

Water & Wastewater

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A. Public Works Financing Issues 12th Annual Water Privatization Report

Privatization of water and wastewater services continue to face some resistance based on the perception that private profits can be put to better use by public utility managers. Despite this perception, figures from the 12th annual water report from *Public Works Financing* suggest that the drivers of future growth of water and wastewater services provision are likely to be private players.

The large companies included in this survey represent approximately 85% of the total U.S. market for outsourcing water services, which is approximately 5% of the 54,000 publicly owned water and wastewater systems in America. Most of these water outsourcing contracts are held by domestic private firms to provide system operations and maintenance services. The move towards privatization is prompted by a change in the operating procedures of public water utilities from an emphasis on technical know-how to management methods and service delivery.

Contract renewal rates for existing contracts have remained high with a 6% jump from 2006, despite a fall in revenues by 4% to \$1.5 billion among the six major players. The total number of wastewater facilities has gone up marginally by 1.3% from 2006. However, industrial outsourcing revenues and facilities have seen substantial

increases, including a 7% increase in total revenue from 2006. Communities adopting long-term water contracts have on average enjoyed a \$30 million in cost savings for primarily wastewater management. Several new contracts have sprung-up on the West coast and Southeast which could remedy the slow gains.

B. Stockton Calls Off Water Privatization Contract

The city council of Stockton decided to let go of its \$600 million water privatization deal in July 2007 as the result of a compromise with three principal citizens groups last July. Stockton's legal battles began when the Concerned Citizens Coalition of Stockton, along with the Sierra Club and the League of Women Voters of San Joaquin County, represented by the law firm Shute, Mihaly & Weinberger appealed to the courts, on the grounds that the city did not abide by environmental requirements before signing the contract.

The city council responded to this appeal with a counter-appeal to the court's ruling that the deal was illegal. This July, the city council dismissed its appeal and formally agreed to pay close to \$2 million as settlement fees along with promising to run the city's water and sewerage facilities as well. Concerned Citizens Coalition of Stockton activist

Dale Stocking said, “This is another nail in the concept that the private industry model is better than the public model in delivering essential services.”

Private contractor OMI/Thames still holds the responsibility to finish upgrading the city’s wastewater treatment plants before it hands over ownership and operation to the city council. The transition plan includes an expansion of staff at an annual cost of about \$1.9 million and \$665,000 for new equipment making costs \$57.8 million annually. This is a \$757,045 increase from what the people of Stockton paid OMI/Thames. The Stockton city council’s unanimous decision to end the contract with OMI/Thames was also supported by Gary Podesto, Stockton’s erstwhile mayor who is popularly thought to be the mind behind the contract; he said “If I were there, I would do the same thing.”

OMI/Thames maintains that its intervention in Stockton saved the city millions of dollars in addition to helping it meet environmental quality standards, while the Sierra Club and League of Women Voters of San Joaquin County called the end of the contract a “victory for democracy” indicative of the acrimony that the contract caused when it was signed 13 days before voters (by a margin of 60%) in the city decided that a public vote would be required in advance of any water privatization. The public vote decision was however overruled by the city council and fuelled the citizen-led litigation to return water to municipal ownership. Stockton Mayor, Edward Chavez, drew political lessons from the Stockton fallout when he said, “The real lesson is: If you really want to make people angry, shut them out.”

C. Eminent Domain Threatens Private Water Company Assets

In several communities nationwide, the threatened use of eminent domain to expropriate the assets of private water companies—the equivalent of involuntary, forced de-privatization—is beginning to raise concerns in the water industry and presents an increasing threat to private property rights. Several incidents involving the use or the proposed use of emi-

nent domain now dot the water utilities landscape.

These attempts at involuntary de-privatization include the proposed takeover of the Arizona American Water utility by the city council of Scottsdale and the battle for municipal control over water by the residents of Felton, California. These are not however isolated attempts; Tiffin, Ohio and Homer Glen, Illinois also appear to be pursuing a similar path. More recently and the residents of the Rosario, Vusario and the Orcas Highlands on Orcas Island in Washington State are threatening to reverse the substantial benefits that emerge from a long-established private provision of municipal water services through the threat of condemnation.

In Scottsdale, the city council voted in July 2008 to undertake a study on the potential condemnation of the Miller Road Treatment Facility—currently owned by Arizona American Water—after two recent contamination incidents. In January 2008, consumers were instructed to switch to bottled water for three days after Arizona American discovered that the levels of the suspected carcinogen trichloroethylene (TCE) briefly exceeded federal drinking water standards due to an equipment malfunction. A similar incident occurred in October 2007. In April 2008, Arizona American paid \$69,000 in fines for the two TCE contamination episodes.

The facility is a Superfund site and while owned by Arizona American, three companies—Motorola, Siemens and GlaxoSmithKline—are responsible for environmental remediation under the terms of a 2003 federal consent decree. The three companies are the original source of the decades-old groundwater contamination on the site and jointly built the water plant as part of the federally mandated Superfund cleanup. The plant was subsequently sold to Arizona American.

After the January incident, the Maricopa County Department of Health Services found that there was never a health danger to any customer and Arizona American subsequently disconnected the well that created the problem from the rest of the water system. The company is also implementing a number of improvements in response to the incident, including new safety measures, on-site

staff around the clock and new control panels, alarms and daily sampling. The Justice Department and U.S. Environmental Protection Agency required Motorola Inc., Siemens Corp. and Glaxo-SmithKline to pay a \$500,000 civil penalty for the system failures that led to the TCE release.

TCE contamination at this Scottsdale facility has been a recurring problem over the years, even when the facility was under municipal control, according to state Department of Environmental Quality records. One investigation reveals that the facility has had excessive TCE levels in drinking water supply 16 times between August 1994 and January 1995. Despite paying fines, Scottsdale admitted no liabilities and also failed to notify public authorities to avert a potential contamination of public waters.

Despite the contamination problems Arizona American's performance has been far better than the municipal record, calling into question the use of eminent domain to take over the water system. As Arizona American Water President Paul Townsley wrote in a July letter to the company's Scottsdale customers, "government's power of eminent domain was never intended to be used to take over a private business providing a good product and good service to its customers."

Scottsdale is not the only city in Arizona pursuing similar action. In March, the town of Cave Creek, Arizona will take over the operation of its water utility from Arizona American Water. After losing a 2005 bid to purchase the water system to a private company, the town opted to pursue condemnation to buy the system, citing a need for public control and service quality issues as its main justifications. In March 2007, Cave Creek finally purchased the water utility through condemnation, though the city opted to contract with Arizona American for another year during the transition to public ownership. The acquisition was facilitated by a low-interest loan from the state Water Infrastructure Financing Authority.

The community of Felton, California also recently used the threat of condemnation to take back control of its water system from California-American Water (Cal-Am), a subsidiary of the

German multinational corporation RWE. Cal-Am and the San Lorenzo Valley Water District (SLVWD) settled less than a week before the planned start of an eminent domain trial.

In February this year, city officials of the Rosario, Vusario and Orcas Highlands on Orcas Island in Washington State decided to sell their private water utility to the publicly owned and operated Eastsound Sewer and Water District as a result of public pressure. For several years now, the residents of Orcas Highlands have been provided water through Rosario Utilities, a small private company. In September last year when a large investor-owned company Washington Water Services purchased Rosario Utilities the threat of eminent domain emerged. The residents of Orcas Highlands set about gathering support for a vote on annexing their private water utility to the publicly owned and operated Eastsound Sewer and Water District. In February the residents of the areas approved the annexation. The residents now intend to work with the publicly owned and operated Eastsound Sewer and Water district to purchase or more likely transfer to public ownership via eminent domain the originally owned private water utility from Washington Water Services.

Earlier this year Fort Wayne, Indiana, began the process of re-establishing publicly owned water utilities by shifting close to 9,000 customers of Aqua Indiana (a subsidiary of Aqua America) to public water. In 2002, Fort Wayne began using eminent domain to purchase the utility from Aqua Indiana.

In the light of the U.S. Supreme Court's 2005 ruling in *Kelo v. City of New London*—and the overwhelming attention in the public policy sphere to protecting private property rights that followed—the attempt to use eminent domain to expropriate the assets of private water companies presents a worrying trend, especially given the record of successful water management by private entities, the counter track record of municipal failures in water management, the tremendous costs and risks local governments take on in the face of rising long-term operations and maintenance, the need to upgrade and expand aging water systems and compliance with increasingly stringent environmental regulations.