
The Big Greedy

A Background Check on the Corporations Vying to Take Over New Orleans' Water System

A special report by
**Public Citizen's
Critical Mass Energy and Environment Program
Washington, D.C.**

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This document can be viewed or downloaded at www.citizen.org/cmep.

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Fortune magazine recently called water "the oil of the 21st century." With a deepening global water crisis already imperiling the lives of hundreds of millions of people, private companies are presenting themselves to government agencies as knights in shining armor who will save the day by purchasing rickety water systems, whip them back into shape, and ensure that the tap won't run dry.

Riding into New Orleans are three corporations that, based on their checkered histories, have local citizens girding themselves for what is shaping up to be one of the dirtiest political battles in a city that practically patented government corruption. As more unseemly information about these companies has come to light, residents of New Orleans are starting to wonder who, if anybody, is looking out for their interests. The answer might be one they don't want to hear:

Nobody.

In 2000, New Orleans became the latest city to step onto the treacherous path of water and wastewater privatization after a team of financial advisors concluded that only a private company would be capable of holding down costs and rates as the city embarked on a \$1.3 billion capital improvement program. The upgrades are expected to raise water rates 45 percent and wastewater rates 39 percent over a mere four-year period.

When city officials went out for bid on the project in February, they were met with fierce criticism from those who found flaws in the bidding documents, and also those who are wary about privatization in general. Among the most vocal critics were the Bureau of Governmental Research, League of Women Voters, and employees of the city's Sewerage and Water Board (S&WB).

In retreat, the Board was forced to extend the deadline for citizens to submit comments on the proposal and to incorporate many of these concerns into the plan. Apparently missing from the final bidding documents,

however, are several crucial changes that the Board itself voted to include.

The prime movers behind the privatization drive are Mayor Mark Morial and City Council President Eddie Sapir. After initially hoping to wrap things up by the end of 2001,¹ the timetable has been pushed back to March 2002.² This would coincide with the mayoral election, raising the ugly possibility that the decision to turn the city's water system over to a private corporation was somehow sullied by political pressure.

Unless someone or something puts a stop to it, the privatization would be the largest of its kind in U.S. history. The company that wins the contract will run the city's water and sewer systems for as long 20 years.

Before the ink dries, however, citizens of New Orleans still have the opportunity to become educated about the sort of company that will be receiving their monthly checks for years to come. By all appearances, it won't be a company run by people you'd be likely to have over for dinner.

OMI Inc.

Operations Management International, or OMI Inc., was created by an engineering firm CH2M Hill in 1980. OMI specializes in managing water and wastewater facilities, but its engineering base allows it to also offer design and construction services — a combination that proves especially popular among municipalities handing out so-called design-build-operate contracts, or DBOs.

With today's popularity of one-stop shopping in water, wastewater and other industries, OMI is perfectly positioned for expansion. OMI has operations in the U.S., Middle East and Asia. Although OMI is small in comparison to its two competitors vying for New Orleans' water systems, its record gives more than enough cause for concern.

- In Bergen County, New Jersey, OMI was embroiled in a scandal involving County Executive William "Pat" Schuber. The official was accused of trying to force the privatization of the county's wastewater treatment facility to pay back his campaign contributors. OMI, its attorneys at Amoroso & Beirman, and CH2M Hill gave thousands of dollars to Schuber and to the local Republican Party.³ This past June, the Bergen County Utility Authority voted 3-1 against privatization, with Vice Chair Joseph Tedeschi expressing concerns that OMI's emphasis on profits would compromise maintenance and increase the risk of spillage and line breaks. Schuber considered whether to veto the decision,⁴ but in July he decided not to.^{4a}

- In May 2000, the City Council of Biddeford, Maine, voted unanimously to withhold a payment for operations and capital expenditures from OMI until the company fixed an odor problem at the city's wastewater treatment plant. City officials took action in response to numerous complaints from residents and business owners, who were regularly confronted with the smell of raw sewage.⁵

- Daniel Wallace, former director of the sewage system that OMI managed for the city of Georgetown, Texas, was charged with using

false invoices to buy more than \$200,000 worth of personal items with company money. City records also showed that Wallace set up a private company that procured a wastewater contract from the city. Even though the company denied that Wallace stole any city funds, OMI paid Georgetown more than \$100,000.⁶

- After OMI took over managing the water system of Clermont County, Ohio, residents saw their water turn brown for several weeks. Last August, county officials were forced to schedule a series of public meetings to address the problem. OMI executives explained that the color was caused by the flushing process it was using to purge the system.⁷

- OMI's operations also stirred a controversy in Oak Ridge, Tennessee, where the company operates the water system for a nuclear site. The workers there alleged that contaminated water caused some of the plant's employees to take ill. Richard Bird, a Boston physician whose specialty is occupational and environmental medicine, said polluted water sources may have been the cause of sicknesses. According to the workers, evidence suggested that water plant operators flushed the system before the water was sampled for possible contamination. The company denied the allegations.⁸

- In September 1999, an OMI-operated plant in Carol Stream, Illinois, dumped untreated and partially treated wastewater into Kline Creek for about 12 hours after a malfunction at the water reclamation center. The discharge lowered the levels of dissolved oxygen in the water, causing a fish kill.⁹

In bidding for the New Orleans contract, OMI will likely form a consortium with British Thames Water,^{9a} now owned by RWE AG, a German energy giant. Thames Water, the largest water company in England and one of the largest in the world, has been a key player in the British water industry since the country privatized its water in 1989. Based on its record, Thames Water is more inclined to put the interests of its shareholders before those of its customers:

- The company raised its rates by 99 percent (44 percent in real terms) during the decade following the 1989 privatization.¹⁰

- In 1995, Thames Water cut its investment in infrastructure by £350 million (\$490 million). Instead of taking the savings and reducing customers' rates — by about £10 per month per customer (about \$14) — the company used the money to boost its already high profits and dividends.^{10a} This transfer of additional public money to the private sector took place after a 50 percent rate increase over the previous six years.¹¹

- From 1989 to 1998, the company's pre-tax profits increased by 160 percent to £419 million (about \$603 million).¹² Thames Water's profit margins in England were almost seven times higher than those of the global conglomerate, Vivendi Water internationally.¹³

- In 1999 alone, the British Environment Agency documented Thames Water's involvement in 233 pollution incidents, resulting in eight prosecutions. Between 1989 and 1997, the company was prosecuted for environmental violations 31 times.¹⁴

United Water Resources

United Water Resources (UWR), formerly Hackensack Water Company, is a U.S. subsidiary of the French water giant Suez Lyonnaise des Eaux. Providing water and wastewater services to 7.5 million people in 17 states, UWR boasts that it holds five of the nation's largest water/wastewater contracts.¹⁵

Before it was acquired by Suez, UWR's 1999 revenues totaled \$362 million with a profit of \$33 million — more than doubling its profits in seven years.¹⁶ In 1998, UWR's chief operating officer Donald Correll pulled in nearly \$900,000 in salary and other compensation.¹⁷ (The most recent data is unavailable because after it was acquired by Suez, UWR ceased being a publicly traded company and stopped reporting its financial data to the U.S. Securities and Exchange Commission.)

Throughout its tenure as the second-largest private provider of water and wastewater services in the U.S., UWR has maintained a

unenviable corporate record. Here are some examples of past activities by UWR, some of its executives, and its parent company, Suez Lyonnaise, that do not speak positively of the company's track record.

- UWR's performance in Atlanta, where it secured a \$21.4 million water service contract in 1998, has been marred by complaints of poor customer service and inoperative fire hydrants. In 2000, some Atlantans started finding debris in their water, which also had begun to take on a brownish color. The company, however, did not initially acknowledge the problem.¹⁸ Four months later, many residents reported they were still experiencing the same problems.¹⁹ Even more complaints resulted from the company's failure to promptly repair broken fire hydrants, a problem that endangered the lives of residents. In response to residents' concerns, UWR executives said that testing fire hydrants after they were repaired was a city's obligation -- a claim that city officials rejected on the grounds that the company should ensure that hydrants are left working.²⁰ Moreover, residents filed numerous complaints about delays and slow service. In March 1999, for example, when the Breakwater Homeowners Association paid \$2,700 to have three meters installed, UWR told the association that the job would take 10 weeks. Six months later, the company installed the first meter.²¹

- In 2000, UWR executives from several states donated \$10,900 to Ralph Campbell's campaign to be elected North Carolina's state auditor — even though UWR has no subsidiaries in that state.²² Here's the connection: Ralph Campbell is a brother of Atlanta Mayor Bill Campbell.

- In 1997, UWR customers in the Florida counties of St. Johns, Duval and Nassau saw their rates increase by an average of \$9.44 per month, drawing no small amount of indignation. One local ratepayer, Richard H. Harlan Jr., was quoted in a Jacksonville newspaper as calling the company "the biggest bunch of highway robbers."²³ In 1998, the company requested yet another rate increase. The request was granted by Florida's Public

Service Commission in 1999. The water rates increased by another 12.5 percent and the sewage rates rose more 5.4 percent. While reviewing the rate hike request, the state's Public Service Commission discovered that UWR overestimated its expenses by \$1.05 million.²⁴

Finally, to the relief of local residents, the Jacksonville Electric Authority in 2001 agreed to buy out UWR's properties. Under public operation, the average residential rates are expected to drop by 25 percent.²⁵

- In 1996, the city of Jersey City, N.J., hired UWR to operate and maintain its water system. Today, just five years later, city officials no longer express much enthusiasm about the UWR's performance. According to Kathleen Deely of the Municipal Utility Authority (MUA), the city has learned that UWR's current performance is "no worse, no better" than MUA's past performance.²⁶ A senior MUA official reports that a lack of financial transparency prevents the city from evaluating whether the UWR's fees are reasonable. The company isn't required to open its books for public review. Instead, it just sends a bill to the city. Hard to believe as it may seem, the contract doesn't prevent UWR from overcharging its customers, because no review process is built into the arrangement.²⁷ Additionally, the company's customer service representatives often direct user complaints to the MUA, even in cases where the company is directly responsible for the problems — many of which should have been prevented in the first place. Moreover, a combination of broken meters and underpaid meter-readers working for a subcontractor frequently causes erroneous billing.²⁸

The record of United Water Resources' parent company, Suez Lyonnaise des Eaux, also deserves close inspection. Suez Lyonnaise des Eaux, the major component of Suez Group, is the world's largest water service corporation. With 110 million customers around the globe and \$30.1 billion in revenues in 2000,^{28a} this multinational behemoth possesses tremendous economic and political clout. And it has liberally used this clout to obtain contracts and expand its sphere of

influence.

In the last few years, Suez has been busy either acquiring or merging with water companies in Europe and the U.S. With the purchase of UWR, it aggressively entered the U.S. market. In 2001, it took over Environmental Systems Co. (Ensco), a leading industrial hazardous waste treatment company. Suez's business practices raise serious concerns:

- In 2000, Limeira City, Brazil tried to reclaim its water system from Suez. In the first five years of the contract, Suez invested only 18 million Brazilian Real (BRL), far short of the 36 million BRL investment requirement specified in the contract.²⁹

- In 1996, government officials in Grenoble, France, and a senior executive of Lyonnaise des Eaux received prison sentences for bribery relating to a contract award.³⁰

- Typically, Suez contracts are secretive, as with most water companies. For example, its contract with a South African municipality states: "The documentation contained herein has been developed exclusively by the operator (WSSA) and shall not be disclosed to third parties without the written approval of the operator."³¹

U.S. Filter

U.S. Filter is a subsidiary of another French giant, Vivendi Environnement, which provides water and wastewater management services in some 100 countries via its Vivendi Water Division. Vivendi is part of Vivendi Universal, a conglomerate that also includes Universal Music Group, Universal Studios and telecom provider Cegetel. In 2000 Vivendi Environnement had revenues of EUR 26.5 billion (about \$24 billion) and profits of EUR 3.5 billion (about \$3.2 billion).³² U.S. Filter is four times larger than the nearest U.S. competitor.³³

New Orleans and its Sewerage and Water Board (S&WB) are already intimately acquainted with U.S. Filter, as the company operates the city's wastewater treatment system. Professional Services Group (PSG) signed the original contract in 1992 but was

soon bought out by U.S. Filter, which, in turn, was acquired by Vivendi. Based on their track records, none of these three companies inspire much confidence in their ability to responsibly steward public resources. Further, U.S. Filter's decision to purchase the scandal-tarnished PSG raises question about U.S. Filter's judgment.

- On July 26, an electrical fire interrupted for two and a half hours the operations of New Orleans' East Bank Sewage Treatment Plant, which serves 440,000 people and is operated by U.S. Filter.³⁴ Raw sewage backed up, covered surrounding property and made its way through some of the plant's offices. The plant's operators diverted the untreated raw sewage into the Mississippi River for two hours before the plant returned to operation.³⁵ City Councilmember Jim Singleton said S&WB officials told him that U.S. Filter was aware of the equipment problems for several weeks and knew they could cause serious damage, but took no action.³⁶ The fire came only a few months after two broken incinerators caused excess, untreated sewage sludge to be removed from the facility in trucks. Residents of the Arabi Park and Carolyn Park neighborhoods of St. Bernard Parish were exposed to the stench for more than two months.³⁷

- The dirt of the operation wasn't limited to how the sewage was handled. It extended to how the money was handled, too. This past May, former S&WB member Katherine Maraldo and three former PSG executives were indicted with giving a \$70,000 bribe to Maraldo, who in turn recommended that the city renew its wastewater treatment contract with PSG for five more years. The company allegedly falsified records to cover up the bribes. PSG's former president, vice president and a consultant (who was once the company's vice president) were also charged with, among other things, conspiracy and mail fraud — charges that could land them up to 50 years in prison. Aqua Alliance, PSG's parent company, agreed earlier to plead guilty to the charge of bribery and pay a \$3 million fine. At the time the payments were made, PSG was not owned by U.S. Filter.³⁸ It is unclear whether

U.S. Filter has replaced all PSG staff members who were involved with the scheme.

- Between 1996 and 1999, PSG gave \$700,000 to two close associates of Joseph P. Ganim, the mayor of Bridgeport, Connecticut, in order to obtain a contract to operate the city's wastewater treatment plant. According to a local press account, one of the mayor's associates "told a PSG employee that the company had to pay — or forget about doing business in Bridgeport." Instead of walking away from the situation, PSG paid the money and received the contract. This past June, the mayor's two associates pleaded guilty to federal charges of bribery, fraud and tax evasion in connection with the plot. Despite the fact that PSG agreed to make what local press accounts termed "kickbacks," federal prosecutors do not believe that the company committed a crime, and that the scheme was initiated by the mayor's associates. However, prosecutors are continuing to investigate allegations of improper payments by PSG to public officials in Bridgeport, as well as in New Orleans.^{39, 39a, 39b, 39c}

- U.S. Filter shareholders took Vivendi to court over allegedly illegal payments the corporation made to U.S. Filter executives in exchange for their support of Vivendi's effort to acquire the company.⁴⁰

- Bribery mars Vivendi's international record, too. In 1997, Vivendi executives were convicted of bribing the mayor of St-Denis, France, to obtain a water concession.⁴¹ And the former mayor of Angouleme, France, admitted accepting \$55,000 from Générale des Eaux in exchange for awarding a contract to the company.⁴²

- A 1999 report on Vivendi's operations in Puerto Rico by the Office of the Comptroller criticized the company for deficiencies in maintenance, repair and operation of Puerto Rico's water and wastewater system. The comptroller charged the company with failing to provide running water in many areas, and with providing customers with bills but no water.⁴³ All the while, the water supply to U.S. military bases and tourist resorts was never interrupted.⁴⁴

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Top 10 Reasons to Oppose Water Privatization

The World Bank has predicted that by the year 2025, two-thirds of the world's population will run short of fresh drinking water. Given such a grim future, it comes as little surprise that *Fortune* magazine recently defined water as "the oil of the 21st century."

The natural response to such a scenario would be to concentrate energy and resources on protecting existing supplies, enhancing conservation efforts, helping vulnerable populations, improving pollution control initiatives and raising public awareness about an impending crisis that could threaten the lives of hundreds of millions – perhaps *billions* – of people. Moreover, such a crisis could unleash an environmental cataclysm from which the planet could never recover.

Unfortunately, this is not the thinking of corporate executives and, increasingly, government officials throughout the world. Instead, more and more of them are proposing to transfer the control of this precious resource from the public sector to the private sector. Today, one cannot avoid

hearing the word "privatization" when the global water crisis is discussed.

Given the track record of corporations that have begun to privatize water systems, and given how privatization has wreaked economic, social and environmental havoc on other utility industries, there is no reason to believe that corporations will demonstrate more responsible stewardship practices if they gain control of drinking water systems.

It is no underestimation to say that the very survival of billions of people could rest on decisions being made today – behind closed doors, in most cases – in corporate boardrooms and government offices throughout the world. With each drop of water that falls into the hands of private interests, any sustainable solution to the global water crisis moves further and further from the public's grasp.

Here are 10 reasons – among many – why the privatization of drinking water supplies could spell doom for many of the world's 6 billion-plus people.

1) Privatization Leads to Rate Increases

Rate hikes have been used in the United States and other countries as a way for private water companies to maximize profits. The bottom line for these companies is profit, which translates into higher prices and inferior service for consumers. The companies are under no obligation to provide water or service when water is defined as a marketable commodity rather than a human right. Thus, when consumers can no longer afford the price increases, water delivery is simply shut off.

Rates have increased in many U.S. communities where water has been privatized, disproportionately affecting low-income families and small business owners. In Pekin, Illinois rates increased 204 percent over the 18 years Illinois-American, a subsidiary of American Water Works Co., ran the water system, according to city manager Dick Heirstein.¹ While the water companies justify these increases as necessary to offset the costs of upgrading the infrastructure, profits and executive salaries continue to grow. In 2000 the American Water Works CEO's compensation exceeded \$2 million.²

In the decade following the 1989 privatization of England and Wales' water system, water companies there did not invest in infrastructure, claiming profitability would be compromised. Consumers, however, saw their rates increase by 102 percent (46 percent in real terms).³ During that time the number of people who had their water shut off rose by 200 percent.⁴

These privatization-induced rate increases have been most devastating in the developing world, often forcing people to choose between food and water, and unleashing epidemics of water-borne diseases. In Nelspruit, South Africa, water rates increased by more than 400 percent between 1995 and 2000, resulting in a cholera epidemic when people were forced to drink from the river. The people demanded cancellation of the contract with the British company, Biwater.⁵ The case remains unresolved and Biwater is still in operation.

Currently, a series of legal precedents are being established by trade agreements and contracts between water companies, governments and organizations such as the World Bank and World Trade Organization (WTO). These agreements cushion the business risks involved in privatization by passing the costs on to consumers. In the United States, for example, rate hikes are usually subjected to approval by the appropriate government authorities. But under rules either already on the books of the North American Free Trade Agreement (NAFTA) or currently being negotiated under the auspices of the General Agreement on Trades and Services (GATS), municipal governments could be prevented from protecting their citizenry from losing control of their water.

Rate arrangements between water companies and governments are a prime example of corporate welfare. This means the governments guarantee the companies will make a certain margin of profitability, thus minimizing their risk. Ironically, this practice is contrary to the very philosophy of free-marketeers, which is to end subsidies to public utilities and reduce the role of government in business operations.

2) Privatization Undermines Water Quality

Because the profit motive drives the corporate agenda rather than serving the public interest, environmental standards are continually compromised. In the United States, the National Association of Water Companies (NAWC), representing the private water industry,

intensively lobbies both Congress and the Environmental Protection Agency (EPA) to prevent higher water quality standards from being adopted. NAWC continually requests that all federal regulations be based on sound cost-benefit analysis. What this means is that public health is compromised for the sake of higher profits.

A notable example comes from the small town of Walkerton in Ontario, Canada, where seven people died and 2,300 others became ill as a result of *E. coli* contamination in the drinking water.⁶ A&L Laboratories, the private company contracted to test the water, knew that the water was contaminated. But under regulations intended to encourage privatization, the company was not required to alert government officials about a public health crisis in the making.⁷

Moreover, the contamination problem was revealed in a federal government study several years earlier, but the study was lost in the privatization frenzy. Eventually, the Drinking Water Surveillance Program, which tested for *E. coli*, was closed down altogether.⁸ The rush to privatize blocked the initiative to require that water testing labs be fully accredited, a regulation that would have taken two years to implement. As it turned out, the private lab testing Walkerton's water at the time of the tragedy was not accredited.⁹

While privatizing water testing in 1996, the Canadian government ordered the Department of Environment to cut its budget by more than \$200 million within two years. As a result, more than 750 employees were laid off, and the ministry's role in monitoring water safety was diluted. A former government official acknowledged that Ontario authorities were aware that these budget cuts would endanger both public health and the environment, but this information was not made public.¹⁰

3) Companies are Accountable to Shareholders, not Consumers

In many cases, the deals that water companies make with government agencies include exclusive access to distribution for 25 or 30 years, effectively sanctioning a monopoly. These private monopolies tend to undermine accountability and result in poor customer service. The company is under little pressure to respond to consumer concerns, especially when the product in question is necessary to the lives of consumers.

Puerto Ricans experienced the disastrous effects of a private water monopoly when, in 1995, Puerto Rico contracted the management of their water authority, PRASA, to the largest water multinational in the world, Vivendi, through a subsidiary now called *Compania de Aguas*.¹¹ Four years later, the Puerto Rico Comptroller's Office issued a scathing report on the many failures of the arrangement, ranging from problems with the repair and upkeep of aqueducts and sewers, to delinquency in submitting required financial reports. Consumer complaints and inquiries were regularly ignored, and there were accounts of citizens not receiving water, but being charged all the same.¹²

While the company was neglecting its duties, its finances also went down the tubes. Under private management, PRASA's deficit reached \$241 million, requiring the Government Development Bank (*Banco Gubernamental de Fomento*) to intervene and provide the agency with emergency funding, according to the Comptroller's report.¹³

4) Privatization Fosters Corruption

The very structures of privatization encourage corruption. Checks and balances that could prevent corruption, such as accountability and transparency, are conspicuously

missing from the process. With water contracts being worked out behind closed doors, executives and government officials are free to make deals in their own, rather than in the public, interest. Executives of Vivendi, Suez Lyonnaise de Eaux, and other water companies, for instance, have been convicted for bribing government officials to obtain contracts.¹⁴

Bribery is commonplace during the bidding process, which is generally closed to the public. Despite calls to expose the bidding process to the light of day, water companies claim that doing so would damage their commercial interests. For the same reason, the water contracts themselves are not made available to the public – even though the public is subject to the terms of these contracts. Moreover, financial information is rarely disclosed, even when the company is obliged to do so. In the French city of Metz, for instance, a private water company failed to submit accounts to the city council for 20 years.¹⁵ And, companies such as Bechtel and Biwater have even more leeway in keeping deals and operations secret because these companies are not publicly traded.

New Orleans experienced a privatization scandal in 2000 when Aqua Alliance Inc., the parent company of PSG, admitted giving more than \$70,000 in bribes to Catherine Maraldo, a member of the New Orleans Water and Sewage Board. In exchange, Maraldo recommended that the city renew its wastewater treatment contract with PSG. Maraldo and three former PSG executives were indicted on counts of conspiracy, mail fraud and interstate travel in aid of bribery.¹⁶

5) Privatization Reduces Local Control and Public Rights

When water services are privatized, public control is transferred to a corporation, be it domestic, foreign or transnational. Once water rights have been signed over, very little can be done to ensure that the private company will work in the best interest of the community. Again, the prime directive of private water companies is to maximize profits, not protect consumers.

In the Ohio community of Huber Heights, Ohio Suburban Water, a subsidiary of American Water Works – the largest private water company in the U.S. – tried to maximize its profits and minimize its investment by serving customers outside Huber Heights using the city's infrastructure. Many city residents complained that people living in these outlying areas were benefiting from the water service but not paying taxes to support water projects, and they argued that these areas should be annexed so that the local government could collect taxes. Company executives ignored the residents' request and went ahead with their plans. Ultimately Huber Heights re-acquired its water system, but the contract continues to cause legal problems.

6) Private Financing Costs More Than Government Financing

When water services are privatized, there is often a false perception that the financial burden has shifted from the public to the private sector. So the story goes, the company promises to repair, upgrade and maintain infrastructure, seemingly saving the taxpayers money. In reality, the public pays for these projects through their monthly bill payments. Tax-free public financing usually translates into lower-cost projects. Taxable private financing, however, invariably brings with it higher interest rates. As a result, the consumers – who are already paying executives' salaries and dividends to shareholders – are also forced to make these higher payments on company loans.

When the Swedish public water system was compared to its privately owned counterpart in England, the study revealed that the public system had lower operation and maintenance costs, and that customers paid less for their water. In England, both the operation costs and customer rates were more than double than those in Sweden.¹⁷

Throughout the U.S., towns and cities – many still using century-old pipes – are in desperate need of repairs and upgrades to their water and wastewater systems. The Water Infrastructure Network estimates that system improvements will cost \$23 billion annually over the next 20 years – \$11 billion more than what is currently being spent.¹⁸ Increasingly, local governments are having trouble raising such large amounts of money without increased federal assistance, which has dwindled since the Reagan administration. Large utility corporations are taking advantage of this dilemma by offering to buy their water and wastewater systems, and perform the needed repairs. What the companies don't make clear, however, are the hidden costs involved in such schemes.

Public financing is a politically sensitive issue because of upward pressure on taxes. San Francisco Mayor Willie Brown recently said that a bond measure, necessary to replace the city's aging infrastructure, would amount to political suicide.¹⁹ But the bottom line is that money for system improvements must be raised one way or another. If funds are not raised through taxes, then they will be raised through rate increases and other private methods that the public has little power to influence, due to a lack of information and lack of transparency. In the long run, public financing saves money.

7) Privatization Leads to Job Losses

Privatization often leads to massive layoffs, at times putting service and water quality at risk due to understaffing. Layoffs are commonly used to reduce costs and increase profits. Such layoffs are not only devastating to workers, but also to consumers.

Following privatization in the England, for instance, the number of employees in water and wastewater in 10 major companies was reduced by almost 10,000 over a 10-year period. In most cases, the companies responded to demands for lower rates by laying off employees.²⁰

In the Philippines, thousands of workers – half the original workforce – were laid off following the privatization of the Metropolitan Waterworks and Sewerage System. Some of these workers had put in more than 20 years of service with the company, and their families and retirement were put at risk by these cost-cutting measures.²¹

Privatization has caused American workers to be laid off as well. In Indianapolis, the water industry's self-proclaimed model city for privatization, nearly 200 workers were laid off between 1994 and 1998 following the privatization of the city's wastewater treatment system.²²

8) Privatization is Difficult to Reverse

Once a municipality signs over part or all of its water system to a private water company, withdrawing from the agreement borders on the impossible. If the company fails to live up to its end of the bargain, proving breach of contract is a difficult, complicated and costly proposition. Multinational trade agreements such as the GATS and NAFTA provide corporations with powerful legal recourse. A private company can use NAFTA's closed tribunals to challenge the reversal of privatization as being a NAFTA-forbidden action tantamount to an "expropriation."

Under GATS, once a service is privatized, the WTO's rules also give special protection for private investors. In deals brokered by the World Bank (which often makes water privatization a condition for a loan), companies are usually guaranteed a cash payment for expropriation if a government agency decides to bring water back under public control.

A recent case filed under NAFTA's Chapter 11 investment provisions provides a classic example of what can happen when water and water systems become commodified and privatized. Sun Belt Water Inc. of California sought to suck up tankers of bulk water from lakes in British Columbia and export it to California. In response to public pressure, Canadian government officials denied the request and proceeded to pass a law prohibiting such bulk water exports in the future. The company's challenge to this decision was unsuccessful in British Columbia's courts. However, as a foreign investor to which NAFTA grants new rights and privileges, Sun Belt took its case to NAFTA for arbitration, seeking \$10.5 billion in damages.²³ Analysts suggest that Canada does not have a strong case. In the event of its defeat, the country would either have to allow bulk export of its water or pay billions of dollars in damages to compensate Sun Belt for future expected profits the company would have gained if it had been allowed to sell the lake water. Under current NAFTA provisions water remains in the public domain, but once a decision to privatize has been made water must be treated as any other freely-traded service. If a municipality tries to reclaim its water, it will have to compete with financially potent, well-connected multinational giants.

Even within the United States, under the light of democracy, reversing the privatization of water resources is a difficult proposition. The City of Chattanooga, for instance, tried to buy back its water system from Tennessee-American – another subsidiary of American Water Works – in response to the company's exorbitant fire hydrant rates. During the course of the highly publicized battle, Tennessee-American paid lawyers and public-relations firms more than \$5 million. Unable to keep up with the company's campaign, the city ended its buyback efforts in September 2000. In an out-of-court settlement, the company agreed to reduce its fire hydrant rates from \$301 to \$50 a month over a two-year period, but it did not allow Chattanooga to reclaim its water system.²⁴

9) Privatization Can Leave the Poor With No Access to Clean Water

Contrary to public assertions, the role of the IMF and World Bank in water privatization schemes in the developing world actually results in a *reduction* of access to water for the poor. "Structural-adjustment" programs forced upon governments seeking loans often include water privatization as a condition for these loans. Impoverished, politically enfeebled countries are hardly in a position to refuse the conditions of the IMF and World Bank, as doing so would cause them to default on their debts. As a result, the IMF and World Bank are able to provide lucrative and virtually risk-free contracts for multinational corporations.

For instance, Bolivia's public water system was recently privatized as a condition for a World Bank loan. The private water company, Aguas del Tunari, immediately doubled water prices. For thousands of families, their water bills accounted for a fourth of their monthly budgets, while other families had their water turned off completely. Hundreds of thousands of Bolivians protested and were met by their government with violence. Bechtel, Aguas del Tunari's parent corporation, finally backed out but is threatening to sue Bolivia, South America's poorest country, for nearly \$40 million in losses under an "expropriation" clause.²⁵

10) Privatization Would Open the Door to Bulk Water Exports

The World Bank has predicted that by the year 2025, two-thirds of the world's population will experience water shortages. Even today, large masses of people around the globe lack access to clean water. Population increases and the dwindling supply of clean fresh water creates a formula for disaster, providing multinational corporations with vast opportunities to reap hundreds of billions of dollars dealing in what *Fortune* magazine calls the “oil of the 21st century.”²⁶ It goes without saying that those who control this precious resource will exercise economic and political power at almost unimaginable degrees.

Fully aware of the bleak prognostications, corporations are in a mad dash to obtain access to fresh water that they can sell at huge profits. Global Water Corporation and Aquaroute Inc., for instance, are expanding their water holdings – both in the form of full ownership and easements (rights to limited use). Even now, companies that work directly with municipalities can request permission to export water outside of their home regions. An agreement between Cadiz Inc. and the Metropolitan Water District of California, for example, will allow the corporation to sell up to 30,000 acre-feet of water a year to third parties through publicly owned pipes.

Bulk water exports could have disastrous consequences. First, massive extraction of water from its sources upsets ecological balance, resulting in damage to natural habitats. So much water is sucked out of the Colorado River, for example, that the waterway no longer reaches the sea.²⁷ Neither does the Rio Grande, a river that has long established the border between the U.S. and Mexico. Failure to protect the Earth's fresh-water systems has already driven 20 percent of the planet's fresh-water fish into extinction or near-extinction.²⁸

Disregarding sustainability concerns, Cadiz wants to extract water from California's Mojave Desert without even knowing how much water is available in the aquifer. The U.S. Geological Survey reports that the estimate by Cadiz and the Metropolitan Water District of California that 750 billion gallons of water can be extracted over 50 years is an exaggeration.²⁹ The Survey also criticized Cadiz's estimates of the likely recharge rates. Conservationists and hydrologists echo this criticism, claiming the area could support only 5,000 acre-feet a year – one-tenth of the 50,000 acre-feet projected by Cadiz.³⁰

Such companies are embarking on a dangerous enterprise. The disruption of an aquifer's status or configuration often results in complex damage to the environment and socio-economic standards. These changes can be difficult to foresee, and once they occur, they are difficult or impossible to remedy. Groundwater is currently being extracted at unsustainable rates. For both economic and technical reasons, once aquifers are emptied or polluted, they are almost impossible to restore.³¹

Conclusion

Water is one of the most basic human needs. Many nations and traditions, in fact, consider water a human *right*. If water rights are handed over to entities whose declared purpose is to maximize profits rather than to serve the public good, hundreds of millions – perhaps billions – of people will be elbowed out of their access to water. Multinational corporations are quick to argue that market forces would bring more efficiency to water systems. But the bottom line is that water resources – by their very public nature – require public oversight to ensure that people, not profits, come first.³²

Notes

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New Orleans' Effort To Privatize Its Water And Sewer Systems: An Analysis

September 2001

Last year, the city of New Orleans began the process of privatizing its water and wastewater systems after a financial advisor recommended hiring a private company to operate, maintain and manage the systems.

The advisor believed that only privatization could avert rate increases as high as 45 percent for water and 39 percent for wastewater over the four years when the city will spend \$1.3 billion on capital improvements to the systems.¹

In February 2001, the New Orleans Sewerage & Water Board (S&WB) released a draft of the documents calling for private bids – the “request for qualifications/request for proposals” (RFQ/RFP). The original time schedule gave the public only 10 days to comment on a very long and cumbersome document. In the wake of public protest, the S&WB agreed to extend the period by four months and pledged to review all public comments.

The Criticism: Swift and Sweeping

Several civic organizations, though not necessarily opposed to privatization, did, however, offer negative assessments of the RFQ/RFP. Among them was the New Orleans Bureau of Governmental Research (BGR), whose report, partially funded by the New Orleans Chamber of Commerce, was instrumental in modifying the proposal.

The BGR outlined several challenges facing

the S&WB, namely those dealing with operations, finances and governance.

According to the BGR, the operational challenges involved maintaining and repairing a system of pipes and pumps situated in unstable soil, and implementing upgrades necessary to comply with increasingly stringent environmental standards.

Financial challenges involved shrinking grant funds, lack of sufficient rate increases and a 1998 agreement with the U.S. Environmental Protection Agency to do nearly a half-billion dollars worth of sewer repairs over 10 years.

Finally, governance challenges involved the Board's lack of independence; all of its members were either elected officials or appointed by the mayor.²

Additionally, the BGR offered the following criticisms:

- ◆ The RFQ/RFP had ambiguous selection criteria, and the document lacked certain protocols and adequate selection guidelines.
- ◆ The RFQ/RFP had no fewer than 18 different bidding scenarios, a complication that the BGR said would discourage bidders from coming forward. The BGR also asked for an extended time period for prospective bidders to review S&WB records and visit facilities.
- ◆ The BGR recommended that bidders not only demonstrate that none of their officers or affiliates had ever been convicted of fraud in the U.S., but also in other countries. The Bureau

also noted that the RFQ/RFP did not require the disclosure of arrangements among bidders and people capable of influencing the process. And, the draft did not require disclosure of payments, gifts or contributions to local politicians.

◆ The Bureau criticized several contract provisions that had the potential to undermine cost savings by facilitating patronage and providing an opportunity for ambiguities in the division of responsibility.³

Despite the criticisms, the Bureau found that managed competition – inviting private firms and the city employees to bid on the contract – would produce better results than would restructuring within the S&WB.

The Sewage & Water Board met in June and July to evaluate the public comments. On July 25 it amended the RFQ/RFP to address some of the criticisms, such as reducing the number of bidding scenarios.⁴ And, the new RFQ/RFP more clearly outlined the criteria by which bidders would be evaluated, and established a detailed point system to grade bidders on their cost effectiveness, technical approach, employee compensation and commitment to hire minority- and women-owned contractors.⁵ The new RFQ/RFP also made clearer the board's intent to comply with state public bidding law.

A 13-member Special Evaluation Committee (SEC) will rank the proposals and direct the best bids to the S&WB, which will in turn create its own ranking.⁶

The Timetable: What's the Hurry?

Still, the proposal comes with a fast-paced timetable – a sure reason for concern. Bids are due by December 21; the SEC will complete its rankings by January 4 and submit them to the S&WB on January 8; the Board will make its decision by January 23 and sign the contract on January 30.^{6a} The speed of a process of such extraordinary complexity that requires intense attention to detail has raised questions about the ability of review panels to devote the time needed to do a thorough job.

Moreover, the Board's signature is due to come just three days before the mayoral election. And the contract would become effective on March 1, the day before the mayoral runoff election. In order to meet these deadlines, the

SEC will have to work through the Christmas holidays.⁷

The timing of this fast-track privatization process vis-a-vis the mayoral election has raised eyebrows in a city that's has more than its share of political intrigue. One of the candidates, City Council member James Singleton, criticized the original RFQ/RFP.

Singleton says he doesn't oppose privatization *per se*, but that he's afraid that the bidding and selection processes don't necessarily promote the public good. Singleton suggested, in fact, that some city officials may be pursuing a process that would favor only one company.⁸

Mayor Marc Morial, who is seeking to change the City Charter to allow him to run for a third term, has been the key force behind the privatization initiative. As mayor, Morial automatically chairs the Sewage & Water Board, obviously giving him the position and the power to influence the privatization process.

The Issues: More than What the City Bargained For?

According to a source within the S&WB, the process is marred by numerous problems.

First, the accelerated schedule may well result in a foregone conclusion. It is not feasible, the source said, to address all the relevant issues in such a short period of time.

Second, the New Orleans Civil Service Commission may seek another injunction to block the S&WB from entering into a contract with a private company without its approval. Under current law, all city privatization proposals must go before the Commission. If the Commission goes to court, the legal proceedings may stall the process.⁹

The commission tried to get an injunction in the spring, but the request was rejected because the RFQ/RFP had not yet been issued. However, when Mayor Morial hired a private company to run the city's Morris F.X. Jeff Municipal Auditorium and the Manila Jackson Theatre of the Performing Arts last year, the Commission successfully sued – claiming that the city could not privatize jobs previously performed by city employees without its

authorization.¹⁰

New rules, implemented in the last two years, have made the task of obtaining the Commission's blessing much more difficult. For example, proof must be shown that the job could not be performed at a lower cost in-house. The Commission has approved privatization efforts in the past, but the water and sewer proposal is by far the largest and the most plagued by unanswered questions.

For example, what about terminal leave, such as severance pay and sick leave? According to the S&WB source, terminal leave is a "property right," just like pension leave, and employees can expect severance pay if their employment is terminated. If the privatization goes through, about 800 employees could be transferred to the private sector and thus cut from S&WB's payroll. The first RFQ/RFP did not make specific provisions for this transfer.

The question of pension plans also remains unanswered. If these questions and other personnel issues are not fully addressed in the final RFQ/RFP or in the contract, lawsuits – messy ones – would likely ensue.

It also appears that the contract would not prohibit the new company to export city water to other areas. This would set up a scenario in which the company – not the city and its residents – could earn extra profits on the sale of a public resource.

The Past: Lessons to Learn?

If implemented, the water and sewer privatization would be the largest public works privatization in the United States, worth about \$1 billion over a 20-year period.¹¹ However, it will not be the first public works privatization for the city.

New Orleans has contracted out its sewage treatment operations and maintenance since 1992. The original contractor, Professional Services Group (PSG), was bought out by U.S. Filter, which was in turn acquired by the French conglomerate Vivendi.

The initial contract was for five years with subsequent one-year extensions that had to be considered by the city. The company lobbied and even bribed one of the S&WB members to

extend the contract for another five years. When the effort failed, the company's performance went into decline.¹²

Then, on July 26, 2001 – the day after the S&WB voted to proceed with the privatization – an electrical fire shut down the East Bank Sewage Treatment Plant, which serves 440,000 people, for two and a half hours.¹³ Raw sewage backed up, covered surrounding land and made its way into some of the plant's offices. Plant operators diverted untreated sewage into the Mississippi River for two hours until the plant was returned to operation.

A spokesperson for S&WB, John Puglia, claimed it was not possible to even estimate the amount of sewage diverted into the river.¹⁴ This begs the question: Because sewage systems generally have flow meters, and because flow estimates are generally not difficult to calculate, why didn't the S&WB know how much sewage went into the Mississippi? Interestingly, Puglia works for a private firm – the Public Relations Group – not for the public S&WB.¹⁵

According to City Council member Jim Singleton, S&WB officials told him that U.S. Filter for several weeks was aware of equipment problems that could lead to such dangers, but failed to address them.¹⁶

The fire came only a few months after two broken incinerators led U.S. Filter to truck out excess, untreated sewage sludge. The residents of the neighboring Arabi Park and Carolyn Park subdivisions of St. Bernard Parish were exposed to the fetid odor for more than two months.¹⁷

Private wastewater operations brought not only environmental violations to the city, but also corruption and bribery.

In May 2001, former S&WB member Katherine Maraldo and three former PSG executives were charged with bribery. According to the indictment, PSG paid more than \$70,000 to Maraldo, who in turn recommended that the city renew its sewage contract with PSG for five years. The company allegedly falsified some of its records to cover up the bribes. PSG's former president, vice president and a consultant (a former PSG vice president) were also charged with conspiracy, interstate travel in aid of bribery, and mail fraud – charges that could yield up to 50 years in prison. Aqua Alliance, PSG's

parent company at the time, has agreed to plead guilty to bribery and pay a \$3 million fine.¹⁸

U.S. Filter, which has since bought out the water and sewage operations from PSG, is among several companies that have expressed interest in taking over the city's water and sewer systems. Mayor Morial's firm commitment to privatization – so near the end of his term – has led many local pundits to wonder whether there is more to the proposal than meets the eye.

The City's Reputation: Is it The Big Sleazy?

New Orleans city officials have a history of rewarding government contracts to return favors to their friends and campaign contributors.

According to the *Times-Picayune*, for example, minority- and women-owned firms (called "disadvantaged business enterprises," or DBEs) that made campaign contributions to local politicians were three times as likely to receive public works contracts.¹⁹


In 1995, shortly after becoming mayor, Morial relaxed the certification rules for DBEs, dropping the revenue limits on personal worth, net income and corporate revenues. As a result, larger – and, at least, theoretically, less disadvantaged – companies that did not qualify under the old rules gained preferential access to city contracts.

In a city that's practically synonymous with public corruption, the poorly handled water and sewer privatization proposal has sown doubt as to the true intentions of the city officials involved. In its April 2000 report, the Bureau of Governmental Research flat-out questioned the validity of assumptions that privatization would result in cost savings, pointing out that the city's financial advisor did not provide any actual data on which these assumptions were based.²⁰

Simply put, no solid evidence has come to light that suggests privatizing the city's water and sewer systems would be in the public's best interest. Until such evidence is brought forth, only a person naive in the ways of New Orleans politics would expect this proposal to pass the sniff test.

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WHAT THE CORPORATIONS DON'T TELL ABOUT WATER PRIVATIZATION. UNITED STATES CASE STUDIES.

22 August 2001.

Introduction.

Rising water rates, increased shortages, legal and legislative battles over water rights, depletion of fresh water sources and crumbling infrastructure have recently drawn attention to a resource that the United States has long taken for granted – water. We expect a flow of clean water every time we open the tap. We also expect this life-giving resource to be available to everyone at affordable prices because our health and our survival literally depend on it.

Over the last century, the majority of the U.S. population has received its water from public utilities. However, today these public providers are in a very difficult position. The water and wastewater infrastructure is in a desperate need for repairs and upgrades. In many cases, pipes still in use are several decades old. The Water Infrastructure Network (WIN) estimates that \$23 billion a year would have to be spent on infrastructure in the following 20 years, some \$11 billion more than the amount currently being spent.¹ It is hard for the municipalities to raise this amount of money without an increased federal funding. However, financial assistance with water infrastructure upgrades is not on the federal government's list of priorities.

The corporations take advantage of the cash-starved municipalities, who are reluctant to implement rate increases necessary to perform infrastructure improvements because the measure is politically unpopular. These companies offer to run or buy the municipal systems promising cost savings, compliance with environmental standards, and elimination of headaches associated with operating the facilities. Even though the case history supplies overwhelming evidence that privatization is not a panacea for the ailing water and wastewater systems, the municipalities begin to consider privatization in increasing numbers.

The proponents of privatization, which also goes by the name of public/private partnerships, outsourcing, procurement, and operation and maintenance contracts, like to highlight success of the private involvement in water and wastewater service provision. For instance, the U.S. Conference of Mayors touts water privatization, as an innovative solution to the country's water challenges. In a study of twenty locales, which chose to privatize their water/wastewater utilities, the U.S. Conference of Mayors Urban Water Council portrays private companies as the municipalities' messiah.² However, the study carefully avoids cities and localities that have had negative experiences with privatization. This comes at no surprise given the membership on the council's Water Development Advisory Board of such private water heavyweights as American Water Works Company, U.S. Filter, United Water, OMI, U.S. Water, and Severn Trent.³

Fortunately, cases countering the corporate propaganda abound. This fact sheet highlights several of them, making a strong case that the private operation of water and wastewater systems may not be the optimal answer to the infrastructure needs.

Pekin, Illinois.

In 1982, Illinois-American, a subsidiary of American Water Works Company, acquired Pekin's water system from a local private owner. In the following 18 years (1982-2000) the rates increased by 204%. At the same time the company failed to keep infrastructure up to date. According to Pekin's city manager Dick Hierstein, pressure problems have plagued several parts of the city, especially those experiencing commercial growth. However, the company hesitated to construct needed water tower it earlier promised or to upgrade the undersized mains. This contributed to the problems.⁴ The company's irresponsible operations and unwillingness to cooperate with the city in development efforts negatively impacted the city's economic growth and added to its expenses.⁵

In 1999, responding to the soaring rates and questionable quality of service, the city chose to consider acquisition of the local water company from Illinois-American through its eminent domain powers. A report by the Water Study Committee, commissioned to evaluate feasibility of the acquisition, made a strong case for purchasing the water system. The Committee found that the company's service record has not been perfect. For example, there was an instance of flooding for over 24 hours. In another case, the water service to two of the city schools was interrupted for a week. In an ultimate display of incompetence, the company workers taped a message to the school doors just before the students arrived for classes instead of notifying the school officials in advance.⁶

Citizens For Locally Owned Water (FLOW), a citizen group that advocated public ownership of the water system, projected that with the present rate of infrastructure upgrades, it would take Illinois-American over 268 years to replace all city mains. This rate of progress was unacceptable, especially when some of the city mains were over 75 years old. The group also pointed out that in 1990 a local business was destroyed in fire when the firemen were confronted with inoperative fire hydrants and low water pressure.⁷

To remedy the problems associated with the Illinois-American operations and ownership the city launched a buyback effort. The company responded with an elaborate public relations campaign that sought to convince the residents that the city does not possess sufficient expertise to run the water system properly. The public relations firms hired by Illinois-American conducted surveying and placed television, newspaper, and radio ads to get the issue on the ballot and then obtain a favorable outcome. Even the company's president was invited to come and try to convince residents to support private ownership of the water system. The city estimates that the company's spending on the public relations offensive approached \$1 million. The city had only \$30,000 to spend on public outreach.⁸

The company's propaganda efforts paid off when it won, although by a narrow margin, a referendum against the city. The close outcome and the battle preceding the referendum made the company a little more attentive to the municipality's requests. According to Hierstein, only now is the company making efforts to solve the problems. The buyback question is presently on hold, but Hierstein believes that it would inevitably be raised again because of the stark differences in priorities of a "profit-driven national company vs. a service-oriented and cost-conscious local government." Having managed cities with both private and public providers, Hierstein is convinced that the citizens and the government are served "far better" with a publicly-owned system.⁹

Atlanta, Georgia.

In 1998, the city of Atlanta awarded United Water, a subsidiary of the French water giant Suez Lyonnaise des Eaux, a contract to operate the city's water system. The company promised cost savings in exchange for a \$21.4 million annual fee. Three years into the contract, the question of whether residents are benefiting from it continues to be raised.

In 2000, some of the Atlanta's residents began to find debris in their water. In addition to the strange additive, the water color assumed brown tones, which usually signals high levels of iron oxide in water. However, the company did not initially acknowledge there was a problem.¹⁰ Four months later, the residents were still experiencing the same problems.¹¹

Numerous cases of dry or inoperative fire hydrants have been reported. However, the company does not address them promptly if at all even though inoperative fire hydrants could be a matter of life and death for those caught in the fire. Moreover, in response to the residents' inquiries the company has said that testing the fire hydrants after they were repaired was a city's obligation – a claim city has rejected, maintaining that the company should leave the fire hydrants operable.¹²

There have been numerous complaints of delays and slow service. For instance, when in March 1999 the Breakwater homeowners association paid \$2,700 to have three meters installed, the United Water informed the association that the request would take 10 weeks. Six months later the company installed the first meter. The contract gives the company one day to respond to leaks and 15 business days to install a meter.¹³ One reason for delays may be understaffing. Currently United Water has just 327 employees, down from 731 in 1997, a year before privatization.¹⁴

Huber Heights, Ohio.

In 1993, Florida-based Avatar elected to sell off its water holdings, including Ohio Suburban Water, a small private water company that provided water for 40,000 customers in the city of Huber Heights, OH and parts of the Mad River Township. American Water Works Company, the largest investor-owned water provider in the

United States, expressed its desire to buy the utility. The city voiced concerns about the New Jersey-based water giant controlling its water. It feared that the American Water Works would raise the water rates and extend water service to areas outside of the city limits without annexation, thus impairing the city's ability to grow.¹⁵ Water services are an important incentive that municipalities use to expand. As a rule, the outlying areas have to annex to the city before they could obtain access to the municipal water.

The city attempted to acquire the water system from Avatar but was outbid by the American Water Works. Ohio Public Utilities Commission approved the transfer of shares and at the same time denied the city a hearing to plead its case.¹⁶ The fears that the city harbored about the Ohio Suburban operation of water system materialized. In the summer of 1993 the company increased its rates by 30%.¹⁷ At the same time the company moved to contract with Industrial Water Inc. for delivery of up to 2 million gallons of Huber Heights water a day to Wiley Industrial park, located outside of the city limits.

In an effort to prevent further rate hikes and to reclaim control of the city's economic development, the city initiated proceedings to take over the system through its eminent domain powers. The company unleashed its public relations force to prevent the takeover and collected enough signatures to put the issue on the ballot. However, its effort collapsed after the city residents voted overwhelmingly in support of the city's efforts to acquire the system.¹⁸

While the city was still fighting the legal battle to reclaim control of the water system under the residents' clear mandate, the company persisted with its efforts to export Huber Heights water outside of the city limits. The city protested arguing that the water pipes should be extended only in the event of annexation. However, in the pursuit of additional profits recognized through the service extension, the company blatantly disregarded the city's pleas and began piping Huber Heights water to the industrial park. The park used only 10,000 gallons a day and the county officials wanted to make the excess water available to the remainder of Bethel Township.¹⁹

In March 1995 the city avoided a lengthy legal battle by negotiating an out-of-court settlement with the company. However, even after the buyback, the preceding activities of the American Water Works subsidiary continued to cause problems. Industrial Water Inc. had subsequently sold its contract to the neighboring Miami County, which claimed the rights for the contracted two million gallons. The settlement agreement provided that the city would continue piping water to the industrial park "until Ohio Suburban's obligations, if any, are resolved."²⁰

Because of the American Water Works misdoings the city is now under a legal obligation to act against its own interest. Huber Heights feels that the Bethel Township is unfairly reaping benefits of the water infrastructure paid for with the money of the city's ratepayers and taxpayers, while avoiding paying city taxes. It continues to argue that the township must be annexed to Huber Heights to have access to its water. The conflict remains unresolved.

San Francisco, California.

The city of San Francisco is among a large number of the U.S. cities, whose water systems require repairs and upgrades. The century-old Hetch Hetchy water system that provides water for 2.3 million of people in San Francisco, San Mateo, Santa Clara, and Alameda counties needs as much as \$8 billion for the facilities' seismic upgrades and repair.²¹

The city decided to contract a private firm's consulting services as it embarked on this ambitious project. In 2000, after much controversy, the city awarded a \$45 million consulting contract to an alliance, led by Bechtel Corporation, the world's largest engineering firm that has aggressively entered the private water markets. The Public Utilities Commission claimed that contracting Bechtel to oversee modernization of the San Francisco water system would produce as much as \$45 million in cost savings over the next four years and allow access to the necessary expertise.

Many spoke out against the contract during the exploratory and negotiation stages. Harvey Rose, San Francisco budget analyst disagreed with the claim of prospective savings, maintaining that no evidence of cost-savings had been provided.²² Supervisor Tom Ammiano both questioned the alliance ability to produce cost-savings for the city and suggested that the contract would eventually lead to further privatization of the Hetch Hetchy water system.²³ Nevertheless, the city's Board of Supervisors approved the deal.

Today, almost a year into the contract many have voiced concern about its value. According to David Novogrodsky, the executive director of the Professional and Technical Engineers Local 21, Bechtel has so far done very little, other than charging "outrageous" fees. Bechtel's workers are not working with the city engineers. There are a few "higher-ups," who often perform in the capacity of management, and many lower-level workers. The director says that the majority of the staff is not qualified and that it is not unusual to see Bechtel employees sitting down studying for their engineering exam, instead of performing real work.²⁴

According to the *San Francisco Bay Guardian*, many city workers felt the company was not aiding them in their work but only slowed down the progress because it had to approve the in-house jobs. They also felt that instead of acquiring valuable skills from Bechtel's engineers, as was originally intended, they had to explain to them even basic operations. Finally, the staff felt that the city was being billed for work already performed by the city employees.²⁵

Charleston, West Virginia.

In the Year 2000 Water and Wastewater Rate Survey of 194 U.S. cities and counties, performed by a leading consulting firm in the water business Raftelis Financial Consulting, the city of Charleston, West Virginia stood out with its exceptionally high rates. The monthly water charges for an average customer using 7,480 gallons of water

were \$46.21, some \$31.84 or 221% higher than the \$14.37 average for a city of a comparable size. The amount was augmented by a \$12.69 monthly charge – once again, the highest in the category. Finally, the affordability index showed that the cost of 7,480 gallons of water amounted to 1.65% of the median income in Charleston. The city was the only one in its category to have its index surpass the 1% mark. The cost of water as a percentage of median income was more than 3.5 times higher than the median value for cities of its category.²⁶

Charleston residents receive their water from West Virginia-American, a subsidiary of American Water Works Company. According to the West Virginia Public Service Commission, the average bill increased by some 66.5% for the company's customers over the last decade.²⁷ The West Virginia-American has increased its rates 15 times in just 10 years.²⁸ Roy Ferrell, the company's Director of Rates and Revenues, explains the skyrocketing rates by West Virginia's mountainous landscape and by the new construction. According to Ferrell, the company has consolidated its plants, reducing the number from 26 to nine. Eight of the remaining plants were either refurbished or replaced. To provide remote locales with access to water, extensions had to be built. The company claims to have spent some \$240 million on the construction.²⁹

Billy Jack Gregg, director of the Consumer Advocate Division in the West Virginia's Public Service Commission, sees the picture a little differently. He agrees that the infrastructure construction may be very costly, yet believes that West Virginia-American is forcing the existing customers to finance its own expansion. The company has extended its water service to areas where the operation is not cost-effective. The investment required for such areas can be twice as high. However, the single tariff pricing shifts the cost to the present customers, who find such procedure rather unfair. The new areas not only receive access to the infrastructure built with their money, but also receive the water service at a price lower than the real costs thanks to the higher rates paid by the existing urban customers. In early 2001 the company filed for yet another rate increase equivalent to approximately \$1 million annual increase in revenues. Gregg says that West Virginia-American is seeking to recover three-quarter million dollars it spent trying to acquire the water system in Parkersburg, WV.³⁰

Roy Ferrell pledged that the company would not request another rate hike for the next 20 years after the current request is approved because all major construction is finished.³¹ However, this promise is hard to believe provided that American Water Works Company depends on rate increases for higher profits and dividends.

It is important to understand that in extending its water lines to more remote regions, West Virginia-American is not driven by a sense of civic responsibility, but by the simple desire of higher profits. The single tariff pricing allows it to expand to the non-profitable areas knowing it can easily increase its statewide rates to maintain existing profit margins.

Charleston wastewater system is owned and operated by the city. The Raftelis survey shows that the median sewer charges are 20% higher than the water rates for the cities of

comparable size. However, in Charleston the situation is reversed. The sewer charges don't amount to even a half of the water rates level.³² The solution to this paradox lies in the fact that the sewer service is provided by the city, and not by a private company.

New Orleans, Louisiana.

The city of New Orleans has contracted out its sewage treatment operations and maintenance since 1992. The original contractor, Professional Services Group (PSG), was bought out by U.S. Filter, which was in turn acquired by the French conglomerate Vivendi.

On July 26, 2001 an electric fire interrupted the operation of the East Bank Sewage Treatment Plant that serves about 440,000 people for two and a half hours.³³ The raw sewage backed up covering the surrounding land and making its way through some of the plant's offices. The plant's operators diverted untreated raw sewage into the Mississippi River for two hours before the plant was returned to operation. John Puglia, in charge of public relations for the city's Sewage and Water Board, claimed that it was not possible to estimate the amount of sewage diverted into the river.³⁴ The statement invites questions because the gates that water passes usually have meter. Interestingly, John Puglia is an employee of a private firm, the Public Relations Group, which carries out a bulk of the S&WB public relations work.³⁵

According to the City Councilman Jim Singleton, S&WB officials have informed him that the company was aware of the problems with equipment for several weeks and the dangers they would have created, but failed to address them.³⁶

The fire came only a few months after the sewage plant's two broken incinerators resulted in transportation of the excess sewage sludge that has not been processed out of the sewage treatment facility by trucks. The residents of the neighboring Arabi Park and Carolyn Park subdivisions of St. Bernard parish were exposed to the sordid odor of sewage for over two months.³⁷

Ironically, the fire accident took place just a day after the Sewage & Water Board voted to invite bids to privatize the municipal water and wastewater treatment systems despite much public and labor discontent. U.S. Filter is among several companies who have expressed interest in running the city's water.

Peoria, Illinois.

Over the last decade the city has attempted to buy back Peoria's waterworks, currently owned by Illinois-American Water Co., a subsidiary of American Water Works Company. The city believes that public ownership would stabilize rates and reduce the operating costs.³⁸ According to Terry Kohlbus, who is coordinating the takeover, in 1998 Peoria rates were among the highest in the Raftelis rate survey. Not surprisingly, the

company has stopped providing information to Raftelis and in the 2000 issue of the rate survey Peoria was not listed.³⁹

The city also argues that the buyback of the company would place the much-needed control over economic development back into the city's hands. The company has not been very cooperative in the city's development efforts. Moreover, a financial analysis prepared by Raftelis Financial Consulting showed that the city would have a \$6 million a year in excess revenue if it owned the company itself.⁴⁰

Washington Court House, Ohio.

In 1991, the city of Washington Court House, OH decided to take over their water system, then owned and operated by the Ohio Water Service Co. The city believed that it would be able to operate the utility more inexpensively and more efficiently. As usually the case, the company mounted legal and public relations campaign. It collected enough signatures to put the issue on the ballot. However, the city residents voted for the municipal control of water. Following a two-year legal battle with the company, Washington C.H. purchased the water system for \$10 million.⁴¹

The city operations proved a true success story. One of the bond conditions required Washington C.H. to collect approximately 20 percent more in revenues that it spent to operate the system. Yet just two years following the takeover the city was collecting 60 percent more and enjoying \$500,000 annual surpluses. Not only did the city live up to its promises not to raise rates in the three years following the takeover, but it was actually able to issue rebates to the local rate payers.⁴²

Duval, Nassau, and St. Johns Counties, Florida.

On August 1, 2001 United Water Resources (UWR) accepted a \$219-million offer by the Jacksonville Electric Authority to buy out the company's Florida holdings. JEA is a municipal authority serving residents of Jacksonville and the surrounding areas. JEA's operations are expected to lower average water and sewer bills of the former UWR customers by 25%.⁴³

The rate cut will be welcomed by many of the counties' residents. In 1997, when United Water was providing the water and sewer services for the three counties, the residents saw their rates increase by an average of \$9.44 per month. Many residents expressed indignation with the rate hike. Richard H. Harlan, Jr., who was among the affected ratepayers, called the company "the biggest bunch of highway robbers."⁴⁴ In 1998, the company requested yet another rate increase. The request was granted by Florida's Public Service Commission in 1999. The water rates increased by 12.53% and the sewage rates rose 5.43%. When reviewing the rate hike request, the PSC found that United Water overestimated its expenses by \$1.05 million.⁴⁵

Jersey City, New Jersey.

In 1996, the city contracted United Water Resources to operate and maintain its water system. Five years later the city no longer expresses as much enthusiasm about the private operations. According to Kathleen Deely of the Municipal Utility Authority, the city has learned that the private operation is “no worse, no better.” The company did improve the bill collection. However, the quality of water service did not change⁴⁶

The rates, which are still being set by the MUA, are influenced by a variety of factors, however, the operation fees paid to United Water are a critical component. According to a senior MUA official, a lack of financial transparency prevents the city from evaluating whether the price commanded by the company is reasonable. The company is not required to open its books for a municipal review. Instead it just sends the bill. The contract does not prevent the company from overcharging because no review process is built in.⁴⁷

According to the same official, the company’s customer service needs improvement. The customer service representatives often direct the user complaints to the MUA, even though in many cases the company is responsible for the events triggering these complaints and some of the problems should have been prevented. United Water contracts out meter reading to another company. A combination of broken meters and underpaid readers often results in erroneous billing.⁴⁸

The official does not believe that Jersey City public/private partnership in water services is a bona fide partnership. The company’s goal is to make a profit, regardless of consequences. It has little concern for public good and will not do anything unless it is compensated for it.⁴⁹

Hingham and Hull, Massachusetts.

Massachusetts-American, an American Water Works subsidiary owns the water system in the Hingham and Hull, Massachusetts. In 1996 it doubled the water rates for its customers in those service areas⁵⁰ despite many objections. The company justified the hike by the having to invest into a new water treatment facility. Meanwhile, the American Water Works profits grew by some 10.4 percent in the same year.⁵¹ In 2001 yet another rate increase requested by the company was approved. The company relied on claims of higher infrastructure spending and increased operation costs to obtain the new increase.

When approached with a request for the schedules of rates prior to the 1996 increase and those currently in effect, Connie Chapman of Massachusetts-American provided the information on rates immediately after the increase, not the ones preceding it. When asked again, she claimed that the 1995 rate schedules would be difficult to locate, even though locating the rate information just one year junior apparently did not pose a problem.⁵²

According to James Lampke, Hull's town counsel, the two communities have some of the highest water prices in the state.⁵³ Lampke said that the city understands that the rates have been influenced by the construction of the new plant. However, he believes that the company chose a process that augmented the costs by millions of dollars – spending, which could have been avoided. For example, the company spent excessively to obtain an approval for a site, whose approval would be very unlikely. According to Lampke, Massachusetts Department of Telecommunication and Energy that regulates private water providers has agreed with the city that some money could have been saved.⁵⁴

¹ Water Infrastructure Network. "Water Infrastructure Now: Recommendations for clean and safe water in the 21st century." Feb 2001.

² "Case studies of selected cities." The United States Conference of Mayors. Urban Water Council." Feb 2000, http://www.usmayors.org/USCM/urbanwater/case_studies/.

³ Ibid. Appendix B.

⁴ E-mail from the City Manager Dick Hierstein, 23 Jul 2001.

⁵ "City ownership of Pekin's water system makes good sense. Here's why." *Citizens For Locally Owned Water*, 2000.

⁶ Water Study Committee Report, City of Pekin, IL, 15 July 1999.

⁷ "City ownership of Pekin's water system makes good sense. Here's why." *Citizens For Locally Owned Water*, 2000.

⁸ E-mail from the City Manager Dick Hierstein, 23 Jul 2001.

⁹ Ibid., 24 Jul 2001.

¹⁰ Soto, Lucy. "Faucets spewing fears, confusion. Watered-down solutions: Virginia-Highland residents get lots of answers about problems with their drinking water. But which should they believe." *The Atlanta Constitution*, 1 May 2000.

¹¹ "Work will start soon on intown water line." *The Atlanta Journal*, 4 Sep 2000.

¹² Campbell, Colin. "Too many hydrants don't go with the flow." *The Atlanta Journal*, 30 Mar 2000.

¹³ Hardie, Ann. "City, firm up to their necks in complaints. Spotlight on a flood of excuses: Getting a problem with your water service solved has proven as difficult as figuring out who is to blame." *The Atlanta Journal*, 6 Sep 2000.

¹⁴ Personal communication with Cherry Yeboah, United Water Human Resources Department, phone, 20 Aug 2001.

¹⁵ Denger, Laurie. "Wrestling control of water. Heights has battle plan." *Dayton Daily News*, 15 Dec 1993.

¹⁶ Denger, Laurie. "Water issue nears boil in Heights. City develops strategy for Jan. 11 election." *Dayton Daily News*, 3 Nov 1993.

¹⁷ Denger, Laurie. "Wrestling control of water. Heights has battle plan." *Dayton Daily News*, 15 Dec 1993.

¹⁸ Denger, Laurie. "Win begins water war in Heights." *Dayton Daily News*, 12 Jan 1994.

¹⁹ Bebbington, Jim. "Lines pipe water to businesses. Miami industrial park seals deal with supplier." *Dayton Daily News*, 16 Nov 1994.

²⁰ Babcock, Jim. "Lawsuit – water fight begins in Miami County." *Dayton Daily News*, 3 Nov 1997.

²¹ Epstein, Edward. "Price estimate doubles for fixing Hetch Hetchy. S.F. mayor seeks ways to cover \$8 billion in repairs." *The San Francisco Chronicle*, 15 November 2000.

²² Wilson, Yumi. "Analyst for S.F. criticizes water contract award. PUC can't prove that money's saved." *The San Francisco Chronicle*, 15 Jul 2000.

²³ Epstein, Edward. "S.F. Board Oks Hetch Hetchy pact. Bechtel-led consortium to renovate water system." *The San Francisco Chronicle*. 29 Aug 2000.

²⁴ David Novogrodsky, Professional and Technical Engineers Local 21, Phone conversation, 23 Jul 2001.

²⁵ Blackwell, Savannah. "Blocking Bechtel." *The San Francisco Bay Guardian*, 20 Jun 2001.

²⁶ Raftelis Financial Consulting. "Year 2000 Water and Wastewater Rate Survey." Raftelis Financial Consulting: Charlotte, 2000.

²⁷ Consumer Advocate Division of Public Service Commission. Monthly residential utility rates 1991-2001, Charleston, chart.

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- ²⁸ West Virginia-American Water Company. Historical Rate Increases, chart.
- ²⁹ Personal communication with Roy Ferrel, Director of Rates and Revenues, West Virginia-American Water, phone, 9 Aug 2001.
- ³⁰ Personal communication with Billy Jack Gregg, Director of Consumer Advocate Division, West Virginia Public Service Commission, phone, 08 Aug 2001.
- ³¹ Personal communication with Roy Ferrel, West Virginia-American Water, phone, 9 Aug 2001.
- ³² Raftelis Financial Consulting. "Year 2000 Water and Wastewater Rate Survey." Raftelis Financial Consulting: Charlotte, 2000.
- ³³ "Fire temporarily closes sewage plant." *The Times-Picayune* (New Orleans), 27 Jul 2001.
- ³⁴ Finch, Susan. "Untreated waste diverted to river." *The Times-Picayune* (New Orleans), 27 Jul 2001.
- ³⁵ Office of Intergovernmental Relations, Sewer & Water Board, phone, 13 Aug 2001.
- ³⁶ Finch, Susan. "Untreated waste diverted to river." *The Times-Picayune* (New Orleans), 27 Jul 2001.
- ³⁷ "Sewer plant blamed for Arabi odors. Broken incinerators to be repaired soon." *The Times-Picayune*, 30 May 2001.
- ³⁸ Ramsey, Mike. "Pekin vote won't deter Bud Grieves." *Peoria Star Journal*, 9 Nov 2000.
- ³⁹ Personal communication with Terry Kohlbus, phone, 2 Aug 2001.
- ⁴⁰ Ibid.
- ⁴¹ Baird, Don. "City-owned water system pays off in first rebates." *The Columbus Dispatch*, 10 Sep 1995.
- ⁴² Ibid.
- ⁴³ Jacksonville Electric Authority. "JEA and United Water reach innovative agreement." JEA News. Available online: <http://www.jea.com/about/news/press/unitedwateragreement.asp>, 20 Aug 2001.
- ⁴⁴ Magee, Keri. "Utility's rate hike enrages residents." *The Florida Times-Union*, 10 May 1997.
- ⁴⁵ Chapin, Veronica. "Water bill mistakes resolved. Agreement reached with United Water." *The Florida Times-Union*, 12 May 1999.
- ⁴⁶ Personal communication with Kathleen Deely, Municipal Utility Authority, Jersey City, phone, 26 Jul 2001.
- ⁴⁷ Personal communication with a senior official of Municipal Utility Authority, Jersey City, NJ, phone, 14 Aug 2001.
- ⁴⁸ Ibid.
- ⁴⁹ Ibid.
- ⁵⁰ Personal communication with Connie Chapman, Customer Service Supervisor, Massachusetts-American Water, phone, 6 Aug 2001.
- ⁵¹ Based on the company's Securities and Exchange Commission filings.
- ⁵² Personal communication with Connie Chapman, Customer Service Supervisor, Massachusetts-American Water, phone, 6 Aug 2001.
- ⁵³ Personal communication with James Lampke, Hull, town counsel, 10 Aug 2001.
- ⁵⁴ Ibid., 13 Aug 2001.

A PRIMER ON WATER ISSUES IN CALIFORNIA

1. Introduction.

California is among the fastest growing states in the nation. By 2020 its population is expected to reach 45.8 million people exceeding the 2000 levels by some 11.3 million.¹ The per capita water consumption is increasing at an even higher rate. Whereas in 1992 an average Californian used 200 gallons a day, today the figure is 229 gallons.² The state continues to experience rapid economic growth, especially in the high tech industry. The growth increases the demand for water. The stress on the water resources is augmented even further by the state's popularity with the water-intensive computer and biotechnology industries. As a direct result of these developments, the state will require more water in the coming years. According to Maurice Ross, the chief hydrologist for the California Department of Water Services, the department anticipates that the "urban demand for water will rise from the 1995 figure of 8.8 million acre-feet to 12 million acre-feet by 2020."³

California's water usage averages 80 million acre-feet annually, however, in the dry years the figure drops to about 65 million acre-feet. In 1998, California Department of Water Resources forecasted that the state would experience increased water shortages by the year 2020 – 2.4 million acre-feet in an average year and 6.2 million acre-feet in a drought year.⁴

Many Californians are intimately acquainted with the consequences of shortages and droughts. In 1976-77 the state experienced a severe drought that forced radical changes in the lifestyles of many, ranging from inability to water lawns, wash cars, and fill up swimming pools to having to put a brick in the toilet to save water. In 1987 the state entered another dry spell that lasted till 1992. Rationing was imposed in many municipalities reaching 50% of the average usage in some communities. Santa Barbara was forced to institute a 14-month ban on lawn watering.⁵

The 1987-1992 drought served yet another reminder of California's dependence on water and the state's limited supplies. To prepare for other possible supply shortages new facilities have been constructed and new water-sharing agreements have been negotiated. For instance, Metropolitan Water District's Diamond Valley Lake Reservoir and Contra Costa Water District's Los Vagueros Reservoir were constructed to provide emergency water supplies.

California water supply fluctuates between the wet and dry years. Seventy-five percent of California's precipitation falls between November and March. Increased winter

¹ California Department of Finance. "Interim county population projections." 1 Jul 2000.

² Martin, Glen. "Drought could be our next crisis. Population growth threatens water supply." *The San Francisco Chronicle*, 22 July 2001.

³ Ibid.

⁴ California Department of Water Resources. "The California Water Plan Update. Bulletin 160-98." Online: <http://rubicon.water.ca.gov/pdfs/b160cont.html#es>, 1998.

⁵ Martin, Glen. "Drought could be our next crisis. Population growth threatens water supply." *The San Francisco Chronicle*, 22 July 2001.

precipitation results in wet years. Conversely, shortages in precipitation lead to droughts. Hence, a number of initiatives to deal with California's water problems involve storage of water in both aboveground and underground reservoirs.

2. Water wars.

The San Francisco Bay/Sacramento-San Joaquin Delta Estuary (the Bay-Delta) is the core of California's water supply, providing water for two-thirds of the state residents and for over 7 million acres of farmland. Both the Central Valley Project and the State Water Projects, California's two largest water distribution systems draw water from the Bay-Delta.⁶ Throughout much of the 20th century the delta has been abused largely to satisfy the demands of consumers in other parts of the state. The dam creation, diversion of the system's water and pollution had calamitous environmental consequences: by the early 1980s fish species were becoming extinct, the salinity intrusions were occurring more frequently, and contamination levels were increasing, largely due to the runoff from the industrial farms.

When the environmental groups began a campaign to save the delta, they were met by the fierce opposition from the state officials and from the powerful agricultural and urban lobbies of Central and Southern California. The residents of Northern California have long harbored resentment towards the southern regions for diversion of their water; however, in 1980s as destructive environmental effects became commonplace, the sentiment intensified. Many have felt that the wildlife habitats and the water quality were being compromised in the interest of the wasteful agricultural sector, urban sprawl, and the economic growth in the arid Southern California. In fact, the Bay-Delta water supports 16 million southern Californians and their \$450 economy.⁷ It is also crucial to the state's agriculture, which grows 45% of America's produce while consuming 80% of California's water.⁸

The Central Valley Project and the State Water Project are the chief instruments of this grandeur water transfer. The Central Valley Project, or CVP, was authorized by Franklin Roosevelt in 1930s with the purpose of transferring the northern water to the Central Valley. The project is administered by the U.S. Bureau of Reclamation. A structure of canals, dams and reservoirs spreads over an area over 400 miles long and 100 miles wide, providing water to irrigate large portions of the Central Valley and its farms while destroying millions of acres of wetlands, threatening half of all the Pacific Flyway birds, and damaging wildlife refuges.⁹ In 1992, a bill introduced by George Miller, a California Representative from the Bay-Delta area, was signed by President Bush. The Central Valley Project Improvement Act was a radical departure from the institutionalized abuse of the delta and a big victory for its environmental community. The legislation ordered

⁶ CALFED Bay-Delta Program. "Program Summary – August 2000."

⁷ CALFED Bay-Delta Program. "Southern California's stake." 31 Jul 2001, http://calfed.ca.gov/pub_info_materials/southern_california.html.

⁸ CALFED Bay-Delta Program. "Central California's stake." 31 Jul 2001, http://calfed.ca.gov/pub_info_materials/central.html.

⁹ "The Largest wetlands reclamation in history – the Central Valley Project." *Great Outdoor Recreation Pages*, 31 Jul 2001, http://www.gorp.com/gorp/resource/us_nwr/ca_cvp.htm

restoration of 800,000 acre-feet of annual fresh-water flow, established a regulated water market, in which farmers could sell their water to urban users, thus decreasing the demand, directed Fish and Wildlife Service to implement a program to double the populations of wild salmon, and created economic incentives to conserve CVP water.¹⁰

The State Water Project is another water storage and delivery system, whose construction began in the early 1960s. The project is managed by the California Department of Water Resources. It consists of canals, aqueducts, dams and pumps, running 662 miles from Plumas to Riverside County. It supplies water for 20 million customers in San Jose, Los Angeles, and other cities, and to 660,000 acres of farmland. Seventy percent of its water supply is allocated to the urban users and the remainder is used by the agricultural sector.¹¹

The two projects have been in the heart of the water wars between the North and the South. The disputes also involved legal battles over how much control the Bay-Delta regions exercised over their water resources.

3. CALFED.

In 1994 the negotiations over water sharing resulted in the Bay-Delta Accord, negotiated by the agricultural, urban, and environmental communities. The accord called for creation of a joint federal/state taskforce to address the California's water issues. The U.S. Congress authorized funds in 1995 and the taskforce began its work. Although the taskforce is not an agency, it works with both the state and the federal agencies to find solutions to the allocation, water quality, water supply reliability and environmental problems in California.

While CALFED did began the most comprehensive ecosystem restoration project in the United States, many environmentalists feel that its activities are skewed in favor of consumption instead of conservation. Recent proposals to expand the water transfer infrastructure have been criticized by the environmental groups. The pending CALFED Reauthorization bills by Sen. Dianne Feinstein (D-Ca) and Rep. Ken Calvert (R-Ca) do little to curb the water usage or explore new sources of water, such as desalination or recycling. Instead they ask the Congress to authorize enlargement of Shasta Dam and Los Vaqueros Reservoir and construction of new storage facilities. Another representative from California, George Miller, has criticized this approach and has introduced a bill that better reflects the interests of the Bay-Delta region.

4. Other Sources of Water: Ground water and Colorado River.

Groundwater is seen by many as a way to alleviate the stress on the Bay-Delta.

¹⁰ The Bay Institute. "A Political History: The Bay Institute and the Bay Watershed." 31 Jul 2001, http://www.bay.org/policy/p_hist.html.

¹¹ California Department of Water Resources. "State Water Project." Online: http://www.dwr.water.ca.gov/dir-state_water_projectR2/State_Water_Project_R2.html, Jul 2001.

According to the California Department of Water Resources, thirty percent of California water supply comes from the groundwater sources, an amount that increases during the dry years. The largest quantities of groundwater extraction take place in Central and Salinas Valleys, as well as in the Southern California coastal plain. Extraction of groundwater exceeds the permitted levels by 1.5 million acre-feet annually. Majority of the overdraft occurs in San Joaquin Valley. In 1995 DWR estimated that developed groundwater supplies were 12.5 million acre-feet below the average hydrologic conditions.¹²

During the droughts, reliance on the groundwater sources increases, often leading to dire environmental consequences. For instance, during the five-year dry period between 1987 and 1992 numerous private wells and wells supplying small rural systems dried up. During the same time period extractions in San Joaquin Valley exceeded recharge by 11 million acre-feet. In 1991 San Antonio and Nacimiento Reservoirs used by Monterey County Water Resources Agency were at just 6% of their capacity.¹³

Colorado River is another important source of California water. The seven adjacent states and Mexico share the river's water. California had been allowed to draw surplus water because other states have not been using their full quotas. However, as the water demand from other states increases in the next 15 years, California will have to reduce the amount drawn from Colorado River. A recent agreement between the states using the river's water, negotiated in 2000, requires California to reduce the extracted amount from 5.5 million acre-feet per year to 4.4 million. Thus the state is forced to find other ways to satisfy its demand for water.¹⁴ The "4.4 Plan" will hit the Southern California especially hard because Colorado River is a key water source for the region.

The Imperial Irrigation District (IDD) and the Metropolitan Water District of Southern California (MWD or the Met) are the two biggest recipients of the Colorado River water, with the former receiving 70% and the latter receiving 12%. The MWD, serving the urban customers, charges high prices for its water, whereas IID continues to charge only a fraction of the MWD prices to its agricultural customers. The two agencies have an antagonistic relationship as a result.¹⁵

The Met, the largest wholesale water supplier in the country with its 17 million customers, is in a perpetual search for new sources of water. Among its initiatives is a controversial deal with Cadiz, Inc., an agricultural business that has land holdings in the Mojave Desert. Cadiz has proposed extraction of water from the underground aquifer located beneath its property to be sold directly to the MWD. The environmentalists argue

¹² California Department of Water Resources. "Preparing for California's Next Drought. Changes since 1987-92." Jul 2000. Online: <http://watersupplyconditions.water.ca.gov>.

¹³ Martin, Glen. "Drought could be our next crisis. Population growth threatens water supply." *The San Francisco Chronicle*, 22 July 2001.

¹⁴ Perry, Tony. "California and the West MWD Delays vote on buying water utilities; with the energy crisis on their minds, board members suggest caution in purchasing from Cadiz Land Co. and selling to consumers at market rates." *Los Angeles Times*, 9 Jan 2001.

¹⁵ Pacific Research Institute for Public Policy. "Ending California's Water Crisis. A market solution to the politics of water." Jul 1999.

that the extraction levels proposed by Cadiz exceed the recharge levels and will be damaging to the desert environment.

5. Water Markets.

In the last decade the idea of water markets has become increasingly popular. It is especially relevant to California because of the state's large agricultural sector. Water markets allow owners of water sources or water rights, which is more common, to sell them. In California, water is classified into three categories: real water, new water, and paper water. The real water is the least difficult to transfer because it does not injure rights of others; in the cases of new water (one that has not been previously available, such as groundwater) and paper water (made available by fallowing of the previously irrigated land) the transfers are more difficult because of their potential to inflict environmental and economic damage.¹⁶

In its *California Water Plan Update*, California Department of Water Resources includes into the definition of water marketing the following arrangements:

- A permanent sale of water right by the water right holder.
- A lease from the water right holder (who retains the water right), allowing the lessee to use the water under specified conditions over a specified period of time.
- A sale or lease of a contractual right to water supply. Under this arrangement, the ability of the holder to transfer a contractual water right is usually contingent upon receiving approval from the supplier. An example of this type of arrangement is a sale or lease by a water agency that receives its supply from the CVP, SWP, or other water wholesaler.¹⁷

Because of the subsidies, the farmers purchase their water at discounted prices, often representing only a fraction of the real costs or the prices paid by the urban areas. For instance, the MWD of Southern California sells treated water to its urban users for \$431 per acre-foot, a price affected by the storage, desalinization, and conservation needs.¹⁸ At the same time, the IID's current rates are only \$15 per acre-foot.¹⁹ Naturally, it makes sense for both the IID and the farmers supplied by the district to sell surplus water to the cities. The idea is often attractive to the urban water users, because the purchased water allows them to increase or stabilize supply without adversely affecting customers' water rates. For example, there is an agreement between the IID and the San Diego County Water Authority that provides for such water transfers for a period of 45 years. The price of the water for San Diego encompasses the cost of water conservation by the Imperial Valley farmers and incentives for them to conserve.²⁰ Because of its conservation incentives the water marketing is supported by some in the environmental community.

¹⁶ Dingler, Megan L., reviewer. "What is needed to create a more efficient market?" *Colby College*, 31 Jul 2001, <http://www.colby.edu/personal/t/thtieten/wat-ca2.html>.

¹⁷ *California Department of Water Resources*. "The California Water Plan Update. Bulletin 160-98." 1998.

¹⁸ Rates available from <http://www.mwd.dst.ca.us/mwdh2o/pages/operations/rates01.htm>.

¹⁹ phone inquiry, 760-339-9426, 31 Jul 2000.

²⁰ Imperial Irrigation District. "Water Transfer Agreement." Accessed 31 Jul 2001, <http://www.iid.com/water/transfer.html>.

Even though the basic premise of water marketing appears simple, the practice is much more complex. A farmer who chooses to sell a portion of real water and whose land property overlies an aquifer may turn to groundwater to satisfy the irrigation needs. The groundwater is generally a shared source that may supply water for others outside of the farmer's property. It may also feed the springs that provide or contribute to the wildlife habitats. Thus the farmer's profit would be made at the expense of others. In a separate scenario, the owner of the overlying property could opt for selling the groundwater. Today the groundwater amounts to 30% of the state's water supply in an average year.²¹

The groundwater rights are very complex and the absence of a comprehensive statute for groundwater management often results in overdrafts. The owners of land overlying aquifers generally share groundwater within the scope of reasonable use under the correlative rights doctrine, yet the property rights approach is being used in some basins, namely Techapi and Mojave.²²

The proponents of water markets argue that applying property rights to water is the only solution to over-extraction. However, a more comprehensive groundwater regulatory environment would accomplish the goal. Also, if the farmers are tempted to overdraft groundwater to compensate for the sold surface water, they would possibly overdraft to make a profit.

The current water marketing system enables the agricultural companies to generate profits by selling a resource they obtain at subsidized prices. Thus, the taxpayers from California and other states (CVP is a federal project) are forced to indirectly subsidize the farming companies and the water brokers in the indirect transactions. Nevertheless, the water marketing arrangements are becoming more commonplace.

In the past eight years California has enjoyed high levels of precipitation. However, in 2001 these levels have decreased, leading to concerns about another drought. Between 1995 and 2000 Sacramento river provided an average of 18.1 million acre-feet of water annually, however, in 2001 it is expected to provide only 9.7 million acre-feet.²³ Another drought would not only re-ignite the water wars, but would also make it easier to market water. The Water Bank, California's first large-scale arrangement to facilitate water marketing, was created in 1991 in response to the drought.

6. Current privatization-related developments in California.

²¹ *California Department of Water Resources*. "The California Water Plan Update. Bulletin 160-98." Online: <http://rubicon.water.ca.gov/pdfs/b160cont.html#es>, p. ES3-5, 1998.

²² *Pacific Research Institute for Public Policy*. "Ending California's Water Crisis. A market solution to the politics of water." Jul 1999.

²³ Martin, Glen. "Drought could be our next crisis. Population growth threatens water supply." *The San Francisco Chronicle*, 22 Jul 2001.

Water markets are the central water privatization-related development in California today. For instance, the MWD of Southern California is looking to purchase 100,000 acre-feet of water to be stored for the next drought. It has received sixteen offers from the agricultural interests and private companies. Among them was Enron's water subsidiary Azurix, which owns cotton acreage and water rights in the San Joaquin Valley.²⁴ Other water companies are also very active in the state. U.S. Filter, a Vivendi subsidiary, owns 43,000 acres of farmland and extensive water rights in the Imperial Valley.²⁵ The privatization of water and wastewater systems is another important development in California. The following two cases showcase these two developments.

Cadiz, Inc. and Mojave Desert.

The Met is searching for new sources of water. Among the solutions is a controversial deal with Cadiz, Inc., an agricultural business that owns property in the Mojave Desert. Cadiz proposes extraction of water from the underground aquifer located beneath its property to be sold directly to MWD. It is estimated that Cadiz would receive approximately \$20 million annually for the sales of the aquifer's water.²⁶ The agreement would last 50 years and cost the state approximately \$1 billion, half of which would go to Cadiz.²⁷ The deal also involves diverting some of the Colorado River water to Cadiz aquifers in the wet years and extracting it together with the native waters during the drought.²⁸ This raises concerns about possible contamination of the aquifer's groundwater. Finally, under the deal the company would sell up to 30,000 acre-feet to the third parties via MWD's pipes.

In April the MWD board approved the plan despite many criticism from citizens and from the environmental community. The desert population is concerned with availability of water for use in the future. The environmental groups are worried about desiccation of springs essential to the sustainability of the natural habitats. They have also pointed out that extracting what could amount to 49 billion gallons of water annually would create dust bowls.²⁹ California's Sierra Club has been especially active in the opposition to the contract.

Monitoring of water levels would be a critical part of the plan. However, according to Kristina Clark of Association of California Water Agencies, the cost of the monitoring program alone would be approximately \$2 million. "If this becomes the new standard [for

²⁴ Flanigan, James. "Decision forces new water era upon California." *Los Angeles Times*, 7 Jun 2000.

²⁵ Gardner, Michael. "California water wars pay off for lobbyists. Metropolitan District is the biggest spender." *The San Diego Union-Tribune*, 19 June 2000.

²⁶ Coy, Debra. "California: Why the electricity crisis should help the private water market." *Public Works Financing*, Jan 2001.

²⁷ Wisckol, Martin. "District cautious in deal with private water supplier." *The Orange County Register*, 17 Jan 2001.

²⁸ Bowles, Jennifer. "Water plan questioned: Residents' concerns center on availability and the environment. Some praise the \$150 million Mojave project at a hearing." *The Press-Enterprise* (Riverside, Ca), 1 Dec. 2000.

²⁹ Bowles, Jennifer. "Panel tables decision on Mojave water plan." *The Press-Enterprise* (Riverside, CA), 9 Jan 2001.

storage programs], we may end up pricing ourselves out of the future,” Clark said.³⁰ Chromium 6, a suspected carcinogen, has been found in the aquifer water in December. The discovery would likely augment the costs of water treatment.³¹

Despite the elaborate plans to extract such massive amounts of water, it is not yet known how much water the aquifer has exactly. The U.S. Geological Survey said that the company and the MWD have exaggerated the amount (the MWD and Cadiz estimated that 750 billion gallons of native water could be safely extracted over the next 50 years).³² The Survey has also criticized the company’s estimations of the recharge rates.³³ The criticism was echoed by the environmentalists and hydrologists, who say that the area is only capable of generating 5,000 acre-feet per year instead of 50,000 projected by Cadiz.³⁴

An Environmental Impact Review of the project, is due to be released in July by the U.S. Bureau of Land Management, which must approve the project before the MWD can proceed. The Bureau can make the decision 45 days after the report’s release.

The final version of the contract that would specify construction and operating costs, establish a pricing formula, and create security provisions is still being negotiated. A tentative plan disallows pumping in the first five years, while more precise data is being collected. The Metropolitan Water District and Cadiz, Inc. have not yet agreed on minimum water levels.³⁵ According to Bob Meer of the Met, the contract could be finalized as early as in September.

The MWD is concurrently pursuing two similar storage programs in the Palm Spring area, however they involve public agencies.³⁶

Keith Brackpool, the chief executive of Cadiz, is a very power figure in the Californian politics. He was the leading campaign contributor to Gray Davis’ campaign for governor.³⁷ Brackpool has also become the governor’s leading advisor and confidant on the water issues. Not only was he appointed to important committees, but he has also

³⁰ Bowles, Jennifer. “Water plan questioned: Residents’ concerns center on availability and the environment. Some praise the \$150 million Mojave project at a hearing.” *The Press-Enterprise* (Riverside, Ca), 1 Dec. 2000.

³¹ Ibid.

³² Wisckol, Martin. “District cautions in deal with private water supplier.” *The Orange County Register*, 17 Jan 2001.

³³ Bowles, Jennifer. “Panel tables decision on Mojave water plan.” *The Press-Enterprise* (Riverside, CA), 9 Jan 2001.

³⁴ Lair, Keith. “Bighorn threat effects of new water plan worry animal conservation officials.” *Los Angeles Daily News*, 10 May 2001.

³⁵ Keith, Leon D. “Fenner Valley aquifer spurs water war. Environmentalists, officials debate plan to sell ground water.” *The Detroit News*, 30 Apr 2001.

³⁶ Perry, Tony. “California and the West MWD Delays vote on buying water utilities; with the energy crisis on their minds, board members suggest caution in purchasing from Cadiz Land Co. and selling to consumers at market rates.” *Los Angeles Times*, 9 Jan 2001.

³⁷ Rabin, Jeffrey. “Firm that seeks water deal gives heavily to Villaraigosa contribution: Cadiz Inc. hopes to operate a \$150-million storage project. The next mayor will appoint water board members.” *Los Angeles Times*, 30 May 2001.

spoken on behalf of the governor in public forums when the latter could not make it.³⁸ According to several government officials, Brackpool influenced the allocation of state funds from a new \$1.9 billion water bond.³⁹

Brackpool and others in Cadiz have also donated \$36,000 to Antonio Villaraigosa's campaign for Los Angeles mayor and \$50,000 to the state Democratic Party, which was campaigning heavily on behalf of Villaraigosa, two weeks before the city election in April 2001.⁴⁰ The mayor appoint the Los Angeles water board members.

San Francisco, CA.

The century-old Hetch Hetchy water system feeds from the Hetch Hetchy Reservoir in Yosemite National Park and provides water for 2.3 million of people in San Francisco, San Mateo, Santa Clara, and Alameda counties. The aging system needs as much as \$8 billion for the facilities' seismic upgrades and repair.⁴¹

In 2000, after much controversy, the city of San Francisco awarded a \$45 million consulting contract to an alliance led by the Bechtel Corporation. The PUC claimed that contracting Bechtel to oversee modernization of the San Francisco water system would produce as much as \$45 million in cost savings over the next four years and allow access to the necessary expertise.

Many spoke out against the contract during the exploratory and negotiation stages. Harvey Rose, San Francisco budget analyst disagreed with the claim of prospective savings, maintaining that no evidence of cost-savings had been provided.⁴² Supervisor Tom Amiano not only questioned the Bechtel's ability to produce cost-savings for the city, but also feared that the contract would eventually lead to a privatization of the Hetch Hetchy water system.⁴³ Nevertheless, the city's Board of Supervisors approved the deal. The Professional and Technical Engineers Local 21 achieved addition of limiting provisions to the contract. These provisions included breaking up the 15-year contract into 4-year segments and conducting an annual performance review, at which point the contract could be cancelled.⁴⁴

The contract does not answer the question of financing the project, the cost of which is estimated to be between four and eight million dollars. The San Francisco's mayor Willie

³⁸ Clifford, Frank and Tony Perry. "Desert water entrepreneur closely tied to governor. Keith Brackpool has Davis' year and his controversial Mojave plan gives him a big stake in state policies." *Los Angeles Times*, 16 April 2000.

³⁹ Gardner, Michael. "Davis water ally awash in criticism. Campaign contributor accused of corrupting bond process." *The San Diego Union – Tribune*, 21 June 2001.

⁴⁰ Rabin, Jeffrey. "Firm that seeks water deal gives heavily to Villaraigosa contribution: Cadiz Inc. hopes to operate a \$150-million storage project. The next mayor will appoint water board members." *Los Angeles Times*, 30 May 2001.

⁴¹ Epstein, Edward. "Price estimate doubles for fixing Hetch Hetchy. S.F. mayor seeks ways to cover \$8 billion in repairs." *The San Francisco Chronicle*, 15 November 2000.

⁴² Wilson, Yumi. "Analyst for S.F. criticizes water contract award. PUC can't prove that money's saved." *The San Francisco Chronicle*, 15 Jul 2000.

⁴³ Epstein, Edward. "S.F. Board Oks Hetch Hetchy pact. Bechtel-led consortium to renovate water system." *The San Francisco Chronicle*. 29 Aug 2000.

⁴⁴ David Novogrodsky, Professional and Technical Engineers Local 21, Phone conversation, 23 Jul 2001.

Brown said that a bond measure to finance the upgrades would amount to a political suicide. At the same time the city government has been blamed for not putting water revenues back into the infrastructure, but instead using it to balance the city budget. In 2000, \$29 million out of \$39 million water funds were used for purposes other than water.⁴⁵

Brown proposed alternative ways to raise funds. One of them is selling more power generated by the PUC owned hydroelectric dams. Another is to invite the bottled water giants such as Evian and Perrier to export water from the Hetch Hetchy.⁴⁶ However, these projects would only cover a fraction of the total costs. Some believe that one reason why the mayor thought consulting services from a private company instead of performing the upgrades in-house was to attract private sector financing, which would require a higher degree of private involvement in operation and management of the water system.

Many have argued that the contract would lead to an eventual privatization of the system. According to David Novogrodsky, the executive director of the Professional and Technical Engineers Local 21, the mayor has been a long time proponent of privatization. Moreover, according to the *San Francisco Independent*, he has met with Bill Wardwell of American Water Services, a company that has expressed interest in running the Hetch Hetchy. According to the mayor's office, Brown would consider ideas that involve privatization schemes of a lesser degree than the outright ownership transfer. So far, no comprehensive financing plan has been developed.

According to Novogrodsky, so far Bechtel has done very little, other than charging "outrageous" fees. Bechtel's workers are not working with the city engineers. There are a few "higher-ups," who often perform in the capacity of management, and many lower-level workers. The director says that the majority of the staff is not qualified and that it is not unusual to see Bechtel employees sitting down studying for their engineering exam, instead of performing real work.⁴⁷ Questioning the contract benefits, the Board of Supervisors, whose composition has changed last December in favor of the Bechtel's opponents, has put most of the Bechtel budget on reserve.

In November 2001, San Francisco will vote on two ballot initiatives. Both call for a creation of a Municipal Utility District in San Francisco to lower electricity rates and take control of the city's electric plants. The mayor opposes proposals because he wants to retain power over the board appointees (the proposals would create utility districts and the PUC members would be elected from those districts). The utility district would encompass the water system. If created, it would hamper the mayor's ability to privatize water against the public desire.

⁴⁵ Lelchuk, Ilene. "Willie Brown Plans for water delivery system. Bonds, taxes last choices on his list for funding repairs." *San Francisco Examiner*, 15 Nov 2000.

⁴⁶ Ibid.

⁴⁷ David Novogrodsky, Professional and Technical Engineers Local 21, Phone conversation, 23 Jul 2001.