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An Independent Regulatory Framework for Water and Waste Water in Maharashtra

A need clearly exists for major reforms aimed at a sustainable improvement in water and sanitation services in Maharashtra, as in other Indian states. Without a change in basic approach, policies, and institutional framework, it will be impossible for the state and local governments to provide universal access to these services, especially for the poor, and ensure their sustainability. The state Water Supply and Sanitation Department (WSSD) appointed the Sukthankar Committee to develop a roadmap for improvement in these sectors. The committee recommended setting up an independent entity to regulate water tariffs and service standards. This Project Note describes the rationale for and proposed functions of this new state-level entity, considerations for tariff determination, and the community role in regulation.

Maharashtra is the most urbanized state in India. While its water and sanitation coverage is better than most other Indian states, service levels in most areas are grossly inadequate. Some areas experience severe water scarcity, especially in summer months, and water must be brought in by tanker trucks. In rural areas, only 55 percent of the villages and 65 percent of the neighborhoods have a supply of more than 40 liters per capita per day (lpcd). Of the 15 municipal corporations, only Mumbai and two others meet the urban norm of 177 lpcd. Service is intermittent everywhere. Few cities have properly planned drain and sewer lines; nearly two thirds do not have an underground drainage system. This situation contributes to the pollution of the water supply. On average, 39 percent of rural and 10 percent of urban water samples are contaminated. Adverse consequences on health and economic development are widely recognized.

Given the poor level of service, citizens are unwilling to pay for it. This leads to a vicious cycle of under performance for both sectors. Since water tariff collection is low, and user fees are not collected for sanitation, cities must use general revenues for operations and maintenance (O&M). Mumbai is the only city in the state with a surplus in its water and sewerage account. Financially-strapped cities underfund maintenance and prior investments decline in value. Thus, physical leakage is now estimated at 40 to 55 percent of piped water supply. Forty three urban bodies in Maharashtra declined to take over new water projects built by the Maharashtra Jeevan Pradhikaran (MJP), a state-level water and sewerage board, largely because they do not have the financial and technical resources required to maintain them. With rapidly increasing population and industrialization, the current system is neither economically nor environmentally sustainable.

The Need for Regulation

The core problem, according to the WSSD and Sukthankar Committee analysis, is that there is no emphasis on consumer preferences and source and system sustainability in the old supply-driven approach. A mutual self-help, community orientation is appropriate for rural areas, while a

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commercial orientation is best for urban areas. The key challenges while moving to a market driven model in the urban sector are: to instill a paying culture among users; to instill a customer focus among utility managers; and to increase transparency in operations.

Because water is viewed as a gift from God, it has been assumed that it would be priced cheaply. Declining investment in the sector is traced to the lack of reasonable and sustainable tariffs. Almost all urban bodies in Maharashtra have tariffs that do not cover costs; cost recovery of only O&M varies from 5 to 83 percent. The rates of many local authorities do not meet minimums set by the state, nor are they revised once fixed. Low collections, as low as 25 percent in rural areas and ranging from 25 to 90 percent in urban areas, and inadequate metering exacerbate the problem. Residents need to be convinced that tap water and sewage connections are services that ought to be paid for, that water is a precious commodity. The lack of a customer focus and poor service result in people's unwillingness to pay.

The main bottleneck is the lack of appropriate institutional arrangements that results in a lack of transparency and accountability. Traditionally, the water supply and sanitation sector evolved as a state-dominated sector. The state built transmission lines, service reservoirs, large pumping stations, distribution networks, and large treatment plants. Current incentives lead officials to focus on large, politically appealing, augmentation projects; there are no incentives to focus on operational and economic efficiency. Thus, skewed investment patterns result in the neglect of maintenance. The parastatal agency, the MJP, which finances, designs, and builds these facilities, also handles policy, regulation, and operations of residential water supply. Another state agency, the Maharashtra Industrial Development Corporation (MIDC), runs a separate water supply for industries, eliminating the opportunity for cross subsidization between residential and industrial users. Little attention is paid to waste water. Municipal corporations and urban bodies have been given responsibility for O&M of systems that they did not design and given the right to set and collect tariffs. Local politicians promise free water or low water tariffs to improve their election prospects. Often government institutions are working at cross-purposes, many with contradictory roles, and political interference is common. A major restructuring is necessary if the goal of universal, sustainable access is to be achieved.

Proposed New Independent Regulatory Commission

The Sukthankar Committee strongly recommended the establishment of an independent Maharashtra Water and Waste Water Regulatory Commission (MWRC) to achieve substantial and far reaching reforms in the water sector in Maharashtra. Its primary objectives would be to determine a range of tariffs for water and waste water, to protect consumers from abuse by the new City/Regional Water Supply Entities (CWSEs) which will have monopoly power in the licensed areas, to create a conducive environment for attracting viable investments in the CWSEs to improve service quality, and to promote economic efficiency in the sector. It will serve as a catalyst for reforms by removing arbitrary decisions in setting tariffs and service standards, which will help lead to new sector investments.

Key Committees Studying Water and Sanitation Sector Reform

The Maharashtra Water Supply and Sanitation Department appointed a committee under the chairmanship of Mr. D.M. Sukthankar in January 2000 to prepare a roadmap for the improved provision of water and sewerage throughout the state. Other committee members were Mr. Venkat Chary of the Maharashtra Electricity Regulatory Commission; Mr. Nasser Munjee of the Infrastructure Development Finance Company (IDFC); Mr. B.V. Rotkar, formerly of the MJP; and Mr. V.P. Raja and Mr. S. Prabhakaran of WSSD. The committee's assignment was to study rural and urban water supply schemes and master plans and to make suggestions for improved performance of existing assets including institutional and tariff restructuring, private sector participation, creating a competitive environment for water and sewerage services, strengthening the MJP, and improving groundwater resource management.

In December 1999, the WSSD set up a Core Group of officers from the Government of Maharashtra, MJP, the Groundwater Survey and Development Agency, the USAID FIRE project, IDFC, and Infrastructure Leasing and Financial Services to prepare a roadmap for encouraging private sector participation in the sector. The activities of the Core Group dovetailed with those of the Sukthankar Committee. The USAID FIRE project managed the Core Group, the technical secretariat of the Sukthankar Committee. This group sent the draft framework, including a proposed act to set up the new regulatory commission, to all urban local bodies in the state for their review and comments.

The committee submitted the *Sukthankar Committee Report on Operation, Maintenance and Management of Rural and Urban Water Supply Schemes* to the state government for review on February 28, 2001.

The committee believes that this independent regulatory framework will facilitate the restructuring of existing service providers indirectly through monitoring tariff determination and service quality. The MWRC will facilitate increased transparency, accountability, and a consumer orientation by requiring public consultation and generation of public information.

The MWRC would be responsible for regulating both water supply and waste water disposal services. Specifically, its **key functions** would include:

1. *Regulation of the quality of service* being provided by local bodies and to be provided by the licensed entities, or those working under contract with the local body, or the MIDC. Service quality would include quality of water supplied, quantity and hours of supply, reliability and continuity of supply, timely redress of consumer grievances, service coverage, and waste water disposal according to agreed standards.

2. *Economic regulation of tariffs* to be charged by the service providers (local bodies, CWSEs, other service agencies such as MIDC, MJP, City and Industrial Corporation, and private sector entities.) The tariffs will be determined on the basis of a fair charge to customers and to ensure the viability of service providers.

3. *Issue and regulation of licenses* to the proposed CWSEs, in association with one or more local bodies or other agencies such as the MJP and the MIDC. The MWRC will issue licenses to all new entrants, including private operators, in the sector after following a transparent procedure.

4. *Coordination with other regulators for environmental regulation*, especially related to drinking water quality and waste water disposal standards. The Department of Health sets standards for drinking water quality and the Maharashtra Pollution Control Board, under the Environment Department, regulates waste water disposal. The MWRC will coordinate with these regulators enforcing standards to the extent they pertain to tariff setting.

5. *Collection and dissemination of sector information* to enable the MWRC to establish good regulations and to assist different interest groups, especially consumer councils, to recognize improprieties by the local water supply entities. Identification of relevant information and its independent collection and dissemination will be the key to effective regulation.

MWRC's **jurisdiction** will be all local bodies, autonomous service providers (the CWSEs), and private sector water service providers operating under long-term contracts with local bodies, MIDC, the MJP, and rural local bodies. Single village schemes, however, will not be under its purview.

Considerations for Tariff Setting

The thorniest regulatory issue revolves around determining water tariffs. Tariff setting should ensure a fair charge to customers in relation to services consumed and the commercial viability of the providers. Tariffs should include incentives to utilities to improve operational and economic efficiency – for example, by reducing leakages, unaccounted for water, and energy costs as well as improving collections. The MWRC would establish mandatory guidelines and principles, such as recovering costs for desired service levels, to help tariffs gradually move toward this goal. It would conduct regular reviews of the tariffs set by local bodies and, over time as more information becomes available, develop yardsticks to measure progress.

The WDSS and the Sukthankar Committee recognize that it may be necessary to subsidize services for the poor and disadvantaged for whom even lifeline rates are not affordable. They maintain that the subsidies must be explicit and well targeted. This contrasts with the current situation in which residences and businesses that can afford to pay are receiving water at no or low cost in hidden subsidies. The committee recommends that local bodies find innovative ways to address the needs of the poor by securing the active involvement of community based organizations and by appropriate design of private sector projects they put out for bid. It warns that, without explicit inclusion of the poor in the reform process, reform may be derailed in their name.

Community Role in Regulation

To make the new regulation and tariff setting more responsive to community needs and willingness, the new entity should initiate a process for effective community participation. First, the MWRC should set up or strengthen consumer councils that can articulate consumer demands and preferences and provide them capacity building support. Second, the MRCW should set up an effective public consultation process for licensing and tariff determination. To be meaningful, such consultation must be backed up by timely provision of relevant information to the public about existing service levels, financial investments and expenses, hidden subsidy transfers, etc. The Sukthankar Committee, noting that enforcement of environmental regulations is weak, recommended that monitoring of water quality be contracted out to the private sector

and non-governmental organizations (NGOs). With access to relevant information, NGOs and other community groups can be powerful advocates for reform. The *Citizens' Charter*, adopted by the utilities in Hyderabad and Chennai, helps introduce a consumer focus to the service. Just as in the power sector, research suggests that users are willing to pay for water as long as tangible improvements can be demonstrated.

Conclusion

The 73rd and 74th Constitutional Amendments, which devolve responsibilities to local governments, present an excellent opportunity for reform of the water and waste water sectors along the lines proposed above for Maharashtra. State funding and MJP technical expertise are being transferred to local governments. The funding transfers should be conditioned in part on local utilities' progress toward meeting the standards for service quality and community participation. This will reinforce, in an affirmative cycle, greater customer participation, a commercial orientation by the utilities, new investment priorities, and improved service and coverage that is more economically and environmentally sustainable.

This *Project Note* is based on two reports produced by the Water Supply and Sanitation Department, Government of Maharashtra: *Discussion Note on An Independent Regulatory Framework for Water and Waste Water for Maharashtra* (August 6, 2000) and *Sukthankar Committee Report on Operation, Maintenance and Management of Rural and Urban Water Supply Schemes* (February 28, 2001). V. Satyanarayana and Kirti Devi of the FIRE project provided technical support to the Committee and GOM. The reports are available from WSSD in Mumbai, the FIRE office in New Delhi, and TCGI in Washington, DC. All *Project Notes* are available online at www.dec.org.

The mission of the Indo-US FIRE(D) Project is to institutionalize the delivery of commercially viable urban environmental infrastructure and services at the local, state and national levels. Since 1994, the Project has been working to support the development of demonstration projects and of a sustainable urban infrastructure finance system. Now, the Project is also pursuing this mission through:

- Expansion of the roles of the private sector, NGOs and CBOs in the development, delivery, operation and maintenance of urban environmental infrastructure;
- Increased efficiency in the operation and maintenance of existing water supply and sewerage systems;
- Strengthened financial management systems at the local level;
- Development of legal and regulatory frameworks at the state level;
- Continued implementation of the 74th Constitutional Amendment; and
- Capacity-building through the development of an Urban Management Training Network.

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