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Water, Development and the GATS

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KEY POINTS:

- **Water is the basis of life; a unique natural resource that makes a critical contribution to human health and the well being of all societies.**
- **Water scarcity and extensive needs for water services are encouraging private entrepreneurs to develop potentially profitable enterprises.**
- **Publicly funded research on new or alternative technologies to improve distribution of water could help find low cost access to water supplies and promote technology transfer.**
- **Safeguards are needed to ensure that GATS provisions do not adversely affect community-managed water services.**
- **The co-existence of several different models for water-services supply should be the norm, offering valuable lessons for water management and provision in the future.**

The high costs and frequently complex setting of water infrastructure (such as reservoirs and pipeline networks) as well as potentially costly quality controls all emphasise that adequate water services are necessary to ensure the availability of clean, safe water. This has led some governments to look for private investment in the water sector. However, market-based models do not lend themselves easily to the construction of water services infrastructure – market ‘efficiency’ could leave unprofitable areas without an adequate supply of water. In the absence of formal infrastructure and quality controls an extensive system of informal provision usually develops.

The incorporation of water services into a broad-based trade agreement for all services results in a number of problems. This paper concentrates on two pressing issues: the importance of promoting and safeguarding community-managed services and the ability of governments to establish market structures that favour effective subsidy regimes.

Water, community-managed services and the General Agreement on Trade in Services (GATS)

Water services and the poor

It is beyond doubt that there are deficiencies in the current reach of public water networks and household connections.¹ WHO and UNICEF say that 1.1 billion people do not have access to safe water supplies.² The proportion of people living in low-income settlements without household connections are high: 66% in Africa, over 50% in Asia and 33% in Latin

America.³ 64% of Africa’s urban population have access to safe water but of these only 14% have household connections.⁴ For many, public standpipes are a considerable distance away from their homes. Overwhelmingly, it is the poor that are not connected. Argentina provides evidence of the relationship between socio-economic status and access to public network water connections: 90% of high-income households have water connections compared to less than 25% of those in the low-income category.⁵

In the absence of piped water, consumers meet their needs from informal providers, their own endeavours and collective activities. Development agencies are increasingly interested in community-managed water services. However little attention has been given to the potentially adverse consequences of adopting GATS liberalisation without appropriate safeguards for community-managed services.

Community-managed services

Community-managed water services have a long tradition in many communities in the South, both rural and urban.⁶ The lack of state and formal-sector private services has encouraged some communities to address their own needs by developing alternative models to secure the services they need for improved livelihoods and development opportunities. The growing significance of such services is a reflection of both local demand and the growing interest of development assistance agencies looking for effective mechanisms to help poor people get access to water, as well as, to a limited extent, the

search by some private sector companies for more cost effective strategies to extend supplies.

Community-managed services should not be seen as a second best option.⁷ Given the limited state investment capacity, local resources can make an essential contribution to improved infrastructure. Their other advantages include inexpensive installation and maintenance strategies, participation by local residents, strong local ownership and accountability, possibilities for locally agreed assistance to the poorest, and flexible provision with management approaches that are closer to community members' needs. In Faisalabad, Pakistan, for example, the Anjuman Samaji Behbook, a local grassroots organisation, worked with 300 families to develop a local piped network that resulted in considerable cost savings for those involved. Despite initial scepticism and some hostility from local politicians and authorities, the success has resulted in public support to extend the scheme.⁸

Conventional suppliers' reactions to community-managed services have been mixed. In Pune, India, the boundary between the community and the public water company is contested; the water company is seeking to take over the communities' role, changing the terms and conditions of supply.⁹

Private sector companies that have recently expanded into urban services have often been open to exploring the potential involvement of the local community. However, effective models for community management components within private sector services do not appear to be emerging.¹⁰ The stronger examples are where communities themselves (generally with the support of NGOs) have developed appropriate approaches that are scaled up.

Implications of GATS-style liberalisation for community-managed services

GATS liberalisation has rendered the future of community-managed supplies uncertain. The threat comes from the commitments made by governments to open specific sectors to competition under the GATS framework. GATS seeks in principle to construct a competitive market with a minimal role for state intervention. If the water sector is committed by governments to be opened for international competition, obligations under Article XVII (national treatment) and Article XVI (market access) prevent preferential treatment of any kind to national companies or community-managed services suppliers in the provision of water for human use, water treatment, and other related services. Neighbourhoods (large or small) will not be able to secure the right to community-managed services unless their governments specifically reserve the right to declare areas for community management (horizontal limitation) when scheduling obligations at the WTO. Without such a reserve, any act that favours community-managed services would contravene Articles XVI and XVII and be seen as a restriction on trade.¹¹

Even though private sector involvement in water services in the South remains limited, some companies have shown interest in working with communities in self-management. However, many of these community-managed service providers would not have the capacity to compete with large-scale water services providers in a freely competitive market. Their higher costs, stemming in

part from longer planning schedules, greater inclusiveness, increased local participation and use of local materials, mean that they would require some form of public support in order to compete. Without it, communities might be left unable to provide themselves with water services.

What can be done to safeguard community-managed services?

Given the high level of interest in community-managed water services, the potentially adverse implications as a result of the GATS provisions are probably unintended. Some safeguards to protect them could be put in place which would probably benefit both pro-liberalisation groups and campaigners for public interest – a few high-profile examples of how inclusive effective community-managed services were forced to close would benefit no one, least of all those in favour of liberalisation.

The following 'safeguards' could be advocated by developing countries to ensure rights for community-managed services:

- WTO Members could include appropriate horizontal limitations in any water services liberalisation commitment to safeguard their right to undertake discriminatory measures in favour of national community managed providers, to designate certain geographical areas only for community management and to establish certain market access limitations. Such limitations would restrict the scope of Articles XVI and XVII of the GATS in the particular sector. Communities would be given the right to choose to manage their own services, restricting access to other suppliers.
- The WTO could issue a stand-alone political declaration emphasising that Members should be aware that the GATS Agreement does not intend to restrict communities' right to self-management of water services.
- Currently there are no rules on subsidies in services. Governments could provide direct (grants) or indirect (tax breaks) subsidies designed to support community-managed services.¹²
- WTO Members could make a decision to ease Article XXI compensation requirements for developing countries that wish to modify liberalisation commitments concerning public utilities.

Subsidies to water services and liberalisation

Global water use has increased in recent decades because of growing population and greater use.¹³ In order to reduce the pressure on water resources, many governments and development agencies are moving towards full cost pricing. However, water supply companies' move to full cost pricing and cost recovery has brought affordability issues to the fore. Although, for the last decade, they have been anathema to governments and development agencies seeking financially viable water services providers, there is an increasing recognition that some kind of public support in the form of subsidies will be necessary if cost recovery is to be achieved while simultaneously extending water services to low-income households.

Issues related to universal access and affordability remain contentious. Governments' Millennium Development Goal 'to halve, by 2015, the proportion of people without sustainable access to safe drinking water' has generated a revision of acceptable mechanisms to achieve the target, including the provision of subsidies in water services.

Subsidies and access to water

Despite the efforts that have been put into reducing the cost of water, not everyone can afford even the lower prices. If they cannot, how can access for the poor be secured?¹⁴

A recent WaterAid evaluation in Bangladesh highlighted that the issue of subsidies is not just one for the private sector but is also relevant to community managed supplies.¹⁵ Some from the private sector acknowledge that they cannot supply to the poor without a subsidy. JF Talbot (chief executive of SAUR International) argues that subsidies are a requirement: *'"water pays for water" is no longer realistic in developing countries: even Europe and the US subsidise services... Service users can't pay for the level of investments required, nor for social projects...'*¹⁶

Consumption subsidies would probably require some kind of rationing in order to prevent excessive consumption and also to ensure that it is the needy socio-economic groups that benefit from them. The definition of a 'socially acceptable consumption standard' is also liable to evolution and change.¹⁷ A recent UNU/WIDER analysis cautions that 'while regulatory reform can bring long term benefits to consumers through lower costs and prices, low income consumers will not necessarily benefit most or fastest from the changes'.¹⁸ In particular the introduction of competition may erode traditional cross-subsidies with adverse distributional effects. New subsidies or regulations obligating utilities to provide services may be needed to protect the interests of the vulnerable and ensure that they receive a 'fair share' of the benefits of reform'. An ideal scheme would 'maximise the benefits for the target group, while minimising the efficiency losses through distortion which any such mechanism inevitably involves.'¹⁹

The development of new technologies for water services provision and the minimisation of waste would help improve the affordability and accessibility of water. In existing pipelines water lost by evaporation, leaking and spills can account for 20% to 40% depending of the state of the network.²⁰ In fact, tackling such waste could be an effective and low-cost method to improve access to water supplies in many countries. Research on new or alternative technologies to improve distribution of water has been somewhat neglected. Public support could help correct this, with a particular eye to finding low cost solutions and promoting technology transfer.

Market trends and non-affordability

There is an increasing interest in 'unbundling' – identifying the potentially lucrative elements of water services, within private sector experiences. In the struggle to achieve cost recovery, companies appear to be moving towards ring-fencing profitable customers and excluding the poor.²¹ The segmentation of markets in this case is detrimental to the interests of the poor as they are excluded from improvements in services. Some experts have even argued that progress

towards greater access to water services requires attention to a range of 'reform levers' including various aspects of market structure (such as partnerships, degree of competition, interconnection and supply-arrangements), price regulation and price-structure, quality regulation and subsidies. The preservation of community models and subsidy systems will also entail formulating complementary and supplementary policies to deal with these other 'levers' so that access is maximised in terms of both quantity and quality.

GATS negotiations on subsidies

Current international trade rules place no horizontal disciplines on subsidies in services. Ongoing WTO negotiations have been dealing with the services subsidies issue since 1995 in the Working Party on GATS Rules (WPGR), where subsidies, in comparison with other issues, have drawn little attention.²² This does not, however, mean that Members attach no importance to the issue in current negotiations. In fact, many countries have observed that the existence of services subsidies will have significant consequences for the effectiveness and value of any new market access concessions made as part of the current negotiations. On the other hand, disciplines regulating the use of subsidies might have a large impact on Members' ability to use subsidies for promoting national policy objectives, including access to, and the affordability of, water.

What is already in the GATS on subsidies?

There are some rules in the GATS that have – in principle – disciplining effects on how WTO Members grant subsidies. When a sector is liberalised under the GATS, subsidies will be subject to non-discrimination unless Members specifically exclude them from the application of the national treatment principle. For example, the US, the EU, Japan, and Canada reserved their ability to provide subsidies in their initial GATS offers in areas such as research and development.

Also, Article XXIII.3 of GATS could theoretically be used to discipline subsidisation by allowing the deposit of 'additional commitments' that could include the non-granting of – or phasing-out of – subsidies in specific sectors. In conclusion, current GATS rules contain some rules that might discipline the use of subsidies when depositing commitments under the GATS.

The consequences of GATS style liberalisation and subsidies schemes available to water

For governments attempting to safeguard water provision, market liberalisation *per se* is not the problem. Private sector involvement in water services has, for the most part, included international companies; many companies welcome subsidies, particularly since they are often required to meet broad inclusion targets. The danger is that the GATS Articles, drafted to minimise the risks of deception by states (e.g., promising liberalisation to gain markets but continuing protection measures at home), will reduce governments' ability to manage water markets for the benefit of the poor.

There are essentially two ways of financing subsidies: through general redistribution or through cross-subsidies (where different consumers are charged different rates with the high rates subsidising the low) within a designated

water market. While the former is thought to be less market-distorting, it is not necessarily appropriate for countries with under-developed tax systems.²³ In South Africa, local authorities receive a central subsidy to provide a basic allowance of free water.²⁴ In Durban, the scheme appears to work relatively well but is critically dependent on the authority's ability to use a cross-subsidy within the city.²⁵ In South African towns that cannot afford such a subsidy, suppliers and users face major problems.²⁶

The highest priority is for all possible options in water subsidisation to remain open. Ongoing studies are assessing the relative advantages of different systems.²⁷ Cross-subsidies, for instance, may be neither possible nor suitable in all circumstances. However, countries facing substantial developmental problems with limited resources need to be free to address the water needs of their population in whatever manner possible.

The GATS is clear that any subsidies should be offered equally to all suppliers once a commitment has been deposited in a particular sector without exceptions. This paper has argued that there is an increasing recognition of the need for subsidies and that cross-subsidies appear to offer a number of advantages. Why should GATS be a reason for alarm?

First, current negotiations on services and subsidies might end in the creation of rules on subsidies which may lead to several of them being phased out. Any future subsidies rules should exempt subsidies necessary to achieve certain public policy objectives, including the universal provision of services and more specifically the provision of water and related services. This demand is backed up by the mandate of Article XV GATS itself, which provides that the '*needs of Members, particularly developing countries for flexibility in [the] area*' of subsidies are to be taken into account.

Second, water markets may need to be constructed and potentially reconstructed – including alterations in the socio economic characteristics of neighbourhoods – in ways that maximise the possibilities for cross-subsidisation. However good the reason, restructuring might be considered a restriction of trade. This is especially true if international companies decide that 'unbundling' (cherry picking) higher-income areas is the answer to problems of affordability. They may resist being asked to use high profits from one area to subsidise losses in another.²⁸

A third concern is that the requirement that regulations not be unduly burdensome (Article VI) may also be used against pro-poor urban planning. One WTO Secretariat background paper has even suggested controls on land use as well as building and environmental regulations may be examples of overly burdensome regulations.²⁹

What can be done?

Negotiations need to respect the global objectives of poverty reduction as well as those of free trade. Many developing country Members are calling for spaces for development policies – WTO permission for developing country governments to use 'active' policies³⁰ to promote competitiveness, including subsidies. In their view, such special and differential treatment must be part of all

normative results of the Doha round, including in the subsidies and services negotiations.

WTO Members need to ensure that area designation and re-designation for the purposes of maximising revenue for a cross-subsidy is allowed under GATS and will not be considered a restriction of trade or a burdensome regulation. Although some argue that governments can include such a limitation within their Schedules, this is clearly inadequate. Pressures could be exerted on developing countries forcing them to commit in areas where they are not ready, or want to keep reserved for reasons of national policy (such as poverty reduction). The co-existence of several different models for water-services supply should be the norm, offering valuable lessons for water management and provision in the future.

Conclusion

For the most part, formal sector water companies, whether public or private, have failed the poor. Levels of access and affordability are grossly inadequate. The experience of the OECD countries suggests that there is no clear consensus in favour of public or private provision of water services. Of the 29 OECD countries, 21 have public ownership of water assets and a further 5 have mixed public and private ownership. 14 OECD countries have exclusively public management while 13 have mixed public and private.³¹ The arguments in favour of private sector involvement in water services are, generally, to improve efficiency and to add to investment funds. Though both reasons may be valid for countries with low GDP, neither argument remains strong as countries grow richer. In the case of water, what appears to be important is the flexibility of the approach towards management of water services.

The GATS text and the current WTO negotiations should incorporate legal flexibilities and spaces to safeguard community-managed services and policy frameworks that allow for the universal provision of water services, the grant of subsidies and cross subsidisation in services. Even if the GATS permits commitments on water and related services, developing country Members should not be required to provide trade compensation when they reverse or modify their commitments schedules to better address the basic needs of the poor, as in the case of water and related services. ●

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- 1 We have used public to refer to large-scale piped networks whether provided by the government or private sector.
- 2 Quoted in OECD (2003, 19).
- 3 From Hardoy, Mitlin and Satterthwaite (2001, 44-62); the data is drawn from Africa (10 cities), Asia (14 cities) and Latin America (8 cities).
- 4 Estache and Kouassi (2002, 3).
- 5 Mazzucchelli, Rodriguez Pardinias and Gonzalez Tossi (2001, 70). In total, an average of 57% of households in the Buenos Aires Metropolitan Area had water connections.
- 6 Gross, van Wijk and Mukherjee (2001, 26). Estache and Kouassi (2002, 4-5) also argue that community driven approaches are

becoming more significant in sub-Saharan Africa in rural and peri-urban areas and also in more central urban areas.

- 7 There is an assumption in GATS that more liberalisation is a good thing (Article XIX). Whilst understandable in the context of many goods and services, this assumption appears curious in the context of basic services. It is evident that OECD countries, with the benefit of considerable expertise, choose to use both public and privately provided water services. (OECD 2003, 57.)
- 8 Alimuddin, Hasan and Sadiq (2001).
- 9 Case study of community managed water provision in India by SPARC and the National Slum Dwellers Federation for the Asian Coalition for Housing Rights.
- 10 Mazzucchelli, Rodriguez Pardinias and Gonzalez Tossi (2001, 99). Nickson (2001a, 25) and Nickson (2001b, 17-19).
- 11 Water is clearly not the only area of concern in regard to community-managed services. Community-managed micro-hydro stations for local energy production are another example. Energy specialists at the Intermediate Technology Development Group are concerned about the future of such ventures.
- 12 The main limitation of this option may be the lack of financial resources from developing country governments.
- 13 OECD (2003, 13).
- 14 Chisari, Estache and Waddams Price (2001, 1).
- 15 Hanchett, Hoque Khan and Akhter (2001).
- 16 Hall (2002, 8).
- 17 Chisari, Estache and Waddams Price (2001,15).
- 18 Ibid.
- 19 Ibid.
- 20 See, for example, UNCHS (2000).
- 21 Hall (2002, 9). In the case of Ghana, Public Citizen/Water for All (2002, 34) suggest that ‘...the World Bank and other PSP advocates argue that it is quite appropriate to rely on private operators for that portion of the sector to which they are attracted; the efficiencies which the private sector is purported to introduce should be obtained to whatever extent possible.’
- 22 Other horizontal issues include ESM and government procurement.
- 23 Gomes-Lobo (2000, 5).
- 24 See, for example, the description in Palmer Development Group (2000b).
- 25 pers. Comm.. Director of Infrastructure, Durban Water.
- 26 McDonald and Pape (2002).
- 27 See Gomez-Lobo (2000).
- 28 See, for example, the concerns expressed in Gould (2003).
- 29 Quoted in Hardstaff (2003, 4).
- 30 Active policies imply policies that are undertaken directly by the government to promote competitiveness.
- 31 OECD (2003, 57).

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