fees intended to service MWSS debts into 84 percent equity in Maynilad; and the payment of the company’s outstanding and future concession fees on installment basis—50 percent in 2004, 65 percent in 2005, 70 percent in 2006 and 70 percent in 2007. Without the concession fees from Maynilad, MWSS was put in a position of having to source out new money to fill up the funds needed to pay its maturing obligations. It thus arranged for a US$125 million loan from the World Bank, $31 million of which was infused into Maynilad when the MWSS, as majority shareholder, assumed the financial burden of subsidizing the firm’s operations.

**The Public Utility Question**

Sometime in 2004, the MWSS Board passed a resolution wherein the two concessionaires were described as “mere agents and contractors”, not public utilities. The implications are significant because as such, the two water and sanitation service providers cannot be held accountable to consumers. They are also exempt from the 12 percent profit margin limitation under Section 12 of the MWSS Charter. Manila Water was, in fact, found by the Commission on Audit to have registered a 40.92 percent rate of return on rate base (RORB) in 1999, translating to Php281 million. They could also continue freely charging consumers with an additional PhP1.55 (Manila Water) and Php4.14 (Maynilad) per cubic meter of water, or about Php6.33 billion and Php56.018 billion, respectively, worth of corporate income taxes being passed on to the public. Moreover, they have also become exempt from the provisions expressed in Article XII, Section 11 of the 1987 Constitution, which limits foreign ownership of public utilities to 40 percent.

**Rebidding government’s shares in Maynilad**

In 2006, MWSS rebidded its 84 percent stake in Maynilad. Out of 11 prospective bidders, only Manila Water and the partnership of the giant construction firm David M. Consunji Inc. (DMCI) Holdings and Metro Pacific Investments Corporation (MPIC) emerged as final competitors. DMCI-MPIC secured their stake in the West Zone for US$503.9 million (Asian Development Bank, 2008).

Advocacy groups saw these developments as inimical to public interest because it effectively honored the anomalous government bailout of Maynilad. They also brought into the picture another private, profit-oriented water service provider whose record as the major shareholder of the distribution utility in Subic Freeport included failure to meet service commitments and skyrocketing water rates.

It is significant to note that the MWSS this time, included in the terms of the rebidding process the requirement for a 60 percent Filipino ownership of the bidders.

As of December 2007, the new Maynilad’s shareholding structure is comprised of 83.9 percent ownership by DMCI-MPIC Water Corp. Inc and 16 percent by Lyonnaise Asia Water (Freedom from Debt Coalition, 2009).

**Continuing Impacts on Consumers**

Manila Water, acclaimed by the Philippine government, ADB and the World Bank for being the “better” concessionaire (compared to Maynilad), remains a threat to water cooperatives in province of Rizal, Luzon island. According to

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* Under the concession agreement, each concessionaire is bound to post a performance bond to protect the interest of the public should they fail to meet their obligations.
law, Manila Water has the sole franchise to operate within its jurisdiction, which includes Rizal province. With massive capital, it has been expanding infrastructure in the area, notwithstanding the operations of several local water cooperatives that have been successfully operating for several decades in their respective communities and their opposition to these actions. FDC submitted a position paper to the House of Representatives in 2008 to “conduct a thorough review and investigation” of the MWSS privatization, pointing out the non-fulfillment and arbitrary amendments in the service targets set in the concessionaire’s contract, consumers’ heavier burdens from ballooning rates, non-prioritization of poor, waterless communities; and increasing public debts. It called, among others, for a comprehensive audit, accounting and evaluation of the concessionaires’ finances and actual performance particularly on loans incurred in the past 10 years, and a review of the MWSS privatization framework and the concession agreement between MWSS and its concessionaires (Freedom from Debt Coalition, 2008).

For MWSS, it was business as usual; in April 2009, it approved Manila Water’s extension of concession contract by another 15 years. Maynilad followed suit with its own proposal a month later for extending the concession agreement. They typically rationalized these moves as redounding to consumer benefits with the collection of proposed capital expenses (rate increases) spread over a longer period.

GOVERNMENT AND LAWS

In 1995, then Philippine president Fidel Ramos obtained emergency powers from Congress to privatize the MWSS and the Local Water Utilities Administration, the regulatory and financial body for local water districts (water utilities outside Metro Manila). The National Water Crisis Act gave him the mandate to enter into contracts to privatize vital government utilities, and allow the facilitation of the privatization “…of any or all segments of these agencies, operations or facilities, if necessary, to make them more effective and innovative to address the looming water crisis (Section 7 of the Republic Act No. 8041: National Water Crisis Act of 1995).”

In turn, the MWSS concession agreement entered into by the Philippine government on the strength of the Water Crisis Act, granted private entities, specifically Manila Water and Maynilad, the sole right to provide water supply and sanitation services within Metro Manila and Rizal Province, including one city and five municipalities in Cavite. A new government agency --the MWSS Regulatory Office (RO) -- was established, but being a creation of the Concession Agreement, it exercises regulatory functions not to protect the public interest but to ensure that the terms of the contract are realized. As such, it remains a mere recommendatory body to the MWSS Corporate Office.

Changes in policies / laws

With the passage of RA 8041, MWSS was able to enter into negotiated contracts with the private sector for the operation and management of its water distribution facilities. (This function is not included in the MWSS Charter.)

Right to Water. Water as a human right is not explicitly included in the 1987 Constitution's bill of rights. There is also no existing domestic law that explicitly declares water as a human right that may be demanded by the people.

The Constitution, however, contains a catch-all provision in Art. II, Sec 2 that adopts generally
accepted principles of international law as part of domestic law. Among The Philippines is a state party of the International Covenant on Economic, Social, and Cultural Rights on which General Comment No. 15, on the right to water is based. In its elaboration of Articles 11 and 12 of the Covenant, it defines the right to water as that which "entitles everyone to sufficient, safe, acceptable, physically accessible and affordable water for personal and domestic uses." It stresses the right to water as “fundamental for the realization of many of the other rights specified in the Covenant, including the right to adequate food, the right to health and the right to adequate housing (Committee on Economic, Social and Cultural Rights, 2003).”

Ownership and Management of Water Utilities.
Presidential Decree 198 or the Provincial Water Utilities Act of 1973 declares a national policy favoring the local operation and control of water systems. Among the most relevant provisions is Sec 2, viz:

“The creation, operation, maintenance and expansion of reliable and economically viable and sound water supply and wastewater disposal system for population centers of the Philippines is hereby declared to be an objective of national policy of high priority. For the purpose of achieving said objectives, the formulation and operation of independent, locally controlled public water districts is found and declared to be the most feasible and favored institutional structure.”

Economic Regulation. The National Water Resources Board is mandated by law with the jurisdiction to control, regulate, and supervise waterworks utilities. It has been upheld by the Philippine Supreme Court to exercise original jurisdiction over all disputes relating to water rates of all water utilities, public and private.

NWRB’s mandate, however, has many times been confused with the specific regulatory powers of the Local Water Utilities Authority (LWUA), the Metropolitan Waterworks and Sewerage System-Regulatory Office (MWSS-RO), the Subic Bay Water Regulatory Board (SBWRB), and the Local Government Unit (LGU) Councils. To sum, the following utilities are also under the special regulatory powers of these agencies/ bodies:

- Water Districts – Local Water Utilities Authority
- MWSS Concessionaires – MWSS-Regulatory Office
- Subic Water – SBWRB
- LGU-run systems – LGU Councils
- Water Cooperatives – Cooperative Development Authority

Utilization of Water Resources

Under Sec 2, Art XII of the 1987 Philippine Constitution, all waters are declared to be owned by the state and may not be alienated. Along with other natural resources, their “exploration, development, and utilization...shall be under the full control and supervision of the State.” The same section, however, also provides that the state may enter into “co-production, joint venture, or production-sharing agreements with Filipino citizens, or corporations or associations at least sixty per centum of whose capital is owned by such citizens” for the exploration, development and utilization of water and other natural resources.

The Water Code of the Philippines (1976) follows the same above principle of state ownership over all water resources, within public and private lands. The NWRB is granted the sole power to issue water permits for the utilization of water resources for all purposes. Water for domestic and municipal purposes is also granted higher priority over all other water uses (power-generation, irrigation, industrial, etc) in times of emergency.
INTERNATIONAL FINANCIAL INSTITUTIONS

The MWSS, at the time of its privatization, was saddled with a US$800 million debt from international financial institutions such as the World Bank and Asian Development Bank.

World Bank

With the prospect of privatizing MWSS, the government sought the assistance of the International Finance Corporation (IFC), the World Bank’s private sector lending arm. IFC accepted a contract fee of US$6.2 million to draft a privatization plan and to administer the bidding procedures between the government and the private companies, with the approval of the MWSS Board. According to reports, IFC received a bonus of US$1 million for the successful privatization of the water utility.

World Bank also approved a US $125 million loan in April 2008 for the “financial strengthening” of the MWSS, which subsequently went into bailing out the debt-ridden Maynilad.

Asian Development Bank

By the time Metro Manila’s water distribution system was privatized, ADB had already funded eight water supply and sanitation projects of the MWSS amounting to US$344,786,111.18 (MWSS Regulatory Office).

One of these projects the Umiray-Angat Transbasin Project (UATP), was ushered in by an advisory technical assistance (TA) grant from the ADB amounting to US$582,000, that aimed “to assist the MWSS in introducing private sector participation in the operation and management of MWSS sector activities.” It also sought to “further promote privatization activities initiated under the TA for the MWSS Operational Strengthening Study approved in December 1994 (Asian Development Bank, 1995).”

ADB extended another loan of $45 million loan to Maynilad and attempted to arrange further access to loans from a syndicate of international commercial banks. It also approved Manila Water’s use of leftover funds from previous projects for its Tubig para sa Barangay (Water for the Community) initiative (IDEM, not dated).

In October 2003, the Bank approved a US$3.26 million additional technical assistance loan for the MWSS New Water Source Development Project. This TA went into facilitating the MWSS and its concessionaires’ groundwork of projects for potential ADB financing by the ADB, such as the 50-MLD Wawa River Project, the Angat Water Utilization and Aqueduct Improvement Project and the Laiban Dam Project (Asian Development Bank, 2009).vii

Promoting private participation outside Metro Manila

To encourage private sector investment in water districts outside Manila, the World Bank approved four Adaptable Program Loans totaling US $283

vi The Laiban Dam Project was withdrawn from the study upon MWSS’ requesty.
million which were released over a period of 12 years, from 1998-2010.

As for the ADB, it approved in 2008 a US $1.2 million TA for the crafting of the Water District Development Sector Project (WDDSP) in support of the institutional development of LWUA and strengthening its role in sector reform (Asian Development Bank, 2008). The release of a US $50 million loan came the following year.

**IMPACTS**

**On Labor**

Of the total 7,370 MWSS employees, only 1 percent was left with the residual MWSS (48 percent women, 52 percent men). Six months later, the MWSS workforce further shrank by 40 percent from the so-called early retirement (27 percent) and voluntary/involuntary separation (13 percent). Also because of the privatization, both female and male employees close to 15 years of services forfeited lifetime pension benefits.

According to one office worker, women employees, especially the seniors in support staff positions (clerks, typists, administrative staff), chose early retirement because they feared they could not ‘compete’. They also felt that they fell short of the necessary skills (such as using computers) to survive in the new set up.

The MWSS Employees Union opposed the plan to privatize the MWSS and filed a petition before the Supreme Court in July 1997. Two weeks later, the petition was dismissed (Corral, 1998).

**On Consumers**

Heavier economic burden from escalating tariffs and overcharging. More than a decade of implementing the privatized set-up, the service areas of the two concessionaires are suffering from unacceptably high water tariffs. In January 2008, water rates stood at Php26.98 for Manila Water and Php32.032 for Maynilad. These rates represent a staggering increase of at least 891 percent and 665 percent, respectively, from 1997 levels (Freedom from Debt Coalition, 2009). Due to the MWSS Board Resolution declaring the concessionaires as agents and contractors, Manila Water and Maynilad continue to bill consumers with the cost of their corporate income taxes amounting to P6.33 billion and P56.018 billion, respectively.

**Cholera outbreak.** In 2003, more than 800 individuals from communities in Tondo, Manila and nearby cities were hospitalized from ingesting contaminated water, and eventually eight of them died. These communities belong to Maynilad’s coverage area.

The Freedom from Debt Coalition (FDC) had a water water sample from one of the affected communities examined by the University of the Philippines National Research Science Institute. The test results confirmed that the water was infected with E. coli bacteria, at 16 counts per 100ml of water or more than 700 percent the national standard of 2.2 per 100 ml of water. Until now, the company has not indemnified the victims of the cholera outbreak.

**CAMPAIGNS**

In 1997, the Freedom from Debt Coalition (FDC) began research on water privatization as part of its campaign on debt and attendant loan conditionalities prescribed by institutions such as the International Monetary Fund and the World Bank. At that time, the MWSS privatization was already underway. The succeeding years would see the Coalition sharpening its critique and analysis on water privatization, enabling it to mount informed and timely interventions in the face of ever-increasing threats posed by big business interests to the Filipinos’ basic right to safe, adequate and affordable water. FDC’s general objectives in the current term include empowering mass movements to effectively demand their right to water and incorporating an alternative rights-based framework in promoting the democratization of water and other essential services.
FDC strengthened its opposition to the privatized setup and raised the call for the reversal of the MWSS privatization, starting with the termination of the concession contract of Maynilad Water Services for the company’s gross inefficiencies and sheer failure to provide decent water and sanitation services. This developed as government frequently sided with the private water firms despite unmet commitments to improve and expand service. When Maynilad filed for early contract termination in December 2002, FDC intensified its campaign to demand that operations and management of the West Zone concession be reverted to public hands.

Holding government accountable for putting the people’s right to water on the line while bailing out the concessionaires from their self-inflicted business failures has been a critical campaign platform. The task is three-pronged: engaging and confronting the government and the private sector in defense of public interest and basic right to water access; enriching the Coalition’s framework and alternatives; and deepening the understanding of the public on water issues. FDC works on all these parallel tracks through numerous activities including research and popular education, networking and alliance-building, lobbying and organizing mobilizations.

In the absence of a strong regulatory regime and under a government that has proven permeable to big business interests, FDC’s interventions have sought to protect public interest. It disclosed Maynilad’s overcharging through unauthorized implementation of cost-escalation mechanisms. It also exposed Maynilad’s contaminated water and rallied the public to hold the company culpable for cholera outbreak in its concession area. In 2006, FDC filed a case in the Supreme Court to nullify the MWSS Board resolution declaring the concessionaires mere agents and contractors.

The Coalition led the formation of the Progresibong Alyansa ng mga Tagatangkilik ng Tubig sa Kamaynilaan (PATTAK, Progressive Alliance of Water Consumers in Metro Manila). PATTAK is envisioned as a grassroots-based, consumer-led movement for the improvement of the quality and delivery of water and sanitation services and to ensure that water remains primarily part of state responsibility, not a business enterprise from which private business profits.

The Coalition is also in the process of advancing a comprehensive framework on water that links the campaign to stop water privatization to a wider range of perspectives and advocacies on potable water. This allows for stronger unities in the wake of the global trend led by international financial institutions to privatize water resources and services through various means and aggressive moves of giant water firms to take advantage of an increasingly scarce and critical resource. This enables greater synergies across sectors, organizations and campaigns on water as a human right, a public good and an ecological resource; water use rights; and in particular, water and its differential impacts on women.

A milestone in advocacy and campaigning on water as a human rights came with First National Conference on Freshwater in 2004. An initiative organized by FDC, it paved the way for the formation of the People’s Freshwater Network (Philippines).
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