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Public-Private Partnerships

Cosatu held a workshop in Port Elizabeth early this year to focus on the role of public-private partnerships in solving the service delivery problems local government faces.

Speakers at the workshop included Chippy Olver of the Department of Constitutional Development (DCD), Sandra van Niekerk of the International Labour Research and Information Group (Ilrig), Mike Pienaar of Rand Water and Peter Wilson of the Port Elizabeth City Council. Enoch Godongwana, MEC for Economic Affairs, Environment and Tourism, opened the workshop.

The Eastern Cape Socio-Economic Consultative Council (Ecsecc) compiled this publication from presentations made at the workshop with added information about different models and approaches. The contents of this document are based on the views of the individuals and organisations quoted and in no way reflect the views of Ecsecc or its staff.

Introduction

The *White Paper on Local Government* that was launched in March 1998 is clear about the role of local government in service delivery. It should work together with local communities to find sustainable ways to meet their needs and improve the quality of their lives. This includes the provision of services such as water, sanitation, local roads, stormwater drainage, refuse collection and electricity.

The White Paper also states that the starting point must be to prioritise the delivery of at least a basic level of services to those who currently have little or no access to services. Three sources of revenue are suggested to achieve this:

- Capital grants from the Consolidated Municipal Infrastructure Programme
- Cross-subsidisation
- Private investment in municipal infrastructure

The document talks about "partners in resource mobilisation" and suggests a range of partnership options – among them *public-private partnerships* and *public-public partnerships*.

In the 1998 Budget Trevor Manuel singles out private-public partnerships as a tool to bring private sector finance into infrastructure projects. He states that a total of 18 pilot projects have been established countrywide in which the private sector has invested R1 billion.

The Labour unions and in particular the South African Municipal Workers' Union (Samwu) have opposed public-private partnerships (PPPs) from the outset. They see PPPs as a threat to job security but also feel that they undermine the democratic process.

This publication aims to focus on all sides of the service delivery discussion and add to the current debate.

Government's views

For the Government the problem is a simple one of growing demand and not enough means to meet it. That is the message from both the DCD's Chippy Olver and MEC Enoch Godongwana.

Godongwana says the privatisation debate is constrained by two extreme positions:

1. The first makes privatisation the "be all and end all of everything that is productive and efficient", and;
2. The second option rules out any kind of delivery of services by the private sector.

He says there is a massive backlog in service delivery in the Eastern Cape. This needs to be confronted but the resources are not available. While there is a commitment to delivery, debt is not to be increased. The Eastern Cape Government consequently continues to grapple with the question of delivering quality and accessible basic services at affordable rates.

In the next ten years a capital investment of R90bn will be necessary to provide basic services in urban and rural areas according to Chippy Olver. He says only R45bn will however be available to local authorities through grants. The rest will have to come from the private sector.

The challenge for the national government is the same as for the provincial government – to find mechanisms that will offer high-quality, low-cost services without increasing the national debt.

Government's solutions

Godongwana says the solution is to avoid extremes. Where infrastructure does not exist public sector capital should be engaged but on the terms of the people who will be the end-users of the service.

He urges workshop delegates to think of creative ways to approach the problem of service delivery, arguing that "the reality of our context requires creative thinking."

Olver says local authorities have two options to access private sector funds.

1. Borrow the money from the private sector.
2. Bring in the private sector to deliver the service and make profit the incentive.

Olver insists his department is not "married" to any particular privatisation option. In some cases the solution can be a "worker-turnaround process" (as supported by Samwu). In other cases the solution can be to use the private sector to manage some services but with the service remaining public property. Another option is community-based partnerships such as a successful refuse removal project in Gauteng.

He says it is important to choose those methods that will achieve the objective of efficient and effective service delivery.

Two processes are crucial for any of the above privatisation options to be successful:

1. There have to be properly designed contracts and legislation is therefore needed for contract-compliance measures.
2. Capacity building needs to take place at local authority level to ensure that municipalities can engage effectively and successfully with service providers.

Another view

Cosatu, and in particular Samwu, agree there is a crisis in service delivery. But for them the problem is government's insistence that the most appropriate solution to the crisis is private sector intervention.

Patrick Bond of the School for Public and Development Management at the University of the Witwatersrand, who attended the workshop, says Government wants to privatise because there was "not enough money flowing through the system". The Government blames the "culture of non-payment" for this. He argues the real problem is the severe budget cuts imposed by the Government on local authorities – up to 80% in some cases. Port Elizabeth has for example suffered a budget cut of 75%.

He describes the problem as one of insufficient political will to supply the public sector with the necessary resources to reform itself into an organ of effective and efficient service delivery.

Samwu adviser, Sandra van Niekerk, says two problems occur when the private sector becomes involved in service delivery:

1. The emphasis shifts from providing a service to users to supplying a product to consumers
2. The private sector will only get involved if it can make a profit.

These two factors have major implications for the community whose rights to basic services are now dictated by forces outside of their control. Democratically elected and accountable local government structures transfer their responsibilities to outside actors who are more responsible to their shareholders than to the community where they deliver the service. This makes it difficult for the community to take charge of its own environment.

The fact that basic services are now managed for profitability is also problematic. Van Niekerk says efficient service delivery is a basic right that should be managed with a non-profit orientation.

She also warns that the transnationals involved in privatisation processes in South Africa are powerful and experienced organisations. South Africa can therefore have the best intentions in implementing an appropriate regulatory framework and well-designed contracts, but if these are too restrictive, companies will simply go elsewhere.

As far as contracts are concerned, Van Niekerk points out that in most cases privatisation contracts are long-term – 25 – 30 years – and not easy to reverse. In the case of a contract being cancelled, the government usually has to step in, inevitably to the detriment of the taxpayer.

Privatisation also affects government policy because the government relies on money from an outside source and there can be a tendency for emphasis to be on infrastructure for which money is available rather than for infrastructure that is necessary. This can also result in incoherent planning.

Because of the financial resources that are required in most of the privatisation bids, only a few international conglomerates run the privatisation show. This leads to an increased concentration of wealth in the hands of a few.

An alternative?

Van Niekerk contests Olver's position that the state has less access to money than the private sector. She says the Government should have access to funds at more favourable interest rates than the private sector or at rates which are at least as favourable.

She says money spent on consultants to advise on privatisation processes should rather be channelled into the transformation of the public sector. She adds that when the private sector becomes a role player there is the added cost of monitoring private companies' performance. Another hidden expense is the cost of corruption that is almost invariably associated with privatisation, particularly in the form of procurement fraud.

Samwu wants the following to happen:

- improved governance

- increased community participation in local governance matters
- creation of partnerships to deepen democracy

Van Niekerk says she believes the Government has not put enough resources into public sector.reform. There should be an investigation into the possibilities for reform within local authorities. This process needs to include labour unions, communities and civic associations.

This reform or "turn-around" should address the following issues:

- financing existing debts
- service levels and tariffs
- re-organising the workplace by identifying racism, poor communication, wastage of resources etc.
- re-organising service delivery by drawing up a plan to improve it
- accountability between local authorities and the community.

"This is not a quick short-term solution but the Department of Constitutional Development has not put resources into this kind of process yet," she argues.

It is important to recognise the power of the elected councillors within a local authority. Van Niekerk says there is a tendency for local government officials to drive the councillors because the officials claim to be the ones with the experience and the know-how on council matters. This should not be the case. Councillors are elected to drive the transformation process and they should take that responsibility seriously.

What government is doing

The Government has set up the Municipal Infrastructure Investment Unit to assist local authorities in their engagement with privatisation agencies.

They have so far spent R1, 2 billion on 18 pilot public-private partnership projects throughout the country.

Among the privatisation projects that are up and running are:

- **Queenstown:** Water and Sanitation services of South Africa (WSSA) has been managing the town's entire water and sanitation system since 1992 on a 25-year contract.
- **Benoni:** Benoni Fire and Emergency Services was the first privately operated company to render emergency services on behalf of a local government in South Africa. The contract created more than 100 new jobs. The contract was for five years when it started in 1992 and has now been renewed.
- **Springs:** The municipal bus service was put on a five-year management contract in 1993.
- **Richard's Bay:** A taxi rank has been transformed into "Taxi City", a privately developed centre featuring shops, hawker facilities, ablution and recreation facilities for commuters.
- **The Billy Hattingh Municipal Refuse Removal Concept:** Billy Hattingh has developed a concept through which communities take part in rendering refuse removal services. Identified entrepreneurs are assisted in taking out loans for equipment, given full training and then start their own small businesses. After five years they take full ownership of their equipment. The service was introduced in KwaNdebele but has since spread to nine more areas throughout South Africa, creating an estimated 700 jobs.

[The above information is taken from *Partnerships*, a bi-monthly publication of the Development Bank of Southern Africa (DBSA) and the Department of Constitutional Development (DCD).]

What the unions are doing

As far back as 1996 Samwu met with the DCD to voice its opposition to the recommendations of the Municipal Infrastructure Investment Framework (MIIF) which suggested that the private sector was best placed to deliver basic services.

According to an article by Samwu's Roger Ronnie in the SA Labour Bulletin (April 1997), Samwu's approach to restructuring is to:

- Actively resist pressures to privatise municipal services
- Focus on local government employees as the key to expanded and improved services. This will be done by investing in training and skills development programmes and changing the way in which services are delivered
- Explore ways of securing finances for local government that promote the maximum use of resources and limit the influence of the private sector on the restructuring process.

The programme is geared towards:

- Resisting ongoing privatisation
- Re-asserting the role of the public sector in the ownership, democratic control and delivery of basic services.

Samwu has drawn up plans for the extension and ongoing supply of water to two pilot projects: Cape Town Metro and Johannesburg Metro.

Samwu demands:

- A moratorium on all major contracts under investigation and negotiation between individual local authorities and the private sector
- That information on all current contracts between local authorities and the private sector be made available to the union
- That further discussion on restructuring of the public sector is dealt with in the National Labour Relations Forum.

The options

In a draft discussion document published by the Department of Constitutional Development in February last year, four institutional options are described.

1. **Public ownership and public operation:** Infrastructure is owned and operated by a public entity owned and controlled by the central, regional or local government. The public entity operates the infrastructure service on a commercial basis. The public entity has a separate budget and financial autonomy based on tariff revenue. It operates as a business.
2. **Public ownership and private operation:** Through concessions and leases, the public sector gives infrastructure facilities to the private sector to operate. The private sector also carries the financial risk.
3. **Private ownership and operation:** This is the most attractive option to the private sector if the revenue potential from user charges is high and when the commercial and political risks are low.
4. **User provision or community self-help arrangements:** This option gives the people who are the primary beneficiaries from services the chance to also provide the service – effectively and at an affordable price. Particularly useful when smaller-scale infrastructure is at stake.

Of these options the Government is particularly interested in implementing the second and third options: Public ownership and private operation or the so-called Public-Private Partnerships (PPPs) and private ownership and private operation.

There are different implementation approaches for both the above options:

1. **Service contracts:** This involves contracting out specific operations and maintenance activities to the private sector. The public provider sets the performance criteria for activity, evaluates bidders, supervises the contractor and pays an agreed fee for the services.

2. **Management contracts:** A private firm manages the operations of a state-owned enterprise without committing its own investment capital or accepting full commercial risks for tariff collection or other matters.

3. **Leases:** A private firm operates and maintains the government-owned enterprise at its own commercial risk. Income comes directly from tariffs. Except for agreed-upon maintenance obligations the lessee does not invest in the infrastructure.

4. **Concessions:** The private operator manages the infrastructure facility, operates it at its own commercial risk and accepts investment obligations. The concession is a common model for water supply and treatment, ports, airports, railways and toll roads where governments want private investment but do not wish to relinquish ownership of assets. Forms of concessions are:

   - Build, own, operate, transfer (BOOT)
   - Build, operate, transfer (BOT)
   - Build, own, operate (BOO)
   - Build, transfer, operate (BTO)
   - Build, lease, operate (BLO)
   - Rehabilitate, own, operate (ROO)
   - Rehabilitate, operate, transfer (ROT)

5. **De-monopolisation and new entry:** While concessions involve temporary transfer of a government-owned facility to a private operator, this approach is to demonopolise a market segment in whole or in part and allow private investors to enter the market at their own risk. New private entry may be complementary to the existing public provider or in competition with it. The incumbent and often dominant enterprise remains the property of the government.

6. **Full privatisation:** The government sells its share in a state-owner enterprise. This is the strongest form of private sector involvement in the provision of infrastructure.

The international experience

In Buenos Aires the Argentine government entered into a concession agreement with a private firm in 1993 as part of a national privatisation programme to stabilise the economy.

Two and a half years after the private sector began operations, an additional 570 000 inhabitants had been connected to the water system (an increase of nine percent) and 340 000 people were connected to the sewerage system (a seven percent increase). During the same period the water production capacity increased by 26 percent and collection rates had gone up.

In Guinea water supply was reaching less than 40% of the urban population in 1989. After failing to reform the public water company, the national government entered into a lease arrangement to provide water services for the capital city of Conakry and 16 other towns. The water supply coverage increased to 52% between 1988 and 1994 and urban households equipped with water meters increased from five to nearly 95%.

But there is also another side.

In Peru after privatisation the cost of gas rose by almost 250%. The cost of lights went up five times and telephone rates increased six times.

In Germany, the water and sewage systems in Rostock were contracted out to a company called Eurawasser. In the original contract, the water price for the consumer was calculated on an assumed level of water consumption. However, in 1994 demand dropped. To continue making the profit they had originally counted on, in 1995 Eurawasser increased the price of water by 24% and sewage levies by 30%.

In Hungary in 1994, a company partly owned and run by Lyonnaise des Eaux (a company involved in several water privatisation bids in South Africa) won a water contract from the town of Kaposvar. Initially the company dropped the price of water, but by February 1996, it had risen by 50%.

In Britain, the price of privatised water rose 177% between 1991/92 and 1992/93. In addition, the number of disconnections rose dramatically because a large number of people were unable to pay their bills. In 1991/92 alone, 21 000 homes were cut off.

The public-public option

Rand Water was established in 1903 using an early form of the Section 21 Company legislation as a non-profit business structure. In terms of this framework the people of the region were the owners of Rand Water and the local authorities became the company's partners in water supply. Rand Water was specifically established to counter private sector profiteering during frequent drought spells.

Today Rand Water is the biggest water board in the world. It is non-profit and finances itself. Tariffs are set by the Minister of Water Affairs and are designed to recover costs.

Rand Water wants to assist the government, and in particular local government to ensure that all South Africans have access to water supplies and sanitation at a cost that every household in the country can afford.

Mike Pienaar, the Legal and Administration Manager of Rand Water's Community Based Projects Department, says Rand Water is a public body supporting public options. But, he says, both the public and the private sector have roles to play to improve service delivery.

Rand Water seeks a balance between urban realities, service delivery and democratic control – in other words a balance between political control and operational independence.

Consumers often find service delivery from government lacking and inadequate, particularly in the area of basic services like water and sanitation, electricity, telephones and transport. To overcome these problems there are five options:

- efficient and effective local government
- internal public corporatisation
- external public corporatisation
- public-public partnerships
- private-public partnerships.

Because it is necessary to manage the basic services infrastructure like a business and not a bureaucracy, commercial principles need to apply to the running of this infrastructure. It is also necessary to introduce competition, says Pienaar. In all of the above, it is essential to involve users and stakeholders in decision-making.

Rand Water operates on the basis of three guiding principles:

- Transparent communication with all stakeholders
- Awareness of all the options
- Maximum competition to ensure the best service.

Pienaar says a private-public partnership is just one of a number of options for effective service delivery. He says the private sector can be a useful tool if used correctly but it is no "magic bullet". "The question is whether privatisation is 'a solution' or 'the solution' to effective and sustainable service delivery", he says.

But, he argues, local authorities should keep in mind that the private sector has a different social perspective.

Water service delivery is a natural monopoly because it is uneconomical to duplicate networks and competition is difficult to achieve. It is also a capital-intensive industry involving long payback periods.

The problem starts when consumers resist payment of services because they feel they are getting little from local councils in return for their taxes. This leads to budget constraints that are compounded by a reduction in available subsidies from Government. Poorly maintained services – between 40 and 50% of water is unaccounted for – set a vicious cycle in motion of non-payment leading to bad customer service.

He explains the options of "internal public corporatisation" and "external public corporatisation" as possible public-public partnership solutions to service delivery.

Internal public corporatisation is when an operation is "ring fenced" and becomes a separate business unit. Local government then owns its assets and operates its facilities through the business unit.

When the local government opts for external public corporatisation it also ring fences the operation but a separate corporation is established to conduct the operation. The corporation owns the assets and operates the facility but the local government is the sole owner of the corporation. Local government can subsidise the corporation and the corporation can retain any surpluses it generated. Surpluses can also be paid to the local government to subsidise other services.

Water boards, such as Rand Water, are one "vehicle" for external public corporatisation argues Pienaar. Other options are companies for gain, section 21 companies, trusts and statutory water committees.

Privatisation in the Eastern Cape

According to Nomhla Hlahla of the Department of Constitutional Development's Municipal Infrastructure Investment Unit (MIIU), several privatisation projects are planned for the Eastern Cape. The Unit is unwilling to disclose the names of the local authorities involved in current discussions about proposed projects because Hlahla says the MIIU fears that union intervention might interfere with the process.

In Queenstown, Water and Sanitation services of South Africa (WSSA) has been managing the town's water and sanitation system since 1992. It is a 25-year contract. The Department of Constitutional Development has given the Port Elizabeth City Council R2 million to conduct a feasibility study into privatisation options for water and sanitation services.

Hlahla says Umtata and Grahamstown are also looking into privatisation models. She says there are also many privatisation possibilities around the Coega development.

Conclusion

Whether or not stakeholders in local government agree with privatisation, the delivery of effective and efficient services to communities remains a critical challenge for local government.

With the introduction of the Development Facilitation Act and the Local Government Transition Act (2nd Amendment Act), local authorities are compelled to involve communities in the planning and management of their areas. Because of this it is important that local people become involved and aware of the issues in the privatisation debate.

It is also important to look at the implications of privatisation for the Eastern Cape. Is it an appropriate solution to the inadequate service delivery and the uneven development that characterises the Province?

Nationally, the question arises whether privatisation will ultimately serve the principles of the Growth, Employment and Redistribution (Gear) strategy. Is it the most effective way to contribute to a strong economy in the long run? Is it the best way to deepen democratic principles and entrench accountability?

In this year's Budget speech Trevor Manuel said there were no short cuts to achieve sustainable growth and development. He said it required difficult choices and regular prioritising, arguing that "it demands a constant and honest evaluation of what we are doing and how we are doing it".

The people of South Africa require the same of all the stakeholders in the service delivery debate. ■

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