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CANADIAN CENTRE
for POLICY ALTERNATIVES
MANITOBA OFFICE

Should The City Of Winnipeg Create A Municipal Corporate Utility And Use Public Private Partnerships To Build New Wastewater Treatment Infrastructure?

Submission to the City of Winnipeg
Executive Policy Committee
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by the
Canadian Centre for Policy Alternatives-Manitoba

Summary of Concerns and Recommendations

The Canadian Centre for Policy Alternatives-Manitoba (CCPA-MB) is registering its opposition to the Winnipeg Public Service Recommendation being considered by the Executive Policy Committee on July 15, 2009 item No. 1 City of Winnipeg Municipal Utility, File GL-5.6.1. The CCPA- MB's opposition to the above proposal stems from the following key concerns:

1. The current proposal to transfer responsibilities of the Water and Waste Department (WWD) from the City to a Municipal Corporate Utility (MCU) will lead to reduced public oversight, political accountability and access to information, as well as the loss of an important economic development tool for the City of Winnipeg, increased relocation of commercial, industrial and residential development outside of the city's jurisdiction and further erosion of the City's tax base.

2. The MCU proposal is intrinsically tied to the pursuit of Public Private Partnerships (P3s) with private sector Strategic Partners to finance, and potentially operate and own, key pieces of wastewater treatment infrastructure. This type of wastewater treatment P3 has had significant negative financial and environmental consequences for other municipalities, and many others after extensively exploring such options have decided against such arrangements.

3. Many of the proclaimed benefits of the MCU, including its claims regarding cost savings and revenues, have been simply asserted and have not been substantiated by quality factual research. Specifically, it is not clear what advantages exist under the MCU - Private Partner model and what advantages can be gained by reforms within the current ownership structure.

4. The establishment of the MCU and the procurement of private sector strategic partners introduce the risk of bringing Winnipeg's water and waste services under the jurisdiction of international trade treaty obligations that could lead to financial compensation and/or forced market access for international corporations.

Given the above, the CCPA-MB therefore issues the following recommendations:

1. That the City commission an independent public sector comparator by an uninterested third party to objectively compare the costs of pursuing the MCU-P3 model with the cost of undertaking upgrades under the current ownership structure. This analysis should clearly distinguish between the current ownership structure, the proposed MCU-P3 model, and a MCU model without a P3 arrangement. This assessment could also be formative in terms of assessing current capacity if the WWD and what the City could do to improve its ability to meet new capital requirements.

2. That the City have an uninterested independent evaluator assess which of the proposed efficiency enhancing reforms require the formation of a MCU, which

can be achieved under the current ownership structure, and provide factual and empirical support conclusively demonstrating that such potential efficiencies exist and have been successfully realised in other jurisdictions.

3. That the City obtain an independent legal opinion to determine what new obligations the water and waste utility will have under the proposed MCU-P3 model, given Canada's international trade treaty obligations.

4. That the City delay pursuing the MCU model until the above independent evaluations can be undertaken.

1. The MCU will lead to reduced public oversight and loss of an important economic development tool

Some of the advantages claimed by the Administrative Report accompanying the Public Service Recommendation are the increased flexibility that the MCU would have compared to the current structure, as it would be freed from "restrictive" public sector governance and "political agendas" (p.3).

While democratic governance structures may be more time consuming, it would be hard to convince the public that this suffices for a reason to replace them with structures that are less democratic. Despite the negative connotations, "political agendas" also include limiting urban sprawl, creating a more sustainable city and using Winnipeg's high quality services as a competitive advantage to attract businesses and spur economic development. The business-like nature of the proposed MCU model will shift emphasis to the narrow bottom line at the expense of incorporating broader city planning objectives.

The Administrative Report states that a key role for the MCU would be "positioning the Utility for future opportunities such as expansion into new services inside and outside of Winnipeg" and that "any future utility service agreements in the Capital Region or elsewhere would be the responsibility of the Utility and its Board to negotiate and conclude" (p. 3-4). It is clear here that responsibility currently held by City Council who is accountable to voters is being transferred to the MCU, which under the current proposal will be governed by an unelected board of directors who are only weakly accountable to City Council. This will lead to reduced public oversight, political accountability and access to information.

Experience in other Canadian municipalities shows that these are not abstract or hypothetical concerns; The Parkland Institute's Diana Gibson prepared an in-depth report on Edmonton's EPCOR, which the Deloitte and Touche report commissioned by the City cites as an example of a MCU responsible for water and waste services. Gibson's report highlights that Edmonton can no longer include EPCOR-run utilities in its broader city-planning objectives, that now there is a singular lack of oversight by City Council, and public transparency has been severely curtailed as EPCOR is not subject to the Freedom of Information and Protection of Privacy Act. Since taking over, Edmonton City Councillors and citizens have not been able to gain access to vital information about Edmonton water utilities.

University of Winnipeg Professor Christopher Leo in a recent publication also expresses concern that the transfer of service provision to the new MCU and the intention to sell services to neighbouring municipalities will result in the loss of an important economic development tool for the City of Winnipeg, increased urban sprawl, the relocation of industry and business outside of the city's jurisdiction and an erosion of the City's tax base. He points to the City of Detroit, which undertook a move similar to the one being proposed, and ended up losing significant manufacturing, commercial and residential development to neighbouring municipalities

which it was now servicing with its water services.

2. The current proposal of the MCU is intrinsically tied to the pursuit of Public Private Partnerships which are based on the privatization of city wastewater services

While the formation of a MCU does not necessitate privatization of services in the form of public private partnerships (P3s), the current proposal is intrinsically tied to the pursuit of P3s with a private sector Strategic Partner to finance and potentially own and operate key pieces of wastewater treatment infrastructure. P3s come in various forms with differing degrees of privatization, although all P3 financing arrangements involve some transfer of assets or employment to the private sector that in the traditional model was in the public sector. Under the current proposal, one alternative scenario has a private partner stake of up to 49 percent in new wastewater treatment infrastructure services (p.37).

These types of water treatment P3s have had significant negative financial and environmental consequences for other municipalities, and after extensively exploring such options many have decided against such arrangements. The most well known water P3 gone wrong is the Hamilton Wentworth P3. The Hamilton Wentworth P3 deal was signed in December 1994 for a $180-million contract agreement with Philip Utility Management Company. "Efficiencies" were found by laying off experienced staff and allowing equipment and working conditions to deteriorate to unsafe levels. The most significant negative consequence that came as a result of this was a pumping system failure at the main sewage treatment plant, resulting in the flooding of over fifty homes and many businesses, and the dumping of 180 million litres of raw sewage into Hamilton harbour (Ohemeng & Grant, 2008). After the P3 contract expired in 2004, wastewater services were brought back under direct public control. Since being brought back in-house, wastewater services have provided high quality services and cost savings for four years in a row (City of Hamilton, 2008). The Greater Vancouver District (Mehra, 2005), Collingwood, Ontario (CUPE, 2005), and Prince Edward County, Ontario (Bell, 2009) have all considered and rejected P3 water schemes.

These rejections have to do with the fact that P3s have repeatedly been shown to be more costly than publicly owned and operated infrastructure. Governments can generally borrow at a lower interest rate - a direct cost advantage over P3 financing. P3 contracts can reduce competition as they almost always guarantee exclusive service provision by the private sector partner and often bind the government to continue the lease arrangement for several years and in some cases decades. Lastly, P3 agreements are incredibly complex leading to substantial amounts of money devoted to lawyers' fees and additional administrative burden. P3s also have to generate a profit to justify the private sector partner's involvement, generally at the expense of higher project costs (compared to public provision) and/or by cutting the costs through layoffs, reducing service delivery and quality, and applying or raising user fees.

While the Administrative Report projects life cycle cost savings of 12 percent from the P3 model, little detail is provided as to how these costs savings will be achieved, what the claims are based on, and how these cost savings might transfer into the Winnipeg context. According to an opinion prepared by University of Manitoba professor and P3 expert John Loxley, the incomplete justification that is given is based on the uncritical acceptance of anecdotal evidence. Problems with the cost savings figures are also not addressed. For example, the City of Moncton cost comparison cited in the Administrative Report (p.38) is based on a comparison to the cost of a design-bid-build

facility that has 30 percent more capacity than the P3 facility.

New research has shown that P3s have become even more costly in the post-financial crisis environment (Mackenzie, 2009). This makes intuitive sense given the significant challenges the current environment poses to securing private capital. Given that the City can now borrow at rates as-low as 5.6 per cent on a 30-year loan (Kives, 2009), it is hard to believe that a P3 arrangement can be more cost effective than the traditional design-bid – build provision framework.

3. Many of the proclaimed benefits of the MCU's corporate model have been simply asserted and have not been substantiated by factual research.

The Public Service report argues that increased efficiencies will arise from the project due to its business-like model, its partnership with the private sector, and its liberation from the burden of public administration, but little evidence is presented to support this proposition and when justification is given it is not stated why these reforms cannot be undertaken under the current ownership structure. While the Public Service and City Council seem to be suffering from an inferiority complex with respect to their ability to manage and operate municipal water and waste services efficiently, the CCPA-MB is more optimistic with respect to their relative capabilities, particularly given the fact that several internal and external accounts have given the City high ratings in service quality and operation.

Studies in peer reviewed journals have little support in general for the argument of private or corporate model superiority. Professor Kwong Leung Tang (1997), in his extensive review of empirical studies of public versus private sector efficiency found contradictory evidence on the general claim that the private sector was more efficient. Edouard Pérard (2009) reviewed 22 empirical tests and 51 case studies and found that private sector participation in water services does not systematically have a significant positive effect on efficiency. Germà Bel and Mildred Warner (2008) undertake an extensive review of statistical studies of water and waste production since 1970 and find little support for private sector involvement leading to cost savings. Willner and Parker (2002) undertake a similarly extensive review and find the same conclusion.

The International Monetary Fund questions the claim of the private sector's superior efficiency when it comes to infrastructure provision. In a 2005 report the IMF states that: "It cannot be taken for granted that PPPs are more efficient than public investment and government supply of services" (p. 3). The report also notes that "much of the case for PPPs rests on the relative efficiency of the private sector [and] while there is an extensive literature on this subject, the theory is ambiguous and the empirical evidence is mixed" (p.14).

David Hall and Emanuele Lobina (2005) found no systematic or intrinsic advantage of private sector operation in terms of efficiency and no evidence to support that a public sector operator is intrinsically less efficient or effective. They argue that "policy discussions should therefore be based on a strictly neutral assumption about relative efficiency, and in particular not regard introduction of private sector operation as a desirable or valuable objective. Otherwise policy decisions risk being distorted and leading to costly economic and social consequences" (p. 5).

The EPC and Council are invited to explore these publications in more detail, but the message is clear: the prediction of efficiency gains from corporatization and private sector involvement put forward in the Public Service recommendations stand in stark contrast to the evidence of peer reviewed research. These claims of efficiency gains need to be justified and substantiated.

It is also not clear that many of the reforms suggested by the report require the formation of a MCU. It is not clear why the use of the Public Utilities Board to set rates, the sale of services to other municipalities, and a revaluation of with whom and how the City contracts cannot be undertaken within the current ownership structure. The way the city contracts and the guarantees it now fails to get is an issue that needs to be confronted by all departments, and a satisfactory in-house resolution of these problems would likely benefit the entire civil service.

4. The proposed MCU – Strategic Partner model may open Winnipeg Water and Waste Services to challenges under of NAFTA and through the WTO

The establishment of the MCU and the procurement of private sector strategic partners introduce the risk of bringing Winnipeg's water and waste services under the jurisdiction of international trade treaty obligations including those of the North American Free Trade Agreement (NAFTA) and the General Agreement on Trade in Services (GATS) through the World Trade Organization (WTO). Under Minimum Standard, Most Favoured Nation, National Treatment, and Market Access provisions of these agreements the greater Winnipeg region may be obligated to allow competing private firms into water and waste service provision or face severe financial penalties for non-compliance. Broadly defined expropriation clauses may limit the ability of the City to withdraw itself from P3 relationships without severe financial consequences. An independent legal opinion should be obtained to determine what obligations the water and waste utility will be under given its new structure and private partnerships.

Recommendations

Given the above, the CCPA-MB therefore issues the following recommendations:

1. That the City commission an independent public sector comparator by an uninterested third party to objectively compare the costs of pursuing the MCU-P3 model with the cost of undertaking upgrades under the current ownership structure. This analysis should clearly distinguish between the current ownership structure, the proposed MCU-P3 model, and a MCU model without a P3 arrangement. This assessment could also be formative in terms of assessing current capacity of the WWD and what the City could do to improve its ability to meet new capital requirements.

2. That the City have an uninterested independent evaluator assess which of the proposed efficiency enhancing reforms require the formation of a MCU, which can be achieved under the current ownership structure, and provide factual and empirical support that such potential efficiencies exist and have been successfully realised in other jurisdictions.

3. That the City obtain an independent legal opinion to determine what obligations the water and waste utility will have under the proposed MCU-P3 model, given Canada's international trade treaty obligations.

4. That the City delay pursuing the MCU model until the above independent evaluations can be undertaken.

Given the fundamental importance of safe water supply management and wastewater treatment to our economy, health and well-being, and environment, the fact that direct public ownership has served Winnipeg well for over 70 years, the irreversible nature of P3 arrangements, and the potentially disastrous consequences of mismanagement, the CCPA-MB believes the precautionary principle should be respected in this case and further research is required before proceeding.

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