

Launch of the OECD report « Water charges in Brazil: The ways forward»

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Vicente Andreu, President of the National Water Agency, Ms Adriana Lustosa (Ministry of Environment), Ladies and Gentlemen,

It is my pleasure to be with you today to launch the OECD report *Water charges in Brazil: The ways forward*. This concludes a two-year multi-stakeholder consultation process and policy dialogue that involved over 150 organisations in Brazil. I have to say that ANA has been visionary in requesting this exercise way before the formal request of Brazil to engage in the accession process to the OECD. Through this dialogue, you have shown not only your courage and determination to “open the books” and learn from international best practice, but also your readiness to get closer to OECD standards. By working with you, we have learned that this diverse and continental country faces common challenges to many of our member countries on the sensitive topic of “charging for water”, but that it also has some practices and success stories from which our members can learn.

As many of you know, this report is a direct follow-up to a first policy dialogue we completed in 2015 on the topic of Water Resources Governance in Brazil. The first OECD report highlighted the decentralised, participatory and integrated characteristics of Brazil’s national water resources system, and emphasised, amongst others, the potential of water abstraction and pollution charges to foster water security now and in the future.

As a longstanding advocate of the Polluter-Pays and User-Pays principles, the OECD argues that economic instruments can play an important role for effective and efficient water resources management when designed and governed adequately, and when combined with other policy instruments. In particular, setting and governing abstraction and pollution charges that can deliver expected policy objectives is not an easy task and remains a necessity in several countries. A number of governments around the globe have been experiencing severe reform challenges as well as fierce resistance from users when putting in place water charges for the first time and/or raising their levels.

In the case of Brazil, the economic crisis and its social and competitiveness consequences have hampered the readiness to charge and the willingness to pay in a country that holds 12% of the world’s freshwater

resources and has long been perceived as “water-rich”. Another reason for resistance is that many water users do not see the direct benefit from water charges and consider them an additional “tax” rather than a collective effort to improve the conditions of the river basins. The 2014 water scarcity crisis in Brazil provided a unique momentum for change. Fierce competition across users opened up a window of opportunity to consider the use of water charges as a resource management tool to transition from water crisis management to water risk management.

Currently, in Brazil, water charges are established at levels that are too low to drive behavioural change of most users (hydropower generators, industries, farmers, and utilities) and to finance water resources management functions. Revenue that is generated is not perceived to directly benefit users or to finance expenditure programmes in the basins where charges are levied. Moreover, as the structure and level of charges are similar across the country, they do not reflect local circumstances or changes in water availability over time. The charges also do not reflect the opportunity costs of using water in specific basins, the risk and consequences of pollution, or the dilution capacity of rivers and water bodies. Finally, objections to water charges mostly build on arguments of affordability and competitiveness. However, these arguments need to be properly assessed and documented.

This new OECD report delivers important messages:

1. **Water charges are a means to an end:** by promoting more efficient water use and prevent and control pollution, they can help prevent water risks from becoming barriers to Brazil’s sustainable growth now and in the future. Effective planning and expenditure management are key to ensure that revenues from water charges can contribute to improve water management in the basin in a tangible way for users.
2. **Water charges** cannot solve the magnitude of the challenge on their own, and **should be combined with regulatory, monitoring and enforcement instruments and with other sectorial policies**. This means, for instance, to avoid conflicts with agricultural, industry and energy policies and rather provide incentives for users to control water availability, quality and demand.
3. **A pragmatic approach should be used when setting and governing water charges: water charges do not need to be universal to be fair and equitable.** In practice, a very large proportion of water is used by a small group of water users. Similarly, a few water users generate a large share of polluted effluents. Transaction costs to cover smaller users or polluters can be high compared to the benefits in

terms of water resources management and revenues raised. Hence, to minimise transaction costs, water charges should be targeted to large users and heavy polluters, at least at an early stage.

Economic instruments: an OECD perspective

The **OECD Council Recommendation on Water**, negotiated by all our member states, provides clear guidance for an efficient and effective implementation of economic instruments as a vehicle for improving water quality and managing water quantity:

- Where appropriate and applicable, **economic instruments should be established in combination with other instruments** (e.g. regulatory, voluntary or other economic instruments), to manage water resources (in particular water conservation), **phase out negative externalities** (e.g. overuse, pollution) and **improve the financial sustainability** of water infrastructures and water services.
- **Economic instruments should reflect each country's social and economic conditions, as well as water risks.** In particular: abstraction charges for surface and ground water should reflect water scarcity (i.e. environmental and resource cost) and cover administrative costs of managing the system, while water pollution charges should represent an incentive effect to prevent and control pollution.
- **Affordability studies and assessment of competitiveness should be carried out** to account for redistributive consequences and priority water uses.
- When designing pricing instruments and revenue management schemes, **transaction costs**, including administrative costs, **should be considered**.

But for water charges to deliver, beyond the consideration of their *level* and *structure*, it is crucial to take into account the overall governance system in which they are set and implemented. The **OECD Principles on Water Governance**, which were welcomed by ANA, provide a reading template to ensure framework conditions are in place for water charges to deliver. This requires, amongst others, clarity and co-ordination on *who does what* in setting, implementing and regulating water charges; appropriate *scale, policy coherence*, adequate technical, human and financial *capacity* to collect and disburse revenues from charges; consistent *data and information* to guide, assess and improve water charges; *transparent practices* for budgeting and accounting; robust *regulatory frameworks* to ensure enforcement and compliance with water charges; *stakeholder engagement* to raise awareness on risks and secure the buy-in for charges; as well as regular monitoring and evaluation to assess if charges fulfil the intended outcomes.

Water charges are a means to an end

Water abstraction and pollution charges operate as economic and financial instruments. They can drive behavioural changes to improve water-use efficiency and reducing pollution: when they reflect the scarcity of water or the cost for the community of one user abstracting water from a river body, they can discourage wastage and allocate water where it creates most value for the community. Similarly, when pollution charges reflect the cost of pollution, they can incentivise investment in cleaner practices and technologies. They can also generate revenues which can be used to cover some of the costs associated with managing water.

To this purpose, it is important to know what you want to achieve with water charges. This is the role of **river basin plans**. They should drive decisions on the level of abstraction and pollution charges, who should pay, and how the revenues generated by charges should be spent, when they are earmarked for water expenditures in the basin. Water charges should reflect local circumstances or changes in water availability over time, the risk and consequences of pollution, or the dilution capacity of rivers and water bodies.

In Brazil, where charges are implemented, they are not able to finance actions foreseen in river basin plans, nor to change the behaviour of water users towards greater water efficiency and less pollution. At federal level, revenues from water charges are able to cover about 10-15% of the financing need to implement water resources plans. Where charges are implemented, the ratio of the financial needs for the water plans over revenues collected is often about ten to one or more: revenues – in the orders of tens of thousands reals – are blended with other sources of funding and spent on the construction of sanitation infrastructure – in the order of hundreds of million reals. The State of Ceará, a pioneer in implementing water charges in 1996, adopted a different approach, consisting in formulating water charges as “tariffs” paid to the public company for Water Resources Management (COGERH) and used to cover administrative expenses, as well as operation and maintenance of water infrastructures. This approach can inspire other solutions nationwide, without requiring legal reforms.

At least for a transition period, revenues of water charges can be earmarked to cover water-related expenditures in the basin. These expenditures should reflect the priorities set out in the river basin plan and the initial objectives set for charging. They ought to make a difference, so that those who pay see the benefit for themselves and the wider community. For instance, it is counterproductive to allocate revenues from water charges to large infrastructure projects to which their contribution is minimal: users will infer that charges are ineffective.

In England and Wales, abstraction charges are used to recover costs related to administration of abstraction licences, but also all the hydrometric monitoring, assessment, and water resource management activities (including the operation of multi-use reservoirs) as set out in detail in law. In France, 90% of revenues collected by the Water agencies are redistributed to water users of the river basin; the remaining 10% is used to fund the river agencies.

Water charges should be combined with other instruments and policies

Water charges should be considered in combination with other policy instruments such as **water allocation regimes** or **water quality standards**. Water charges deliver best when water use (abstraction and pollution) is monitored and regulations are enforced. In England and Wales inspections are carried out on a risk basis: non payers are pursued and licences can be revoked in case of refusal to pay. In Brazil, there is room for improvement: sound inspection and control mechanisms, as well as sanctions and penalties in case of non-compliance, should be strengthened to make the entire system more robust and credible.

Also water charges should be combined with energy, agricultural and industrial policies to avoid negative impacts on water management. Industrial policy, for example, on the one hand, industrial policy can support compliance with water regulation, such as subsidies to green technologies, which can reduce the cost of meeting water quality standards. On the other hand, can increase water use and, therefore, intensify water conflicts. Two case studies analysed in the report, the Paraiba do Sul river Basin and the State of Rio de Janeiro, are industrialised areas in which parts of the revenues from abstraction or pollution charges paid by industries could be used to support the adoption of water-efficient or clean technologies. Moreover, giving access to funds to the industry would be an incentive for the sector to accept water charges and their increase.

Water charges do not need to be universal to be fair and equitable

To maximise benefits for water management and revenue raising, and to minimise the transaction costs of setting and managing charges, water charges should target users who abstract or pollute most (although in the longer term, a fair and inclusive approach is required). This scenario is similar to other countries (e.g. France), where focusing on big users allows to reduce transaction costs for collection, monitoring and enforcement of small users activities

I am well aware that a number of water users object that water charges are unbearable or affect their competitiveness, within the country or in global markets. These objections can be overstated. The real impact of abstraction and pollution charges on the competitiveness of firms or large farms need to be assessed thoroughly. Moreover, the impact on the Brazilian economy and society of mismanagement of

water - which derives from inexistent or poorly designed abstraction and pollution charges - should be assessed as well.

For example, the irrigation sector abstracts more than 50% of water, but is almost exempt from paying water charges: in the Paraíba do Sul River Basin and the Piracicaba, Capivari and Jundiaí (PCJ) river basins, the agricultural sector pays from 2 to 20 times less than other water users. Currently, in the São Francisco and the Doce River Basin, the volumetric charge for agricultural users is 40 times lower than for other sectors. Approximatively, farmers pay only 2-5% of what other users pay on a volumetric basis, the affordability issue stemming from paying the full water charge is not self-evident.

In a continental country like Brazil, the hydrological complexity and institutional framework of river basins and states vary enormously and so the capacities and the conditions to set and implement water charges. The current implementation of water charges in six interstate river basins and six states allowed us to draw two considerations that deserve attention:

- **The strategy which consists in setting charges at a low level, hoping that users will get familiar with them and rates can be increase at a later stage, fails.** It has proven just as difficult to adjust and increase rates as to set up charges from the outset. International experience shows that a successful strategy consists in setting charges that deliver positive outcomes in the basin: they should be set at a level that allows to finance expenditure programmes that benefit water users in the basin.
- **Water charges certainly require a place-based approach.** They may not be needed everywhere in Brazil. Setting water charges depends on states and basins' exposure to water-related risks, but their function as a source of revenue to cover costs of management for water resources should not be overlooked.

Next steps

The report concludes with an **Action Plan** to set out concrete actions and suggest champions or institutions that can lead implementation over the short, medium and long run. The ultimate goal is to create the conditions for the effective design and efficient implementation of water charges in a **shared responsibility** across levels of government as well as the public, private and non-profit sectors.

The study grouped the existing experiences of water charges implementation in interstate and state river basins in 5 clusters, from the “**pioneers**” (the Pariba do Sul River Basin, the state of Rio de Janeiro, the

Piracicaba, Capivari and Jundiaí River Basin), to “**followers**”, “**inspirational**”, “**newcomers**” and “**aspirants**” (the Piancó-Piranhas-Açu River Basin). This clustering could be used to test the proposed actions in the most institutionally advanced basins/states with high capacities to prepare and implement plans, and then illustrate the benefits of the water charges systems to other basins/ states engaged in or thinking about implementing similar practices. We believe that exchanging experiences and sharing information is a good vehicle for increasing awareness on water management and overcoming implementation issues for water charges.

Allow me to warmly thank Mr Vincente and Mr Lotufo for their relentless dedication and commitment throughout the dialogue, Ms Gisela, Mr Ney and Mr Ricardo, as well as their highly professional team (Aline, Carlos, Cristiano, Elisa, Giordano, Humberto, José Luiz, Mariana Marco Antonio e Sérgio).

The OECD remains committed to shoulder with Brazilian authorities and facilitate such an ambitious agenda.