WATER NOT FOR ALL: THE CONSEQUENCES OF WATER PRIVATISATION IN JAKARTA, INDONESIA[1]

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INTRODUCTION

There is a growing trend towards water privatisation[2] in all parts of the world. By 2003, at least 55 countries had privatized water services, and the fastest privatization has take place in East Asia in the 1990s (Prasad 2006). In total, during the period of 1990 to 2001, the private sector has been involved in more than 2000 water and sewerage projects in developing countries (Kirkpatrick and Parker 2005).

In Indonesia, privatization of local water companies has become a dominant approach taken by the government to solve water crisis, as a part of 'water reform' process. This process is a part of structural adjustment reforms required by the World Bank and the

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[2] Three types of water privatization (Kickpatrick and Parker 2005, Barlow and Clarke 2002):

a. Full privatization: governments completely sell-off water system to private companies (eg. UK).
b. Concessions or Public-Private Partnerships: private sectors take over the service deliveries, managing the system, collecting the revenues and keeping the surplus as a profit.
c. Others: BOT schemes, private sectors are contracted for and administrative fee

International Monetary Fund (IMF) in exchange for a US$ 46 billion loan package during the 1990's economic crises (Zaman 2003). This process, supported by the World Bank's Water Resources Sector Adjustment Loan lead to the establishment of the 2004 Water Law, which provides legal justification for privatization. Hence, since 2004 the Indonesian government has started to implement a plan to privatize 80 – 90 % of the local water companies. Water privatization took place rapidly, at least in eight areas of highly populated cities in Indonesia, and in 2005 solely there were 20 water projects offered to the private sector (Kompas, 15 February 2005).

With this growing trend of water privatization in Indonesia, it is important to investigate whether privatization has been and likely to be the best solution for water crisis. In this paper I will discuss water problems in Indonesia, with a specific case of Jakarta's water privatisation and the social, economic and environmental consequences to follow the privatisation. A decade of Jakarta water privatization could provide a unique setting to investigate the consequences of water privatization, and thus it could become a lesson to learn for the current government's policy towards privatization. In this paper I will argue that the assumptions underpinning water privatization as a better solution to water crisis have not been proven in the reality of water privatization in Jakarta.

JAKARTA'S WATER PRIVATISATION

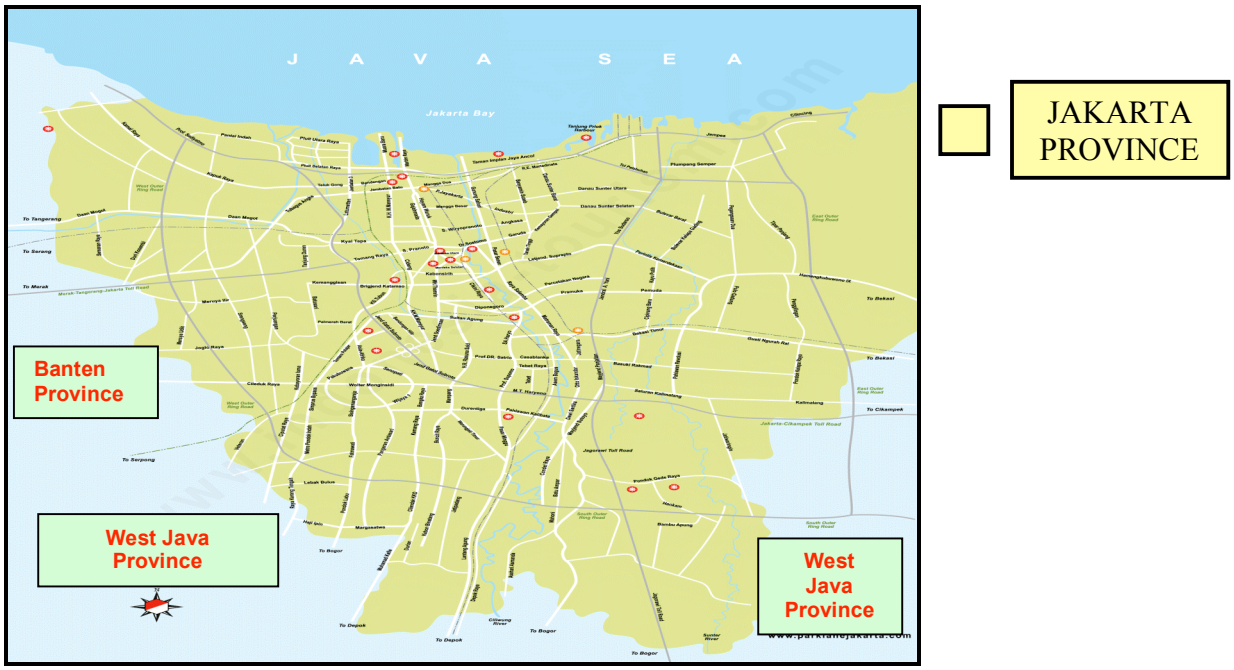
In order to provide the context of water privatization, I will firstly describe the current Jakarta water supply system. There are two types of water supply system in Jakarta: the formal water supply system and informal system. The informal water supply system includes, for example, water vendors, private wells, bottled water and bore water. Meanwhile, the formal water system is piped water system inherited from the Dutch during the colonial era. After independence, this piped water system is managed by the government, via the local water company PAM Jaya, until 1997 when it was privatized.

The piped water supply is not available for all populations in Jakarta. In 2007, only around 61 % of Jakarta residents has accessed to this system while the rests of the

residents rely on informal water supply (JWRB 2007). This problem relates to the demographic and geographic challenges in the management of piped water. With around 10 million people living in Jakarta in 2007, fulfilling the demand for safe water has been problematic because of limited capacity of the piped water facilities. This problem is complicated by its geographical location which affects the raw water supply for the city. The city is surrounded by the West Java province to the east and south side, Banten province to the west and the Java Sea to the north (see figure 2).

Raw water supply for Jakarta originates mainly from the Citarum River in West Java which is used through several dams (Saguling, Cirata and Jatiluhur). Water from the dams is distributed through 70 km-long West Tarum Canal, an open canal which flows through industrial and settlement areas so that pollution level is very high (Tutuko 2001). These dams are also used for other purposes such as power generation, tourism and irrigation, therefore securing a raw water supply requires coordination with other users. Other sources of raw water for example from Cisadane River (15%) and Ciliwung, Krukut and Pesanggrahan (5%) are also highly polluted. Meanwhile, alternative water sources such as ground water are limited, especially in the coastal areas in the northern part of Jakarta. Even where ground water is available, the contamination level and the impacts of excessive abstraction have become a great concern.

Figure 2. Jakarta Map and its boundaries

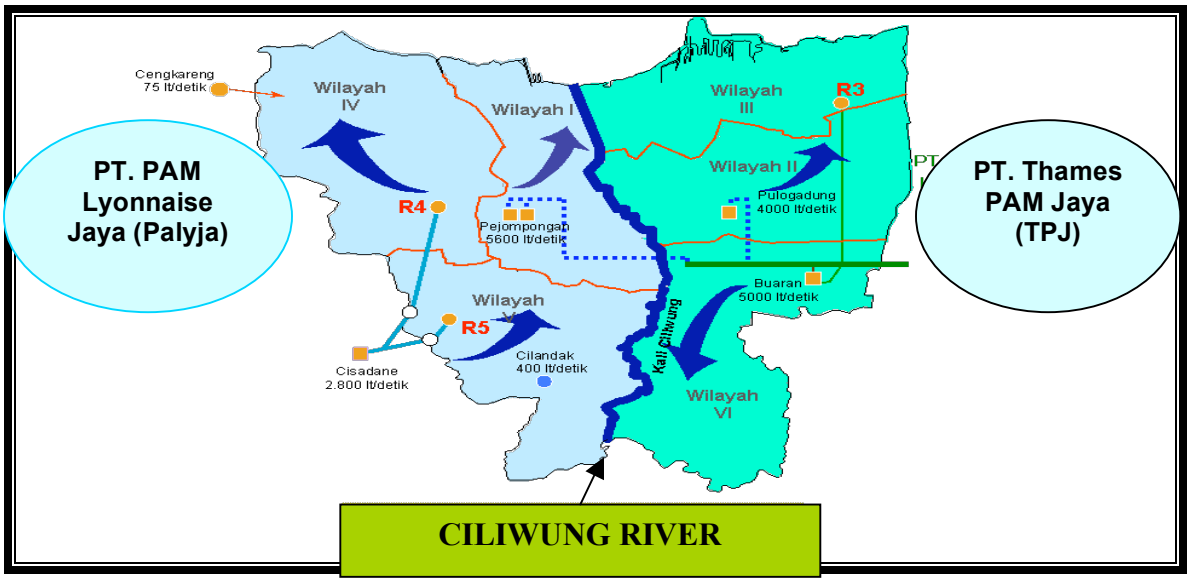


Adapted from www.indonesia-tourism.com

Water Privatisation in Jakarta

In 1998, the formal water system was privatized, and the management changed from PAM Jaya, the local government's water company, to two private companies: Thames Water Overseas (partnership with PT. Kekar Pola Airindo) and Suez Lyonnaise des Eaux. (Ondeo) (partnership with PT. Garuda Dipta Semesta). These companies were awarded contracts for 25 years to run the water supply system in Jakarta. These two local partners of Thames and Suez were owned by Suharto's son and crony (Harsono 2003). The Jakarta water system was then divided into two service areas; Western sector is operated by Ondeo, through the locally established enterprise PAM Lyonnaise Jaya (Palyja) and the Eastern sector which is operated by RWE Thames through PT. Thames PAM Jaya (TPJ) (Lanti, 2006). The boundary between the Western and Eastern sector is the Ciliwung River (see figure 1).

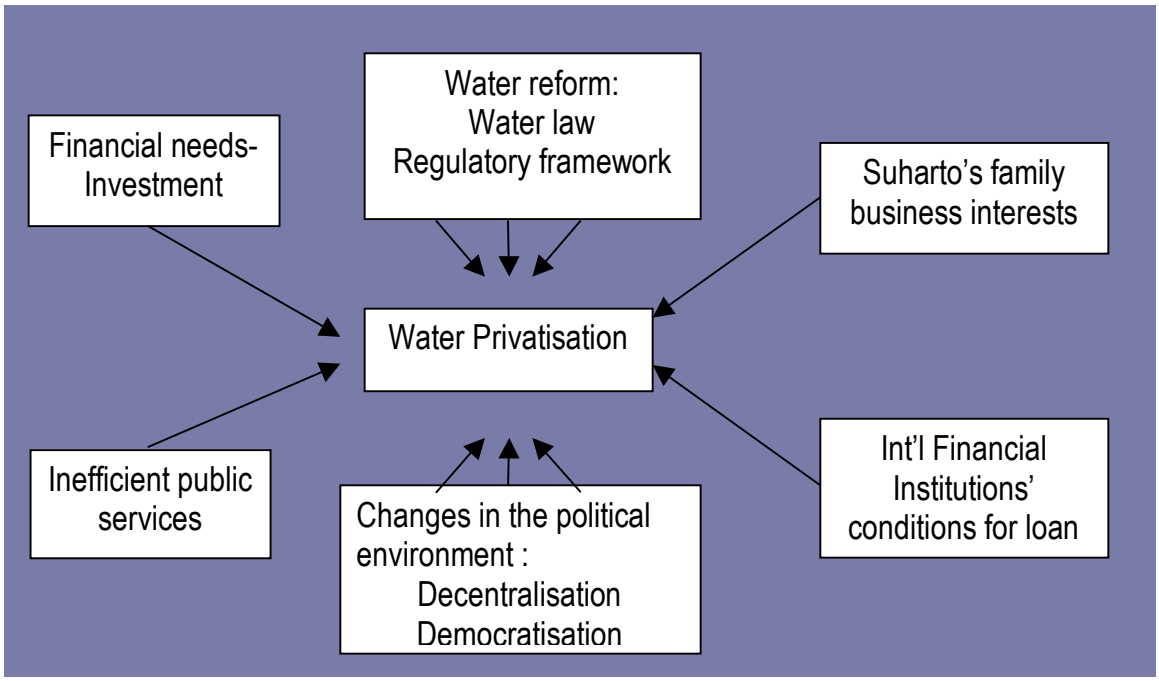
Figure 1. Two services area of Jakarta water supply



Source: Adopted from PAM Jaya

There are several factors that influenced Jakarta's water privatization. PAM Jaya which had main responsibilities to provide and distribute safe drinking water (Regional Regulation No. 13 1992) faced complex problems: limited distribution of water, aging infrastructure, and financial constraint. Until 1998, PAM Jaya distributed water only to 51 % of the population. PAM Jaya needed to rehabilitate old facilities, however, it had limited financial capacity and thus desperately need new investments. Concurrently, since the 1990s the Indonesian government has been also attracted to the concept of water as an economic good and a cost- recovery tariff promoted by international financial agencies. At the same time, Thames Water, then followed by Suez, had approached Suharto government to involve in Jakarta water business and it had also established cooperation with a local company (Harsono 2003). Figure 2 illustrates the series of factors that encourage the government to privatized water.

Figure 2: Factors in Jakarta privatisation



Privatisation was believed, especially by international institutions such as the World Bank, as a promising solution for water problems. Lee and Floris (2003) suggest that private sector participation is necessary to fulfill the need of large investments for water infrastructure. The World Bank is confident that privatization is the solution for water problems (Kessides 2004). The private sector was considered to have better managerial capacity, stronger financial capacity, and better experiences and technological capacity to solve the problems of supply adequate water to Jakarta. It has become evident in Jakarta, however, that these assumptions have not been realised, and problems exist despite of being a decade since privatisation.

PROBLEMS OF WATER PRIVATISATION IN JAKARTA

Three fundamental problems underlying water privatisation in Jakarta are, as follows: governance problems, regulatory problems and technical performance problems. The governance problems include three aspects: legal problems, lack of tendering process, and lack of public involvement and transparency.

Remarkably, privatisation is against the Indonesian Constitution and other regulations. The Article 33 (3) of the 1945 Constitution states:

> 'Land, water and all of the embedded resources are controlled by the State and are used for the best interests of the people'.

The Water Resources Law 11, 1974 and Government Regulation 22, 1982 also provided legal justification for the State management of water. In addition, the Foreign Investment Law also excluded water from the sectors in which foreign companies could invest. However, the regulations were changed to enable the transfer of control from the public sector to the private sector. For example, in 1996, the Instruction of Minister of Home Affairs No. 21 1996 set up procedures for private sectors to invest in water sector in Jakarta. Thus, privatization occurred despite it being against the Constitution and the Laws. The only legal basis for water privatization in Indonesia is New Water Law 2004 which legally justifies privatization to fulfill the investment needs (Water Law 2004). However, this Law cannot legitimize the Jakarta water privatization which occurred six years earlier. In addition to these legal issues, the private companies were directly appointed by the government without transparent tendering. The public was also excluded from this process (Harsono 2003).

These problems have created prolonged conflict in the Jakarta water management. It can be seen, for example, when president Suharto fell from power in May 1998, the privatisation contracts were considered illegitimate by PAM Jaya employees and NGOs as public sentiments against Suharto-related businesses heightened. PAM Jaya attempted to regain its previous authority especially when the Thames and Suez's executives fled Jakarta and left Jakarta water management unattended during the crisis (ICIJ 2003). These factors added pressure to the Habibie government, successor of Suharto, to cancel the contracts. However, the government was reluctant to cancel the contracts considering the legal action that would be taken by the companies and the potential destructive images to Indonesian investment environment such a move would create. In trying to solve the tensions, the Indonesian government attempted an alternative way through the renegotiation of contracts (ICIJ 2003).

The new contract, often called the Renegotiated Contract Agreement (RCA) was signed in 2001. In these contracts, the government set the target of reducing groundwater abstraction, increasing service coverage to 70 %, reducing unaccounted water to 35 %, and increasing volume sold to 342 million m3/ year in 2002 (Lanti 2006). Despite a hope that the new contracts would be fairer for both parties and thus could solve the problems in the previous contracts, there are some existing problems with the contract. The contracts are complex in aspects such as water charge and tariff mechanism (RCA 2001). They are also unclear about positions of actors which created overlapping roles among actors involved in Jakarta water management. These contracts are problematic in providing legal guidance as to how both the public and private interests will be achieved. Furthermore, important aspects, such as consumer's protection has been neglected in the contracts.

The contents were inadequate; for example, low penalties for the private sector's failure, unclear investment targets, and unclear dispute resolution processes. Furthermore, the final decisions about important aspects of the contracts such as the amount and priorities of investment are on the private companies hands; Consequently, the private companies, TPJ for example, has reduced the capital expenditure, has invested only half of the plan, and has drawn down half of the loan facilities set in 1998, which subsequently lead to the underachievement of the target. The rate of annual investment of TPJ (5.61 percent a year from 1998-2007) has been even lower than PAM Jaya investment (11.68 percent a year from 1988-1997) (Barlow 2008, from the Jakarta Post, February 2007).

Meanwhile, the established monitoring institution, the Jakarta Water Regulatory Body (JWRB), has limited power to be function effectively. JWRB plays important roles in water privatization: to bridge public authorities and private operators, to monitor the implementation of the agreement, and to mediate disputes between contracting parties (RCA 2001). However, this body was established in 2001, only after other actors had established their roles and positions in Jakarta's water management. Despite its important regulatory functions, the JWRB has not also been equipped with enough resources, has had limited authority and its role has been constrained by the contracts. In addition, it

could only provide suggestions and mediation but not make decisions and has no legal power to force the private sector to accept its recommendation. More importantly, the regulatory functions of JWRB are hindered by the contracts which set unclear mechanisms for regular independent audit and exclude the clause on the company's financial accountability; consequently, in implementing its function JWRB relied solely on the private company's reports. The private companies have not been also financially transparent, especially in relation to the costs which form the water charge, as this is justified as a part of business privacy (Personal Commmunication, JWRB 2007)..

Consequently the regulatory frameworks could not work effectively despite low performance of the private companies. The private companies have performed below the technical targets set in the contracts, such as continuing high water losses and there has been slow progress in water service expansion. The private companies have also failed in fulfilling service standards, such as the residents still need to boil water for drinking, low pressures, and continuing water disruption.

While the performance is low, the water tariff has increased significantly. The JWRB has been concerned about the continuing tariff increase which has not been accompanied by increasing performance of the private sectors. Thus, in 2006, for example, the JWRB recommended that the Governor should not increase the tariff for the reasons that the performance of private companies were low and the existing tariff has been already too high. However, the private companies have responded and delayed the investment plans for the reason that the tariff did not fulfill the operational needs of the companies (Personal Communication JWRB 2007).

Thus, JWRB stated that Jakarta water privatization has been actually not profitable and is not feasible to be continued except and unless the contracts are amended (JWRB Policy Paper 2007). The weaknesses of the contracts and uncooperative private companies contributed to the failure of privatization. Despite the failure, the option to stop the contract is too costly for the Jakarta government, because the government will need to pay high compensation to the private companies (JWRB Policy Paper 2007). This failure

of privatization has social, economic, and environmental consequences to the residents of Jakarta.

CONSEQUENCES OF WATER PRIVATISATION

The problems of privatization in Jakarta lead to three main consequences. Firstly, the residents who have access to piped water have been affected by privatisation through significant water tariff increases, which especially affect poor and lower middle class residents. Meanwhile, water services are poor; consequently, they need to source other alternatives for safer drinking water like buying bottled water, buying from UV water treatment kiosks, or having bore water in their backyard.

Secondly, privatisation constraints service provision for the poor because water service expansion is mainly based on profit considerations. Water provision for the poor is considered as socially feasible but not commercially profitable, which means that serving the poor will diminish private sector profit. Therefore, privatization contracts often exclude the private sector from this responsibility, or even though the contract includes this, the poor are still excluded for reasons such as legal issues of their settlement (Budds and McGranahan 2003). Consequently, a large part of their income is spent on water to pay expensive water from informal water vendors. This exclusion increases environmental risks (Pelling 2003) and health problems for the vulnerable residents.

Thirdly, environmental problems increase as the private sector focuses on economic management and profit while neglecting environment management. The ground water abstraction is continuing despite a decade of privatisation, because the rich and businesses are reluctant to pay high piped water tariff for unreliable supply, and they prefer cheaper alternative water source, namely ground water. The Policy Paper of the JWRB (2007) warns that the implication is massive: it will decrease revenue for the piped water operator, leading to services' deterioration, and further ground water abstraction. The vicious cycle of ground water abstraction continues, which at current levels has reached worrying levels; it has caused the city to sink five to seven feet lower in three

decades (Kompas, 6 September 2007) and this has lead to greater risks for flooding and saltwater intrusion (Kamil 2001).

These impacts can be seen as a result of elitist processes within water privatisation which involve political, business and administrative elites (Pelling 2003). Privatisation in Jakarta leads to the exclusion of the public from decision making and the lack of transparency. Firstly, the public involvement in water services is diminished (Haque 2001) which means that public is excluded from decision making processes. The process not only excluded the public and eliminated public criticism, but also benefited the companies and the actors within the state from under-the-table deals. In this regard, privatisation is incompatible with democratic principles (Swyngedouw 2005).

Decision making processes have also been removed from local political control to the executive boardrooms of global companies (Swyngedouw 2005). The actors that should be accountable to the public are removed from the national, local and municipal level to transnational level. This process is referred to as 'glocalisation' (Kaika 2003), which consequently creates difficulties in defining the responsibilities of these actors. Meanwhile, the government function is mainly as an actor to support privatisation and to encourage global business investment (Soderbaum and Taylor 2001). For example, the very important process of the TPJ's management changes from Thames Water to Acuatico, a new investor, in 2007 excluded the public. This was business to business decision, by multinational companies (Thames and Acuatico), in foreign country (Singapore), and based on the global business strategy of this company. Then, after the business to business process is over, decisions were left to the political elites and the new investor. These processes reflect that the powerful private sector has cooperated with, if not replaced, the powerful actors within the state. Meanwhile the voice and control of the public, which are the main elements of a democratic society, over the way local water should be managed have been diminished.

Secondly, private companies are difficult to monitor because the lack of business accountability to the public. The excessive power of the company to make strategic and

investment decisions cuts the traditional channel of democratic accountability. Water provision processes are depoliticized, and there is a lack of transparency in the way water is managed and a lack of public access to information (Haque 2001).

The performance of private companies could not be measured by the public. In Jakarta, the private sector's financial reports were inaccessible to the public (Personal Communication JWRB 2007). NGOs and the media have also limited access to information and limited capacity to monitor the government who was to act on behalf of the public rather than the private company. Equally, the residents have limited information regarding water services, and their right to information has been neglected.

MYTHS AND REALITIES OF WATER PRIVATISATION

Privatisation is justified on the basis that it will increase efficient management, inject new investment, bring the skills and experiences to enhance the efficiency, and create competition to benefit the consumers. However, privatization has often failed because of the flaw in theoretical foundation of privatization which intersects with domestic political economy environment and the weaknesses of regulatory mechanisms (Prasad 2006). The evidence of the contradictory assumptions about privatisation and the real practice in Jakarta are, as follows:

1. **Privatisation increases competition based on market mechanism**:

Privatisation does not necessarily increase competition because of limited numbers of water companies in the world which often cooperate with each other to maximize the profits; meanwhile the local private sector has limited capacity to be involved because of the large scale nature of water services provision (Prasad 2006). In Jakarta, no competition occurs between service providers; the residents living in the eastern part of Jakarta have no choice but to connect to TPJ (Thames subsidiary), similarly for the residents in the western part of Jakarta to connect to Palyja (Suez subsidiary). Secondly,

there was no competitive tendering to choose the best service providers. Thames Water and Suez were directly chosen by the Suharto's government without any tendering process.

Market mechanisms as a fundamental component of privatisation also are not operative in Jakarta water privatisation as the government provides profit guarantees to the private sector rather than leaving the process to the market. In addition, the private sector also uses similar sources of funding as the public sector: for example multilateral guarantee from the Multilateral International Guarantee Agency (MIGA) (Jensen 2005) and multilateral loans to finance its capital investment programs, as it has occurred in Latin American water privatization (Kirkpatrick and Parker 2005).

2. **Privatisation increases efficiency and reduces government subsidy burden**

A review of privatization found that private sector is not more efficient in delivering water services than the public sector (Prasad 2006). In Jakarta, the private companies are not more efficient than PAM Jaya and this inefficiency is borne by the consumers through tariff increases. More importantly, privatisation does not eliminate subsidy but only removes a subsidy to the poor, e.g. low tariff, to a subsidy for the private sector through the automatic tariff increase mechanism, the water charge system and the fixed profit guarantee. Furthermore, the government also provides indirect subsidies through its intervention in securing raw water supply and providing water for unprofitable areas while profitable areas are served by the private companies.

3. **Increasing tariff will lead to decreasing water consumptions**

It is assumed that demand of water will decrease as the tariff increases. This assumption has not been proven in reality because despite steep tariff increases, the average water consumption in Jakarta has increased significantly from 115 litres/consumer/day in 1998, to 127 l/c/d in 2005. In 2006, consumption slightly decreased to 118/l/c/d, but this is still higher than prior to privatisation (JWRB 2007). In addition, the residents, especially the

rich who have also access to ground water, use water for unnecessary purposes such as washing cars and watering gardens.

4. **Effective regulatory mechanism will protect the poor**

It is argued that the impacts of privatisation to disadvantaged groups can be eliminated with appropriate regulations and institutional arrangements (Kessides 2004). In fact, the regulations are ineffective to protect the poor because of the strong power of the private sector which attempts to maximise their profit. For example, in order to maximise profit, the piped water network will be prioritised to profitable areas rather than marginal areas. Furthermore, in order to increase profit, the cross-subsidy mechanism is ignored or modified through differences in tariff increases between consumers in the category poor and rich; the poor and lower middle class residents have experience the highest tariff increase, even higher than the rich, so that they need to pay almost the same tariff as the rich residents.

5. **Privatisation reduces bureaucratic red-tape**

It is assumed that the private sector will manage water more effectively because privatisation will reduce the role of governments and replace them with free-market mechanisms. In reality, privatization always leads to the establishment of new agencies, within and outside the state, in order to support the process. This process is referred to as ‘regulating dispossession’ (Swyngedouw 2005). The state also remains the central actor in facilitating privatization through establishing regulatory procedures and providing guarantees for private sector investment from political and economic risks (Swyngedouw 2005).

In Jakarta, new regulations and institutions such as the Jakarta Water Regulatory Body, were established, however, it added a complexity into existing institutional arrangements. For example, the JWRB was established for monitoring, but PAM Jaya at the same time is also responsible for this task. This complexity has disconnected the public from taking

part in the decision making process. Furthermore, the private sector is also not accountable to the public; public information is treated according to the business confidential principles, and 'business red-tapes' are established replacing bureaucratic red-tapes.

The regulatory and governance problems within Jakarta's water privatisation reflect the flawed logic underpinning water privatisation. This also reflects the continuing struggle for power among actors involved in a Third World's environmental issue which is characterised by the cooperation between powerful actors (the state and business) in maximising their interests (Bryant and Bailey 1997). The state's role is mainly to support the operation of the global economic system rather than the interests of the public.

CONCLUSION

In this paper, I have discussed two important aspects which are at the centre of my arguments: the regulatory frameworks underpinning water privatisation processes are ineffective so that privatisation has brought massive economic, health, and environmental consequences. The private sector's failure to provide better water services reflects both the flawed principles of water privatisation and the state's failure to protect public interests through effective regulations.

In Jakarta, water privatization has failed to meet its assumptions: it has not increased competition among providers which will lead to better services; the private sector has also been equally inefficient as the public sector in managing water services. The re-regulation process embedded in privatization has not eliminated bureaucratic red-tape but rather replaced it with 'business red-tape'. In addition, the tariff increases mechanism may remove government subsidy to the residents who previously enjoyed lower tariffs, but at the same time the private sector is 'subsidized' through profit guarantee mechanisms. The tariff increases do not necessarily lead to decreasing demands as it was assumed. Meanwhile, regulations to protect the most vulnerable actors, the residents, are less effective.

These failures of privatization can be linked to the local and global political economic environment that influences the privatization process. Jakarta water privatization occurred within a country which since 1970s has been closely attached to the global capitalism system, characterized by the promotion of water infrastructure development rather than the development of the capacity of water institutions and society. Under the public sector; Jakarta's water management which was focused on large investments to develop water facilities has failed to achieve the target of better provision of water, a failure that has been repeated by the private sector. International institutions such as the World Bank have also continuously encouraged 'water reform', which include privatization of water services despite the recognition of its limitations and even larger evidence of failures.

Using the political ecology approach to analyse water privatisation in Jakarta, there are two important aspects that have been discussed in this paper. Firstly, the consequences of water privatisation are related to the way decisions over water have been made (political aspects). An important part of the political ecological analysis of urban water privatisation is a power struggle among actors to control the mechanisms of resource distribution and to determine the policy priorities on water. Privatisation has become the priority of Indonesian government elites as it supports their interests and is consistent with the strategy adopted by the state to integrate the Indonesian economy into the global economic system.

Secondly, water privatisation impacts are related to the relative vulnerability of the residents to environmental problems. Environmental considerations have been generally neglected in the bottom lists of targets to be achieved in privatising water supply. As water is transformed into a commodity, water is considered merely as a product to fulfil the need of human beings while separating the interconnection between human beings and water itself. In this regard, the residents have been disadvantaged by the processes of transforming nature into a commodity for sale in the global market as water has become too expensive and inaccessible, especially for the poor residents. These processes have

strengthened the existing circuits of water provision in which formal piped water system is for the rich, while the poor are served by informal system.

Since 2004, water privatisation has been expanded to many other cities in Indonesia. Therefore, it is important to establish new schemes for water management, instead of merely replacing public sector with private service providers. In this regard, there is a need for a strong regulatory framework by the state accompanied by the provision of substantial private company shares to the poor. Further research is required in this area.

Furthermore, the investigation of alternatives for water privatization is important to find solutions for water crisis faced by many countries in the world. Community-based water management which has strong roots in traditional water management in Indonesia may be able to lead to better water provision for citizens because it has strong roots among grassroots actors, and it recognises the importance of citizen involvement and everyone's right to water. Further research in this area will be useful to identify the challenges in implementing community based water management and subsequently will contribute to find solutions for urban water problems.

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