

World Cup 2018: private water and sewage companies score high in Brazil

Copa do Mundo de 2018: gol das empresas privadas de saneamento no Brasil

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During the 2018 FIFA World Cup, the Brazilian Administration issued an Executive Order (MP) that substantially altered the regulatory framework for basic water and sewage utilities (MP n. 844/2018). According to the order, the purpose was “to improve the structural conditions for basic sanitation in the country” ¹. The order was signed only a few hours before Brazil’s last match, just under the binding deadline according to election-year rules, with the condition that Congress ratify it within 45 days.

Opposition to the order drew a broad range of interest groups in the utilities industry. States and municipalities promised to challenge the Executive Order in court, on grounds that it violates the Constitution, and also because they had not been properly consulted. Of all the representative organizations from the sector, only the private companies seemed to be happy with the order. The Brazilian Association of Private Water and Sewage Utility Companies (ABCON) ² and the National Confederation of Industry (CNI) ³ defended the measure publicly, claiming that it encourages the expansion of private enterprise in the sector. They stated that they intended to help Congress “approve the best possible wording for society and the productive sector” ³. Based on this, the new law has been dubbed the “Executive Order for Privatization of Water and Sewage”.

The main changes proposed by the order relate to the industry’s regulation and contracts on concessions for water and sewage utilities. Briefly, it specifies the National Agency of Water (ANA, for its acronym in Portuguese) as responsible for standardizing the regulation of basic water and sanitation services nationwide and eliminates mandatory municipal sanitation plans as a condition for hiring utility companies. More controversially, the order applies to program contracts (the instrument for collaboration between different levels of government, or between government agencies and public consortia, for common public utilities) the essential clauses for concession contracts provided in *Law n. 8,987/1995*. Let us see what this involves.

National Agency of Water

At present, public water and sewage utilities in Brazil are regulated by the municipalities (cities), which can delegate them to specialized agencies. Under the Executive Order, ANA issues the national standards for regulation of public water and sewage services by their owners and the respective regulatory and inspection agencies, conditioning access to federal funds on compliance with the

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guidelines and standards issued by ANA (Executive Order, Article 4-B). The proposal's critics contend that the centralization of regulatory standards for a sector operated with such diverse scales and models poses a challenge for a federal agency like the ANA that lacks the institutional profile for such a task, besides the potential conflicts of interest in the mission of operating other uses of water. ANA has not taken a public stance on the issue, especially in relation to the challenge involved. But the existence of a federal agency with the responsibility of harmonizing the sector's regulatory activities seems to be positive, in the sense of creating a national parameter for the multiple existing regulatory practices. At any rate, a study on the Growth Acceleration Program for Sanitation (PAC saneamento) showed that the problems with the financial execution of the projects during the program were due not specifically to the sector's regulation by the Federal government, but to the insufficient technical and administrative conditions on the part of the proponents (municipalities and states) to deal with the basic requirements under the legislation for such projects⁴. The study showed that under Brazil's current federative framework, it is necessary to invest more in training for the local administrations to manage the available resources rather than in the federal supervision over regulatory agents, an issue that the Executive Order overlooks.

Water and sewage plans

The adoption of technical studies by the Executive Order to replace the municipal water and sewage plans (Article 11, §5), claiming that they would simplify the administrative procedures involved in hiring service providers, ignores the reasons why they were included in the original law. Water and sewage plans are an important municipal planning tool, for local administrations that integrate these utilities with other vectors of urban expansion. The argument that investment in utilities has failed to materialize because the municipalities generally lack the mandatory plans ends up masking the reality and inverting the logic of the facts. In reality, the absence of such plans results from the lack of planning by municipal authorities, who should produce the plans but do not⁵. It also reflects the weakness of local governance in such services, a problem that the requirement in the original law aimed to solve. The minimum development of governance in water and sewage services by municipalities is essential for strengthening them in their relations with service providers and public utilities, in favor of the population, which was the purpose of the law requiring the plans. The replacement of the plans with technical studies is apparently intended merely to facilitate signing contracts, with no regard for encouraging the involvement of the services' ultimate owners (the municipalities) through improved local planning, which is essential.

Mandatory bidding for utilities concessions via program contracts

The main controversy over the Executive Order is the change in the process of signing the so-called program contracts between municipalities and water and sewage utility companies. Until now, the municipal governments could sign contracts directly with the state utility companies and automatically renew them without the need to conduct a public tender, when the concession on the services assumes collaboration between levels of government (e.g. between municipalities and states), as in the case of water and sewage⁶. The new Executive Order will now require that all municipalities issue a call for prior manifestation of interest before closing or renewing any procedure connected to the concession of services (Article 10A). If another service provider expresses interest in such services, the municipal government will be required to conduct a new public bid, as required by *Law n. 8,987/1995*.

The change responds to a demand by private water and sewage companies, which criticize the current model, claiming that municipalities tend to opt for the program contracts with the public companies out of convenience and lack of infrastructure to conduct the bids. The problem is that with the change, the tenders are certain to attract bidders to the cities that are running on a financial surplus, but not to those running on a deficit. Public and private operators will compete for the former, while the latter will be left to the cities and states, which will either turn to the state-owned companies or be forced to cover the services with their own tax revenues (already scarce). For state-owned util-

ity companies, as the wealthier cities leave, their contracts will be fragmented, which tends to make cross-subsidies unfeasible (having been used widely to extend coverage to the poor in regionalized provision). The Executive Order fails to provide any alternative for these poor cities, which account for the vast majority of the Brazilian population. In addition, the stimulus for individualization of concessions hinders cooperation between different local and state administrations (which brings gains for the whole population).

The states and the organizations linked to the state-owned companies have real reasons to be concerned, and so do the municipalities. The Executive Order provides that in case of privatization of state companies, the contracts with the municipalities will be maintained normally, even with the change in the companies' ownership, which was not allowed by the previous legislation. Before the Executive Order, the contracts automatically became defunct, since municipalities would have to agree to the new provider and the new contract's rules. This rule meant a high risk for private investors, who saw the potential danger of operations and services being drained in a company that was up for acquisition. With the new rule, if the municipality refuses to stay in the contract, the exit cost is that it inherits the debt on non-amortized investments made by the old company. Curiously, in case of consent to the new provider, there is no mention of compensation of those debts for the state companies. The transaction grants all the advantages for the incoming concessionaire, which inherits the structure and customer base but not the business risk. This was the most important change provided by the Executive Order to unlock the privatizations program in water and sewage utilities, launched by the Federal government in 2016 (without the expected success).

The voices that have spoken out against the Executive Order are correct in demanding that such impactful changes should not be made by a temporary order, which appears to have precisely the purpose of avoiding public debate and vetoes by key stakeholders. In a democratic system, such changes should be made through a proper Bill of Law, in which Congress, organizations, and utilities workers can contribute to collectively drafting the proposal.

The Administration's response has been to ignore the outcry and insist on the discourse that blames underfinancing of the services for the structural problems in the sanitation sector. The Administration claims that the fiscal crisis and lack of government funds for the major investments required by the utilities industry do not allow dealing with the huge gap in access to such services, that the public sector cannot meet this demand for investment without the help of private enterprise, and so on. But the fact is that financing is just one of the industry's obstacles, and not even the most important one ⁷. Besides, private enterprise could already draw on abundant legal provisions in order to participate in Brazil's utilities industry (Article 175 of the 1988 *Federal Constitution*, the Concessions Law, public-private partnerships, etc.).

The changes proposed by the Executive Order do not touch the underlying and structural issues afflicting the water and sewage utilities industry in Brazil. They encourage privatization in the municipalities by promoting individual bids, without the local governments being properly strengthened to face the economic power of private groups in exploiting vital public services for the population. The order also penalizes local governments that take a stance against staying in contracts with which they disagree, in case of a change of ownership in the concessionaire (privatization). The order has the power to force a city that is ideologically against privatization to hire a private company that may have won a mandatory bidding process – the same bidding process that the private sector sees being avoided by cities that adhere to program contracts because they do not consider themselves capable of performing the services themselves. The order imposes extremely high financial reversal costs and human costs in the short term, since it can lead to rate hikes and very likely to the exclusion of large shares of the population from access, as in various cities around the world where this has happened. In Bolivia, price hikes on water led to violent popular uprisings. In Chile, they led to a dramatic shortage of water for human consumption in favor of agribusiness ⁸. Why would the situation be any different in Brazil, where poverty and inequality go hand-and-hand with an agribusiness that razes forests, enslaves, and pollutes?

The Executive Order's main strategy is to guarantee a business that is not only risk-free, but free of any burden or competition for the private companies interested in exploiting the sector in Brazil. If such companies are interested in taking over state-owned utility companies, they can inherit the customer base without the burden of non-amortized investments. If they do not take over, they will

have competitors that are fragmented and have their finances undermined. The order fails to improve the structural conditions in the water and sewage utilities industry as claimed, but rather favors action by private sanitation companies in the country.

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