

In this issue, Fred Rosensweig and Jean de la Harpe discuss the following statement:

‘How should the financing of rural water supply be organized to support scaling up?’

Dear Jean,

Scaling up community management of rural water supply is dependent on a range of factors, but the most important may be the financial policies and the availability of adequate resources.

Financial policies must take into account three categories of costs – capital costs, recurrent costs, and programme costs – and find ways to pay them. Capital costs for rural water systems will largely come from donors and the national and local government budgets, although in some countries users do pay for a small percentage of capital investments. Recurrent costs – including operations and maintenance, depreciation and debt service – must be paid by users, although paying debt service is usually not feasible for rural populations. Programme costs – capacity building, sanitation promotion, hygiene behaviour change, and technical assistance – are generally paid by government and are not recovered through user fees.

In general, rural communities do not have sufficient household income to pay for the initial capital required for a community water supply system. These investments are usually paid from a combination of donor and government grants. Because resources are finite, government resources should not be used for the one category of costs that rural users can and should pay – recurrent costs. If governments subsidize recurrent costs, there will be less money available for investments and programme costs for unserved populations. Respecting this principle will become even more important as more people are served because of the increased level of recurrent costs. Some argue that poor people should not be required to pay recurrent costs, and cite the free water policy of South Africa as a model. While there will always be

some households that are too poor to pay their monthly user fees, there are ways to make adjustments for the poorest of the poor through progressive tariff schemes and direct subsidies.

Where will the resources come from to scale up? As discussed above, the first priority is to get the financial policies right and maximize the use of available resources by having rural users pay recurrent costs. Second, loan funds should be used for investments in those jurisdictions (generally large urban areas and some medium and small towns) that are creditworthy. Grant funds should then be directed to those that have no other realistic source of investment funds. Rural areas will certainly fall into this category. Third, as countries increasingly decentralize and investments become the responsibility of local governments, national governments must also get their municipal financial policies right so local governments have their fair share of national revenues as well as the ability to raise their own sources of revenues. For the foreseeable future, the majority of local governments in most countries will not be sufficiently creditworthy to be able to borrow money from commercial sources, although that should be the long-term objective.

*Yours,
Fred*

Dear Fred,

Getting the right financial policies in place is indeed the critical issue. However these policies must not only ensure that available resources are maximized, but also that the benefits of access to safe water are realized. It was this latter objective that brought about the introduction of a Free Basic Water Policy in South Africa. The policy is to provide poor households with a basic supply of water free of charge, being 6000 litres of safe water per household per month (based on the standard of 25 litres per person per day) within 200 metres of a household.

How the 25 litres is measured and delivered depends on the poverty relief option used. Where service-level targeting is used, communal standpipes are

most commonly used – everyone using a communal standpipe gets their water free. In this case there is no direct delivery control, but the distance which the water has to be carried makes the amount self limiting. (From experience we know that the average consumption of people having to carry water up to 200m is in the 2–4000 l/hhold/month range.) On the other hand, if water is delivered to tanks in the house’s yard, the system would limit the amount delivered to the free basic amount, and those wanting more can apply to pay a fixed monthly amount for the additional water.

There have been many debates about whether ‘free basic water’ is the right approach, whether it is feasible and sustainable and who should pay for it. However the starting point of any debate must be why this policy?

A famous South African story in this regard was a visit by our Minister of Water Affairs to a relatively new rural scheme. When he asked why so many community members were still using the polluted river he was told that they could not afford the monthly tariff (which equalled approximately US\$1.2).

The Free Basic Water Policy is based on the recognition that supply of water at a ‘basic’ level assists in alleviating poverty and minimizes health threats that affect the poor. The challenge is how to achieve the benefits of the policy whilst at the same time maximizing available resources so that rural water supply can be scaled up. In South Africa, this problem is addressed through the national fiscus (the pot of money which the government has for distribution or use) where government has established redistributive financial mechanisms in the form of two national grants to local government.

The first grant is an infrastructure grant to cover the capital costs of basic infrastructure for the poor. The policy framework for this grant defines what is meant by ‘basic infrastructure’ and who qualifies as being poor. The total allocation from the national fiscus to this grant is based on an infrastructure backlog and poverty formula. The second

grant is an operating grant called the Local Government Equitable Share, which is designed to cover recurrent costs. The policy objective behind this grant is ensuring *equity* so that people who cannot afford to pay for services still have access to basic services.

Water always has a value, but its value to the poor is often far greater than what is reflected in its costs.

*Yours,
Jean*

Dear Jean,

Thanks for reminding us about the importance of the poor having access to safe water. I couldn't agree more.

While I appreciate the explanation of the case from South Africa, I can't help but ask two basic questions. Is the approach affordable in the long run in South Africa? And even if it is, do you really think it's a viable solution for other developing countries? I have not worked in any country in the past 20 years that could afford to pay for recurrent costs on a large scale. After all, South Africa is by far the wealthiest country in Africa and the only one with the possibility of being able to afford such a policy and having the systems in place to implement it effectively.

Let's examine the South African example. The provision of grants for capital costs to cover basic infrastructure for the rural poor is entirely consistent with what I said originally. My issue is with the subsidies for recurrent costs. Perhaps you can explain how local governments determine who cannot afford to pay for services and how the central government uses this information to determine the size of the operating grants. This would seem to require a very good data collection and information system, which very few developing countries have.

My other concern with the free water policy is the issue of ownership. I take it as an article of faith that people value more those things that they pay for. Well-run systems that are 'owned' by the community are a source of pride and, as a result, are more likely to be maintained and provide sustainable services over time.

The issue of how to help poor people who truly cannot pay gain access to

services is important. Progressive tariff schemes and direct subsidies to the poor are two mechanisms that have been used to address this issue. In a recent visit to Bolivia, I asked the president of a community water committee serving fewer than 500 people what they do when there are people who truly cannot pay. The response was that they allow them to pay later, ask them to pay a reduced tariff, or temporarily suspend payment. The key point is that the community handles the issue themselves without external subsidies.

When looked at from a national perspective with the goal of scaling-up in mind, subsidizing recurrent costs on a massive scale means that less capital for infrastructure would be available in absolute terms and therefore ultimately the number of people with access is limited.

*Yours,
Fred*

Dear Fred,

I have no argument with your points, with one exception, that rural users 'can and should pay' recurrent costs. I dispute the 'can'. In many instances rural users cannot pay and this is why we need alternatives. Free basic water is one alternative. It is essentially a mechanism for cross-subsidizing a basic amount of water for those that cannot pay.

I am glad that you have raised the issue of how to help poor people who cannot pay for services because this is the crux of the matter – poor users and recurrent costs. The mechanisms you mention, namely progressive tariff schemes and direct subsidies are in essence the same as free basic water, where surpluses and subsidies are used to cover a basic amount of water to the poor.

In South Africa the approach is affordable in the long run so long as government continues to prioritize the allocation of resources to the free basic water policy. In some municipalities the subsidies need to be increased, but the South African fiscus is strong enough to provide for this.

With respect to other developing countries – no, I do not think it is viable, but this was never suggested. However as these countries move to

middle income countries, government subsidies for recurrent costs of basic water services for the poor is an option for consideration.

In terms of how a municipality determines who cannot afford to pay for services – households who fall within the 'poor household' definition (based on income), and who wish to receive free basic water, must register with the municipality. It is questionable whether this system will successfully target poor households. However, currently municipalities are applying free basic water to poor *areas* and this appears to be working effectively.

With respect to central government determining the size of operating grants, you are correct that it requires very good data collection and information systems. South Africa's central statistical service provides excellent statistics to the national treasury who determine with a fair degree of accuracy the subsidies (operating grants) to each municipality.

I agree that a sense of 'ownership' and consumer payments result in sustainable services. However, this can also be achieved to some extent through educating communities about the importance of a safe water supply and why they should look after it. Provision of this education is part of the definition of a basic water supply service.

In South Africa the lack of external subsidies resulted in communities resorting to unsafe water. Bolivia is a different story – and one cannot generalize.

We need to strike a balance between financial sustainability (charging users) and achieving equity (government subsidies) so that we reach the maximum number of poor households. Reducing subsidies will also reduce the number of poor who benefit from safe water – which means scaling down rather than scaling up.

*Yours,
Jean*

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