

Economic Failures of Private Water Systems

food&waterwatch

December 2007

www.foodandwaterwatch.org

Cities across the country have found that, despite corporate claims, private ownership of water systems significantly increases the price of water. A close look at data from more than 1,000 U.S. utilities and existing academic research reveal that private water companies are not only no better performing, but are also more expensive than publicly owned utilities.

Private Control of Water Increases Consumer Costs

Food & Water Watch compared average water rates charged by publicly and privately owned utilities in four states -- California, Illinois, Wisconsin, and New York.¹ The analysis found that privately owned water utilities charge customers significantly higher water rates than their publicly owned counterparts: anywhere from 13 percent to almost 50 percent more.

California

Data from Black and Veatch's 2006 California Water Rate Survey show that households in districts with privately owned systems are paying, on average, 20.28 percent more

per month for clean drinking water than households served by either municipal systems or special water districts created by citizens and overseen by government officials. When Food & Water Watch divided the water districts into five population size categories, publicly owned water systems proved significantly more affordable for every bracket.²

Wisconsin

Wisconsin is served primarily by publicly owned water utilities, but there are seven privately owned utilities operating. Averages compiled from a survey conducted by the Wisconsin Public Service Commission reveal that the average monthly residential water price for customers served by the seven utilities to be a startling 49 percent more than the average bill for customers served by publicly owned utilities. While public customers paid an average of \$22.98 a month, private customers paid an average of \$34.26 a month. In other words, residents of cities where the private sector controls the water flow are paying an average of \$135.36 more each year.³

Illinois and Nine Other Midwestern States

A 2000 survey of Illinois and nine Midwest states revealed that customers of privately owned systems paid 13.65 percent more than customers of public municipal systems.⁴ It stated that "publicly owned systems charged an average of \$1.28 per 1,000 gallons of water less than private and ancillary systems."⁵ Based on this survey's average monthly water consumption estimate of 6,000 gallons, this price difference equates to an additional \$92.16 paid each year by consumers in privately owned districts.⁶

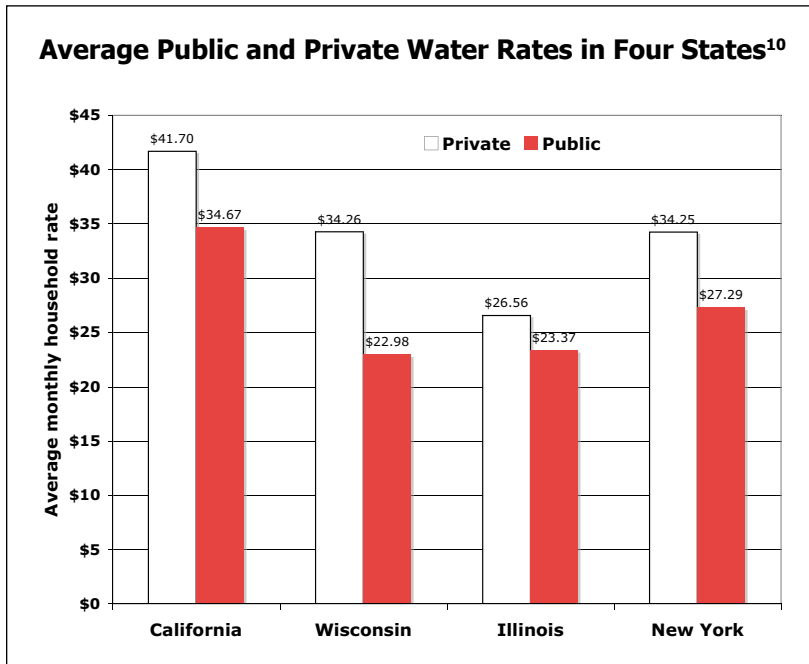
| City or water district population category | Consumers in privately owned districts in California paid, on average, this much more than consumers in publicly owned districts each year |
|--|--|
| 25,000 or less | \$63.48 |
| 25,000 – 50,000 | \$73.92 |
| 50,000 – 100,000 | \$107.88 |
| 100,000 – 200,000 | \$86.76 |
| 200,000 or more | \$112.92 |

New York

The six largest private water providers in New York state charge an estimated average of \$34.25 to families consuming an average of 1,000 cubic feet (7,480.52 gallons) of water per month.⁷ A survey conducted by the American Water Works Association estimated that the average monthly water charge for households in this region consuming the same amount of water is \$27.29, making privately owned New York utilities 25 percent more expensive than the average public utility in their region.^{8,9}

interest, taxes, depreciation, and amortization) came from its water division, known as U.S. water provider American Water.¹⁴

In the United States, regulations limit the profits of private water companies to a margin of approximately 10 percent. However, companies get around this by leveraging their assets. In other words, instead of using money they had borrowed for needed improvements to water operations and infrastructure, the companies invest in side businesses or other activities that diversify their operations to increase profits. In general, private companies have incentives to spend more on investments not directly related to the original purpose of improving water infrastructure so that more money goes into the pockets of corporate shareholders and executives.



Private Companies Charge More to Provide Water for a Number of Reasons:

Corporate Utilities Funnel Money Out of Communities and into the Pockets of Shareholders

International corporations can easily expect to make a 20 percent to 30 percent margin of profit from investment in water service. Multinational water-providing giants Veolia, Suez, and RWE are hugely profitable corporations. In 2006, Veolia made a consolidated net income of €759 million (nearly \$1.12 billion), according to its 2006 annual report. In addition, 35 percent of Veolia’s total revenue came from water, with 10 percent from North America.¹¹ In the same year Suez earned a gross operating income of €7,083 million (nearly \$10.38 billion), and RWE had a net income of €3,847 million (almost \$5.66 billion).^{12,13} Some €689 million (\$1.02 billion) of RWE’s EBITDA (earnings before

In California, three of the six corporate water companies reported a combined income of \$78.88 million in 2006.¹⁵ If this money had remained in local areas to be reinvested in water infrastructure, it would have constituted a contribution in excess of \$20 million more than the entire federal capitalization grant to California for the Drinking Water State Revolving Fund (a federal fund that administers money to states for water projects), which was able to grant only \$67.15 million in 2006.¹⁶

Financing is More Expensive for Private Companies

In order to protect the public interest, private water companies, unlike public utilities, are not eligible for municipal, tax-free bonds that carry low interest rates. Therefore, they must rely on private bonds that carry interest rates 2 percent to 3 percent higher.¹⁷ These essentially are costs that companies often pass on to consumers in the form of higher water rates. Private companies also have their operating costs driven up by property and income taxes from which public utilities are exempt.

Private Control of Water Does Not Lead to Greater Efficiency

It is commonly believed that the private sector can offer greater performance and economic efficiency than the public sector, but in the case of public water utilities this has not proven to be true. Various studies have concluded that publicly owned utilities have lower costs than privately owned utilities.¹⁸ Another study of 214 water providers in the United States found that public sector performance was superior to private sector performance.¹⁹

The theory that private ownership is superior to public ownership is based on the assumption of competition in the marketplace. However, in the case of water utilities, one system controls an entire area, so competition rarely, if ever, exists. Economists Germá Bel and Mildred Warner write: “That private production has failed to deliver consistent and sustained cost savings shows the inadequacy of theoretical approaches based mainly on assumptions about competition and ownership.”²⁰ Because competition is absent in the water sector, they conclude that, “Little support is found for a link between privatization and cost savings. Cost savings are not found in water delivery.”²¹ Writing in the journal *Land Economics*, Arunava Bhattacharyya found that, “private water utilities in the sample of the study are less efficient than public water utilities both technically and in the use of variable inputs of labor, energy, and materials.”²²

Lessons From the United Kingdom and France

The United States would do well to learn from the problems of France and the United Kingdom, where governments have given private companies much greater control of water. In France it was found that choosing to involve private companies in water distribution over direct public management increases the average retail price of water. “In all specifications, we find that consumers pay more when municipalities choose PPPs [public-private partnership].”²³ Chong et al. found that the average price for 120 cubic meters of water in a year jumped from approximately €151 to €176 when French public authorities decided to contract with private companies instead of managing their own systems.²⁴ Several studies have found that water privatization in the United Kingdom has also been unsuccessful. Saal and Park found higher prices and little improvement in productivity following the 1989 U.K. privatization of water.²⁵ Cowan et al. estimated that “privatization in the U.K. led to a net loss in total welfare, with consumers and the government net losers and the firm [private corporation] and its employees net gainers.”²⁶

Conclusion and Recommendations for the Future of America’s Water

Many citizens have had no choice but to pay a private corporation for their water. They are forced to pay higher rates and contribute to the profits of distant executives and stockholders. Whereas private corporations are biased toward capital-intensive solutions that benefit the corporation, and raise consumer rates, public utilities emphasize the needs and goals of the local community. Public management gives every citizen part ownership and direct say in the policies of their water service provider and reinvests

money in local infrastructure. To prevent private corporations from manipulating money-scarce municipalities into believing that privatization will benefit their system, America needs secure public funding for water. Communities often are pressed into privatization in hopes of avoiding the financial investments needed to maintain a water utility. To protect America’s water, the federal government should have a share in these investments. The establishment of a clean water trust fund will ease the financial burden on communities, help maintain public ownership of water utilities, and keep water clean, safe, and affordable for everyone.

Endnotes

¹ In order to draw comparisons, Food & Water Watch determined average rates per month regardless of whether the utility billed monthly, bi-monthly, or quarterly. For instance, if a utility billed by the quarter, these average rates were divided by three to create a monthly average.

² Calculations conducted by Food & Water Watch based on data drawn from the cited survey, “2006 California Water Rate Survey.” Black & Veatch, Los Angeles, California. Available by calling: 213.312.3300.

For more information, please call 202.797.6550 or email foodandwater@fwwatch.org.

³ Calculations conducted by Food & Water Watch based on data drawn from the cited study, “Comparison of Net Quarterly Bills of Wisconsin Water Utilities Using Rates in Effect as of February 26, 2007.” Public Service Commission of Wisconsin, Division of Water, Compliance and Consumer Affairs, Bulletin 25, February 2007. Available at: <http://psc.wi.gov/apps/waterbill/bulletin25/default.asp>

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⁴ “Benchmark Investigation of Small Public Water Systems Economics.” Department of Geography and Department of Agribusiness Economics, Southern Illinois University Carbondale, Carbondale, IL, November 2000, p V-26. Available at: <http://mtac.sws.uiuc.edu/mtacdocs/BenchFinRpt/BenchFinRptoo.pdf>

⁵ *Ibid.* p. VI-26

⁶ Calculations conducted by Food & Water Watch based on data drawn from the cited study.

Ibid.

\$1.28 x 6 (per thousands of gallons a month) x 12 months a year = \$92.16 a year.

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⁷ Calculations conducted by Food & Water Watch based on the tariffs listed by the cited companies’ websites in October 2007.

Long Island American Water: www.illinoisamerican.com/awpr1/nyaw/customer_service/rates/rates_schedules/page5097.html

New York Water (acquired by Aqua New York Inc): Tariff Query – New York Water Service Corporation, Electronic Tariff System, New York Public Service Commission. Available at: www2.dps.state.ny.us/ETS/home/index.cfm

United Water New Rochelle: www.unitedwater.com/uwnr/customer.htm

United Water New York: www.unitedwater.com/uwny/customer.htm

Aquarion New York (acquired by United Water),
www.aquarion.com/newyork.html

Aquarion Sea Cliff (acquired by Aqua New York):
www.aquarion.com/seacliff.html

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⁸ “2006 Water and Wastewater Rate Survey.” American Water Works Association, Denver, CO and Raftelis Financial Consultants Inc., Charlotte, NC, 2007, p. 80. Please note that this regional survey was used because no information on average public rates for New York State was available.

⁹ Calculations conducted by Food & Water Watch based on data drawn from the cited survey,

Ibid.

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¹⁰ Note that although the average public and private water rates are comparable to each other within states, rates cannot be directly compared between states because averages for each state are based on different estimated levels of water consumption. For California, average water consumption was estimated to be 11,220.78 gallons a month; for Wisconsin it was 6,250 gallons a month; for Illinois and the surrounding states it was 6,000 gallons a month; and for New York it was 7,480 gallons a month. Also note that the average “Public” figure for New York comes from data that is regional, rather than state specific, and that the survey it comes from lumped a negligible amount of rates from privately owned companies into this average.

¹¹ “Annual Report 2006.” Veolia Environment, Paris, France, p. 10. Available at: www.veoliaenvironnement.com/en/newsroom/publications.aspx

¹² “Annual Results 2006.” Suez, Paris, France, p.3. Available at: www.suez.com/en/finance/investors/2006-annual-results/2006-annual-results/

¹³ “Investing in Innovation and Growth: Annual Report 2006.” RWE, Essen, Germany, p. 60. Available at: www.rwe.com/generator.aspx/investor-relations/finanzberichte/language=en/id=15704/page.html.

¹⁴ Ibid., p. 52.

¹⁵ Calculations conducted by Food & Water Watch based on data drawn from the cited sources:

Form 10-K of the United States Securities and Exchange Commission. California Water Service Group, filed 3/14/2007, p.28. Available at: <http://ir.calwatergroup.com/phoenix.zhtml?c=108851&p=irol-sec>

Form 10-K of the United State Securities and Exchange Commission. American States Water Company, filed 3/26/07, p 16. Available at: <http://phx.corporate-ir.net/phoenix.zhtml?c=87080&p=irol-sec>

Form 10-K of the United States Securities and Exchange Commission. San Jose Water Corporation, filed 3/09/2007, p. 15. Available at: http://ir.10kwizard.com/files.php?source=1033&welc_next=1&XCOMP=0

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¹⁶ “Revised Final Intended Use Plan for FFY 2006 DWSRF Grant.” Division of Drinking Water and Environmental Management, California Department of Health Services, Sacramento, CA, June 2007, p. 7. Available at: www.cdph.ca.gov/services/funding/Pages/SRF.aspx

¹⁷ Personal Communication via Email. American Water Works Association, October 9, 2007.

¹⁸ Ibid. Citing the following studies:

Pescatrice, D. R. and Trapani, J. M. III. “The performance and objectives of public and private utilities operating in the United States.” *Journal of Public Economics* 13(2):259-76, 1980

Färe, R. et al. “The relative performance of publicly-owned and privately-owned electric utilities.” *Journal of Public Economics* 26(1):89-106, 1985. And:

Meyer, R. A. “Publicly owned vs. privately owned utilities: a policy choice.” *Review of Economics and Statistics* 57(4):391-99, 1975.

¹⁹ Shirley, Mary and Walsh, Patrick. “Public vs. private ownership: the current state of the debate.” World Bank Policy Research Working Paper 2420, Washington, DC, August 2000, p. 51.

Citing: Mann, Patrick C. and Milksell, John L. “Ownership and Water System Operation.” *Water Resources Bulletin*, 12, 1976.

²⁰ Bel, Germá and Warner, Mildred. “Local privatization and costs: theoretical expectations vs. empirical evidence.” Submitted to *Public Administration Review*, October 26, 2006.

²¹ Ibid.

²² Bhattacharyya, Arunava et al. “An examination of the effect of ownership on the relative efficiency of public and private water utilities.” *Land Economics*, 70(2):197-209, May 1994.

²³ Chong, Eshien et al. “Public-private partnerships and prices: evidence from water distribution in France.” *Review of Industrial Organization* 29(1-2):149-169, October 2006.

²⁴ Ibid.

²⁵ Saal, David S. and Parker, David. “Productivity and price performance in the privatized water and sewerage companies of England and Wales.” *Journal of Regulatory Economics* 20(1):61-90, July 2001.

²⁶ Wallsten, Scott and Kosee, Katrina. “Public or private drinking water? The effects of ownership and benchmark competition on U.S. water system regulatory compliance and household water expenditure.” Working Paper 05-05, AEI-Brookings Joint Center for Regulatory Studies, Washington, DC, March 2005. Citing:

Cowan, Simon et al. “Competition and regulation in urban water supply: the privatization of Thames water.” Washington, DC, 2000.

About Food & Water Watch

Food & Water Watch is a nonprofit consumer organization that works to ensure clean water and safe food in the United States and around the world. We challenge the corporate control and abuse of our food and water resources by empowering people to take action and by transforming the public consciousness about what we eat and drink.

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