



**Leaky Propositions:
The Ontario Watertight Report**

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LEAKY PROPOSITIONS: THE ONTARIO WATERTIGHT REPORT

CUPE'S RESPONSE TO THE REPORT OF THE WATER STRATEGY EXPERT PANEL

INTRODUCTION

The Canadian Union of Public Employees brings experience and expertise to the discussion of long-term planning for water systems in several ways. Our union represents most municipal workers in Canada and in Ontario, and thereby represents the majority of the men and women who work in our water and wastewater systems.

We represent their pride in delivering safe, clean water to the public, and their interests as working people. CUPE as a whole – our members in all sectors – has made a commitment to defending public water systems through research, consultation and community organizing.

We are a part of community-based water watch coalitions across the country campaigning for high-quality public water systems.

CUPE is also part of a global labour and environmental network promoting water as a basic human right.

CUPE not only defends public water, but also promotes the protection of our water sources, conservation, democratic governance and adequate long-term funding of publicly owned and controlled water systems and resources.

Canada's water and wastewater systems are publicly delivered to meet basic human needs and to protect public health. Municipal water systems were one of the first major services to be publicly delivered in Canada – essential to our public health system. Water infrastructure is public precisely because the private sector could not be relied upon to deliver a quality service at a price that all residents could afford. But a belief that we can count on the private sector to manage our public water resources is gaining ground in government and policy circles.

Now it is 2005 and private interests increasingly view water as a source of profit. A May 2000 edition of Fortune Magazine foretold that water would be to the precious and lucrative commodity of the 21st century that oil was to the 20th century.

Commercialization of water is creeping up in private treatment and delivery of drinking water; bulk water exports to the United States, and bottling of municipally treated water for resale by private companies.

Meanwhile, estimates of Canada's public water infrastructure deficit across Canada vary, but are as high as \$50 billion. Regardless of the price tag, there is consensus that investment is required and difficult choices have to be made by all orders of government as they decide how best to manage Canada's fresh water resources. Privatization is presented to municipal

governments in a pretty package, their proponents eager to capitalize on the difficult budget binds municipal councils often find themselves in.

Private financing schemes, called public private partnerships (P3s), are coming under increasing scrutiny for their higher costs, compromised quality, secrecy, lack of public control and accountability, and other problems. Proposals are made in groupings of companies, without clear lines of accountability and usually with at least one international player. A consortium of financing, construction, and service companies, purports to give local officials *choice* and *flexibility*. P3s are appealing because they allow governments to show balanced budgets, but only by hiding debt and passing higher costs on to future generations.

Governments have a responsibility to ensure access to and protection of clean water as a basic human right and touchstone of environmental stewardship. Their choices have implications for this critical question: *who benefits?* From CUPE's point of view, the choice is as clear as public water itself – public investment must benefit people, communities and ecosystems, not international for-profit water companies.

The recent release of **Watertight: The Case for Change in Ontario's Water and Wastewater Sector** by the Water Strategy Expert Panel¹, should have marked a turning point in the confusion that has become the public water system of the Province of Ontario. Sadly, that is not the case for a number of reasons, which we will highlight in this brief letter.

OUR CONCERNS

CUPE has several serious and fundamental objections to the findings, recommendations, and philosophical outlook of the Water Strategy Expert Panel as presented in their report **Watertight: The Case for Change in Ontario's Water and Wastewater Sector**.

Our review found that the *Watertight* report is muddle-headed, patronizing, anti-democratic and fiscally irresponsible.

The roots of Ontario's growing water infrastructure problems were largely caused by policies put in place by the previous government in Ontario. These include:

- Further downloading of responsibility for water and wastewater services to the municipalities while they were already being saddled with other responsibilities;
- Cuts to the operating budget of OCWA and the MOE during the late 1990s;
- An aging infrastructure, growing infrastructure demands and increasing regulatory standards not matched by increasing public investment in this crucial element of our infrastructure.

It is very disturbing that the *Watertight* report advocates even more of the very same policies that have put Ontario's water infrastructure into this precarious situation:

- More downloading of costs onto municipalities
- Greater privatization and corporatization of the publicly-owned infrastructure

¹ Ontario, *Watertight: The Case for Change in Ontario's Water and Wastewater Services*, (Toronto: Queen's Printer 2005) (hereinafter referred to as "Watertight") at p. 33

- Heavy-handed interference with decision-making over public services.

The recommendations of the report are based on an unfounded ideological assumption that private business operation will always be more efficient than public operation. This is completely false, and particularly so in the case of public services.

REDUCES ACCOUNTABILITY

The report also betrays a deep distrust of the ability of elected officials at the municipal and provincial level to make the appropriate policy and financial decisions. This is reflected not only in the recommendations to corporatize water services, with minority representation on their boards by elected officials, but also to take responsibilities away from the Minister of the Environment with its recommendations in relation to OCWA and the proposed Ontario Water Board. This approach is patronizing towards Ontario's elected officials and is also profoundly anti-democratic.

Citizens will always look to their elected officials for leadership when it comes to the quality and adequacy of our public services. Whatever the administrative arrangements, elected officials will not be able to pass the buck when it comes to an emergency or public policy issue related to water. The experience of Walkerton and Kashechewan have clearly demonstrated that members of the public look to their political leaders to safeguard their water, no matter where the jurisdictional and administrative responsibilities lie.

In this context, it is surprising to see the report recommend that municipal water services be corporatized and that at least two-thirds of the directors of the board of a water services be drawn from private life with "any remainder" being appointments from municipal council (p. 34). Corporatization of water services in this direction would reduce responsibility, accountability and transparency for this essential public services. In many cases, the accountability and transparency of water services can be improved, but this is best done through direct public sector control, ownership and delivery rather than through a corporatized model.

Similarly, the proposal to create an Ontario Water Board is another exercise that would reduce direct accountability and control over regulatory aspects of water services.

Over and over, the report advocates "business planning", using a "business model" and having "business-oriented boards" and contracting out. The report also says that the onus should be on municipalities to explain why they are not using a corporatized model to deliver water services (p. 23). Despite all this emphasis, the report never really explains why the proposed "business planning" is superior for water services than other types of planning that currently take place, nor does it examine alternatives. Risk management should be a major factor in responsible financial and business planning of water services, but the report does not address this issue, except in its overriding faith that consolidation of municipal water services will lead to more effective risk management (p. 18).

We are certainly in favour of responsible financial planning for water services and other public services. But this report uses the term "business planning" etc. as a superficial and rhetorical buzzword without any real meaning – except to push towards further corporatization, privatization and contracting out of water services. This bias is demonstrated all through the

report. The report appears to frown on the fact that governance of water services in large cities sometimes responded to broader social and political concerns (p. 31) and simultaneously appears to applaud the fact that the board of EPCOR does not include any members of the council or of the municipal shareholder (p. 32).

A major argument of the report is that contracting out will allow water services to harness economies of scale and adopt innovative technologies. In particular, the report cites EPCOR's use of remote operation for water services and wastewater plants (p. 20). We find it troubling that the report advocates this practice without assurances of human operator backup, particularly in light of recent water emergencies.

It is remarkable that there is no discussion of why and how the favoured corporatization model would improve accountability, except because it would be handled through a "business-like corporate structure". There are different forms and aspects of accountability and this report barely delves into a discussion on the issue. It is clear that the emphasis of the report is on financial accountability, and not on the issues of political, social or environmental accountability.

There is some cursory acknowledgement of what is called the "principal-agent" problem in economics: that contractor agents don't share the same objectives and goals as the municipality. But the only recommendation for dealing with this problem is to commission and publish basic contract templates (p. 36). This does not address the deep-seated aspects of this problem.

Financial accountability can of course be improved in many instances. But this can be achieved much more simply and effectively through existing municipal structures (as mentioned on p. 11) instead of moving towards the elaborate, bureaucratic, costly and inappropriate corporatized structures proposed in the Watertight report.

The report similarly involves a generally superficial discussion of the role of subsidies and cross subsidies. There are many different aspects of subsidization and pricing that should have been discussed in a consistent and coherent manner. There is a brief acknowledgement that in some cases cross-subsidization may be warranted where the social costs of not providing the subsidy exceed the costs of the subsidy (p. 63). But in general the report is opposed to the use of subsidies and cross subsidies, without delving into the complexities of marginal rate pricing. At the same time – and without calling it a subsidy – the report calls for provincial trusteeship of water systems where the average unit costs exceed 2.5 times the provincial average (p. 52). Why 2.5 times the average? Why is a subsidy appropriate in these circumstances but not in others?

FINANCIALLY IRRESPONSIBLE APPROACH

We also find that the recommendations of the report are likely to be financially irresponsible to the Ontario public in a number of ways. The report advocates for increased commercial borrowing (p. 48, 51, 35) instead of advocating for continued low cost sources of financing, such as through municipal borrowing or through OSIFA. This is bound to be more expensive than municipal or provincial borrowing at the AAA and AA rate, and yet the report doesn't discuss this issue, despite the fact that financing costs should be very significant, with a projected \$34 billion in capital investment required over the next 15 years. It is not clear why the issue of access to pooled-debt financing through OSIFA was covered under the heading of "Grants and Subsidies"

in the report (p. 50). Perhaps improvements should be made to the operation of OSIFA, but this issue was not addressed in the report. We believe that OSIFA funding should be expanded to this sector, instead of restricted as is advocated in this report (p. 51).

It is also befuddling that the report argues for the use of municipal corporations to deliver water services, in full realization that they would be subject to the GST, while municipalities now receive a full rebate of the GST they pay. The report incorrectly states that municipalities are fully exempt from the GST (p. 58). There is a difference between being *GST exempt* and receiving a *GST rebate*. Provision of water services is GST exempt for customers, but municipalities were provided with a full rebate of the GST as part of the New Deal announced in the February 2004 Throne Speech. Water service corporations would also be subject to other taxes, such as income taxes.

These additional financing and taxation costs (together with the higher costs associated with the proposed business planning, operation of the water Board and the higher costs of contracting out and administration through a corporate structure) would cause a very significant cost increase for customers. These additional costs are unnecessary and will not be well-received by Ontarians at a time when there are very real needs in terms of improving our water infrastructure and services.

The estimates of savings “if the panel’s recommendations are adopted” in the final chapter (p. 75) are to put bluntly, highly disingenuous. All they are is an estimate of the benefits of making planned investments instead of emergency replacements, based on some heroic assumptions about the costs of emergency replacement relative to normal replacement. They have nothing to do with the relative costs of following the Panel’s recommendations of following a corporate model instead of increasing investment through other governance structures.

It should have been incumbent on the Panel to provide a comprehensive and reliable assessment of the relative costs of alternative governance models for delivery of water services. Since the Panel did not provide some of the relative costs for alternative governance models, here are some rough estimates.

If all municipal water services in Ontario converted to the corporatized utility model as is recommended in this report (p. 33) and contracted out for the \$34 billion in capital investment that is estimated to be required, the additional cost for the GST on capital investments alone would amount to \$2.38 billion over 15 years. Since municipal-type water services are GST exempt, the water service corporations would not be able to recoup the GST on the water services that they provide, but they would have to recoup these additional costs through increased rates charged to individual and business customers in Ontario. However, the business customers would not even be able to claim GST input tax credits on these costs because no GST would be explicitly charged.

This seems like a significant loss, but it only includes the estimated capital costs and not operating costs. Since this report recommends greater use of contracting out, the additional costs in this area would mount significantly since GST is applied on contracted services as well as most goods. The federal government would be at least \$2 billion richer, but individual Ontarians and Ontario businesses would be that much poorer if these recommendations were followed.

This is something that should give the Ontario government serious reservations about proceeding with the Watertight recommendations, but it is not all.

As part of move to the corporatized water services, the report advocates a shift to commercial financing of investments (p. 48, 51) and away from OSIFA's pooled debt financing. The cost of corporate financing invariably tends to be higher than lower cost municipal or pooled debt financing. For example the spread on longer term 20-25 year corporate issues (of large entities such as GTAA or Bell Cda) in comparison with the Ontario or OSIFA financing for a similar length is currently about 70 to 100 basis points. The increased cost for this higher financing cost would amount to \$70 to \$100 million per year on \$10 billion of debt. Over 15 years, these additional financing costs could amount to a total of \$1 billion to \$1.5 billion. Of course, the newly corporatized water companies would not have to swallow these increased costs, but they would be passed on to Ontario customers through full-cost recovery as mandated by SWSSA.

These key recommendations – that could on their own increase costs for Ontarians by more than \$3 - \$4 billion over the next 15 years – certainly do not strike us as wise public policy for Ontario.

It is interesting that the literature review in Annex D of the report (pp. 83-85) finds little definitive evidence about economies of scale and scope in water systems: economies of scale in plant are often offset by diseconomies of scale in distribution and collection networks. The World Bank study found wide ranges in economies of scale, even among small systems. Despite the lack of evidence that there would be economies of scale, the *Watertight* report has no hesitation in proposing consolidation of water services. Consolidation is exactly what the private sector wants to exploit greater profits from Ontario's water services. Consolidation might not serve the Ontario's municipalities and residents well, but it could be very beneficial for the private water companies.

OPENS ONTARIO TO RISKS UNDER INTERNATIONAL TRADE AGREEMENTS

The Watertight report does not once mention the implications of international trade agreements on the issue organization, structure and governance of water systems and on the other recommendations contained in the report. In particular, international trade agreements such as NAFTA and the WTO can have very different implications, depending on whether water and wastewater operations that are publicly owned and operated, or privately operated.

The interest of a private partner to a contract to design, build and/or operate a water operation would be an investment according to the NAFTA definition. A law, regulation, procedure, requirement or practice of the provincial government, municipal governments or regional authorities that might affect such a contract would be a measure under NAFTA and would be subject to the disciplines of the NAFTA regime.

Similarly, GATS requirements would also apply to water operations, unless the supply of water services is considered exempt from the application of the WTO agreement. Whatever claim to exempt status that water services have would be compromised by entering into a public-private partnership to deliver these services. It is sometimes assumed that public water services are exempt under the "government authority" or government procurement" exemptions in the GATS, but the key terms here are undefined and no one can say what is definitely exempt. If a

municipality decided to sell water services to another municipality, as is envisaged in the Watertight report, this could mean that their public water utility failed to meet the conditions of the GATS exemptions. The risks are much greater for a contract that involves the operation rather than just the design and build of a water supply system or water treatment plant.

Government measures that diminish the profitability of foreign investments through public private partnerships in this area could lead to a legal claim for damages. There have already been claims for damages initiated by multinational water service companies as a result of P3 contract disputes with provincial and national governments in South America under investment agreements similar to NAFTA.

While these cases would be brought against the federal government, the province and municipalities would be under very considerable pressure to comply with the requirements of NAFTA and the WTO to the detriment of provincial and municipal environmental, public health, and local economic development objectives.

ADDITIONAL CONCERNS

The Expert Panel makes several references to the Ontario Water Industry and frequently notes that the water industry in Ontario would be ready and able to step up to the plate to ensure that Ontario's water systems are maintained and operated to the highest standards. This is totally misleading in CUPE's view. Currently, there is no private water industry in operation in Ontario. The current systems are either operated directly by Municipal employees directly employed by their respective municipal bodies or operated by OCWA personal on behalf of the municipalities. Systems operated without municipal or OCWA involve are close to non-existent presently in Ontario. Ontario companies are unlikely to even benefit significantly from further moves to privatization and corporatization of our water services.

The **Watertight** Report suggests, that by creating a Water Board, the Ontario government will somehow be able to transfer its responsibility for the safe provision of drinking water to Ontario residents to the Water Board. This is simply an impossible outcome in CUPE's view based on our experience and reading of the tragic events of Walkerton. The Ontario government will be held accountable for water quality by the people of Ontario regardless of what agencies, or organizations are notionally created to take over these tremendous responsibility on behalf of the Ontario Government.

CUPE is vehemently opposed to what seems to be the clear bias of the expert panel in favour of privatization of water systems operations. The authors of **Watertight: The Case for Change in Ontario's Water and Wastewater Sector** repeatedly and throughout the report, make observations such as the following:

- "Contracting out has proven to be a good solution in many areas and should continue." (p.20)
- "efficient provisions of service, including existing or revised contracting possibilities;" (p.23)

- “To be cost-effective over the long term, contracting out the operation of water services requires water services to develop strong contract negotiation and contract management skills, as well as to seek bidders of good repute and long-term financial stability.” (p.36)
- “MOE will also have an entirely new responsibility in the scheme we propose: as trustee of water services (and in some instances, systems) declared “unsustainable” by the Water Board, as discussed in Chapter 7. Contracting for the operation of these while searching for better solutions will fit well with a stronger role for MOE in assessing new technologies, including those for treating water at the point of entry or point of use.” (p.44)
- “Once a water service has been deemed unsustainable, the Province should contract with a competent operator, through a bidding process where it is possible, to operate the assets. The Province should pay the operator all costs of running the water service above the capped amount collected from the customers.” (p.52)
- “This anticipated future for OCWA is in line with the belief that allowing system owners who want to contract out to choose among as many competent operators as possible is the best way to meet the public policy goal of providing safe, affordable water services in Ontario. This is particularly the case in places where local conditions invite competition – which would appear to include most communities in Ontario.” (p.72)

Contracting out is not the answer. CUPE’s research and real world experience shows this to be true for water services.

PRIVATIZATION FAILURES

Hamilton has become Canada’s most famous (or infamous) example of water and wastewater treatment privatization with disastrous consequences. Phillips United Water Corporation (PUWC) was awarded an untendered bid in 1994 in return for its promises of local economic development, new jobs and cost savings. What the community got instead was a workforce slashed in half with 18 months, a spill of 180 million litres of raw sewage into the harbour and the flooding of almost 200 homes. The company refused to accept any liability for the damage and the municipality was forced to pick up the tab. A legal settlement for claims between the private operator and the municipality several years later has been kept secret. In nine years, five different companies held the contract to manage Hamilton’s water – four of them foreign, two of them bankrupt, one of them Enron. When the contract came up for renewal in 2004 neither City Council nor the public was given complete financial accounting of the costs and profits shared by the municipality and corporation over the course of the contract. No performance report was made to Council in the 4 years prior to the end of the contract.

The story of Hamilton’s eventual decision to bring water and wastewater treatment back into direct municipal operation is instructive. Council was presented with a staff report in January 2004 that compared two possible courses of action – tendering another 10-year contract (with a 5 year extension) or bringing the service back in house (called the municipal model). Council chose to pursue the private option and instructed staff to issue an RFP and to draft a new contract that would overcome some of the public problems of the previous agreement. The three issues that had come under closest public scrutiny were liability in the case of another spill, liability insurance carried by the operator, and the private operator’s requirement to pay for

system maintenance and upkeep. The private operators and the City agreed that the municipality would take back responsibility for approximately \$11 million annually for electricity costs and sewage sludge disposal. Both issues represented potential problems for the private operator. Electricity costs are expected to rise as privatization of generation progresses over the next 10 years. Sewage sludge is likely to become a problem as the province moves on water source protection.

Given the experience with the contract and public sector comparator, the City anticipated bids between \$13 and \$16 million annually. American Water, the only proponent to submit a final bid, present a bid for \$39 million – three times the expected operating costs. They explained that they could deliver the service for \$13 million, including paying for electricity and sludge disposal, if the City would take over all liability and maintenance expenses. (McGuinness, Eric. "City prepares to take back water, sewer operations". *Hamilton Spectator*, September 14, 2004. P. A1)

"[Robin] McLean [a U.S. vice-president of American Water] said that the extra \$26 million was largely a premium for added risk the city wanted private operators to assume in the proposed new contract."

P3 proponents often point to the transfer of "risk" to the private sector as a key reason to pursue those kinds of arrangements. It is very illuminating to know that the private contractor was prepared to charge at least 200% over and above operating costs in order to assume additional risk. The information about allocation of risks (who has what liability) and the amount the private opponent is charging as a "premium" for their portion of the risk should be public in every private contract bid.

The City of Hamilton turned down American Water's high bid and disqualified the lower one. The City is resuming direct municipal service. The biggest RFP for private water/wastewater services on the continent in 2004 ended up back in the public hands.

Several of Canada's large municipalities have considered contracting out or privatizing some part of their water and wastewater systems since the Regional Municipality of Hamilton-Wentworth entered into a P3 contract with Philips Utilities in 1994. Most cities have decided to keep their water operations and facilities public.

Last year, Winnipeg City Council chose to proceed with a new publicly owned and operated water treatment plant, rather than involving private corporations in service provision. (*Canadian Union of Public Employees*, "P3 alert", July 2003. <http://cupe.ca/www/summer2003/5635>)

Halifax awarded a contract for harbour cleanup and sewage treatment to Suez in the fall of 2002, but backed out of the contract in 2003 when the French multinational refused to take responsibility for meeting environmental standards. The mayor admitted that cancelling the P3 deal would save millions of dollars on the project.

U.S. Filter, a subsidiary of the French corporation Veolia, owns and operates Moncton's sewage treatment plant. The company made an unsolicited bid to take over the whole system and the mayor was tempted by the prospect of taking a 20-year upgrading program off the City's books. A consultant hired to evaluate the options reported back in 2003 that Moncton can implement a

20-year upgrading program more economically itself than through the proposed P3 arrangement over that same period.

Late in 2002, Toronto City Council turned down a proposal for transferring its water and wastewater system to an arms-length board.

In 2000, the Greater Vancouver Regional District decided against a P3 arrangement for the operation of a new water filtration plant. Council was concerned that privatization of the service would open it up to international trade agreements.

Saint John, New Brunswick chose the public route. So did Kamloops in British Columbia in 2001.

These examples demonstrate that it cannot be assumed that contracting out operations is the best municipal option. Each municipality has to weigh the supposed advantages of private operations against the advantages of public operation. Major Canadian municipalities are coming to the conclusion that public service delivery is better.

PROBLEMS AROUND THE WORLD

The biggest growth areas for all of the large multi-national water companies in the past decade have been in the developing world – Latin America, Africa and South East Asia. In far too many countries around the world there is insufficient access to potable water and inadequate sewage systems for public health and safety. There, governments do not have the tax base to build water and wastewater infrastructure. The International Monetary Fund and the World Bank made funding for the development of infrastructure contingent on encouraging and allowing private investment. These practices have not been without controversy. Private companies are in business to make money. Having foreign (usually European) multinationals making money selling water – a necessity of life – to people too poor to buy it has led to a number of conflicts. It has also turned out not to be as profitable as the big operators had hoped.

David Hall of the Public Services International Research Unit (PSIRU) presented a paper to the 2003 World Water Forum in Kyoto reporting on a change in this trend. The big companies are withdrawing from the developing world because the returns on investment are too low or even non-existent. He examines the very recent experiences of Suez, Vivendi (now Veolia), Saur and RWE (American Water in Ontario) in places as diverse as Turkey, Peru, Estonia, Manila and Morocco. He explains that these giant private firms are now looking in two new directions: a) focusing on expanding markets in North America and Europe; and b) seeking to reduce risks and guarantee profits in governments contracts. (*Hall, David. Water Multinationals – No longer business as usual. Public Services International Research Unit, University of Greenwich. March 2003.*)

We see that both of these trends are true in Ontario.

Proponents of various private and P3 arrangements for water systems will often point to the United States to convince Canadians that this can all work very well. But there are problems in the U.S. as well.

Atlanta ended its contract with United Water, a subsidiary of Suez, in 2003, after four years of private operation proved that the company was not keeping its promises. It was the biggest water contract in the U.S.

New Orleans spent five years analyzing whether or not it would be advantageous to privatize its water/wastewater system and decided in early 2004 that it could save more through its own innovations and initiatives if it retained public control. The big companies spent millions promoting their side of the story in both cities.

Some American cities, like Stockton Illinois and Lexington Kentucky, have had to spend millions fighting these same big water companies. The public and politicians in those cities, dissatisfied with private operators, want to bring water back into the public domain but have ended up in expensive, protracted court and public relations battles as the multi-nationals try to prevent such a move. American Water spent over \$6 million on public relations and legal fees fighting against public buy-outs of its subsidiaries in Chatanooga and Peoria Illinois – just two cities. (*Public Citizen. Reclaiming Public Assets: From Private to Public Ownership of Waterworks. Washington. 2002.*)

As in Canada and around the world, the participation of the private sector in water systems in the U.S.A. is often problematic.

One of the most significant features of the international water industry is rapid corporate concentration over the past decade. The industry is now a global oligopoly with only six major firms in limited competition with each other: Suez (United Water), Veolia (formerly Vivendi), RWE – AG (American Water), Bechtel, United Utilities and Saur. Only about 4 of these firms have any significant presence in North American and are likely to be active in the Canadian market.

CUPE SUPPORTS THE POSITION OF THE CANADIAN ENVIRONMENTAL LAW ASSOCIATION (CELA)

CUPE supports the following comments drawn from the Canadian Environmental Law Association (CELA) response **Watertight: The Case for Change in Ontario's Water and Wastewater Sector**:

“(a) GOVERNANCE THROUGH A CORPORATIZED UTILITY MODEL

The Panel recommends municipalities be allowed to form corporations to deliver water and wastewater services. According to the Panel "the corporatized utility models offers the greatest benefits in terms of governance, transparency, financial sustainability and accountability" (*Watertight*, p. 33). The Panel concludes by stating that municipalities should be able to organize their water and waste water services as corporations for either non-profit under Part III of the *Ontario Corporations Act*, or for profit under the *Ontario Business Corporations Act* (p. 33).

The Panel cites EPCOR, which is owned by the public, its common shareholder being the City of Edmonton as a model example of a corporatized utility model. However, a recent study of EPCOR by the Parkland Institute (University of Alberta, 2005) has raised serious concerns about EPCOR's accountability. The study found that "EPCOR operates at the corporate end of the accountability spectrum; its primary accountably concern is in its relation to the shareholders and growth" (p. 2). Furthermore, the study concludes,

On EPCOR's board there is a lack of participation and oversight by City Council and other stakeholders. The utilities EPCOR controls are no longer the subject of democratic decision-making and their is no requirement for public transparency. The City can not set the operational priorities like environmental protection or wisely managed cost-efficient development. Finally, direct accountability to the public has been curtailed, as the corporatized utilities model is no longer subject to the *Freedom of Information and Protection of Privacy Act*. Key documents governing EPCOR's accountability with the City are unavailable to the public (p. 2).

The issue of good governance in relation to the provision of water services was also examined in a report jointly commissioned by the Federation of Canadian Municipalities and the University of Toronto's Munk Centre for International Studies entitled *Good Governance in Restructuring Water Supply: A Handbook* (Bakker, K., undated). The report echoes a number of concerns highlighted by the Parkland Institute's study regarding the use of a corporatized model for the provision of municipal water services. The report states that the disadvantages of a corporatized public utility model include potentially higher capital costs, a weakening of accountability, commercial confidentiality limits on access to information by consumers and politicians as well as an incompatibility with some public services mandates. Moreover the report also notes that

corporatization is often a precursor to full privatization and is sometimes recommended as an intermediate step prior to privatization by international lending agencies such as the World Bank (p. 2, 12).

In view of the foregoing CELA takes issue with the Panel's conclusion that the corporatized utility model offers the greatest benefit in terms of governance, financial sustainability and accountability. The research done by academic and public policy research institutions suggest that, in fact, a corporatized utility model would greatly reduce accountability and transparency. Consequently, CELA does not support the Panel's conclusion that the corporatized utility model provides the best governance structure to manage and operate water systems in the province.

(b) CREATION OF WATER BOARD

(i) Establishment of Ontario Water Board unnecessary

The Panel recommends the creation of an Ontario Water Board to carry out many of the functions delegated to municipalities under the *Sustainable Water and Sewage Services Act*, ("SWSSA") which was enacted by the Ontario government in December 2002.

The Panel suggests that this new body could be created by amending the SWSSA or by a separate statute or through an omnibus act that could include all the legislative changes required by the recommendation of its report (p. 39). The Ontario Water Board would, among other things, be required to analyze and rule on the water services "business plans" prepared by municipalities. The business plans would bring together all the local information and planning done under the SWSSA and look at the planning area as a whole and not just an individual municipality (Ibid. p. 38-39). These plans would look for options of working with neighbouring municipalities to save further costs (Ibid. p. 22). The Ontario Water Board would also require water services to provide information annually about their compliance with its regulatory regime and their financial services performance.

The Panel has stated that this business planning process is "not intended to happen in addition to full cost recovery plans required by SWSSA. Instead it would in effect, bring together all the local information and planning done to date and integrate it at a higher level" (p. 22). The Panel notes that systems on a combined basis will reduce the costs of preparing full cost recovery plans and provide more integrated solutions and better outcomes (p. 21). However, the panel has failed to provide any evidence to suggest that municipalities are unable or unwilling to do this under the present regulatory framework. Indeed, the Panel notes that full cost recovery planning and other regulatory instruments may well get the job done. The Panel also notes in its report that a number of municipalities, such as Perth and Sudbury have already completed the transition to full cost recovery (p. 49).

If the Panel's concern is simply that some municipalities may fail to address the additional savings that could be derived from consolidating waters systems, it could have

simply recommended that the regulations passed under the SWSSA specifically require this information be provided in the full cost recovery plan. This would avoid the need to create an elaborate new regulatory scheme and a new institutional body to address cost savings which municipalities are already statutorily required to undertake under the SWSSA.² It should be noted that under section 5 of the SWSSA the Minister has authority to require two or more municipalities to prepare a joint full cost and cost recovery reports.³ Thus, under the SWSSA the Minister can, where appropriate, promote economies of scale by requiring municipalities work together in preparing their reports.

Economies of scale can be addressed in other ways such as by bulk purchasing policies, regional transport of treatment chemicals and equipment, regional training and inspections, appropriate treatment technologies and energy efficiencies in operations. All of these should be applied to the problems of small systems and remote communities in the North. The Ontario Clean Water Agency (OCWA) was originally developed to provide such assistance and expertise to small operators. The need for this assistance has since grown as these communities work to comply with Ontario's new drinking water and SWSSA laws.

It is CELA's view that the creation of a new Ontario Water Board is unwarranted and would only add unnecessary complexity and create duplicate the roles and responsibilities under the SWSSA.

(ii) Creation of Ontario Water Board would reduce political accountability

The Panel states in its report that "a considerable burden has been placed on the Minister under the SWSSA, which would, in most other jurisdictions be placed on an arm's length regulatory body" (p. 38).

It should be noted, however, that it was precisely this type of organizational structure that was rejected by Mr. Justice O'Connor in his Part 2 report. For example, in his discussion about the need for a Drinking Water Branch, Mr. Justice O'Connor notes in his report that locating the Drinking Water Branch within the Ministry of Environment can be useful in maintaining accountability. The report states that a

...branch that is assigned the responsibility of drinking water will help eliminate confusion over who is responsible for what. However, since the branch remains under the direct authority of the minister, direct political accountability remains intact as well. *This to be contrasted*

² Subsection 4(5) of the SWSSA states that full cost recovery reports must contain information on the inventory and management plan for the infrastructure need to provide water services, an assessment of the full cost of providing the water services and revenue obtain to provide them and any other matter specified by regulation.

³ Subsection 5(1) of the SWSSA allows the Minister to require two or more municipalities to provide a joint report on full cost. Subsection 11 of the SWSSA allows the Minister to require two or more municipalities to provide a report on full cost recovery.

with a commission or other arm's-length entity that enables the government of the day to be shielded to some extent from responsibility (emphasis added) (p. 415).

Although Justice O'Connor's comments were directed to the relation the institutional arrangements under the *Safe Drinking Water Act*, CELA believes his comments are equally applicable in relation to the regulatory framework governing the financing and operation of water systems in Ontario.

The Panel fails to recognize that the responsibility placed on the Minister under the SWSSA to approve the full cost and cost recovery reports constitutes the most essential and effective means of ensuring government oversight and political accountability for the provision of water services to Ontarians. In contrast, the delegation of the Minister's responsibilities under the SWSSA to an arms-length regulatory body would seriously undermine political accountability. It may also render a number of statutes which provide for transparency and accountability in the government's decision making process, such as the Ontario *Freedom of Information and Protection of Privacy Act*, the *Municipal Freedom of Information and Protection of Privacy Act* and the *Ombudsman Act* inapplicable.

(iii) Creation of the Ontario Water Board would not address need for adequate resourcing

The Panel is of the view that the Ontario Water Board can only be effective if the number of water services in Ontario falls. According to the Panel no "regulator could deal effectively or in a timely fashion with plans submitted by the hundreds of water services that currently exists" (p. 39). It appears that one of the reasons prompting the Panel to recommend the creation of the Ontario Water Board was a concern about the availability of government resources to review cost recovery plans. It is important to note however, that the establishment of a new institutional body will not address the issue of adequate resourcing. If the Panel was concerned about the lack of adequate resourcing to review the plans submitted by water services, the appropriate recommendation would have been to request that the provincial government be provided with the adequate resources to match its regulatory responsibility.

(iv) Ontario Water Board would lack retention of expertise and experience in water services

The Panel recommends that support for the Board be provided "mainly by non-permanent staff members" (p. 40). The Panel recognizes that a small core of staff would be needed however, these members would carry out primarily administrative duties. With respect to other needs, such as in the regulation, performance measurement, business, planning, finance and law, the Panel categorically rejects the creation of a large permanent bureaucracy. Instead, the Panel recommends that to the extent possible, the Board should engage staff on contract from the private and academic worlds on secondment to the public service of the Province and Ontario municipalities.

While the Panel's proposed institutional arrangement may create lucrative consulting opportunities for those in the private and academic world, it does not serve to ensure the effective oversight of water systems in the province. It is CELA's view that the Panel's proposed institutional arrangements fail to ensure the development of institutional knowledge experience, technical expertise, and experience on the part of those delegated the responsibility for overseeing water systems in the province. Furthermore, the creation of a body staffed by non-permanent members reduces accountability for the management of water systems, since there would be no long-term oversight. CELA is therefore strongly opposed to the creation of Ontario Water Board as well as the proposed institutional arrangements of this Board.

(c) INSPECTIONS AND ENFORCEMENT

The Panel has raised the question whether the inspections and enforcement functions should reside with the Ministry of Environment. It is the Panel view that that other possibilities be considered, such as a regulatory body funded by a sector participants. The Panel cites the Technical Standards and Safety Authority ("TSSA") as an example of an "arms-length" entity that could be considered. The Panel has also suggested that there should be a move from the detailed command and control over inputs and processes to a focus on desired results (p. 40). It should be noted that similar recommendations were advocated by some parties at the Walkerton Inquiry but these recommendations were categorically rejected Mr. Justice O'Connor.

In his report, Mr. Justice O'Connor states:

Although the general recommendation of movement away from a command and control model to a more integrated, co-operative approach that would encourage potential polluters to change their ways may be useful for some aspects of the MOE's mandate, including the abatement of pollution, it is not in my view appropriate for the regulation of drinking water safety (p. 68).

According to Mr. Justice O'Connor, "given the public importance of safe drinking water system, safety can best be ensured when the government is directly involved in regulation and oversight" (p. 69).

A key factor underlying the Panel's recommendation to devolve the inspection and enforcement functions to an arms-length body is to ensure that "inspection functions are insulated from the provincial budget process" (p. 43). However, as Mr. Justice O'Connor notes the other effect of independence from political influence, is a "decrease in political accountability. If responsibility is passed on to a commission, the government will find it easier to deflect blame when something goes wrong. So long as processes are in place to promote transparency, political accountability can be a powerful democratic tool" (Part 2 Report, p. 414).

The Panel's recommendation in regards to inspection and enforcement are clearly at odds with Mr. Justice O'Connor's recommendations in his Part Two Report of the Walkerton Inquiry. Moreover, the Panel fails to provide any compelling evidence why there is a need to fundamentally depart from Mr. Justice O'Connor's recommendations regarding inspections and enforcement of drinking water systems. CELA is of the firm view that the inspection and enforcement functions over water systems should continue to reside with the Ontario Ministry of Environment.

(d) THE ROLE OF OCWA

In his Part Two reports, Justice O'Connor notes that the primary role of the Ontario Clean Water Agency ("OCWA") "remains the same: to operate water systems under contract with the municipal owner" (p. 294-295). Mr. Justice O'Connor observed that "OCWA offers an important alternative to other external operating agencies, especially for small or remote municipalities that have limited options to operate their own water systems or to pursue regionalization. Also OCWA is a useful vehicle for the provincial government in circumstances where it finds it necessary to mandate the restructuring of "non viable" municipal systems or to respond to emergency situations, as in the case of Walkerton" (p. 294-295). Consequently, Mr. Justice O'Connor emphasized that he saw "OCWA continuing to play an important role in the province's water industry" (p. 295).

In view of the above, CELA was very surprised the *Watertight* Report would recommend that the government take measures to significantly alter the structure, mandate and role of OCWA. The report even considers the prospect that OCWA could be "wound down" or "sold off -either to a private sector firm or to a government owned company seeking to enter or expand into the Ontario Water sector " (p. 69-72). These recommendations are fundamentally at odds with the recommendations in the Part Two Report of the Walkerton Inquiry.

CELA also takes issue with the premise in the *Watertight* Report that "all of Ontario's water service providers can stretch their resources to cope with local or nearby failures" (p. 74). The nature of recent emergencies in Ontario and elsewhere serve to highlight the fact that the Walkerton tragedy cannot be regarded as a unique event. A neighbouring community would not have had the expertise or the resources to replace the entire contaminated water infrastructure of the Town of Walkerton, an activity that took well over a year. Nor are there any near neighbours to help with the unfolding disaster on the Kashechewan Reserve that has resulted in the relocation of an entire community. Both of these tragedies underscore the importance having a body such as OCWA to deal with emergency response.

CELA recommends that OCWA emergency response mandate be retained and that its role be expanded to also address emergency prevention. In particular, there needs to be a focus on innovative treatment methods for drinking water. Replacing chlorine based water treatment with activated carbon and/or ultraviolet treatment, for example, will

eliminate more pathogens as well as carcinogenic by-products of chlorination, trihalomethane and other harmful substances from drinking water. OCWA should develop expertise in these and other alternative treatment methods and best practices.

The report that CELA commissioned for the Walkerton Inquiry *Financial Management of Municipal Water Systems in Ontario* prepared on by consultants C. N. Watson and Associates Ltd. (2001) highlights a number of advantages governments have over the private sector in financing of infrastructure. In particular, loans are available at better rates for the public sector in comparison to the private sector. The report also included guidance on how amortising capital expenses and planning for infrastructure over longer timeframes have proven to assist water and wastewater services to achieve greater self-sufficiency while planning for routine infrastructure renewal.”

[Canadian Environmental Law Association, Comments of the Canadian Environmental Law Association Regarding *Watertight: The Case for change in Ontario's water and wastewater sector*. November 22, 2005. Toronto.]

PUBLICLY FINANCING INFRASTRUCTURE

Both Canadian and American municipalities have concluded that public ownership and operation is the preferred route for building strong, efficient and sustainable community services. But how can they finance municipal infrastructure?

Despite debt hysteria, the ratio of debt to GDP is low and falling at both federal and provincial levels. Provincial and municipal governments have the ability and the “room” for significantly more borrowing to finance infrastructure. Debt charges for municipalities in Ontario, for example, were 3.5% of revenues in 2001, well-below provincial guidelines. Meanwhile, grants from other orders of government to municipalities have declined over the past 10 years. Municipal debt charges have also declined.

While there is no one-size-fits-all solution for Canadian communities, there are a host of cost-effective alternatives to P3s that protect the public interest. Along with investment from revenue and reserves, infrastructure construction and refurbishment could be funded through debt financing. Municipalities have an opportunity to arrange debt financing that maximizes benefits and services to the public while minimizing costs, thanks to having access to the lowest available borrowing rates.

Along with lower cost direct government borrowing, municipalities can pursue low; public bonds (infrastructure bonds, tax-exempt bonds); pooled debt financing such as through OSIFA; subsidies to municipalities from other orders of government; establishing Crown corporations to channel public investments in infrastructure; and public interest companies.

Municipalities can also create efficiencies and cost-saving by entering into *public-public-partnerships* with other municipalities. These will enjoy the advantages of public financing, maintain clear public accountability, and have public service objectives as their primary motivations, and can also overcome many of the financial problems faced by smaller municipalities (or even large ones) undertaking the upgrading and management of water systems on their own.

Pension funds have been, could be and should be a major source of capital for publicly owned and controlled infrastructure. Unfortunately, both the Ontario Municipal Employees Retirement System (OMERS) and the Canada Pension Plan Investment Board are actively investing in P3 infrastructure. Public investment vehicles are appropriate and reliable channels for pensions fund investment in infrastructure.

Private sector financing, through long-term leasebacks or other arrangements, is costly given the higher cost of borrowing to start with, and of course, the need to generate a profit. Large global water corporations are among the richest in the world with revenue in the realm of \$25 billion (Veolia) and \$40 billion (Suez/Ondeo) annually.

Keeping in public not only reduces direct and indirect costs, it improves quality and strengthens communities, it is the only way to protect government’s ability to regulate in the public interest and made sovereign policy choices. Public ownership acts as a bulwark against the danger of growing legal claims to investor “rights” by trans-national corporations under international trade agreements. It was concerns about the powerful “investor-state” provisions, and other provisions of the North America Free Trade Agreement (NAFTA), which led Vancouver’s city

council to decide against pursuing the P3 option for its Seymour water filtration water plant in 2001.

Only a few of the tools that have been used successfully to leverage public financing for infrastructure in the past are discussed here. They remain viable options for financing and maintaining municipal control over operations at a reasonable cost. We don't need to give away control over precious resources and threaten public health in order to fund water and wastewater infrastructure. There are prudent, rational public solutions to these challenges.

Any of these measures would more effectively achieve the \$8 billion in savings estimated by the report (p. 75) without the more than \$3 billion in additional costs from following the corporatization model proposed in the *Watertight* report.

Public investment forms the backbone of CUPE's plan for keeping water infrastructure and services in community hands. Other key features of our plan include national standards, source protection and removing water and water services entirely from trade agreements. The country desperately needs an overall national strategy for source protection and water conservation, including pan-Canadian standards for drinking water and water operator education and training, controlling water "takings" by water bottling companies and other industries, banning outright large-scale water exports, reducing and eliminating industrial and landfill contamination of lakes, streams, rivers and water tables, and preserving wetlands

CONCLUSIONS

Based on the foregoing analysis of **Watertight: The Case for Change in Ontario's Water and Wastewater Sector**, CUPE would suggest that the recommendations of the Expert Panel would take the Ontario Government in a direction on water policy that is fraught with peril and would lead to a whole scale reduction in accountability, safety and public trust on perhaps the most critical policy/public safety issue in the Minister's portfolio of responsibility.

What is needed from the Ontario government is a strong public commitment to having publicly owned and operated water resources and systems confirmed as the most critical public good in Ontario and that the delivery of water services should remain (and where necessary, be reinstated) as the highest public service priority of the Government of Ontario.

Public financing governance and service delivery provides the means of ensuring that our water systems are financially sustainable, that water is affordable and that we have the control to implement achievable, practical solutions today and in to the future.

Ensuring access to water and high water quality, adopting new technologies, accessing expertise, preventing fragmentation, increasing efficiency, planning for adequate and fair financing, enhancing public accountability and involvement, and keeping water and wastewater services in the Canadian hands are all reasons why public financing and control is a more responsible choice than privatization in the provision of water and wastewater services for the Province of Ontario.

Water is essential to life - no one should be able to control it or expropriate it for profit. The right to water has been recognized internationally through the United Nations Committee on

Economic, Social and Cultural Rights. The world's water companies would like to see water regarded as a human need, enabling them to control and sell water to the highest bidder for profit.

The Ontario government should support the real interests of the people of Ontario on this crucial issue – and not pander to the narrow interests of the multinational water companies.

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