



# Research and Surveys Series: The Interface between Regulatory Frameworks and Tri-Sector Partnerships

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## Business Partners for Development

Sustainable development is a global imperative, and strategic partnerships involving business, government and civil society may present a successful approach for the development of communities around the world. Business Partners for Development (BPD) is an informal network of partners that seeks to demonstrate that partnerships among these three sectors can achieve more at the local level than any of the groups acting individually.

Among the three groups, perspectives and motivations vary widely however, and reaching consensus often proves difficult. Different work processes, methods of communication, and approaches to decision-making are common obstacles. When these tri-sector partnerships succeed though, communities benefit, governments serve more effectively and private enterprise profits, resulting in the win-win situation that is the ultimate aim of BPD and its divisions, or clusters.<sup>1</sup>

### THE WATER AND SANITATION CLUSTER<sup>2</sup>

The Water and Sanitation Cluster aims to improve access to safe water and effective sanitation for the rising number of urban poor in developing countries. By working in partnership it is presumed that governments can ensure the health of their citizens with safe water and effective sanitation while apportioning the financial and technical burden, the private sector can effectively meet their contractual obligations while ensuring financial sustainability over the long term, and communities can gain a real voice in their development.

The Water and Sanitation Cluster works with eight focus projects around the world, most of which predated the Cluster. The approach to extracting information from which to analyse the efficacy of tri-sector partnership is three-pronged: 1) by supporting partnership-oriented research on thematic project elements (cost recovery, education and awareness, etc.); 2) by creating forums for analysing the sector specific (civil society, public and private sector) benefits and challenges of working so closely with organisations from other sectors; and 3) by documenting the evolution of the partnership in specific focus projects.

The Cluster supports learning and then disseminates findings through newsletters, a web site and other key publications to share best practice widely.

### THE FOCUS PROJECTS

- Drinking water supply and sewer system in the El Pozón quarter, Cartagena, Colombia
- Water supply improvements to Marunda District, Jakarta, Indonesia
- Restructuring public water services in shanty towns, Port-au-Prince, Haiti
- Developing water supply and sanitation services for marginal urban populations, La Paz and El Alto, Bolivia
- Innovative water solutions for underprivileged districts, Buenos Aires, Argentina
- Sustainable water and wastewater services in underprivileged areas, Eastern Cape and Northern Province, South Africa
- Management of water services, Durban and Pietermaritzburg, South Africa
- Upgrade and expansion of local water networks, Dakar, Senegal

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<sup>1</sup> The five clusters of the BPD include: the Global Partnership for Youth Development; the Global Road Safety Partnership; the Natural Resources Cluster; the Water and Sanitation Cluster; and the Knowledge Resource Group (which collects and disseminates the lessons learned from the four thematic clusters for wider audiences).

<sup>2</sup> In the context of this report, the terms BPD and Water and Sanitation Cluster are used interchangeably. Although the goals of the other BPD clusters are the same, the approaches have varied widely.

## Executive Summary

*Addressing regulatory issues rarely figures at the centre of tri-sector partnerships' preoccupations,<sup>3</sup> even though the constraints set by regulation may have a great impact on what they can achieve. Similarly, regulatory institutions do not necessarily see the relevance of co-operating with local-level partnerships on issues related to the provision of water and sanitation services to poor consumers. Based on BPD experience,<sup>4</sup> this report calls for a greater dialogue between regulatory institutions and partnerships for two main reasons: first, because partnerships can significantly contribute to making regulation more pro-poor; and second, because partnerships should more clearly understand how regulatory frameworks can affect their activities so as to improve their design and objectives.*

### INTRODUCTION

Governments, private sector operators and international donors alike have all become increasingly aware of the importance of addressing the needs of the poor when introducing private sector participation. But they still need to find the most appropriate ways of doing so, particularly for the design of regulatory frameworks that would be most conducive to expanding water and sanitation services to the urban poor.

Indeed, the poor face very specific constraints for accessing water and sewerage services. Private operators are sometimes reluctant to serve poor people because they see them as not profitable or too risky: supply costs are often higher in poorer areas, which tend to be inaccessible; demand per head is relatively low; and debt collection can be hazardous if mafias are operating in the area. Customers are often difficult to identify, especially if they live in illegal settlements that the government wishes to uproot. Even if a utility does extend its network into poor neighbourhoods (either willingly or to comply with its contractual obligations), the poor might find the connection charge too high or the billing schedule too demanding.

Regulation can play a decisive role in making water and sanitation services more accessible to the poor and in providing private operators with the right incentives to serve them. Furthermore, this report argues that partnerships can help regulation in achieving just that.

### What is regulation and why is it important?

The term 'regulation' should be understood, in a broad sense, as a set of functions that can be carried out by a wide range of public institutions. In the 'independent regulation' model, a specialised agency is created to carry out regulatory functions in a way that is as independent as possible from the setting of policy objectives for the sector. In other models, the separation between such functions is not as clear and a Ministry or a municipality may be in charge of ensuring that the private operator provides the service according to a set of pre-defined principles. But in both cases, these institutions are carrying out 'regulatory functions', i.e. they are ensuring that the service is provided by a private operator with the best interests of society in mind and, thereby, protecting customers from potential abuses of monopoly position by the private operator.

In the water and sanitation sector, regulatory functions can be broadly divided into three categories: economic, environmental and public health regulation. The way in which these functions are performed can have a significant impact on whether or not the poor have access to the service, and at a price they can afford. For example, the definition of blanket quality standards ('one standard for all') may hinder access for the poor if quality is set too high (thereby increasing the cost of service) and alternative lower quality service options, such as

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<sup>3</sup> Further description of tri-sector partnerships can be found overleaf.

<sup>4</sup> Business Partners for Development (BPD) was established to explore partnerships between business, government and civil society sectors. The Water and Sanitation Cluster of the BPD has been working with eight partnership projects around the world to determine the efficacy of the partnership approach in providing water and sanitation services to the poor.

small-scale water vendors, are simultaneously banned. In general, the poor tend to benefit from regulation carried out in a flexible, transparent and accountable manner.

### **What roles can partnerships play in making regulation more pro-poor?**

Around the world, partnerships between the private, public and civil society sectors have been formed at the local level in an effort to better tackle the challenge of providing water and sanitation services to the poor. The underlying premise is that, through working together, these sectors can provide services to the poor more effectively than by working alone.<sup>5</sup>

Study of the eight partnerships within the BPD Water and Sanitation Cluster has shown that partnerships can play very important roles in making regulation more pro-poor:

- *Partnerships can help focus the attention of regulatory institutions on poverty issues:* The partnerships in question have usually been created with the specific remit of helping the poor. Therefore, their very existence can draw attention to poverty issues and provide a voice to poor consumers who would otherwise be ignored.
- *Partnerships can help gather information on the needs of the poor and make it available for regulation:* In many cases regulators tend to ignore the poor because they do not have readily available information about them, or enough human and financial capital to go and collect it. Partnerships can play an important role in gathering and relaying information to decision-makers, due to their continuous presence in the field.
- *Partnerships may also provide a way for the poor to make their voice heard – serving as one recourse mechanism for poor customers' complaints:* This role is especially useful when regulatory institutions are weak or inaccessible to the poor.
- *Partnerships can create a more flexible, innovative and co-operative environment for developing rules better suited to the needs of the poor:* Existing rules may hinder the provision of services to the poor because they do not fit their requirements in terms of costs and quality. Partnerships can provide the framework for experimenting with alternative services (and corresponding rules) by acting in two ways: they either obtain an exception to the existing rule and work on a pilot project basis, or they have to work around the existing rule to demonstrate the usefulness of changing the rule to the regulator. Partnerships can achieve this as they represent more than one stakeholder – partners thus avoid being seen as wanting to change a particular rule simply to serve their own interests.
- *Partnerships can help partners understand each other's interests and constraints with respect to regulation:* Each member of the partnership has its own agenda and interests with respect to regulation but also has its own constraints. Working in partnership allows partners to understand each other's interests and constraints better and work towards a consensus solution. This may make regulation both more appropriate and more effective.
- *Partnership may also serve as a self-regulation mechanism:* The process of developing a formal partnership encourages regular meetings between partners and should lead to the introduction of reporting mechanisms. These mechanisms can create a form of self-regulation, thereby reducing the need for strong regulation.

In **Port-au-Prince**, the adoption of a partnership approach convinced the public sector service operator (CAMEP) to provide services in poor boroughs where it was previously too fearful to go. As the situation improved, the NGO changed its role from that of community intermediary to one of advocate and watchdog, providing customers with a recourse mechanism.

<sup>5</sup> These partnerships are very diverse and the range of actors and manner in which they work together varies widely: partnerships are very context-driven and hence no one model exists for how tri-sector partnerships should be structured. In leveraging their own resources, however, all actors are able to achieve more than by working on their own – partners can rely on their core competencies and have other actors fill in gaps in their skills, abilities or mandates. Diversity is the key – choice of actors and modes of working depend very much on the context faced and should build upon existing assets. Partnerships should go deeper than mere contractual relationships: an emphasis on shared decision-making and resource allocation typifies this, as does the stress on formalised governance structures. These underpin the legitimacy, accountability, effectiveness and equity of the partnership.

### ... And how can they contribute to making regulation more pro-poor?

In practice, the BPD partnerships have been able to influence regulation in a number of ways, although they have fallen short of expectations in some areas where they could potentially be of use:

- *Price regulation:* Partnerships have been effective at developing strategies for pro-poor tariff structures. In particular, some partnerships have worked as a targeting mechanism for reduced connection charges, which often represent the biggest barrier for the poor. Others have helped develop more appropriate billing regimes and payment methods. By contrast, their role in setting overall tariff levels has tended to be limited to one of consultation.
- *Quality regulation:* In rigid regulatory regimes, without variable approaches to service quality regulation, partnerships have sometimes been effective at introducing variable service quality standards. In more flexible regimes, they have rarely sought to experiment further. Overall, their role in developing more flexible approaches to quality regulation has not reached its full potential, either in terms of regulating customer service quality or setting environmental and health standards.
- *Coverage targets:* When private sector operators have contractual coverage targets, partnerships have played an important role in adapting coverage obligations to an evolving reality. Focusing coverage targets on specific areas and setting more manageable short-term targets has achieved this. However, partnerships have usually been ineffective at promoting the provision of sanitation services if those are not required in the contract.
- *Competition regulation:* Several partnerships have led to the establishment of independent providers who signed bulk supply agreements with the main operator, therefore contributing to the organisation of this market. However, few partnerships have dealt with, or have explicitly considered' the impact of their activities on totally independent private providers.

In *La Paz-El Alto*, the partnership was allowed to pilot alternative quality standards to those imposed by the national regulations. The successful experimentation with the condominium approach to service delivery has led to the development of alternative regulations, better suited to the needs of the poor. This might have been aided by the fact that the regulator took part in the partnership, although only as an observer.

### What factors may influence partnerships' success in making regulation pro-poor?

While some of the BPD partnerships have played several of the roles outlined above, others have not. Two factors seem to influence partnerships' relative success in making regulation more pro-poor:

- *Partnerships are more likely to be empowered to lift a regulatory constraint when the regulatory body is involved in the partnership and acts at the same level:* The involvement of the regulatory body usually ensures a speedier and more direct approach for modifying potential regulatory obstacles to pro-poor service delivery.
- *Partnerships are more effective when partnership agreements are in place to regulate relations between actors:* Partnerships can more effectively undertake the various roles outlined above when they are formally defined and, thus, when partners clearly understand each other's roles and responsibilities in addition to the partnership's overall objectives. Where such formal agreement is not in place, some partners (and especially civil society partners) have tended to fade away.

In *KwaZulu-Natal* the partnership was created through two co-operation agreements between the partners from each sector, one for Durban and one for Pietermaritzburg. These agreements outline roles, responsibilities and financial commitments for the BPD projects. Powers in the partnership are equally shared, and financial contributions do not imply more influence in decision-making. This has allowed the partnership to take decisions based on consensus and adopt a flexible approach to adapt to new issues linked to pro-poor services.

## **How could regulatory institutions make better use of partnerships in future?**

Given the roles that partnerships can play in making regulation more pro-poor, institutions in charge of regulating the water sector should see partnerships as a key instrument for achieving their regulatory objectives. However, this depends largely on regulatory institutions' incentives: some may simply not concern themselves with partnerships because poor consumers are not their priority. As a result, a number of key implications for regulatory design can be drawn.

*Regulatory institutions should be designed in a way that makes them address the needs of poor customers and see partnerships as a tool for pro-poor regulation:* Regulatory institutions are a product of the work of policy-makers. The onus is therefore on policy-makers to design institutional and regulatory frameworks so that institutions in charge of regulation have a clear incentive for addressing the needs of poor customers, know how to engage with partnerships and have the means to do so.

Whilst the most obvious way forward is explicitly giving institutions in charge of regulation clear pro-poor objectives in their statutes, this objective might also be met by giving them the responsibility to promote an enabling environment for stakeholder engagement as well as to promote deeper relationships between the public, private and civil society sectors.

*Regulatory institutions should work with partnerships to solve some of the difficulties associated with pro-poor regulation:* There are a number of tasks that regulatory institutions have difficulties carrying out, particularly when poor customers are involved. For example, the design of pro-poor tariff structures may require designing subsidy schemes, which raise issues related to finding ways of targeting such subsidies to the right type of population. As partnerships have proved effective in reducing in connection charges, for example, regulatory bodies may want to work with partnerships to address similar issues.

*There are many practical ways in which regulatory institutions could actively facilitate the activities of partnerships and collaborate with them in order to improve regulation:*

- Ensuring an enabling environment for partnerships to develop in and providing access to support organisations, for both technical and, potentially, financial support;
- Providing partnerships with adequate tools to sustain themselves, such as model contracts and access to external arbitration mechanisms;
- Facilitating the establishment of pro-poor partnerships (for example, by keeping up to date on existing and potential organisations that work with civil society and may be able to represent their interests within a partnership. Such organisations may be difficult for private actors to locate).

*Regulatory institutions should not intervene in the internal functioning of partnerships:* Their responsibility is not to regulate the partnership: partners should regulate themselves on the basis of well-specified agreements (which should be flexible: rigorous but not rigid). Therefore, the distinction between regulation of the overall environment and regulation of the partnership should remain clear – it is not the regulator's job to become involved in the day-to-day running of the partnership. Accordingly, direct participation in the partnership may not be necessary, with participation as an observer more preferable.

*Regulating agencies should not seek to merely copy approaches developed by partnerships in different contexts:* It would almost be impossible for a regulatory body to simply copy an approach used by a pro-poor partnership in order to achieve the same pro-poor objective in another context. Partnerships can carry out the roles highlighted above because they engage a variety of stakeholders and leverage their complementary resources, looking to create local solutions on the basis of local information and conditions. Therefore, there are no short cuts: in order to develop payment methods suited to the particular local context, a local partnership should be set up and work collectively on these issues rather than having a regulatory institution copy a solution developed elsewhere.

## **How can partnerships maximise their potential for making regulation more pro-poor?**

Partnerships are not always successful at improving how regulation functions. In many cases, it is because partnership members would not consider improving regulation as an explicit aim and would consider their activities quite separately from the overall framework in which they operate, and particularly from the regulatory framework. Failing to realise the impact and the powerful role the regulatory framework might play, they fall short of maximising their potential. Partnerships can be useful in making small improvements on the ground, but by taking a more macro view when framing and designing their activities they could also contribute significantly in making regulation more pro-poor. So what does that imply for partnership design?

*Partnerships should seek to understand how the regulatory regime affects the delivery of services to the poor, and take this into account when designing their activities: Specifically, they should seek to understand:*

- What regulatory constraints or barriers may affect planned partnership activities; and
- What regulatory constraints or barriers are currently affecting the main service provider's ability to service the poor.

This should allow the partnership to either ensure that their activities will not be subject to a regulatory barrier, or to frame their objectives and activities in a way that directly addresses existing regulatory constraints, or to try to go around such constraints.

*Partnerships should actively seek to open dialogue with regulatory bodies as early as possible:* This dialogue should not be seen as a one-off event and should rather evolve with the partnership activities and the development of an understanding of regulatory barriers affecting both the partnership and the delivery of services to the poor. This dialogue should aim to discuss what the partnership can specifically offer the regulatory institutions in terms of making regulation more pro-poor and what regulatory barriers will have an impact on partnership activities. It should also cover whether the regulatory institution is willing to work with the partnership to look at ways to lift or bend such barriers.

*The development of clear rules for the partnership (i.e. partnership self-regulation) can improve partnership effectiveness in general, and particularly in improving regulation:* To maximise their potential, internal partnership agreements should clearly define the activities of the partnership and its key objectives (which might be formulated as coverage and service delivery targets), the roles and responsibilities of each partner, decision procedures, internal reporting and arbitration mechanisms. Such clarity would help the partnership in building its credibility vis-à-vis the regulatory institutions and would increase its effectiveness.

## **What are key areas for future analysis of partnership design?**

Examining the experience of the eight BPD case studies has allowed the extraction of useful lessons, but also raises a number of questions to be resolved through further research into partnerships. These further questions mostly relate to the appropriate timing and process for forming partnerships within the context of regulatory and institutional reform and to the most appropriate make-up of those partnerships.

*In the context of private sector reform, when should partnerships be set up in order to maximise their potential for improving regulatory design?* The exact role that partnerships can play in improving the regulatory process varies depending on the stage that private sector participation has reached. At first glance, because of their role in gathering and relaying information, it appears that partnerships should be created early in the process of introducing private sector participation in order to improve and inform contract preparation. While the involvement of private operators prior to bidding is problematic, dialogue could be encouraged between the public sector and civil society (and potentially donors), and the foundations for later partnerships laid. However, the potential for doing so may be limited, given the levels of uncertainty (and sometimes tension) often created during the process of introducing private sector participation.

A few of the BPD focus projects, for instance the BoTT contractual form, provide food for thought when considering alternative ways of involving partnerships at various stages of the

privatisation process. It appears that further research into contractual forms and the timing of partnership would be helpful.

In 1997 the Department for Water Affairs and Forestry chose a cross-sector approach to roll out new infrastructure in four provinces and then transfer it to local government as part of national decentralisation. A public-private partnership scheme known as **BoTT** (Build, operate, Train and Transfer) was developed. Project implementation work, funded by the public sector, was undertaken by private sector partners. DWAF actively encouraged bid proposals from consortia that included business and NGOs and, following government suggestions, two of the winning private consortia brought in Mvula Trust, a national NGO with valued community-based experience in the sector. Following transfer of the new systems, local governments are then free to choose between operating services themselves or introducing private sector participation.

*What is the most appropriate make-up of a partnership?* While a whole variety of different arrangements can undoubtedly be considered as tri-sector partnerships, it still remains difficult to identify the optimum arrangement in terms of service delivery to the poor. This question is complicated by the fact that many influencing factors are likely to be location specific. It is, therefore, key that more research is carried out in two areas:

- Firstly, what should the role and nature of civil society actors be? In many cases the exact nature of civil society's involvement has been an issue. Questions regarding which civil society actors (NGOs or community-based organisations) should be involved, how they should be involved (via a contract for services or as partners) and under which type of regulatory regime remain open.
- Secondly, the role of regulatory institutions in promoting a partnership approach will need to be further developed. Indeed, there is very little experience so far of regulatory institutions pro-actively engaging with partnerships. It is therefore important to investigate how exactly the dialogue between regulatory institutions and partnerships should take place in order to achieve accountability on both sides.

*Overall, partnerships should be more ambitious and consider their role in making regulation of water and sanitation services more pro-poor:* Partnerships can play a very significant role in making regulation more pro-poor, that is if both partners and regulatory institutions understand what they can achieve and what needs to be done to maximise their potential. More often than not the fact that regulatory regimes do not provide an enabling environment for serving the poor is due to the heritage of the past. Responsibility for initiating and carrying out the necessary reforms does not only lie with regulatory institutions – it should be a process involving all stakeholders. This process, one of practical research and experimentation, is one where partnerships, as an institutional form, have a paramount role to play.

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**Business Partners for Development  
Water and Sanitation Cluster**

*The Interface between Regulatory Frameworks and  
Tri-Sector Partnerships*

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## **Acronyms**

BoTT	Build, operate, Train and Transfer
BPD	Business Partners for Development
CRA	Comisión de Regulación de Agua Potable y Saneamiento Básico
DWAF	Department of Water Affairs and Forestry
ETOSS	Ente Tripartito de Obras de Servicios de Saneamiento
NGO	Non-Governmental Organisation
ONAS	National Office for Urban Sanitation
PIA	Project Implementing Agency
SDE	Sénégalaise des Eaux
SSB	Superintendencia de Saneamiento Básico
SSIPs	Small Scale Independent Providers
WSP	Water and Sanitation Program



## 1 Introduction

### 1.1 OBJECTIVES OF THE RESEARCH

This research examines the linkages between regulation and the partnerships in place in the eight focus projects of the Business Partners for Development (BPD) Water and Sanitation Cluster.<sup>6</sup> Those partnerships bring together the private, public and civil society sectors in an effort to better tackle the challenge of providing water and sanitation services to the poor. The underlying premise is that, through working together, these sectors can provide water services to the poor more effectively than by working alone.<sup>7</sup>

A research investigation, focused on regulation, was initiated based on a number of prior observations:

- Institutional and regulatory contexts can have a very important impact on partnerships: abrupt changes in national rules may seriously compromise the viability of locally-managed projects;
- Regulatory frameworks can have a significant effect on how private operators function, what they can achieve, and the costs and rewards they face in doing so;
- Improving services to the poor requires an understanding of the specific issues that they face and the adoption of a flexible approach to regulation.

Therefore, even though regulation might not necessarily affect the daily life of the BPD partnerships, it can be a critical determinant of their goals and of their success assessed against such goals. Consequently, the research objectives were framed as follows:

- To analyse the regulatory frameworks that the BPD partnerships evolve in and how these frameworks have influenced the creation of partnerships;
- To examine the roles that BPD partnerships play in the regulatory process;
- To understand how the BPD partnerships have acted to alleviate or remove potential regulatory constraints;
- To formulate recommendations for the design of regulatory frameworks and partnerships that improve water and sanitation services for the poor.

Developing practical recommendations on ways of making the introduction of private sector participation in the water sector more pro-poor is currently a key priority for development practitioners. It is hoped that this report will contribute to this debate by looking specifically at whether partnerships can contribute to making regulation more pro-poor, i.e. by looking at whether they can provide ways of better understanding and serving the needs of the poor, preserving a regulator's neutrality and deterring political interference.

Going further, it might also be important to examine whether partnerships can improve the regulation of water services for all customers, rather than just the poor. Generally speaking, improving regulation for the poor is likely to increase the financial viability and stability of the contract. However, partnerships' role in improving the regulatory regime for all customers in more specific terms has been limited because this does not usually form part of their objectives. Therefore, this does not form the main body of this analysis and the interaction between the partnerships and the broader regulatory regime is considered only where relevant.

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<sup>6</sup> The Cluster works with eight focus projects around the world, most of which predated the Cluster. It supports partnership-oriented research on specific project themes (cost recovery, education and awareness, etc.); creates forums where sector specific (civil society, public and private sector) benefits and challenges are debated, and documents the evolution of the partnership in each specific focus project. Findings are disseminated through newsletters, the web site ([www.bpd-waterandsanitation.org](http://www.bpd-waterandsanitation.org)), policymaker / practitioner notes and other key research publications in order to share best practice widely.

<sup>7</sup> The BPD has found that tri-sector partnerships work best where they are adapted to local contexts, and has therefore offered guiding principles rather than developing a formal model for such partnerships. Partnerships should build on existing assets (using what is available on the ground, enhancing the capacities of existing resources and filling gaps) and roles and responsibilities develop from there. These can then be harnessed to formalised governance and decision-making structures (with corresponding benefits for the legitimacy, accountability, effectiveness and equity of the partnership).

## 1.2 METHODOLOGY

Based on the review of existing BPD documentation and available information on the projects from external sources, a detailed questionnaire was prepared and circulated to project partners. On this basis, a comparative analysis of all eight BPD partnerships was conducted, focusing on the regulatory frameworks and those aspects that are most relevant to poor customers.

In this study, the term ‘project’ usually refers to the broader contractual and regulatory framework in which the BPD partnerships evolve. ‘Partnerships’ refer to the more local, and generally pro-poor, arrangements that have materialised between partners. Whereas the BPD initiative usually tends to focus on the partnerships, the purpose of this research is to broaden the analysis to the project level in order to better understand the linkages between the activities of the partnership on the ground and the broader regulatory environment.

## 1.3 STRUCTURE OF THE REPORT

This report is structured as follows:

- *Section 2* defines regulation and formulates hypotheses on the roles that partnerships can play in making regulation more pro-poor;
- *Section 3* examines the regulatory frameworks in place in the eight BPD projects and highlights some of their key characteristics, particularly in terms of their interaction with the partnerships;
- *Section 4* analyses the various roles that partnerships can play in improving the regulatory process and making regulation more pro-poor;
- *Section 5* analyses how different regulatory functions are performed in the environments in which the eight BPD partnerships operate and examines how the latter have acted to focus regulation on the poor;
- Finally, *Section 6* draws key conclusions and recommendations for the design of partnerships and regulatory frameworks that would facilitate the introduction of pro-poor partnerships in the future.

In addition, there are two Annexes to this document:

- *Annex A* contains some background on regulation in the water sector and existing regulatory models in European countries;
- *Annex B* contains a summary description of the key institutional actors at play, both at the level of the BPD partnership and in the broader institutional framework for each of the eight BPD projects.

## 2 Regulation and Poverty

This section sets out a conceptual framework for the analysis, with a focus on establishing a commonly accepted definition of the term ‘regulation’. It then examines the regulatory functions that must be carried out in the water sector (examining the potential impact on the poor), the type of regulatory models that have emerged to do so and the type of instruments that may be used. This analysis forms the basis for formulating hypotheses on the role that partnerships may play in making regulation more pro-poor.<sup>8</sup>

### 2.1 DEFINING REGULATION

In its broadest sense, regulation can be seen as a “sustained and focused control exercised by a public agency over activities that are valued by a community”.<sup>9</sup> It can be inferred from this quote that regulation should be defined as a set of functions that can be exercised by a variety

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<sup>8</sup> Initial responses to the questionnaire from BPD partners highlighted a relatively high degree of misunderstanding as to what regulation is and how it might affect the activities of the partnerships on the ground. This is partly due to the fact that the term ‘regulation’ is often abusively associated with the ‘independent regulation’ model, as practised in the UK.

<sup>9</sup> Anthony L.Ogus (1994) ‘Regulation: Legal Form and Economic Theory’, Oxford University Press.

of public institutions and instruments rather than as a rigid set of rules.<sup>10</sup> There is indeed a fundamental difference between regulation and rules: whereas policy-makers set general rules by passing an Act or a decree, regulators must interpret those rules in a way that is true to their long-term rationale and is suited to practical circumstances.

The objectives of regulation can be broken down in three elements:

- To protect customers from private sector abuses and political interference;
- To protect the private sector from politically-driven decisions;
- To enable the public sector to carry out long-term policy objectives.

Regulation is more or less needed depending on the economic characteristics of the activity under consideration; it is most needed when private markets are not operating as efficiently as they should be and when they are not delivering the optimal solution for consumers and society as a whole. The water sector presents a number of characteristics that call for regulation.<sup>11</sup>

- First, water services tend to have strong monopolistic elements, which means that the potential for introducing competition to reduce prices and improve services to consumers is limited;
- Second, as essential services, they often get a lot of attention from politicians eager to preserve their political situation. Political interference is therefore common, either to keep prices as low as possible irrespective of the sector's financial needs or to interfere with personnel management.<sup>12</sup>

## 2.2 REGULATORY FUNCTIONS

Regulatory functions in the water and sanitation sectors can be broadly divided into three categories: economic, environmental and public health. Below, the content of such functions is reviewed in broad terms, as well as how performance of these functions may affect the interests of the poor.

### 2.2.1 Economic regulation

Economic regulation is itself comprised of three functions: price regulation, service quality regulation and competition regulation.

#### *Price regulation*

Price regulation consists of setting overall tariff levels and tariff structures so as to ensure delivery of services at an affordable cost while ensuring the long-term financial viability of the sector.

Price regulation can explicitly take into account the needs of the poor by setting tariff levels on the basis of how much the poor are willing and able to pay and for which level of service, introducing pro-poor tariff structures and allowing more flexible payment methods. One key

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<sup>10</sup> One of the challenges of looking at regulation in the BPD projects is that the term 'regulation' is not understood in the same way in different legal traditions. Vocabulary in itself can create barriers to mutual understanding. In French, it is only relatively recently that the word 'régulation' can be used to refer to the regulation of public services, although this is not a universally accepted translation. An alternative translation, 'réglementation', may be more correct from a linguistic point of view, but it narrowly focuses on a set of rules ('règles') as defined through Acts and decrees.

<sup>11</sup> Annex A explains in further detail why regulation is particularly needed in the water sector.

<sup>12</sup> It is important to stress the distinction between the policy-setting role of the public sector, which sets the rules and defines the objectives for the regulator (such as overall tariff structure and inclusion of social goals), and the regulator itself, which assures adhesion to these goals (and thus seeks to act as an independent referee). Political interference becomes a problem when politicians try to change the rules of the game after they have been set, or try to influence the regulator to take decisions that favour political interests over society's interests. Where pro-poor or social goals are an objective these are best included before contracts are bid upon and, in addition to having general pro-poor obligations required of the service provider, they can usefully be included in the responsibilities of the regulator, in, for example, the constitution of the regulator. This should also help to minimise later political interference.

aspect of pro-poor price regulation is to introduce incentives for the private sector operator to provide services in poor areas, which might be costly to serve or less accessible.<sup>13</sup>

### ***Service quality regulation***

Service quality regulation entails defining levels of service on product characteristics such as technical requirements or customer responsiveness.

Pro-poor regulation may allow service providers to offer variable service levels in different service areas to adapt to local conditions, by contrast to blanket quality standards that raise the costs of water and sanitation services to the poor. In addition, the setting of coverage targets can be essential for increasing access by the previously unconnected poor, which often represent the great majority of poor water service consumers.

### ***Competition regulation***

Competition needs to be regulated under various forms: to monitor competition for the market (in the case of a monopoly provider) and also to ensure competition in the market where applicable, and thus encourage private sector investment on a fair and competitive basis.

Competition regulation usually focuses on ensuring that the main service provider is protected by exclusivity rules in a given service area. By contrast, pro-poor regulation may wish to encourage a reasonable amount of competition from alternative service providers (such as water vendors) given that they provide important service options to the poor. Regulation should seek to preserve a level-playing field between all types of operators in order to preserve choice between service options for poor customers.

## **2.2.2 Environmental regulation**

Environmental regulation in the water sector broadly consists of regulating water abstractions and discharges so as to manage resources in a sustainable manner. Abstraction and discharge rights are often ill defined in developing countries, where water extracted from the ground or from rivers tends to be taken for granted and environmental costs are seen as nobody's problem. Adequate sanitation is rarely provided, with at best sewage collection but rarely sewage treatment. As a result, sewage tends to be put back in the rivers or in the sea with only rudimentary treatment.

The poor are usually the first ones to suffer from a deterioration in the resource situation, since they tend to be the last ones to be served and the impact on their living environment can be much more significant. By contrast, environmental standards may be set too high compared to what the poorest can afford. Setting high standards may also be a way of granting monopoly rights to the private operator, thereby reducing service options for the poor.

## **2.2.3 Public health regulation**

Public health regulation is usually performed independently of the water sector, except for the specific function of drinking water quality regulation, which is a key determinant of the quality and, therefore, of the price of water services.

As with environmental standards, high water quality standards can result in prices set beyond the means of poor customers, whereas insufficient monitoring of drinking water quality affects the poor most, as their financial means to pay for coping strategies (e.g. boiling water, filters) are much less.

## **2.3 REGULATORY MODELS**

The way in which regulatory functions are allocated to different institutions may have a substantial impact on the efficiency of regulation, as well as the way they inter-relate with other important functions, such as policy setting and operations.

Regulation can be performed through a variety of models with varying degrees of separation between these functions:<sup>14</sup>

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<sup>13</sup> However, regulatory institutions' ability to affect tariff levels would often depend on political decisions, with the poor being willing to pay but the politicians often unwilling to charge.

- *Independent regulation*, as practised in the United Kingdom: an autonomous agency is set up to regulate on the basis of laws and licences, with a relative independence from the institution in charge of policy setting;
- *Regulation by contract*, as practised in France: a public institution regulates the provider via a well-specified long-term contract – this institution may be the same one as the policy-maker;
- *Self-regulation*: the (publicly-owned) utility regulates its activities, with some limited degree of guidance and oversight from the institution in charge of policy setting (either the national Ministry or a municipality).<sup>15</sup>

***Characteristics of efficient regulatory frameworks include independence, transparency and accountability. Although independence is a desirable characteristic, it might not always be achievable.***

For regulation to fulfil its objectives most efficiently in a pro-poor manner, the institution performing regulatory functions should be shielded as much as possible from political interference. This can be achieved through introducing a clear separation between policy-making, regulating and operating functions and also giving a clear remit to the regulator to preserve the long-term interests of the poor versus short-term political prerogatives.

In developing countries, due to the lack of appropriate monitoring structures and the general weakness of the judicial system, it is often recommended that an autonomous regulatory body be set up in order to perform regulatory functions in a way that is shielded from political interference. This is also because such regulatory bodies tend to be more flexible to adapt to unforeseen circumstances and changes in operating conditions than an overly rigid contractual framework.

However, achieving such clear separation of functions is often problematic, as governments are often reluctant to transfer to an autonomous agency what they see as essential functions. In some cases, an autonomous agency is nominally set up, but in practice, its independence is curtailed by repeated political interventions. Therefore, the strength and suitability of the regulatory regime cannot be assessed simply by looking at whether an independent regulatory body is in place: instead, it is important to understand in detail how regulatory functions are performed, by which institutions and for which objectives.

A regulator can be independent from political powers, but this would not have much positive impact on customers if it was not aware of their needs and was not accountable to them for its decisions. This is particularly important for poorer customers, who can have specific needs and often lack a political voice.

## **2.4 REGULATORY INSTRUMENTS**

For each of the regulatory functions set out in *Section 2.2*, a wide variety of regulatory instruments can be employed for delivering expected results.

Attention is usually focused on the ‘command-and-control’ or administrative types of regulatory instruments since they are the most straightforward to use for the institutions in charge of regulation. However, more ‘market-based’ instruments can also be used to achieve similar results (see *Table 2.1* below).

***A flexible approach in the use of regulatory instruments is usually preferable to meet the needs of the poor.***

The poor get water from a larger variety of providers, ranging from the network utility (i.e. if they are connected) to small-scale independent providers supplying water from trucks, independent water sources or bulk supply agreements with the main utility provider. Regulating such alternative providers through ‘traditional’ instruments (the setting of prices and quality standards) might be overly difficult and costly. Instead, it may be preferable to place an emphasis on gathering and publishing information on their performance, so as to let

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<sup>14</sup> Prior to introducing private sector participation, all such functions are often closely inter-linked. When private sector participation is introduced, however, the potential for monopoly abuse is perceived to be higher, which is why regulatory regimes are usually redefined at the time of privatisation.

<sup>15</sup> Annex A provides some background on how these types of regulatory models have developed in European countries.

reputation play its regulating effects without costly intervention. In any event, the choice of regulatory instruments should be based on a comparative assessment of the trade-offs between effectiveness, ease of implementation and costs and benefits.

TABLE 2.1 REGULATORY INSTRUMENTS

REGULATION	OBJECTIVES	TYPES OF REGULATORY INSTRUMENTS
<i>Economic</i>	<i>Prices at ‘fair’ value, close to competitive level</i>	<ul style="list-style-type: none"> <li>• <i>Administrative: set a maximum or an average tariff, prescribe a tariff structure</i></li> <li>• <i>Market-based: introduce competition (or threat of competition) wherever possible: rely on competitive pressures to bring prices down</i></li> </ul>
	<i>Quality at an affordable and practicable level</i>	<ul style="list-style-type: none"> <li>• <i>Administrative: set quality standards through general legislation or in the contract</i></li> <li>• <i>Market-based: licensing, reputation, publication of league tables</i></li> </ul>
	<i>Fair competition wherever possible</i>	<ul style="list-style-type: none"> <li>• <i>Administrative: comparative competition</i></li> <li>• <i>Market-based: competition for the market or introduction of competition in segments with no natural monopoly characteristics</i></li> </ul>
<i>Environmental</i>	<i>Water resources are managed sustainably</i>	<ul style="list-style-type: none"> <li>• <i>Administrative: definition of water rights and allocation regimes</i></li> <li>• <i>Market-based: water abstraction and pollution charges, tradable water rights</i></li> </ul>
<i>Public health</i>	<i>Water is safe to drink</i>	<ul style="list-style-type: none"> <li>• <i>Administrative: drinking water standards</i></li> <li>• <i>Market-based: reputation (cannot be relied on)</i></li> </ul>

## 2.5 LINKS BETWEEN REGULATION AND PARTNERSHIPS

Establishing the regulatory functions, models and instruments in such broad terms inevitably leads to a central question for this study, which is what role can partnerships play in improving regulation and making it more pro-poor? As a starting point, it appears that partnerships may contribute to fulfilling the characteristics of pro-poor regulation, as discussed above, in the following ways:

- *Independence, transparency and accountability are important for poor customers, who may have specific needs and often lack a political voice:* when these characteristics are not in place, and in particular when independence of the regulatory body is limited, partnerships may provide a forum for protecting the interests of private sector and civil society. They may also strengthen the protection of private sector and civil society’s interests through direct representation in a transparent context. Overall, they may make regulation more accountable to the needs of the poor;
- *Flexibility:* as pro-poor regulation often hinges on flexibility and adaptation to local circumstances, locally-developed, context specific partnerships may provide a good base from which to derive and develop pro-poor regulation and furthermore, go on to act as flexible regulatory instruments.

The rest of this report examines in more detail, based on the experience of the eight BPD partnerships, the role that partnerships can play in making regulation more pro-poor and the impact that regulatory frameworks can have on their activities.



### 3 Regulatory Frameworks around the BPD Partnerships

This section characterises the regulatory frameworks in which the eight BPD partnerships operate. In order to facilitate comparisons, they have been broadly allocated to the types of regulatory models defined in *Section 2.3* (independent regulation, regulation by contract, self-regulation). Another category has also been added, the ‘partnership model’, to reflect the fact that the BPD partnerships in South Africa have experimented with new models that do not compare with anything that has been attempted elsewhere.

Key characteristics from the regulatory frameworks and how they interact with partnerships are compared in this section, whereas **further information on each of the partnerships is presented in Annex B.**

#### 3.1 REGULATORY MODELS

Regulatory frameworks for the BPD partnerships can be broadly allocated to the following types of regulatory models:<sup>16</sup>

- *Independent regulation*: the three BPD projects in Latin America (*La Paz-El Alto*, *Buenos Aires* and *Cartagena*) operate in fairly similar regulatory environments, characterised by the presence of semi-autonomous regulatory bodies in charge of supervising the activities of large private sector water operators with various degrees of autonomy;
- *Regulation by contract*: in both *Jakarta* and *Dakar*, regulation is carried out by a public body on the basis of detailed contracts with a main private operator. In both cases, the contract specifies who is in charge of monitoring those provisions;<sup>17</sup>
- *Self-regulation (public sector provision)*: the BPD project in *Port-au-Prince* is the only one that does not involve a large private sector operator, although standpipe operators represent the private sector. The public sector provider (CAMEP) is largely self-regulated;
- *Partnership models*: in the *BoTT* contracts and *KwaZulu-Natal*, innovative partnership models have developed which are difficult to classify in existing categories.<sup>18 & 19</sup>

#### 3.2 OVERALL COMPARISON

##### 3.2.1 Regulatory institutions and instruments

The regulatory frameworks surrounding the eight BPD projects are characterised in more detail in *Table 3.1* below, according to the institution in charge of economic regulation and the type of contractual arrangements in place, for both the project and the partnership. The table also characterises the partnership form, pointing to any departure from the model of tri-sector partnership.

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<sup>16</sup> These categories should by no means be considered as rigid or exclusive, since we are in fact dealing with hybrid models, borrowing from several regulatory models at a time.

<sup>17</sup> Even though at the time of the project, there was no autonomous regulator in Jakarta, this will change following the passing of a decree in September 2001.

<sup>18</sup> Strictly speaking, the BoTT could be an example of regulation by contract, and the KwaZulu-Natal projects examples of self-regulation. However, the contracting of NGOs in both projects raises specific regulatory issues and challenges.

<sup>19</sup> Following the end of the apartheid regime, South Africa embarked on an ambitious policy to provide water and sanitation services to 12 and 21 million people respectively. In 1994, the government published a White Paper on Community Water Supply and Sanitation (CWSS) that marked the start of a wave of legal and administrative reforms to make this an achievable aim and placed strong emphasis on community participation and poverty reduction. In difficult and risky circumstances, traditional forms of public-private partnerships were not seen as very appropriate, especially given some resistance from populations and trade unions to the introduction of private sector participation. This led to the creation of interesting new models for linking business, government and civil society in the water sector.

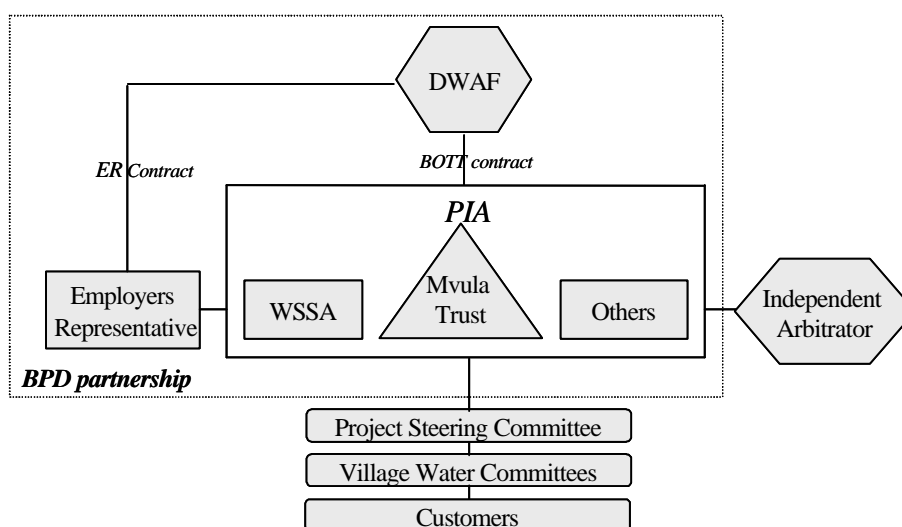
TABLE 3.1 REGULATORY INSTITUTIONS AND INSTRUMENTS IN BPD PROJECTS AND PARTNERSHIPS

PROJECTS	INSTITUTION FOR ECONOMIC REGULATION	PROJECT CONTRACTUAL ARRANGEMENT	PARTNERSHIP AGREEMENT	PARTNERSHIP FORM
<i>Independent Regulation Model</i>				
La Paz-El Alto	<i>National regulator: SBB</i>	<i>Concession</i>	<i>Not explicit, but Project Steering Committee</i>	<i>Civil society's role limited</i>
Buenos Aires	<i>Tri-partite regulator: ETOSS</i>	<i>Concession</i>	<i>Not explicit</i>	<i>Civil society only involved short term</i>
Cartagena	<i>National regulator: CRA</i>	<i>Joint ownership Management contract Loan contract</i>	<i>Not explicit</i>	<i>NGO short-lived but CBO throughout</i>
<i>Regulation by Contract</i>				
Jakarta	<i>Asset-holding company (Pam Jaya) / Regulator</i>	<i>Concession</i>	<i>Not explicit</i>	<i>Civil society's role limited</i>
Dakar	<i>Asset-holding company (SONES) and Water Ministry</i>	<i>Affermage</i>	<i>Loose voluntary agreements</i>	<i>Tri-sector partnership</i>
<i>Self-regulation</i>				
Port-au-Prince	<i>Municipality Self-regulation (CAMEP)</i>	<i>No contract (public ownership)</i>	<i>Memorandum of understanding</i>	<i>No large private sector</i>
<i>Partnership Models</i>				
BoTT	<i>Ministry (DWAF)</i>	<i>BoTT contract</i>	<i>BoTT contract</i>	<i>Tri-sector partnership</i>
KwaZulu-Natal	<i>Municipality</i>	<i>No contract (public ownership)</i>	<i>Co-operation agreements</i>	<i>Tri-sector partnership</i>

It appears that partnerships for water and sanitation service provision have developed in a great variety of regulatory models: not one model seems to be more conducive to establishing a partnership than another.

However, there are substantial differences between the regulatory environments that have influenced the activities of the partnerships and the nature of the partnerships that have been established.

**Various types of institutions are in charge of economic regulation but overall, their independence from political interference is somewhat limited.**



Organisational relationships in the BoTT project

One of the challenges of looking at the regulatory frameworks surrounding the BPD partnerships is that regulatory functions are not always well separated from other types of functions. For example, the Ministry may be in charge of both setting policies and carrying out regulation, as it is in the case of DWAF in South Africa for the **BOTT** project. Or, as in **Port-au-Prince**, the public service provider may be simultaneously in charge of operations and self-regulation.

This being said, the existence of an autonomous body is no guarantee of political independence: in the three cases where an autonomous body is in place (i.e. in the Latin American partnerships), partners pointed out that the independence of such bodies had been repeatedly curtailed on a number of occasions, especially for important decisions such as setting prices or renegotiating the contract.

***When a public-private contract is in place at project level, partnerships have left their commitments rather undefined. By contrast, in the absence of a public-private contract, partnerships have better specified their activities.***

In about half of the BPD partnerships, the basis is a public-private partnership (which is usually formalised through a contract). In those partnerships, the main contractual arrangement drives the relations between the public and the private sector and efforts to formalise relations between partners from all sectors (including civil society) have remained somewhat limited. This is particularly the case in the projects in Latin America (**La Paz-El Alto, Buenos Aires, Cartagena**), in **Jakarta** and partly in **Dakar** where the partnership arrangements are voluntary, predominantly grounded in personal relationships and relatively undefined. This has not prevented the partnerships from undertaking specific activities (i.e. distinct from the project as a whole) but the civil society organisations remain partly sidelined, as an add-on to the broader contract.

In the rest of the cases, the role of the NGO or the community-based organisation is more central to the arrangements. For example, in **Port-au-Prince**, there is no private sector as such and the NGO has taken a leading role in organising water service provision in poor areas that were previously not served by the main utility. In **KwaZulu-Natal**, the three sectors are bound together through a purely voluntary agreement with a life of its own. In the **BoTT** projects, the public sector mandated the formation of a consortium between private sector organisations and an NGO as a prerequisite to bid for the contract. However, in both of these cases, contracting and regulating the activities of the NGO has raised some difficulties. The NGO partner (Mvula Trust) considered that it has not been given the opportunity to act as a partner in its own right but merely as a contractor, unable to influence the strategic direction of the project. However, the resolution of these issues has been largely left to the partners themselves, with limited reliance on external regulation mechanisms for mediation.

The form of partnership may also be partly determined by the timing of its creation: when the partnership is created at the initiative of the private operator following privatisation, civil society is often less firmly integrated into the partnership. By contrast, when private sector participation has not yet been introduced, civil society is more likely to have a stronger voice, as in **Haiti** or in **KwaZulu-Natal**.

### 3.2.2 Interaction between regulatory frameworks and partnerships

Table 3.2 summarises the observations on the process of interaction between regulatory frameworks and partnerships formulated in Annex B: whether or not regulation has been a key determinant of the partnership's creation and activities, whether the regulatory body took part in the partnership and whether replication is sought, and how.

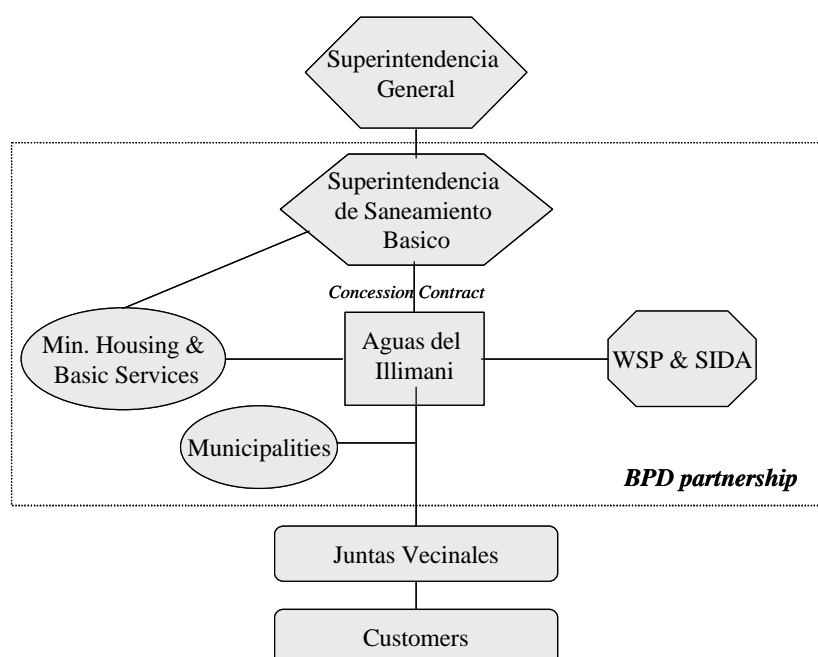
TABLE 3.2 INTERACTION BETWEEN REGULATORY FRAMEWORKS AND PARTNERSHIPS

PROJECTS	IMPACT OF REGULATION ON PARTNERSHIP'S APPROACH	REGULATORY BODY'S PARTICIPATION	POTENTIAL FOR REPLICATION
<i>La Paz-El Alto</i>	Rigid quality standards: <i>Pilot approach to develop alternative standards</i>	<i>SSB takes part as observer</i>	<i>Explicitly sought through modification of national rules</i>

PROJECTS	IMPACT OF REGULATION ON PARTNERSHIP'S APPROACH	REGULATORY BODY'S PARTICIPATION	POTENTIAL FOR REPLICATION
<i>Buenos Aires</i>	<i>Ambitious coverage targets: Bulk supply agreements and schemes for reducing connection charge without need for regulatory approval</i>	<i>ETOSS not involved but tolerant</i>	<i>Has taken place without modification of rules</i>
<i>Cartagena</i>	<i>Rigid billing rules: After regulatory approval was denied, went around the rules</i>	<i>CRA not involved and created obstacles</i>	<i>Sought without modification of rules – concerns over long-term feasibility</i>
<i>Jakarta</i>	<i>Relatively loose regulation: No need for regulatory approval, varying tariffs (e.g. waiving connection charges) is allowed elsewhere</i>	<i>Pam Jaya or Ministry not involved</i>	<i>Sought without modification of rules – however, concerns on the overall financial viability</i>
<i>Dakar</i>	<i>Relatively loose regulation: Standpipes are allowed in other areas, but the partnership contributed to improving their performance</i>	<i>SONES involved, more as investor</i>	<i>Has already taken place without modification of rules</i>
<i>Port-au-Prince</i>	<i>Relatively loose regulation: Standpipes are allowed in other parts of the city</i>	<i>CAMEP directly involved</i>	<i>Has taken place without modification of rules but active CAMEP involvement</i>
<i>BoTT</i>	<i>Rigid approach to contracting: The partnership worked on getting some of these constraints lifted but only on a project by project basis</i>	<i>DWAF involved in setting up partnership but not in subsequent regulation</i>	<i>Will need modification to be replicated: existing contract is too prescriptive</i>
<i>KwaZulu-Natal</i>	<i>Favourable regulatory environment: Most regulatory constraints had already been lifted – partnership used only for experimentation</i>	<i>Municipalities actively involved in creating partnership and shaping activities</i>	<i>Replication currently sought but raises some issues, such as NGO contracting</i>

**Regulatory environments tend to be both rigid and prescriptive or relatively loose – both circumstances can lead to the creation of partnerships. The attitude of the regulator towards the partnership can vary substantially, from one of indifference to one of active engagement.**

Regulatory frameworks are more or less forthcoming for the type of approaches promoted by partnerships and have had a varied influence on the formation of partnerships and their activities. In the Latin American cases, regulatory frameworks are fairly rigid and regulatory constraints have motivated partnership formation in all three cases. The attitude of the regulatory agencies, however, has been somewhat varied. In *La Paz-El Alto*, the regulatory body got involved as an observer and it was indeed one of the few cases where the regulator was



**Organisational relationships in the La Paz-El Alto project**

prepared to actively engage with the partnership. Whilst ETOSS’s attitude in *Buenos Aires* may be characterised as ‘benign neglect’, that of the CRA in *Cartagena* has been more confrontational, as they specifically refused to provide regulatory approval for an alternative billing regime. In some ways, regulatory rigidity has also been an issue in the *BoTT* contract. There, however, the creation of the partnerships was actually prescribed by regulation (and by policy-makers) rather than as a consequence of rigid regulation.

In the other cases, regulatory frameworks are relatively loose and the creation of the partnerships cannot be directly attributed to the need to address a regulatory constraint. Indeed, the partnerships did not require regulatory approval for conducting their activities. In some way, however, the lack of regulation may have been what led to the creation of the partnerships in such cases. For example, in *Port-au-Prince*, the NGO developed a partnership approach with small-scale private providers and established itself as an intermediary between those providers, communities and the public sector to balance all these interests, a role normally played by regulatory bodies (see *Box 4.1*).

**Regulatory institutions’ attitude can be influenced by various factors, linked to the incentives that they have to engage with the partnership, such as:**

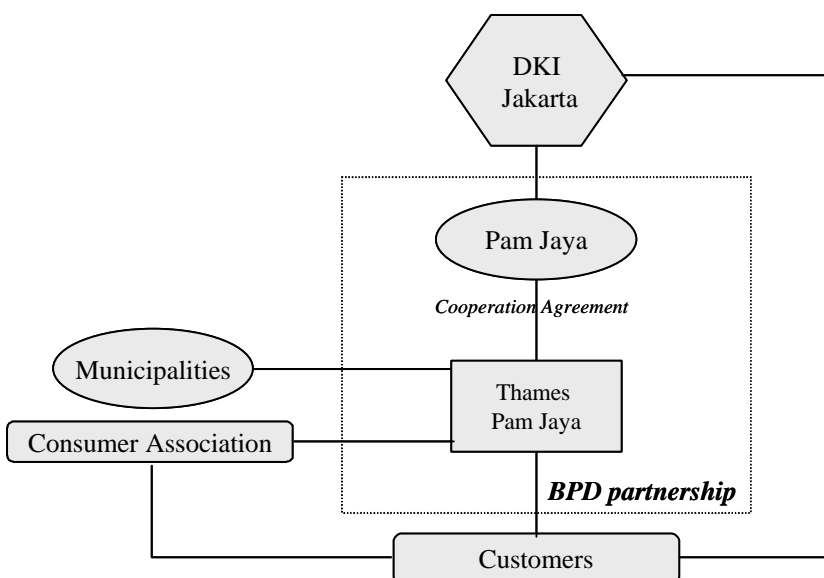
**The regulatory body’s mandate, as defined by policy-makers:** regulatory institutions have usually no clear incentive to deal with poor customers, except if they have received a specific mandate for doing so. Indeed, regulating services to poor customers can be difficult, cumbersome and almost an impossible task, when the regulation of services to the major customers can already prove challenging. In most cases, such mandate is not very explicit but is clear in the case of DWAF in South Africa (which happens to be both policy-maker and regulator, although it has delegated day-to-day contract management to a private body).

**The geographical location of the regulatory body in relation to the partnership:** when the body exercising regulatory functions is at the same geographical level as the partnership (for example, a largely self-regulating municipality and a local partnership, such as in *KwaZulu-Natal*), their interest in improving regulation may be better aligned. In addition, decisions on alleviating regulatory constraints can be taken more quickly and efficiently, with an overall benefit to the poor. This was reflected in a recent decision by ETOSS in *Buenos Aires* to grant more responsibilities to municipalities for defining the exact nature and the phasing of coverage obligations, which were not clearly defined in the concession contract.

**The strength of the regulatory body versus the private company that it regulates:** in some cases, the regulatory body did not get involved as it was substantially weaker than the private company it was supposed to regulate. For example, in *Jakarta* or in *Buenos Aires*, the companies largely drove the partnership process (with limited involvement from civil society) and did not need to seek regulatory approval for their actions.

**Whether or not the regulatory body is involved has partly influenced the strategy adopted for replication of the partnership’s approach.**

Many of the BPD partnerships have been looking at replication simply in terms of ‘organic growth’, i.e. adopting the same approach in a growing number of areas or boroughs without thinking very hard about the long-term sustainability of their approach when adopted on a larger scale. For example, in *Jakarta* it is doubtful that all new connections could be provided for free (as it was in the partnership area) if no tariff rebalancing is provided for elsewhere. However, since the partnership did not engage with the regulatory body, such tariff



**Organisational relationships in the Jakarta project**

modification has not been discussed.

Very few of the partnerships have placed an emphasis on setting up the regulatory mechanisms that would allow such expansion. The partnership in *La Paz-El Alto* is effectively the only one that has been looking at the institutionalisation of its approach (using condominium network provision) via the introduction of national standards from the start of its activities. This was probably due to the fact that the national regulatory body was involved, and that issues emerging in the capital city were of special interest to it. But this approach appears as something to be encouraged, since it also bridges the gap between pro-poor regulation and regulation of services for all customers. Indeed, in *La Paz-El Alto*, the take up of condominium sewerage connections could be considerably higher if they were not seen as a low-cost solution for the poor, hence affecting property prices (see *Box 5.3*). Modifying rules to introduce such standards would be the best solution for mainstreaming a pro-poor solution and making it accessible to all.

From this analysis, it transpires that regulatory frameworks can have a substantial impact on why partnerships form and which form they take. Following this general analysis, *Section 4* goes into more detail in analysing the various roles that partnerships can play in improving the process of regulation and making regulation more pro-poor.

## 4 BPD Partnerships and Pro-poor Regulation

This section presents an analysis of the roles that partnerships can play with regard to making regulation more pro-poor, summarised as follows:

- Attract attention to linkages between water services and poverty;
- Gather information and make it available for regulation;
- Help partners understand each others' regulatory interests and constraints;
- Balance each sector's interests through partnership's 'self-regulation';
- Create publicity that affects reputation;
- Serve as a secondary recourse mechanism or act as a watchdog;
- Create a more flexible environment to develop rules better suited to the needs of the poor.

The factors that influence partnerships' success in doing so are also looked at.

### 4.1 ROLES OF PARTNERSHIPS IN MAKING REGULATION PRO-POOR

*Partnerships have usually been created with the specific remit of helping the poor: their existence may therefore help focus the attention of the institution in charge of regulation on poverty issues.*

There is a growing recognition that poor customers are not like usual customers, and that in order to serve them better, they should have a sense of ownership of the water or sanitation project that serves them. Of course, this distinction should not be over-emphasised: over time, the objective is to help people move out of poverty and have access to services comparable to the rest of the population. However, this process takes time and partnerships do have a role to play during that interim period, as getting an NGO or a community-based organisation on board can help in building a sense of ownership amongst poor communities.

In addition, having a partnership in place helps sensitise all institutional actors involved in the sector to poverty issues. For example, in *Port-au-Prince*, prior to the partnership involvement, CAMEP was only providing piped water services to 10 per cent of households and did not physically enter the poor neighbourhoods, which they regarded as violent and dangerous. Therefore, one of GRET's initial roles was to attract attention to the issue of the unconnected poor and to alleviate CAMEP's fears about operating in these neighbourhoods.

*Partnerships can help gather information on the needs of the poor and make it available for regulation.*

Information is a key input to regulation. Most regulators tend to ignore the poor because they do not have readily available information about them, or enough human and financial capital

to go and collect it. Baseline surveys often do not exist and the assumption is that those not accounted for in the statistics are not important.

Partnerships can play an important role in gathering and relaying information to decision-makers. For example, in *La Paz-El Alto*, the partnership decided to conduct a series of anthropological surveys of the Aymara population in order to understand why actual demand was much lower than forecast prior to signing the concession contract. Indeed, even with in-house connections, the Aymara people's water consumption is as low as 15 to 20 litres per person per day, raising technical issues for the management of sewerage networks for example. The surveys conducted by the partnership conveyed some very important information about cultural beliefs and practices and consumption patterns that explained such low consumption.

Had such information been gathered prior to designing the contract, it might have been recommended to adopt less ambitious quality standards than the provision of in-house connections to all inhabitants. In particular, more communal standards of service provision might have been better suited to the needs of poor people in *El Alto*. However, this information has not directly fed through into a modification of tariff levels or structures in order to adapt to new demand assessments. Instead, the partnership chose to explore alternative quality service levels (see *Box 5.3*).

In other cases, the partnership has been in a better position to use information as an input for designing its activities. One of the key innovations of the *BoTT* has been the integrated project-cycle approach required from the PIA (Project Implementation Agency) for delivery of projects, especially in rural areas such as in the Eastern Cape. The *BoTT* contract is basically a framework contract that gives responsibility for implementation of new projects within a given area (the Province) to a consortium of firms that it also helps establish in the process. For each particular project that DWAF, the public signatory to the contract, is considering financing, the PIA must submit a business plan evaluating the needs of the local population and proposing both technical and institutional solutions for providing services to that particular community. Such a mechanism has proved very useful in gathering information and examining supply options for communities previously 'off the map'. However, this process could be improved. Substantial delays have slowed down the business plan approval process, with repercussions on the project start date. Also, the NGO partner has had a limited involvement in the preparation of the business plans, which means that too little attention is paid to institutional and social development aspects when alternative supply options are considered. Also once a business plan has been approved, it is difficult to modify the choice of options. Many of these difficulties have stemmed from a lack of appreciation of the constraints faced by all members of the partnership.

***Partnerships can help partners understand each other's interests and constraints with respect to pro-poor regulation.***

Each member of the partnership has its own agenda and interests with respect to regulation, but also has its own constraints:

- Private operators often consider a stable and effective regulatory regime as a key determinant for their involvement in a particular country or town. Their degree of confidence in a given regulatory regime is usually reflected in their assessment of investment risk, factored in as a 'risk premium'. They are also bound by contracts that limit what they can and cannot do.
- Consumers favour a stable and transparent regulatory regime as a protection from monopolistic providers and especially private ones, which they tend to see as powerful and eager to put profit before public interest. The constraint there is that they might have difficulties in organising themselves and expressing a coherent message. NGOs may not always be representative of customer interests, as they have their own agenda and interests.
- The public sector is the main driver behind regulation and needs to align its interests with long-term development goals, in order to limit political interference. However, political interests might sometimes constrain the activities of public sector bodies involved in regulation, especially when policy-setting and regulation functions are not clearly separated. The public sector is also constrained by fixed rules and procedures.

Because of their diverging interests, each of the parties to the partnership may try to influence regulation in a slightly different way and this might lead to conflicts if they are perceived to be acting against another party's interest. Working in partnership, however, allows partners to understand each other's interests and constraints better and work towards a consensus solution.

For example, a private sector operator may face regulatory constraints that are beyond its control but an NGO would need to understand this in order to focus its efforts where it is most appropriate (on lobbying to change the regulatory framework rather than on criticising the private sector). In *Buenos Aires*, for example, the partnership has not functioned as well as it could have done because the private sector operator and NGOs did not understand each other's objectives very well. It seemed that the NGO did not understand that some of the issues were actually due to regulatory constraints placed by the regulator rather than the private sector being uncooperative.

***Partnerships can act as a 'self-regulation' mechanism to balance each partner's interests.***

Internal reporting requirements and regular meetings within the partnership can create a form of 'self-regulation'.

For example, in the *BoTT* project, the NGO is involved on the Board of the Project Implementation Agency (PIA), albeit only in an observer role given that they refused to become a shareholder in order not to damage their reputation in the communities they are involved in. Despite this limitation, reporting to the Board is a useful mechanism for keeping all partners in check and solving any outstanding issues.

In *KwaZulu-Natal*, the Project Steering Committee decides on all actions to be undertaken by the partnership on a consensus basis. If one of the partners does not agree, the proposed action is either dropped or must be substantially reformulated by its proponent. This mechanism helps ensure that the interests of the partnership (and the mutual interests of the partners) prevail over those of one particular partner, irrespective of how much financial or political clout it may have. An external arbitration mechanism is also included in the Co-operation Agreements but it has never been used.

***Partnerships can be useful tools to create publicity and reputation based on experience of dealing with the interests of the poor.***

Publicity and reputation are important regulatory instruments, although relatively diffuse and uncertain ones. Working in partnership may improve the reputation of each individual partner in the sense that they are seen as working for the partnership's interests instead of simply their own interests. These reputation concerns should act as a form of self-regulation on the operator, and help to ensure that the poor are given due attention. For example, the private operator in *KwaZulu-Natal* has no direct financial interest in taking part in the BPD partnership. However, it initiated the idea of such a partnership (on the back of the BPD initiative) for a number of reasons independent of immediate profit motives. Although these reasons are not explicitly stated, it can be assumed that the partnership is useful to the private operator for developing its knowledge of pro-poor service delivery issues (a way of accessing information). It is also useful for establishing a pro-poor reputation in the international arena and amongst existing customers, in an era where corporate responsibility issues are scrutinised, but more importantly as experience in serving the poor is expected to become a part of bid documents.

***Partnerships may serve as a secondary recourse mechanism for customers' complaints particularly relaying poor customers' interests.***

On all issues related to regulation, poor customers need to have access to fair recourse mechanisms in case of complaint. The service provider should usually be in charge of dealing with complaints in the first instance, but means of secondary recourse must also be available when disputes cannot be settled.

Regulatory bodies can play a very important role as secondary recourse mechanisms. Whether or not they are responsive to the needs of the poor depends partly on their organisational structure: for example, a special unit in charge of dealing with the interests of the poor may facilitate the process. In all of the cases where an independent regulator exists, i.e. *Buenos Aires*, *La Paz-El Alto* and *Cartagena*, dealing with customer complaints is part of



the regulator's remit but none of these have departments focused on poor customers specifically.

Partnerships may therefore be useful as an alternative secondary recourse mechanism, particularly where regulatory institutions are relatively weak or inaccessible to the poor. Specifically, within the partnership, the civil society partner may be more likely to relay the problems of the unconnected poor, as opposed to both the regulator and the service provider who are primarily concerned with connected customers. For example, in *Port-au-Prince* the role of the NGO has evolved from that of intermediary between the service provider and the communities to one of secondary recourse mechanism (see *Box 4.1* below).

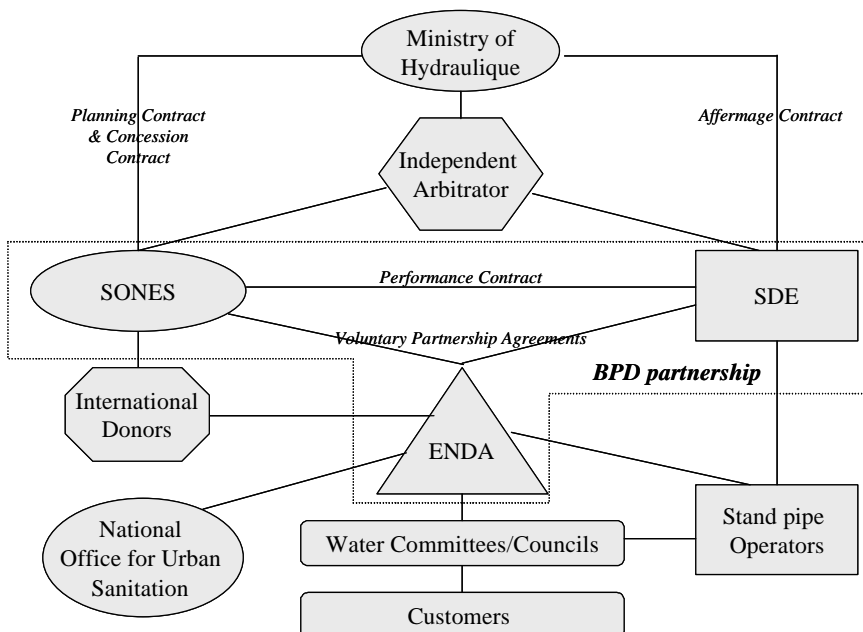
**BOX 4.1 GRET RELAYING THE NEEDS OF THE POOR IN PORT-AU-PRINCE**

The project in *Port-au-Prince* was initiated by an NGO, GRET. At the outset the public sector service provider (CAMEP) simply refused to enter poor boroughs, let alone provide them with any services. Initially, GRET played an intermediary role, establishing the water committees and preparing the terrain before CAMEP started getting involved. From the start, GRET had planned to withdraw from the process, leaving CAMEP to deal with the water committees directly. CAMEP faced up to this challenge very well, through the establishment of a Low Income Users Unit within the organisation to sensitise staff to the conditions, needs and capabilities of local communities. As a result, GRET was able to change its role from that of community intermediary to one of advocate and watchdog (i.e. one of secondary recourse for both connected and unconnected poor customers).

One factor that probably facilitated this evolution was the lack of an independent regulatory body in place, and, therefore, an institutional vacuum in terms of secondary recourse mechanisms, which the NGO was able to fill. However, the water committees feel that their position in discussions with CAMEP has weakened since the NGO has changed its role.

*Partnerships can create a more flexible, innovative and cooperative environment for developing rules better suited to the needs of the poor.*

In some of the more loose regulatory environments, such as *Haiti* or *Senegal*, the partnership has not had to work very hard on easing regulatory constraints because they were more or less able to experiment as they wanted. On the other hand, partnerships operating in Latin America where an independent regulator is in place have had to deal with more rigid regulatory environments, and they have had to develop specific strategies to ease such constraints in order to improve service delivery for the poor.



**Organisational relationships in the Dakar project**

Once they have identified a regulatory constraint, partnerships may operate in a variety of ways to ease it. If allowed by the institution in charge of regulation, they may experiment on a pilot basis to define a new rule. If not allowed, they may work 'around the rule' and rely on the mutual confidence created via the partnership to operate in a more flexible manner. The figure below attempts to show the types of approach that partnerships working to address regulatory constraints have adopted.

Partnerships may be successful in two ways: they either change the rules in order to enable further replication of the pilot project or they demonstrate the usefulness of changing the rule to the regulator or the policy-maker who

might decide later on to modify that rule. A good example of a partnership operating on a pilot basis to address regulatory constraints is found in *La Paz-El Alto*, where the private operator was allowed to experiment with condominal sewerage for 10,000 connections (see *Boxes 5.1* and *5.3*). It is also the only partnership where modifying the rules has been set as an explicit objective in order to facilitate future replication at the national level. By contrast, the partnership in *Cartagena* worked around the rules on the issue of billing methods (see *Box 5.2*), by developing trust in the communities to adapt to their needs.

**Partnerships can provide a flexible environment to adapt to new circumstances.**

In *Port-au-Prince*, the NGO withdrew progressively in order to ensure that the project could continue without its participation and to ensure long-term sustainability. It also chose to remain involved by moving into other activities, applying the successful partnership experience to the sanitation sector. The NGO had stated its intention to eventually withdraw from the start of the project. Even though this appears as a good intention from a sustainability point of view, some might argue that the NGO actually withdrew too early, before some major regulatory issues had been resolved in a sustainable manner: the main public operator is still largely self-regulated for bulk and retail prices and there is no regulation of water committees (potential ideas for regulatory mechanisms, such as internal assemblies or federation of water committees, have all failed).

In other cases, however, where relations between partners have been less forthcoming, such evolution might require a change in partners. For example, in *Buenos Aires*, the private operator decided to apply lessons on partnership on a much larger scale but brought in new civil society partners and stopped working with one or two of the NGOs it had originally worked with.

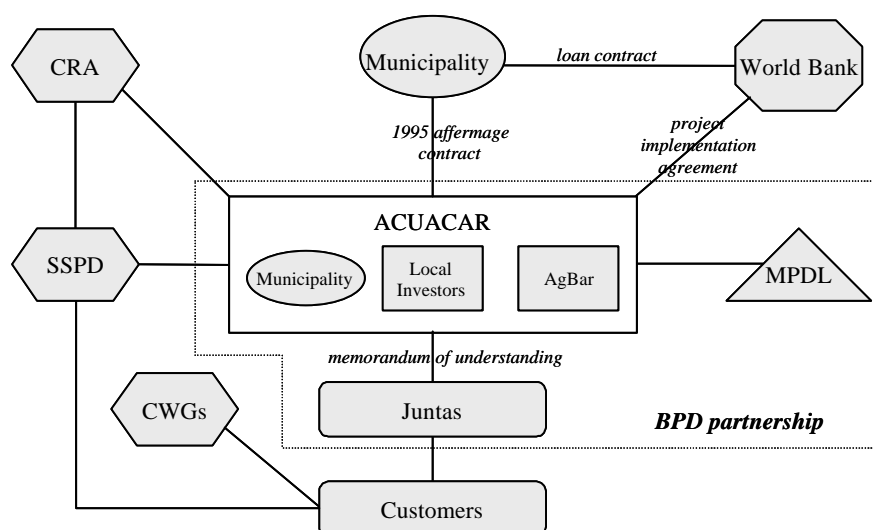
**4.2 FACTORS IN PARTNERSHIPS' SUCCESS**

Observation of the BPD projects suggests that two key factors influence partnerships' relative success in making regulatory frameworks more pro-poor.

**Partnerships are more likely to be empowered to lift a regulatory constraint when the regulatory body is part of the partnership and acts at the same level.**

In the *KwaZulu-Natal* project, both municipalities are party to the partnership and have considerable leeway for changing the rules in a pro-poor way. In fact, following the recommendations of the municipal provider, the municipal council in Durban had actually modified some rules before the partnership was set up, with the introduction of pro-poor measures such as a free water allowance and variable service levels. But entering the partnership was actively sought by the municipal provider as a way of further experimenting with these measures and actually implementing them in practice. We note that some of these measures, such as the free water allowance, were later turned into national policies, which benefited from this earlier experimentation.

By contrast, in *Cartagena*, the national regulatory body is not involved at all in water services in the city. Therefore, it has been unable to understand the specific problems emerging in relation to billing methods (see *Box 5.2*). A sense of disempowerment has emerged since the project is taking place at municipal level (with municipal interlocutors) but most of the regulation is decided at national level.



**Organisational relationships in the Cartagena project**

The distinction between regulation of the overall environment and regulation of the partnership should remain clear in order to avoid regulatory capture. This is why the regulatory body's direct participation in the partnership would not necessarily be appropriate, but its participation as an observer, taking interest in the partnership's activities, should be encouraged.

***Partnerships are more effective when partnership agreements are in place to regulate relations between actors.***

Formal partnership agreements are in place in *KwaZulu-Natal* and in the *BoTT*, and relatively informal ones in *Dakar*. In the other partnerships, no explicit partnership agreement is in place, although sub-contracts with NGOs might be used (see *Annex B* for more details). When there is no formal agreement between partners, the engagement of community representatives (and particularly, of NGOs) often tends to fade away as their initial role of information seeker or facilitator is fulfilled. Instead, they could be associated with developing the actions of the partnership further, in a dynamic and process-based way.

Formal partnership agreements are useful to set out the roles and responsibilities of each partner and establish the rules of the game between partners, i.e. setting some sort of internal regulatory regime for the partnership itself. The signing of co-operation agreements, together with the adoption of a consensus-based mode of decision-making in *KwaZulu-Natal* certainly contributed to the success of the partnership there.

By contrast, the lack of a formal partnership agreement and rules in *Jakarta* has led to a number of problems, especially with the municipality moving beyond its assigned role to get involved in network construction in the partnership area. In addition, excessive reliance on personalities (rather than formal agreements) has led to a sharp reduction in the partnership's dynamics following the departure of a number of key individuals from the various partners: the institutional memory of the project seems to have been lost. Such problems have been partially limited in *Dakar* or *Port-au-Prince* where the projects are also heavily reliant on personalities rather than the institutionalisation of the partnership, but mostly because the turnover of key individuals has been less.<sup>20</sup>

This analysis shows that partnerships have a substantial role to play in improving regulation and particularly in making regulation more pro-poor. *Section 5* goes into more detail and, based on a review of the eight partnerships, analyses what has been achieved in practice and where the partnerships have failed.

## 5 The Impact of Regulation on BPD Partnerships

In this section, the interaction between partnerships and regulation is examined in more detail to understand what partnerships have contributed to the process of pro-poor regulation. The approach taken is to examine the impact that partnerships have had on the performance of regulatory functions, distinguishing between economic, environmental and public health. Of particular concern is whether or not partnerships have increased flexibility and contributed to the adaptation of regulation to the needs of the poor.

### 5.1 ECONOMIC REGULATION

#### 5.1.1 Price Regulation

There are many aspects of price regulation that can have an impact on the poor, either through the setting of tariff levels or through the setting of tariff structures and the determination of payment methods.

*Table 5.1* presents an overview of how price regulation is carried out in the BPD projects and assesses whether or not the partnerships have influenced tariffs or payment structures. Based on this analysis, observations about the role that partnerships may play in price regulation are made.

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<sup>20</sup> See Caplan, et al., *Flexibility by Design: Lessons from Multi-Sector Partnerships in Water and Sanitation Projects* [BPD publication] for more discussion on the role of individuals versus institutions in the focus projects.

**Partnerships are usually unable to affect tariff level regulation on a large scale, even though tariff regulation may affect them substantially. They often fall back on developing alternative strategies to address issues associated with pricing policies over which they have little influence.**<sup>21</sup>

In many cases, the setting of tariff levels is carried out by an institution not directly involved in the partnership, such as the regulator in *Cartagena* or the Water Ministry in *Dakar*. To set tariffs, these institutions tend to consider the overall financial position of the water service provider (as well as other considerations, such as political ones) rather than detailed circumstances at the level of particular projects. Partnership actors may therefore feel unable to play a major role in influencing this process.

However, when poor customers represent a large and growing share of the customer base, the constraints affecting poor customers' ability to pay and the ability (or willingness) to charge them for services may be a key factor in determining the long-term viability of the service provider as a whole, and within it, of the partnership project.

For example, in *La Paz-El Alto*, the partnership did not provide a sufficiently good communication platform between the private and public sectors for modifying tariffs: instead, it chose to focus on experimenting with service quality standards. This is further explained in *Box 5.1*.

TABLE 5.1 PRICE REGULATION IN THE BPD CASE STUDIES

PROJECTS	PROCESS FOR TARIFF SETTING	PRO-POOR TARIFF AND PAYMENT STRUCTURES?	HAS THE PARTNERSHIP INFLUENCED TARIFFS OR PAYMENT STRUCTURES?
<i>La Paz-El Alto</i>	<i>Regulator (SSB) sets tariffs every five years</i>	<i>Poor consumers pay a subsidised rate for the first 30m<sup>3</sup> they use per month</i>	<i>No direct influence</i>
<i>Buenos Aires</i>	<i>Regulator (ETOSS) sets tariffs every five years</i>	<i>A basic tariff is factored on the basis of five income proxies, including property area and type of construction</i>	<i>Reduced connection charges NGO partner included in discussions with regulator regarding tariff revisions</i>
<i>Cartagena</i>	<i>Regulator (CRA) sets tariffs every year</i>	<i>Tariffs are set for six different domestic groups according to income proxies such as property size and age</i>	<i>Reduced connection charges Monthly bills collected bi-weekly to reduce financial burden on the poor</i>
<i>Jakarta</i>	<i>Local government (DKI Jakarta) determines water tariffs on the basis of advice from the government-owned utility (Pam Jaya)</i>	<i>There are tariff bands according to house size and consumption level</i>	<i>In Marunda, connection fees have been waived and billing has been simplified</i>
<i>Dakar</i>	<i>The national ministry (the Ministry of Hydraulique) sets the tariffs on the basis of proposals made by the state asset holding company (SONES)</i>	<i>A social tariff for low-consumption households (those that consume less than 20m<sup>3</sup> every two months)</i>	<i>The standpipe operator is responsible for collecting payment from users and paying the private operator for services</i>
<i>Port-au-Prince</i>	<i>The public utility (CAMEP) sets tariffs</i>	<i>Community billing at standpipe level</i>	<i>Bulk and retail tariffs for standpipes are set in agreements between the public utility and community water committees</i>

<sup>21</sup> See also Komives and Stalker, *Cost Recovery in Partnership: Results, Attitudes, Lessons and Strategies* [BPD publication].

PROJECTS	PROCESS FOR TARIFF SETTING	PRO-POOR TARIFF AND PAYMENT STRUCTURES?	HAS THE PARTNERSHIP INFLUENCED TARIFFS OR PAYMENT STRUCTURES?
<i>BoTT</i>	<i>Based on national ministry (DWAF) policy, municipalities set tariffs every financial year. In BoTT, the Project Implementing Agency (PIA) advises the municipality on tariffs (and most are set on a project by project basis)</i>	<i>Community billing  'Free Water Policy' (6m<sup>3</sup> per household per month) not yet implemented in rural areas</i>	<i>Recommendations regarding tariff setting are part of O&amp;M support to be provided by the PIA</i>
<i>KwaZulu-Natal</i>	<i>Based on national ministry (DWAF) policy, municipalities set tariffs every financial year</i>	<i>'Free Water Policy' (6m<sup>3</sup> per household per month) initiated in Durban prior to the national policy with cross-subsidies  In Durban, tariffs differ according to service standards</i>	<i>The partnership has reviewed the effect of price on demand over the last seven years. The results of this analysis will feed into future tariff setting discussions  Advises on the setting of the new sanitation charge</i>

#### **BOX 5.1 LA PAZ-EL ALTO: REGULATORY INFLEXIBILITY ON TARIFFS LED TO EXPERIMENTATION ON SERVICE QUALITY**

In La Paz-El Alto, the concessionaire bid on the number of new in-house connections to be installed, which mostly concerned poor areas in El Alto. This resulted in the setting of ambitious coverage targets in the contract, for tariffs that remained close to pre-privatisation levels. Demand from these new connections turned out to be much lower than expected at the time of signing the contract for a variety of reasons, such as low household usage and the slowing down of in-country migration from rural areas. This, combined with relatively low tariffs, placed the private operator in a difficult financial position within the first five years of signing the contract. Despite attempts from the private operator to obtain an extraordinary tariff renegotiation, the regulator considered that the impact of low demand was not substantial enough to justify it.

In such a context, the partnership (of which the regulator is part) decided to focus on:

- Analysing the root causes for such low demand, through anthropological studies of the cultural perception of water and consumption practices of the Aymara people;
- Carrying out an education and awareness campaign to promote hygiene;
- Developing lower cost service options via condominial water and sewerage networks on a pilot basis, with explicit interest in replication via the preparation of national standards.

Such initiatives were only partially successful in specifically addressing the regulatory constraint due to an inflexible approach to the setting of tariff levels and structures adopted by the economic regulator:

- Reduced charges for condominial network connections were set at arbitrarily low levels, with no direct relation to the true cost of such connections and no subsidy to compensate for this, thereby reducing the private operator's financial incentive to use such standard;
- There is no differentiation between water and sewerage tariffs (tariffs are the same whether households receive one or both services), which means that the private operator derives no additional return from sanitation investments.

The *BoTT* project is another example where the regulatory framework regarding tariff levels and structures has affected the project's ability to recover costs, and where the partnership has had a limited ability to influence tariff policy. The South African legal framework specifies a

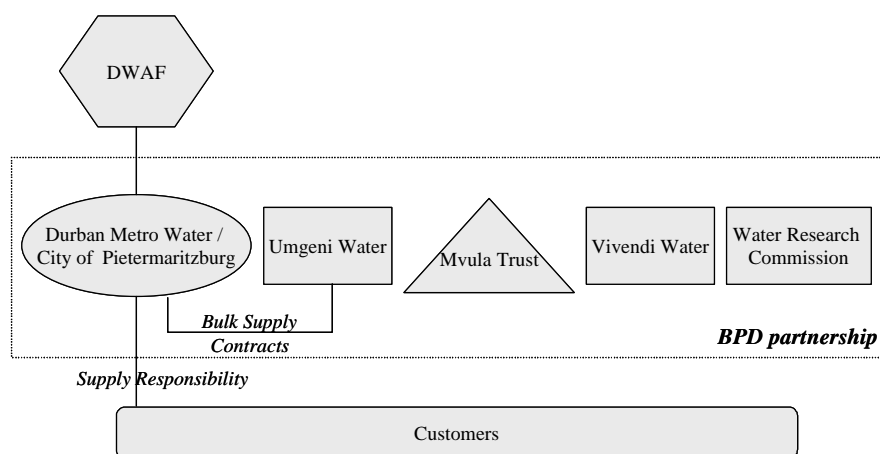
three-block tariff structure but, in theory, it gives relative freedom to municipalities (who are now responsible for provision of water and sanitation services according to a recent decentralisation law) for defining the level of each block. In December 2000, however, the national government expressed its political commitment to a ‘Free Water Policy’, which entails the provision of six cubic metres of water per household per month for free. Municipalities (including Pietermaritzburg) were scheduled to implement this policy by July 2001, although many rural municipalities were not able to do so, due to insufficient financing.<sup>22</sup>

In municipalities managed by the **BoTT** programme in the Eastern Cape Province, this new constraint posed a substantial threat to the projects’ ability to recover costs, in a context where the cost-recovery performance was already quite low. It also rendered a pilot use of electronic pre-payment meters practically redundant, although they are still being used in order to control demand (which is often limited to the free water allocation) and keep costs down. Through community liaison, however, the partnership managed to convince some communities that, while free water is a right, the schemes are unlikely to be viable in the long term without some level of community payment. Due to such activities, those communities are continuing to pay for water even following the introduction of the ‘Free Water Policy’.

**Partnerships can play a consultative role in setting tariffs for the poor**

There are several cases where the partnership has been included in discussions regarding tariff levels. In the **BoTT** projects, it is part of the partnerships’ contractual responsibilities to recommend tariff levels to local governments in the areas where they are carrying out a project, as part of the process of training and gradually transferring responsibilities to municipalities.

In **KwaZulu-Natal**, the partnership is advising Durban Metro on appropriate tariffs for the new service levels included in the project, and is also providing advice concerning the new sanitation charge (previously, the cost of sanitation was included in property tax).



**Organisational relationships in the KwaZulu-Natal project**

In **Buenos Aires**, tariff-setting procedures offer limited opportunity for involving the public, and particularly the poor (for example, at the last tariff review in 2001 only one public hearing was organised). The regulator has only recently become conscious of the need to get more direct feedback and has invited one of the community-based organisations involved in the BPD to take part in discussions regarding the setting of the social tariff. In this case, however, the CBO was quite dissatisfied about its involvement, suggesting that their role in the discussions was not specified clearly enough and that many of the issues they raised were not taken into account. This shows that, when civil society organisations are involved in discussions with the regulator, it is essential that the discussions and the decision process be transparent in order to ensure that they do not end up feeling further disenfranchised by the regulator.

**With respect to tariff structures, partnerships have worked on reducing or waiving connection charges**

Payments for water and sanitation services are usually made via two main types of charges: one-off connection charges and tariffs for usage. Connection charges, if too high, may

<sup>22</sup> The BPD project in Durban was not affected by this decision since the Durban municipality had pioneered the ‘Free Water Policy’, on the grounds that it is actually less expensive to provide water for free in poor areas than to bill customers due to a high potential for cross-subsidisation from high-income and industrial users.

prevent the poor from having access to those services, given that most of them are usually not connected to the network. Tariffs for usage can be structured in several ways with varying pro-poor properties: for example, incremental block tariff structures may be detrimental to the poor who use collective water connections and are therefore more likely to consume in the higher block.

Partnerships seem to be more successful at reducing the connection charge to more affordable levels rather than obtaining a modification of tariff structures. This is particularly true when partnerships are mostly driven by private operators, such as in *Jakarta*, where the latter have a clear economic advantage in getting people to connect because of the subsequent increases in revenues (particularly in the case of *Jakarta* where the water charge per volume sold is the same, irrespective of whether water is sold at a lower tariff or not).

In *Buenos Aires*, for example, the connection charge has been a difficult stumbling block for providing services to the poor since the start of the contract. Originally set at US\$600 for water and US\$1,000 for sanitation, connection charges were reduced to US\$120 each following contract renegotiation (with cross-subsidisation from customers already connected). However, this still proved a hurdle for the poorest households: the BPD partnership therefore sought to further reduce connection costs by using group connections and contributing community labour towards the cost of connection in some well specified areas. Even though it was not directly involved in the project, the regulator proved flexible and let this experimentation take place.

In *Jakarta*, connection fees were waived completely in one area of the project, the Marunda district. In a loose regulatory environment, this did not require any specific approval. This is also partly due to the fact that the private operator did not seek to increase any other tariffs in order to recoup the costs of providing free connections. Note that this approach is suitable for a relatively small area of experimentation. It might not be viable for providing connections to all of the recognised unconnected poor in order to meet the 100 per cent coverage target by 2023, as it compromises long-term financial viability. Ultimately, this shifts the financial risk of providing free connections onto the public sector, which may not want it in the long term.

***Billing regimes and payment methods are an area where partnerships can also usefully contribute, as they are usually regulated at a smaller scale.***

The introduction of more pro-poor billing regimes and payment methods has been a component of several BPD projects, for both the connection and the on-going charges. Variations in billing regimes have taken two forms: the spreading of payment schedules and group payments. Some of the BPD projects have introduced standpipes with associated group payments on a large scale, such as in *Dakar* and *Port-au-Prince*. In both cases, no regulatory approval was needed, given that this service standard is explicitly allowed. In the case of *Cartagena*, on the other hand, modification of the billing structure was not possible due to national regulations. The partnership had, therefore, to go around the rule and adapt its services (see *Box 5.2* below).

#### **BOX 5.2 LACK OF REGULATORY FLEXIBILITY ON BILLING REGIMES IN CARTAGENA**

Through discussions with community representatives and a pilot demand assessment carried out by the NGO, the partnership identified the billing regime as one of the most significant factors preventing cost recovery in *El Pozón*, the main focus area for the BPD partnership. Most of the residents of *El Pozón* are daily cash earners and, as such, they find it difficult to manage their finances and save the money required to pay their water service bill each month.

The partnership asked the regulator's permission to pilot bi-monthly billing in *El Pozón*. However, the regulator refused to modify national regulations, which stipulate that bills cannot be issued to customers at intervals less than once a month. Therefore, the partnership had to develop a different approach: through local community organisations, mobile payment collection units were set-up which collect money from residents in *El Pozón* on a bi-weekly basis. This system complies with the national regulations, as bills are only actually calculated and printed once per month, while still giving the residents of *El Pozón* the flexibility to pay more frequently than they had been.

This is a clear example of where regulation has caused a barrier to an improvement in service delivery to the poor, and where partnership, in this case between the service provider and community organisations, has provided the means to side-step such a barrier and provide the service demanded by the community concerned. Overall, it is hoped that this strategy will have the desired impact to make service more accessible to the poor and increase cost-recovery levels. However, this is yet to be seen as the project was recently started. Although the partnership feels that this model has real potential for replication, there has been little interest on the part of CRA, the national regulator.

### 5.1.2 Service Quality Regulation

Blanket service quality standards can raise costs of service provision to the poor: in many cases, service quality standards are set higher than those they can afford. Therefore, service quality regulation should allow for variable service levels so that operators can adapt service levels to the needs of poor customers.

Table 5.2 provides an overview of the service quality being provided by the BPD partnerships.<sup>23</sup> Within this research, it was impossible to consider all aspects of service quality that might be regulated (such as product quality, customer service quality, etc.). Instead, aspects of service quality that the partnerships themselves identified as issues to work on are analysed.

TABLE 5.2 SERVICE QUALITY REGULATION IN THE BPD CASE STUDIES

PROJECTS	OVERALL APPROACH	PARTNERSHIP SERVICE QUALITY	DOES THE PARTNERSHIP COMPLY WITH THE GENERAL APPROACH?
<i>La Paz-El Alto</i>	<i>Blanket</i>	<i>Condominial water and sewerage</i>	<i>Introduced alternative standard on a pilot basis. Change of rules needed for replication</i>
<i>Buenos Aires</i>	<i>Blanket</i>	<i>In-house connections and bulk supply agreements between private operator and communities</i>	<i>Introduced varying service levels without need for regulatory approval</i>
<i>Cartagena</i>	<i>Blanket</i>	<i>In-house connections</i>	<i>Did not seek to experiment</i>
<i>Jakarta</i>	<i>Blanket</i>	<i>In-house connections</i>	<i>Did not seek to experiment</i>
<i>Dakar</i>	<i>Variable</i>	<i>Communal metered standpipes with community billing</i>	<i>Such standard is allowed</i>
<i>Port-au-Prince</i>	<i>Variable</i>	<i>Metered standpipes</i>	<i>Such standard is allowed</i>
<i>BOTT</i>	<i>Variable</i>	<i>Pre-paid standpipes</i>	<i>Such standard is allowed – service levels are very flexible</i>
<i>KwaZulu-Natal</i>	<i>Variable</i>	<i>Several: in-house connections (in Durban: ground tank, roof tank and full pressure) and standpipes</i>	<i>Such standards were approved through local by-laws</i>

***Partnerships’ focus on affecting quality regulation has remained limited and has largely depended on the approach taken at project level. In some cases, a variable approach at project level meant that the partnerships did not seek to experiment further.***

Regulatory systems with an independent regulatory body, such as in *La Paz-El Alto* or *Cartagena*, tend to have a less flexible approach to service quality regulation than those which are loosely regulated, such as in *Dakar* or *Port-au-Prince*. By contrast, some regimes have experimented with a high degree of flexibility with respect to quality regulation.

(23) The column ‘overall approach’ gives a general assessment about how service quality regulation is performed in the regulatory regime as a whole, distinguishing between a ‘blanket’ approach, where uniform and generally high standards are set, and a ‘variable’ approach, where variable service standards are allowed.



For example, in *KwaZulu-Natal*, the municipality had been experimenting with variable service levels for the poor on its own, before the partnership approach was adopted. In South Africa, national quality regulations focus mainly on setting minimum service standards (25 litres per person per day at a maximum distance of 200 metres from any household, as per the ‘Reconstruction and Development Programme’), based on the premise that a little water for all is better than more water for only a few. It is down to municipal governments, acting as water service authorities, to define quality standards within their territory. Apart from standpipe provision, which it is trying to phase out, Durban Metro Water introduced differentiation between three types of in-house service standards, with corresponding differences in tariffs: ground tank and roof tank/semi-pressure (where consumption is limited to a daily allowance) as well as full pressure. Consumers in poor areas accepted such differentiation, as it helped them adapt their consumption to fit their means. In addition, it led to some improvement in the cost-recovery record of the water service provider.

***In rigid regulatory regimes, only some partnerships have tried to introduce variable service quality standards.***

As shown in *Table 5.2*, the partnerships in *Cartagena* or *Jakarta* did not seek to experiment on quality standards. As an exception, the BPD project in *La Paz-El Alto* obtained permission to experiment with different service quality standards, but only on a pilot basis for 10,000 households, as discussed in *Box 5.3* below.

**BOX 5.3 LA PAZ-EL ALTO: PILOTING THE CONDOMINIAL APPROACH TO REDUCE COSTS**

The National Regulations for Water and Sanitation Service in Urban Areas, developed in 1992 by the Ministry of Housing and Basic Services, defined in-house water and sewerage services as the only acceptable long-term water and sanitation solution for urban areas. The concession contract set even more stringent water quality standards, with extra quality and reliability requirements. The partnership was allowed to pilot alternative quality standards through a condominial approach. Condominial systems deviate from the normal system in several ways, including reduced pipe diameters, shallow trenching and drainage incline. These systems involve additional maintenance requirements at community level, but the supply company can easily carry out such activities.

In *La Paz-El Alto*, those receiving condominial connections benefited from a sharp reduction in connection charges, as set by the regulator. However, some customers involved in the pilot were reluctant to get connected to what they saw as a ‘lower-grade’ system, because they considered that it would reduce the value of their properties. Due to the tariff structure and popular perception, the take-up for condominial connections has not been as high as originally anticipated.

This highlights two points to bear in mind when experimenting with alternative service levels:

- Appropriate information on each quality standard should be provided: condominial networks are used for entire cities in Brazil, including rich households who are more than ready to accept them as long as it does not introduce any additional burden. Therefore, it is not appropriate to market it as a ‘solution for the poor’;
- Ultimately, customers can only accept a given service standard if it has a legal status comparable to other service standards.

In order for the pilot to be replicated, it will be necessary to convince the Ministry of Housing and Basic Services to modify the legal status of condominial sewerage. This is why, from the start, an objective of the partnership has been to facilitate the modification of the standards by the Ministry. Meeting this objective might be aided by the fact that the regulator takes part in the activities of the partnership, although only as an observer.

**5.1.3 Regulation of Coverage Targets**

Increasing service coverage is often an objective of the contract under which private companies operate when they have investment obligations (such as in *La Paz-El Alto*, *Buenos Aires* or *Jakarta*). Extension of coverage can be required through formal obligations

or encouraged through the provision of financial incentives. For public operators, coverage objectives are much more loosely defined and are basically dependent on the financial resources available for investment and political priorities.<sup>24</sup>

In *Table 5.3* below, the presence of formal coverage targets imposed on the main water service provider is analysed. Coverage objectives for the partnership itself are also looked at.

TABLE 5.3 COVERAGE TARGETS IN THE BPD CASE STUDIES

PROJECTS	OVERALL	PARTNERSHIP
	DEFINITION	OBJECTIVE
<i>La Paz-El Alto</i>	<i>Long-term coverage targets expressed as percentage of population covered based on assumed population growth. Five-year objectives expressed as number of connections</i>	<i>Water: 100 per cent coverage within first five years Sewerage: increase from 41 per cent to 90 per cent</i>
<i>Buenos Aires</i>	<i>Five-yearly targets regarding percentage of population serviced by water and sewerage.</i>	<i>Objective to cover 10,000 low-income households in three years No specific targets</i>
<i>Cartagena</i>	<i>Number of in-house connections</i>	<i>Water: 100 per cent in target area by 2001 Sanitation: 100 per cent by 2002</i>
<i>Jakarta</i>	<i>Percentage of population with access to water services</i>	<i>Water: 89 per cent by 2004 Sewerage: 90 per cent by 2004 100 per cent coverage in Marunda district Sewerage: not in contract</i>
<i>Dakar</i>	<i>No specific targets for SDE (affermage contract) Investment targets for SONES in World Bank loan contract and in the Performance Contract with the State Sanitation handled separately</i>	<i>SONES: 100kms of pipes and 36,000 connections in five years. No specific targets for standpipes No specific targets, informal agreements only</i>
<i>Port-au-Prince</i>	<i>No set targets, CAMEP defines its investment programme. Mostly water</i>	<i>Non applicable Standpipe coverage in 21 communities</i>
<i>BoTT</i>	<i>DWAF and municipalities carry out investments as funds become available. Overall objective is 25 litres per person per day available at no more than 200 metres from each household. Mainly water</i>	<i>Non applicable No set targets: the contract is for conducting projects in an area which is directly funded by DWAF</i>
<i>KwaZulu-Natal</i>	<i>Same as above</i>	<i>Water: 100 per cent coverage within five years 100 per cent water coverage in six pilot areas.</i>

***The majority of private sector operators involved in the BPD case studies have some contractually expressed incentives to extend service coverage, but some partnerships have also agreed coverage objectives for their activities.***

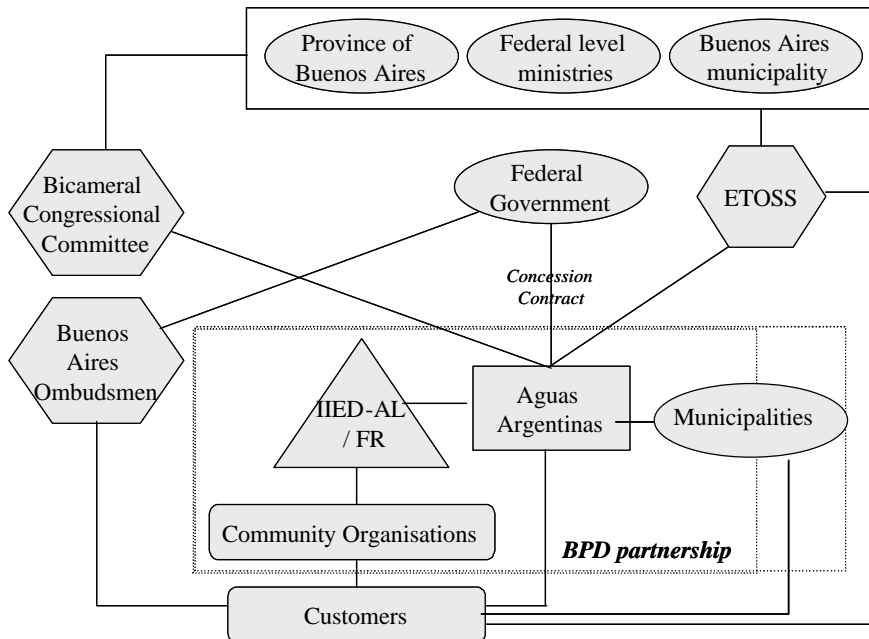
If coverage obligations are set out in the contract, their formulation may have a very important impact on whether or not the poorest benefit from the contract. In **Buenos Aires**, for example, the concession contract sets out coverage targets with associated penalties for

<sup>24</sup> Although it is rare, public sector operators can also have coverage objectives. For example, in Dakar, SONES has investment obligations through the World Bank loan contract and the Performance Contract with the State.

non-compliance. These targets, however, were defined at quite a general level, leaving some room to the concessionaire for defining coverage extension priorities. This has been a source of contention between the municipalities and the regulator, who had failed, according to the municipalities, to determine the concessionaire's investment priorities in a sufficiently pro-poor manner. During the most recent tariff-setting process, the municipalities asked for the

power to determine local investment plans and this power was granted. In addition, the regulator has proved to be relatively flexible in determining what counts towards coverage targets, by allowing connections provided through bulk supply agreements and use of community labour to count towards meeting the concessionaire's coverage targets. In *La Paz-El Alto*, by contrast, the regulator did not grant such flexibility and only in-house connections count towards coverage targets.

In the majority of the case studies, the partnerships have adopted defined service coverage objectives for their activities, in addition to any contractual obligations for service coverage that the private operator might be subject to. There are a number of exceptions: in *Buenos*



**Organisational relationships in the Buenos Aires project**

*Aires* no specific coverage targets were defined for the BPD partnership, whilst in *Cartagena* or *La Paz-El Alto* the service coverage targets for the areas concerned were set by the main service provider rather than by the partnership. While it is difficult to evaluate the impact that this has had in terms of service delivery to the poor, these three case studies have the least clearly defined partnerships and the involvement of civil society organisations has not been visible or central to their activities. This might partly explain a certain lack of determination of the partnerships' objectives.

***Partnerships usually find it difficult to be active in areas where other regulatory issues (such as a lack of land tenure) are a constraint. However, partnerships can be active in areas where the project would not be allowed.***

In two of the partnership case studies, land tenure issues have limited the potential for the project to extend services to some of the poorest: in *La Paz-El Alto* the concessionaire cannot supply services to those without land tenure, or to those who live outside the designated served area, whilst in *Buenos Aires* service cannot be provided to neighbourhoods that are not recognised by the authorities or in areas where land tenure is uncertain. By contrast, in *Cartagena* the partnership has been able to overcome such limitations thanks to specific support from the municipality. Even though the joint-stock operator is only permitted to supply water within the municipal boundaries, a large and growing population lives outside these boundaries in an area called Nelson Mandela. Following the municipality's intervention, the partnership was able to provide services through communal connections as opposed to the in-house connections that it can only provide in its legally authorised service area.

***Where regulation does not stipulate parallel extension of sanitation service coverage, it is unlikely that the partnership will provide such a service.***

It is immediately striking that most of the partnerships are not involved in the delivery of sanitation services. In fact, this is often a reflection of the obligations introduced by the wider project: provision of sanitation services (with corresponding coverage targets) is only required in *Buenos Aires*, *La Paz-El Alto* and *Cartagena*.

Many partnerships have only recently become involved in sanitation services and at a relatively small scale. This might be due to an institutional separation between water and sanitation services. In **Dakar**, for example, whilst water and sanitation services are managed by SDE and SONES on a public-private partnership basis, sanitation services are still under the control of a public sector body, ONAS. Even though the degree of co-ordination between those institutions is limited, it appears that ENDA, the NGO active in the BPD partnership, has recently got involved in activities with ONAS to develop sanitation services. Management of water resources would undoubtedly benefit from greater co-ordination between those institutions, particularly in a context where the resource situation is fragile, with a lowering of the water table in the Dakar area and saline intrusions.

In **Haiti**, the GRET has also recently started a sanitation programme as a way of maintaining its presence in the BPD project area and continuing the unfinished task of building lasting water and sanitation institutions in poor boroughs. For greater co-ordination, however, these activities might have benefited from being conducted simultaneously.

#### 5.1.4 Competition Regulation

Table 5.4 below indicates whether service providers have exclusivity of service provision and how partnerships have interacted with other service providers in the project area where applicable. It distinguishes between two types of alternative service providers: those that operate completely independently from the main network supplier, and those that operate in co-ordination with the latter, generally through the signing of bulk supply agreements (the main operator supplies water in bulk whereas the small operator is responsible for retail services).

TABLE 5.4 COMPETITION REGULATION IN THE BPD CASE STUDIES

	DOES THE MAIN SERVICE OPERATOR HAVE EXCLUSIVITY?	INTERACTION WITH OTHER SERVICE PROVIDERS IN THE PARTNERSHIP AREA
<i>La Paz-El Alto</i>	<i>No explicit exclusivity; however, it is effectively introduced via other means such as obligation to disconnect standpipes after network construction and control of abstractions</i>	<i>After network construction, other providers are shut down: standpipes are disconnected</i>
<i>Buenos Aires</i>	<i>Explicit exclusivity is set via the concession contract: independent service providers are only permitted in those areas where the concessionaire does not offer a service</i>	<i>Bulk supply agreements with community operators</i>
<i>Cartagena</i>	<i>Explicit exclusivity via the concession contract, although this is not enforced as other providers cannot compete with network supply and tend to disappear</i>	<i>No interaction within the project area; however, bulk supply agreements are in place in other parts of the city with small-scale operators</i>
<i>Jakarta</i>	<i>Explicit exclusivity is granted via the concession contract</i>	<i>Bulk supply agreements with registered privately-owned standpipes and the municipality</i>
<i>Dakar</i>	<i>Explicit exclusivity for water supply via the affermage contract, reinforced via a ban on reselling of water from private connections</i>	<i>Bulk supply agreements with community standpipe operators</i>
<i>Port-au-Prince</i>	<i>Monopoly held by the public sector utility</i>	<i>Bulk supply agreements with standpipe operators</i>
<i>BoTT</i>	<i>No explicit exclusivity: the PIA is only asked to work on certain projects by DWAF</i>	<i>Other providers operate freely, including municipalities, water boards and SSIPs</i>
<i>KwaZulu-Natal</i>	<i>Municipalities are exclusive water service authorities but they can choose who they want to be service provider</i>	<i>None</i>

*Even though in most cases, the main service provider has some sort of service exclusivity, several partnerships have led to the establishment of independent providers, with bulk supply agreements with the main operator.*

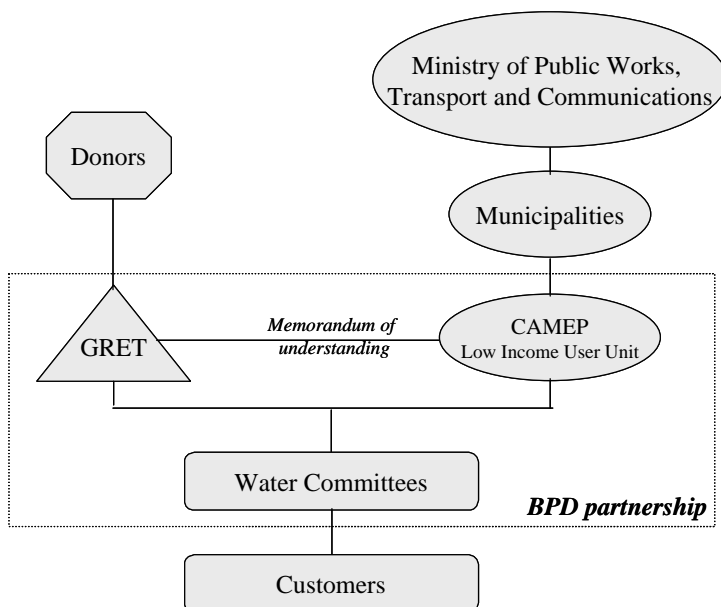
The main service provider in the BPD partnerships usually benefits from some level of service exclusivity in its area of operations. In particular, exclusivity rights for private operators are either expressly defined in the contracts, such as in *Buenos Aires* or *Cartagena*, or they can be granted via alternative means, such as in *La Paz-El Alto*.

In the latter case, although the concession contract does not explicitly grant monopoly rights, it requires the concessionaire to eliminate all pre-existing communal standpipes once network services have been provided (in those areas where networks are yet to be constructed, water can be provided via public stand-pipes). In addition, national regulations effectively protect the concessionaire from competition in a number of forms: for example, the re-sale of water by connected households is prohibited and the concessionaire is allowed to charge a fee for groundwater extraction within its service area.

In several cases, the partnerships have led to the creation of community operators with the remit of servicing areas without networks. In *Cartagena* and *Buenos Aires* the partnerships have encouraged the setting up of community operators, with whom they have signed bulk supply agreements. The community operators are then responsible for the retail of water and ensuring that the group bills are paid.

In *Dakar* and *Port-au-Prince*, similar systems apply, but with retail supply via standpipes. Prices are usually regulated by the same body for direct retail from the main operator and indirect through independent providers. In *Dakar*, this is done in a very simple way since standpipe operators are treated as any other of SdE's clients. The partnership simply assisted in identifying the most adequate standpipe operators, who are all well-known and trusted people in the areas where they operate.

*Few partnerships have dealt with or have explicitly considered the impact of their activities on totally independent private providers.*



**Organisational relationships in Port-au-Prince project**

In *Port-au-Prince* the public utility CAMEP benefits in theory from a monopoly position for piped services, but coverage levels are so low (especially at the start of the partnerships, when only 10 per cent of the households in the city had in-house piped water services) that small-scale private service providers have inevitably sprung up to provide services.

What is unique to *Port-au-Prince* is that even though the partnership established its own standpipes and operators, it has deliberately limited the storage capacity of its standpipes so as not to eliminate competition from completely independent private providers. This avoids confrontation and ensures water supply options for the poor. This was not required by competition regulation, but the NGO suggested that it would be a way of increasing the project's acceptability amongst local populations.

*The activities of the partnerships have had very limited impact on competition regulation outside the sphere of pro-poor activities.*

In *KwaZulu-Natal*, relations between the bulk water supplier for both municipalities, Umgeni Water, and the municipal water operators purchasing this bulk water have recently become strained due to the lack of external regulation of bulk supply agreements. The municipal operators receive no explicit supply guarantees and their efforts at reducing losses may be negatively affected by increases in bulk water prices (by a bulk water supplier eager to preserve its revenue base), with a zero net gain. Although both the bulk supplier and the municipalities work in partnership, this collaboration has had no impact on resolving the

broader competition issue. It seems that the Ministry itself should get involved to improve regulation.

## 5.2 ENVIRONMENTAL REGULATION

It is not the objective of this report to comprehensively review how environmental regulation is carried out in the BPD partnerships. However, environmental regulation can have a large impact on the poor. Some examples of how environmental regulation can affect the poor and how partnerships may need to get involved are presented below.

***Partnerships have been looking at alternative solutions when environmental regulation increases the costs of service delivery for the poor.***

In **Buenos Aires**, when the concession contract was renegotiated in 1997, a new charge was introduced to cover the costs of service expansion (two-thirds of the charge) and environmental clean up (one third). This SUMA charge, as it was called, is a flat rate payable on top of every bill. When poor customers are billed on a communal basis, this charge of initially US\$3 a month remains affordable as it can be divided between many users. However, where poor people are connected individually it can represent a significant financial burden. In many ways this additional burden can be seen as a barrier to connecting and billing poor households individually, and perhaps a motivator for partnership development: communal billing requires a high level of community organisation, which is usually achieved through the involvement of NGOs or CBOs in the partnership.

***The costs of environmental degradation may also severely affect the poor in the long term, but partnerships are insufficiently pro-active in this area.***

In **Jakarta** there is no appropriate regulation of water abstractions, which means that the groundwater table is rapidly going down. The partnership may inadvertently help address this problem since promoting water connections should lead to a reduction in over-abstraction from alternative providers. However, the provision of increased piped water supply combined with no appropriate drainage or sanitation services may also lead to a deterioration of water resources through infiltration to the groundwater table, particularly in slum areas. Despite this, the partnership has limited itself to water services without trying to carry out activities to improve sanitation and drainage. This might be due to the fact that the private operator largely drives the partnership's agenda and its concession contract is purely limited to water services.

## 5.3 PUBLIC HEALTH REGULATION

***In a number of cases, drinking water standards have been a constraint for delivering services to the poor and partnerships have worked on alleviating such constraints.***

In the **BoTT**, the PIA found that provision of services to communities in rural areas could prove disproportionately expensive, unless it could provide services at lower levels of drinking water quality. It therefore approached DWAF for permission to depart from national drinking water quality standards for remote areas where it proved impossible to deliver water at the quality stipulated in the regulations. Such departure was allowed, but only on a project-by-project basis, rather than through a general lowering of drinking water quality standards.

In **La Paz-El Alto**, the partnership actors have been involved in the process of developing new national drinking water quality standards. This process was initiated because national laboratories lack the facilities to analyse all of the parameters included in the current standards and with the ultimate objective of reducing the cost of service.

## 6 Key Findings and Recommendations for Future Design

This last section draws out the key findings of this research and formulates recommendations, both in terms of regulatory framework and partnership design.

The key findings can be framed to answer four main questions that drove this research:

- How do regulatory regimes affect partnerships and their activities?
- What role can partnerships play in making regulation more pro-poor?<sup>25</sup>
- What attributes are key to partnerships playing a role in regulation?
- What impact have partnerships had on the performance of regulatory functions?

On the basis of these questions, recommendations for partnership and regulatory design attempt to answer two further questions:

- How could regulation make better use of partnerships?
- How could partnerships maximise their potential for making regulation more pro-poor?

Finally, proposals for future research are developed, which may require experimentation with new forms of partnerships in future.

The overall message is that partnerships should be more ambitious. If they are well designed, they have the potential to make the overall regulatory framework more favourable to poor consumers. To maximise their potential, regulatory institutions should also take a direct interest in helping partnerships form and then in their activities also.

### 6.1 KEY FINDINGS

#### *How do regulatory regimes affect partnerships and their activities?*

As discussed in *Section 3*, the partnerships within the BPD case studies have developed within a wide variety of regulatory models: not one model seems to be more conducive to establishing a partnership than another. However, there are substantial differences between the regulatory environments, which have influenced the nature of the partnerships and their activities

*When a public-private contract is in place at project level, partnerships have left their commitments rather undefined. By contrast, in the absence of a public-private contract, partnerships have better specified their activities.*

When a public-private contract is in place at project level, partnerships are often created at the initiative of the private operator following privatisation and civil society is often less firmly integrated into the partnership. By contrast, in the absence of a public-private contract, partnerships have better specified their activities and civil society has tended to have a stronger voice.

*The activities that partnerships undertake partly depend on the wider regulatory environment in which they evolve.*

Regulatory frameworks are more or less forthcoming for the type of approaches promoted by partnerships and have had a varied influence on the formation of partnerships and their activities. In broad terms, regulatory regimes tend to be either rigid or relatively loose:

- In a more rigid regulatory environment, the partnership would often work on addressing a specific regulatory constraint: working in partnership provides sufficient

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<sup>25</sup> Note that the focus on pro-poor regulation has been maintained throughout the report: because most partnerships have been formed with a clearly pro-poor remit, their roles and activities have focused on these customers with a limited impact on improving regulation as a whole, except potentially for improving general transparency. This pro-poor focus has generated some perverse incentives in some cases, however, with the feeling that solutions developed in partnership are only 'solutions for the poor'. Clearly, the partnership must play a role in communicating that this is not the case when such solutions might have wider benefits, such as with condominal sewerage.

trust between partners to develop an alternative rule, either on a pilot basis or by working around the existing rule.

- In a looser regulatory environment, the creation of a partnership cannot be directly attributed to the need to address a regulatory constraint. Indeed, the partnerships did not require regulatory approval for conducting their activities. In such cases, however, the lack of regulation may have been what led to the creation of the partnerships: in the absence of existing regulatory mechanisms, partners may have had a stronger incentive to form a partnership in order to create a space for representing and defending their common interests as well as society's interests. In such contexts, partnerships may even end up performing some regulatory functions themselves, such as acting as a recourse mechanism for customers' complaints.

*Where regulatory institutions are in place, their attitude towards the partnership can vary substantially, from one of indifference to one of active engagement.*

Attitude can be influenced by a variety of factors, linked to the regulatory body's incentives for engaging with the partnership, such as:

- *The regulatory body's mandate (as defined by policy-makers):* in most cases, regulatory institutions have no clear incentive to deal with poor customers, as they have not received a specific mandate for doing so;
- *The regulatory body's geographical location in relation to the partnership:* when the body exercising regulatory functions has offices near to the work of the partnership, their interests in improving regulation may be better aligned;
- *The regulatory body's strength relative to the private company that it regulates:* in some cases, the regulatory body is not involved as it is substantially weaker than the private company it is supposed to regulate.

*Whether or not the regulatory body is involved has partly influenced the strategy adopted for replication of the partnership's approach.*

Many of the partnerships have looked at issues of replication in terms of 'organic growth', i.e. adopting the same approach in a growing number of areas without thinking very hard about the long-term sustainability of the approach when adopted on a larger scale. Very few of the partnerships have placed an emphasis on setting up the regulatory mechanisms that would allow such expansion. In fact, the clearest case of this taking place was in **La Paz-El Alto**, where the participation of the regulatory body in the partnership as an observer probably facilitated this process of replication.

#### ***What role can partnerships play in making regulation more pro-poor?***

Section 4.1 highlights the diversity of roles that partnerships can play in making regulation more pro-poor:

- *Partnerships can help focus the attention of regulatory institutions on poverty issues:* partnerships have usually been created with the specific remit of helping the poor, whereas in many cases the regulating agency or the main service provider may not regard the poor as a priority. Therefore, the very existence of the partnership may help focus the attention of the institution in charge of regulation on poverty issues.
- *Partnerships can help gather information on the needs of the poor and make it available for regulation:* in many cases regulators tend to ignore the poor because they do not have readily available information about them, or enough human and financial capital to go and collect it. Partnerships can play an important role in gathering and relaying information to decision-makers.
- *Partnerships can help partners understand each other's interests and constraints with respect to pro-poor regulation:* each member of the partnership has its own agenda and interests with respect to regulation but also has its own constraints. Working in partnership allows partners to understand each other's interests and constraints better and work towards a consensus solution. In particular, private sector operators face regulatory constraints that may be beyond their control, and NGOs would need to understand this in



order to focus their efforts where it is most appropriate (on lobbying to change the regulatory framework rather than on criticising the private sector for example).

- *Partnerships can act as a ‘self-regulation’ mechanism to balance each partner’s interest:* the process of developing a formal partnership may lead to the introduction of reporting mechanisms and regular meetings between partners. These mechanisms can create a form of self-regulation and make decision-making on partnership activities more transparent.
- *Partnerships can be useful tools to create publicity and establish reputation for dealing with the interests of the poor:* working in partnership may improve the reputation of each individual partner in the sense that they are seen as working for the partnership’s interests instead of simply their own interests. Although the reasons are not explicitly stated, it can be assumed that the partnership is useful to the private operator for developing its knowledge of pro-poor service delivery issues (a way of accessing information) and also for establishing a pro-poor reputation on the international arena, and amongst existing customers, in an era when corporate responsibility issues are of critical importance. These reputation concerns should act as a form of self-regulation on the operator and help to ensure that the poor are given due attention.
- *Partnerships may provide an alternative focus for customer complaints and particularly help to relay poor customers’ interests:* particularly where regulatory institutions are relatively weak or inaccessible to the poor, partnerships may offer another recourse to address their concerns. Specifically, within the partnership, the civil society partner may be more likely to relay the problems of the unconnected poor, as opposed to both the regulator and the service provider who are primarily concerned with connected customers.
- *Partnerships can create a more flexible, innovative and co-operative environment for developing rules better suited to the needs of the poor:* in doing so, partnerships may act in two ways: they either obtain to change the rules in order to enable further replication of the pilot project, or they may demonstrate the usefulness of changing the rule to the regulator or the policy-maker who might decide later on to modify that rule.
- *Partnerships can provide a flexible environment to adapt to new circumstances:* as a given regulatory environment evolves, the flexibility of partnerships should allow actors to adapt, thus minimising disruption and smoothing regulatory change.

#### ***What attributes are key to partnerships playing a role in regulation?***

While some of the partnerships have played several of the roles outlined above, others have not. While it is impossible to entirely distil why this is so, it is possible to identify two factors that do play a part in partnerships’ relative success, as discussed in *Section 4.2*:

- *Partnerships are more likely to be empowered to lift a regulatory constraint when the regulatory body is part of the partnership and acts at the same level:* the involvement of the regulatory body usually ensures a speedier and more direct approach for modifying potential regulatory obstacles to pro-poor service delivery. However, this does not mean that the regulator should become involved in the regulation of the partnership’s activities themselves.
- *Partnerships are more effective when partnership agreements are in place to regulate relations between actors:* overall partnerships can more effectively undertake the various roles outlined above when the partnership itself is formally defined. Partners clearly understand each other’s roles and responsibilities in addition to the partnership’s overall objectives. Where such formal agreement is not in place, some partners (and especially civil society partners) tend to fade away.

#### ***What impact have partnerships had on the performance of regulatory functions?***

More detailed analysis in *Section 5* reveals that partnerships as a whole have been able to have some influence on the performance of regulatory functions, in the following ways:

- *Price regulation:* partnerships have often been unable to influence tariff level regulation on a large scale, even though this may affect them substantially. Although, in some cases, they do play a consultative role in setting tariffs for the poor, it is more

usual for them to concentrate on developing alternative strategies for improved pro-poor tariff structures. In particular, some partnerships have been effective in reducing or waiving connection charges, or introducing better-suited billing regimes and payment methods.

- *Service quality regulation:* partnerships' focus on affecting quality regulation has remained limited and has largely depended on the approach taken at project level. In some cases, a variable approach at project level meant that the partnerships did not seek to experiment further. However, in rigid regulatory regimes without variable approaches to service quality regulation, partnerships did try to introduce variable service quality standards.
- *Coverage targets:* the majority of private sector operators involved in the BPD case studies have some contractually expressed incentives to extend service coverage, but some partnerships have also agreed coverage objectives specifically for their activities. Projects usually find it difficult to extend coverage to areas where other regulatory issues (such as a lack of land tenure) are a constraint. Partnerships have played an important role in adapting coverage obligations to an evolving reality, by focusing coverage targets on specific areas and setting more manageable short-term targets.

However, where regulation does not stipulate parallel extension of sanitation service coverage, it is unlikely that the partnership will provide such a service, therefore failing to tackle an issue that has a deep impact on poor people's daily lives.

- *Competition regulation:* even though, in most cases, the main service provider has some sort of service exclusivity, several partnerships have led to the establishment of independent providers with bulk supply agreements with the main operator. However, few partnerships have dealt with, or have explicitly considered, the impact of their activities on totally independent private providers. Furthermore, the activities of the partnerships have had very limited impact on competition regulation outside the sphere of pro-poor activities.
- *Environmental regulation:* in some cases, partnerships have been looking at alternative solutions for service provision when environmental regulation had increased the costs of service delivery to the poor. However, partnerships appear to be insufficiently pro-active in this area, even though the costs of environmental degradation may severely affect the poor in the long term.
- *Public health regulation:* in a number of cases, drinking water standards have been a constraint for delivering services to the poor and partnerships have worked on alleviating such constraints.

## 6.2 RECOMMENDATIONS

It is important to build upon these observations of the eight partnerships studied by the BPD Water and Sanitation Cluster in order to consider how regulatory and partnership design could be improved. These recommendations are therefore more speculative: they do not necessarily rely on hard facts (eight cases would not be sufficient to do so) but make proposals for the development of new approaches, both by partnerships and regulatory institutions.

### *How could regulation make better use of partnerships?*

Given the roles that partnerships can play in making regulation more pro-poor, institutions in charge of regulating the water sector should see partnerships as a key instrument for achieving their regulatory objectives. However, whether or not regulatory institutions interact with partnerships, and for which outcomes, depends largely on their own incentives: some may simply not concern themselves with partnerships because poor consumers are not their priority. As a result, a number of key implications for regulatory design can be drawn.

*Regulatory institutions should be designed in a way that makes them get involved with pro-poor regulation and see partnerships as a vector for this type of regulation:* In some respect, regulatory institutions are a product of the work of policy-makers. The onus is therefore on policy-makers to design institutional and regulatory frameworks so that institutions in charge of regulation have a clear incentive for addressing the needs of poor customers, know how to engage with partnerships and have the means to do so.

Whilst the most obvious way forward is by explicitly giving institutions in charge of regulation clear pro-poor objectives in their statutes, this might also be achieved by giving them the responsibility to promote an enabling environment for stakeholder engagement as well as to promote deeper relationships between the public, private and civil society sectors.

*There are many practical ways in which regulating agencies could facilitate the activities of partnerships and collaborate with them in order to improve regulation:* In practice, interacting with the partnerships could be taken to mean a number of things, with an increasing degree of involvement on the part of the regulatory institution:

- Ensuring an enabling environment for partnerships to develop in and providing access to support (for example, providing access to organisations that can assist with partnership formation and evolution, or building links with institutions in charge of delivering subsidies in order to provide partnerships with independent means to sustain themselves);
- Providing partnerships with adequate tools to sustain themselves, such as model contracts and access to external arbitration mechanisms;
- Facilitating the establishment of pro-poor partnerships (for example, by keeping updated on existing and potential organisations that may adequately represent civil society, which may be difficult for private actors to locate).

*Regulators should consider partnerships as a means to solve some of the difficulties associated with pro-poor regulation:* There are a number of tasks that regulatory institutions have difficulties carrying out, particularly when poor customers are involved. For example, the design of pro-poor tariff structures may require designing subsidy schemes, which raise issues related to finding ways of targeting such subsidies at the right type of population. This review has shown that in many cases, partnerships have been effective in targeting subsidies (particularly connection charge subsidies) – therefore, regulatory institutions may want to encourage the setting up of partnerships to solve such specific issues.

This attitude could apply to a large number of regulatory issues, such as:

- For piloting different and more flexible approaches to service delivery (in order to develop alternative service quality regulation) or negotiating alternative environmental quality or drinking water quality standards;
- For organising the market of independent small-scale providers to enable them to compete with the main provider on fair grounds and provide alternative services to poor customers who are not yet connected to the network.

*Regulating agencies should not intervene in the internal functioning of partnerships:* Regulatory institutions should not intervene in the partnerships to regulate relationships between partners. Indeed, the distinction between regulation of the overall environment and regulation of the partnership should remain clear (and help to avoid accusations of regulatory capture). This is why the regulatory body's direct participation in the partnership would not necessarily be appropriate, but its participation as an observer and interest in the partnership activities might be encouraged. The responsibility of the regulator is not to regulate the partnership: partners should regulate themselves on the basis of well-specified agreements, which should also allow for flexibility. External arbitration mechanisms should also be included, even though the intention should be to limit their use.

*Regulating agencies should not seek to copy approaches developed by partnerships in different contexts:* It is almost impossible that a regulatory body could simply copy an approach used by a pro-poor partnership in another context in order to achieve the same pro-poor objective. Partnerships can carry out the roles highlighted above because they engage a variety of stakeholders and leverage their complementary resources, looking to create local solutions on the basis of local information and conditions. Therefore, there are no short cuts: for example, in order to develop payment methods suited to the particular local context, a local partnership should be set up and work collectively on these issues rather than having a regulatory institution copy a solution developed elsewhere.

#### ***How could partnerships maximise their potential for making regulation more pro-poor?***

Partnerships are not always successful at improving how regulation functions. In many cases, it is because partnership members would not consider improving regulation as an explicit aim

and would consider their activities quite separate from the overall framework in which they operate, and particularly, from the regulatory framework. Failing to realise the impact and the powerful role the regulatory framework might play, they fall short of maximising their potential. Partnerships can be useful in making small improvements on the ground, but by taking a more macro view when framing and designing their activities, they could also contribute significantly to making regulation more pro-poor.

### ***So what does that imply for partnership design?***

*Partnerships should attempt to understand how the regulatory regime affects the delivery of services to the poor, and take this into account when designing their activities:* Partnerships should develop an understanding of how the regulatory framework in which they evolve affects the delivery of services to the poor. Specifically, they should aim to understand:

- What regulatory constraints or barriers may affect their planned activities; and
- What regulatory constraints or barriers are currently affecting the main service provider's ability to service the poor.

This should allow the partnership to either ensure that their activities will not be subject to a regulatory barrier, or to frame their objectives and activities in a way that directly addresses existing regulatory constraints, or tries to go around such constraints.

*Partnerships should actively seek to open dialogue with regulatory bodies:* Partnerships should seek dialogue with regulatory bodies early on in their activities. This dialogue should not be seen as a one-off event. It should evolve with the partnership activities and the development of an understanding of regulatory barriers affecting both the partnership and the delivery of services to the poor. This dialogue should have several objectives:

- To discuss the constraints that poor consumers face and ways of removing such constraints;
- To discuss what the partnership can specifically offer the regulatory institutions in terms of making regulation more pro-poor e.g. targeting of subsidies etc.;
- To discuss what regulatory barriers will have an impact on partnership activities, and whether the regulatory institution is willing to work with the partnership to look at ways to lift or bend such barriers;
- To discuss approaches for replication of partnership activities and formal mechanisms for dissemination of lessons learnt.

*The development of clear rules for the partnership (i.e. partnership self-regulation) can improve effectiveness in general, and regulation in particular:* A number of factors of partnership success have been identified during the course of this research, including the definition of clear objectives and explicit agreements on future activities of the partnerships (although these should be sufficiently flexible to allow for changes in circumstances). Such agreements are useful and should be developed as much as possible. To maximise their potential, agreements should include:

- Definition of partnership activities and key objectives;
- Definition of coverage and service delivery targets;
- The definition of the roles and responsibilities of each partner;
- Decision procedures and arbitration mechanisms;
- Internal reporting mechanisms to track activities (potentially very important to ensure that lessons learnt can be reported in a manner acceptable to the regulatory institution).

## **6.3 DIRECTIONS FOR FUTURE RESEARCH**

The eight BPD case studies have enabled many interesting conclusions to be drawn regarding the interaction between partnerships and the regulatory regimes within which they operate. These conclusions give rise to a further set of questions, which provide directions for future research. These further questions mostly relate to the appropriate timing and process for forming partnerships within the context of regulatory and institutional reform, and to the most appropriate make-up of those partnerships.

***In the context of private sector reform, when should partnerships be set up in order to maximise their potential for improving regulatory design?***

The exact role that partnerships can play in improving the regulatory process varies depending on the stage that private sector participation has reached. At first glance, because of their role in gathering and relaying information, it appears that partnerships should be created early in the process of introducing private sector participation in order to improve and inform contract preparation. While the involvement of private operators prior to bidding is problematic, dialogue could be encouraged between the public sector and civil society (and potentially donors), and the foundations for later partnerships laid. However, the potential for doing so may be limited, given the levels of uncertainty (and sometimes tension) often created during the process of introducing private sector participation.

This being said, interesting experiences carried out as part of the BPD initiative provide food for thought for alternative ways of involving partnerships at various stages of the privatisation process. For example, in South Africa partnerships were set up in the early stages of the private sector participation process, either by DWAF itself, who mandated the creation of a Project Implementation Agency with NGO partners in the **BoTT** contracts, or at the initiative of partners themselves in **KwaZulu-Natal**.

Although it might be difficult to go as far in other contexts, it appears that further experimentation with contractual forms which give a place to partnerships would be helpful. A useful first step in that direction could be to take account of the private sector operator's previous experience in creating and taking part in partnerships at the bidding stage and potentially, to grant points on this basis in the technical offers. There may be a number of issues with such a proposal: it may be, for example, that civil society organisations would resist what they may see as an association with private sector operators who wish to enhance their business interests. If this was the case, points allocated would need to focus on abilities being available in-house, rather than on strong links with local community-based organisations.

The question of when a partnership is created, and how this is woven into the process of reform, is an issue that should be further explored in a variety of settings. This should include where private sector participation is in the process of being introduced and where public-private partnerships have been in place for some time.

***What is the most appropriate make up of a partnership?***

While a whole variety of different arrangements can undoubtedly be considered as tri-sector partnerships, it still remains difficult to identify the optimum arrangement in terms of service delivery to the poor. This question is complicated by the fact that many influencing factors are likely to be location specific. It is, therefore, key that more research is carried out in two areas.

Firstly, what should the role and nature of civil society actors be? In many cases the exact nature of civil society's involvement has been an issue. In South Africa, relations with NGO partners have not always been very smooth. In both **KwaZulu-Natal** and **BoTT** case studies the NGO partner has become dissatisfied by its treatment more as a contractor than as a proper partner by other partnership actors. Therefore, questions regarding which civil society actors (NGO, community-based organisations or water committees) should be involved, how they should be involved (via a contract for services with performance targets or as partners) and under which type of regulatory regime remain open.

Secondly, the role of the regulatory body in the activities of the partnership will need to be developed in further work. Indeed, whilst it was concluded that regulatory bodies could play a number of useful roles in assisting the development of the activities of partnerships, there is very little experience on the ground to confirm this. It is, therefore, important to experiment in order to define how exactly the dialogue between regulatory institutions and partnerships should take place, in order to maintain real dialogue and achieve a certain level of accountability on both sides.

***Overall, partnerships should be more ambitious and consider their role in making regulation of water and sanitation services more pro-poor.***

Partnerships can play a very significant role in making regulation more pro-poor, that is if both partners and regulatory institutions understand what they can achieve and what needs to be done to maximise their potential. More often than not the fact that regulatory regimes do not provide an enabling environment for serving the poor is due to the heritage of the past. Responsibility for initiating and carrying out the necessary reforms does not only lie with regulatory institutions, but it should be a process involving all stakeholders. This process, one of practical research and experimentation, is one where partnerships, as an institutional form, have a paramount role to play.

