

Network of Associations of Local
Authorities of South-East Europe



REGIONAL WATER MANAGEMENT

POLICY POSITION PAPER

Table of Contents

1. Introduction.....	2
2. The Issues Underlying the Water Management Sector in the Region.....	3
3. NALAS Vision of the Water Management Sector in South-East Europe.....	6
4. Criteria to Assess Policy Options.....	7
5. Policy Positions.....	8
6. Recommendations.....	13

Water supply and sanitation are among the essential communal services that citizens directly connect with local authorities and therefore hold them accountable for their quality, accessibility, and availability. As an integral part of water management, water supply, and sanitation are at the core of sustainable development, represent one of the basic human needs and make an important factor in economic and social well-being, as well as environmental protection. Therefore, their accessibility and development are recognized as one of the UN sustainable development goals.

Water management including water supply and sanitation is perceived by the EU as the services of general interest essential for the well-being of the citizens and economic activities. Services of general interest make an important contribution to the overall competitiveness of European industry and economy, as well as social, and territorial cohesion. As users of water supply and sanitation services, European citizens expect and are entitled to high-quality services at affordable prices. Because of that, citizens' requirements are the main focus of water policies and action in the EU countries, and those will be the principles that would be demanded from all future EU members.

Network of Associations of Local Authorities of South-East Europe (NALAS), which brings together 13 local government associations (LGAs) that represent roughly 7000 local authorities in the region of South-East

Europe (SEE), wants to mainstream the efforts of local governments in the region to provide their citizens with high-quality water services and ensure them the same conditions as other Europeans have regarding the water supply and sanitation. To do so a strategic approach to the water management sector with policy position and recommendations for the LGAs in the SEE region is prepared as a common advocacy and capacity development platform.

The platform, which was prepared as a joint effort of the Water Management Group of the NALAS Task Force for Solid Waste and Water Management, should serve as a good basis for LGAs in the region to represent the interest of their member local authorities vis-à-vis central governments and in front of other relevant forums regarding aligning national, regional and local water and sanitation policies to the needs of local populations and requirements provided by the EU acquis.

This document is prepared within the Project "Regional Capacity Development Network for Water and Sanitation Services in South-East Europe (RCDN)" with the financial support of the German Federal Ministry of Economic Cooperation and Development (BMZ) and the Swiss State Secretariat for Economic Affairs (SECO).

The Issues Underlying the Water Management Sector in the Region 2

The Water Management sector in the SEE Region, as in the case of any other economic sector, is burdened by certain underlying issues which are identified and described below. These issues are of a general nature and can, to a greater or lesser extent, be applied to all the economies in the region. They are the consequence of several factors and can be attributed to different types of barriers including legal and regulatory barriers, economic and financial barriers, organizational and management barriers, human resources and technical barriers, and political barriers.

The NALAS network intends to address the identified issues as well as barriers due to which they occur through policy positions and recommendations which can then be taken over in full or in part, adapted to the context of a specific economy, and used by LGAs for advocacy and capacity development purposes.

The absence of financial sustainability in water management is one of the major issues that can be attributed to the sector. Provision of water supply and sanitation including wastewater treatment is associated with significant production costs which are a consequence of the need for large investments in the infrastructure, demanding technological processes, maintenance, and operation. On the other hand, other factors exist, primarily of a political and social nature due to which in many cases in the region inadequate tariff policies based on low, non-covering prices of water and sanitation is led, that in the long run leads to deterioration and unsustainability of the system.

Pricing and tariff policy are among the key elements of policy-making within the sector. Still, the decision to increase the price of water and sanitation is never an easy and popular one for the politicians, especially in cases when traditionally local social policy has been conducted through the price of basic communal services.

Low prices and inadequate tariff policies are major problems for the sustainability and development of the water management systems at the local level, but not the only ones. Other **inefficiencies in the provision of water supply and sanitation services** exist such as low collection rates, lack of monitoring, inefficient use of resources, the poor structure of PUC employees, overwork, or poor maintenance of the equipment, which add to the increase of operating and maintenance costs.

Lack of capital projects and funds for capital investment is a huge issue for the normal operation of the water management sector. In many cases, municipalities in the region struggle to provide finance for operation and maintenance and lack the capacity to raise funds for capital investments. Also, many local authorities lack the resources to fund capital investment projects from the existing municipal capital budget and have to rely on external sources regardless of whether they are funds from national budgets, donations, loans, or private capital participation. The water management infrastructure is costly and requires a long time to amortize, and once built usually cannot be used as collateral which further reduces the ability of local governments to independently finance capital projects.

The Issues Underlying the Water Management Sector in the Region

In addition to tariff setting, the capability to invest in water management infrastructure heavily depends on local revenues and a sustainable system of local finances. The development of water provision and sanitation services can often be hampered by the economic situation local authorities are facing, including limited fiscal space for borrowing. **The level of local government finance autonomy is decreasing in SEE** which can be a huge obstacle to the recovery and development of the water management sector. On average, local government revenues in SEE decreased by 0.5% between 2009 and 2019, both as a percent of the GDP and total public revenues (Source: 8th NALAS Fiscal Decentralisation Indicators Report).

Even in cases when funding for capital investments in water management infrastructure is available usually there is a **lack of administrative capacity at the local level** to utilize it. Local authorities in the region and their administration in many cases suffer from the lack of knowledge to plan, prepare, tender, organize, implement, manage, and monitor capital investment projects. **The centralization of these functions** in some economies of the region is also noticeable, which may result in further weakening of otherwise scarce local administrative capacities.

Regardless of whether they are already members of the EU or are in some phase of the negotiation process majority of the economies in the region are lacking behind or having difficulties reaching EU water management standards. This primarily refers to the **insufficient service coverage and especially to the coverage of the population with the sewerage and wastewater treatment**. This issue is even

more prevalent in rural areas where the service coverage percentages are significantly lower than in urban areas.

The condition of the water supply and sanitation infrastructure, especially networks, its state, capacity, age, and obsolescence, poses a serious issue for the quality of water management services in the region. It is the consequence of a lack of investments or underinvestment in the sector in the past period, standards applied at the time of construction, and the absence of asset management practices.

Needed investments also include the **construction of a multitude of wastewater treatment plants** across the region. The treatment of urban wastewater is fundamental to ensuring public health and environmental protection. In some economies in 2017, the percentage of collected wastewaters discharged without treatment reached as much as 49.75% (Source: European Environmental Agency).

Non-revenue water is still one of the major issues in most economies of the region. This problem is connected to leakages, but also illegal connections, and in some cases poor collection rates. Non-revenue water levels in the region are the highest in Europe ranging as high as 75 % in some municipalities (source: IB-NET Database).

Environmental issues including water management remain **low on the priority lists of political decision-makers** at the local levels. Pollution caused by the absence of standards and poor sanitary practices is rarely on the local political agenda. There is little incentive for local governments to develop strategies or set goals and

The Issues Underlying the Water Management Sector in the Region

objectives for improving water and sanitation services. The consequence is that this topic does not come to the fore in local policies and strategic documents and does not receive adequate attention.

There is an obvious region-wide discrepancy between the adopted water management legal framework and the **enforcement at the local level**. The low level of law implementation can be attributed to insufficient capacities at the local level, but also the absence of needed by-laws for the operationalization of legal prerequisites and strategies and targets for water and sanitation services.

Service operators, i.e., **Public Utility Companies** in the region **are usually under political influence** from the local authorities, and not always independent in making business decisions, thus can be overstuffed and suffer from financial, operational, and other inefficiencies.

There isn't an established practice in the region of **clearly defining the relationship between local self-government and the PUC** regarding the level, quality, and standards of services provided to citizens and other customers.

The unclear status of water management assets in terms of ownership and depreciation, a situation common in the region, can cause management, business, and financial issues for the asset holders. If the asset managed by the utility company does not appear on its balance sheets the depreciation cannot be calculated which is an obstacle to reimbursing the cost of capital assets, and raising funds to replace fixed assets.

An unclear governance structure in the water management sector can pose a serious threat to investment potential, efficiency, and the quality of the services. Good practices in water management governance include the clear distinction between policymaking, regulation, and service provision, subsidiarity, long-term predictability, accountability for the service provision, and involvement of customers and other relevant actors in service planning.

The absence or underdeveloped public participation in matters related to planning and decision making and the governance of water management at the local level can lead to inappropriate infrastructure planning or poor quality of the services which do not fulfill the needs of local populations.

Sludge from the wastewater treatment process is an increasingly important issue that burdens both local governments and their public utility companies in the SEE region. This is because sludge management strategies are not yet in place or implemented and there is an increasing number of wastewater treatment plants in the region.

Rising energy prices, caused by the energy crises and the market instability increase the production cost of water supply and sanitation services and put more pressure on public utilities and customers, but consequently also on local authorities to either increase service prices or cover financial losses that service providers might incur. Such a situation put additional emphasis on energy efficiency and efficient provision of the services.

3 NALAS Vision of the Water Management Sector in South-East Europe

NALAS as the regional umbrella organization of the LGAs envisages Water Management Sector in South-East Europe as fully aligned with EU acquis and European water management standards in terms of service coverage, accessibility, sustainability, affordability as well as customer satisfaction, and protection of the environment and the natural resources. By creating a common sectoral platform NALAS aims to support its member LGAs to advocate and strengthen the capacities of LSGs and PUCs in the region and stream their efforts to provide their citizens, institutions, and businesses with high-quality water services and ensure them the same conditions as other Europeans have regarding the water supply and sanitation.

Criteria to Assess Policy Options 4

In the provision of water management services, different policy options and approaches can be applied to the different levels of governance to ensure high quality and efficiency in water supply and sanitation. To assess the effects of different options, policy analysis is applied as a structured way to find, evaluate, and choose alternative courses of action in the sector. Policy options analysis is applied to increase the chances of choosing or shaping, policies that will contribute to achieving the Vision. The analysis is based on the following set of criteria per which options have been compared:

- **Affordability** of the water supply and sanitation to the general public and the socially endangered groups.
- **Service coverage** as a measure of equality is an indicator that represents the population covered with water services as a percentage of the total population.
- **Accessibility** or access to safe drinking water is defined as the percentage of the population having access to and using high-quality water services.
- **Quality of the service.** In addition to the technical and biological characteristics of water, the quality of service includes coverage, reliability, continuity, the sufficiency of quantity, the possibility to complain, and the speed of reaction of the authorities to the complaints.
- **Impact on the environment.** Water management services can have a huge negative impact on the environment if not managed properly, this especially goes for wastewater treatment but can be applied also to the extraction of the water.
- **Impact on social cohesion.** Social cohesion involves building shared values in communities, reducing disparities, and generally enabling people to have a sense that they are engaged in a common enterprise.
- **Impact on economic growth.** Economic growth as a measure of the increase in the production of economic goods and services heavily relies on the state of water management as one of the basic communal services.

5 Policy Positions

- **Continuous development of the legal framework** and transposition of the EU water acquis is the priority for all the economies in the SEE region, those already members, and those who have that aspiration alike. European standards set through public policies are constantly evolving. To reach this moving target central governments will have to ensure continuous alignment with EU legislation. Still, the majority of environmental acquis is implemented at the local level which puts enormous pressure and expectations on the local authorities in the SEE region.

To ensure timely and enforceable water management commitments, **NALAS and the LGAs should continuously monitor the development of the EU legal framework in the field of water management**, and thus contribute to the harmonization of national legal frameworks with the EU acquis and ensure the representation and appreciation of the local government views in this process.

- **The strategic or ad hoc approach to service and infrastructure development** is a par excellence policy issue. A strategic in opposite to an ad hoc approach is an element that defines a shared vision among all stakeholders in a coordinated and collaborative way ensuring the implementation of water management objectives at all levels. In this respect, such an approach is to ensure that actors at all levels clearly understand their roles, responsibilities, and authorities. Applying a strategic approach makes easier allocation of needed resources to carry out

tasks and provisions of water management services.

LGAs in collaboration with NALAS should **advocate for a strategic approach in the governance over the water management at all levels**, which refers to the action towards institutions of higher levels of governance, as well as towards local self-governments and public utility companies that should adopt policy document in this field and link them to multi-annual financial planning at the local level.

- **More strict regulation or liberalization of the provision of water management services** is an ongoing discussion. These opposing concepts and the processes leading to them could have been observed going back and forth in some European countries in the past period. Liberalization means that services are provided more market-based and that the prices of water and sanitation are determined more freely even in the conditions of a natural monopoly. On the other hand, regulation can be done at the local level through the decisions of local authorities but also at the central level through a water regulator.

Having in mind aspects of affordability, coverage, accessibility, and impact on the environment NALAS will support LGAs in their effort to stand on the position of **defending the public interest and advocate for the regulation of water management services**, whether it is done from the local or central level.

- **Financing of water supply and sanitation capital investments** is one of the major preconditions for development and reaching high standards in the water management sector. In the most general sense, financing of capital and other investments in the water management sector including the development of the water supply and sewage networks, drinking water facilities, and wastewater treatment plants **can be done predominantly either through tariffs or via budgetary allocations**. According to the 8th NALAS Fiscal Decentralisation Indicators Report, in 2019 local governments in the SEE region on average spent 25.6% of their budgets on capital investments, which is significantly more compared to their counterparts in the EU which allocate 12.5% from their budgets for these purposes. This is due to the different investment needs, in the SEE region more funds are spent on building new infrastructure and reconstructing the old while in the EU more is spent on maintaining the existing infrastructure which is treated as an operational expense.

Either of these two policy options for financing capital investment (from the price of the service or the budget) in the water management sector is valid but it needs to be viewed through a prism of the current economic strength of local authorities, but above all by the affordability of the water management services for the local population. In this sense, it seems that in the coming period in the SEE region, capital investments will continue to be predominantly financed through the local budgets.

Therefore, NALAS and the member associations should **advocate for sufficient, predictable, and stable general budget revenues** for municipalities in SEE from their revenues or general grants to fulfill, among other environmental responsibilities, their water management tasks including infrastructure investments and service development.

- **Pricing and tariff policy** are important aspects of the development and quality of water management services. The economies of the SEE region inherited low prices of communal services, which in the current conditions are not even enough to cover operating costs of the water supply and sewage services, not to mention wastewater treatment, as well as the **practice of conducting social policy through the prices of utility services**. Such a common practice continues to be a politically opportune approach but one that leads toward unsustainability and the collapse of the system and the quality of services. Other policy option, applied in developed economies and socially responsible societies includes **tariff policies based on cost-covering service prices**, while the social policy for groups in a state of social need is conducted through budget allocations for social benefits.

Both policy options meet and can pass the affordability criterion, however from the aspects of long-term quality of the service, impact on the environment, and impact on economic growth the only possible option is to apply cost-covering service prices in the water management sector. The transition from the current approach to a full cost recovery policy through the price of the service cannot be introduced all at once

Policy Positions

as this would come as a shock to many users, but a step-by-step approach over a defined period should be applied.

LGAs with the support of NALAS should **advocate before their membership the immediate introduction of a tariff policy based on the full cost coverage principle**, but also provide support to municipalities in determining real operational costs of the services and utilities' financial performance so the transition is anchored on a realistic basis.

- ▶ **Capacities of local authorities in the SEE region to absorb external funds** can be an important element in the green transition, in which the water sector is a big and important part. Within the EU Green Deal and green transition process, more and more external funds for interventions in the field of environment, and therefore in the water sector too, will be available to local authorities in SEE. The financing will be intended for the improvement of services that local authorities provide to their citizens, but also for meeting the EU standards in the field of environmental protection. European Commission but also other reports emphasize that local authorities primarily in the Western Balkan region do not have a sufficiently developed awareness of the importance of environmental protection and that their existing administrative capacities to address environmental issues and absorb funding for local projects are insufficient. In such a situation, the **processes of centralization of certain water management functions** like planning of investments, development of technical documentation, and procurement

are evident in some economies as opposed to a continuous **building of local capacities** to perform these tasks efficiently and at a high level.

From the point of view of the sustainability and affordability of the services building local capacities is a much more viable option than centralization since it provides ownership of the presses by the local communities which enables addressing the specific needs of the local population and businesses.

In this regard, NALAS and the LGAs should provide support to local governments and their utility companies in carrying out the duties that will be assigned to them in the green transition process. This support should be reflected in **awareness-raising and capacity-building activities** to address water management issues, in particular through intensive training, advisory services, mentoring, and information sharing.

- ▶ **The issue of bookkeeping of fixed assets** for the provision of water supply and sanitation, primarily networks that have a long depreciation period, is an important one because it influences the financial performance and creditworthiness of public utility companies. In many instances, assets are occurring in the books of both local authorities and public utilities, and in some cases, they are even not in any books.

NALAS should support LGAs to further **advocate for the resolution of such a situation on both levels, in terms of finding adequate legal solutions, as well as in terms of encouraging local authorities**

to register assets and, where possible, do so on behalf of the public utility companies.

- **Capacities at the local level** including both local authorities and public utility companies to organize and provide water supply and sanitation including planning, financing, decision making, regulation, and monitoring are essential elements of the water management services. The public sector in particular in the SEE region is prone to losing the already scarce quality staff who move either to the private sector or to more developed economies in the EU. This is especially evident in smaller municipalities in the region that anyhow have problems with technical and human capacities.

In this regard, LGAs with the support of NALAS should ensure a **systemic approach to capacity development**. Implementation of regular and targeted capacity development measures, independently or in cooperation with proven international, regional, and local partners, including the Waterworks Association, should ensure an upgrade of knowledge and skills of local representatives in terms of new approaches, methodologies, and procedures that can contribute to the improvement of the water management services provision.

- **Capacities at the local level** to operate technically demanding water management facilities. This problem becomes even more pronounced if the requirements regarding the construction and operation of wastewater treatment plants are taken into account. One of the solutions to this problem is collaboration

in the water management sector. This process in a policy sense can be driven **top-down by the central governments or bottom-up by the means of inter-municipal cooperation**. Furthermore, local capacities should be constantly upgraded through capacity development activities.

Both policy options have their advantages, while the top-down approach is usually faster and done through extensive reforms through legislative intervention, the bottom-up requires more time and effort from local authorities but in the long run, ensures ownership of the process, adequate approaches, and solutions applicable to the local context.

NALAS network and the member LGAs should provide support to local authorities in the region by ensuring **information exchange** on inter-municipal cooperation good practices.

- **The operational and financial efficiency of the service providers, i.e., Public Utility Companies** is one of the key features of high-quality water supply and sanitation service. These companies in the region suffer from inherited inefficiency due to various factors including political influences, poor employee structure, old equipment, technical obsolescence of the system, inadequate management practices, and more. In that regard, several clusters of policy options can be considered.

One such dilemma is **whether water and sanitation services should be cross-subsidized** with each other or by other more profitable services possibly

Policy Positions

provided by utilities. Economic theory, but also the practice of developed EU economies, says that cross-subsidization is not a good approach for the development of services in the long run and that it can lead to financial inefficiency of the service provider. Clear and separate management of expenditures and revenues for each specific activity within the water management service is crucial for the health of the company and the quality of service.

Another possible discussion can be conducted on the **introduction of private operators in the sector vs. the corporatization of publicly owned enterprises.**

In most cases in the region water provision as a whole cannot be privately run, but for some activities within the service, it is possible to engage a private operator. Corporatization, on the other hand, means that the publicly owned companies introduce modern management practices, including corporate management, the introduction of accountability for the performance, etc., and are relieved to a great extent from the political pressures. In connection with this dilemma, the question also arises of the organizational form of a publicly owned company, i.e., whether a public utility company or an enterprise in majority public ownership is a better form of organization in terms of efficiency and operational capability.

Since the local context varies from economy to the economy and local authority to local authority, NALAS and the LGAs should **advocate for the conduction of thorough analyses of the benefits and drawbacks** of each option before action is taken either in the

individual case or as a legal reform action at the central level.

- Often **public participation in the decision-making process** regarding water management at the local level is neglected and instead is replaced by an expert approach that in most cases means involving external consultants who do not necessarily have to be familiar with the local context and the needs of the local community. This approach often leads to the Not In My Back Yard effect (NIMBY). In addition, the participation of citizens is an important, but also a necessary precondition in the process of preparation and implementation of capital investment projects.

In terms of customer satisfaction, service coverage, affordability, and long-term sustainability involvement of public and relevant stakeholder early in the planning and decision-making process make a lot of sense, but it doesn't exclude the involvement of the experts.

For this reason, **NALAS emphasizes the importance of establishing public participation practices** and will support LGAs in their efforts to ensure acceptance of the binding mechanisms that will secure public participation in matters related to the provision of water supply and sanitation.

In the coming period, NALAS will work on promoting a common vision of the water management sector in South-East Europe and the role and responsibilities of LGAs and local authorities in reaching it.

Taking into account current European policies and initiated processes under the EU Green Deal, NALAS will be committed to the actions that will support member LGAs and their local governments to take an active and competent part in these processes and will support them in absorbing and utilizing more funds for capital investments in the water sector that will become available.

Furthermore, NALAS will be a valid partner to the LGAs in their struggle to represent the needs and positions regarding the management of water services of local authorities vis-à-vis national governments. Nalas will also strongly insist on the need for capacity development at the local level for high-level water management services to be provided to citizens, institutions, and businesses in the SEE region.

To achieve the Vision of the Water Management Sector in the region, NALAS will join LGAs and support them in taking action in several directions:

- Representing the interests of local authorities in front of central governments concerning strategic approach in the governance over the water management at all levels, including continuous monitoring of the EU water acquis development

and ensuring local positions are respected in its transposition into national legal frameworks as well as advocating for sufficient, predictable, and stable general local budget revenues for the fulfillment of responsibilities in the water management sector.

- Advocating toward member local authorities for introduction of a tariff policy based on the full cost coverage principle, setting standards of services delivery and establishing a clear division of obligations and responsibilities between local governments and service providers, and introducing sound management practices in the publicly owned utilities. These actions should also include advocating of necessity to conduct thorough analyses of the benefits and drawbacks of each option when it comes to changes in the governance structure of water management at the local level.

- Developing local capacities which is one of the most significant needs in the water management sector in the SEE region. Capacity development should be directed toward the absorption of external funds for capital projects, i.e., the increasing of the capabilities to plan, prepare, tender, organize, implement, manage, and monitor capital investment. Increasing efficiency in the provision of water supply and sanitation services both by local authorities and service providers will also be the subject of capacity development and should include training on modern management practices, monitoring, and reporting on water management-related issues.

Recommendations

- Information sharing and awareness-raising about the importance of environmental-related issues including water management services, and EU policies in the sector, as well as about good practices in joint service provision, solutions for sludge management, and other developments in the sector.

Based on the policy positions and recommendations NALAS will further direct and develop its activities in the water management sector, both towards its member LGAs and in interaction with international partners and other actors on regional, European-wide, and international forums. Furthermore, NALAS will use this document during the discussions and preparation of future development programs in the water sector directed toward local authorities in the SEE region.



NALAS Secretariat
Varshavska 36 A, 1000 Skopje,
Republic of North Macedonia
Phone: +389 23090818
E-mail: info@nalas.eu



Implemented by
giz Deutsche Gesellschaft
für Internationale
Zusammenarbeit (GIZ) GmbH



Schweizerische Eidgenossenschaft
Confédération suisse
Confederazione Svizzera
Confederaziun svizra

Swiss Confederation

Federal Department of Economic Affairs,
Education and Research EAER
State Secretariat for Economic Affairs SECO



This document is prepared within the Project "Regional Capacity Development Network for Water and Sanitation Services in South-East Europe (RCDN)" with the financial support of the German Federal Ministry of Economic Cooperation and Development (BMZ) and the Swiss State Secretariat for Economic Affairs (SECO).