



‘3Ts’

Tariffs, taxes and transfers in the European water sector

Short guide



DANVA
Dansk Vand- og
Spildevandsforening





FOREWORD

Drinking water and waste water service providers in Europe have a common goal: to provide safe, reliable and sustainable water supplies and waste water services. Delivering this vision in the future will require operators to meet new challenges, including scarcity, affordability and environmental challenges such as climate change. These factors, among others, will require water professionals to make ever better use of limited financial resources in order to ensure that the necessary funding and investment is secured for a sustainable water supply for present and future generations.

The 3Ts framework developed by the OECD represents a powerful tool in unlocking our understanding of the sources of the funds which underpin this sustainable future. The 3Ts acknowledges that Tariff, Taxes and Transfers (e.g. users, taxpayers, foreign aid...) are the ultimate sources of funding for water services. The current mix between those terms, and its future evolution, should result from an explicit choice at local level from the responsible authorities depending on the socio-economic and historical conditions. This guide seeks to explain how the 3Ts analysis can be applied in a variety of national and institutional contexts.

We hope that this demonstration will act as a significant spur to a broader understanding and adoption of the 3Ts approach to provide a useful tool for stakeholder consultations and strategic financial planning in this most vital infrastructure sector. We encourage all stakeholders to contribute to the application of this toolkit, and look forward to the publication of further case studies on the 3Ts framework beyond the 6th World Water Forum.

Carl-Emil Larsen - President of EUREAU

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Acknowledgements

Agbar, Águas de Portugal, Arno River Basin Authority, Aquawal, Brest Métropole Océane, BWB, Cetaqua, DANVA, EIB, FP2E, OECD, Publiacqua, SPGE, SUEZ ENVIRONNEMENT, VCS, Veolia Eau, Vitens, VEWIN, Water UK. [See p. 9]

This guide* is based on the report titled Methodological guide on Tariffs, Taxes and Transfers in the European Water Sector, prepared by ECOLOGIC Institute further to a study ordered by DANVA in 2011.

This guide represents a contribution to European Regional Process towards the 6th World Water Forum.

**In some cases, data has been simplified to aid presentation.*

THE 3Ts FRAMEWORK

The 3Ts are a concept initiated by the OECD to describe and categorise the three ultimate sources of financial investment for the water and sanitation sector: Tariffs, Taxes and Transfers.

What is it about?

In the coming years, countries at all stages of development will need to raise significant amounts of finance to develop, modernize, maintain, and operate their water supply and sanitation systems to comply with new legislation.

The 3Ts framework addresses only one facet of the economic equilibrium of water services; it deals with funding and not with costs. This does not mean cost optimisation is unimportant. But establishing a way of understanding the appropriate balance and relationship between the 3Ts for funding purposes is a significant step towards developing a financially sustainable basis for the future of the water and sanitation sector.

It is important to note that use of the 3Ts approach does not infer that the sustainable method of establishing full cost recovery should be based on tariffs alone. Such an approach might, for example, place unreasonable burdens on the poorest consumers and who might need to receive a subsidy in order for their supply to be sustainable.

Why apply the 3Ts?

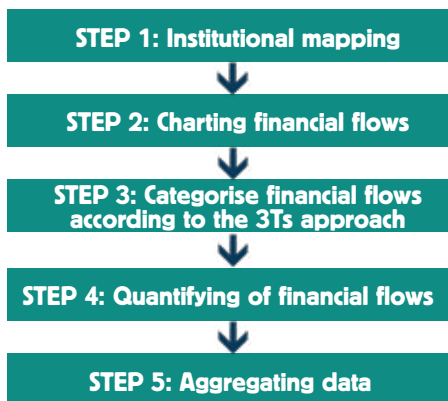
The 3Ts represents one tool to analyse financial flows. It contributes to a policy dialogue to reconcile the water and sanitation sector's financial needs with its available revenue, costs reduction, and opportunities for tapping into commercial sources of funding. Good governance and management of the water and sanitation sector must accompany strategic financial planning. This guide represents an initial step

to apply the 3Ts concept into practice in order to promote:

- A source contribution increasing transparency of the financing of water services and to facilitate the reporting obligations on the costs recovery of water services [article 9 of European Water Framework Directive]
- A useful diagnosis and decision-making tool.
- A means of informing on water and sanitation related investment targets.
- A tool to raise general awareness of sectoral financing issues.

How to apply the 3Ts?

This practical manual recommends ways to aggregate the information to develop the 3Ts from the utility level to the municipal, regional, or national level. It is intended to be a policy tool, to be applied for water utilities as a whole [operators and entities who own the assets]. Case studies have been undertaken to better understand the different sources of financing for the water sector across Europe. The following sequential steps are recommended, representing a tiered approach to harmonise the method used for comparisons of the 3Ts at different levels within a country as well as between different countries.



STEP

1

INSTITUTIONAL MAPPING

What?

Gaining a complete picture of the water and waste water sector and identifying all relevant players.

How?

Establishing who the players are and how they are involved in **investments and operations**.

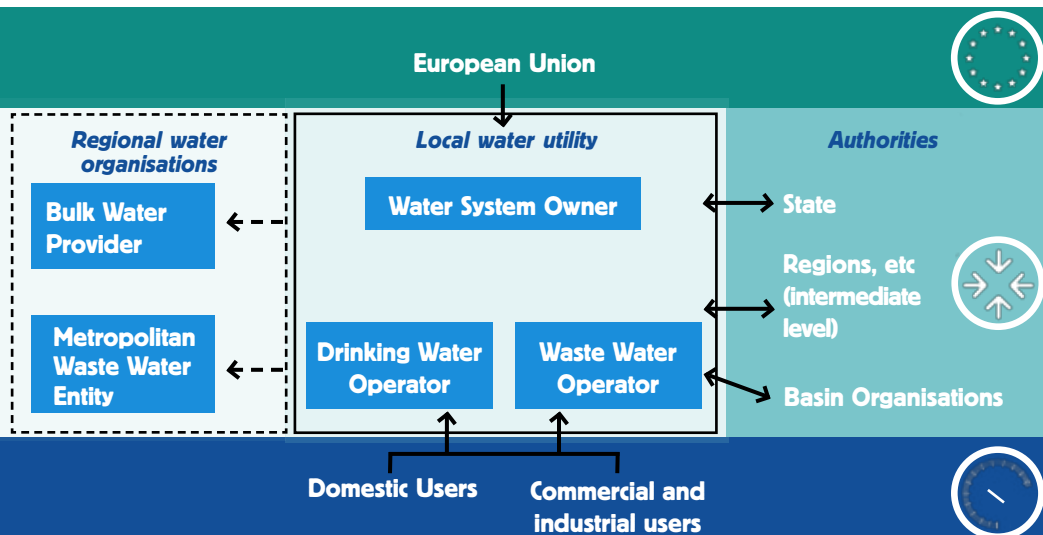


Figure 1 : Institutional mapping

—————→ **Indicates a financial flow**

To map drinking and waste water services, answer the following questions:

1. Who operates the water services? Who

operates the waste water services?

2. Who is collecting the bill from water users?

3. Who is the owner of the water infrastructure? Who is the owner of the waste water infrastructure?

STEP

2

CHARTING FINANCIAL FLOWS

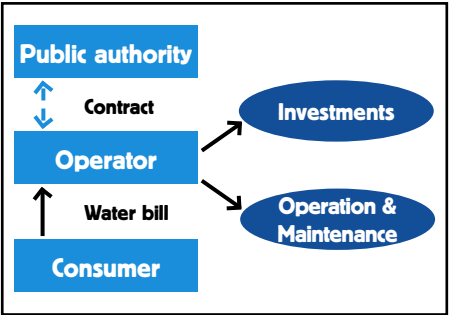
What?

Illustrating the interactions and cash flows between the organisations responsible for the provision and administration of drinking and waste water services.

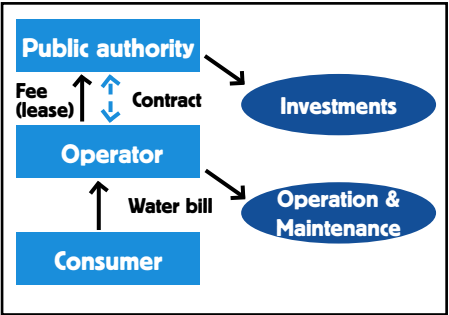
How?

Assessing who collects revenues and how revenues are shared and allocated among

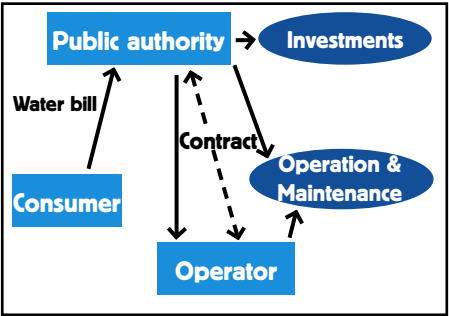
the different organisations managing the drinking and waste water services. Specifying the contractual arrangements that may exist between the public authorities responsible for the service and operators. [Examples are shown on figure 2.]



Type A: Concession contract



Type B: Lease contract

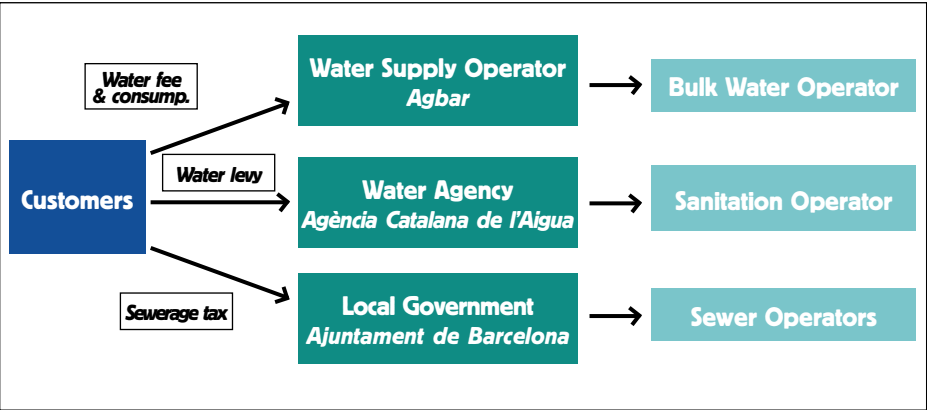


Type C: Service / management contract

Figure 2:

Illustration of contractual framework

This chart helps to understand the differences related to the type of contractual arrangement between the public authorities and the operators.



Example 1: Financial flows chart in Barcelona

At the local level of the Metropolitan Area of Barcelona, the financial flows are portrayed as originating from consumption fees as well as taxes and levies and continuing through the network of entities that

are involved at the different stages of the water cycle. The proper understanding of the ownership of the asset and the contractual relationships between the different actors are crucial to ensuring the correct application of the 3Ts framework.

STEP 3 CATEGORISE FINANCIAL FLOWS

What?

Categorise financial flows according to the 3Ts framework.

How?

- Defining Tariffs, Taxes and Transfers.
- Identifying relevant revenues entries.



TARIFFS

Tariffs are defined as user fees or contributions. They are revenues of the water utilities being paid by the **water users**.

Service providers can levy such fees for providing access to a service (connection charges) and for delivering the service (either a flat charge, a volumetric one, or a combination of both). Additional fees can be derived from meter rentals, penalties, fees from real estate developers, etc.

'Tariffs' include:

- a) Revenues of operators from service provision.*
- b) Revenues of infrastructure owners (relevant only if reinvested in the water and sanitation sector).*



TAXES

Taxes are subsidies to the water utilities from the local or national **tax payers** which are subsequently applied to the water and sanitation supply sector.*

While subsidies or grants are the most visible form of tax funds directed to the water and sanitation supply sector, "hidden" forms of subsidies may include tax rebates, soft loans, transfers from local government housing taxes, donations, subsidised inputs (e.g., electricity services), or "dormant" equity investments.

Subsidies from the national tax base include:

- a) Subsidies to local or national water operators.*
- b) Subsidies to infrastructure owners.*

*The qualification of "tax" for a given financial resource in the report or synthesis does not presume the actual legal status of this resource in an EU Member State.



TRANSFERS

Transfers include any contributions from **foreign donors**.

Transfers include:

- a) EU subsidies.*
- b) Official development assistance (ODA).*
- c) Philanthropic donations.*

COMPONENT OF THE 3TS



TARIFFS

Source: Financial statements of water companies or public budget reports.

Include

For drinking and waste water service providers:

- Water charges
- Meter charges
- Connection charges

For asset owners and managers:

- Infrastructure charges
- Fees from real estate developers

Exclude

- Revenues from other activities
- VAT payments
- Any other tax collected through the water bill and going to the general budget



TAXES

Source: Financial statements of water companies or public budget reports.

Include

- National / Municipal subsidies
- Hidden subsidies [e.g. tax deductions]

Exclude

- Loans
- Funds originating from outside the country



TRANSFERS

Source: Financial statements of water companies, public budget reports, EU funding reports.

Include

- European funds
 - ERDF
 - Cohesion Funds
- Private donations

Exclude

- Loans
- Funds originating from inside the country

STEP

4

QUANTIFY FINANCIAL FLOWS

What?

Collection of financial information at the utility level.

How?

- Analysis of financial reports.

- Identifying the 3Ts for the past 5 years.
- Focusing on the main financial resources (e.g. those which account for >1% of total revenue.)



- If possible, revenues shall be split into revenues from the drinking and waste water services. The items listed in this category shall be noted separately as sub-categories of tariffs in the 3Ts table.
- Charges which are collected by the operator, but go to the general budget of a local or national government like VAT are not to be included in the Tariff category.
- Revenues derived from miscellaneous activities (additional to the water services) shall not be included in the tariff.



- This information may be stated in the profit and loss accounts. However, if the subsidies are less apparent, such as tax rebates, they may not be listed explicitly, requiring further investigation and estimation.
- The taxes category should be subdivided into different levels of subsidies according to possible sources of financing: subsidies often come from different governing bodies in the country (national, regional and local authorities) and water agencies or river basin authorities with a role in the management of charging mechanisms and financing instruments for the water sector.



- Information may be stated in the profit and loss accounts of the water utility. A cross checking may be necessary with the financial programme set up by the national government for the water sector.

STEP

5

AGGREGATION OF DATA

What?

Aggregating data at relevant level.

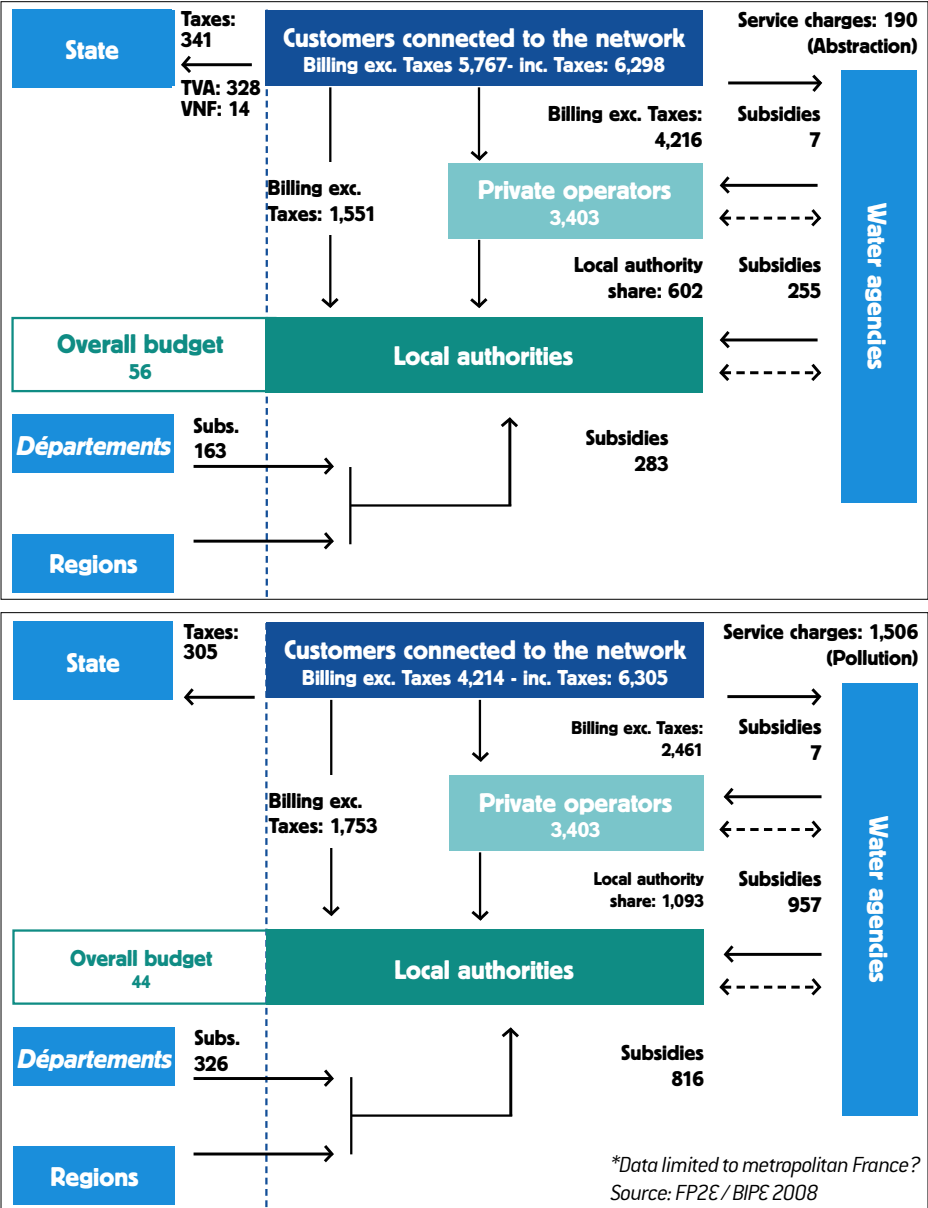
How?

- Identifying all relevant parties.
- Aggregating revenues for each entity.
- Revenues collected from customers are distributed mostly between the local authorities, the private operators, the

State and the water agencies. Some public subsidies are made available from the department. When the territory includes a very large number of entities, it may not be necessary to document each individual one and an extrapolation or approximation may be more appropriate.

Charts on financial flow drinking water (top) and waste water (bottom) in France
(in millions of Euros, 2008)*

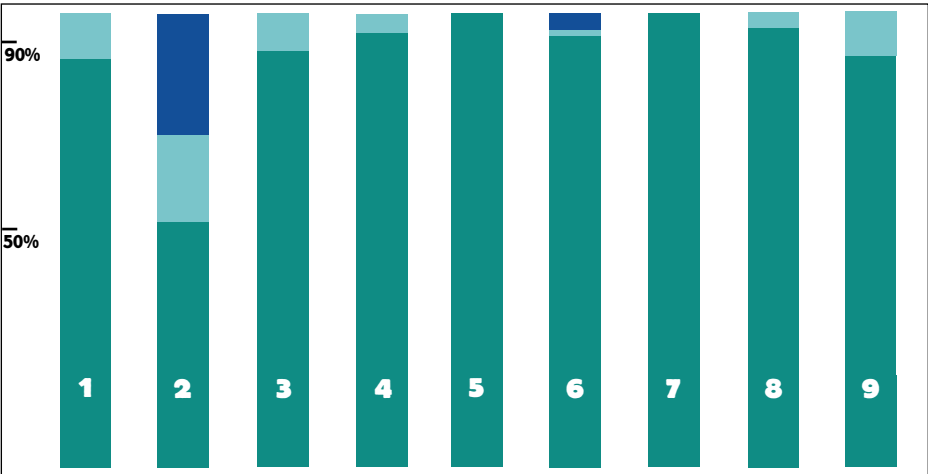
In France, the provision of drinking water and waste water services falls under the competence of the municipalities. They can manage services directly, set up public companies, or contract out the services to private companies.



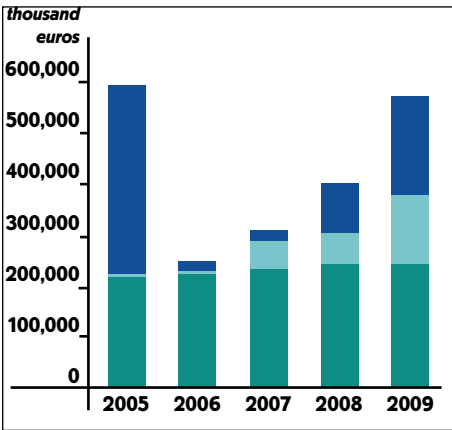
9 CASE STUDIES

This table shows the part of the Tariffs, Taxes and Transfers in the overall budget in 9 different cases at different levels in 8 countries.

The data aggregated are in %.



- (1) Berliner Wasserbetriebe (BWB, DE): 3,4 M inhab. (2010). Taxes are not to be exhaustive.
- (2) Metropolitan area of Barcelona. (ES, 2009)
- (3) Brest Métropole Océane (FR): 210,000 inhab. (2010)
- (4) Vitens (NL): Provinces of Friesland, Overijssel, Flevoland, Gelderland and Utrecht; a number of municipalities of Noord-Holland and Drenthe. (2010)
- (5) Bristol Water (UK): 1 million customers. (2010)
- (6) Wodociagi Warszawskie (PL), City of Warsaw. (2009)
- (7) Vand Center Syd, City of Odense (DK): 155,000 customers. (2010)
- (8) Publiacqua, Tuscan region (IT): 1,277,000 inhab. (2010)
- (9) Public water and waste water services (FR), FP2E. (2008)



Evolution of the 3Ts for the metropolitan area of Barcelona (2005-2009 - Source: Cetaqua).

This graph shows the variability of the taxes and transfers components caused by substantial investments during the period which had been funded by grants from different sources.



Glossary

Relevant authority

A public body entitled to set general policies, plans, or requirements or to check compliance with these rules, concerning all the water utilities included in within its jurisdiction.

EXAMPLES: National, regional, or local governments, public agencies, and regulators.

Responsible body

A body that has the overall legal responsibility for providing drinking water or wastewater services for a given geographic area.

EXAMPLE: A local or municipal government (i.e., for a village, town, or city), a regional government, a national or federal government through a specified agency, or a private company.

Water utility

The whole set of processes, activities, means, and resources organised for abstracting, treating, distributing, or supplying drinking water, for collecting, treating, and disposing of waste water, and for providing associated services.

Source: ISO 24510

References

EU

The main relevant EU legislations for the water services sector in Europe includes the EU Water Framework Directive (WFD) (2000/60/EC) and related laws, the Urban Wastewater Treatment Directive (91/271/EEC) and the Drinking Water Directive (98/83/EC).

http://ec.europa.eu/environment/water/index_en.htm

EU sources of funding

- The European Regional Development Fund (ERDF)
- The Cohesion Fund (CF)
- Instrument for pre-accession assistance (IPA)
- The European Investment Bank (EIB)

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A short guide

Drinking and waste water service providers in Europe have a common goal: **to provide safe, reliable and sustainable drinking water supplies and waste water services.**

The 3Ts framework developed by the OECD represents a powerful tool in unlocking our understanding of the sources of the funds which underpin this sustainable future.

What is the 3Ts framework? How can it be implemented? What can it bring in terms of planning finances and investments for the water supply and sanitation sector?

This guide seeks to explain how the 3Ts analysis can be applied in a variety of national and institutional contexts.

This guide represents a contribution to European Regional Regional Process towards the 6th World Water Forum.



EUREAU is the European Federation of National Associations of Water and Wastewater Services. Through these associations, EUREAU gathers 70.000 water & waste water utilities & operators across Europe that provide sustainable water services to around 405 million European citizens.

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