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What is the Benefit of Privatizing Water?

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A recent Wall Street Journal article reports on what seems to be an accelerating trend: cities privatizing their water supplies. According to the article, the Indianapolis city–county council voted last month to sell its water and sewer utilities to a charitable trust; San Jose and Pittsburgh are considering selling their water systems as well, while Sacramento is now allowing Nestle, SA to bottle and sell "excess" tap water.

Privatization: Half–full or half–empty?

Worldwide, private ownership of water utilities has been growing for a number of years. According to a 2004 editorial by Gary H. Wolff in the Journal of Water Resources Planning and Management the number of people served by private water companies worldwide grew from 51 million in 1990 to nearly 300 million in 2002.

The reason for the most recent uptick is trend financial: in the current economic climate, municipalities across the country are strapped for cash and will, it seems, take any measure to shore up finances.

But is privatizing water good for the public?

Wolff takes a balanced view of what he calls the "Gordian Knot" of the public/private water debate, suggesting, "we do not need to decide if private or public 'players' are superior, in the abstract. We need to implement and enforce the 'rules of the game' under which private or public utilities or operators are efficient and responsive to social needs and desires."

Wolff further points out that worldwide, the greatest water problems occur in places where the government is too weak to either provide adequate services or to regulate private companies—no doubt true.

But leaving aside the very real problems of water access, quality and accessibility that must be addressed in the developing world, what is the case for private water ownership in a place like the United States?

Chicago Water Tower. Source: Melissa Gasser on Wikimedia

Privatization advocates point out that private water companies must still comply with local and federal regulations on water safety, and argue that privatizing water saves the consumer money.

However, when the non–profit water advocacy group Food and Water Watch looked at average water rates charged by utilities in California, Illinois, Wisconsin, and New York, it found that private utilities charged consumers "significantly higher water rates" than public ones did—as much as 50 percent more.

The group listed several reasons that private companies charge more for water. First, corporate utilities are required to provide returns to shareholders, not the community. While regulations in theory limit profit margins to approximately 10 percent, companies can get around this requirement by leveraging their assets. "In other words, instead of using money they had borrowed for needed improvements to water operations and infrastructure, the companies invest in side businesses or other activities that diversify their operations to increase profits."

In addition, Food and Water Watch says, financing is also more expensive for private companies, which are not eligible for tax–free bonds, and private water companies are usually less efficient at water delivery. And because there is no effective competition to provide water in a given area (private water utilities are essentially local monopolies) there is no market incentive to cut costs.

According to the Wall Street Journal article, Atlanta privatized its water service in the late 1990s, but had to retake control four years later because of poor water quality and cost overruns. And there was a public uproar in Illinois last year when the largest private water company, Illinois American Water Co., requested a 30 percent rate increase, which it said was needed for infrastructure improvements.

Given that access to clean water is among the most basic human needs, shouldn't we think twice before selling it off for a short–term financial fix?