

International Drinking Water Supply  
and Sanitation Consultation  
Interlaken, Switzerland

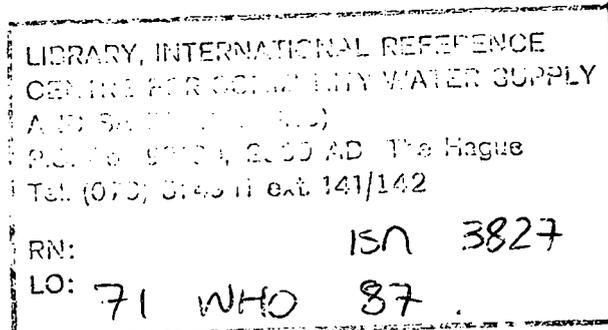
13.- 16. October 1987

Cost Recovery and Financial Management

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71WHO87-3827

1. As the constraints on external resource flows and the availability of domestic public resources in developing countries have not been eased, the call for cost-recovery and improvement of financial management, voiced from the beginning of the Water Decade, is today as justified as ever. On the contrary: WHO's regional consultative meetings have supplied strong evidence that this topic is at the heart of any problem-solving strategy in the water and sanitation sector. To produce funds for operation and maintenance, for depreciation and system expansion within the projects themselves seems to be their only chance for survival, the only basis for sustainable development.

2. German technical assistance projects have given support and advice to our partner organisations in the field of financial management since the early seventies. In May '84 the BMZ sector paper "Water Supply and Sanitation Projects in Developing Countries" officially stated:

"As a matter of principle, cost-covering charges should be aimed at for water supply as well as for sewerage/sanitation....Projects in which present revenues do not comply with this requirement because tariffs are too low or collection systems inefficient, are eligible for financial assistance only if the necessary tariff increases and improvements of collection systems and financial administration management can realistically be expected to be enforced."

Activities of technical assistance like institution building, advisory services, tariff studies or training in financial management can thus pave the ground for donors' investments and a solid financial basis for effective services in the water and sanitation field.

3. Water is not a free good - at least its collection, transport, storage, treatment and distribution costs money. Water supply and sanitation services are not a social benefit to be financed by external donors or Government subsidies, but a service like all others which has to be paid for.

These should be the basic messages to all target groups. It should become accepted by them that there can only be one ultimate goal: full cost recovery to pay for investment and secure operation, maintenance and expansion of services.

4. Ultimate goals need not always be identical with realistic step by step solutions. The rate at which full cost recovery can be attained depends on the country, the target population (urban or rural), the ability of populations to pay, the sector (water supply, sewage disposal or sanitation), the availability of traditional alternatives to supply schemes and many other factors. Ultimate goals can, nevertheless, only be reached if certain defined first targets are set and met. In the case of cost recovery it is the coverage of operation and maintenance, be it by cash or services, which must be regarded as minimal input of the target groups, particularly in rural and urban fringe areas.

5. Since the attention of donors has shifted from residential and commercial urban areas to these periurban fringes and rural populations whose resources are most seriously limited, the cry for cost recovery should only be voiced if certain preconditions have been observed by our projects. Without going into details the following qualities of

a good Technical or Financial Assistance project leading to an affordable development should be remembered

- participation of the target group ( confidence-building, sensibilisation, information, acceptance, if possible involvement in planning-, construction- and operation -phases)
- use of appropriate, if possible low-cost technologies, tailored to the ability of the consumers to pay
- reasonable supply- and sanitation-standards and staged development concepts, avoiding over-designed and therefore under-used systems
- fair tariff-structures

6. Even if those preconditions have been met, underprivileged groups of society may not always be able to immediately and fully cover the costs of a scheme. In this case partial cost recovery by manual labour during the construction-phase and delivery of service for operation and maintenance will have to substitute actual pay of cash.

7. In all other cases the key-role in cost-recovery is played by the tariff-structure. The ideal solution looks like this:

- everybody profiting from a scheme pays; also those served e. g. by standpipes; flat-rates are applied if individual consumption cannot be determined.

- relatively low rates are applied to basic consumption ( e.g. up to 30 l / capita.day)
- beyond this steeply progressive tariffs discourage waste of water and allow for cross-subsidizing
- tariffs are adjusted in regular intervalls, depending on inflation-rates, etc.
- if on-site discharge of sewage and disposal of wastes is not feasible, water-tariffs incorporate and cover the costs for centrally organised services.

8. This key-role of tariffs and the call for regular checks whether or not they have to be updated should, however, not mislead decision makers to call for a raise of rates unless the necessity has been thoroughly investigated. First to be scrutinized are, among others:

- possibilities to reduce the number of staff in the responsible organisations (e. g. by streamlining job-descriptions)
- possibilities to reduce water-losses, e. g. by block-mapping and leak detection programmes, particularly for networks carrying expensive drinking water from the treatment-plant to the consumers
- possibilities to cut back the consumption of energy or chemicals by improving operation procedures

- possibilities to improve revenue-collection (e. g. by quicker billing for longer consumption-periods)

9. Willingness to pay and therefore chances for cost-recovery are positively influenced by a number of other circumstances.

- Initial tariffs of a new scheme should be oriented either at previous prices paid for water, e. g. to water vendors, or at the efforts to provide the water (time, resp. distance to well or standpost); this is important because experience has shown that water-rates which are felt as being too high, drive people back to their traditional sources of (usually polluted) supply.
- Trivial as it may be, it must be pointed out that good and reliable service drastically improves the willingness to pay. What was just said about traditional sources of water also applies here.
- Water meters are quite often damaged, destroyed or manipulated; regular checks by staff who may get an extra bonus for reliable work or risk to be fired if found to support such manipulation may significantly increase revenues. If this does not work the alternative is to forget about individual household water-metering and substitute it by bulk-metering for more or less homogenous consumer groups, applying flat tariff-rates.
- Big and "prominent" customers for water supply or sanitation-services like government bodies, military institutions, industries, hospitals or schools have to set a good example for willingness to

pay. The higher ranking or more powerful a customer is the more sensitive this question may become. Backing "from the top" has to be assured so that disconnections can be consequently executed. Countries are known where this happened even to Prime Ministers - who payed in the end!

- Consumers should - wherever possible - have direct influence and control over the entity to whom they pay their rates; this will be easier in rural than in urban communities. Means to ensure such a participation are for example hearings, cooperatives, consumer-committees or political parties.
- Control of management and expenditures of a service-organisation will usually be better if they are partly or fully owned by the consumers themselves.
- More efficient than monopolistic, central institutions which try to serve a whole country, are regional decentralized organisations close to the consumer.
- Parastatal or private authorities can usually be expected to have a more effective financial management und thus a better chance in regard to cost recovery than government bodies, because they are able to pay higher, performance-oriented wages and have - by way of budget autonomy - the right to use tariff-money exclusively for O + M and investment, without obligations towards the Ministry of Finance except paying taxes.

10. Finally a few words about chances to improve cost-recovery by engaging the private sector:

Surveys in towns and even villages will usually reveal that private activities play a greater role in water supply and sanitation than assumed.

Examples are water vendors who regularly turn up with their donkey carts and trucks, small contractors, who dig wells or pipe-trenches, mechanics, who do the plumbing, etc. As these private enterprises cannot afford to constantly lose money, cost-recovery is an in-built control mechanism. Supply, demand and competition, on the other hand, will usually regulate prices on a level fair to the customer. Our advice would therefore be to open the sector to private initiatives by allowing for sub-contracting, franchising and concessioning of (part-)services. Contracts should always be limited in time, to be extended only in case of reliable and efficient work. "Pilot-projects" should be small, for example licencing water-kiosks, with bigger involvement of the private sector, e. g. for construction work to follow in case of success in these pilot projects.

11. Even more than other issues of the Water Decade the cost-recovery problem calls for international information and coordination. Possibly nothing can be more detrimental to the willingness to pay of a population than widely differing policies of donors in regard to their demand for financial contributions to a project. Information exchange, in our opinion, is necessary particularly in two aspects

- stories of success and failure of specific projects or programmes
- terms of reference and results of pertinent studies

It is obvious that lessons learned in practical project-management, -appraisal and -evaluation are more valuable than any theoretical unproved theories and hypotheses. Mr. Goodman will present to you examples of how the financial situation of partner organisations was remarkably improved; he will try to analyse common conceptual elements of these success stories.

To know the terms of ongoing studies and the summary statements of publications helps to avoid duplication of efforts and enables donors to freely discuss and find consensus on possibly controversial issues. To mention a few: World Bank, with support by BMZ / GTZ is working on a study "Willingness and Ability to Pay for Water Supply and Sanitation in Rural and Suburban Areas", WHO is conducting an "Informal Consultation on Institutional Development, Cost Recovery in Community Water Supply and Sanitation" or UNDP is preparing a study on Institutional Development with inputs by Mr. Kalbermatten.

The findings and suggestions of studies and other papers can only be commonly analysed by meetings like this one and implemented in consensus, if they are known and coordinated within the international community of donors and recipients. This coordination and cooperation may seem cumbersome in the beginning. Splendid isolation in working on such documents admittedly avoids a lot of nasty investigative questions. We believe, however, that particularly in sensitive topics like Financial Management and Cost Recovery early harmonization of strategies and efforts will pay off in the end.