

## Privatization model for water enterprise in Kenya

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### Abstract

The world over, the role and eligibility of the state in the provision of water supply is increasingly coming into question. Policy makers and analysts are advocating the abdication of the state in favour of private participation. This is expected to bring with it a host of benefits to all the stakeholders concerned. Kenya is one of the developing countries that have endeavoured to privatize their water sectors. Kenya has done this by enactment and implementation of the Water Act of 2002. The paper carries out an analysis of the water institutions being created under the new legislation. This has been done against conventional policy and conceptual frameworks. Overall, the institutional set-up is found to be public sector-oriented rather than private sector-oriented. Recommendations are made for legislative review for mainstreaming private sector participation.

*Keywords:* Commercialization; Kenya; Privatization; Public–private policy; Water sector reform

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### Introduction

Dwindling water resources is a great concern for many countries of the world and especially for water scarce countries. Owing to scarcity of water resources, countries are forced to make rational choices between competing domestic, industrial, agricultural and commercial uses, among others. In response to this situation, a new paradigm has evolved to place water within the mechanism of market allocation. This entails the consideration of water as an economic good that would be subject to the dictates of demand and supply as well as emphasis on demand-oriented management strategy. The move is expected to promote conservation of scarce water resources. This necessitates reforms in the water sector in order to mainstream the new paradigm in water policy and praxis.

In Kenya, this reform is being implemented via the implementation of the Water Act of 2002. The Water Act makes far-reaching recommendations on the management of water resources in Kenya. Particularly, it purports to create a water market where private players are expected to transact business

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for the overall national benefit. Water and sanitation is a sector of particular interest that this Act deals with in Part IV.

This paper takes a critical look at the reforms proposed and implemented for water supply and sewerage services in favour of private sector players against the backdrop of privatization policy and concept. Specifically, it looks at the institutional options that are possible *vis-à-vis* what the reformers have settled for. The outcome of this evaluation faults the reforms in the sense that contrary to the claims that private sector is being involved; the private sector has actually been barred. The public participants' position, on the other hand, has been strengthened against the basic objectives of reform. In this matter, recommendations are made for actual involvement of the private sector.

## **Water service provision paradigm**

### *Public provision*

In the current debate, proponents of public sector provision see water as a basic need and a service of public interest. This is because water is essential for human life and indeed for all life on earth. This places water in a metaphysical position such that some cultures or religious persuasions may not welcome the sale of water. In this case water would preferably be left in the public hands in order to ensure public interest although private provision does not necessarily rule out public interest. Other arguments have sought to portray water as a public good that must be left in the public hands (Budds & McGranahan, 2003). But nowadays water does not qualify as a public good because it is no longer abundant but scarce, especially in urban areas, and hence is the root cause of conflicts among uses and users. Secondly, consumption of water by one group of people (e.g. the rich in urban areas) excludes the others (in this case the poor). Consumers of water will also make choices depending on its quality. In fact the phenomena of population growth and environmental degradation have challenged the concept of public good. Even air is no longer a public good as it can be supplied as a private good in the form of air conditioning, for example. Pollution of water in both urban and rural areas makes it unfit for public consumption. The concept of water as a public good therefore is not tenable.

The other point proponents have raised is that water enterprise is a natural monopoly. Many writers agree that it is a natural monopoly (see for example Marvin & Laurie, 1999; Budds & McGranahan, 2003; Bakker, 2003b) because it requires a huge capital investment in plants and networks. Investing in plants and networks in the same geographical region in a competitive manner will be tantamount to gross misallocation of resources. However natural a monopoly it may be, does not explain why the natural monopoly must only be a public one. After all, it is easier to regulate a private monopoly rather than a public one. Secondly, there are innovative ways by which competition may be introduced, for example, competitive bidding.

Another point that has been propped up to back public provision is that water is a human right. We have seen that water is a basic need and is quintessential for life. It is for this reason that international conventions have endorsed water as a human right. Human rights can only be ensured by the state. However it does not mean the state has to engage in the provision of water in order to ensure human rights. The state only needs to establish a system of equity and justice that would ensure that such rights are not violated.

### *Private provision*

Private companies have been in the water sector as long as it has been in existence. Existing literature is very much conversant with this fact. Bakker (2003b) acknowledges the long history of private sector participation in water management both in the developed and developing world. Budds & McGranahan (2003) also note the fact that the first water and sanitation services were provided by the private sector to well to do communities who were able and willing to pay. But in the near past, private sector players have been confined to peripheral roles, away from the ownership and operation of main systems. In developed countries the sector has been responsible for technological innovations and solutions for water management and for the provision of commercial (bottled) water (While & Haughton, 2001). In developing countries, the sector has been responsible mainly for tankered water to unconnected or shortage-prone communities. Private provision in developing countries has been hampered by shortage of local capital and an underdeveloped private sector, among other things (Rakodi, 2000). It was not until recently that thinking on private provision took centre stage.

Those who support private initiative as a sustainable approach to service provision would rather see water as an economic good that can be exchanged in the market at a price. It does not mean that under public provision water has not been sold at a price. In practice it has been sold at a price that is not the market price. The market price is determined by demand and supply. The market price would allocate water according to competing uses, taking into account the opportunity cost. Water is a scarce resource nowadays and should therefore be used in a sustainable and economical way. By paying for water at market price, consumers within a particular use will face a situation where they only consume the amount of water for which they can pay. This would cut down on wastage that was rampant within the supply management approach under public provision. The current focus in demand management therefore has potential for conservation.

The other reason cited by the proponents of private sector approach is the obvious failure of the public sector to provide an adequate and sustainable supply for the urban population. This is in spite of the donor support that was available for it in the early days (Budds & McGranahan, 2003). Failure of the public sector is marked by: inability to extend services to the poor, inability to rehabilitate existing infrastructure, inability to recover cost for self-sustenance and dependence on the exchequer which has limited funds, among others. Donor funding is no longer available to address the enormous problems afflicting the sector hence the need to turn to private financing and control.

### *Paradigms and performance*

As the debate continues, it is imperative to note that theoretical constructs and empirical validations in economics do not unambiguously support the assumption that private ownership would lead to improved performance (Renzetti & Dupont, 2003). A general notion in the neo-liberal thinking is that there is a clear relationship between performance and ownership (Schulpen & Gibbon, 2001). According to Nellis (1994), private ownership will perform better than public ownership because: it establishes a market for managers, leading to higher quality management; capital markets subject private enterprises to greater security; private enterprises are much more subject to exit; politicians interfere less in the affairs of private enterprises than they do for public enterprises; and private firms are supervised by self-interested

board members and shareholders, rather than by disinterested bureaucrats. However, in the water sector some studies have proved the contrary to this assumption (see [Renzetti & Dupont, 2003](#)).

[Byrnes \*et al.\* \(1986\)](#) undertook a comparative study in the USA and found no difference in efficiency between public and private ownership. In contrast, [Lambert \*et al.\* \(1993\)](#) also undertook a study in the USA and found publicly owned water utilities to be more efficient. [Bhattacharyya \*et al.\* \(1994\)](#) also undertook a study in the USA and also found no difference in overall efficiency, but privately owned utilities were found to be technically inefficient. While in the UK, [Saal & Parker \(2001\)](#) found that privatization increased profits but not productivity. The case is therefore clear that in spite of the drive for privatization in the water sector, its main economic expectation of improved performance is not guaranteed by mere shift of ownership from the public to the private sector. [Grosh \(1991\)](#) carried out a study of public enterprises in Kenya and found “scant reason to expect that privatization will yield improvements in either efficiency or profitability”. But this should not be considered in the resolute sense in which it is expressed, as the study never took into account water enterprises that exhibit unique problems compared to other public enterprises.

### **Institutional models of water enterprises**

[Table 1](#) exhibits a continuum of possible institutional arrangements for the provision of water services, with public enterprise at one extreme and private enterprise at the other, while in between are various degrees of public–private partnerships. Traditionally, water services have been provided by the public sector. A water institution is termed public if (1) ownership is in the public sector and (2) control is in the public sector. Control is in terms of responsibility for day-to-day management of the utility. Privatization will occur with any introduction of private sector participation in the ownership and/or control of a water service institution. Privatization of water therefore refers to the process and outcome of the introduction of the private sector in the ownership and/or control of water utilities. The more the private sector is involved in the ownership and control of a water institution the more private sector oriented it becomes. The extreme case, where water utility is wholly owned and controlled by the private sector, is known as divestiture.

[Table 1](#) groups the arrangements as follows: (A)—those that involve both public ownership and public control; (B)—those that combine public ownership with private control and; (C)—those that involve private ownership and private control. Under all aspects of privatization, the public sector will always retain the responsibilities of tariff regulation and the monitoring of cost and quality. In this continuum, as we progress from A to C, the degree of private participation and that of autonomy increase and reach their highest under divestiture. Increased participation is assumed to promote autonomy and autonomy leads to efficiency in resource allocation.

#### *Public enterprise*

As we have noted, water has been traditionally provided through public enterprise. There are various reasons for this as discussed under provision paradigms. Public enterprise may be in the form of a government department or public corporation. For the former, local authorities have provided water

Table 1. Public–private continuum of water enterprises.

Classification	A1	A2	B1	B2	B3	B4	B5	C1	C2	C3
Responsibility/ Form	Public enterprise	Public PLC	Service contract	Management contract	Affermage contract	Lease contract	Concession contract	BOT	Joint venture	Divestiture
Asset ownership	Public	Public	Public	Public	Public	Public	Public	Private	Private	Private
Tariff regulation	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public
Capital investment	Public	Public	Public	Public	Public	Public	Private	Private	Private	Private
Cost and quality monitoring	Public	Public	Public	Public	Public	Public	Public	Public	Public	Public
Utility manage- ment	Public	Public	Public & private	Public & private	Private	Private	Private	Private	Private	Private
Operations and maintenance	Public	Public	Public & private	Private	Private	Private	Private	Private	Private	Private
Working capital	Public	Public	Public	Public	Private	Private	Private	Private	Private	Private
Commercial risk	Public	Public	Public	Public	Private	Private	Private	Private	Private	Private
Contract duration	Unlimited	Unlimited	1–2 years	3–5 years	8–15 years	8–15 years	20–30 years	20–30 years	Indefinite	Indefinite
City/country examples	Original set-up	Netherlands, Poland, Chile	Mexico City, Uganda	Johannesburg, Monagas State (Venezuela), Gambia	Côte d'Ivoire, Senegal, Guinea, France	Mozambique	Buenos Aires, Manila, La Paz, Nelspruit	San José, São Paulo, Cancún	Colombia, Czech Republic, Hungary, Poland	England and Wales
Private participation, Autonomy	Low	→								High

Source: Adapted from Stottman (2000), Onjala (2002) and UN-Habitat (2003); see also Budds & McGranahan (2003) and Bakker (2003b).

services predominantly. In this case the public sector wholly owns the assets, is responsible for all capital investment, is responsible for the management of the utility, is responsible for operations and maintenance, is responsible for working capital and bears the commercial risk of the whole enterprise (Table 1). In this case private participation is non-existent and the degree of autonomy is low because of political interference by public officials. Because of this, services tended to be inefficient and inadequate thus prompting the change to privatization.

### *Public PLC*

A public limited company (PLC) is a company limited by shares. A PLC can be private if the private sector holds the shares and public if the shares are held by the public sector. A public sector may incorporate a PLC in order to enhance its autonomy from public control so that it can compete in the market. However, generally, the public PLC model is similar to the public enterprise situation except that for the former, a company owned by the public sector but limited by shares is formed to undertake the management of the utility, while a public enterprise may be a statutory body or a government department. The utility company is subject to the same rules and regulations as any other limited company. Although the public PLC is owned by the public sector, it is expected to operate on a commercial basis that involves some degree of profit making. Local, provincial or national governments own its shares. In the public PLC model, the public sector will retain asset ownership, responsibility for capital investment and responsibility for working capital. The commercial risk will also remain with the public sector (Table 1). The private sector is not involved in any way in the management of the utility and in operations and maintenance except that business principles and practice are to apply. For that matter, private participation is non-existent and the degree of autonomy also remains low owing to public control. Public PLC models can be found in the Netherlands, Germany, Poland and Chile (UN-Habitat, 2003).

### *Service contract*

In a service contract, the public sector still retains ownership, control and responsibility for capital as in A1. The public sector also bears the commercial risk. However, when it comes to operations and maintenance of the system, the public sector retains overall responsibility but contracts out to the private sector specific services such as meter reading, billing and collection, equipment rental and construction of new facility (Onjala, 2002). The fees in a service contract are fixed per unit of work and are decided in advance. Owing to their low requirement for capital investment by the contractor, these contracts can last a period of 1–2 years (Table 1). A service contract allocates the least responsibility to the private sector and its examples can be found in Mexico City and Uganda (UN-Habitat, 2003)

### *Management contract*

In this case the public sector retains responsibility for capital investment and expansion of the system. However, the responsibility for operations and maintenance is transferred to the private sector by

contracting a private company (UN-Habitat, 2003). The private company is free to make management decisions without assuming any commercial risk (Onjala, 2002). The payment for a management contract can be fixed or performance related. According to UN-Habitat (2003), a management contract is generally used in cities and countries that the private sector consider too risky for long term investment. For that matter they may be initiated as a way of testing the investment environment and later on develop into concession contracts. A management contract typically would last 3–5 years. An example of this contract can be found in Johannesburg, South Africa.

#### *Affermage contract (the French model)*

*Affermage* is a French term derived from the historical practice of the French land tenure system. For that matter the term derives its roots from the following French words: *ferme*—farm, *fermier*—farmer and *fermage*—farm rent. It simply means a lease. *Affermage* and concession contracts are common in France (Renzetti & Dupont, 2003). This explains why *affermage* is the most preferred model for Francophone Africa. An *affermage* contract is similar to a lease contract. Under an *affermage* contract the operator is paid an agreed-upon *affermage* fee for each unit of water produced and distributed (Budds & McGranahan, 2003), whereas in the lease contract, the operator's fee is dependent on the amount of tariff collected *vis-à-vis* the standard lease fee payable to the public sector. Like a lease contract, the *affermage* contract will typically last 8–15 years. Example of an *affermage* contract may be found in Côte d'Ivoire (Bi, 1996), as well as other Francophone West African Countries.

#### *Lease contract*

In a lease contract, the public sector rents out the entire operation and maintenance of the water utility to a private operator. The operator consequently assumes the operation, maintenance and management of the utility. However the public sector remains with ownership of the assets and is responsible for capital investment. In a lease contract the operator collects tariff, then pays the lease fee to the public sector and retains the difference (UN-Habitat, 2003). A lease contract may last 8–15 years.

#### *Concession contract*

In a concession contract, the private contractor has overall responsibility for the utility, including financing, but ownership still remains with the public sector. In this case the contractor operates the system at its own commercial risk. However, in practice, the contractors always seek to minimize the risks by negotiations and in contractual agreements (Loftus & McDonald, 2001). The contractor is also responsible for expansion of the system apart from normal maintenance. A concession contract takes a longer period of time, usually 20–30 years in order to give the contractor time to recoup its capital investment. Upon expiry of the contract the assets revert back to the public sector including the expansion made by the contractor. In a concession contract the government only assumes the role of regulation and monitoring as indicated in Table 1. An example of a concession is found in Buenos Aires, Argentina where *Aguas Argentinas S.A.* has contracted a water utility from *Obras Sanitarias de la Nación*—OSN (Pirez, 1996; Schneier-Madanes, 2001).

### *Build-Operate-Transfer (BOT)*

BOT is variably referred to as BOOT—Build-Own-Operate-Train, BOO—Build-Own-Operate and BOTT—Build-Own-Train-Transfer (Budds & McGranahan 2003). The contractual conditions of BOT are similar to that of the concession contract. But concession as a process is more of a reverse BOT because it involves transfer of ownership and control from the public sector to the private sector, while BOT involves transfer from the private sector to the public sector after fulfilling private economic interests. However, the main difference is that in the case of BOT, the private contractor is responsible for building the infrastructure right from scratch (unlike in a concession where the infrastructure is already built by the public sector). It then operates it for the contractual period in order to recoup its investment. Upon expiry of the contractual time the private operator transfers the facility to the public sector. In the water sector, BOT arrangements can only work for water and sewage treatment plants. It is rarely applied to distribution networks as these are normally already built (UN-Habitat, 2003).

### *Joint venture*

This is a case in which the private sector and the public sector jointly form a private company. The joint company thereafter may directly undertake provision of water services as a private entity through any possible public–private sector arrangements.

### *Divestiture (the English–Welsh model)*

The English–Welsh model is the extreme end of privatization. It involves outright sale of assets to a private company that then takes over their operations and maintenance on a permanent basis. The utility is operated on business principles. The public sector may also sell its ownership in terms of shares in the stock market. In this model the government is also only left with the regulatory and monitoring roles, while the private sector takes over ownership, control and capital responsibilities. But the private company is not free to operate like any other company. The water company is subject to extraordinary regulation; for example, normal bankruptcy rules do not apply in its case (UN-Habitat, 2003). This in a way limits its efficiency as a private sector outfit since the threats of takeover and bankruptcy are eliminated. Divestiture is similar to concession and BOT except that the others are terminal while it is permanent. This model, as the name suggests, has been implemented in England and Wales (Bakker, 2003a; Frade & Sohail, 2003).

## **The concept of commercialization**

Privatization and commercialization can be two confusing concepts. Is commercialization a subset of privatization or is it the other way round? Rakodi (2000) views commercialization as an attempt to create quasi market conditions in public service delivery through increased cost recovery and introduction of performance measurement systems. In making a distinction between the two

concepts, Bakker (2003b: 331) deems commercialization to refer to “a networking of the management institutions (rules, norms and customs) and entails the introduction of markets as allocation mechanism, market stimulating decision-making techniques and the displacement of Keynesian-welfarist by neo-liberal principles in policymaking”. Commercialization, according to the two writers, is simply a culture of or discipline in transacting business. This culture may be introduced both under public or private enterprise. The introduction of business principles and management techniques into the public sector is what is known as the new public management paradigm (Drechsler, 2004 and König, 1997). Jaglin (2002) has defined commercialization as a form of privatization involving the transformation of a public body into a private company with public capital common in Anglophone Africa. A study of privatization trends in East Africa conducted in 1998 found out that commercialization was the most common form of privatization for the water sector in this region (UNCHS, 1998a). In this case commercialization was conceived to denote operation of enterprises on business-like principles that would achieve efficiency and profitability. In this case, commercialization entailed incorporating water and sanitation public PLCs that were owned by the respective local authorities (Onjala, 2002; K'Akumu & Appida, 2006). The local authorities in Kenya introduced commercialization as a strategy for ensuring sustainable and efficient delivery of water and sanitation services (UNCHS, 1998b). The performance and management of these services had deteriorated owing to factors common in public sector provision (see, for example, Anton, 1993; Khan & Siddique; 2000; Biswas, 2001; Ahmed & Sohail, 2003; K'Akumu, 2004).

For example, according to Khan & Siddique (2000), problems of public sector provision like poor billing and collection practices, high levels of unaccounted for water, and high default rates and arrears, are principally caused by lack of commercial orientation in service delivery characterized by lack of accountability and poor management systems. By implication, therefore, commercialization could eliminate all these and related problems. It is actually possible for commercial operation to solve common problems facing public provision in Kenya such as non-cost recovery tariffs, delays in approval of tariff increases, diversion of water revenue to meet unrelated expenditure, difficulties in the recruitment and retention of professionally and technically qualified top and middle management staff, deferred maintenance of facilities, high water losses, and low billing and collection efficiency (derived from the example of the Eldoret Municipality: UNCHS, 1998b).

Bakker (2003b) put liberalization as a key element of commercialization. Liberalization in this case entails selective deregulation and re-regulation designed to allow and encourage competition in the product market. UNCHS (1998b) on the other hand has likened privatization, read commercialization, to decentralization. In this case decentralization as a political and administrative transformation epitomizes a shift in the locus of power from one level of government to another, in the same way that privatization shifts responsibility from government to the non-state sector. Given that commercialization in the example of East Africa was meant to overcome the hurdles of centralized government control and also that it involved a shift of control from one public sector to another (K'Akumu & Appida, 2006), commercialization is objectively similar to decentralization.

Lastly, relating commercialization to privatization is not difficult. Privatization means the transfer of public sector assets, control and financing of water enterprise to the private sector. The private sector, on the other hand, is known to transact its business for commercial gain. Therefore, as Bakker (2003b) concludes, private sector participation and/or privatization of water supply often implies commercialization.

## Reaction to water privatization in developing countries

There is mounting opposition to privatization of water in developing countries, especially from the civil society and consumers. A case in point is Bolivia, for example, where in Cochabamba, the third largest city, it was found necessary to privatize water (Marvin & Laurie, 1999). For that reason in 1999, the government granted a 40-year concession to private practitioners (Italian-owned International Water Limited and US-based Bechtel Enterprise Holdings) to run the city's water system—a move that was intensely opposed by the civil society (La Coordinadora) leading to the cancellation of the contract (Grusky, 2001). Bolivia stands as a unique example of a country where privatization has slim chances of survival. The privatization of water for El Alto City by *Aguas Illimani* that took place in 1997 has also been reversed owing to civil protests (NACLA, 2005). Nickson and Vargas (2002) report that Cochabamba was not the first water privatization fiasco in a developing country, citing the case of a provincial water concession in Tucumán, Argentina that had been awarded to Vivendi in 1995. In 1998 the privatization was reversed following civil protests.

In Africa there have been reported protests in South Africa against Suez, a foreign water company, over excessive profits and high service charges, while in Ghana, the civil organization National CAP of Water led protests against privatization of water (Grusky, 2001). Developing countries must therefore be cautious in the privatization process. Kenya as a developing country is also likely to face such opposition in the case of full privatization. Nevertheless, there is a pressing need to review the public sector's role in water provision. This need has been expressed on many occasions (Republic of Kenya, 1996; Onjala, 2002; K'Akumu, 2004; K'Akumu & Appida, 2006).

## Privatization policy in Kenya

Privatization in Kenya has proceeded haphazardly so far. This is because there has been no proper policy guideline. The first round of privatization was executed on a sectoral basis and took place mainly in the late 1980s and early 1990s. This involved financial corporations and utility corporations like electricity, telecommunications and water. Privatization of the concerned enterprises were guided by privatization policy entrenched through the revision of statutes for the concerned sectors or corporations. Privatization in Kenya began with a divestiture exercise that saw the government sell proportions of its shares in the public enterprises to cooperatives or dispose of public enterprises assets through receivership or winding up (Karanja, 1989). This mainly affected the financial, communications, energy and manufacturing sectors. The government, for example, pulled out of air travel and the petroleum markets. All this happened without a comprehensive national policy on privatization. Moreover privatization was implemented at the behest of the World Bank (Alexander, 1989). In this case the World Bank identified enterprises or sectors suitable for privatization and earmarked them for the same.

The second round of privatization is yet to come following the publication of The Privatization Bill, 2004. This is a comprehensive national policy framework that is to be put in place to manage the privatization process in Kenya. The law is quite useful to the extent that it defines privatization as “(a) The transfer of public entity's interests in a state corporation or other corporation; (b) The transfer of the operational control of a state corporation or substantial part of its activities”, to a non-public entity (Republic of Kenya, 2004: 55). This conforms to the standard definition of privatization as a process of

institutional change that has been expressed earlier in this paper. The law expects privatization to bring out the following benefits to the Kenyan economy:

1. the improvement of infrastructure and the delivery of public services by the involvement of private capital and enterprise;
2. the reduction of demand for government resources;
3. the generation of additional government revenue by receiving compensation for privatization initiatives;
4. the improvement in regulations of the economy by reducing conflicts between the public sector's regulatory and commercial functions;
5. the improvement in the efficiency of the Kenyan economy by making it more responsive to market forces; and
6. the broadening of the base of ownership in the Kenyan economy and the enhancement of capital market development.

These benefits may also be considered as the principal objectives of privatization of public enterprise in Kenya. Any sectoral privatization policy must therefore conform to these national objectives. It is these objectives that are expected to guide the formulation and implementation of a privatization programme that the bill stipulates the formulation of under Part II. Under Part III the bill provides details of the official procedure for privatization. Under Part IV, it establishes a Privatization Commission to “formulate, manage and implement” the Privatization Programme. The privatization objectives are adequate and acceptable for Kenya. They are also conventional and universal in application. This review will therefore rely on them in evaluating the privatization endeavours in the water sector.

### **Privatization in the water sector**

As we have noted, privatization of the water utility is one of the earlier privatization initiatives that took place in Kenya outside the provision of a national policy framework. Yet in the water sector itself, privatization had begun earlier on before a sectoral policy framework was put in place (K'Akumu, 2004). The sectoral framework came into being in the name of the Water Act of 2002 (Republic of Kenya, 2002). The new Act came into actual implementation in March 2003 (Water Sector Reform Secretariat, 2005). The new Act was enacted to repeal the erstwhile Water Act chapter 372 of the laws of Kenya that had been in operation since 1962 (Republic of Kenya, 1972). This was done in order to usher in reforms in the water sector. The reforms are entrenched in the new Act in two main aspects; the management of water resources and the management of water services. The latter is considered under Part IV of the Act covering water supply and sewerage.

#### *Creation of water service institutions*

*Water Services Regulatory Board.* The new Act establishes a regulator in the name of the Water Services Regulatory Board (WSRB) to regulate the water market. The WSRB is responsible for the fixing

of tariffs, ensuring cost-effective and efficient operations, and promoting water conservation and demand management measures, among other things. These functions point to the market-oriented paradigm of service provision.

*Water Services Board.* The Act also makes provision for the creation of Water Services Boards (WSBs). The WSB as a statutory creation is therefore incorporated as a public enterprise. The Act states that “the water services board shall by force of this section be constituted a corporation” (Republic of Kenya, 2002: 982). In implementing the Act, the minister in charge of water services has gazetted seven WSBs as regional bodies in charge of water provision (see Table 2).

The WSB is to be licensed by the WSRB, a fellow public body, for the purposes of providing “efficient and economical” water services.

*Water services provider.* After the WSB has been licensed, it is expected to contract the licence to an agent, in this case designated as Water Services Provider (WSP), which is to be responsible for direct water service provision to the consumers. There is an express rule that water services must be provided by an agent (WSP) “except in circumstances where the Regulatory Board [WSRB] is satisfied that the procurement of such an agent is not possible” (Republic of Kenya, 2002: 983). In practice the state has gone ahead to incorporate PLCs to play the role of WSPs. The Act does not provide for the formation of PLCs; this could be a matter of administrative decision. Nevertheless, the effect is that all actors in the Kenya “market” are from the public sector.

#### *Transactions among water institutions*

*WSB and WSPs.* There is division of labour between the WSB and WSP. The main role of the WSB is asset ownership and financing. Section 53(2) states that a WSB is mandated to “purchase, lease or otherwise acquire on such terms as the Minister may approve, premises, plant, equipment and facilities; and purchase, lease or otherwise acquire land, on such terms as the Minister may approve” (Republic of Kenya, 2002: 983). A WSP on the other hand is generally responsible for operations or control of water assets, although the degree of responsibility may be varied according to the agency agreement between the two bodies.

Table 2. Gazetted Water Services Boards.

Name of WSB	Number of districts	Area (km <sup>2</sup> )	1999 Population
Coast	7	82,816	2,487,000
Nairobi	6	40,130	5,617,000
Central	13	52,777	5,032,000
Rift Valley	8	113,771	2,999,000
Northern	9	244,864	1,703,000
Lake Victoria North	11	16,977	5,135,000
Lake Victoria South	16	20,340	5,730,000
Total	70	571,675	28,703,000

Source: Water Sector Reform Secretariat (2003: 6).

The relationship between the WSB and WSP is crafted in a mock market model. The assumption seems to be that WSPs, whether private or public, have the chance to compete to enter into agreement with a WSB that is the sole licensee to be given the opportunity to provide services. However, this is a mock chance because it presents a situation in which a public body is competing with private sector players for a tender from a public body. Obviously, the public body would win. In practice, bidding does not take place. The PLCs have been formed and directly handed over the functions of Water Services Departments (WSDs) without consideration of private sector actors (see [Figure 1](#)). Other actors are locked out unless a WSB decides to engage any. The law clearly states that “no person shall, within the limits of a supply licensee [WSB]—provide water services. . . except under the authority of a licence” ([Republic of Kenya, 2002: 985](#)). Authority of a licence means only a situation whereby a WSB has engaged a WSP for service provision.

*WSRB, WSBs and WSPs.* The relationships created among the public enterprises are rather farcical. For example, why does the law require a WSB to apply for a licence when the said law also says that only a WSB can apply for the licence? If the law has already said that only a WSB can apply and get a licence and given that a WSB is the only applicant, it will definitely get it since there is no competition. Commercialization or privatization aims to create market competition for efficient allocation of resources. As pointed out by [Budde & McGranahan \(2003\)](#), given that water enterprise is a natural monopoly, competition is only possible for the market and not within the market. Here is a case in which the market has been allocated by legal decree to a public enterprise in spite of the claim of commercial objectives.

Secondly, a PLC, which is a public enterprise, has to enter into an agency agreement with the WSB that has to be endorsed and overseen by the WSRB. All these are public institutions participating in the water market. Thirdly, under section 60(1), WSB as a licensee is supposed to pay the state “on issue of the licence and at prescribed intervals thereafter, such fees as Regulatory Board [WSRB] may determine” ([Republic of Kenya, 2002: 989](#)). This payment is not a benefit from privatization as it is only a transfer of funds from one public sector to another. In essence, it is a situation in which public enterprises trade among themselves and call it commerce.

### *Commercialization*

Where is the privatization aspect of the whole set-up? The law only alludes to privatization or commercialization. One of the conditions attached to the approval of an application for a licence is that “the applicant [WSB], or any water service provider by whom the functions authorized by the licence are to be performed will provide the water services authorized by the licence on a commercial basis and in accordance with sound business principles” ([Republic of Kenya, 2002: 987](#)). Beyond this pronouncement, there is no instrument or strategy for achieving “commercial basis” or “sound business principles”. The Act does not create by any means a market-oriented water supply system.

### *Overall institutional structure*

[Figure 1](#) is a comparative schematic presentation of old and new institutional structures of the water sector. Level 1 is the point of service provision (i.e. operation and management of water assets).

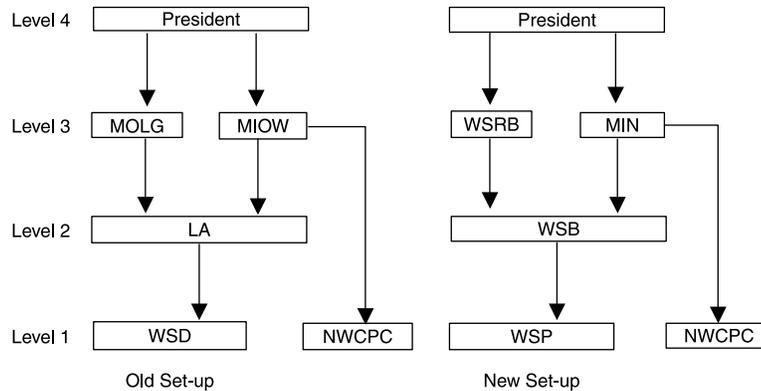


Fig. 1. Institutional set-up for water supply management in Kenya.

In the previous set-up, this was undertaken by the Water and Sewerage Departments (WSDs) of local authorities. This has been taken over by WSPs, which are public owned limited companies.

Level 2 is the level of asset ownership. It is also the level where investment decisions are made and implemented. In the old set-up, local authorities that were water undertakers occupied this position. For local authorities that were not water undertakers, water was directly provided by NWCPC (National Water Conservation and Pipeline Corporation), a state water enterprise. There were also instances where NWCPC supplied water in bulk to the local authorities, which then distributed it to the consumers through their own networks, as in the case of Nakuru Municipal Council. This set-up was problematic, especially because of the connections between levels 2 and 3. The local authority was being controlled by MOLG (Ministry of Local Government) through the Department of Urban Development on general administration and investment issues and by MIOW (Ministry In Charge of Water) through the Department of Water Development. Both departments were headed by directors. These two centres of control at times were not in concert hence causing instability in decision making at Level 2. The new set-up has proposed that WSBs take the position of local authorities. But the problem is not clearly solved, as both the minister and the WSRB will directly control the WSBs (K' Akumu, 2006). At the same time, the minister to some extent is in control of the affairs of the WSRB. Otherwise the WSRB is assumed to be autonomous. Overall, just as the local authorities were not autonomous, WSBs shall remain the same way, under the control of the minister and the WSRB.

Level 3 actually represents the centre of control both in the old and new set-ups. In the old set-up the ministries, through directors of urban and water development departments, exercised control over local authorities concerning the management of water provision. In the new set-up, the position, as decreed by law, has remained with the minister in charge of water who, to some extent, shares the powers with the WSRB. Nevertheless, the WSRB is somewhat redundant given its position as a national public body regulating seven regional public bodies that are also directly under the direction of the minister. In the final analysis, decision making is still centralized at the national level.

Level 4 is the President who wields inter-sectoral and inter-ministerial executive powers and could have overall say, directly or indirectly, over matters of water management. The situation remains the same both in the old and new set-ups. Unlike the minister, the President has a limited direct influence on

the WSRB apart from appointing its chairman. The minister on the other hand singly appoints its twelve board members and gives it directions.

Lastly, the NWCPC is a public enterprise that was operating in the old set-up under the auspices of the Water Department and was involved in the supply of water at the national level and this is retained in the new structure. In the new set-up, the NWCPC has been retained under the auspices of the minister to provide water services where no applicant has qualified for a licence, or where the licensee is in default, or in cases of emergency shortages. Also, according to section 22(4), NWCPC is responsible for “development works and management of assets for the purposes of a state scheme for the provision of bulk water supplies for use by licensees [WSBs] and water service providers [WSPs]” (Republic of Kenya, 2002: 959). Now, who said there is privatization?

From Figure 1 we can see that the old set-up and the new set-up are symmetrical and hence there is little change. Elsewhere, the author has argued that the new structure characterized by unaccountable public participants does not promote good governance (K'Akumu, 2006).

## Recommendations

The government claims that its reforms in the water sector via the Water Act of 2002 places emphasis on “enhancing the role of private sector participation” for sustainable services (Water Sector Reform Secretariat, 2005: 6). However, from the foregoing discussions, the private sector is not involved in any demonstrably significant way. Hence privatization remains a mere claim by the government which is reluctant to release the sector to private participation.

If privatization were to take place, it would have to be guided by the benefits/goals of privatization as spelt out in the national privatization policy (see 1–6 under ‘Privatization Policy in Kenya’). The said goals have not been realized by the reforms as legislated and implemented by the government. Therefore the reforms are not serving any privatization purpose.

In terms of institutional analysis, the resultant institutional framework does not entrench privatization at all. By going for a public PLC model, no privatization, or commercialization for that matter, can be said to have taken place in Kenya’s water “market”. The system remains a public-own-operate affair with extra bureaucratic baggage in the name of WSRB (see Figure 1). In this system, public enterprises are expected to regulate or trade with other public enterprises. This is contrary to Al-Jayyousi’s contention that that the government is more likely to criticize and act against a private operator than a government corporation (see Al-Jayyousi, 2003).

Secondly, this is contrary to objective 1 as expressed in the Privatization Bill. Under objective 1, the government intended to improve public services by engaging private resources. The move also contradicts objective 3 concerning revenue generation from the private sector, objective 4 of reducing conflicts between the government’s regulatory and commercial functions, objective 5 of leaving the economy to the forces of the market and objective 6 of enhancing capital market development.

Thirdly, the dominance of public institutions means that no attempts have been made to capture private sector financing or transfer technical know-how. All the institutions remain public in character contrary to the requirement of objective 1 for involvement of private capital and enterprise and objective 2 for reduction on demand of government resources.

Other general benefits associated with privatization have also not been met in the reform endeavour. These include decentralization and liberalization. There is no difference from the past as

the system is still centralized (see [Figure 1](#)). This is unfortunate, as previous attempts at privatization had intended to decentralize the system in order to improve its efficiency ([UNCHS, 1998b](#); [Onjala, 2002](#); [K'Akumu & Appida, 2006](#)). Liberalization was also expected in the drive for reforms. This would promote private sector participation and autonomy of service management. This was another objective of the early attempt at privatization. The outgoing system entertained too much central and local government interference with operations. These interferences were responsible for inefficiency in the operation of the previous system. Yet the present system has not adequately addressed these issues.

The case of Kenya can be generally stated as that of “putting the cart before the horse” in the process of policymaking. We have seen that privatization has taken place in the sectors since the 1980s without a clear national policy. In the water sector in particular, privatization endeavours started in the 1990s, way before the establishment of the policy mechanism for privatization, which later came up in the form of the Water Act of 2002 ([K'Akumu, 2004](#)). Hence the early endeavours were flawed owing to lack of policy direction ([K'Akumu & Appida, 2006](#)). This review also indicates that the policy mechanism is flawed since it was put in place without being given direction by a national framework for privatization. The mechanism, in the form of legislation, was enacted in 2002, while the framework in the form of a bill was published in 2004 and is yet to undergo the process of legislation. This is the reason why there is a mismatch between the two.

The way forward is for the government to go ahead with the enactment of the Privatization Act and hence require all the sectoral reform initiatives to comply with the objectives of the Act. The Act will form a comprehensive national policy framework in which the water reform policy should fit. This will give the water sector a clear direction on how to proceed with market reforms. For this to happen smoothly, an overriding clause should be included in the Act to the effect that, past reforms notwithstanding, all sectors should conform with the Act to the extent that these sectors need to privatize services. As of now, it can be said that it is the government that is dragging its feet on the issue, given that the bill has not been pushed through Parliament for almost two years since it was published. This shows that the government is generally not fully committed to privatization. It should move fast to enact the privatization law and make it operational as recommended.

Lastly, [Table 1](#) presents a very important consideration when making recommendations on which privatization model would suit Kenya. As it has emerged, A1 and A2 are virtually the same, hence moving from public enterprise to public PLC does not constitute any significant change. We have also noted that the flash point for water privatization in developing countries is B5 (concession), as the case in Bolivia would attest to. It is also notable from [Table 1](#) that most African examples fall under B1–B4. Kenya, as a developing country and an African nation, would therefore be comfortable within this range.

## **Conclusion**

This paper intended to carry out an analysis of the resulting institutional set-up following the reform of the water sector in Kenya. It particularly picked on the issue of privatization in the sector. Privatization involves transformation that moves ownership and/or control of water utilities from the public to the private sector. There are various shades of public–private interplay as summarized in [Table 1](#). The analysis has shown up the fact that Kenya has settled for commercialization through public PLCs.

Commercialization is a form of privatization that introduces commercial norms and practices in the management and operations of a publicly owned enterprise. The public PLC has been cast in an institutional framework that includes statutory enterprises like the WSRB—a national regulatory institution and WSBs—regional asset owning enterprises.

An evaluation of this institutional framework has indicated that no privatization has taken place. All the institutions legalized to operate are public, yet there are no structures and systems for ensuring that they operate in a way that may bring commercial benefits. So far privatization only exists in the pronouncements of policy makers but not in the policy framework and practice. For that matter, none of the desired benefits of privatization can be achieved. Therefore, the possibilities that problems besetting public sector provision of water services would be offset through water sector reform (in the name of Water Act of 2002) is left in doubt.

The inability to achieve privatization objectives can be blamed on a process of policy making that is not well coordinated. Policy reforms regarding privatization have been starting at the end points, as has been pointed out in the recommendations. But the government now has a comprehensive policy framework on privatization that it needs to put in place. However, it seems the government itself is reluctant to see the policy through. This begs the question, who was pushing the government into privatization that it seems to have no heart for? Is this the same reluctance we see in the water sector where we are privatizing and not privatizing?

Finally, the advice to the government is that it had better be serious about privatization, it has to enact the Privatization Act and then make the water sector conform to it. As it is, some degree of privatization is vital for the water sector, but as a developing country, the government should not go full blast. Neither should it pretend to be privatizing while in the real sense it is increasing public bureaucracy.

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