

# en breve



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## ARGENTINA

# The Salta Water Public-Private Partnership

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### Introduction

The 1990s saw a big drive to increase private sector participation in water services especially in Latin America. While there is currently less enthusiasm for the use of concessions and other public-private partnerships (PPPs), it is still instructive to inquire as to why certain partnerships succeeded where others did not. The case of a water concession in the province of Salta, Argentina provides an example of a successful PPP that survived despite its location in a poor province and a severe economic crisis. This paper posits that the Salta Water PPP's longevity is at least in part due to the spirit of cooperation between various levels of the government and the private operator. That cooperation is embodied by three contributing factors including: coordination across government levels and ministries, practical measures to extend service to the poor and a flexible contract. Stable financing from the Provincial Government was another key factor. Most notable is that this approach is in direct contrast to the 1990s trend where reforms focused on improving sector efficiency and reducing the drain on public resources. The use of a local private operator instead of a large international firm is also of interest. These lessons can be applied to future PPP schemes or other interventions in the water sector.

### General Background

Located in northwestern Argentina, the Salta Province, one of 23, covers 155,488 km<sup>2</sup> or 5.6% of Argentina's territory. With an estimated population of one million (about 2.9% of the total population of country), Salta has some of the most difficult social problems and lowest development in Argentina. Around 40% of Salta's urban

households are considered poor—a surprising 50% of the province's population.

Prior to 1982, a national public utility company provided water and sanitation (WSS) services in the main urban areas. After that, service provision responsibilities were transferred to provincial governments. Each province enacted its own provincial law defining water sector principles and objectives and the means to achieve them. Currently, most provinces have a combination of both private and public service providers and cooperatives; eight other provinces have concessions for main urban area services.

The public entity General Water Administration Authority (Administración General de Aguas de Salta, AGAS) provided WSS in 43 of Salta's 58 municipalities with a 76% coverage rate for water and 68% for sewage before Salta's water sector reform process began in 1996. Poor management and a number of other factors contributed to relatively low coverage and performance including the sale of land without access to basic public services (water and electricity), political groups that encouraged residents to connect illegally to the network in order to force AGAS expand the network, and, as is the case with many publicly-owned utilities in developing countries, a lack of investment in rehabilitation and maintenance which resulted in deteriorated infrastructure and low-quality service.

### Water Sector Reform

Salta's Water Sector Reform started in early 1996 when the Provincial Legislature delegated the power to

1 - This paper draws on a case study prepared by Gustavo Saltiel in 2003 for the Inter-American Development Bank, as well as interviews with Salta Government officials and SPASSA staff, mainly Daniel Nallar (ENRESP) and Jose Luis Guarch (SPASSA).

define the rules and procedures for concessioning State water companies to the Provincial Executive Branch of government. By December that year, the water company was put up for sale, the concessionaire selected, and the contract finally awarded in 1999.

Some municipalities opposed the idea of a PPP. In a strategic move, instead of just using its legal authority to force municipalities to enter into concessions, Salta's Provincial Government conducted a series of public meetings with local authorities to publicize the benefits of joining the concession. The newly created regulator's board of directors played a key role in gaining local government support by steering a number of public hearings with municipal authorities and user organizations.

WSS services were granted to the private concessionaire, Aguas de Salta S.A. (ASSA). ASSA, later called SPASSA, was selected through an international public tender. This company was controlled by MECON, S.A., an important construction company that had expanded to electricity generation, toll roads and oil extraction. In order to fulfill the technical assistance requirements contained in the bidding documents, MECON, S.A. signed a contract with the Brazil's Parana State public utility (SANEPAR). Later, the shares were transferred to Latin Aguas, S.A. that operates two other water concessions in Argentina.

After the contract was effective, ASSA began to service additional municipalities along with the original 43 it received. In some cases, the concessionaire initiated negotiations with the municipality while in others, local authorities approached the operator.

## **The Government's Commitment and Coordination**

Salta has well-developed coordination between provincial (including the regulator) and municipal governments. A Joint Working Commission handles difficulties in implementing the contract which supports productive relationships between stakeholders.

### **Local Governments and Users**

The PPP's main stakeholders are the Provincial Government (the granting authority), ENRESP (the regulator), Aguas de Salta (the concessionaire) and the users. Neither the regulatory framework nor the concession contract provided for the involvement of municipalities, but once the concession was granted,

*Box 1. The PPP's Performance : some of the concession's achievements:*

- Coverage increased from 76% to 96% for water supply and from 54% to 84% for sanitation
- The number of municipalities served by the concessionaire increased from 43 to 56 in 2005
- The percentage of population affected by service interruptions decreased from 32% to 8%
- Annual billing increased 56% from \$ARG 33 million to \$ARG 51 million
- Revenue collection reached 90% by combining billing with the electricity distribution company
- The total volume of water produced increased from 130 million m<sup>3</sup> per year to 165 million m<sup>3</sup> per year
- 95% of collected wastewater is treated
- A toll-free customer service line with capacity to receive 300 calls per hour was introduced

Finally, a clear indicator of this PPP's accomplishments is that it is financially healthy and continuously contributes to the investment program.

both the concessionaire and regulator recognized the need to engage local governments since services are delivered locally. Therefore, a strategy was designed to build bridges between these stakeholders which included the afore-mentioned public meetings with the municipalities and user organizations. Through some of these arrangements, SPASSA provides technical assistance (engineering, supervision, and general documentation for works) to municipalities; in turn, the municipalities and user organizations provide unskilled workers and materials to extend the systems. In some cases the concessionaire entered into arrangements with user organizations, but without the municipalities' participation. Since some of these arrangements encountered difficulties from political interference or from bankrupt contractors, the concessionaire now requires the municipality to be part of the arrangements. One hundred twenty agreements were signed between June 1999 and July 2002—85% of these were directly with municipalities while the others were with user organizations. Finally, a direct relationship between the concessionaire and local governments contributed to improving the communities' understanding, and likely acceptance, of the PPP.

### **Regulating the PPP**

The regulator of the partnership has been adaptable in its supervision contributing to the overall government

cooperation across levels and ministries to make the partnership work.

The Ente Regulador de los Servicios Públicos (ENRESP), an autonomous decentralized entity with legal standing in the province, was created under the purview of the Provincial Ministry of Employment and Development and is independent of the Provincial Ministry of Infrastructure and Public Services. The multi-sectoral ENRESP covers WSS, electricity and urban transport and is financed mostly through a charge of 2% included in the billing of the water and electricity operators. This financing arrangement grants the regulator autonomy from political authorities. Since the regulator's resources come from different service providers, the regulator's financial state does not depend on the fate of any particular operator. That is, if one provider fails, the regulator will survive since it will continue to work with others. Its main responsibilities involve:

- Tariff setting, monitoring and enforcement
- Monitoring and enforcement of water quality standards (service continuity, pressure, quality parameters, etc.) and sewage effluent quality
- Inspection and supervision of compliance with the investment plan (which includes a description of how service quality and efficiency objectives will be achieved)
- Sanctioning of the concessionaire in cases of non-compliance
- Primary adjudication of conflicts between WSS consumers or third parties and the concessionaire

The regulator is entitled to allow service provision under different standards in remote or isolated areas where service is deemed unprofitable. In cases when standards cannot be met due to technical or economic conditions, the regulator can grant temporary waivers allowing the concessionaire to provide service under lower standards. This innovative feature solves some problems in other concessions where uniform standards provided weak incentives for investment in poor areas and triggered endless legal disputes between the government and service providers.

### **Universal Coverage and Practical Implementation of Pro-poor Measures**

Universal coverage was one of the sector reform priorities which influenced the way the PPP contract was

*Box 2. Subsidies* - One important aspect of the government's support for the partnership is the funding it has committed for subsidizing low-income customers directly. The government uses a formula to determine a household's eligibility for the subsidy which considers income, housing characteristics, household size and number of students. The application process includes controls to ensure that only low-income households benefit from the subsidy program. Additionally, the government participated in financing the investment plan and approved tariff adjustments that allowed the concessionaire to reach financial equilibrium despite political opposition for such moves.

structured as well as the partnership's overall development. The Provincial Government and the regulator have been consistent in maintaining the pre-eminence of this objective and their actions have supported the concessionaire in achieving it. In contrast to other PPPs which also have a universal coverage goal, Salta's objective to extend service to the poor was concretized using practical tools such as a targeted subsidy plan sponsored by the government and a menu of permissible service levels. The Provincial Government contributes to achieving this goal by co-financing the investment plan and consumption subsidies from its own budget as well as approving tariff adjustments that allow the concessionaire to reach financial equilibrium. In fact, the Provincial Government has approved a series of tariff increases since the 2002 crisis in order to maintain funding for expansion of coverage while simultaneously guaranteeing the allocation of fiscal resources to continue subsidizing poorer consumers. In short, there is a virtuous cycle of improved service leads to increased support to the PPP which results in political willingness to grant tariff increases. In contrast, tariffs in most of the other Argentine water utilities have remained frozen since the crisis.

### **A Flexible Contract**

The concession contract has evolved as a partnership between the concessionaire and the provincial government. It is flexible for three reasons. First, it explicitly allows for its renegotiation and provides a framework that creates an enabling environment for collaboration between the concessionaire and the government. Second, it is possible to incorporate new priorities arising from the consumer and local

government participation during the decision making process into the contract. Third, as mentioned earlier, the contract allows the concessionaire to negotiate with the regulator on the levels of service to be provided in order to supply unprofitable areas. Although frequent renegotiations are not part of an advisable long-term policy, in this case it allowed the partnership to endure the ravaging 2001/2002 macroeconomic crisis.

## The Concessionaire: A Local Provider

The provincial government's decision to ignore the traditional paradigm of only permitting companies with significant previous experience in WSS to compete in the bidding process has allowed a strong local utility services provider to develop. The Province believed that a local company could be more responsive and flexible to its particular political context than a larger international company with more experience; however, technical assistance from a qualified regional water service provider in the beginning of the partnership was required. Later the concessionaire developed its own expertise—a major contributor to its success in obtaining additional concessions in Argentina and Peru.

## Conclusions and Lessons Learned

A number of considerations embedded in the contract and the Government's continuous commitment to make the Salta Water PPP sustainable in the long-term have contributed to its survival when others in Argentina failed. Coordination across government levels and ministries, practical pro-poor measures to expand service and a flexible contract were major reasons why this concession succeeded. The Provincial Government's stability and continuous finance of subsidies and the investment program have also been factors in the concession's success. Similarly, a number of experiences on Colombia's Caribbean coast, supported through the Bank-financed Water Sector Reform Project, demonstrate that a project can achieve results with stable long-term financing.

The Provincial Governments' decision to make the PPP work led it to take actions that facilitate an enabling environment for the partnership. There is considerable cooperation between the Provincial and Municipal governments as well as with the regulator. The use of practical methods to expand service to the poor includes subsidies and choice in level of service provided. Finally,

the flexible contract permits renegotiation, review/revision of priorities and varying quality of service avoiding the trap of endless court battles and disputes that other PPPs have experienced.

Lessons Learned from the Salta Water PPP include:

1. A water PPP can successfully use a local private partner which, in turn, can increase its capacity through the partnership.
2. Expansion of services to the poor requires practical measures such as targeted subsidies, flexible regulation and government (provincial and/or federal) participation in the funding for the investment programs.
3. Flexible service quality regulation is useful in avoiding interminable disagreements while still expanding the network especially to unprofitable or poor areas.
4. Municipal Government and user involvement is strongly correlated with successful results.

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