food&water watch

Fact Sheet

The Top 10 Ways That Water Privatization Costs the Public

Our country's valuable water resources must stay in public hands to protect taxpayers and consumers. Sadly, in these tough economic times, many cities and towns are struggling to keep up with the escalating costs of rejuvenating their aging water systems. The federal support that once helped sustain our nation's vital water infrastructure has all but washed away, and an extensive credit crunch threatens state and municipal budgets.

Confronted with these hard realities, certain public officials have attempted to abdicate their responsibility by transferring control of water and sewer utilities to the private sector. This practice is unaccountable and damaging to communities. When multinational water corporations take over the ownership, operation or management of water systems, costs grow and households must pay much more, if not through their water bills then through damage to the environment.

The research shows 10 main ways that private control of our public water resources costs the public:

High Rates. A survey of the rates in more than 20 states shows a strong trend: corporations charge much more than municipalities for both water and wastewater. Private water costs as much as *80 percent* more than public water.[1] Private sewer service costs up to *twice* as much as public service.[2,3]

Bad Service. Many multinational water corporations cut corners to increase profits at the public's expense. They often use shoddy construction materials, ignore needed maintenance and downsize the workforce, which impairs customer service. Such neglect hastens equipment breakdowns and increases replacement costs, which the public must pay for. In many contracts, private operators can technically comply with their contract terms while effectively shifting upkeep costs to the public.[4]

Expensive Financing. Private financing is more expensive than public financing. Even the best-rated corporate bonds are *25 percent* costlier than municipal bonds and *2.5 times* costlier than State Revolving Fund loans.[5,6]

Inefficiency. Private utilities are *not* more efficient than public utilities, according to several academic studies. In fact, more studies have found that the public is the more efficient operator.[7,8]

Profits and Taxes. Private utilities usually pay income, property and other taxes, whereas government utilities pay no local or state property taxes.[9] They also typically seek at least a 10 percent profit on their investment. In total, corporate profits, dividends and income taxes add *20 to 30 percent* to operation and maintenance costs.[10]

Cost Inflation. The profit motive can further drive up costs. That's because private utilities tie higher earnings to *increased* costs. They earn a rate of return on investment, so that the more they spend on a system, the more they profit. Perhaps that's why a study of the construction of 35 wastewater treatment plants found that "choosing the privatization option is more costly than going with the traditional municipally owned and operated facility."[11]

Contracting Expenses. Contract preparation can easily set a city back *$75,000 to $100,000*.[12] Monitoring a corporation can cost as much as *20 percent* of the total contract.[13] In total, contract monitoring and administration, conversion costs, charges for extra work and the contractor's use of public equipment and facilities can add up to *25 percent* to the price of a contract.[14] Change orders, cost overruns and termination fees also can inflate the cost of private service.

Limited Competition and Consolidation. The water market is "rarely competitive," and the little competition there is faces "increasing difficulties," including consolidation, according to one academic study.[15] The nation's massive infrastructure needs may only make this worse as water corporations merge for greater access to capital to finance improvement projects.[16] Without competition, the public has no room to negotiate and can get stuck with bad and expensive contracts.

Lost Public Benefits. Municipal operation often has several additional benefits that cities lose when they privatize: revenue from *government entrepreneurial sales* of services and products, including biosolids and wastewater effluent; *intra-government coordination* to pool resources and assist other government departments;[17] and *inter-government coordination* to protect water resources, manage watersheds and work for long-term sustainability.

Lack of Accountability. Multinational water corporations are primarily accountable to their stockholders, not to the people they serve. For example, private utilities cherry-pick service areas to avoid low-income neighborhoods where low water use and bill collection problems drive down profits.[18]

Ways Forward. Instead of allowing irresponsible private control of our water, we need to plan ahead and create a dedicated source of public funding that will help public utilities protect our country's valuable water resources. A national water trust fund and an infrastructure reinvestment bank can achieve this feat and ensure the safe and sound operation of our water systems, but to get the best deal for consumers and taxpayers, this assistance must go only to public entities and public projects. Public utilities are more responsive, reliable and cost-effective.

With a renewed federal commitment, our nation's good public operators can keep our water safe, clean and affordable for generations to come.

For more information, see our report, *Money Down the Drain: How Private Control of Water Wastes Public Resources*.

End Notes

1 Kauffman, Gerald J. et al. "Synthesis of water rates in Delaware and contiguous states." University of Delaware, Newark, DE, July 2004.

2 "2008 Water/Wastewater Survey." Texas Municipal League, 2008. Available at www.tml.org/surveys.html.

3 "Notice of proposed sewer rate change." Texas-American Water Company, El Campo, TX, February 2008. Available at amwater.com/txaw/customer-service/rates-information.html.

4 "Evaluating Privatization II: An AMSA/AMWA Checklist," op. cit., p. 27.

5 "Weighted average interest rate of Clean Water SRF assistance, by state." Office of Water, U.S. Environmental Protection Agency, Oct. 26, 2007. Available at www.epa.gov/owm/cwfinance/cwsrf/cwnims/pdf/ratest.pdf.

6 Data download program, H.15 selected interest rates for Nov. 20, 2008 — Annual Moody's yield on seasoned corporate bonds - all industries, AAA (1989-2007); Monthly Bond Buyer GO 20-bond municipal bond index, Moody's yield on seasoned corporate bonds - all industries, AAA (October 1998-October 2008), the Federal Reserve Board. Available at www.federalreserve.gov/datadownload/Choose.aspx?rel=H.15/.

7 Bel, Germa and Warner, Mildred. "Local privatization and cost: theoretical expectations vs. empirical evidence." Submitted to *Public Administration Review,* Oct. 26, 2006, p. 29.

8 Renzetti, Steven and Dupont, Diane. "Ownership and performance of water utilities." *Greener Management International* 42: 9-19, Summer 2003, p. 12-16.

9 "Public Private Partnerships in the Provision of Water and Wastewater Services: Barriers and Incentives." Environmental Financial Advisory Board, April 2008, p. 11.

10 "Evaluating Privatization II: An AMSA/AMWA Checklist." Association of Metropolitan Sewerage Agencies and Association of Metropolitan Water Agencies, 2002, p. 23.

11 Holcombe, Randall G. "Privatization of municipal wastewater treatment." *Public Budgeting & Finance* 11(3):28-42, Fall 1991, p. 38.

12 Evaluating Privatization II: An AMSA/AMWA Checklist," op. cit., p. 22.

13 Warner, Mildred and Hebdon, Robert. "Local government restructuring: privatization and its alternatives." *Journal of Policy Analysis and Management* 20(2):315-336, Spring 2001, p. 317.

14 "Government for Sale: An examination of the contracting out of state and local government services." Eight Edition, American Federation of State, County and Municipal Employees, AFL-CIO, Washington, D.C., p. 3.

15 Bel, Germa and Warner, Mildred. "Challenging issues in local privatization." *Environment Planning C: Government and Policy* 26:104-109, 2008, p. 105.

16 "Fitch: Escalating capital costs may lead to consolidation for U.S. water utilities." *Business Wire,* Jan. 23, 2008.

17 "Evaluating Privatization II: An AMSA/AMWA Checklist," op. cit., p. 23, 42-43.

18 Boland, John J. "The business of water." *Journal of Water Resources Planning and Management* 133(3):189-191, May/June 2007.

For more information:
web: www.foodandwaterwatch.org
email: info@fwwatch.org
phone: (202) 683-2500 (DC) • (415) 293-9900 (CA)